

A vision to become a
world-class Sri Lankan Bank



Our Vision

To be a world-class Sri Lankan Bank.

Our Mission

To be dominant in the financial services sector, creating superior long term shareholder value and contributing to economic development in Sri Lanka by exploiting regional opportunities and delivering innovative solutions, with best-in industry service excellence, through an inspired team.

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Registered Name: National Development Bank Limited

Trade Name:  **NDB bank**

Financial Highlights

	NDB BANK			NDB GROUP		
	2006	2005	Per Cent Change	2006	2005	Per Cent Change
(Rs mn)						
Total Income	6,888	4,288	60.6	8,209	7,116	15.4
Net Interest Income	2,402	1,595	50.6	2,853	2,693	5.9
Net Other Income	1,193	814	46.5	2,127	2,061	3.2
Net Income	3,595	2,409	49.2	4,979	4,754	4.7
Profit Before Tax	2,086	1,071	94.7	3,427	1,866	83.7
Profit After Tax	1,005	626	60.7	2,207	1,273	73.4
Profit Attributable to Equity Shareholders	1,005	626	60.7	2,030	1,036	96.0
Shareholders' Funds	8,555	7,930	7.9	10,567	8,815	19.9
Total Assets	63,253	50,950	24.1	64,977	64,714	0.4
Total Lending Portfolio	44,325	37,813	17.2	44,359	39,172	13.2
Total Portfolio	53,025	44,541	19.0	53,071	52,835	0.4
Gross Dividend	327	322	1.6	327	322	1.6
(%)						
Return on Average Equity *	12.19	7.98	52.8	20.95	12.05	73.8
Return on Average Assets *	1.76	1.50	17.3	3.13	1.70	84.2
Capital Adequacy Tier 1	16.26	19.08	(14.8)	22.10	18.83	17.4
Tier 1 & 2	15.58	14.18	9.9	21.95	18.48	18.8
(Rs per Share of Rs 10)						
Earnings *	12.28	7.64	60.7	24.81	12.70	95.3
Book Value	104.51	96.88	7.9	129.09	107.70	19.9
Dividends	6.00	3.90	53.8	6.00	3.90	53.8
(Times)						
Debt/Equity	6.09	5.22	16.7	4.77	4.73	0.8
Net Income/Overheads *	2.39	2.10	13.7	2.84	1.84	54.4
Interest Cover	1.73	1.86	(6.9)	1.89	2.10	(10.2)

* Includes exceptional capital gains of Rs 1.01 bn in NDB Group (See Note 1 on page 70).

Chairman's Message

I have pleasure in presenting to you the Annual Report and Audited Accounts of NDB Bank and the NDB Group for the year 2006.

In spite of 2006 being a difficult year because of high oil and other commodity prices and fluctuating financial markets, world economic growth continued during the year at a healthy pace of just below 5 per cent, helped by more rapid growth in China, India and Russia. Our business community and government officials should now be looking at improving trade channels into Asia and Russia, in particular, to promote higher growth of our own economy.

background of balancing economic progress and peace building, the country was able to register a robust growth of 7.2 per cent during 2006. It has, however, to be emphasized, this is still below the potential that can be achieved in an era of peace.

The country's economic health and progress has improved in 2006 and is reflected in the following indicators:

- Investments have risen to 29 per cent of GDP
- The stock market indices reached record levels
- Exports grew by 8.4 per cent over the year
- Foreign direct investment reached a record level of US\$ 500 mn during the year
- Expatriate workers' remittances surged to US\$ 2,326 mn in 2006
- Government revenue increased to over 17 per cent of GDP
- Government debt declined to 92.9 per cent of GDP at the end of the year
- Unemployment declined

There was, however, a downside to the Government's performance and that was an increase in inflation which, calculated on a point to point basis in terms of the Colombo Consumer Price Index, rose in January/February this year to its highest level in 10 years. This puts at risk the sustainability of the Government's economic achievements.

Recently a road map to reduce inflation to below 11 per cent has been announced by the authorities. This is welcome and if unsparingly implemented should secure benefits for all. The programme requires restraint in government spending and strict limits on recurrent expenditure even at the price of dissatisfaction on the part of those affected by such restrictions. Tight budgetary control is essential and failure to impose such control would pose serious problems to the economic health of the country. In this environment, it is expected that the Government will curb unproductive expenditures and credit expansion and that the banking sector will be called upon to play a significant role in implementing the road map.

Two significant developments dominated the political scene in Sri Lanka during the year under review. One was the change in the composition of the Government with a prominent constituent political party, the Janatha Vimukthi Peramuna, leaving the ruling alliance and a large number of Members of Parliament from opposition parties joining the Government subsequently. The second development was the increase that has taken place in the intensity of military operations in the North and East of the country, albeit with a political solution very much in the sights of the President's horizon. Against this complex and difficult



The year 2006 was an excellent one for the NDB Group with strong contributions both from its core banking business, as well as at the NDB Group level. The NDB Group profit before tax increased by 84 per cent to Rs 3,427 mn from Rs 1,866 mn in 2005. This large increase was due to the NDB Group figure for 2006 including an exceptional capital gain of Rs 1,016 mn realized from the sale by Capital Development and Investment Company Ltd. of part of its shareholding in NDB Finance Lanka (Pvt) Ltd. - the holding company of Eagle Insurance Co. Ltd. - to Aviva International Holdings Ltd. on 1 February 2006. NDB Bank's effective shareholding in Eagle Insurance Co. Ltd. is now 32.42 per cent. The after tax profit of the NDB Group increased by 73 per cent to Rs 2,207 mn from Rs 1,273 mn in 2005. Additionally, the core banking business of the National Development Bank Ltd. (NDB Bank) also improved significantly. Thus, profit before tax increased by 95 per cent to Rs 2,086 mn and loans and advances grew by 17 per cent to Rs 44 bn in 2006. During the same period deposits also grew by 52 per cent to Rs 21 bn.

I commented in my statement last year that there had been a steep increase in the rate of taxation on banks. Now a further charge of 1 per cent of the performing portfolio, as a general provision, has been imposed on all banks. This provision cannot be set off against profits and will effectively increase the rate of tax on banks. The provision was allowed to be spread out over 10 quarters consequent on an appeal made by the banks. Banks such as ours that have made fairly large general provisions will be better positioned than others to meet this impost, which also comes at a time when the NDB Bank has successfully reduced its non-performing loan level to 2.1 per cent in 2006 from 14.2 per cent in 2002.

A major issue correlated to the tax levies on banks is the need for banks to increase their capital to meet the international Basel standards that are being applied by Central Banks including our own. Banks also need large amounts of capital if they are to expand their overseas activities, even if this is confined to the South Asian region. The current high rates of tax, however, discourage banks from building up reserves which is the preferred way they can meet these needs. I must, therefore,

reiterate the view I expressed last year that the authorities should take a fresh look at the structure of taxation of the banks taking a longer perspective into consideration.

After preliminary confidential discussions between the Chairmen and Chief Executive Officers of the National Development Bank and the Commercial Bank of Ceylon, the Boards of Directors of the two banks approved a proposal to initiate negotiations to see whether a merger between the two banks would be possible, in view of their activities being generally complementary to each other to some extent. During the negotiations, the assistance of an international consultant, who is well versed in the evaluation of merger proposals, would be sought whenever necessary.

We bade farewell in 2006 to Mr U L Kadirugamuwa and Mr A A Pio who resigned from the Board of Directors. I wish to express our sincere appreciation to them for the invaluable contributions they made during their period of office.

I extend a warm welcome to Mr Richard Vokes of the Asian Development Bank who joined our Board in December 2006.

The noteworthy results for 2006 could not have been achieved without the valued advice and assistance of my colleagues on the Board and the unstinted support of the staff. I would like to convey my sincere thanks to all of them.

I would like to conclude on a personal note. I wish to inform shareholders that, though I had given the Board one year's notice of my resignation from NDB Bank to take place at the end of March 2007, the Directors have not accepted the effective date I had communicated to them. They have prevailed on me to continue in office for a further short period to ensure continuity until completion of the initial negotiations with the Commercial Bank of Ceylon on the possible merger of the two banks.



S K Wickremesinghe

19 March 2007

Chief Executive's Review

Banking Industry Trends

In my report last year, I stated that the banking industry in Sri Lanka was going through a period of structural change, driven by several fundamental forces. These pressures continued and intensified in 2006. Change is being driven mainly by increased capital requirements, intensified competition from regional and international banks with advanced technologies, lower cost structures and global brands, as well as by issues pertaining to the ownership of banks and corporate governance.

These matters are analyzed below.

Prudential regulations introduced last year for commercial banks, either increased the need for new capital or reduced an important source of new equity, namely retained profits. Thus, new risk weightings assigned to different classes of loans, effectively increased the Tier I and Tier II ratio capital requirement from 10 per cent to around 11 per cent, depending on the composition of loan portfolios of individual banks. The implementation of Basel II regulations by 1 January 2008 will also result in the need for new capital. It is noteworthy that many

banks are operating at the limit of regulatory capital needed to support existing asset portfolios. Growth will necessarily need to be supported by new capital infusion. Further, new prudential regulations require banks to build up general provisions of 1 per cent on performing loans, by the first quarter of 2009. The resulting charge to profits for the industry at

31 December 2006 is estimated at around Rs 8 bn, with new loans booked thereafter also being subject to an additional charge of 1 per cent. Rational investors, who are asked to provide new capital, will seek percentage returns after tax on their funds invested, which reflect an adequate premium over the risk free Treasury bill rate. However, both retained profits and return on equity are further depressed by the high taxes imposed on banks in particular. The VAT on financial services effectively amounts to around 22 per cent on profits generated by banks, in addition to the generally applicable income tax charge of 35 per cent. This level of taxation makes the tasks of raising or retaining capital by banks, hard to achieve.

Competition from foreign banks intensified during the year. Foreign banks with global economies of scale have brought new products, technology and branding to this industry, which has enabled them to take a dominant market share especially in selected consumer finance markets. If local banks are to meet this challenge, they will have to invest in innovation, and do so while operating at competitive costs, despite the comparative disadvantage they face, in terms of scale of resources. They cannot easily do so without fundamental structural changes being made in the way that they do business.

The Central Bank in an important recent policy statement emphasized its commitment to the principle of broad-based ownership of banks. Detailed guidelines were issued, which



limited ownership of any bank by a single entity or individual to 10 per cent, with Monetary Board approval being required to increase this limit to a maximum of 15 per cent. A process was established for existing shareholders who exceed the limit, to obtain Monetary Board approval to hold the excess, but only for a defined time period. It was also announced that a Code of Governance for banks would be introduced shortly. It is assumed that this would define in particular, the roles and responsibilities of, and the demarcation lines between, shareholders, boards and management, the disclosure and resolution of potential conflicts of interest, and workable enforcement procedures.

The leadership of the Central Bank on policies in this regard, is most welcome. These policies will undoubtedly be tested in practise over the coming months, but their strict enforcement will contribute greatly to achieving the structural changes that the industry must make, if it is to thrive in a fast changing and intensely competitive environment.

NDB Bank Strategies

NDB Bank took early steps both to manage its own internal structural problems summarized below, as well as to position itself to deal with the external pressures described earlier.

It is well known that the project lending model of development finance institutions globally, was crucially dependent on the availability of long-term funding from multilateral agencies, often at concessionary borrowing rates. When this source of funding dried up generally as a matter of global policy, DFIs were forced to diversify their business activities to become commercially viable, or to rely on Governmental support for

their survival. While the old credit lines are gradually being repaid, NDB Bank recognized that a business strategy based on the hope of new lines being available would not be sustainable, and changed course accordingly.

The transformation from DFI to a commercially competitive financial group, is well under way. A balanced business strategy was adopted, with an integrated corporate banking division handling both long- and short-term lending, and an SME group, both working closely with our powerful capital markets and insurance sectors. Additionally, a consumer finance capability is being built, which will transform the prospects for NDB Bank over the medium term.

In turning this vision to reality, many actions have been taken. The commercial banking business of ABN Amro was acquired, and NDB's Act of Parliament was repealed, to permit the merger of the two institutions on 1 August 2005. Subsidiaries and affiliates were rationalized to give sharper strategic focus. Credit processes were introduced which reduced the non-performing loan ratio to 2.1 per cent, possibly the lowest among Sri Lankan banks. New IT systems were introduced together with supporting processes. Our channels of distribution have increased, with 31 branches, the introduction of a consumer sales force, and by the use of technology to distribute more products to more customers. A new management team and culture was built, blending those from the former NDB, with recruits from local and foreign banks. This diversity of backgrounds is one of our great strengths. HR management is being strengthened to recruit and retain good people, to align their goals with those of NDB Bank, and to reward them based on their achievement. This process is no doubt a continuing journey, but good progress has been made.

The challenge now, as we enter a new phase of strategic implementation is to build scale of operations.

NDB Bank made an announcement recently to the shareholders and the public regarding a possible merger with the Commercial Bank of Ceylon Ltd., and negotiations are presently taking place with the latter to work out a possible basis for such an event.

We will keep shareholders informed of major developments, and seek their approval at the appropriate time.

The strategies described above are being implemented with a view to achieving our vision to become a world-class Sri Lankan bank.

NDB Bank Performance

The results for 2006, which are analysed in detail elsewhere in this report, reflect both strong profitability and the good progress that has been made, in implementing the new business strategy after the merger between National Development Bank Ltd. and NDB Bank Ltd. on 1 August 2005.

Overall, there was strong growth in core banking business in terms of loans, deposits and fee income, combined with greatly improved credit quality. NDB Bank with a strong financial profile, sound asset quality and strong capital position has been given a Fitch Credit Rating of "AA" with a positive outlook.

NDB Bank's profit before tax grew by 95 per cent from Rs 1,071 mn in 2005 to Rs 2,086 mn in 2006. The NDB Group's profit before tax also grew by 84 per cent from Rs 1,866 mn in 2005 to Rs 3,427 mn in 2006, including an exceptional capital gain generated in the first quarter of 2006 as described below. Excluding the

exceptional capital gain, the NDB Group's profit before tax grew by 29 per cent from Rs 1,866 mn in 2005 to Rs 2,412 mn in 2006. The NDB Group's profit attributable to shareholders, including the exceptional capital gain, increased significantly from Rs 1,036 mn in 2005 to Rs 2,030 mn in 2006. The profit attributable to shareholders, excluding the exceptional capital gain, was Rs 1,014 mn compared with Rs 1,036 mn in 2005, due to the impact of higher rates of Income Tax and Financial VAT. The effective overall tax rate inclusive of the Financial Services VAT charge for NDB Bank amounted to 52 per cent in 2006, which was substantially higher than the levels of 43 per cent in 2005 and 36 per cent in 2004. The increased tax charge was primarily due to increases in the Income Tax rate from 30 per cent to 35 per cent and the VAT on financial services from 15 per cent to 20 per cent. Shareholders' Funds as at 31 December 2006 amounted to Rs 8.55 bn and Rs 10.57 bn for NDB Bank and the NDB Group respectively, which are well in excess of the regulatory minimum standards. The Tier I and Tier II capital for NDB Bank and the NDB Group amounted to 15.57 per cent and 21.95 per cent respectively compared with the regulatory minimum of 10 per cent.

The increased level of business activity is reflected in the financial results. Thus, the loan book grew appreciably to Rs 44 bn, mainly in terms of commercial banking exposure, while at the same time, the quality of the portfolio improved. The non-performing loan ratio at 2.1 per cent is amongst the lowest among Sri Lankan banks. The increased investment in branch distribution resulted in the growth of customer deposits by over 50 per cent to Rs 21 bn, which reduces NDB Bank's reliance on dwindling credit lines. Fee, commission and foreign exchange income, also grew at a fast pace to reach Rs 666 mn (an increase of 47 per cent over the previous year).

The overheads of NDB Bank increased to Rs 1,505 mn in 2006 after four years of relatively small increases, due to merger related expenses, and the aggressive expansion of commercial banking activities including an increase in the branch network. This increased expenditure will realize benefits in future years as the commercial banking operations develop. However, the cost income ratio of NDB Bank at 46 per cent still compares very favourably with the local Banking sector.

The exceptional increase in the NDB Group profits over the comparative period was due to Capital Development and Investment Company Ltd. making a capital gain in the first quarter of 2006 on the sale of part of its shareholding in Aviva NDB Finance Lanka (Pvt) Ltd. (the holding company of Eagle Insurance Co. Ltd.) to Aviva International Holdings Ltd. on 1 February 2006. The capital gain earned by the NDB Group net of minority interest was Rs 1.01 bn. NDB Bank's effective holding in Eagle Insurance Company Ltd. is now 32.42 per cent.

Our achievements and realization of our plans, are of course dependent on the commitment and dedication of our employees, as we manage the process of transformation of the NDB Group. I would like to take this opportunity to express my sincere thanks to them for their support.

Let me conclude by thanking the Chairman and Board of Directors for their assistance and guidance, during this period of complex change. We look forward to their continuing support.



N S Welikala

19 March 2007

Management Discussion and Analysis

Review of Operations

Corporate Banking

Corporate Banking consists of three business divisions i.e. Commercial Banking, Specialized Commercial Markets & Project Finance.

Commercial Banking

The Commercial Banking Division of NDB Bank provides comprehensive, customized financial solutions to large and mid-sized corporate customers. The division offers a complete range of corporate banking products and services, including working capital facilities, securitizations, commercial paper, cash management and transaction banking.

In today's increasingly competitive landscape, banks are judged on key attributes including relationship management quality, service excellence, risk management capability and technology. Individually and collectively, these are the parameters of success. NDB Bank optimizes these elements to achieve growth and success in commercial banking.

Portfolio Growth of NDB Bank

Year ended	Total Outstanding Rs mn	Total Direct Outstanding Rs mn	Total Contingents Rs mn
31 December 2005	46,317	37,813	8,504
31 December 2006	58,196	44,325	13,871
YoY Growth (%)	26	17	63

Relationship Management

The concept of 'relationship management' is based on creating and sustaining mutual value between NDB Bank and its clients. Companies place great value on the predictability and continued availability of services and products that meet their most important needs; this is known as the 'relationship premium'.

Service Excellence

Segmentation and accurate targeting are central to successful relationship management. Equally important is innovation: the ability to produce customer-specific solutions is a key determinant of 'service excellence'. At NDB Bank, a highly motivated team of relationship-management professionals supports this

function, creating conditions that enable NDB Bank to drive its commercial banking business successfully. These relationship managers are specialized in and have a thorough understanding of the industry in which their companies are involved in. They also possess detailed knowledge of the specific business entity and the regulatory environment within which they operate. The presence of this team gives NDB Bank a strong competitive advantage.

Progress in 2006

Despite heavy competition and continuous pressure on margins, good progress was made during the year under review. In line with projections, assets grew 33 per cent over the previous year. Greater emphasis was given to improving profitability and portfolio quality.

Risk Management

Prudent 'risk management' has ensured that the commercial banking portfolio remains well diversified, avoiding excessive exposure to any particular sector while strengthening the credit portfolio of the Division. A further improvement was seen in the divisional NPL ratio, now below 1 per cent, which is a testament to the overall quality of the portfolio.

Overall, the commercial banking business constitutes about 36 per cent of the total loans and advances portfolio of NDB Bank, while its deposits account for approximately 34 per cent of the total deposit base. The Division contributed 20 per cent to overall banking revenue.

The Commercial Banking will continue to be a critical business segment of NDB Bank, contributing a sustainable and a profitable lending portfolio.

Electronic Banking

The division has successfully used 'technology' as both enabler and differentiator, achieving high penetration in transaction banking and making a sizeable contribution to the fee income stream. Through the implementation of a world-class service-delivery solution, electronic banking now forms an integral part of the division's portfolio of effective cash and treasury management services. Over half the division's customers now use the system to perform transactions.

Talk is not cheap

Helping Sri Lankans stay connected, NDB Bank in 2006 granted finance amounting to Rs 1.5 bn for the network expansion and operational improvements for the country's major telecom operators.



The shirt on your back



Of critical importance to Sri Lanka's economy, the textile and garment industry accounts for some 43 per cent of national exports by value. NDB Bank has supported this vital industry ever since inception, helping it stay solvent and profitable in good times and bad. The sector accounts for over a tenth of the NDB Bank's total loan portfolio.

Specialized Commercial Markets Division

As customers grow more sophisticated, bankers are challenged by a growing demand for unique, customized financial solutions. Responding to this demand, in 2006 NDB Bank set up a Specialized Commercial Markets Division within its Corporate Banking business.

The Division offers integrated customer solutions across different corporate market segments. Its products are structured and developed to meet the varying, often unique requirements of enterprises of different sizes.

Structured trade finance, focused on providing unique value propositions to customers engaged in small and medium-scale industry, is one of the key

products of the Division. Another product, channel finance, focuses on strengthening the supply and distribution channels of customers operating in the local market, adding value to NDB Bank's growing Commercial Banking and SME franchises.

Project Finance

Sri Lanka will require substantial investments in infrastructure to fulfil its economic potential. Upgrading of ports, airports, highways, rail networks and capacity enhancements of power and communication sectors require substantial investments. Funding these projects is no longer confined to the Government. Public-Private Partnerships and direct private sector participation is now a global phenomenon. Hence, in today's world, Project Finance places a pivotal role in economic and social development.

Project Finance remains a core product for the NDB Bank. The NDB Bank has an admirable track record of funding projects in all significant economic sectors. Given the Project Finance skill base available, NDB Bank is well positioned to continue its important role in providing term funding. However, the availability of long-term funding under credit lines dwindled. Therefore, the key challenge facing providers of long-term finance is to source long-term market funding at rates that are affordable for long-term borrowers.

Following the merger with NDB Bank in August 2005, the Project Finance, Commercial Banking and SME Divisions of the Bank have been working closely to exploit synergies for the benefit of NDB Bank and its customers. NDB Bank's Corporate Banking objectives have changed accordingly, and with them the divisional organization, staffing and processes. One of the key strategies adopted by the Corporate Banking Department was the cross selling of commercial banking products and term loan products to clients who were not enjoying the same prior to the merger. NDB Bank attaches priority to projects that provide working capital business opportunities.

Notwithstanding decades of diversification, the plantation industry still plays a sizeable role in the country's economy. The tea and rubber sectors continued to receive substantial financial support from NDB Bank in 2006.



Sowing and growing

During the period under review, NDB Bank acted as joint arranger to raise an aggregate sum of Rs 7.7 bn for two of the largest debt syndicates in the country. Leading and arranging debt syndications will play an important role in the strategy of the Project Finance where the focus would be to enhance the fee income.

NDB Bank is widely recognized for its strength in project finance skills. NDB Bank places great importance in retaining and improving this core competence, which will be of vital importance in providing finance for the many development projects that will follow the dawn of peace. In the future, NDB Bank will leverage on this vital competence to generate fee based income streams by providing value added advisory and outsourcing services to target customers.

NDB Investment Bank (NDBIB) the NDB Group's investment banking subsidiary has structured several securitizations for various industries ranging from plantation companies to leasing and finance companies. NDB Bank participates in selected securitizations in accordance with its own credit guidelines. The Project Finance Division acts as a conduit between the NDBIB and NDB Bank to capture banking business.



Fit to print

Today, some of the most profitable firms in the printing industry are involved in label and pack printing for Sri Lanka's exports. The Corporate Banking Department provided financial assistance to this sector to satisfy the growing demand for around Rs 800 mn in 2006.

Portfolio

Corporate Banking and SME

In keeping with the national economic picture, the Services sector accounted for the largest share of the portfolio (36.5 per cent). The services sector consists of well- diversified sub sectors such as financial services, telecommunications, energy, transport, shipping, printing, healthcare, construction and warehousing. This diversity mitigates the risk of high sectoral concentration.

Metals, chemicals and engineering sector accounted for 15.9 per cent of portfolio. The portfolio remained stable during the year in the context of scheduled term loan recoveries. Sector portfolio is expected to increase during 2007 provided a return of peace and a consequent boom in construction. Demand for steel, cement, tiles, glass, paints, cables and PVC is expected to be strong in the context of a construction boom.

Textile and Garments sector portfolio ranked third in 2006 by posting a healthy growth of Rs 1,403 mn. The year end portfolio of this sector had a share of 12.5 per cent. This was largely driven by extension of trade finance facilities. Portfolio is expected to continue with the growth trend during 2007.

Food, Beverage & Tobacco is an active sector for both project finance and commercial banking. However, the portfolio recorded a decline due to the maturity of particular short-term facility limits. NDB Bank expects this sector to provide good banking prospects in 2007.

Agriculture, agro business and fisheries sector portfolio was sizeable with outstandings of Rs 2,667 mn. This included extension of facilities to the plantation sector. During the year, facilities to regional plantation companies were granted in the form of loans under the ADB's dedicated credit line and as subscriptions to securitization instruments.

Maximus (Pvt) Ltd. won first place in the coveted BBC World Challenge 2006 conducted in association with Shell International and Newsweek. Mr Thusitha Ranasinghe received the prize on behalf of Maximus, an NDB Bank SME Banking Client. Maximus was voted by 33,000 people around the world as the best enterprise and innovator at grass root level, for its revolutionary manufacturing process, which converts elephant dung into paper.



SME Banking

Since its inception in 1979, NDB Bank has pioneered project lending to small and medium enterprises (SME) supporting over 35,000 ventures and creating in excess of 500,000 employment opportunities.

SMEs are estimated to make up more than 80 per cent of all Sri Lankan enterprises and employ 70 per cent of the national workforce. Their significant contribution towards the country's economy provides many opportunities for banking relationships. However, the nature and size of SMEs bring with them a number of inherent structural weaknesses that pose risks to institutions wishing to take up the opportunities presented by the sector. NDB Bank's new strategy, coupled with the considerable sector expertise NDB Bank has built over the years, has enabled the SME Banking Unit to address these opportunities while mitigating the inherent risks.

A New Business Model

During the year a more focused strategy for the SME sector was redesigned with the help of KfW consultants. Emphasis was placed on creating a new business model through the restructuring of the SME Banking Unit to raise the quality of the SME portfolio. Portfolio quality improved to a great extent during the year due to the careful management of the non-performing loans (NPL). The restructuring process has resulted in a new operational configuration that optimizes branch resources and increases operational efficiencies.

The redesigned business model achieved through this re-engineering of the SME Banking Unit will enable the Bank to provide SMEs with a wide range of products structured to their specific requirements. The strategy lays emphasis on a customer-focused approach to business, capitalizing on expertise built up over the years. The creation of an efficient lending process, use of unconventional delivery channels and other

innovations will ensure shorter turnaround time, wider reach and high service quality.

Refinance Operations

NDB Bank has continued with its pivotal role as an apex institution for refinance schemes to the commercial lenders who provide much-needed capital to 'micro', small and medium sector projects. NDB Bank also acted as a participating credit institution in a number of refinance schemes operated by the Central Bank of Sri Lanka and other institutions.

The funds for NDB Bank-operated refinance schemes were derived from credit lines made available by international lending agencies through the Government of Sri Lanka. During the year under review four such schemes were in operation. The Asian Development Bank (ADB)-funded Southern Province Rural Economic Advancement Project (Dasuna) scheme supported the development efforts of enterprises in three districts of the Southern Province. The Aquatic Resources

Development and Quality Improvement Project (Miridiya Sampath) scheme promoted inland fisheries and aquaculture.

The Japan Bank for International Co-operation (JBIC) supported the development efforts of small and micro enterprises with two such schemes: Small & Micro Industries Leader & Entrepreneur Promotion Project (SMILE II) and the SMILE I Revolving Fund.

The German funding agency KfW continued to assist NDB Bank in development of large, small and micro enterprises.

The Japan Social Development Fund (JSDF) 'Grant for Empowering the Poorest of the Poor Women and Girls in South and North-East of Sri Lanka' project came into operation in 2003 to support destitute women in remote regions

of the country. The NDB Bank joined hands with the World Bank and the Government of Sri Lanka to manage this grant, which was made available by the Japanese Government.

NDB Bank approved 2,351 refinance loans amounting to Rs 2,969.9 mn under the above credit lines. These facilities were instrumental in creating a substantial amount of new employment opportunities, mainly in rural areas.

Hauling in their livelihood



Many fishing families depend for their livelihoods on boats, equipment and other resources obtained with an SME loan from NDB Bank. The bulk of NDB Bank's post-tsunami relief work was also directed at this community. In 2006, 43 facilities were granted by the SME Division of NDB Bank.

Refinance approvals by NDB Bank during 2006, along with disbursements under the aforesaid credit lines, are tabulated below:

Re-Finance Approvals & Disbursements for the year 2006				
	Approvals		Disbursements	
	No. of Projects	Amount (Rs mn)	No. of Projects	Amount (Rs mn)
APEX				
SMILE I Revolving	123	108.1	86	70.0
SMILE II	73	131.7	69	123.4
DASUNA	1,661	422.6	1,011	231.5
MIRIDIYA SAMPATH	54	22.2	46	20.9
	1,911	684.6	1,212	445.8
DIRECT				
KfW VI (Micro)	42	15.7	34	12.6
KfW V	153	1,560.1	150	965.3
	195	1,575.8	184	977.9
NDB as a PCI				
SMILE III	199	376.4	232	423.6
SAHANYA	20	153.5	6	38.8
E-Friends II	26	179.6	23	182.7
	245	709.5	261	645.1

Leasing

NDB Bank's Auto Finance product was rebranded and relaunched in year under review as "NDB Leasing". At the end of the year, the portfolio of the Auto Finance Department stood at Rs 1,757 mn. This represents an increase of approximately 108 per cent. The department disbursed 726 facilities, amounting to Rs 1,390 mn. Reflecting a well-designed credit process, non-performing facilities amounted to only Rs 10.3 mn, distributed among four clients - a near-negligible 0.54 per cent of the portfolio.

The department expects to introduce several value additions and a number of new products during the next year.



Profits on paper...

...but these profits are real, too. Many companies, from those involved in paper manufacturing to paper recycling and even bookshops to small scale packaging companies were granted 26 facilities leading to a portfolio growth of 38 per cent.



NDB Bank launches a new consumer banking operation in Kandana.

Consumer Banking

The year 2006 was a growth year for NDB Bank's consumer banking business, with marked expansion in NDB Bank's product portfolio, distribution capabilities and brand salience. The consumer deposit base and the loan portfolio expanded by 81 per cent and 67 per cent respectively.



NDB Bank now offers a wide range of commercial banking products and services. These products and services are backed by efficient electronic processing and multiple delivery channels operated by experienced banking professionals. Delivery channels include ATMs, Debit cards, Internet banking and Phone banking. NDB Bank now reaches a greater number of customers through its expanded distribution capabilities and its wide array of products and services.

Branch Expansion

NDB Bank added eight new branches during the year, bringing the total number of branches, marketing consumer-banking products, to thirty. NDB Bank will continue to expand its reach through its aggressive branch expansion.

A full Portfolio of Products and Services

Following the 2005 merger and subsequent rationalization of functions, the Consumer Banking Division now offers a full range of products and services, including:

- current accounts
- savings accounts
- fixed deposits
- minors' savings accounts
- foreign currency accounts
- call deposits
- personal loans
- auto loans and leases
- housing loans
- privilege banking
- safe deposit lockers
- Internet banking
- debit cards (Visa)
- phone banking
- ATM facilities
- Western Union money transfer service
- Bancassurance products



Our new Mobile Banking Unit making banking even more convenient to our customers.



NDB Bank carried out many door-to-door campaigns to familiarize the public of NDB Bank's Products and Services.

Mobile Banking Unit

A new Mobile Banking Unit is now on the road, bringing the Bank's services to more people around the island and spreading the word to customers about the latest available products and services.

Savings Drive

Deposit mobilization is a key source of funds for lending. NDB Bank is focusing on a double-pronged strategy in this area. While conducting campaigns and introducing products and services to stimulate deposits, NDB Bank is also expanding its distribution network through branch openings, mobile banking, etc. Selected branches are also open seven-days-a-week with extended banking hours daily.

Deposit mobilization was boosted by a major two-phase savings drive in 2006. This took the form of a depositor promotion offering monthly and quarterly cash prizes. The savings portfolio grew by 35 per cent during the course of the year, in part due to these promotions.

Privilege Banking

This exclusive private-banking service for high-net-worth customers continued to show healthy growth in terms of both the customer base and portfolio size. The overall liability portfolio grew by 56% in 2006.

The range and depth of wealth-management services on offer will be further enhanced in the future through the introduction of structured products and other services.

Dream Maker Personal Loans

"Dream Maker" is a personal loan scheme with additional benefits such as the release of funds within 24 hours and trouble-free, friendly service. This product has shown an excellent performance, growing by 150 per cent in the year under review. Initially marketed by a centralized sales team, Dream Maker was made available through all NDB Bank branches in the fourth quarter of 2006.



Home Loans

Following its recent merger with NDB Housing Bank, NDB Bank's growth strategy in the housing-finance segment is based on a core product, the "NDB Home Loan". The merger helps overcome constraints that earlier affected competitiveness in this segment. At the same time, the home loan product is now being made available to a larger and geographically more widely distributed market through the NDB Bank branch network.

NDB Bank now caters to the housing-finance needs of a wider range of customers from corporate employees,





A tie-up between NDB Bank and Western Union giving customers a convenient and reliable money transfer service.



Easy access to home loans for all through NDB Bank.

professionals, entrepreneurs to non-resident Sri Lankans. Loans are structured according to the needs of the individual customer, who may borrow as much as his or her repayment capacity permits. Loans are offered for the construction, extension or purchase of a house, to finance home improvements or to purchase land for building.

With the ongoing boom in residential construction, housing finance is a growing business.

Operational Improvements

To increase growth by leveraging the burgeoning housing-finance market segment, NDB Bank is putting in place a loan origination, management and collection system in line with its world-class vision. Complementing the system is a lean organization with well trained staff to deliver according to the agreed service-levels. With this system in place, NDB Bank will be able to handle higher volumes, competing more effectively with other banks and finance organizations in the segment.

Overall, the housing-finance portfolio recorded good results in 2006, with a total portfolio growth of 34 per cent.

Bancassurance Products

Three attractive bancassurance products were launched in partnership with Eagle Insurance. These allow customers to tailor-make their own investment plans by choosing from a wide range of investment options. The three bancassurance products are:

- **Power One**, a single-premium life insurance policy with a choice of investment plans.
- **Life Venture**, a long-term plan to accumulate funds towards a specific savings objective, such as meeting a child's future higher education expenses.
- **Future Plus**, a retirement plan with a maturity period of between ten and thirty years that helps customers look forward to retirement with confidence.

Western Union Agency

A leading provider of money-transfer services, Western Union, appoint NDB Bank as a Principal Agent in the year under review. Western Union services are now available at all NDB Bank branches.

According to the Central Bank, Sri Lanka receives US \$2 bn in remittances annually; they form approximately 10 per cent of the country's GDP. Money transfers are a popular way for Sri Lankans living overseas to send funds home. Through this new partnership, NDB Bank will contribute to national development by executing



rapid, convenient and reliable money transfers from Western Union's network of approximately 285,000 agent locations in more than two hundred countries and territories, to Sri Lanka.

Investment Banking

NDB Investment Bank (NDBIB) maintained its position as Sri Lanka's premier investment bank in 2006, continuing to introduce innovative financial products to Sri Lankan capital markets. During the year under review, the NDBIB focused on the broad areas of corporate advisory services and debt-and-equity distribution.

The highlight of the year was the structuring and placement of a Rs 2 bn debenture issue for John Keells Holdings Ltd. This was Sri Lanka's largest AAA (Ika)-rated, unsecured, redeemable debenture issue to-date.

Additionally, the NDBIB's Debt Unit structured deals exceeding Rs 5 bn by way of securities, debentures and commercial paper. Amongst these were a debenture

issue for Singer Sri Lanka Ltd. worth Rs 800 mn and the raising of about Rs 1 bn in total debt for the Ceylinco Group.

The NDBIB's Advisory Division was responsible for several landmark deals, the most prominent being the structuring of a Rs 3 bn syndicated loan for Suntel Ltd. Other transactions featured a private-equity placement for Overseas Realty Ceylon Ltd., several company valuations and the formulation of key business plans on behalf of its clients.

In all, NDBIB secured deals exceeding Rs 12 bn in 2006. This is especially commendable considering the relatively volatile economic conditions that prevailed in a year marked by rising interest rates (which dampened borrowings) that discouraged several planned IPOs. NDBIB secured several new clients and first-time investors with a number of disintermediated instruments. The participation of foreign banks in numerous deals added to the strength of an already diverse portfolio.

The NDBIB's skilled and highly qualified team of professionals has established an outstanding reputation in this niche of the financial services sector, creating a solid platform for future growth and achievement.

NDBS Stockbrokers

It was another outstanding year for the Colombo Stock Exchange. The ASPI rose by 42 per cent, once again making the CSE one of the world's best performing markets. Daily turnover averaged Rs 436 mn, second only to the Rs 482 mn per day generated in the CSE's record-breaking year, 2005. Even more encouraging was the proportion of foreign turnover, with inflows of Rs 5.4 bn, the best recorded in recent times.

The Company once again generated excellent returns to shareholders despite the issue of five new licences and a fall-off in average daily market turnover. A lack of primary market activity limited NDBS Stockbrokers to trading in the secondary market, while 'negotiated' brokerage arrangements also substantially reduced fees.

The Company and industry will face unprecedented challenges in 2007, given the current macroeconomic environment. NDBS Stockbrokers will endeavour to position itself through an optimal mix of funding clients, quality research and an aggressive sales force. It will also attempt to leverage synergies created by its relationship with other group companies such as NDB Bank, Eagle NDB and NDB Investment Bank.

Treasury Operations

The main activities carried out by the Treasury in support of the core business were as follows:

Liquidity Management

NDB Bank's exposure to large credit-line liabilities and project loan assets, which often have different maturity dates, frequently results in liquidity gaps. Dealing with these calls for a reliable understanding of cash flows and the ability to devise funding plans well in advance of need. Treasury tables these funding plans with the Asset and Liability Management Committee, a forum

representing all business units of NDB Bank. Thus a broader understanding of liquidity issues and their management is gained by providers and users of NDB Bank's funds.

During the year under review, Treasury negotiated several long-term funds from institutional lenders such as the National Savings Bank, various insurance companies and provident funds. These were intended to replace credit lines that matured during the year.

NDB Bank's exposure to the money market was very moderate. During the first half of the year, it borrowed small sums from the market but became a net overnight lender of small amounts over the second half.

Treasury was also actively involved in assessing the liquidity outlook in 2007 and formulating plans to meet NDB Bank's liquidity needs. These needs include the planned repayments of principal on credit line borrowings incurred many years ago.

The funding plan produced by Treasury has been approved by the ALCO and will be implemented in stages throughout 2007, depending upon actual cash flow patterns.

Foreign Exchange Operations

Foreign exchange transactions were undertaken to meet customer needs and in NDB Bank's trading on its own account as market maker. In addition to quoting competitive rates for businesses, the Treasury provides regular market updates and views on interest and exchange rates. These inputs helped many customers weather the extremes of interest and exchange rate volatility experienced during the second half of 2006.

NDB Bank recorded a revenue of Rs 280 mn from Foreign Exchange Transactions this year as compared to Rs 251 mn earned in 2005. These figures do not include the translation effect of Foreign Currency Banking Unit (FCBU) capital, which is held as a separate revaluation reserve.

Trading in Government Securities

Debt trading was conducted with a low maturity mismatch between investments and funding repurchase agreements ('repos') due to the rise in rupee interest rates. Treasury adopted a duration-based risk management discipline to replace the traditional repricing bucket method formerly used to manage interest rate risk. The use of this powerful interest rate risk management tool was made possible through the operationalization of new asset-and-liability management software in mid-2006.

Revenue from debt trading amounted to Rs 45 mn for 2006, Rs 37 mn of which was net interest income while the rest was derived from capital gains.

Asset and Liability Management Committee (ALCO)

Treasury drives NDB Bank's ALCO process by providing its members with interest and exchange rate updates and data on other macroeconomic developments.

Based on these inputs, the Committee sets parameters for the management of maturity mismatch risks in the Balance Sheet. It also fixes product and transfer pricing rates based on prevailing market conditions. The ALCO process ensures that various internal business units are made aware of the many Balance Sheet and funding issues faced by the NDB Group. This promotes consensus in the process of allocating available resources to various lines of business.

Equity Investments

Non-Quoted Equity Portfolio

NDB Bank's non-quoted equity portfolio amounting to Rs 392 mn net of provisions as at 31 December 2006 comprised Rs 172 mn in ordinary shares and Rs 220 mn in preference shares. The respective figures for the preceding year were Rs 150 mn and Rs 220 mn. Preference shares of two companies amounting to Rs 11 mn, of which one has been fully provided for, were redeemed during the period, resulting in a profit of Rs 4 mn.

Net dividend income during the year amounted to Rs 40 mn (2005 - Rs 58 mn) from the ordinary share portfolio and Rs 34 mn (2005 - Rs 40 mn) from the preference share portfolio.

Quoted Equity Portfolio

The All Share Price Index (ASPI) at the Colombo Stock Exchange stood at 1,948 at the beginning of the year, while the Milanka Index stood at 2,496. The indices continued their upward momentum with temporary set backs to reach a peak of 2,789 (ASPI) and 3,795 (Milanka) on 1 December 2006. The market closed in December with ASPI at 2,722 and Milanka at 3,711.

The quoted ordinary share portfolio of NDB Bank stood at Rs 20 mn (at cost) and Rs 404 mn (at market) at the end of December 2006. This excludes investment in Eagle Insurance Co. Ltd.

Dividend income from the quoted portfolio amounted to Rs 30 mn as against Rs 31 mn in 2005.



Aviva and NDB Group partner on Eagle Insurance.

Information Technology

Our commitment to be 'a world-class Sri Lankan' is backed by a capable and efficient Information Technology Division. This year, the in-house development of a Cheque Imaging and Truncation (CIT) system and its successful implementation well in advance of other industry players was a Divisional highlight.

A profitability system developed in-house by the IT Division provides accurate and timely information at unit, product, officer and customer level. The detailed information provided by this system has enabled the relationship management team that handles high networth customer accounts to provide these customers with superior service.

The Division also supported NDB Bank's Customer Relationship Management (CRM) programmes and decentralization of the decision-making process through the in-house development of a purchase order monitoring system that continuously monitors customer transactions.

Operations

NDB Bank follows the internationally accepted practice of centralizing processing functions in order to achieve higher efficiencies. With that concept NDB Bank has its centralized Processing Unit and a centralized Trade Finance Unit to handle processing for all NDB Bank's branches under one roof. This concept has benefited NDB Bank in improving its processing efficiencies and also manage the cost effectively.

The choice of location for these centralized processing departments at Dharmapala Mawatha was based on customer considerations.

During the course of the year, the Operations Department signed several service-level agreements with NDB Bank's business units, thus ensuring that benchmarked, consistently high service standards are maintained. Service levels are monitored through internal and external customer surveys.

NDB Bank with the assistance of a firm of consultants drew up a comprehensive business continuity

plan that would ensure uninterrupted service in case of a disaster.

Eagle Insurance

Eagle Insurance Company Ltd. recorded consolidated revenue of Rs 4,813 mn for the year ended 31 December 2006. This reflects 13 per cent growth over the previous year. The total gross written premium of Life and General insurance business increased by 14 per cent compared to the prior year. The profit after tax of Rs 523 mn reflects a marginal growth of 2 per cent over the previous year. The low growth in profit after tax is primarily due to the capital gains on equity portfolios realized during the pre-election period in 2005 of Rs 124 mn. When adjusted for this, the underlying increase in profit after tax is strong at 34 per cent. The recorded profit in 2006 is in line with the Company's profit expectation for the year and is a reflection of the effective execution of planned strategies in the areas of business development, revenue expansion, investment and operational efficiency.

The Company was able to maintain its track record in delivering impressive shareholder returns with a Return on Net Assets (RONA) of 31 per cent for the year 2006. Eagle's Balance Sheet was further strengthened, with net assets recording a growth of 19 per cent over the previous year.

In February 2006, the Aviva group acquired a majority stake in Eagle from the NDB Group, with NDB Bank remaining a significant indirect shareholder. Aviva is the world's oldest insurance group, with a history dating back 300 years to 1696. Today, it is the world's fifth largest insurance group and the biggest in the UK.

During the year a number of new initiatives were launched. Responding to a timely opportunity to develop a new business channel, Eagle introduced bancassurance distribution to Sri Lanka by successfully launching two bancassurance partnerships with indirect shareholder, NDB Bank and Standard Chartered Bank. Aviva's long-standing experience in

bancassurance distribution world-wide was instrumental in developing this business channel. Eagle expects bancassurance to be an important and growing source of future new business.

Eagle's partnership with Aviva has reaped benefits not only for the Company, but for the industry as well as the country. The introduction of unit-linked products added a value proposition to customers by providing them with a unique combination of health and protection benefits along with a range of investment options.

Eagle was recognized as Sri Lanka's No. 1 in 'Good Corporate Governance Disclosures' by the Institute of Chartered Accountants of Sri Lanka at their 2006 Annual Report awards ceremony. Eagle was also ranked as one of the "10 Best Corporate Citizens" for the third successive year and was awarded "Winner of the Customer Relations Category", presented by the Ceylon Chamber of Commerce. In addition, the Company was ranked Asia's No. 1 for CSR in the industry by Asia Insurance Review, in light of Eagle's policy of 'CSR without fanfare'.

Financial Review

Overview

2006 was the first full year of operations by NDB Bank as a Licensed Commercial Bank, having taken over the assets and liabilities of its subsidiary, NDB Bank Ltd., on 1 August 2005.

NDB Bank's profit before tax grew by 95 per cent from Rs 1,071 mn in 2005 to Rs 2,086 mn in 2006. The NDB Group's profit before tax also grew by 84 per cent from Rs 1,866 mn in 2005 to Rs 3,427 mn in 2006, including an exceptional capital gain generated in the first quarter of 2006 as described below. Excluding the exceptional capital gain, the NDB Group's profit before tax grew by 29 per cent from Rs 1,866 mn in 2005 to Rs 2,412 mn in 2006. The NDB Group's profit attributable to shareholders, including the exceptional capital gain, increased significantly from Rs 1,036 mn in 2005 to Rs 2,030 mn in 2006. The profit attributable to shareholders, excluding the exceptional capital gain, was Rs 1,015 mn compared with Rs 1,036 mn in 2005, due to the impact of higher rates of Income tax and Financial VAT as explained later in this review.

The exceptional increase in the NDB Group profits over the comparative period was due to Capital Development & Investment Company Ltd. (CDIC) making a capital gain in the first quarter of 2006 on the sale of part of its shareholding in NDB Finance Lanka (Private) Ltd. (now known as Aviva NDB Finance Lanka (Private) Ltd. - the holding Company of Eagle Insurance Co. Ltd.) to Aviva International Holdings Ltd. on 1 February 2006. This sale generated a profit of Rs 1.64 bn to CDIC. The capital gain earned by the NDB Group net of minority interest was Rs 1.01 bn.

The NDB Group structure underwent significant changes during 2006.

As stated above, the international savings, investments and insurance group, Aviva, entered the Sri Lanka insurance market by acquiring the controlling stake of Eagle Insurance Company Ltd. Under the new ownership of Aviva, the world's sixth largest insurer, Eagle Insurance Company Ltd. once again becomes the only international composite insurer to

operate in Sri Lanka. Eagle Insurance Company Ltd's consolidated revenue for the year was Rs 4,813 mn reflecting a growth of 13 per cent over the previous year. The net profit after tax was Rs 523 mn, a growth of 2 per cent over 2005. Consequently, the NDB Bank's effective holding in Eagle Insurance Company Ltd. reduced from 65.98 per cent in 2005 to 32.42 per cent in 2006.

NDB Housing Bank Ltd. became a wholly-owned subsidiary of NDB Bank in April 2006. NDB Bank took over the assets and liabilities of NDB Housing Bank Ltd. on 1 September 2006.

In addition, the results of NDB Investment Bank Ltd., NDBS Stock Brokers (Pvt) Ltd., Capital Development & Investment Company Ltd. and Development Holdings (Pvt) Ltd. representing the spectrum of the NDB Group businesses have been consolidated.

The core banking business grew significantly during the year. However, the results of NDB Bank

in 2005 include the performance of National Development Bank Ltd. up to 31 July 2005 and thereafter the performance of the merged entity. For the purpose of meaningful comparison of the performance of the merged bank, the analysis below also contains comparisons between 2005 and 2006 as if both banks were merged throughout 2005. (referred to below as the merged basis)

Net Interest Income (NII)

Net Interest Income of Rs 2,402 mn for 2006 compares with Rs 1,595 mn earned in the previous year. On a merged basis net interest income increased by 21 per cent over the previous years to Rs 2,402 mn. This was primarily due to the increase in the commercial banking lending portfolio of Rs 4.0 bn over the previous year and a significant reduction in non-performing loans as explained later in this review.

At the NDB Group level, contribution to NII, primarily came from interest income earned by

Capital Development & Investment Company Ltd. which had liquid funds arising from the disposal of the part of the holdings in NDB Finance Lanka (Private) Ltd. [now known as Aviva NDB Finance Lanka (Private) Ltd.] as stated above.

Net Other Income

NDB Bank's net other income excluding provisions for equity losses increased by 46 per cent during the year. On a merged basis the net other income of NDB Bank for the year increased by 47 per cent over the previous year. This was mainly due to the increased level of commercial banking activities after the merger, resulting in increased fee, commission and forex income. The "other income" component of NDB Bank formed an increasing proportion of income as expected since NDB Bank is now a fully-fledged commercial bank with trade finance and forex activities cross selling a range of products to its customers. In addition, NDB Bank has also diversified its avenues of fee income through Bancassurance, Western Union Money Transfer, etc.

NDB Bank's equity income decreased by 9 per cent over the previous year. This was mainly due to higher capital gains from quoted investments in 2005.

At the NDB Group level, net other income excluding provisions for equity losses increased by 21 per cent. However, excluding the capital gain arising on Capital Development & Investment Company Ltd's disposal of part of its holding in NDB Finance Lanka (Private) Ltd. [now known as Aviva NDB Finance Lanka (Private) Ltd.] net other income reduced by 37 per cent over the previous year. This was mainly due to the results of Eagle Insurance Company Ltd. (through Aviva NDB Finance Lanka (Pvt) Ltd.) not being accounted for as a subsidiary with effect from 1 February 2006.

Operating Expenses Excluding Provisioning

The operating expenses excluding provisioning and a write off of intangible assets on business combinations as explained below, increased by 29 per cent over the

previous year. On the basis that both banks were merged throughout 2005 and 2006 the overheads of NDB Bank increased by 9 per cent over the previous year to Rs 1,505 mn in 2006 after four years of relatively small increases, due to merger related expenses and the aggressive expansion of commercial banking activities including an increase in the branch network from 13 prior to the merger to 31 now. This increased expenditure now, will realise benefits in future years as the commercial banking operations develop. The cost income ratio of NDB Bank was 46 per cent for the year as compared with 41 per cent for the previous year. The increased cost income ratio is still well below the industry norm in Sri Lanka.

The value of goodwill on the transfer of assets and liabilities of NDB Bank Ltd. on 1 August 2005 on a provisional basis was Rs 529 mn. As required by Sri Lanka Accounting Standard No. 41, Impairment of Assets, an independent valuer, namely PricewaterhouseCoopers was appointed to determine the fair

value of assets and liabilities taken over from NDB Bank Ltd. on 1 August 2005. They have confirmed that the excess over the identifiable assets and liabilities taken over from NDB Bank Ltd. on 1 August 2005 amounts to Rs 553 mn. Out of this amount as required by the Standard, the value of the customer base taken over from NDB Bank Ltd. on 1 August 2005 was identified as Rs 172 mn by PricewaterhouseCoopers. This amount was written off in full in the Income Statement in 2005. The Balance goodwill of Rs 381 mn for which full provision has been made against reserves will be tested for impairment annually. Accordingly, the previous year's figures have been restated.

Provision for Credit Losses and Non-Performing Loans (NPLs)

The non-performing loans, leases and advances portfolio of NDB Bank decreased significantly to Rs 931 mn from Rs 1,591 mn at the last year-end, Rs 2,431 mn at the end of 2004, Rs 2,700 mn at end of 2003, Rs 3,683 mn at the

end of 2002 and Rs 4,064 mn at the end of 2001. The ratio of NPLs to the total lending portfolio was also down to 2.1 per cent at the end of the year compared with 4.2 per cent at the end of 2005, 9.9 per cent at the end of 2004, 10.9 per cent at the end of 2003 and 14.0 per cent at the end of 2002.

The Central Bank mandated specific provisions at the year-end amounted to Rs 343 mn compared with Rs 597 mn as at the previous year-end. The percentage of such specific provisions to NPLs of 37 per cent was on par with last year. Total specific provisions including the judgmental provisions made over and above the minimum Central Bank mandated provisions at the year-end amounted to Rs 1,508 mn compared with Rs 1,854 mn as at the previous year-end. Total specific and general provisions together amounted to Rs 1,783 mn at the year-end compared with Rs 2,018 mn at the previous year-end. During the last quarter of 2006, the Central Bank mandated that banks build up a 1 per cent general provision on their

performing portfolio and have given them time to make this provision over ten quarters ending on 31 March 2009. However, NDB Bank built up its general provision to Rs 275 mn by 31 December 2006, leaving a shortfall of only Rs 155 mn, based on the portfolio at that date. This shortfall along with 1 per cent of any incremental performing portfolio needs to be provided for, over a period of 27 months.

NDB Bank's open loan exposure, being NPLs net of Central Bank mandated specific provisions against NPLs, as a percentage of shareholders' funds reduced to 6.9 per cent as compared with 12.7 per cent at the end of 2005.

The net charge for doubtful debts for the year, amounted to Rs 37 mn, as compared with Rs 165 mn for the previous year.

The charge for the year on a merged basis amounted to Rs 37 mn as compared with Rs 145 mn for the previous year.

Taxation

NDB Bank's corporate taxation for the year increased significantly over the previous year.

On a merged basis the effective overall tax rates inclusive of the VAT charge was 52 per cent for the year and 43 per cent for the previous year. The increased tax charge was primarily due to increase in the rates of income tax from 30 per cent to 35 per cent and the VAT on financial services from 15 per cent to 20 per cent.

The overall tax rate of the NDB Group inclusive of the VAT charge was 36 per cent as compared with 32 per cent for the previous year. The reduced effective rate over last year was mainly due to the exceptional capital gains made by the Capital Development & Investment Company Ltd. on the sale of 58.44 per cent of its shareholding in NDB Finance Lanka (Private) Ltd. [now known as Aviva NDB Finance Lanka (Private) Ltd.]. The effective tax rate excluding the capital gains was 51 per cent.

Capital Adequacy

The minimum levels of capital mandated by the Central Bank are 5 per cent for Tier 1 and 10 per cent for Tier 1 and 2. The minimum Tier 1 capital required is Rs 2.5 bn.

The Tier 1 Capital Adequacy Ratio of NDB Bank declined from 19.08 per cent to 16.26 per cent at the end of the year mainly due to the take over of the assets and liabilities of NDB Housing Bank Ltd. on 1 September 2006. The Tier 1 and 2 ratios improved from 14.18 per cent to close at 15.58 per cent as at 31 December 2006. The reason for the Tier 1 and 2 ratios being lower than the Tier 1 ratio was due to the deduction of investments made in financial subsidiaries and associates from the Tier 1 capital in arriving at the Tier 2 capital.

The ratio for the NDB Group improved from 18.83 per cent to 22.10 per cent for Tier 1 and from 18.48 per cent to 21.95 per cent for Tier 1 and 2.

Regulatory Developments

NDB Bank is substantially in compliance with all the directions, and complies with the monthly and quarterly reporting requirements of the Central Bank.

NDB Group Returns

The NDB Group's earnings per share for the year, increased to Rs 24.81 as compared with Rs 12.70 for the previous year, an increase of 96 per cent. The NDB Group's return on equity for the year increased to 20.59 per cent compared with 12.10 per cent in 2005 while its return on average assets increased to 3.13 per cent for the year compared with 1.70 per cent for the previous year.

Excluding the capital gain made by Capital Development & Investment Co. Ltd. on the sale of part of its holdings in NDB Finance Lanka (Pvt) Ltd. [now known as Aviva NDB Finance Lanka (Private) Ltd.], the NDB Group's return on equity was 10.47 per cent and its return on average assets was 1.78 per cent.

Adoption of new and Revised Sri Lanka Accounting Standards

During the year NDB Bank adopted the new and revised Sri Lanka Accounting Standards as detailed under Accounting Policies on pages 61 to 69. Accordingly, the previous year's figures have been restated where necessary.

Share Price

NDB Bank's share price closed at Rs 201 as compared with Rs 215 at the end of 2005. The All Share Price Index increased during the year from 1,922 to 2,722 (an increase of 42 per cent). The price/book value (PBV) at the year-end was 1.92 as compared with 1.50 at the previous year-end. There was considerable activity on the CSE this year and NDB Bank's share was one of the most heavily transacted.

Post-Balance Sheet Events

The Board of Directors of NDB Bank decided to enter into negotiations with the Commercial Bank of Ceylon Ltd. on a possible merger of the two Banks.

In the event that negotiations are successful, and the manner in which the merger may be achieved is agreed upon, the proposal for such merger will be submitted to the Monetary Board of the Central Bank of Sri Lanka, for its approval.

At this stage therefore, the possible merger of the two Banks is dependent upon the success of the negotiations, and the grant of the necessary approvals by the Monetary Board and other regulatory bodies as well as by the respective shareholders of the two Banks.

Board of Directors



01. S K Wickremesinghe

Chairman

Mr Wickremesinghe is a well known and much respected figure both in Sri Lankan business and diplomatic circles. He was Sri Lanka's High Commissioner to the UK from 1995 to 1999. Before and after this assignment, he chaired the Boards of a number of Sri Lankan blue-chip companies including Commercial Bank of Ceylon, Ceylon Tobacco Company, Chemical Industries (Colombo), CTC Eagle, SriLankan Airlines and Chemanex, a company founded by him.

Mr. Wickremesinghe has served as a Trustee of the Employees' Federation of Ceylon and on a number of Government commissions and boards including the Securities and Exchange Commission, National Education Commission, the Sri Lanka Institute of Development Administration and the Postgraduate Institute of Management of the University of Sri Jayawardenapura.

02. N S Welikala

Director/Chief Executive

Mr Welikala is a Bachelor of Laws of the University of Sri Lanka, a Fellow of the Institute of Chartered Accountants of England and Wales, and an Associate Member of the Institute of Chartered Accountants of Sri Lanka. He worked for several years at the London offices of Ernst & Young, and prior to joining NDB, was CEO of Citibank NA, Colombo.

Mr Welikala served on the Board of NDB as an Alternate Director for the ADB, since its privatization, and joined the NDB as the Deputy General Manager in January 1999. He assumed duties as the General Manager of NDB on 1 January 2002 and became the Chief Executive Officer of NDB Bank on 1 August 2005 with the merger of NDB and NDB Bank. He is also a Director of several NDB Group companies.

03. H D S Amarasuriya

Director

Mr Amarasuriya brings to NDB Bank an impressive range of management, marketing and business skills from his tenure as Chairman of the industrial and retailing conglomerate Singer Sri Lanka, and his experience on the Boards of such companies as Regnis Lanka, Commercial Leasing, Bata Shoe Company and First Capital. He also brings with him substantial experience in international management as a Vice President of Singer N.V. He is also involved in regional management and human resource development programmes across the Asian region.

04. G C B Wijeyesinghe

Director

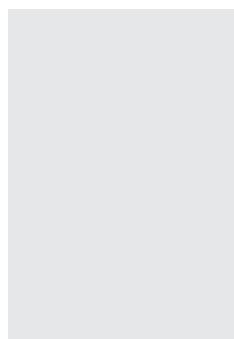
Dr Wijeyesinghe is a Fulbright Scholar and has had a distinguished professional career, retiring as Precedent Partner of KPMG Ford, Rhodes, Thornton & Co. He

also served on the Board of KPMG - Asia Pacific, the External Audit Committee of the IMF and the Council of Corporate Governance. He is a Past President of the Institute of Chartered Accountants of Sri Lanka and the Organization of Professional Association of Sri Lanka. He holds directorates in other public quoted companies. He is a Fellow of the Institute of Chartered Accountants of Sri Lanka, a Fellow of the Society of Chartered Management Accountants and has been conferred a Doctorate (D. Litt) Honoris causa, by the Postgraduate Institute of Management affiliated to the University of Sri Jayawardenapura.

05. L de Mel

Director

Mr Lal de Mel was Managing Director of CIC Paints from 1995 to 2001, prior to which he was a Director of Chemical Industries (Colombo). He was Chairman of the Sri Lanka Insurance Corporation and a Director of the Bank of Ceylon in 2001. He is currently the Chairman of N. Chandraratne Decorators Ltd. and Language Skills Development (Pvt) Ltd. He is a Director of a number of NDB Group companies including Eagle Insurance. He is Co-Chairman of the Trade & Tariff Cluster of NCED. He has served as Chairman of the Ceylon National Chambers of Industries, as



President of the Federation of Chambers of Commerce & Industry and as President of the Sri Lanka Institute of Marketing. Mr de Mel is a Member of the Chartered Institute of Marketing, U.K. He has a Bachelor of Science Degree from the University of Ceylon and Diplomas in Marketing (CIM) and Management (NIBM).

06. S R de Silva

Director

Mr de Silva is a Lawyer, holding an LL.B. (Hons.) Degree. He was the Chief Executive of the Employers' Federation of Ceylon which he served for 25 years till end 1989. He served the International Labour Organization from 1990 until his retirement in July 2001, as Deputy Director of the Employers' Bureau in Geneva. From August 2001 to July 2003 he was Senior Adviser to the International Organization of Employers in Geneva. He is a Director of Lanka Walltile Ltd., Lanka Tiles Ltd., Ceradec (Pvt) Ltd., Lanka Tiles Trading (Pvt) Ltd. and Lanka Walltile (Meepe) Ltd. He is the author of several books and other publications on labour law and relations, human resource management, globalization, the informal economy and other related subjects.

07. A R Gunasekara

Director

Mr Gunasekara is a Fellow of the Institute of Chartered Accountants of Sri Lanka. His career includes a spell of 17 years overseas where he worked for several years with Coopers & Lybrand in Zambia and Botswana. He then joined the Lloyds Insurance Broking Group, Minets, as Head of Finance of its Botswana operation before transferring to Minet's Head Office in London where he served as Financial Controller/Executive Director of the International Holdings Company. On returning to Sri Lanka in 1994, he joined NDB Bank, and retired as its Chief Financial Officer in 2004.

08. S T Nagendra

Director

Mr Nagendra is presently Chairman and Director of several public and private limited companies. He was formerly Chairman of the James Finlay Group, one of Sri Lanka's oldest-established business houses. He is a former Chairman of the Employers' Federation of Ceylon and the British Business Association, and has served on the Committees of the Planters' Association of Ceylon and the Ceylon Chamber of Commerce.

09. Ravindra B Thambiayah

Director

Educated at the University of Madras, where he received a Degree in Economics, Mr. Thambiayah's early career was in tourism. He was appointed to the Board of NDB Bank in February 2006. He is Chairman and Managing Director of several companies in the Renuka Hotels Group as well as of the Cargo Boat Development Company Ltd. and sits on the Board of a number of other companies. He is a Fellow of the Chartered Management Institute (UK).

10. Richard Vokes

Director

Richard Vokes is an economist by training with over 30 years experience working on development in Asia. He joined the Asian Development Bank in 1991 and was Senior Economist in the Office of the Vice-President - East between 1995-1997. Prior to joining ADB, Dr. Vokes held teaching positions at the University of Kent in the United Kingdom and at the Asian Institute of Technology in Bangkok. He has also worked as an Adviser in the Ministry of Agriculture and Cooperatives, Zambia. Dr. Vokes has a PhD in Economics from the University of Hull (awarded in 1978) and a Joint BA (Hons) Degree in Economics and South-East Asian Studies, also from the University of Hull (awarded in 1972).

Senior Management



01. Nihal Welikala - Chief Executive

Mr Welikala is a Bachelor of Laws of the University of Sri Lanka, a Fellow of the Institute of Chartered Accountants of England and Wales, and an Associate Member of the Institute of Chartered Accountants of Sri Lanka. He worked for several years at the London offices of Ernst & Young, and prior to joining NDB, was CEO of Citibank NA, Colombo.

Mr Welikala served on the Board of NDB as an Alternate Director for the ADB, since its privatization, and joined the NDB as the Deputy General Manager in January 1999. He assumed duties as the General Manager of NDB on 1 January 2002 and became the Chief Executive Officer of NDB Bank on 1 August 2005 with the merger of NDB and NDB Bank. He is also a Director of several NDB Group companies.

02. Eran Wickramaratne - Deputy Chief Executive

Mr Wickramaratne is currently Deputy Chief Executive of the NDB Bank. Prior to the merger of the National Development Bank and NDB Bank Ltd., he functioned as Director/Chief Executive Officer of the NDB Bank Ltd. He joined the NDB in 1999 from Citibank, where he was Vice- President and Corporate Bank Head. Mr Wickramaratne was a pioneer of the Government of Sri Lanka's Information Communication Technology driven Development Programme, e-Sri Lanka. He was Chairman of the Information Communication Technology Agency (ICTA). He also served as a Director on the Board of Investment. He holds a Degree in Economics and Politics and a Masters in Economics from the University of London. Mr Wickramaratne is an Eisenhower Fellow.

03. Ranjit Bibile - Vice-President**Head of Corporate Business Development**

He is an Associate Member of the Institute of Bankers, UK. Prior to joining the NDB Bank he served Nations Trust Bank as its Assistant General Manager - Corporate Banking and was Head of Corporate Banking at Deutsche Bank AG. His experience in Banking and Finance exceeds 36 years.

04. Russell de Mel - Vice-President**Head of Risk Management, Credit Administration & Special Projects**

Mr de Mel has served NDB Bank over 25 years, largely in the field of corporate banking. An Associate of the Chartered Institute of Management Accountants (UK), he worked for several private sector organizations prior to joining the Bank.

05. Sujeewa Dissanayake - Vice-President
Head of Information Technology

Before joining the NDB Bank, Mr Dissanayake worked at Pan-Asia Bank and the Union Bank of Colombo as Head of IT. He came to banking from the IBM World Trade Corporation, where he was IT specialist for the finance industry. He has over 23 years experience in IT, 17 of which were acquired in the banking sector. Mr Dissanayake holds a Master's Degree in Business Administration from the University of Lincoln and is a Chartered Member of the British Computer Society.

06. Manilka Fernando - Vice-President**Head of SME Banking & Organizational Development**

Mr Fernando holds a Master's Degree in Business Administration from the University of Georgia, USA, and is a Fellow of the Institute of Chartered Accountants, Sri Lanka. Before joining NDB Bank, he worked at Mashreq Bank, Dubai, UAE and at Citibank, Colombo. He has also held previous positions in finance and accounting. He has over 25 years of working experience in Banking and Finance.

07. Nilam Jayasinghe - Vice-President**Head of Group Audit & Compliance**

Mr Jayasinghe joined the NDB Bank ten years ago and is currently the Head of Group Audit and Compliance. He is a Fellow of the Chartered Institute of Management Accountants (CIMA), UK. Before joining NDB Bank, he served at Aitken Spence & Co. as its Group Treasurer and Director, Aitken Spence Corporate Finance Ltd., prior to which he worked as Finance and Commercial Manager, Lanka Tiles Ltd. Mr Jayasinghe is a Past President of the CIMA Sri Lanka Division and was a member of the Sri Lanka Accounting and Auditing Standards Monitoring Board. He counts over twenty years experience in Finance and Treasury.

08. Chrishanthi Jayawardena - Vice-President**Head of Legal**

She is an Attorney-at-Law who counts over 25 years experience at the NDB Bank. Mrs. Jayawardena was employed at Messrs F. J. & G. De Saram, Attorneys-at-Law before joining the Bank.

09. Nimal Ratnayake - Vice-President**Head of Treasury**

He is an Associate of the Chartered Institute of Bankers, UK. He joined the NDB Group in 1995 and functioned as the Head, Trade Finance for 5 years. He also served the Commercial Bank of Ceylon Ltd. in the capacity of Chief Dealer/ Senior Manager, Treasury and has to his credit over 27 years banking experience.

10. Kumar Weerasuriya - Vice-President**Head of Operations**

Prior to joining NDB Bank he was with several local and international banks, more recently with Standard Chartered Bank and MasterCard International. He counts over 35 years of experience in Banking and IT.

11. Indrajit Wickramasinghe - Vice-President**Head of Consumer Banking & Marketing**

He holds a Master's Degree in Business Administration from the University of Sri Jayawardenapura. He is also a Member of the Chartered Institute of Marketing, UK. Before joining NDB Bank six years ago, he held the position of Head of Marketing at Reckitt & Colman of Ceylon Ltd. Mr Wickramasinghe has over 17 years experience in the Fast-Moving Consumer Goods and Financial Service Sectors.

12. Ajith Wickremaratne - Vice-President**Head of Corporate Banking**

Mr Wickremaratne holds an Engineering Degree from the University of Peradeniya and a Postgraduate Diploma in Business and Financial Administration from the Institute of Chartered Accountants, of Sri Lanka. He has been with NDB Bank for twenty years, his experience ranging from project/infrastructure financing to investment banking and venture capital financing. Presently, he is responsible for corporate banking operations of the Bank. Mr Wickremaratne also holds corporate memberships of the Institute of Civil Engineers, UK and Institute of Engineers, Sri Lanka.

Human Resources

2006 saw the beginning of a new era for NDB Bank following its merger in August 2005. The merger was a long-drawn-out process, achieved in the face of many challenges. In retrospect, the merger was achieved without any labour disputes, in which the successful integration of organizational structures, practices and processes paved the way for the journey to come.

The merger thus presented several strong challenges to HR, which had to be addressed in the context of successful business growth. NDB Bank was transformed into a fully fledged universal bank, with the addition of commercial banking and consumer finance dimensions, to the existing business franchise. NDB Bank was created for demanding Sri Lankans, meeting their corporate and personal banking needs with a widely expanded branch network and a range of products supported by state-of-the-art technology. The human resources challenge is to make this transformation work.

Challenges Posed to HR

The merger presented NDB Bank with the challenge of sustaining teamwork among a group of people, linked through visible and invisible lines of connection, in a way that would meet the demands of a fast-growing business

without compromising service standards and productivity. HR had to recruit the right people for the right jobs, retain key people in critical positions and help people develop new skills and competencies in order to perform new tasks, even as we strove to manage a higher attrition rate than in the previous year. These challenges were made more acute by the high career expectations created by the merger, which had to be addressed in its immediate aftermath. Meeting the expectations of a team of professionals drawn from a wide variety of cultures, backgrounds and demographic groups was challenging enough in itself; it was made more so by skilled professional staff taking up careers beyond our shores or moving to jobs that would pave the way for a move overseas.

Meeting the Challenge

Organisational and business-line 'strategy focus sessions' were held in the context of a post-merger scenario, with HR playing the role of a key partner in the task of aligning human resources and business strategies. The division facilitated the recruitment of over 200 staff to handle the new consumer, personal loans, leasing and debit cards business, resulting in staff growth of 40 per cent by the end of 2006. Furthermore, the division had to act as a catalyst in training and retraining staff.

'Strategy and creativity' training sessions were conducted for senior staff, while the management skills of senior and middle management were further developed to enable them keep abreast of their new, demanding situations. These skills were bolstered by continuous product training, operational risk management training, relationship management, negotiation and selling skills training; in all, our people underwent a total of 1,921 training days during the year.

The acquisition of a subsidiary company, NDB Housing Bank (which became NDB Bank's Home Loans Division) saw the addition of a further 26 staff members, whom HR had to welcome and integrate into the current structure of NDB Bank.

Staff Welfare

As mentioned before, all HR policies were reviewed at the point of merger and the best options available in terms of business and staff implemented with effect from January 2006. This called for extraordinary efforts in terms of staff welfare activity. Salient welfare initiatives included staff loans and assistance in attaining educational and professional qualifications.

Community Upliftment

NDB Bank is keenly aware of the responsibilities of corporate citizenship. Discharging those responsibilities is one of NDB Bank's priorities.

In the year under review, NDB Bank continued its support for the "Prevention of Child Abuse Trust", an ongoing commitment that has now lasted several years. NDB Bank continued its support for the Fishermen's Relief Trust, which provided occupational support for Sri Lankan fishing communities affected by the Asian tsunami of 2004. NDB Bank also donated to the Children's Heart Project of Sri Lanka which is a Government approved charity.

In addition to the above, a variety of public and customer-related initiatives were undertaken.

The Prevention of Child Abuse Trust

Working closely with the Department of Probation & Child Care, the Prevention of Child Abuse Trust has initiated several programmes to help eradicate child abuse. The Trust has, in the past, conducted abuse awareness and prevention programmes among schoolchildren, teachers and parents, together with programmes for the Police Department and numerous publicity initiatives.

In the year under review, NDB Bank supported a donation of books to the National Training and Counselling Centre for Children at Paratta, Panadura, which is run by the Department of Probation & Child Care, and gave gifts of linen to the inmates of the Certified Girls School at Ranmutugala. Three computers were donated to the National Training and Counselling Centre for Children at Paratta, Panadura.

This year, too, a number of awareness programmes on child abuse and its prevention, targeting parents, were held at schools in different parts of the country under the auspices of the Trust.

The Fishermen's Relief Trust Fund

Following the Boxing Day Tsunami of 2004, NDB Bank focused its relief efforts on providing fishing families, the worst-affected members of Sri Lanka's coastal population, with the means to recover their lost livelihoods.



Supporting child abuse prevention: Computers donated to the National Training and Counselling Centre, Paratta, Panadura.

A total of Rs 81 mn was collected from donors at home and abroad, while an additional Rs 20 mn was donated by NDB Bank. NDB Bank took the lead and facilitated the purchase and repair of boats and their distribution among the neediest fishing families. NDB Bank's branch network was of immense value in expediting the programme.

This project was concluded on the 31 March 2006 with a total of 989 fishing boats, engines and fishing nets being donated through the Fund to fishermen in Ampara, Batticaloa, Galle, Gampaha, Colombo, Hambantota, Kalutara, Matara and Trincomalee, thus restoring the livelihoods of nearly 3,000 families affected by the tsunami.

Other Community Activities

Among other community activities carried out in the year under review, the donation of 25 computers to the Training Centre for Disabled Soldiers at Ganemulla was carried out.



An exercise in corporate social responsibility: NDB Bank presents a set of computers to disabled soldiers.

Risk Management

The nature of risk in a financial institution is necessarily dynamic. The risk management process is therefore a constantly evolving one. At NDB Bank, the risk management function was expanded during the year to capture all products under one umbrella in the merged entity. This involved reviewing and updating the processes of Project Financing, Commercial Banking and Housing Finance to bring them onto a common platform without affecting business flow.

NDB Bank focused on structured products during the year, for which appropriate guidelines and speedy processes had to be devised.

The objective of NDB Bank's risk management is to ensure acceptable portfolio quality with a pre-determined return on risk-adjusted capital, thus minimizing volatility of return.

Credit Risk

This is defined as the uncertainty that a borrower or counterparty will meet its agreed obligations. It covers non-payment of capital or interest in full within the agreed timeframe, at the agreed rate of interest and in the agreed currency.

Credit risk is the most important among risks affecting financial institutions, whose main assets are loans and advances. In the case of NDB Bank, loans and advances totalled Rs 44 bn at the end of 2006. Maintaining control of this risk protects customers, investors, employees and other stakeholders, as well as the banking community at large.

Over the years, NDB Bank has implemented adequate measures to keep credit risk exposure within acceptable levels. The indicators below testify to the success of these measures:

Internal policies and processes play a vital role in maintaining the above ratios. The independent Credit Risk Management (CRM) Department reviews and updates these policies periodically in keeping with NDB Bank's business plan. All internal and external credit policies are well documented in a comprehensive credit manual.

To mitigate default risk, a detailed credit evaluation process is in place, carried out by well-trained credit officers. Approval limits, where delegated, are based on the skills and experience of the officer, the internal risk rating of the customer, the size of the facility and the total exposure to the customer or group. To strike a balance between business aggression and credit quality, volume-driven consumer products are offered under pre-approved product programmes with enhanced delegation and appropriate control mechanisms. An overall objective of CRM is to avoid unexpected losses. CRM has therefore introduced procedures to anticipate, track and control potential problem accounts, well in advance.

Portfolio Indicators

	2002	2003	2004	2005	2006
NPL Ratio %	14.0	10.9	9.9	4.2	2.1
Fitch Rating			AA(Ika)	AA(Ika)	AA(Ika)

AA rating denotes very high credit quality. In January 2007, outlook was changed from Stable to Positive indicating favourable prospects.

The Credit Administration and Credit Audit Units monitor the post-approval process to ensure compliance.

Credit concentration is managed by setting appropriate client, group and sector limits. Depending on macro-economic or client-specific factors, these may be changed accordingly.

Apart from the CRM, other institutions managing credit risk include two Internal Credit Committees (ICCs) and the Board Credit Committee (BCC). ICCs are made up of senior management staff from both operational and risk management areas. The ICC for commercial banking functions as an approving body while its counterpart deals with policy matters. The BCC, comprising four Non-Executive Directors, meets once every quarter to critically review portfolio quality, portfolio movement and NPLs, provisioning adequacy, etc. The BCC has the mandate to review existing credit policies and propose changes where necessary.

Preparing for Basel II

Implementation of the Basel II Accord on Capital Adequacy from 2008 is progressing on schedule according to the time frame announced by the Central Bank of Sri Lanka. This Accord will be implemented under the following methodology:

- a standardized approach for credit risk
- a basic indicator approach for market risk
- a standardized approach for operational risk

Based on preliminary calculations the capital required to support the existing portfolio under Basel II, including Credit, Market and Operational risk, will not differ materially from the capital required under present regulations.

As part of the preparatory work for Basel II, presentations have been carried out to educate Bank staff across all divisions and units. The road-map drawn up in 2006 is now being implemented in stages, mainly in the IT system. Periodic updates on progress towards

implementation are provided to the Board. Parallel runs under Basel II commenced from 31 December 2005.

Operational Risk

This category encompasses those risks arising as a result of processing errors, systems and procedural failures, human error, fraud, natural disasters and non-compliance with internal policies, external laws and regulations. While operational risk can never be fully eliminated, NDB Bank endeavours to minimize it by continuously assessing and refining the systems of internal controls. An effective compliance function is also designed to ensure adherence to both internal policies and regulations and external regulatory and statutory requirements.

The internal audit function, which is an integral part of this control framework, assists in identifying, evaluating and mitigating operational risks. The Internal Audit Department through the CEO, reports to the Board Audit Committee, which is a Board

sub-committee entirely composed of Non-Executive Directors. The Committee is independent of NDB Bank's operations, thereby enabling the Internal Audit Department to provide proper assurance to the Committee on the quality and effectiveness of the system of internal controls. The Committee reviews internal and external audit plans and findings, then makes recommendations for appropriate action.

Market Risk

This is the risk that the on- and off-Balance Sheet positions of a financial institution will be adversely affected in value by movements in rates and prices, such as interest rates, foreign exchange rates, equity prices, credit spreads or commodity prices, resulting in a loss of earnings and capital.

Financial institutions may be exposed to market risk in a variety of ways. The exposure may be explicit, in portfolios of securities and equities and in instruments that are actively traded, or implicit, as in interest rate risk arising from a mismatch of loans and deposits.

NDB Bank has complied with and continues to update and maintain a detailed list of all the statutory and other legal requirements it is obliged to fulfil as a bank, taxpayer, employer and listed company. Such compliance is also monitored at Board level.

Balance Sheet Risk

Balance Sheet risks arise as a result of mismatches between related interest-bearing or foreign currency assets and liabilities in the Balance Sheet. These mismatches occur as it is not practically possible to create matching sets of assets and liabilities with every transaction.

Managing Balance Sheet mismatch risk is the responsibility of the Asset and Liability Management Committee (ALCO) of NDB Bank, which meets on fixed calendar dates (or more often if required). Balance Sheet risks can be categorized into interest rate, liquidity and exchange rate risks.

Interest Rate Risk

Interest rate risks arise when matching assets and liabilities do not reprice at the same interval. In such a case, either the asset or the

liability has to be repriced at prevailing market rates, which may be detrimental to NDB Bank.

NDB Bank manages its interest rate risks in the following manner:

- a. by placing limits on mismatches between interest-bearing assets and liabilities maturing at various time 'buckets', according to the risk appetite of NDB Bank at a given interest rate volatility level;
- b. incorporating suitable penalty conditions on the premature uplift of time deposits and fixed tenor loans;
- c. avoiding the use of different benchmarks in pricing assets and liabilities to overcome the basis risk;
- d. focusing on large business lines interest rate risks (such as the government debt trading operation) by having separate ALCO approved mismatch limits placed on such business.

Due to narrowing interest margins in business, even marginal interest movements can cause a significant impact on revenue due to repricing

mismatches in assets and liabilities. To manage these impacts, NDB Bank acquired a state-of-the-art asset and liability management software solution during the last quarter of 2006. It is now in a position to measure liquidity and repricing gaps in the Balance Sheet and resultant revenue implications accurately. This will enable the Bank to take timely corrective action.

Liquidity Risk

A liquidity risk arises when NDB Bank is unable to meet payment obligations for want of funds. This risk is managed by categorizing the liquidity shortfalls in the Balance Sheet into suitable time buckets and placing exposure limits on each bucket. The limits placed correspond to the liquidity available to NDB Bank through various providers, at an agreed confidence level. NDB Bank has also adopted a liquidity policy with the objective of ensuring it has sufficient liquidity to execute its financial obligations on a timely basis and at a fair market price.

Foreign Exchange Risks

NDB Bank exposes itself to foreign exchange risks when assets and liabilities denominated in numerous currencies it deals with do not match one to one in value. NDB Bank's Treasury manages the exposure of each currency separately and also in aggregate with all currencies, within a series of limits approved by the Board. These limits are structured to manage the foreign exchange risks of NDB Bank within its risk appetite while giving a reasonable degree of flexibility to the traders to exploit market opportunities in full.

Legal Risk

This is the risk arising from the inability to enforce contracts, from unexpected lawsuits or from adverse judgments that cause material, unforeseen financial loss to NDB Bank. Inadequate documentation, legal or regulatory incapacity and other factors may result in the unenforceability of contracts (including security documents) with counterparties. Such risks are managed through

the use of advice obtained from NDB Bank's Legal Department, as well as the legal officers allocated to or retained for each unit or branch of NDB Bank. The advice of external counsel is obtained in appropriate circumstances.

Reputation Risk

An organization's reputation is its greatest asset. If impacted, the consequences on financial performance and licence to operate can be detrimental.

In order to maintain its reputation and preserve the confidence of its various stakeholders, NDB Bank has in place an effective compliance system. The Compliance Officer monitors adherence to all applicable laws, regulations and statutory requirements and makes quarterly submissions to the Board and the Board Audit Committee.

A compliance policy and code of conduct has also been issued to all employees to ensure that the highest ethical behaviour is maintained at all times.

Corporate Governance

The Governance Framework

Corporate Governance emphasizes the need to balance the achievement of corporate objectives against the need for a sound framework of controls, in the best interest of all stakeholders, while maintaining high standards of industrial and professional ethics.

NDB Bank, in its endeavour to maintain a high degree of commitment to Corporate Governance practices, has adopted its own Code of Governance, in January 2007. In addition, the following strategies and techniques have been introduced:

- A well articulated corporate strategy against which the success of the overall enterprise and the contribution of individuals can be measured.
- An organization structure, which clearly defines the assignment of responsibilities and accountability backed by appropriate financial and managerial incentive schemes.

- An appropriate structure of the Board and appointments to the Board of Directors.
- Strong internal control systems including internal, external audits and risk management functions independent of the business lines.
- Effective internal and external information flows and ensuring appropriate financial reporting.
- Promoting fairness and transparency in the NDB Bank.
- Appropriate financial and managerial incentives tied to accountability and responsibility.

NDB Bank as a responsible corporate citizen, is guided by the guidelines and regulations issued by the Central Bank of Sri Lanka, Securities and Exchange Commission and the Institute of Chartered Accountants of Sri Lanka and fully supports the recommendations of the Committee on Financial Aspects of Corporate Governance initiated by the Institute of Chartered Accountants of Sri Lanka, including the aspects referred to by the SEC.

Accordingly, this section sets out NDB Bank's responses to these recommendations and the governance practices followed by NDB Bank in general.

The Board of Directors

Directors are representatives of all shareholders and stakeholders, including depositors and ensure that corporate management acts in their best interest. The Board of NDB Bank comprises of ten Directors, nine of whom including the Chairman are Non-Executive Directors. The Chief Executive Officer (CEO) of NDB Bank, functions as an Ex-officio Director. The positions of the Chairman and CEO are kept separate. The filling of vacancies of elected Directors are made on the recommendations of the Nominations Sub-Committee of the Board. The Directors of NDB Bank are professionals and eminent personalities from both the private and public sectors, who are able to add value to the Corporate Governance process. The Board has also formulated appropriate checks and balances to ensure that the Corporate Governance process is upheld at all

times. In addition to the basic governance issues, the Board lays strong emphasis on transparency, accountability and integrity of transactions, in line with some of the recent papers issued on sound governance practices by the Central Bank and the Basel Committee on Banking Supervision. While the Board is entrusted with the responsibility of providing leadership in terms of NDB Bank's strategic aims, it is the responsibility of the corporate management to ensure the implementation of these strategies. To this end, the Board has delegated its authority to the corporate management in operational areas within clearly defined limits.

The Board has met 13 times during this year. Matters considered at these meetings include reviewing of corporate strategy, budgets and forecasts, operational and financial performance, including portfolio quality and reporting to shareholders.

Board Sub-Committees

To facilitate focused attention on specific areas of review, the Board of NDB Bank has appointed five sub-committees that are deemed necessary for effective discharge of their duties. These sub-committees comprise of all Non-Executive Directors. They are the Audit Committee, Credit Committee, Nomination Committee, Strategic Issues Committee and the Human Resource Committee. The minutes of these meetings are tabled at the Board Meetings for information.

Audit Committee

The Audit Committee serves as a means of communication between the Board of Directors, the External Auditors, the Internal Auditors and the management of NDB Bank. NDB Bank has an effective Internal Audit Department which reports to the Audit Committee and which continuously monitors the internal controls, systems and processes of NDB Bank and makes recommendations to improve the processes where necessary. This enables the Internal Audit Department to provide reasonable assurance to the Audit Committee

on the quality and effectiveness of the system of internal controls prevalent within the organization. The Audit Committee approves the audit plans in advance and provides a forum for discussion of issues and recommendations highlighted in the audit reports.

The Audit Committee has a Chairman and three members who are Non-Executive Directors of the Bank. The Audit Committee Charter clearly lays down the authority, responsibilities and the specific duties of the Audit Committee. The Head of Internal Audit acts as its Secretary and the convener. The Audit Committee assists the Board in providing an independent review of financial reporting, the effectiveness of the internal controls and the sufficiency of the internal and external audits and the compliance with Legal/Statutory requirements. The Committee met nine times during the year. The Audit Committee complies with most guidelines for Audit and Audit Committees of listed companies, released by the Securities and Exchange Commission to be adopted on voluntary basis.

Credit Committee

The Credit Committee comprises of four Non-Executive Directors while the Head of Risk Management acts as its Secretary (see also Risk Management Report on pages 36 to 39). The Credit Committee is empowered to approve principles, policies, strategies, processes and control framework for the management of risk. The Credit Committee reviews the quality of the portfolio, large credit exposures, adequacy of provisioning and impact of macro economic changes.

Nomination Committee

The Nomination Committee is headed by the Chairman of NDB Bank and has four Non-Executive Directors serving on it. They evaluate the requirements of the Board of Directors and are responsible for the identification of suitable persons to be recommended by the Board of Directors to the shareholders to be appointed at the AGM and whenever a vacancy arises.

Strategic Issues Committee

The Committee is headed by the Chairman of NDB Bank and has four Non-Executive Directors serving on the Committee. The Committee is responsible for evaluating all major strategic decisions taken by NDB Bank. The Committee reviews the strategy development and implementation process and assesses the key business drivers. The Committee met three times during the year.

Human Resources Committee

This Committee is responsible for maintaining NDB Bank's performance and market oriented remuneration policy for its staff and thereby attracting and retaining quality staff with proven business experience and other required qualities. It is further responsible for reviewing recruitment and promotions of the senior management and executive officers and thereby ensuring that an effective succession plan is in place for NDB Bank. The Committee has a Chairman and four Non-Executive Directors serving on it.

Structure and Composition of the Board Committees as at end 2006

Name of Director	Audit Committee	Credit Committee	Strategic Issues Committee	Human Resources Committee	Nomination Committee
S K Wickremesinghe			*✓		*✓
A A Pio [•]			✓	✓	
H D S Amarasuriya			✓	*✓	✓
G C B Wijeyesinghe	*✓		✓		✓
L de Mel	✓	*✓			✓
S R de Silva		✓		✓	✓
A R Gunasekera	✓		✓	✓	
S T Nagendra		✓		✓	
R B Thambiyah	✓	✓			

* Indicates Chairman of the Sub-Committee

• Resigned w.e.f. 15 October 2006

Compliance

NDB Bank has a process to ensure compliance with applicable laws and regulations and reports to the Board Audit Committee. Monthly and Quarterly Compliance Reports are submitted to the Central Bank of Sri Lanka confirming NDB Bank's compliance with Central Bank guidelines and regulations. Quarterly Compliance Reports are submitted to the Board Audit Committee of NDB Bank in compliance with statutory requirements and with the NDB Bank's Internal Compliance Policy and Code of Conduct. Monthly and Quarterly Compliance Reports are also circulated to the Board of Directors for their information.

In conforming with Anti-Money Laundering legislation, reporting to the Financial Intelligence Unit is done through the Compliance Department as required. The Compliance Officer ensures compliance with regulatory requirements and with internal policies. Regulatory compliance ensures compliance with Central Bank regulations and guidelines, Inland Revenue statutes,

Securities and Exchange Commission of Sri Lanka and the Colombo Stock Exchange regulations, Prevention of Money Laundering Act, Financial Transaction Reporting Act, Suppression of Terrorist Financing Act, Labour Laws of Sri Lanka, The Banking Act, Companies Act, Civil Procedure Code, Mortgage Act, Parate and Debt Recovery Acts and other applicable laws and regulations.

There is a strong culture of internal compliance within NDB Bank, which ensures conformity with the Compliance Policy, and Code of Conduct, the Anti-Money Laundering Policy, the IT Security Policy, the Credit Policy and the HR Policy. NDB Bank has strengthened its Know Your Customer (KYC) and Anti-Money Laundering practices in line with the new regulations and both frontline and operational staff are given appropriate training in this area.

As a bank, we are conscious of our responsibilities to the shareholders, customers and other stakeholders and therefore ensure

our commitment to the highest standards of ethical behaviour in our organization.

Details of Board Meeting held and Attendance of Directors

During the financial year 2006, 13 Board meetings were held. The details of the Directors' participation of such meetings are given below:

Name of Director	No. of Meetings Attended
S K Wickremesinghe	13
H D S Amarasuriya	10
G C B Wijeyesinghe	9
L de Mel	13
S R de Silva	10
A R Gunasekera	12
U L Kadurugamuwa*	–
A A Pio **	8
S T Nagendra	10
R B Thambiayah	8
R W A Vokes***	1
N S Welikala	13

* Resigned with effect from 23 January 2006

** Resigned with effect from 15 October 2006

*** Appointed with effect from 11 December 2006

NDB Group Companies

as at 31 December 2006

Aviva NDB Finance Lanka (Pvt) Ltd.

[formally known as NDB Finance Lanka (Pvt) Ltd.]

Eagle House,
75, Kumaran Ratnam Road, Colombo 2
Tel: +94 11 2310300

Cost of NDB Group's Investment	Rs 741 mn
Profit after Tax	Rs 437 mn
Net Assets	Rs 1,779 mn

Directors: Joydeep Mukherji
(Chairman), S K Wickremesinghe,
N S Welikala, S Roye, A W Paterson

Aviva NDB Finance Lanka (Private) Ltd. is
the holding company of Eagle
Insurance Company Ltd.

NDB Bank's indirect holding - 31.42%

Aviva International Holdings Ltd.	Capital Development & Investment Company Ltd.
58.44%	41.56%

Eagle Insurance Company Ltd.

Eagle House, 75, Kumaran Ratnam Road,
Colombo 2
Tel: +94 11 2310300

Cost of NDB Group's Investment	Rs 741 mn
Profit after Tax	Rs 523 mn
Net Assets	Rs 1,743 mn

Directors: G Barrans (Chairman),
Deepal Sooriyaarachchi (Managing
Director), S Roye, J Mckay,
A W Paterson, S N P Palihena, L de Mel,
N S Welikala, D S P Wikramanayaka

Aviva Finance Lanka (Pvt) Ltd.	Others
87.27%	12.73%

Capital Development and Investment Company Ltd.

40, Navam Mawatha, Colombo 2
Tel: +94 11 2437701

Cost of NDB Bank's Investment	Rs 1,169 mn
Profit after Tax	Rs 1,962 mn
Net Assets	Rs 3,216 mn

Directors: L de Mel (Chairman),
N S Welikala, K Dharmasiri,
A R Gunasekara

NDB Bank	BOC	Others
75.60%	23.92%	0.48%

NDB Investment Bank Ltd.

40, Navam Mawatha, Colombo 2
Tel: +94 11 2300385

Cost of NDB Bank's Investment	Rs 32 mn
Profit after Tax	Rs 35 mn
Net Assets	Rs 75 mn

Directors: S K Wickremesinghe
(Chairman), N S Welikala,
E Wickramaratne, L de Mel,
A Wickremeratne, V Kulatilleke
(CEO and Ex-Officio Director)

NDB Bank	Citi Group
80.1%	19.9%

NDBS Stockbrokers (Pvt) Ltd.

40, Navam Mawatha, Colombo 2
Tel: +94 11 2314170

Cost of NDB Bank's Investment	Rs 27 mn
Profit after Tax	Rs 17 mn
Net Assets	Rs 134 mn

Directors: S K Wickremesinghe
(Chairman), N S Welikala,
S N Jayasinghe, L de Mel,
D S P Wikramanayaka

NDB Bank
100%

Development Holdings (Pvt) Ltd.

42, Navam Mawatha, Colombo 2
Tel: +94 11 2436279

Cost of NDB Bank's Investment	Rs 428 mn
Profit after Tax	Rs 117 mn
Net Assets	Rs 1,352 mn

Directors: N S Welikala, S N Jayasinghe,
A R Gunasekara, D S P Wikramanayaka,
B A S Angunawela, G V W D Gamaarachchi

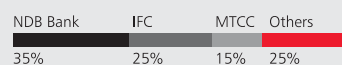
NDB Bank	EDB
58.61%	41.39%

Maldives Finance Leasing Company (Pvt) Ltd.

04-01 Aage, 12, Boduthakurufaanu
Magu, Male 20-094, Republic of Maldives
Tel: +(960) 315605 / 315606

Cost of NDB Bank's Investment	Rs 165 mn
Profit after Tax	Rs 69 mn
Net Assets	Rs 670 mn

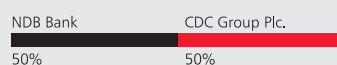
Directors: Rifaath Jaleel (*Chairman*),
N S Welikala, Hussain Afeef, Moosa Zameer,
Abdul Mushin Abdulla,
Ms Fathimath Manike, G Galludec,
E D P Soosaipillai (*Director & CEO*)

**NDB Venture Investments (Pvt) Ltd.**

7th Floor, McLaren's Building, 123,
Bauddhaloka Mawatha, Colombo 4
Tel: +94 11 4510505

Cost of NDB Bank's Investment	Rs 67.5 mn
Profit after Tax	Rs 2 mn
Net Assets	Rs 10 mn

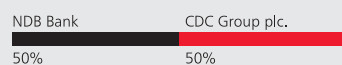
Directors: Ms R L Nanayakkara
(*Chairman*), G C B Wijeyesinghe,
Ms A M Byworth, N S Welikala

**Ayojana Fund (Pvt) Ltd.**

7th Floor, McLaren's Building,
123, Bauddhaloka Mawatha, Colombo 4
Tel: +94 11 4510505

Cost of NDB Bank's Investment	
Investment	Rs 0.1 mn
Profit after Tax	Rs 22 mn
Net Assets under Management	Rs 98 mn

Directors: Ms R L Nanayakkara
(*Chairman*), G C B Wijeyesinghe,
Ms A M Byworth, N S Welikala



Evolving through the years

Milestones

1979

State-owned National Development Bank of Sri Lanka (NDB) established, funded by the Government of Sri Lanka and multilateral agencies

World Bank appoints NDB apex refinancier for its SMI credit lines

1989

NDB moves to its own building at Navam Mawatha, Colombo

1992

NDBS Stockbrokers and NDB Venture Investments set up

1993

Privatization: 67 per cent of NDB equity now in private hands and listed on the Colombo Stock Exchange

1996

First branch opens in Negombo

1997

Full privatization

NDB Investment Bank established

Eagle Insurance acquired via CDIC Ltd.

1999

NDB partners with Zurich Insurance and Eagle Insurance

NDB Housing Bank was set up

2001

NDB Bank Ltd. launched, and the business of ABN Amro Bank NV, Sri Lanka (Colombo branch) operations taken over by NDB Bank Ltd.

2005

NDB converts from an incorporated body to a Public Company under the Companies Act

NDB Bank Ltd. merges with NDB to create a new, expanded National Development Bank Ltd. (NDB Bank)

2006

NDB Bank partners with Aviva Insurance on Eagle Insurance

NDB Housing Bank merged with NDB Bank to promote home loans through the branch network

Report of the Directors

The Directors of the National Development Bank Ltd. (NDB Bank) have pleasure in presenting their Report and the audited Financial Statements for the year ended 31 December 2006.

Principal Activities

The principal activities of NDB Bank and the NDB Group are described under Note 1 to the Financial Statements on page 70.

Details of the NDB Group companies indicating NDB Bank's own holding in key companies is shown on pages 44 and 45.

Review of Business

The Chairman's Review, the Chief Executive's Review, the Financial Review and the Operations Review which form an integral part of the Directors' Report, contain a detailed description of the operations of NDB Bank during the year ended 31 December 2006 and contain a fair review of NDB Bank's affairs.

Directors' Responsibility for Financial Reporting

The Directors are responsible for the preparation of the Financial Statements of NDB Bank to reflect a true and fair view of the state of its affairs. The Directors are of the view that these Financial Statements have been prepared in conformity with the requirements of the Sri Lanka Accounting Standards, Companies Act No. 17 of 1982 and the Banking Act No. 30 of 1988 (as amended).

The Directors are satisfied that the Financial Statements, presented on pages 54 to 104 inclusive, give a true and

fair view of the state of affairs of NDB Bank and the NDB Group as at 31 December 2006 as well as the profit for the year then ended.

The Directors consider that, in preparing these Financial Statements, suitable accounting policies have been used which are applied consistently and supported by reasonable and prudent judgement and that all applicable accounting standards have been followed. The Financial Statements are prepared on a going concern basis.

The Directors are satisfied that all statutory payments have been made up to date.

Corporate Governance

The Directors are responsible for the governance of NDB Bank including the establishment and maintenance of NDB Bank's systems of internal financial control. Internal control systems are designed to meet the particular needs of the organization concerned, and the risks to which it is exposed and by their nature they can provide reasonable but not absolute assurance against material misstatement or loss. The Directors are satisfied that a strong control environment is prevalent within NDB Bank and that the internal control systems referred to above are effective.

A description of NDB Bank's Corporate Governance practices is set out on pages 40 to 43.

Profits, Reserves and Dividends

The NDB Group's profit before taxation including that of its subsidiaries and its share of profit from associate

companies amounted to Rs 3,427 mn (compared to Rs 1,866 mn in 2005). After deducting Rs 1,220 mn (compared to Rs 593 mn in 2005) for taxation, the profit after tax for the year amounted to Rs 2,207 mn (compared to Rs 1,273 mn in 2005). Details are given in the Income Statement on page 54.

The figures relating to the operations of NDB Bank are summarized as follows:

	2006 Rs mn	2005 Rs mn
Profit before tax	2,086	1,071
Less tax	1,081	446
Profit after tax	1,005	626

Final Dividend

The Directors propose that a final dividend of Rs 5.00 per share, on the increased number of shares resulting from the bonus issue made during 2006, be paid out of the profits of NDB Bank for the year 2006. NDB Bank paid a final dividend for the previous year of Rs 6.00 per share on the number of shares in issue prior to the said bonus issue.

Details of the reserves are shown in the Statement of Changes in Equity on page 59.

Branch Expansion

In keeping with NDB Bank's Branch expansion scheme eight branches were opened during the year thereby bringing the total number of branches to 31 as at the end of 2006.

Property, Plant & Equipment and Depreciation

Details of the property, plant and equipment of NDB Bank, additions made during the year and the depreciation charges for the year are shown in Note 30 to the Financial Statements on pages 86 to 88.

Donations

No donations to external charitable or political organizations were made by NDB Bank during the year, except for funds donated to the Children's Heart Project of Sri Lanka (a Government approved charity).

Corporate Social Responsibility

The report on the Community Upliftment of NDB Bank is given on page 35 of the Annual Report.

Portfolio Loss Provision

The Directors have taken all reasonable steps in relation to the writing off and providing for portfolio losses. In respect of bad and doubtful loans they have satisfied themselves that all known bad loans and advances have been written off and that, where necessary, adequate provision has been made for doubtful loans. During the last quarter of 2006, the Central Bank mandated that banks build up a 1 per cent general provision on their performing portfolio and have given them time to make this provision over ten quarters ending on 31 March 2009. Accordingly, NDB Bank built up its general provision to Rs 275 mn by 31 December 2006.

In terms of the Sri Lanka Accounting Standards, provision has been made for any permanent diminution in value in the case of investment securities and any fall in value of dealing securities on an aggregate portfolio basis.

As at the date of this report, the Directors are not aware of any circumstances, which would render inadequate the amounts written off or provided for portfolio losses in the accounts of the NDB Group.

Post Balance Sheet Events

The Board of Directors of NDB Bank decided to enter into negotiations with the Commercial Bank of Ceylon Ltd. on a possible merger of the two Banks.

In the event that negotiations are successful, and the manner in which the merger may be achieved is agreed upon, the proposal for such merger will be submitted to the Monetary Board of the Central Bank of Sri Lanka, for its approval.

At this stage therefore, the possible merger of the two Banks is dependent upon the success of the negotiations, and the grant of the necessary approvals by the Monetary Board and other regulatory bodies as well as by the respective shareholders of the two Banks.

Share Capital

The authorized share capital of NDB Bank at the beginning and end of the year under review was Rs. 2 bn.

The issued share capital which was Rs 545.7 mn at the beginning of the year, increased to Rs 818.5 mn due to the issue of 27,285,128 new shares to the shareholders by way of bonus shares at a ratio of 1 share for every 2 shares held in NDB Bank. Accordingly, a sum of Rs. 272,851,280/- was capitalized from the balance standing to the Credit of the Revenue Reserves Account in the Balance Sheet of NDB Bank as at 31 December 2006.

Directors and their Interests

In terms of the provisions of the Memorandum and Articles of Association of NDB Bank, the Board of Directors, as at 31 December 2006, consists of ten Directors, including the Chairman, is made up as follows:

- Six Directors appointed as the first Directors of National Development Bank Ltd.
- The Chief Executive Officer is an ex-officio Director, with voting rights.
- Three Directors appointed on casual vacancies.

In terms of the provisions of the Memorandum and Articles of Association of NDB Bank, one-third of the elected Directors shall retire from office and new Directors will be elected at each Annual General Meeting of NDB Bank.

Directors' interests in contracts with NDB Bank, both direct and indirect, are disclosed in Note 45 to the Financial Statements on pages 100 to 102. These interests have been declared at and recorded in the minutes of the relevant Board meetings and such Directors have not taken part in any deliberations or decisions of the Board with respect to such contracts.

The Directors who held office during the year under review are shown on the Inner Back Cover.

Major Shareholders

The 20 largest shareholders of NDB Bank as at 31 December 2006 are given on page 107 together with an analysis of the shareholdings. As at that date NDB Bank had 7,275 shareholders.

Board Sub-Committees

There are five permanent sub-committees of the Board, namely the Audit Committee, the Strategic Issues Committee, the Human Resources Committee, the Credit Committee and the Nominations Committee. Members of these five committees during the year are given on the Inner Back Cover.

Directors' Shareholdings

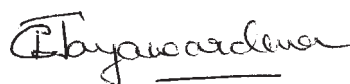
Shareholdings of the Directors in NDB Bank as at the year-end and their corresponding holdings as at the end of the previous year are as shown below:

Name	As at 31.12.06	As at 31.12.05
S K Wickremesinghe	450	300
H D S Amarasuriya	9,075	3,950
A R Gunasekara	883	589
Mrs S Cooray	—	—
G C B Wijeyesinghe	—	—
A A Pio	—	—
N S Welikala	—	—
S R de Silva	—	—
Lal de Mel	15,541	10,361
U L Kadurugamuwa	—	—
S T Nagendra	4,575	3,050
R B Thambiyah	—	—
R W A Vokes	—	—

Auditors

The Financial Statements for the year ended 31 December 2006 have been audited by M/s. Ernst & Young, Chartered Accountants. The said Auditors have indicated their willingness to offer themselves for reappointment. A resolution appointing M/s. Ernst & Young as Auditors and authorizing the Directors to fix their remuneration will be proposed at the Annual General Meeting.

By Order of the Board



C L Jayawardena

Secretary to the Board

19 March 2007

Statement of Directors' Responsibilities

The Directors of the National Development Bank Ltd. (NDB Bank) are required by relevant statutory provisions to prepare and table at a General Meeting of NDB Bank, such Financial Statements as may be necessary, which give a true and fair view of the state of NDB Bank and the NDB Group.

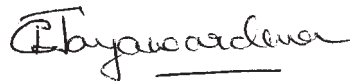
It is also the responsibility of the Directors to ensure that NDB Bank maintains proper accounting records and to take reasonable steps as far as practical to ensure the accuracy and reliability of accounting records and to prepare Financial Statements using appropriate accounting policies applied consistently and supported by reasonable and prudent judgment and estimates in compliance with the Sri Lanka Accounting Standards, the Banking Act No. 30 of 1988 (as amended), the Companies Act No. 17 of 1982 and the Listing Rules of the Colombo Stock Exchange. Changes in the accounting policies where applicable and the rationale for the changes have been disclosed in the 'Notes to the Financial Statements'.

The Directors have been responsible for taking reasonable measures and care to safeguard the assets of NDB Bank and the NDB Group and to prevent and

detect frauds and other irregularities. The Directors have instituted an effective and comprehensive system of internal controls and an effective system of monitoring its effectiveness, internal audit being one of them. The Board has been provided additional assurance on the reliability of the Financial Statements through a process of independent and objective review performed by the Audit Committee. Please refer the Audit Committee Report on page 52 of this Report.

Ms. Ernst & Young, Chartered Accountants have been made available with all records of NDB Bank including the Financial Statements by the Board of Directors which they have examined and have expressed their opinion which appears as reported by them on page 53 of this report.

By Order of the Board



C L Jayawardena

Secretary to the Board

19 March 2007

Financial Reports

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55	Balance Sheet
56	Cash Flow Statement
59	Statement of Changes in Equity
61	Significant Accounting Policies
70	Notes to the Financial Statements

Financial Calendar 2006

Interim Quarterly Unaudited Reports for 2006

March	19 May 2006*
June	21 August 2006*
September	23 November 2006*
December	28 February 2007*

Annual Reports and Accounts

2004	12 April 2005
2005	4 April 2006
2006	4 April 2007

Meetings

Twelfth Annual General Meeting	20 April 2004
Thirteenth Annual General Meeting	6 May 2005
First Annual General Meeting of National Development Bank Ltd.	26 April 2006
Second Annual General Meeting	26 April 2007

Dividends

Final Dividend 2003	20 April 2004
Final Dividend 2004	6 May 2005
Final Dividend 2005	26 April 2006
Final Dividend 2006	26 April 2007**

* Published in the newspapers

** Subject to approval by the Shareholders

The Audit Committee is empowered to review and monitor the financial reporting process of NDB Bank, so as to provide additional assurance on the reliability of the Financial Statements through a process of independent and objective review. As such, the Audit Committee acts as an effective forum in assisting the Board of Directors in discharging their responsibilities of ensuring the quality of financial reporting and related communications to the shareholders and the public.

As at year end, the Audit Committee comprised of four non-executive members of the Board. The CEO/Deputy CEO, Vice President (Audit & Compliance), Heads of Audit, Audit staff, Compliance Officer, representatives from the External Auditors and relevant Operational Managers attend these meetings by invitation. The Head of Internal Audit functions as the Secretary to the Committee.

The Board Audit Committee's authority, responsibilities and the specific duties have been formalized through an Audit Committee Charter. By this, the Audit Committee is empowered among other things to examine any matters relating to the financial affairs of NDB Bank and to review the adequacy of the internal control procedures, coverage of internal and external audit programmes, disclosure of accounting policies, compliance with statutory and corporate governance requirements etc. The Committee also provides a forum for the impartial review of the reports of internal and external audits, and to take into consideration findings and recommendations stated therein relating to significant business risks and control issues.

The Audit Committee reviews significant business risks and internal control issues and suggests appropriate remedial measures. The Committee along with the Board reviewed the quarterly financial results to ensure compliance with mandatory banking and statutory requirements.

The Compliance Officer monitors NDB Bank's compliance with the applicable laws and regulations and ensure adherence to NDB Bank's Compliance Policy/Code of Ethics by all employees. The Compliance Officer reports to the Audit Committee and the Board of Directors, and submits a quarterly statement on the status of NDB Bank's compliance with Central Bank Directions/Regulations, Local Statutory Requirements and appropriate International Regulations.

During the year, nine Audit Committee meetings were held and reports of internal and external audits were discussed at these meetings. The minutes of the Committee were made available to the Board of Directors for information.

Based on the reports submitted by the External Auditors, Internal Auditors and the risk reviews performed by NDB Bank, the Audit Committee is of the view that the control environment prevalent within NDB Bank is satisfactory and provides reasonable assurance that the financial position of NDB Bank is well monitored and the assets are safeguarded.

The Audit Committee has recommended to the Board of Directors that M/s. Ernst & Young, (Chartered Accountants) be reappointed as Auditors for the financial year ending 31 December 2007 subject to the approval of the shareholders at the Annual General Meeting.



G C B Wijeyesinghe
Chairman

Board Audit Committee

23 February 2007



■ **Chartered Accountants**
201 De Saram Place
P. O. Box 101
Colombo 10
Sri Lanka

■ Telephone : (0) 11 2463500
Fax Gen : (0) 11 2697369
Tax : (0) 11 5578180
E-Mail : eysl@lk.ey.com

AUDITORS' REPORT TO THE MEMBERS OF NATIONAL DEVELOPMENT BANK LTD.

We have audited the Balance Sheet of National Development Bank Ltd. as at 31 December 2006, the Consolidated Balance Sheet of NDB Bank and its Subsidiaries as at that date and the related Statements of Income, Cash Flows and Changes in Equity for the year then ended, together with the Accounting Policies and Notes as set out on pages 54 to 104.

Respective Responsibilities of Directors and Auditors

The Directors are responsible for preparing and presenting these financial statements in accordance with the Sri Lanka Accounting Standards. Our responsibility is to express an opinion on these financial statements, based on our audit.

Basis of Opinion

We conducted our audit in accordance with the Sri Lanka Auditing Standards, which require that we plan and perform the audit to obtain reasonable assurance about whether the said financial statements are free of material misstatements. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the said financial statements, assessing the accounting principles used and significant estimates made by the Directors, evaluating the overall presentation of the financial statements, and determining whether the said financial statements are prepared and presented in accordance with the Sri Lanka Accounting Standards. We have obtained all the information and explanations, which to the best of our knowledge and belief were necessary for the purposes of our audit. We therefore believe that our audit provides a reasonable basis for our opinion.

Opinion

In our opinion, so far as appears from our examination, NDB Bank maintained proper books of account for the year ended 31 December 2006, and to the best of our information

and according to the explanations given to us, the said Balance Sheet and related statements of Income, Cash Flows, Changes in Equity and the Accounting Policies and Notes thereto, which are in agreement with the said books and have been prepared and presented in accordance with the Sri Lanka Accounting Standards, provide the information required by the Companies Act No. 17 of 1982 and the Banking Act No. 30 of 1988 and amendments thereto and give a true and fair view of NDB Bank's state of affairs as at 31 December 2006 and of its Profit and Cash Flows for the year then ended.

In our opinion, the Consolidated Balance Sheet and Statements of Income, Cash Flows, Changes in Equity and the Accounting Policies and Notes thereto have been properly prepared and presented in accordance with the Sri Lanka Accounting Standards, provide the information required by the Companies Act No. 17 of 1982 and the Banking Act No. 30 of 1988 and amendments thereto and give a true and fair view of the state of affairs as at 31 December 2006 and of its Profit and Cash Flows for the year then ended of NDB Bank and its Subsidiaries dealt with thereby, so far as concerns the members of NDB Bank.

Directors' Interest in Contracts with NDB Bank

According to the information made available to us, Directors of NDB Bank were not directly or indirectly interested in contracts with NDB Bank during the year ended 31 December 2006, except as stated in Note 45 to these financial statements.

(Sgd.)

Ernst & Young

Chartered Accountants

Colombo

23 February 2007

■ **Partners** : A D B Talwatte FCA FCMA T K Bandaranayake FCA M P D Cooray ACA FCMA
Ms. Y A De Silva ACA W R H Fernando FCA FCMA A P A Gunasekera FCA FCMA
A Herath FCA D K Hulangamuwa ACA FCMA LLB (Lond) A S M Ismail ACA FCMA
H M A Jayasinghe ACA FCMA Ms. G G S Manatunga ACA Ms. L C G Nanayakkara FCA FCMA

		NDB BANK		NDB GROUP	
<i>For the year ended 31 December</i>		2006	2005	2006	2005
	Note	Rs '000	Rs '000 * Restated	Rs '000	Rs '000 * Restated
GROSS INCOME	2	6,888,379	4,288,138	8,208,824	7,116,094
Interest income	3	5,689,394	3,454,199	6,075,601	5,035,347
Interest expenses	4	3,287,181	1,859,555	3,223,014	2,342,038
NET INTEREST INCOME		2,402,213	1,594,644	2,852,587	2,693,309
Other income	5	1,191,487	808,034	2,125,725	2,054,842
Income from operating leases		7,498	25,905	7,498	25,905
Depreciation - operating leases		(6,312)	(19,845)	(6,312)	(19,845)
NET OTHER INCOME		1,192,673	814,094	2,126,911	2,060,902
NET INCOME		3,594,886	2,408,738	4,979,498	4,754,211
OPERATING EXPENSES	6				
Personnel costs		710,940	475,230	816,856	1,087,928
Staff retirement benefits	7	11,460	24,078	13,183	43,579
Other administrative and general expenses	8	782,527	494,490	923,173	1,411,726
Write off of intangible assets on business combinations		–	171,763	–	171,763
Amortization of goodwill		–	–	–	41,737
Total operating expenses		1,504,927	1,165,561	1,753,212	2,756,733
PROFIT BEFORE PROVISIONS		2,089,959	1,243,177	3,226,286	1,997,478
Provision for bad and doubtful debts and for fall in value of securities	9	3,559	171,786	13,385	153,461
		2,086,400	1,071,391	3,212,901	1,844,017
Share of associate companies' profit	10	–	–	214,453	21,665
PROFIT BEFORE TAXATION		2,086,400	1,071,391	3,427,354	1,865,682
Taxation	11	(1,081,403)	(445,817)	(1,220,449)	(593,019)
PROFIT FOR THE YEAR		1,004,997	625,574	2,206,905	1,272,663
PROFIT ATTRIBUTABLE TO EQUITY HOLDERS OF THE PARENT		1,004,997	625,574	2,030,484	1,036,078
PROFIT ATTRIBUTABLE TO MINORITY SHAREHOLDERS		–	–	176,421	236,585
		1,004,997	625,574	2,206,905	1,272,663
Earnings per share (in Rs)	13	12.28	7.64	24.81	12.66

* Refer Note No. 48 on page 104.

Significant Accounting Policies and Notes to the Financial Statements disclosed on pages 61 to 104 are an integral part of these Financial Statements.

23 February 2007

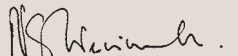
		NDB BANK		NDB GROUP	
As at 31 December		2006	2005	2006	2005
	Note	Rs '000	Rs '000	Rs '000	Rs '000
			*Restated		*Restated
ASSETS					
Cash and short-term funds	14	3,394,766	1,288,970	4,467,154	2,098,775
Balances with Central Bank	15	1,575,260	818,660	1,575,260	818,660
Investment in sinking fund	16	2,873,288	2,396,305	2,873,288	2,396,305
Investments held for trading	17	5,632,180	4,503,337	5,632,180	4,781,859
Investments held to maturity	18	3,048,178	2,077,246	3,059,602	8,871,549
Securities purchased under resale agreements		—	—	—	2,931,816
Commercial paper		605,100	97,181	605,100	97,181
Bills of exchange	19	1,591,931	970,797	1,591,931	970,797
Loans and advances	20	38,947,962	33,849,732	38,957,189	35,167,150
Lease rentals receivable	21	1,449,077	731,303	1,449,077	731,303
Interest receivable	22	420,018	94,915	420,018	106,650
Investments in subsidiary companies	25	1,656,466	2,363,966	—	—
Investments in associate companies	26	233,062	165,562	1,179,006	241,216
Group balances receivable	27	36,247	64,799	1,663	25,309
Other assets	28	1,073,927	811,238	1,231,308	2,978,902
Deferred tax	29	43,192	17,777	43,192	17,777
Property, plant & equipment	30	671,883	698,260	691,529	1,606,599
Investment property	44	—	—	1,200,000	—
Goodwill	31	—	—	—	872,719
Total assets		63,252,537	50,950,048	64,977,497	64,714,567
LIABILITIES					
Deposits	32	21,161,104	13,953,729	21,161,104	13,953,729
Borrowings	33	24,938,204	22,705,464	23,181,509	23,273,095
Securities sold under repurchase agreement		6,022,016	4,525,758	6,022,016	4,525,758
Non-life insurance reserve		—	—	—	858,759
Long-term insurance fund		—	—	—	9,238,184
Other liabilities	34	1,869,744	1,635,587	1,983,671	2,846,951
Taxation		598,824	191,220	640,408	220,429
Dividends payable		107,918	7,996	107,918	7,996
Total liabilities		54,697,810	43,019,754	53,096,626	54,924,901
FUNDS EMPLOYED					
Share capital	35	818,554	545,703	818,554	545,703
Share premium reserve	36	214,377	214,377	214,377	214,377
Statutory reserve fund	37	818,554	545,703	818,554	545,703
Revenue reserves	38	6,703,242	6,624,511	8,715,154	7,509,404
		8,554,727	7,930,294	10,566,639	8,815,187
Minority interests		—	—	1,314,232	974,479
Total funds employed		8,554,727	7,930,294	11,880,871	9,789,666
Total liabilities and funds employed		63,252,537	50,950,048	64,977,497	64,714,567
Commitments and contingencies	40	14,052,983	8,925,857	14,052,983	9,025,490

*Refer Note No. 48 on page 104.

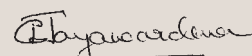
Significant Accounting Policies and Notes to the Financial Statements disclosed on pages 61 to 104 are an integral part of these Financial Statements.

Approved for and on behalf of the Board of Directors on 23 February 2007.


S K Wickremesinghe
 Chairman


N S Welikala
 Chief Executive Officer


G C B Wijeyesinghe
 Director


C L Jayawardena
 Secretary to the Board

		NDB BANK		NDB GROUP	
<i>For the year ended 31 December</i>		2006	2005	2006	2005
	Note	Rs '000	Rs '000	Rs '000	Rs '000
CASH FLOWS FROM OPERATING ACTIVITIES					
Interest received		5,130,972	3,274,573	5,592,273	4,980,879
Fee based income received		352,579	143,114	491,938	275,827
Dividend income received		522,853	277,836	288,323	104,849
Other income received		322,247	113,535	518,186	2,394,120
Lease rentals received		338,115	159,934	338,115	159,934
Lease disbursements		(1,018,838)	(469,769)	(1,018,838)	(469,769)
Interest paid		(2,889,555)	(1,764,714)	(2,953,947)	(2,056,393)
Personnel costs paid		(688,716)	(398,480)	(676,121)	(671,747)
General expenses paid		(624,283)	(416,268)	(937,251)	(2,058,168)
VAT paid		(349,001)	(207,699)	(354,625)	(256,865)
Income taxes paid		(202,603)	(143,377)	(239,562)	(217,921)
Net (increase)/decrease in other receivables		(262,890)	(79,585)	(272,910)	(25,920)
Net increase/(decrease) in other liabilities		(132,920)	(163,713)	(54,168)	134,373
Net cash provided by operating activities		497,960	325,387	721,413	2,293,199
CASH FLOWS FROM INVESTING ACTIVITIES					
Net increase in investments					
Acquisition of subsidiaries	b	(156,000)	(390,000)	(131,412)	(273,000)
Redemption of preference shares held in a subsidiary		–	90,000	–	–
Disposal of a subsidiary	c	70,000	–	2,391,272	–
Government treasury bills and bonds		(1,312,163)	535,490	(1,528,431)	2,487,447
Change in other investments		(1,677,710)	(41,799)	(2,870,308)	(3,746,960)
Securities sold under repurchase agreements		1,496,258	50,026	1,496,258	73,926
Transfer of assets and liabilities of subsidiaries		24,588	1,405,736	–	–
Net increase in loans and advances		(5,166,127)	(1,838,704)	(5,470,102)	(2,134,395)
Deposits from customers		7,207,375	2,752,470	7,207,375	2,555,764
Net due to/(from) related companies		28,553	7,037	31,077	5,870
Expenditure on property, plant & equipment		(164,992)	(75,862)	(166,130)	(163,646)
Proceeds from sale of property, plant & equipment		9,692	330	9,714	330
Net cash provided by/(used in) investing activities		359,474	2,494,724	969,313	(1,194,664)
CASH FLOWS FROM FINANCING ACTIVITIES					
(Decrease)/increase in borrowings		2,232,742	(832,111)	1,838,379	(303,568)
Dividend paid		(227,500)	(321,958)	(380,833)	(375,525)
Net cash provided by/(used in) financing activities		(2,005,242)	(1,154,069)	1,457,546	(679,093)
NET INCREASE/(DECREASE) IN CASH AND CASH EQUIVALENTS					
		2,862,676	1,666,042	3,148,272	419,442
CASH AND CASH EQUIVALENTS AT THE BEGINNING OF THE YEAR					
		2,107,350	441,308	2,893,867	2,474,425
CASH AND CASH EQUIVALENTS AT THE END OF THE YEAR	a	4,970,026	2,107,350	6,042,139	2,893,867

Significant Accounting Policies and Notes to the Financial Statements disclosed on pages 61 to 104 are an integral part of these Financial Statements.

	NDB BANK		NDB GROUP	
	2006 Rs '000	2005 Rs '000	2006 Rs '000	2005 Rs '000
NOTE A				
RECONCILIATION OF CASH AND CASH EQUIVALENTS				
Cash and short-term funds	3,394,766	1,288,970	4,467,154	2,098,775
Balances with Central Bank	1,575,260	818,660	1,575,260	818,660
Less: Bank overdraft	–	(280)	(275)	(23,568)
	4,970,026	2,107,350	6,042,139	2,893,867

NOTE B

TRANSFER OF ASSETS AND LIABILITIES OF NDB HOUSING BANK LTD. WITH EFFECT FROM 1 SEPTEMBER 2006		2006 Rs '000
Cash and bank balances		24,588
Loans and advances		2,007,810
Other assets		6,022
Property, plant & equipment		1,666
Total assets		2,040,086
Borrowings		760,695
Other liabilities		617,923
Total liabilities		1,378,618
Net assets		661,468
Difference between the investment and net assets		64,532
		726,000
Discharged by:		
Cost of earlier acquisition		570,000
Acquisition during the year		156,000
		726,000
Analysis of outflow of cash and cash equivalents in respect of the transfer of assets and liabilities of NDB Housing Bank Ltd. on 1 September 2006.		
Cash and cash equivalents on acquisition		131,412

NOTE C**DISPOSAL OF PART OF HOLDING IN SUBSIDIARY COMPANIES**

	NDB Venture Investments (Private) Ltd.	NDB Finance Lanka (Private) Ltd.	2006 Total Rs'000
Cash and bank balances	168,810	194,848	363,658
Goodwill	–	196,998	196,998
Insurance assets	–	1,900,706	1,900,706
Investment securities	101,343	10,250,451	10,351,794
Other assets	7,409	245,490	252,899
Property, plant & equipment	–	302,162	302,162
Total assets	277,562	13,090,655	13,368,217
Insurance liabilities	–	10,739,162	10,739,162
Other liabilities	290	611,601	611,891
Minority interest	–	188,811	188,811
Cost of acquisition	–	18,070	18,070
Total liabilities	290	11,557,644	11,557,934
Net assets	277,272	1,533,011	1,810,283
unamortized goodwill	–	605,613	605,613
	277,272	2,138,624	2,415,896
Discharged by Sales Proceeds	70,000	2,703,000	2,773,000

Analysis of net inflow of cash and cash equivalents in respect of the disposal of assets and liabilities of NDB Finance Lanka (Private) Ltd. on 1 February 2006.

Cash and cash equivalents on disposal	(98,810)	2,490,082	2,391,272
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For the year ended 31 December

		Share Capital	Share Premium	Statutory Reserve Fund	General Reserve	Retained Profit	Total
	Note	Rs '000	Rs '000	Rs '000	Rs '000	Rs '000	Rs '000
NDB BANK							
Balance as at 1 January 2005		537,500	91,667	537,500	5,805,707	782,953	7,755,327
Effect on adoption of revised SLAS-14 on Income Taxes	29	–	–	–	–	121,561	121,561
Balance as at 1 January 2005 (Restated)		537,500	91,667	537,500	5,805,707	904,514	7,876,888
Issue of new shares		8,203	122,710	–	–	–	130,913
Net profit for the year (Restated)		–	–	–	–	625,574	625,574
Transfer to statutory reserve fund		–	–	8,203	–	(8,203)	–
Provision for goodwill on business combinations (Restated)	31	–	–	–	–	(380,581)	(380,581)
Dividend paid		–	–	–	–	(322,500)	(322,500)
Balance as at 31 December 2005		545,703	214,377	545,703	5,805,707	818,804	7,930,294
Balance as at 1 January 2006		545,703	214,377	545,703	5,805,707	818,804	7,930,294
Issue of bonus shares	35	272,851	–	–	–	(272,851)	–
Transfer to statutory reserve fund	37	–	–	272,851	–	(272,851)	–
Exchange difference on conversion of FCBU reserves		–	–	–	–	11,390	11,390
Net profit for the year		–	–	–	–	1,004,997	1,004,997
Difference between the investment and net assets on the transfer of assets and liabilities of NDB Housing Bank Ltd.		–	–	–	–	(64,532)	(64,532)
Dividend paid		–	–	–	–	(327,422)	(327,422)
Balance as at 31 December 2006		818,554	214,377	818,554	5,805,707	897,535	8,554,727

For the year ended 31 December

		Attributable to equity holders of the parent							
		Share Capital	Share Premium	Statutory Reserve Fund	Revaluation Reserve	General Reserve	Retained Profit	Minority Interests	Total
	Note	Rs '000	Rs '000	Rs '000	Rs '000	Rs '000	Rs '000	Rs '000	Rs '000
NDB GROUP									
Balance as at 1 January 2005		537,500	91,667	546,485	86,156	5,805,707	1,308,996	1,093,241	9,469,752
Effect on adoption of revised SLAS-14 on Income Taxes	29	–	–	–	–	–	121,561	–	121,561
Balance as at 1 January 2005 (Restated)		537,500	91,667	546,485	86,156	5,805,707	1,430,557	1,093,241	9,591,313
Issue of new shares		8,203	122,710	–	–	–	–	–	130,913
Adjustment on disposal of subsidiaries		–	–	(8,985)	(86,156)	–	(112,914)	–	(208,055)
Net profit for the year (Restated)		–	–	–	–	–	1,036,078	236,585	1,272,663
Transfer to statutory reserve fund		–	–	8,203	–	–	(8,203)	–	–
Exchange gain from valuation of foreign associate		–	–	–	–	–	1,215	–	1,215
Provision for goodwill on business combinations (Restated)	31	–	–	–	–	–	(320,536)	(355,347)	(675,883)
Dividend paid		–	–	–	–	–	(322,500)	–	(322,500)
Balance as at 31 December 2005		545,703	214,377	545,703	–	5,805,707	1,703,697	974,479	9,789,666
Balance as at 1 January 2006		545,703	214,377	545,703	–	5,805,707	1,703,697	974,479	9,789,666
Issue of Bonus shares	35	272,851	–	–	–	–	(272,851)	–	–
Fair value adjustment on adoption of SLAS-40 - Investment Property		–	–	–	–	–	340,252	240,383	580,635
Adjustment on disposal of subsidiaries	44	–	–	–	–	–	(255,412)	47,261	(208,151)
Net profit for the year		–	–	–	–	–	2,030,484	176,421	2,206,905
Exchange difference on conversion of FCBU reserves		–	–	–	–	–	11,390	–	11,390
Transfer to statutory reserve fund	37	–	–	272,851	–	–	(272,851)	–	–
Exchange gain from valuation of foreign associate		–	–	–	–	–	16,692	–	16,692
Difference between the investment and net assets on the transfer of assets and liabilities of NDB Housing Bank Ltd.		–	–	–	–	–	(64,532)	–	(64,532)
Dividend paid		–	–	–	–	–	(327,422)	(124,312)	(451,734)
Balance as at 31 December 2006		818,554	214,377	818,554	–	5,805,707	2,909,447	1,314,232	11,880,871

1. GENERAL

1.1 Accounting Convention

The Financial Statements of NDB Bank and the NDB Group, comprising the Balance Sheet, Income Statement, Cash Flow Statement, Statement of Changes in Equity, Accounting Policies and Notes to the Financial Statements are prepared on the basis of the historical cost convention other than certain investments as explained in 2.3 below and investment property as explained in 2.5 below in conformity with generally accepted Accounting Principles and Accounting Standards issued by the Institute of Chartered Accountants of Sri Lanka. These principles and standards have been applied consistently with that of the previous year, except as given in 1.3 below.

These Financial Statements are prepared and presented in Sri Lankan Rupees.

No adjustments are made for inflationary factors affecting these Financial Statements.

1.2 Format of Accounts, prior year Figures and Phrases

The Financial Statements are presented in accordance with the format of accounts prescribed by the Central Bank of Sri Lanka.

Certain prior year figures and phrases are rearranged wherever necessary to conform to the current year's presentation.

1.2.1 Date of Authorization for Issue

The Financial Statements of National Development Bank Ltd. for the year ended 31 December 2006 were authorized for issue in accordance with a resolution of the Board of Directors on 23 February 2007.

1.2.2 Significant Accounting Judgements and Estimates

In the process of applying NDB Bank's accounting policies, management has used its judgements and made estimates in

determining the amounts recognized in the Financial Statements. The Management believes its estimates for determining the valuation of its assets and liabilities where appropriate.

1.2.3 Going Concern

The Directors have made an assessment of NDB Bank's ability to continue as a going concern and they do not intend either to liquidate or cease trading.

1.3 Changes in Accounting Policies

The accounting policies adopted are consistent with those used in the previous financial year except as follows:

NDB Bank has adopted the revised Sri Lanka Accounting Standards that are applicable in the current financial year.

SLAS-3 (Revised)	- Presentation of Financial Statements
SLAS-10 (Revised)	- Accounting Policies, Changes in Accounting Estimates and Errors
SLAS-12 (Revised)	- Events after the Balance Sheet date
SLAS-14 (Revised)	- Income Taxes
SLAS-18 (Revised)	- Property, Plant & Equipment
SLAS-19 (Revised)	- Leases
SLAS-21 (Revised)	- The Effects of Changes in Foreign Exchange Rates
SLAS-26 (Revised)	- Consolidated and Separate Financial Statements
SLAS-27 (Revised)	- Investments in Associates
SLAS-30 (Revised)	- Related Party Disclosures
SLAS-34 (Revised)	- Earnings Per Share
SLAS-40 (Revised)	- Investment Property
SLAS-41	- Impairment of Assets

The Accounting Policies and Notes have been revised accordingly and are disclosed in the Financial Statements.

With effect from 1 January 2006, NDB Bank has presented its Financial Statements in compliance with Sri Lanka Accounting Standard No. 3, Presentation of Financial Statements. Accordingly, the net assets attributable to the minority shareholders are disclosed separately in the Income Statement, Balance Sheet and the Statement of Changes in Equity. The previous year's figures have also been restated accordingly.

1.4 Basis of Consolidation

1.4.1 The NDB Group Financial Statements include the consolidated results, assets and liabilities of NDB Bank and its subsidiaries made up to the financial year-end. The results of subsidiaries are included from the date on which NDB Bank effectively acquires control of each subsidiary. The interests of outside shareholders of the subsidiaries in the net assets and their proportion of the results are grouped separately in the Consolidated Balance Sheet, Income Statement and the Statement of Changes in Equity respectively under the heading of minority interests.

All significant intra group balances and transactions are eliminated in full.

1.4.2 In the NDB Group Financial Statements, investments in associate companies described in Note 26 to the Financial Statements, are accounted for under the equity method of accounting. Under the equity method of accounting, the NDB Group's share of profits and losses of the associate companies made up to their respective year-ends is accounted for in the Consolidated Income Statement for the year. The carrying value of the investment in the Consolidated Balance Sheet is thereby increased or decreased to recognize NDB Group's share of retained profits and

losses of the associate companies since the date of acquisition. An associate company which becomes a subsidiary during the year is accounted for under the equity method of accounting up to the date on which it becomes a subsidiary, after which date it is accounted for as a subsidiary.

1.4.3 In NDB Bank's Separate Financial Statements, investments in subsidiaries and associate companies are accounted for at cost. Income is recognized only to the extent that dividends are declared from the accumulated profit. Provision is made for any permanent diminution in value of such investments determined on an individual basis.

1.5 Business Combinations and Goodwill

1.5.1 Business combinations are accounted for using the purchase method of accounting. This involves recognizing identifiable assets (including previously unrecognized intangible assets) and liabilities (including contingent liabilities and excluding future restructuring) of the acquired business at fair value. Any excess of the cost of acquisition over the fair values of the identifiable net assets acquired is recognized as goodwill. If the cost of acquisition is less than the fair values of the identifiable net assets acquired, the discount on acquisition is recognized directly in the Income Statement in the year of acquisition.

Goodwill acquired in a business combination is initially measured at cost, being the excess of the cost of the business combination over NDB Bank's interest in the net fair value of the identifiable assets, liabilities and contingent liabilities acquired. Following initial recognition, goodwill is measured at cost less any accumulated impairment losses. Goodwill is reviewed for impairment, annually.

1.5.2 For the purpose of impairment testing, goodwill acquired in a business combination is, from the acquisition date, allocated to each of NDB Bank's cash-generating units, or groups of cash-generating units, that are expected to benefit from the synergies of the combination, irrespective of whether other assets or liabilities of the acquiree are assigned to those units or groups of units.

Where goodwill forms part of a cash-generating unit (or group of cash-generating units) and part of the operation within that unit is disposed of, the goodwill associated with the operation disposed of is included in the carrying amount of the operation when determining the gain or loss on disposal of the operation. Goodwill disposed of in this circumstance is measured based on the relative values of the operation disposed of and the portion of the cash-generating unit retained.

When subsidiaries are sold, the difference between the selling price and the net assets plus cumulative translation differences and unamortized goodwill is recognized in the Income Statement.

A full provision has been made against equity for the goodwill arising from the transfer of the assets and liabilities of NDB Bank Ltd. to be in line with the provisions contained under Section 22 of the Banking Act to declare dividends.

1.6 Intangible Assets - Other than Goodwill

The cost of intangible assets acquired in a business combination is their fair value as at the date of acquisition. Following initial recognition, intangible assets are carried at cost less any accumulated amortization and any accumulated impairment losses.

However, intangible assets arising from the transfer of the assets and liabilities of NDB Bank Ltd., has been written off in full in the year the transfer of assets and liabilities took place to be in line with the provisions contained in Section 22 of the Banking Act to declare dividends.

1.7 Foreign Currency Translation

1.7.1 Financial Statements are presented in Sri Lankan Rupees which is NDB Bank's functional and presentation currency.

Monetary assets and liabilities denominated in foreign currencies are translated at the middle exchange rate ruling at the Balance Sheet date. The resulting gains and losses are accounted for in the Income Statement.

Non-monetary assets and liabilities that are measured on a historical cost basis in foreign currency are translated using the exchange rates prevailing at that date. Non-monetary assets and liabilities measured at fair value in a foreign currency are translated using the exchange rates at the date when the fair value was determined.

1.7.2 Forward exchange contracts are valued at the forward market rates prevailing at the date of the Balance Sheet. Forward profits and losses are dealt within the Income Statement.

1.7.3 Liabilities in respect of foreign currency borrowings guaranteed by the Government of Sri Lanka are not translated at rates of exchange prevailing at the Balance Sheet date, since the Government of Sri Lanka is required to bear any exchange risk that may arise at the time debt service payments are being made. NDB Bank pays a premium to the Government of Sri Lanka for bearing such risk.

1.7.4 As at the reporting date, the assets and liabilities of overseas subsidiaries/ associates are translated into NDB Bank's presentation currency at the rate of exchange ruling at the Balance Sheet date, and their Income Statements are translated at the weighted average exchange rates for the year. Exchange differences arising on translation are taken directly to a separate component of equity.

1.7.5 On disposal of a foreign subsidiary/ associate, the deferred cumulative amount recognized in equity relating to that particular foreign subsidiary/associate is recognized in the Income Statement in 'Other operating expenses' or 'Other operating income', accordingly.

1.8 Post-Balance Sheet Events

All material events occurring after the Balance Sheet date are considered and where necessary, adjusted for or disclosed in the Financial Statements.

1.9 Taxation

1.9.1 Domestic Banking Unit

Provision for taxation is based on the elements of income and expenditure as reported in the Financial Statements and computed in terms of the provisions of the Inland Revenue Act No. 38 of 2000 and the amendments thereto, at the rate of 35% (2005 - 30%).

1.9.2 Foreign Currency Banking Unit

The provision for income tax is based on the elements of income and expenditure as reported in the Financial Statements and computed in accordance with the provisions of the Inland Revenue Act No. 38 of 2000 and amendments thereto, at the rate of 35% (2005 - 30%) on on-shore foreign currency transactions, and at 20% (2005 - 20%) on off-shore foreign currency transactions.

1.9.3 Deferred Taxation

Deferred tax is provided on temporary differences at the Balance Sheet date between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes. Deferred tax liabilities are recognized for all taxable temporary differences except:

- where the deferred tax liability arises from the initial recognition of goodwill or 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 and associates, 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 recognized 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 credits 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 and associates, deferred tax assets are recognized only 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 utilized.

The carrying amount of deferred tax assets is reviewed at each Balance Sheet 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 utilized. Unrecognized deferred tax assets are reassessed at each Balance Sheet date and are recognized to the extent that it has become probable that future taxable profit will allow the deferred tax asset to be recovered.

1.10 Impairment of Assets - Other than Goodwill

NDB Bank assesses at each reporting date whether there is an indication that an asset may be impaired. If any such indication exists, or when annual impairment testing for an asset is required, the NDB Bank makes an estimate of the asset's recoverable amount. An asset's recoverable amount is the higher of an asset or cash-generating unit's fair value less costs to sell and its value in use and is determined for an individual asset, unless the asset does not generate cash inflows that are largely independent of those from other assets or groups of assets. Where the carrying amount of an asset 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 recognized in the Income Statement in those expense categories consistent with the function of the impaired asset, except for property previously revalued where the revaluation was taken to equity. In this case the impairment is also recognized in equity up to the amount of any previous revaluation.

For assets excluding goodwill, an assessment is made at each reporting date as to whether there is any indication that previously recognized impairment losses may no longer exist or may have decreased. If such indication exists, the company makes an estimate of recoverable amount. A previously recognized impairment loss is reversed only if there has been a change in the estimates used to determine the asset's recoverable amount since the last impairment loss was recognized. If that is the case, the carrying amount of the asset is increased to its recoverable amount. That increased amount cannot 'exceed' the carrying amount that would have been determined, net of depreciation, had no impairment loss been recognized for the asset in prior years. Such reversal is recognized in the Income Statement unless the asset is carried at revalued amount, in which case the reversal is treated as a revaluation increase. Impairment losses recognized in relation to goodwill are not reversed for subsequent increases in its recoverable amount.

2. ASSETS AND BASES OF THEIR VALUATION

2.1 Loans and Advances to Customers

2.1.1 Advances to customers are stated in the Balance Sheet net of provisions for possible loan losses and net of interest, which is not accrued to revenue.

2.1.2 Provision for Bad and Doubtful Loans

Provision for bad and doubtful loans is made on the basis of a continuous review of all advances, in accordance with the directions issued by the Central Bank of Sri Lanka to the banking sector, which mandates minimum specific provisions on a sliding scale linked to the age of the debt, net of any realizable security value. In addition, a general provision is also made by NDB Bank to cover unforeseen losses on all loans and advances excluding those for which a specific provision is being made and for refinance loans and staff loans. However, during the last quarter of 2006, the Central Bank mandated that banks build up a 1% general provision on its performing portfolio. Banks have been given time to do so over ten quarters ending on 31 March 2009. Accordingly, NDB Bank will build up its general provision over the next ten quarters to be in line with the guideline mandated by the Central Bank.

2.2 Leases

Assets leased to customers under agreements that transfer substantially all the risks and rewards associated with ownership other than legal title, are classified as finance leases. Lease rentals receivable in the Balance Sheet include total lease payments due net of unearned interest income not accrued to revenue, interest in suspense and provisions for bad and doubtful recoveries.

Assets leased to customers under agreements in which NDB Bank retains substantially all the risks and rewards associated with ownership and legal title are classified as operating leases. The lease rentals receivable in the Balance Sheet include rental instalments receivable, net of provisions for bad and doubtful recoveries.

Provision for bad and doubtful recoveries is made in the same manner as for loans and advances as described under 2.1.2.

2.3 Investments

2.3.1 Securities held for Trading Purposes

Government securities held for trading purposes are accounted for at the lower of cost and market value as at the Balance Sheet date, determined on a portfolio basis and interest is accrued up to the end of the year. Adjustment for fall in market value below cost, if relevant is accounted by charging the difference to the Income Statement as per the provisions under Sri Lanka Accounting Standards.

Dealing securities comprise of shares and debentures quoted on the Colombo Stock Exchange and are accounted for at the lower of cost and market value as at the Balance Sheet date, determined on a portfolio basis.

2.3.2 Investments held to Maturity

Investments held to maturity are regarded as long-term investments and comprise of investments in treasury bonds, investments in unit trusts quoted on the Colombo Stock Exchange, non-quoted equity investments and sinking fund investments. Sinking fund investments consist of treasury bills and bonds.

Non-quoted equity investments are accounted for at cost, net of provisions for any permanent diminution in value on an individual basis. Investments in unit trusts and sinking fund investments are each carried at the lower of cost and market value as at the Balance Sheet date, determined on a portfolio basis. Temporary declines in value are charged to equity. All other investment securities are stated at cost and provisions are made for permanent diminutions in value on a case by case basis.

2.3.3 Securities purchased under Resale Agreement

Securities purchased under agreements to resale are classified as part of assets and accounted for accordingly.

2.3.4 Securities sold under Repurchase Agreement

Obligations to repurchase resulting from securities sold under Repurchase Agreements are accounted for as a liability and are classified under liabilities.

2.4 Property, Plant & Equipment

2.4.1 The cost of property, plant & equipment is the cost of purchase or construction together with any incidental expenses thereon. Property, plant & equipment are accounted for at cost less accumulated depreciation which is provided for on the bases specified below.

2.4.2 Depreciation

The provision for depreciation is calculated on the cost of property, plant & equipment so as to write off such costs over the estimated useful lives of the assets by equal annual instalments as follows:

Buildings/improvements	5% - 10%
Motor vehicles	25%
Furniture and office equipment	20%

Depreciation is provided proportionately for the completed number of months the asset is in the books of NDB Bank.

Leasehold assets are amortized over lower of the useful life and the lease period of the respective assets.

2.5 Investment Property

Investment property are property held either to earn rental income or for capital appreciation or both.

Investment property is measured initially at cost, including transaction costs. Subsequent to initial recognition, investment property is stated at fair value, which reflects market conditions at the Balance Sheet date. Gains or losses arising from changes in the fair values of investment property is included in the Income Statement in the year in which they arise.

Development Holding (Pvt) Ltd., a subsidiary company whose principal business activity is renting out premises for trade, business or vocation adopted the Sri Lanka Accounting Standard No. 40, Investment Property during the year. Accordingly, the property owned by Development Holdings (Pvt) Ltd. was revalued by an independent valuer on 1 January 2006 and the surplus arising over the net book value of the property as at that date was credited to retained earnings on 1 January 2006. Further, another revaluation was done on 31 December 2006 and the incremental surplus over the valuation as at 1 January 2006 has been credited to the Income Statement. Thereafter a valuation of the property will be done annually and any surplus or deficit arising thereon over the previous valuation will be adjusted in the Income Statement.

2.6 Cash and Cash Equivalents

Cash and cash equivalents comprise of cash balances, short-term funds, balances with Central Bank of Sri Lanka and Government of Sri Lanka Treasury bills readily convertible to known amounts of cash and subject to insignificant risk of changes in value. The cash flow has been prepared by using the "Direct Method", whereby gross cash receipts and gross cash payments of operating activities, financing activities and investing activities have been recognized.

2.7 Other Assets

All other assets are valued net of specific provisions, where necessary, so as to reduce the carrying value of such assets to their estimated realizable values.

3. LIABILITIES AND PROVISIONS

- 3.1** All discernible risks are taken into account in quantifying the liabilities of NDB Bank.

3.2 Pensions and Retirement Benefits

3.2.1 NDB Bank operates an approved non-contributory Pension Plan for the payment of pensions to members of its permanent staff who qualify for such payments when retiring. Up to 31 December 2002, annual contributions to the Pension Plan were payable by NDB Bank based on a percentage of gross salaries, as stipulated in the pension deed. However, following the formulation of a revised pension deed, which has been approved by the Department of Inland Revenue, the contributions in subsequent years are determined on the basis of an actuarial valuation each year.

3.2.2 Provision is made for the payment of retirement gratuities payable under the Payment of Gratuity Act No. 12 of 1983, in respect of employees who do not qualify for a pension, on the basis of an actuarial valuation each year.

3.2.3 Employees are eligible for Employees' Provident Fund contributions and Employees' Trust Fund contributions in accordance with the respective statutes and regulations. NDB Bank contributes 15% and 3% of gross salaries of employees to NDB Bank's Employees' Provident Fund and the Employees' Trust Fund respectively.

3.2.4 Commitments and Contingencies

All discernible risks are taken into consideration in determining the amount of liabilities.

4. INCOME STATEMENT

4.1 Revenue Recognition

4.1.1 Interest Income from Loans and Advances

Interest income from loans and advances is recognized on an accrual basis. However, no accrued interest income is recognized where any portion of capital or interest is in arrears for three months or more. In such cases interest income is accounted for on a cash basis.

4.1.2 Lease Income

- (a) Financial Leases - The excess of aggregate rentals receivable over the cost of the leased asset constitutes the total unearned interest income. The unearned interest income is taken into revenue on an accrual basis over the term of the lease in proportion to the remaining balance of the lease. However, no accrued interest income is recognized where any portion of capital or interest is in arrears for three months or more. In such cases interest income is accounted for on a cash basis.
- (b) Operating Leases - Rental income is recognized as revenue on a straight-line basis over the term of the lease. However, no accrued income is recognized where the rental is in arrears for three months or more. In such cases, rental income is accounted for on a cash basis.

4.1.3 Interest Income from other Sources

Interest income from Government securities is recognized on a time proportion basis as discounts on purchase, over the period to maturity or the date of sale.

Income from other interest bearing investments is recognized as revenue on an accrual basis.

4.1.4 Bills Discounted

Income on bills discounted is recognized proportionately over the tenor of the bill.

4.1.5 Dividend Income

Dividend income from shares is recognized when NDB Bank's right to receive the payment is established.

4.1.6 Profit or Loss on sale of Marketable Securities

Profit or loss arising from the sale of equity shares, units, commercial paper and other marketable securities is accounted for on a cash basis.

4.1.7 Income from Fee-based Activities

Fees for underwriting, advisory work, loan syndication, management of funds and all other fees and commissions are recognized on a cash basis.

4.1.8 Other Income

Other income is recognized on an accrual basis.

4.1.9 Recovery of Loans and Advances Written Off

Recovery of amounts written off as bad and doubtful loans is recognized as income on a cash basis.

4.2 Expenditure Recognition

Expenses are recognized in the Income Statement 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 & equipment in a state of efficiency has been charged to income in arriving at the profit for the year.

Interest expenses are recognized on an accrual basis.

NDB Bank enters into off Balance Sheet transactions such as forward exchange contracts. At the year end losses on such transactions are dealt with in the Income Statement.

5. CASH FLOW

The cash flow has been prepared by using the "Direct Method". Cash and cash equivalents include cash balances, time deposits and Treasury bills and bonds. Cash and cash equivalents are presented net of bank overdrafts for the purpose of the Cash Flow Statement.

6. BUSINESS SEGMENT REPORTING

A business segment is a distinguishable component of an enterprise that is engaged in providing an individual product or service or a group of related products or services that is subject to risk and returns that are different from those of other business segments. The accounting policies adopted for segment reporting are the same accounting policies adopted for preparing the Financial Statements of the NDB Group.

7. DIVIDENDS ON ORDINARY SHARES

Dividends on ordinary shares are recognized as a liability and deducted from equity when they are approved by NDB Bank's shareholders. Interim dividends are deducted from equity when they are declared and are no longer at the discretion of NDB Bank.

1. INCORPORATION, PRINCIPAL ACTIVITIES AND THE SIGNIFICANT CHANGES IN THE NDB GROUP STRUCTURE

The National Development Bank of Sri Lanka was incorporated under the National Development Bank of Sri Lanka Act, No. 2 of 1979. In 2005, pursuant to the Provisions of the National Development Bank of Sri Lanka (Consequential Provisions) Act, No. 1 of 2005, a Company by the name of 'National Development Bank Ltd.' was incorporated for the purposes of taking over the business of National Development Bank of Sri Lanka. Accordingly on 15 June 2005, the National Development Bank Ltd. was incorporated and with effect from that date the National Development Bank of Sri Lanka Act, No. 2 of 1979 was repealed, except for certain provisions contained therein.

The principal activities of NDB Bank, its subsidiaries and associate companies included in consolidation, consist of the business of commercial banking, development financing, merchant banking, investment banking, leasing, housing finance, venture capital, stockbroking, fund management, property investment and insurance.

The number of staff employed by NDB Bank as at 31 December 2006 was 713 (2005 - 643).

The number of branches of NDB Bank as at 31 December 2006 was 31 (2005 - 24).

The growth in number of staff and branches are principally as a result of the transfer of the assets and liabilities of NDB Bank Ltd. with effect from 1 August 2005 and the consequent expansion in the commercial banking activities.

On 1 February 2006, Capital Development and Investment Company Ltd., a subsidiary of NDB Bank disposed of 58.44% of its holding in its fully-owned subsidiary NDB Finance Lanka (Pvt) Ltd. (now known as Aviva NDB Finance Lanka (Pvt) Ltd.) to Aviva International Holdings Ltd. The current holding of Capital Development and Investment Company Ltd. in Aviva NDB Finance Lanka (Pvt) Ltd. is 41.56%. Aviva NDB Finance Lanka (Pvt) Ltd. holds 87.27% of Eagle Insurance Company Ltd., thus giving Aviva International Holdings Ltd. a 51% stake in Eagle Insurance Company Ltd.

The capital gain earned by Capital Development and Investment Company Ltd. on this transaction was Rs 1.64 bn. In accordance with Sri Lanka Accounting Standard No. 26, 'Consolidated and Separate Financial Statements' the capital gain attributable to the NDB Group was Rs 1.01 bn.

On 2 February 2006 NDB Bank purchased a 5% stake in Eagle Insurance Company Ltd. from James Finlay and Company (Colombo) Ltd. Consequently, NDB Bank's original and current effective holdings in Eagle Insurance Company Ltd. are 65.98% and 32.42% respectively.

From 1 February 2006, Aviva NDB Finance Lanka (Pvt) Ltd., the holding Company of Eagle Insurance Company Ltd. was accounted for as an associate. During the comparative period it was accounted for as a subsidiary.

NDB Bank's holding in NDB Housing Bank Ltd. which originally was 41.34% (direct holding of 30% and 15% through Capital Development and Investment Company Ltd.) was increased to 80% as at 31 December 2005 by the acquisition of the shares held by Capital Development and Investment Company Ltd. and some of the minority shareholders at a price of Rs 13 per share. NDB Bank further acquired the balance minority shareholding of 15% during the first quarter of 2006 and the balance 5% in April 2006. Consequently, NDB Bank's holding in NDB Housing Bank Ltd. was 100% as at 31 August 2006.

On 1 September 2006, NDB Bank acquired the assets and liabilities of NDB Housing Bank Ltd. Consequently, NDB Housing Bank Ltd. is now under liquidation.

	NDB BANK		NDB GROUP	
	2006 Rs '000	2005 Rs '000	2006 Rs '000	2005 Rs '000
2. INCOME				
Gross income	6,888,379	4,288,138	8,208,824	7,116,094
Interest income (Note 3)	5,689,394	3,454,199	6,075,601	5,035,347
Other income (Note 5)	1,191,487	808,034	2,125,725	2,054,842
Income from operating leases	7,498	25,905	7,498	25,905
	6,888,379	4,288,138	8,208,824	7,116,094
3. INTEREST INCOME				
Loans and advances	4,390,169	2,914,000	4,545,463	3,485,580
Treasury bills, bonds and placements with other banks	1,299,225	540,199	1,530,138	1,549,767
	5,689,394	3,454,199	6,075,601	5,035,347
4. INTEREST EXPENSES				
Long-term borrowings	1,211,227	1,086,236	1,211,227	1,095,699
Other term borrowings	1,160,790	527,773	1,096,623	768,519
Deposits	915,164	245,546	915,164	477,820
	3,287,181	1,859,555	3,223,014	2,342,038
5. OTHER INCOME				
Dividend income from securities				
- Quoted investments	42,092	31,006	42,092	62,130
- Non-quoted investments	73,823	98,134	100,774	103,272
Dividend income from subsidiaries/associates				
- Quoted investments	331,211	74,752	—	—
- Non-quoted investments	75,727	73,944	—	—
Gain/(loss) from dealing securities	—	330,060	(4,313)	330,060
Gain/(loss) from investment securities	3,752	(30,936)	3,752	(30,936)
Gain/(loss) from group companies (b)	—	—	1,016,068	27,000
	526,605	576,960	1,158,373	491,526
Net gain/(loss) from government securities	(15,836)	(35,217)	(15,836)	(71,408)
Fee and commission income	306,328	116,332	306,328	235,301
Income from other fee-based activities	46,285	28,386	341,965	399,860
Net insurance income	—	—	6,790	416,289
Exchange gain	280,421	104,274	280,421	221,652
Income from other activities	47,684	17,299	47,684	361,622
	1,191,487	808,034	2,125,725	2,054,842

- (a) Provisions made/released for the change in value of quoted and non-quoted securities are disclosed in Note 9 to the Financial Statements.
- (b) The capital gain made by the Group on the sale of part of its holding in Aviva NDB Finance Lanka (Pvt) Ltd. by Capital Development and Investment Company Ltd. has been shown net of minority interest. This was confirmed by the Urgent Issues Task Force of the Institute of Chartered Accountants of Sri Lanka.

	NDB BANK		NDB GROUP	
	2006 Rs '000	2005 Rs '000	2006 Rs '000	2005 Rs '000
6. OPERATING EXPENSES				
Operating expenses include the following:				
Employees' Provident Fund	43,127	27,525	44,793	59,848
Employees' Trust Fund	10,904	5,717	11,237	12,253
Gratuity	11,460	6,226	13,995	25,969
Pension contribution	–	17,852	–	17,851
Auditors' remuneration	2,200	2,000	3,205	7,426
Depreciation - own assets	186,175	112,437	189,174	261,274
Chairman's emoluments	1,025	811	1,025	811
Emoluments of nine Directors paid over Rs 50,000/- each per annum (2005 - 12 Directors)	5,629	3,138	5,629	4,396
Emoluments of other Directors paid less than Rs 50,000/- each per annum	–	–	–	–
Legal charges	33,764	11,093	34,305	16,932

7. STAFF RETIREMENT BENEFITS

NDB Bank operates an approved non-contributory Pension Plan for the payment of pensions to members of its permanent staff who qualify for such payments when retiring. Please see accounting policy 3.2.

The amount funded since the inception of the Plan is the amount recognized as expense over the respective periods. The adequacy of the contributions was reviewed by an actuary as at 31 December 2006. Accordingly, the actuarial experience losses or gains have been recognized over the expected future working life of the participants. As the current year's amortization of the actuarial gains and expected returns on assets were more than the cost of benefits this year, no provision has been made in the accounts.

Provisions for retirement gratuities have been made based on the actuarial valuation carried out as at 31 December 2006. Accordingly, gratuity benefit expense for the year was Rs 11 mn.

The Pension Plan is fully funded.

The actuarial method used is the Projected Unit Credit method. The principal assumptions, which have the most significant effect on the valuation, are the investment return net of taxes, and the rate of increase in salaries, which have been estimated at 10% and 10% respectively.

	NDB BANK		NDB GROUP	
	2006 Rs '000	2005 Rs '000	2006 Rs '000	2005 Rs '000
8. OTHER ADMINISTRATIVE AND GENERAL EXPENSES				
Premises, equipment and establishment expenses	268,105	203,918	401,586	553,195
Depreciation - own assets	186,175	112,437	193,340	261,274
Other overhead expenses	328,247	178,135	328,247	597,257
	782,527	494,490	923,173	1,411,726
9. PROVISIONS FOR BAD AND DOUBTFUL DEBTS AND FOR FALL IN VALUE OF SECURITIES				
Bad and doubtful debts	37,165	164,594	41,278	146,269
Fall in value of non-quoted securities	(33,606)	7,192	(27,893)	7,192
	3,559	171,786	13,385	153,461

	Percentage Holding	NDB GROUP	
		2006 Rs '000	2005 Rs '000
10. SHARE OF ASSOCIATE COMPANIES' PROFIT			
Ayojana Fund (Pvt) Ltd.	50.00%	10,893	6,755
Maldives Finance Leasing Co. (Pvt) Ltd.	35.00%	24,245	14,910
NDB Venture Investments (Pvt) Ltd. (with effect from 31 May 2006)	50.00%	3,530	–
Aviva NDB Finance Lanka (Pvt) Ltd. (with effect from 1 February 2006)	31.42%	175,785	–
		214,453	21,665

The share of profit/(loss) in respect of the above associate companies are based on the draft financial statements of those companies for the year ended 31 December 2006.

	NDB BANK		NDB GROUP	
	2006 Rs '000	2005 Rs '000	2006 Rs '000	2005 Rs '000
11. TAXATION				
Provision for taxation				
On profit for the year (a)	650,654	215,151	778,875	328,015
Transfer from deferred taxation (Note 29)	(25,415)	13,665	(25,415)	13,665
VAT on financial services	456,164	217,001	466,383	251,339
On associate companies' share of profit	–	–	606	–
	1,081,403	445,817	1,220,449	593,019

	2006 Rs '000	2005 Rs '000
a. Reconciliation of Effective Tax Rate - NDB Bank		
Profit before tax	2,086,400	1,071,391
Statutory tax at 20%	3,270	2,026
Statutory tax at 30%	78,658	369,907
Statutory tax at 35%	632,750	–
Add: Effect of tax on non-deductible expenses	234,470	153,336
Less: Effect of tax on claimable expenses	(298,494)	(310,118)
Total tax	650,654	215,151

NDB Bank is liable to VAT on financial services at 20% (2005 - 15%).

NDB Investment Bank Ltd. is liable to taxation at 35% (2005 - 32.5%).

Ayojana Fund (Pvt) Ltd. is liable to taxation at 20% (2005 - 20%).

NDBS Stockbrokers (Pvt) Ltd. is liable to taxation at 35% (2005 - 32.5%).

The profits earned by Capital Development and Investment Co. Ltd. is liable to taxation at 35% (2005 - 20%).

Profits earned by Development Holdings (Pvt) Ltd., through the business of construction and operation of an office complex was exempt from tax for a period of seven years commencing from 1997 under an agreement with the Board of Investment of Sri Lanka. With effect from 2004, the Company is liable to tax at 2% of its turnover of such business for a period of 15 years. The Company is liable to tax on other income at 35% (2005 - 32.5%).

Aviva NDB Finance Lanka (Pvt) Ltd. is liable to income tax at 35% (2005 - 32.5%). The tax charge for the year consists wholly of dividend tax paid at source. However, no tax provision has been made for the current year due to the tax losses incurred by the Company.

Profits earned through the business of venture capital by NDB Venture Investments (Pvt) Ltd. is taxed at 20% (2005 - 20%).

Maldives Finance Leasing Co. (Pvt) Ltd. is a company based in the Republic of Maldives and is not subject to taxation.

12. DIVIDENDS PAID AND PROPOSED

The Director's intend to propose a first and final dividend of Rs 5.00 per share for the year 2006. No provision is made in the accounts in accordance with Sri Lanka Accounting Standard No. 12.

13. EARNINGS PER SHARE

The basic earnings per share for 2006 and 2005 have been calculated by dividing the profit after taxation and minority interests for each year by the number of ordinary shares in issue on a time basis as required by the Sri Lanka Accounting Standard No. 34 on Earnings per Share. Further, the number of shares have been adjusted retrospectively for the bonus issue in accordance with SLAS - 34.

	NDB BANK		NDB GROUP	
	2006	2005	2006	2005
Profit attributed to ordinary shareholders (Rs '000)	1,004,997	625,574	2,030,484	1,036,078
Ordinary shares in issue (Number)	81,855,007	81,855,007	81,855,007	81,855,007
Earnings per ordinary share (Rs)	12.28	7.64	24.81	12.66

	NDB BANK		NDB GROUP	
	2006 Rs '000	2005 Rs '000	2006 Rs '000	2005 Rs '000
14. CASH AND SHORT-TERM FUNDS				
Cash in hand	271,689	170,555	271,704	170,570
Dues from banks and other financial institutions	3,123,077	1,118,415	4,195,450	1,928,205
	3,394,766	1,288,970	4,467,154	2,098,775

15. BALANCES WITH CENTRAL BANK

Balances with Central Bank includes the cash balance that is required as per the provisions of Section 93 of the Monetary Law Act and contains the effects of cheques pending realization. The minimum cash reserve requirement was 10% of the rupee deposit liabilities as at 31 December 2006 and 2005. This reserve requirement is not applicable for the foreign currency deposit liabilities of the Domestic Banking Unit and the deposit liabilities of the Foreign Currency Banking Unit.

16. SINKING FUND - TREASURY BILLS AND BONDS

In terms of the provisions of an agreement entered into between NDB Bank and the Government of Sri Lanka for the latter to guarantee a US\$ 55 mn loan obtained by NDB Bank from the Industrial Bank of Japan, Nippon Life Insurance Company and the Asian Development Bank in 1997, NDB Bank has established a Sinking Fund to provide funds for the repayment of the loans which is due in August and September 2007.

	NDB BANK		NDB GROUP	
	2006 Rs '000	2005 Rs '000	2006 Rs '000	2005 Rs '000
17. INVESTMENTS HELD FOR TRADING				
Treasury bills	2,637,543	2,895,077	2,637,543	2,895,077
Treasury bonds	2,598,056	1,444,139	2,598,056	1,444,139
Dealing securities (Note 17.1)	396,581	164,121	396,581	442,643
	5,632,180	4,503,337	5,632,180	4,781,859

17.1 Dealing Securities

Quoted shares (Note 17.2)	288,854	30,481	288,854	309,003
Quoted debentures (Note 17.3)	107,727	133,640	107,727	133,640
	396,581	164,121	396,581	442,643

	2006			2005		
	Number	Cost	Market	Number	Cost	Market
	of Ordinary Shares	Rs '000	Value Rs '000	of Ordinary Shares	Rs '000	Value Rs '000
17.2 Quoted Ordinary Shares						
Banks and Finance						
DFCC Bank Ltd.	199,999	15,141	35,650	133,333	15,141	29,333
		15,141	35,650		15,141	29,333
Diversified Holdings						
Hayleys Ltd.	60	4	8	60	4	6
John Keells Holdings Ltd.	59	2	12	52	2	7
		6	20		6	13
Footwear and Textiles						
Hayleys MGT Knitting Mills Ltd.	6,912,400	5,334	368,085	6,912,400	5,334	295,505
		5,334	368,085		5,334	295,505
Insurance						
Eagle Insurance Co. Ltd.	1,500,000	268,373	268,373	—	—	—
		268,373	268,373		—	—
	2006			2005		
	Number	Cost	Market	Number	Cost	Market
	of Preference Shares	Rs '000	Value Rs '000	of Preference Shares	Rs '000	Value Rs '000
Quoted Preference Shares						
Banks and Finance						
Commercial Bank of Ceylon Ltd.	—	—	—	1,000,000	10,000	10,000
		—	—		10,000	10,000
Total as at 31 December - NDB Bank		288,854	672,128		30,481	324,851
Investments in quoted shares by subsidiaries at market value		—			58,793	
Investments in quoted shares by subsidiaries at cost		—			219,729	
Total as at 31 December - NDB Group		288,854			309,003	

	2006			2005		
	Number of Debentures	Cost Rs '000	Market Value Rs '000	Number of Debentures	Cost Rs '000	Market Value Rs '000
17.3 Quoted Debentures						
Commercial Bank of Ceylon Ltd.	50,000	50,000	50,000	50,000	50,000	50,000
Hatton National Bank Ltd.	60,000	6,000	6,000	60,000	6,000	6,000
Suntel Ltd.	24,227	24,227	24,227	50,140	50,140	60,168
Sampath Bank Ltd.	175,000	17,500	17,281	175,000	17,500	17,500
Seylan Bank Ltd.	100,000	10,000	10,000	100,000	10,000	10,000
Total as at 31 December - NDB Bank		107,727	107,508		133,640	143,668
Investments in quoted debentures by subsidiaries at market value		–			–	
Total as at 31 December - NDB Group		107,727			133,640	

	NDB BANK		NDB GROUP	
	2006 Rs '000	2005 Rs '000	2006 Rs '000	2005 Rs '000
18. INVESTMENTS HELD TO MATURITY				
Treasury bonds	1,460,643	1,045,224	1,460,643	7,060,529
Tradable corporate securities	1,019,955	486,588	1,019,955	486,588
Investment securities (Note 18.1)	567,580	545,434	579,004	1,324,432
	3,048,178	2,077,246	3,059,602	8,871,549
18.1 INVESTMENT SECURITIES				
Non-quoted shares (Note 18.2)	392,580	370,379	404,004	1,011,678
Non-quoted debentures (Note 18.3)	175,000	175,055	175,000	175,055
Unit trusts (Note 18.4)	–	–	–	137,699
	567,580	545,434	579,004	1,324,432

	2006			2005		
	Number	Cost	Net	Number	Cost	Net
	of Shares	Rs '000	Realizable Value Rs '000	of Shares	Rs '000	Realizable Value Rs '000
18.2 Non-Quoted Shares						
A. Ordinary Shares						
Anuradha Ceramics (Pvt) Ltd.	1,399	14	38	1,399	14	49
Arpitalian Compact Soles (Pvt) Ltd.	2,500,000	25,000	18,550	2,500,000	25,000	14,725
Beico Link Carbons (Pvt) Ltd.	328,500	2,190	4,399	328,500	2,190	4,911
Ceylinco Developers (Pvt) Ltd.	250,000	2,500	12,090	250,000	2,500	8,078
Coats Thread Lanka (Pvt) Ltd.	374,574	9,785	98,112	374,574	9,785	89,549
Coats Thread Exports (Pvt) Ltd.	13,564	273	72,916	13,564	273	60,756
Credit Information Bureau of Sri Lanka	30,395	3,039	171	30,395	3,039	17,108
Fitch Ratings Lanka Ltd.	62,500	625	736	62,500	625	736
Hethersett Hotels Ltd.	1,500,000	15,000	20,505	1,500,000	15,000	18,480
Lak Jaya Thrift & Credit Foundation Ltd.	–	–	–	50,000	500	355
Link Development (Pvt) Ltd.	–	–	–	150,000	750	4
Mahaweli Livestock Enterprises Ltd.	600,000	6,000	21,702	600,000	6,000	25,542
MPS Hotels Ltd.	180,000	900	7,508	180,000	900	7,513
Prime Carbons (Pvt) Ltd.	–	–	–	210,720	2,107	3,045
Sampath Centre (Pvt) Ltd.	1,000,000	10,000	10,625	1,000,000	10,000	18,510
South Asia Regional Fund	500	41	32,407	500	41	118
Suntel Ltd.	11,729,794	117,296	157,297	11,729,794	117,296	139,115
Wayamba Plantations (Pvt) Ltd.	–	–	–	2,750,000	25,000	34,457
Sub-Total		192,663	457,056		221,020	443,051

Non-quoted ordinary shares which are fully provided for are not included in the above list. The total cost of such investments is Rs 88.06 mn (2005 - Rs 59.60 mn).

	2006			2005		
	Number of Shares	Cost Rs '000	Net Realizable Value Rs '000	Number of Shares	Cost Rs '000	Net Realizable Value Rs '000
B. Redeemable Cumulative Preference Shares						
Aqua Packaging Ltd.	–	–	–	6,000,000	60,000	60,000
Aqua Gardens (Pvt) Ltd.	–	–	–	2,500	2,500	2,500
Champion Apparel Exports (Pvt) Ltd.	–	–	–	500,000	5,000	5,000
Sampath Centre (Pvt) Ltd.	22,000,000	220,000	220,000	22,000,000	220,000	220,000
South Asia Regional Fund	–	–	–	109	8,906	8,906
Techno Optics Lanka Ltd.	–	–	–	100,000	1,000	1,000
Sub-Total		220,000	220,000		297,406	297,406
Total		412,663	677,056		518,426	740,457
Less: Provision for losses		(20,083)			(148,047)	
Total as at 31 December - NDB Bank		392,580			370,379	
Investments in non-quoted shares by subsidiaries net of provision		11,424			503,600	
Investments in non-quoted shares by subsidiaries at market value		–			137,699	
Total as at 31 December - NDB Group		404,004			1,011,678	

The redemption of the cumulative preference shares are due between 2007 and 2008.

Redeemable cumulative preference shares which are fully provided for are not included in the above list. The total cost of such investments is Rs 66 mn (2005 - Nil).

The net realizable value of the non-quoted shares was the net book value of these shares as at the Balance Sheet date.

	2006			2005		
	Number of Debentures	Cost Rs '000	Market Value Rs '000	Number of Debentures	Cost Rs '000	Market Value Rs '000
18.3 Non-Quoted Debentures						
Riverina Hotels Ltd. (31.12.2006)	–	–	–	5,540	55	55
Singer Sri Lanka Ltd. (18.11.2008)	250,000	25,000	25,000	250,000	25,000	25,000
Singer Sri Lanka Ltd. (15.09.2008)	1,500,000	150,000	150,000	1,500,000	150,000	150,000
Total as at 31 December - NDB Bank		175,000	175,000		175,055	175,055
Investments in non-quoted debentures by subsidiaries		–			–	
Total as at 31 December - NDB Group		175,000			175,055	

The redemption dates are shown within brackets.

	NDB BANK		NDB GROUP	
	2006 Rs '000	2005 Rs '000	2006 Rs '000	2005 Rs '000
19. BILLS OF EXCHANGE				
Export bills	1,576,942	933,656	1,576,942	933,656
Import bills	14,989	37,141	14,989	37,141
	1,591,931	970,797	1,591,931	970,797

	NDB BANK	
	2006 Rs '000	2005 Rs '000
20. LOANS AND ADVANCES		
<i>(a) NDB Bank</i>		
Corporate - long-term	16,203,729	20,036,600
Corporate - short-term	17,656,638	11,817,313
Refinance loans	2,313,939	2,737,648
Consumer loans	3,928,992	759,501
Staff loans	571,809	456,065
	40,675,107	35,807,127
Less: Provision for bad and doubtful loans (Note 20.1)	1,727,145	1,957,395
Net loans and advances	38,947,962	33,849,732

	Specific	General	2006 Total Rs '000	2005 Total Rs '000
	Rs '000	Rs '000		
20.1 Provision for Bad and Doubtful Loans				
At the beginning of the year	1,795,357	162,037	1,957,394	2,014,006
Resulting from the transfer of assets and liabilities of NDB Housing Bank Ltd.	–	20,119	20,119	39,397
Amounts recovered/provisions written back	(319,603)	–	(319,603)	(272,613)
Amounts written off	(285,540)	–	(285,540)	(273,640)
Provision made during the year	277,493	77,282	354,775	450,245
At the end of the year	1,467,707	259,438	1,727,145	1,957,395

NDB GROUP		
	2006	2005
	Rs '000	Rs '000
(b) NDB Group		
Corporate - long-term	16,229,329	21,395,622
Corporate - short-term	17,656,638	11,817,313
Refinance loans	2,313,939	2,737,648
Consumer loans	3,928,992	759,501
Staff loans	581,035	456,065
	40,709,933	37,166,149
Less: Provision for bad and doubtful loans (Note 20.2)	1,752,744	1,998,999
Net loans and advances	38,957,189	35,167,150

	Specific	General	2006	2005
	Rs '000	Rs '000	Total	Total
			Rs '000	Rs '000
20.2 Provision for Bad and Doubtful Loans				
At the beginning of the year	1,820,896	178,103	1,998,999	2,101,507
Amounts recovered/provisions written back	(319,603)	–	(319,603)	(263,447)
Amounts written off	(285,540)	–	(285,540)	(284,440)
Provision made during the year	277,493	81,395	358,888	456,800
Brought forward from new subsidiaries	–	–	–	39,397
Adjustment on disposal of subsidiary	–	–	–	(50,818)
At the end of the year	1,493,246	259,498	1,752,744	1,998,999

	NDB BANK		NDB GROUP	
	2006	2005	2006	2005
	Rs '000	Rs '000	Rs '000	Rs '000
21. LEASE RENTALS RECEIVABLE				
Total rentals receivable	2,057,620	1,034,721	2,057,620	1,034,721
Less: Provision for doubtful recoveries (Note 21.1)	55,432	61,069	55,432	61,069
Interest in suspense (Note 21.2)	10,942	13,900	10,942	13,900
Unearned income	542,169	228,449	542,169	228,449
Net rentals receivable	1,449,077	731,303	1,449,077	731,303

21.1 Provision for Bad and Doubtful Recoveries

At the beginning of the year	61,069	73,675	61,069	73,675
Amounts recovered/provisions written back	(20,144)	(13,731)	(20,144)	(13,731)
Amounts written off	(7,631)	(1,740)	(7,631)	(1,740)
Provision made during the year	22,138	2,865	22,138	2,865
At the end of the year	55,432	61,069	55,432	61,069

	NDB BANK		NDB GROUP	
	2006 Rs '000	2005 Rs '000	2006 Rs '000	2005 Rs '000
21.2 Interest in Suspense				
At the beginning of the year	13,900	19,641	13,900	19,641
Amounts written back to profit	(2,170)	(1,470)	(2,170)	(1,470)
Amounts written off	(5,380)	(8,918)	(5,380)	(8,918)
Transfer to interest in suspense	4,592	4,665	4,592	4,665
Transfer to loans	–	(18)	–	(18)
At the end of the year	10,942	13,900	10,942	13,900

	Up to 1 year Rs '000	1 to 5 years Rs '000	More than 5 years Rs '000	Total Rs '000
21.3 Maturity of Lease Rentals Receivable of NDB Bank				
Total rentals receivable	204,920	1,759,686	93,014	2,057,620
Provision for doubtful recoveries	(32,946)	(21,798)	(688)	(55,432)
Interest in suspense	(10,571)	(371)	–	(10,942)
Unearned income	(72,019)	(444,632)	(25,518)	(542,169)
Net rentals receivable	89,384	1,292,885	66,808	1,449,077

	NDB BANK		NDB GROUP	
	2006 Rs '000	2005 Rs '000	2006 Rs '000	2005 Rs '000
22. INTEREST RECEIVABLE				
Interest receivable	1,262,913	1,130,246	1,262,913	1,143,130
Less: Interest in suspense (Note 22.1)	842,895	1,035,331	842,895	1,036,480
	420,018	94,915	420,018	106,650
22.1 Interest in Suspense				
At the beginning of the year	1,035,331	1,589,728	1,036,480	1,589,728
Amounts written back to profit	(191,964)	(483,951)	(191,964)	(483,951)
Amounts written off	(353,231)	(835,835)	(353,231)	(835,835)
Transfer to interest in suspense	352,759	765,389	352,759	766,513
Brought forward/disposal of new subsidiary	–	–	(1,199)	25
At the end of the year	842,895	1,035,331	842,895	1,036,480

	NDB BANK		NDB GROUP	
	Loan Loss Provision Rs '000	Interest in Suspense Rs '000	Loan Loss Provision Rs '000	Interest in Suspense Rs '000
23. ANALYSIS OF PROVISION FOR LOAN LOSSES AND INTEREST IN SUSPENSE				
Loans and advances	1,727,145	842,895	1,752,744	842,895
Lease rentals receivable	55,432	10,942	55,432	10,942
	1,782,577	853,837	1,808,176	853,837

24. ASSET QUALITY INFORMATION

24.1 Concentration of Credit Risk

In granting credit facilities NDB Bank exposes itself to a credit risk. This concerns the Balance Sheet items, Loans and Advances and Lease Rentals Receivable. Concentration of the credit risk could result in a material loss for NDB Bank if a change in economic circumstances were to impinge upon a whole industry or the country. However, in order to maintain such risk at a manageable level NDB Bank has established prudent credit controls, such as predetermined sector and group exposure limits and Board and Management Credit Committees. Security is also invariably obtained when granting credit.

NDB Bank's exposure to credit risk is concentrated in companies domiciled in Sri Lanka. NDB Bank's lending portfolio is diversified covering all sectors of the economy. The total lending exposure of NDB Bank as at the Balance Sheet date, shows the following analysis:

	2006 %	2005 %
Food, beverage and tobacco	8.4	11.5
Agriculture, agro-business and fisheries	6.0	8.4
Textiles and garments	9.5	7.5
Wood and paper products	0.5	1.4
Rubber and leather products	7.4	8.4
Metals, chemicals and engineering	12.1	13.7
Hotels and tourism	1.0	1.5
Utilities	6.8	7.8
Housing Finance	4.8	0.2
Services	35.8	26.9
Transport	4.3	2.7
Other	3.4	10.0
	100.0	100.0

These concentrated exposures, direct and indirect have been considered in setting the level of specific and general provisions for bad and doubtful loans, advances and lease receivables.

24.2 Non-Performing Loans, Advances and Leases

Non-performing loans, advances and leases are those balances where capital or interest is in arrears for three months or more. Interest is not accrued to revenue on these accounts. Non-performing loans, advances and leases that are rescheduled need to perform for six consecutive months before they can be reclassified. The capital balance outstanding on the non-performing accounts are as follows:

Bank	Loans and Advances Rs '000	Lease Capital Rs '000	2006 Total Rs '000	2005 Total Rs '000
Gross	881,058	50,380	931,438	1,591,036
Net of tangible securities and Central Bank mandated specific provisions	577,441	10,669	588,110	533,209

	2006 Percentage Holding	2006 Cost Rs '000	2006 Directors' Valuation/ Fair Value Rs '000	2005 Percentage Holding	2005 Cost Rs '000
25. INVESTMENTS IN SUBSIDIARY COMPANIES					
Capital Development & Investment Co. Ltd.	75.60%	1,169,336	2,981,772	75.60%	1,169,336
Development Holdings (Pvt) Ltd. - ordinary shares	58.61%	228,150	305,719	58.60%	228,150
Development Holdings (Pvt) Ltd. - preference shares	100.00%	200,000	200,000	100.00%	200,000
NDB Housing Bank Ltd.	—	—	—	80.00%	570,000
NDB Investment Bank Ltd.	80.10%	32,040	60,261	80.10%	32,040
NDBS Stockbrokers (Pvt) Ltd.	100.00%	26,940	134,252	100.00%	26,940
NDB Venture Investments (Pvt) Ltd.	—	—	—	61.11%	137,500
		1,656,466	3,682,004		2,363,966

NDB Bank has a 100% holding in NDB Industrial Estates (Pvt) Ltd., in which Company, Rs 30 has been invested as share capital.

NDB Bank's holding in NDB Housing Bank Ltd. which originally was 41.34% (direct holding of 30% and 15% through Capital Development and Investment Company Ltd.) was increased to 80% as at 31 December 2005 by the acquisition of the shares held by Capital Development and Investment Company Ltd. and some of the minority shareholders at a price of Rs 13 per share. NDB Bank further acquired the balance minority shareholding of 15% during the first quarter of 2006 and the balance 5% in April 2006. Consequently, NDB Bank's holding in NDB Housing Bank Ltd. was 100%.

On 1 September 2006, NDB Bank acquired the assets and liabilities of NDB Housing Bank Ltd. NDB Housing Bank Ltd. is now under liquidation.

On 1 February 2006, Capital Development and Investment Company Ltd, a subsidiary of NDB Bank disposed of 58.44% of its holding in its fully-owned subsidiary NDB Finance Lanka (Pvt) Ltd. (now known as Aviva NDB Finance Lanka (Pvt) Ltd.) to Aviva International Holdings Ltd. The current holding of Capital Development and Investment Company Ltd. in Aviva NDB Finance Lanka (Pvt) Ltd. is 41.56%. Aviva NDB Finance Lanka (Pvt) Ltd. holds 87.27% of Eagle Insurance Company Ltd., thus giving Aviva International Holdings Ltd. a 51% stake in Eagle Insurance Company Ltd.

On 2 February 2006, NDB Bank purchased a 5% stake in Eagle Insurance Company Ltd. from James Finlay and Company (Colombo) Ltd. Consequently, NDB Bank's original and current effective holdings in Eagle Insurance Company Ltd. are 65.98% and 32.42% respectively. The capital gain earned by Capital Development and Investment Company Ltd. on this transaction was Rs 1.64 bn. In accordance with Sri Lanka Accounting Standard No. 26, 'Consolidated Financial Statements and Accounting for Subsidiaries', the capital gain earned by the NDB Group net of minority interest was Rs 1.01 bn.

From 1 February 2006, Aviva NDB Finance Lanka (Pvt) Ltd., the holding Company of Eagle Insurance Company Ltd. was accounted for as an associate. During the comparative period it was accounted as a subsidiary.

There was a capital reduction of the total investment in 'A' portfolio of NDB Venture Investments (Pvt) Ltd., a subsidiary of NDB Bank, during the period. Consequently, the 'B' portfolio of NDB Venture Investments (Pvt) Ltd. in which NDB Bank holds 50% was accounted for as an associate with effect from 31 May 2006.

All subsidiary companies are audited by Ernst & Young.

	Percentage Holding	2006 Cost Rs '000	2006 Directors' Valuation Rs '000	Percentage Holding	2005 Cost Rs '000
26. INVESTMENTS IN ASSOCIATE COMPANIES					
(a) NDB Bank					
Ayojana Fund (Pvt) Ltd.	50.00%	100	49,090	50.00%	100
Maldives Finance Leasing Co. (Pvt) Ltd.	35.00%	165,462	234,661	35.00%	165,462
NDB Venture Investments (Pvt) Ltd	50.00%	67,500	91,839	—	—
		233,062	375,590		165,562

There was a capital reduction of the total investment in 'A' portfolio of NDB Venture Investments (Pvt) Ltd., a subsidiary of NDB Bank, during the period. Consequently, the 'B' portfolio of NDB Venture Investments (Pvt) Ltd. in which NDB Bank holds 50% was accounted for as an associate with effect from 31 May 2006.

	As at 01.01.06 Rs '000	Conversion of Subsidiary to an Associate Rs '000	Exchange Gain on Valuation Rs '000	Profit Net of Dividend Received Rs '000	As at 31.12.06 Rs '000
(b) NDB Group					
Ayojana Fund (Pvt) Ltd.	38,268	—	—	10,822	49,090
Maldives Finance Leasing Co. (Pvt) Ltd.	202,948	—	16,692	15,021	234,661
NDB Venture Investments (Pvt) Ltd.	—	88,843	—	2,997	91,840
Aviva NDB Finance Lanka (Pvt) Ltd.	—	720,524	—	82,891	803,415
	241,216	809,367	16,692	111,731	1,179,006

NDB Bank's investment in Development Insurance Brokers (Pvt) Ltd. is Rs 10/-. The Company has not commenced commercial operations.

All associate companies are audited by Ernst & Young, except for Aviva NDB Finance Lanka (Pvt) Ltd. which is audited by PricewaterhouseCoopers.

	NDB BANK		NDB GROUP	
	2006 Rs '000	2005 Rs '000	2006 Rs '000	2005 Rs '000
27. GROUP BALANCES RECEIVABLE				
Ayojana Fund (Pvt) Ltd.	–	25,000	–	25,000
Capital Development and Investment Co. Ltd.	–	32	–	–
Maldives Finance Leasing Co. (Pvt) Ltd.	1,663	309	1,663	309
NDB Industrial Estates Ltd.	34,584	39,458	–	–
	36,247	64,799	1,663	25,309

	NDB BANK		NDB GROUP	
	2006 Rs '000	2005 Rs '000	2006 Rs '000	2005 Rs '000
28. OTHER ASSETS				
Sundry receivables	863,015	604,208	1,016,475	2,240,994
Payments in advance	61,959	35,161	65,880	134,357
Employee Share Ownership Plan (ESOP)	148,953	171,869	148,953	171,869
Policy loans	–	–	–	431,682
	1,073,927	811,238	1,231,308	2,978,902

The ESOP represents the written down value of the NDB shares paid for by NDB Bank on behalf of a trust for the benefit of the employees. The total cost of Rs 229 mn is being amortized over a period of 20 years with effect from 1 January 2000.

	NDB BANK		NDB GROUP	
	2006 Rs '000	2005 Rs '000	2006 Rs '000	2005 Rs '000
29. DEFERRED TAXATION				
Balance as at 1 January as previously reported	–	(90,119)	–	(121,572)
Effect due to adoption of revised accounting standard	–	121,561	–	184,467
Balance as at 1 January (Restated)	17,777	31,442	17,777	62,895
Acquisition/(disposal) of a subsidiary	–	–	–	(31,453)
(Charge)/release for the year	25,415	(13,665)	25,415	(13,665)
Balance as at 31 December	43,192	17,777	43,192	17,777

NDB Bank has adopted the Sri Lanka Accounting Standard No. 14, Income Taxes (revised) which came into effect from 1 January 2006, with retrospective effect as per the transitional provisions therein. Accordingly, the prior year figures have been restated.

	Land and Buildings Rs '000	Motor Vehicles Rs '000	Furniture and Equipment Rs '000	Total Rs '000
30. PROPERTY, PLANT & EQUIPMENT				
30.1 Bank				
Cost				
Freehold Assets				
As at 1 January 2006	541,852	253,155	519,056	1,314,063
Additions during the year	36,302	40,550	89,806	166,658
Disposals during the year	–	(15,917)	(517)	(16,434)
As at 31 December 2006	578,154	277,788	608,345	1,464,287

	Land and Buildings Rs '000	Motor Vehicles Rs '000	Furniture and Equipment Rs '000	Total Rs '000
Depreciation/Amortization				
Freehold Assets				
As at 1 January 2006	143,284	200,258	272,261	615,803
Charge for the year	27,239	27,244	137,804	192,287
On disposals	–	(15,247)	(439)	(15,686)
As at 31 December 2006	170,523	212,255	409,626	792,404
Written down value as at 31 December 2006 (a) - (b)	407,631	65,533	198,719	671,883
Written down value as at 31 December 2005	398,568	52,897	246,795	698,260

	Land and Buildings Rs '000	Motor Vehicles Rs '000	Furniture and Equipment Rs '000	Work-in- Progress Rs '000	Total Rs '000
30.2 NDB Group					
Cost					
Freehold Assets					
As at 1 January 2006	1,262,369	288,177	1,160,499	145,693	2,856,738
Transfer to investment property	(653,946)	–	–	–	(653,946)
Additions during the year	36,302	43,311	90,892	–	170,505
Disposals during the year	–	(15,917)	(5,838)	–	(21,755)
Adjustment on disposal of subsidiaries	(66,571)	(25,581)	(514,702)	(145,693)	(752,547)
Adjustment on transfer of fixed assets*	–	–	(16,364)	–	(16,364)
As at 31 December 2006	578,154	289,990	714,487	–	1,582,631
Depreciation/Amortization					
Freehold Assets					
As at 1 January 2006	250,436	232,137	767,566	–	1,250,139
Transfer to investment property	(72,581)	–	–	–	(72,581)
Charge for the year	27,239	29,060	143,353	–	199,652
On disposals	–	(15,247)	(5,760)	–	(21,007)
Adjustment on disposal of subsidiaries	(34,571)	(27,534)	(388,297)	–	(450,402)
Adjustment on transfer of fixed assets*	–	–	(14,699)	–	(14,699)
As at 31 December 2006	170,523	218,416	502,163	–	891,102
Written down value as at 31 December 2006 (a) - (b)	407,631	71,574	212,324	–	691,529
Written down value as at 31 December 2005	1,011,933	56,040	392,933	145,693	1,606,599

* As a result of the disposal of 58.44% holding in Aviva NDB Finance Lanka (Pvt) Ltd. on 1 February 2006.

30.3 Assets on Operating Leases

Assets purchased for the purpose of granting operating leases to customers are included above. The details are as follows:

	NDB BANK		NDB GROUP	
	2006	2005	2006	2005
	Rs '000	Rs '000	Rs '000	Rs '000
Cost as at 31 December	157,931	163,201	157,931	163,201
Less: Accumulated depreciation as at 31 December	(156,678)	(156,410)	(156,678)	(156,410)
Written down value as at 31 December	1,253	6,791	1,253	6,791

	NDB BANK		NDB GROUP	
	2006	2005	2006	2005
	Rs '000	Rs '000	Rs '000	Rs '000
31. GOODWILL				
Goodwill arises on consolidation of NDB Bank's subsidiaries				
At the beginning of the year				
Gross amount	380,581	–	1,033,866	1,654,481
Accumulated amortization	–	–	(161,147)	(119,410)
Provision for goodwill (b)	(380,581)	–	–	–
	–	–	872,719	1,535,071
Movement during the year				
Recorded during the year	–	–	–	70,106
Realized on conversion of an subsidiary to an associate	–	–	(802,613)	(690,721)
Realized on transfer of assets and liabilities of an subsidiary to NDB Bank Ltd.	–	–	(70,106)	–
Amortization	–	–	–	(41,737)
Acquired on business combinations (Restated)	–	380,581	–	–
At the end of the year				
Gross amount	380,581	380,581	161,147	1,033,866
Accumulated amortization	–	–	(161,147)	(161,147)
Provision for goodwill (b)	(380,581)	(380,581)	–	–
Net balance	–	–	–	872,719

- (a) With effect from 1 June 2005, any unamortized goodwill as at that date and any goodwill arising on consolidation subsequently will be tested for impairment annually and any impairment loss will be recognized in the Income Statement.
- (b) A full provision has been made against equity for the goodwill arising on the transfer of assets and liabilities of NDB Bank Ltd. on 1 August 2005 to be in line with the provisions contained under Section 22 of the Banking Act to declare dividends.

	NDB BANK		NDB GROUP	
	2006 Rs '000	2005 Rs '000	2006 Rs '000	2005 Rs '000
32. DEPOSITS				
Savings deposits	2,506,488	2,035,756	2,506,488	2,035,756
Time deposits	13,828,460	8,905,031	13,828,460	8,905,031
Certificate of deposits	43,030	94,448	43,030	94,448
Demand deposits	4,381,230	2,562,599	4,381,230	2,562,599
Margins	401,896	355,895	401,896	355,895
	21,161,104	13,953,729	21,161,104	13,953,729

	2006 Rs '000	2005 Rs '000
33. BORROWINGS		
(a) NDB Bank		
Government of Sri Lanka loans under ADB, IDA, KfW and JBIC credit lines	14,493,976	14,427,237
Other Government of Sri Lanka loans	118,000	177,000
Foreign borrowings	3,211,476	3,398,941
Local borrowings	7,114,752	4,702,006
	24,938,204	22,705,184
Dues to banks	—	280
	24,938,204	22,705,464

	Up to 1 year Rs '000	1 to 5 years Rs '000	More than 5 years Rs '000	Total Rs '000
(a.1) Maturity of Borrowings				
Government of Sri Lanka loans under ADB, IDA, KfW and JBIC credit lines	1,909,135	6,948,095	5,636,746	14,493,976
Other Government of Sri Lanka loans	88,500	29,500	—	118,000
Foreign borrowings	3,211,476	—	—	3,211,476
Local borrowings	3,463,199	2,462,663	1,188,890	7,114,752
	8,672,310	9,440,258	6,825,636	24,938,204

	2006 Rs '000	2005 Rs '000
(b) NDB Group		
Government of Sri Lanka loans under ADB, IDA, KfW and JBIC credit lines	14,493,976	14,424,183
Other Government of Sri Lanka loans	118,000	177,000
Foreign borrowings	3,211,476	3,401,995
Local borrowings	5,357,782	5,246,349
	23,181,234	23,249,527
Dues to banks	275	23,568
	23,181,509	23,273,095

	Up to 1 year Rs '000	1 to 5 years Rs '000	More than 5 years Rs '000	Total Rs '000
(b.1) Maturity of Borrowings				
Government of Sri Lanka loans under				
ADB, IDA, KfW and JBIC credit lines	1,909,135	6,948,095	5,636,746	14,493,976
Other Government of Sri Lanka loans	88,500	29,500	–	118,000
Foreign borrowings	3,211,476	–	–	3,211,476
Local borrowings	1,706,229	2,462,663	1,188,890	5,357,782
Dues to banks	275	–	–	275
	6,915,615	9,440,258	6,825,636	23,181,509

	NDB BANK		NDB GROUP	
	2006 Rs '000	2005 Rs '000	2006 Rs '000	2005 Rs '000
34. OTHER LIABILITIES				
Interest payable	802,283	463,244	802,283	489,944
Accrued expenses	171,500	174,632	196,257	211,451
Other liabilities	895,961	997,711	985,131	2,145,556
	1,869,744	1,635,587	1,983,671	2,846,951

	NDB BANK & GROUP			
	Number	Par Value Rs	2006 Rs '000	2005 Rs '000
35. SHARE CAPITAL				
Authorized				
200,000,000 ordinary shares of Rs 10/- each			2,000,000	2,000,000
Issued and fully paid				
Balance as at 1 January	54,570,257	10	545,703	537,500
Issue of new shares (Note a)	820,257	10	–	8,203
Issue of bonus shares (Note b)	27,285,128	10	272,851	–
Balance as at 31 December			818,554	545,703

- (a) The increase in the issued share capital in 2005 was due to the issue of 820,257 new shares to the shareholders of NDB Bank Ltd. at a ratio of 1 share for every 5.6 shares held in NDB Bank Ltd. as a consideration for the transfer of the assets and liabilities of NDB Bank Ltd. to NDB Bank on 1 August 2005.
- (b) At an Extraordinary General Meeting of NDB Bank held on 26 April 2006, the shareholders approved a bonus issue of one ordinary share for every two shares held in the issued share capital of NDB Bank.

	NDB BANK & GROUP	
	2006 Rs '000	2005 Rs '000
36. SHARE PREMIUM RESERVE		
Balance as at 1 January	214,377	91,667
Transfers resulting from the issue of new shares	–	122,710
Balance as at 31 December	214,377	214,377

The Share Premium Reserve of Rs 91.7 mn arose in 1997 from the early conversion of the Government held convertible debentures into ordinary shares. During 2005, a further share premium arose on the issue of 820,257 new shares to the shareholders of NDB Bank Ltd. as explained in Note 35 (a) above.

37. STATUTORY RESERVE FUND

A Statutory Reserve Fund was created out of revenue reserves to comply with a direction issued to Licensed Banks by the Monetary Board of the Central Bank of Sri Lanka under Section 76J (1) of the Banking Act, No. 30 of 1988.

	NDB BANK		NDB GROUP	
	2006 Rs '000	2005 Rs '000	2006 Rs '000	2005 Rs '000
Balance as at 1 January	545,703	537,500	545,703	546,485
Issue of new shares	272,851	8,203	272,851	8,203
Adjustment on disposal	–	–	–	(8,985)
Balance as at 31 December	818,554	545,703	818,554	545,703

	General Reserves Rs '000	Retained Profit Rs '000	Total Rs '000
38. REVENUE RESERVES			
(a) NDB Bank			
As at 1 January 2006	5,805,707	728,396	6,534,103
Effect of adopting revised SLAS - 14	–	90,408	90,408
Retained profit b/f (Restated)	5,805,707	818,804	6,624,511
Profit after taxation	–	1,004,997	1,004,997
Dividends paid	–	(327,422)	(327,422)
Bonus issue	–	(272,851)	(272,851)
Transfer to statutory reserve fund	–	(272,851)	(272,851)
Exchange difference on conversion of FCBU reserves	–	11,390	11,390
Difference between the investment and net assets taken over from NDB Housing Bank Ltd.	–	(64,532)	(64,532)
As at 31 December 2006	5,805,707	897,535	6,703,242

	General Reserves Rs '000	Retained Profit Rs '000	Total Rs '000
(b) NDB Group			
As at 1 January 2006	5,805,707	1,613,289	7,418,996
Effect of adopting revised SLAS - 14	–	90,408	90,408
Retained profit b/f (Restated)	5,805,707	1,703,697	7,509,404
Exchange gain from valuation of foreign associate	–	16,692	16,692
Profit after taxation	–	2,030,484	2,030,484
Investment property fair value adjustment	–	340,252	340,252
Dividends paid	–	(327,422)	(327,422)
Bonus issue	–	(272,851)	(272,851)
Transfer to statutory reserve fund	–	(272,851)	(272,851)
Exchange difference on conversion of FCBU reserves	–	11,390	11,390
Adjustment on disposal of subsidiaries	–	(255,412)	(255,412)
Difference between the investment and net assets taken over from NDB Housing Bank Ltd.	–	(64,532)	(64,532)
As at 31 December 2006	5,805,707	2,909,447	8,715,154

39. MATURITY ANALYSIS - NDB BANK

An analysis of the assets and liabilities based on the remaining period at the Balance Sheet date to the respective contractual maturity dates, is as follows:

	Up to 3 months Rs '000	3 to 12 months Rs '000	1 to 3 years Rs '000	3 to 5 years Rs '000	More than 5 years Rs '000	Total Rs '000
Interest Earning Assets						
<i>Cash and Short-Term Funds</i>						
Cash in hand and with banks	271,690	–	–	–	–	271,690
	271,690	–	–	–	–	271,690
<i>Investments Held for Trading</i>						
Treasury bills	2,637,543	–	–	–	–	2,637,543
Treasury bonds	2,598,056	–	–	–	–	2,598,056
	5,235,599	–	–	–	–	5,235,599
<i>Bills of Exchange</i>	1,180,221	411,710	–	–	–	1,591,931
<i>Commercial paper</i>	605,100	–	–	–	–	605,100
<i>Investments Held to Maturity</i>						
Sinking fund investments (Note 24.4)	–	2,873,288	–	–	–	2,873,288
Other securities	190,319	416,204	398,607	14,825	–	1,019,955
Treasury bonds	98,716	–	1,261,927	–	100,000	1,460,643
	289,035	3,289,492	1,660,534	14,825	100,000	5,353,886

	Up to 3 months Rs '000	3 to 12 months Rs '000	1 to 3 years Rs '000	3 to 5 years Rs '000	More than 5 years Rs '000	Total Rs '000
Loans and Advances						
Direct loans (Gross)	15,320,769	4,757,370	7,305,780	3,270,690	1,085,320	31,739,929
Refinance loans (Gross)	198,669	376,010	783,710	416,880	538,670	2,313,939
Staff loans	35,133	102,770	274,050	148,450	11,406	571,809
Overdrafts	6,157,157	–	–	–	–	6,157,157
Provisions for bad and doubtful debts	(1,727,144)	–	–	–	–	(1,727,144)
	19,984,584	5,236,150	8,363,540	3,836,020	1,635,396	39,055,690
Interest receivable	420,018	–	–	–	–	420,018
Lease rentals receivable	32,920	56,464	428,699	864,185	66,808	1,499,077
	452,938	56,464	428,699	864,185	66,808	1,919,095
Non-Interest Earning Assets						
Balances with Central Bank	1,575,260	–	–	–	–	1,575,260
Dues from banks	3,123,076	–	–	–	–	3,123,076
	4,698,336	–	–	–	–	4,698,336
Investments Held to Maturity						
Quoted shares	20,481	–	268,373	–	–	288,854
Non-quoted shares/debentures	–	–	175,000	–	392,579	567,579
	20,481	–	443,373	–	392,579	856,433
Investments in subsidiaries and associates	–	–	–	–	1,889,528	1,889,528
NDB Group balances/other assets	1,110,174	–	–	–	–	1,110,174
Deferred tax	–	–	–	–	43,192	43,192
Property, plant & equipment	–	–	–	–	671,883	671,883
As at 31 December 2006	33,848,159	8,993,816	10,896,146	4,715,030	4,799,386	63,252,537
As at 31 December 2005	22,708,557	6,317,845	13,126,175	3,546,850	5,250,621	50,950,048
Interest Bearing Liabilities						
Borrowings						
Government of Sri Lanka loans under						
ADB, IDA, KfW and JBIC credit lines	397,300	1,511,835	3,590,112	3,357,983	5,636,746	14,493,976
Other Government of Sri Lanka loans	29,500	59,000	29,500	–	–	118,000
Foreign borrowings	–	3,211,476	–	–	–	3,211,476
Local borrowings	1,850,783	1,612,416	2,251,803	210,860	1,188,890	7,114,752
	2,277,583	6,394,727	5,871,415	3,568,843	6,825,636	24,938,204

	Up to 3 months Rs '000	3 to 12 months Rs '000	1 to 3 years Rs '000	3 to 5 years Rs '000	More than 5 years Rs '000	Total Rs '000
Securities sold under repurchase agreements	5,319,146	701,600	1,270	–	–	6,022,016
Deposits	14,190,094	4,920,320	87,610	146,220	1,816,860	21,161,104
	21,786,823	12,016,647	5,960,295	3,715,063	8,642,496	52,121,324
Non-Interest Bearing Liabilities						
NDB Group balances/sundry creditors	1,869,744	–	–	–	–	1,869,744
Taxation	598,824	–	–	–	–	598,824
Dividends payable	107,918	–	–	–	–	107,918
	2,576,486	–	–	–	–	2,576,486
As at 31 December 2006	24,363,309	12,016,647	5,960,295	3,715,063	8,642,496	54,697,810
As at 31 December 2005	19,496,801	6,725,620	8,063,227	2,882,590	5,851,516	43,019,754

40. COMMITMENTS AND CONTINGENCIES

40.1 Business Commitments

In the normal course of business, NDB Bank makes various commitments and incurs certain contingent liabilities some of which give rise to legal recourse to its customers. No material losses are anticipated as a result of these transactions.

These commitments are quantified below:

	NDB BANK		NDB GROUP	
	2006 Rs '000	2005 Rs '000	2006 Rs '000	2005 Rs '000
Undisbursed financing commitments	2,036,481	1,517,824	2,036,481	1,617,457
Guarantees	5,993,511	3,277,187	5,993,511	3,277,187
Commitments on account of letters of credit	4,137,415	2,509,857	4,137,415	2,509,857
Forward exchange contracts	109,199	349,473	109,199	349,473
Acceptances	1,703,606	1,198,846	1,703,606	1,198,846
Travellers cheques	72,771	72,670	72,771	72,670
	14,052,983	8,925,857	14,052,983	9,025,490

40.2 Litigation against NDB Bank

In the normal course of business, NDB Bank is a party to various types of litigation, including litigation with borrowers who are in default in terms of their loan agreements. As of the Balance Sheet date 28 client companies have filed cases against NDB Bank preventing the sale of assets mortgaged to NDB Bank. NDB Bank's legal counsel is of the opinion that litigation which is currently pending will not have a material impact on the reported financial results or the future operations of NDB Bank.

41. SEGMENTAL ANALYSIS - NDB GROUP

	Banking		Equity		Property Investment		Insurance*		Others		Consolidated	
	2006 Rs '000	2005 Rs '000	2006 Rs '000	2005 Rs '000	2006 Rs '000	2005 Rs '000	2006 Rs '000	2005 Rs '000	2006 Rs '000	2005 Rs '000	2006 Rs '000	2005 Rs '000
Revenue												
External income	6,524,820	4,739,806	1,158,374	480,973	171,797	104,489	76,570	1,521,655	270,952	210,513	8,202,513	7,057,436
Inter-segment income	–	–	–	–	11,825	14,228	–	10,545	139,038	14,040	150,863	38,813
Total income	6,524,820	4,739,806	1,158,374	480,973	183,622	118,717	76,570	1,532,200	409,990	224,553	8,353,376	7,096,249
Segment expenses	(4,790,533)	(3,882,270)	25,361	(63,423)	(41,710)	(42,111)	(60,227)	(1,008,893)	(122,503)	(174,985)	(4,989,612)	(5,171,682)
Inter-segment expenses	–	–	–	–	(11,825)	(14,228)	–	(10,545)	(139,038)	(14,040)	(150,863)	(38,813)
Segment results	1,734,287	857,536	1,583,062	417,550	130,087	62,378	16,343	512,762	148,449	35,528	3,212,901	1,885,754
Unallocated expenses	–	–	–	–	–	–	–	–	–	–	–	(41,737)
Operating profit	–	–	–	–	–	–	–	–	–	–	3,212,901	1,844,017
Share of associate companies' profit before taxation	24,243	14,910	14,424	6,755	–	–	175,786	–	–	–	214,453	21,665
Taxation	–	–	–	–	–	–	–	–	–	–	(754,066)	(341,680)
VAT on financial services	–	–	–	–	–	–	–	–	–	–	(466,383)	(251,339)
Profit after taxation	–	–	–	–	–	–	–	–	–	–	2,206,905	1,272,663
Other information												
Segment assets	60,611,906	50,173,149	867,859	1,293,543	1,237,112	617,271	–	12,208,632	1,081,614	180,755	63,798,491	64,473,350
Investment in associates	234,661	202,948	140,929	38,269	–	–	803,416	–	–	–	1,179,006	241,217
Consolidated total assets											64,977,497	64,714,567
Segment liabilities	52,957,355	43,655,442	–	–	28,881	21,676	–	11,191,943	110,390	55,840	53,096,626	54,924,901
Consolidated total liabilities											53,096,626	54,924,901

* The insurance segment is given only up to 1 February 2006, due to the disposal of a part of Aviva NDB Finance Lanka (Pvt) Ltd. shares by Capital Development & Investment Company Ltd. to Aviva International Holdings Ltd. as explained in Note 1 to the Financial Statements.

42. CAPITAL ADEQUACY

This term is used to describe the adequacy of Bank's aggregate capital in relation to the risks which arise from its assets and its off balance sheet transactions. The minimum risk sensitive capital required to be maintained by NDB Bank is prescribed by Central Bank of Sri Lanka and is consistent with the international standards of Basel Committee on Banking Capital Regulations and Supervisory Practices. The aim is to ensure minimum capital, commensurate with risks assumed by NDB Bank, is maintained as a buffer to absorb credit losses.

Basis of Computation

The risk weights assigned to the on and off balance sheet assets and composition of capital are prescribed by Central Bank of Sri Lanka.

	NDB BANK	
Capital Base as at 31 December	2006	2005
	Rs '000	Rs '000
Tier 1: Core Capital		
Paid-up ordinary shares	818,554	545,703
Share premium	214,377	214,377
Statutory reserve fund	818,554	545,703
Published retained profits	897,536	818,804
General & other reserves	5,805,707	5,805,707
Minority interest	–	–
	8,554,728	7,930,294
Deductions		
Goodwill	–	–
Total Tier 1 Capital	8,554,728	7,930,294
Tier 2: Supplementary Capital		
General provision	275,159	164,630
Approved subordinated term debt	924,750	–
Total Tier 2 Capital	1,199,909	164,630
Total Tier 1 & Tier 2 Capital	9,754,637	8,094,924
Deductions		
Equity investments in unconsolidated banking & financial subsidiaries	1,228,316	1,935,816
Investments in capital of other banks and financial associates	331,703	264,203
Capital Base	8,194,618	5,894,905

Risk Weighted Assets and Off-Balance Sheet Exposure

	NDB BANK				
	Principal Amount		Risk	Risk Weighted	
	of On-Balance Sheet Items		Weights	Asset Amount	
	2006	2005		2006	2005
	Rs '000	Rs '000	%	Rs '000	Rs '000
Cash,treasury bills & other securities with Central Bank	11,416,479	8,769,961	0	–	–
Loans secured against Sri Lanka Government guarantee	308,692	167,324	0	–	–
Loans secured by Provident Fund	150,327	98,882	0	–	–
Loans against cash deposits & gold	952,627	132,261	0	–	–
Loans guaranteed by OECD incorporated banks	303	23,436	20	61	4,687
Dues from banks abroad	1,244,282	1,077,972	20	248,856	215,594
Placements with and loans to other banks and financial institutions	4,234,898	843,083	20	846,980	168,617
Loans secured by Primary Mortgage	2,519,652	291,034	55	1,385,808	145,517
Other loans and advances	36,486,566	33,661,677	110	40,135,223	33,661,677
Other investments (excluding items deducted from total capital)	2,620,784	1,525,652	100	2,620,784	1,525,652
Property and equipment	671,883	713,923	100	671,883	713,923
Other receivables	1,004,414	1,449,043	100	1,004,414	1,449,043
Total Assets	61,610,907	48,754,248		46,914,009	37,884,710

Off-Balance Sheet Exposure

	Credit Conversion Factor, %	Principal Amount		Risk	Risk Weighted	
		of Off-Balance Sheet Items		Weights	Asset Amount	
		2006	2005		2006	2005
		Rs '000	Rs '000	%	Rs '000	Rs '000
General guarantees of indebtedness	100	2,662,053	1,770,388	100	2,662,053	1,770,388
Performance Bonds, Bid Bonds	50	423,881	300,561	100	211,941	150,281
Trade related acceptances	20	1,703,606	1,198,846	100	340,721	239,769
Shipping guarantees	20	2,907,577	1,206,238	100	581,515	241,248
Documentary letters of credit	20	4,137,415	2,509,857	100	827,483	501,971
Other commitments with an original maturity up to 1 year	20	72,771	72,670	100	14,554	14,534
Undrawn term loans	0	1,583,881	1,306,524	100	–	653,262
Others - Refinance loans	0	452,600	211,300	100	–	105,650
FX contracts - Banks	2	109,199	349,473	50	1,199	1,055
Total off balance sheet exposure		14,052,983	8,925,857		4,639,466	3,678,158
Market risk					1,059,998	–
Total Risk Weighted Assets and Off Balance Sheet Exposure					52,613,473	41,562,868
Risk Weighted Capital Ratios						
Tier 1 (Required statutory minimum ratio is 5%)					16.26	19.08
Tier 1 & Tier 2 (Required statutory minimum ratio is 10%)					15.58	14.18

NDB GROUP		
Capital Base as at 31 December	2006 Rs '000	2005 Rs '000
Tier 1: Core Capital		
Paid-up ordinary shares	818,554	545,703
Share premium	214,377	214,377
Statutory reserve fund	818,554	545,703
Published retained profits	2,909,448	1,703,697
General & other reserves	5,805,707	5,805,707
Minority interest	1,314,232	974,479
	11,880,872	9,789,666
Deductions		
Goodwill	–	872,719
Total Tier 1 Capital	11,880,872	8,916,947
Tier 2: Supplementary Capital		
General provision	275,159	180,637
Approved subordinated term debt	924,750	–
Total Tier 2 Capital	1,199,909	180,637
Total Tier 1 & Tier 2 Capital	13,080,781	9,097,584
Deductions		
Investments in capital of other banks and financial associates	1,277,647	344,077
Capital Base	11,803,134	8,753,507

Risk Weighted Assets and Off-Balance Sheet Exposure

	Principal Amount of On-Balance Sheet Items		Risk Weights	Risk Weighted Asset Amount	
	2006 Rs '000	2005 Rs '000	%	2006 Rs '000	2005 Rs '000
Cash, treasury bills & other securities with Central Bank	11,416,494	17,717,096	0	–	–
Loans secured against Sri Lanka Government guarantee	308,692	167,324	0	–	–
Loans secured by Provident Fund	150,327	98,882	0	–	–
Loans against cash deposits & gold	952,627	132,261	0	–	–
Loans guaranteed by OECD incorporated banks	303	23,436	20	61	4,687
Dues from banks abroad	1,244,282	1,077,972	20	248,856	215,594
Placements with and loans to other banks and financial institutions	5,307,271	1,652,873	20	1,061,454	330,575
Loans secured by Primary Mortgage *	2,519,652	291,034	55	1,385,808	145,517
Other loans and advances *	36,495,792	34,837,579	110	40,145,371	34,837,579
Other investments (excluding items deducted from total capital)	2,204,060	2,150,802	100	2,204,060	2,150,802
Property and equipment	691,529	1,040,897	100	691,529	1,040,897
Other receivables	2,327,211	4,908,478	100	2,327,211	4,908,478
Total Assets	63,618,240	64,098,634		48,064,350	43,634,129

* In 2005 Risk Weight % for loans secured by primary mortgage and other loans and advances were 50% and 100% respectively.

Off Balance Sheet Exposure

	Credit Conversion Factor	Principal Amount of On-Balance Sheet Items	Risk Weights	Risk Weighted Asset Amount
		2006	2005	
	%	Rs '000	Rs '000	%
		2006	2005	
		Rs '000	Rs '000	%
General guarantees of indebtedness	100	2,662,053	1,770,388	100
Performance Bonds, Bid Bonds	50	423,881	300,561	100
Trade related acceptances	20	1,703,606	1,198,846	100
Shipping guarantees	20	2,907,577	1,206,238	100
Documentary letters of credit	20	4,137,415	2,509,857	100
Other commitments with an original maturity up to 1 year	20	72,771	72,670	100
Undrawn term loans	0	1,583,881	1,406,157	100
Others - Refinance loans	0	452,600	211,300	100
FX contracts - Banks	2	109,199	349,473	20
Total Off-Balance Sheet Exposure		14,052,983	9,025,490	
Market risk				
Total Risk Weighted Assets and Off-Balance Sheet Exposure				
Risk Weighted Capital Ratios				
Tier 1 (Required statutory minimum ratio is 5%)				
Tier 1 & Tier 2 (Required statutory minimum ratio is 10%)				

43. POST BALANCE SHEET EVENTS

The Board of Directors of NDB Bank decided to enter into negotiations with the Commercial Bank of Ceylon Ltd. on a possible merger between the two banks.

In the event that negotiations are successful and the manner in which the merger may be achieved is agreed upon, the proposal for such merger will be submitted to the Monetary Board of the Central Bank of Sri Lanka for its approval.

At this stage therefore a possible merger of the two banks is dependent upon the success of the negotiations and the grant of the necessary approvals by the Monetary Board and other regulatory bodies as well as by the respective shareholders of the two banks.

No other material events have taken place after the Balance Sheet date which require an adjustment to or a disclosure in the Financial Statements.

44. INVESTMENT PROPERTY

	NDB GROUP	
	2006	2005
	Rs '000	Rs '000
Balance as at 1 January	–	–
Additions/Transfers	581,365	–
Fair value adjustment transferred to equity	580,635	–
Fair value adjustment during the year	38,000	–
	1,200,000	–

Development Holdings Private Ltd., a subsidiary of NDB Bank, whose principal activity is renting out premises for commercial use, adopted the Sri Lanka Accounting Standard No. 40 - Investment Property. Accordingly, the property was revalued on 1 January 2006 and the surplus over the net book value of the property amounting to Rs 580 mn of which the Group's share after minority interests was of Rs 340 mn was credited to reserves. Further, another revaluation was done on 31 December 2006 and the incremental surplus over the valuation as at 1 January 2006 amounting to Rs 38 mn was credited to the Group Income Statement in 2006, in accordance with the Standard.

Investment Property is stated at fair value, which has been determined based on valuations performed by a professional valuer as at 1 January 2006 and 31 December 2006 on the basis of an open market value, supported by market evidence.

45. DIRECTORS' INTERESTS IN CONTRACTS WITH NDB BANK

The interest of each Director, direct or indirect in all financing and other arrangements have been disclosed to NDB Bank in accordance with Article 97 of the Memorandum and Articles of Association of National Development Bank Ltd. (NDB Bank) and the Companies Act, No. 17 of 1982.

45.1 S K Wickremesinghe, H D S Amarasuriya, A R Gunasekara, S T Nagendra, L de Mel, S R de Silva, G C B Wijeyesinghe and N S Welikala were Directors of NDB Bank from 1 January 2006 to 31 December 2006.

U L Kadurugamuwa and A A Pio resigned from the Board with effect from 23 January 2006 and 15 October 2006 respectively.

R B Thambiayah and R Vokes were appointed to the Board on 6 February 2006 and 11 December 2006 respectively.

45.2 Certain Directors of NDB Bank are also Directors of the following entities which have financing arrangements with NDB Bank in the normal course of business.

Name of Director	Relationship	Company	Balance as at 31.12.2006 Rs '000	Balance as at 31.12.2005 Rs '000	Nature of Transaction
S K Wickremesinghe	Director	CIC Fertilizers Ltd.	121,042	138,542	Project Loan
			226	121,065	Letter of credit
			2,124	779	Overdraft
N S Welikala	Director	Lakjaya Thrift and Credit Foundation Ltd.	2,378	6,125	Project Loan
			336	308	Deposits
	Director	Lanka Hospitals (Pvt) Ltd.	218,757	251,564	Project Loan
			27	687	Deposits
H D S Amarasuriya	Chairman	Commercial Leasing Co. Ltd.	484,800	517,500	Securitization
			373	(257)	Current Account Balance/ (Overdraft)
	Chairman	Regnis (Lanka) Ltd.	30,976	52,633	Project Loan
			90,000	90,000	Short-Term Loan
			8,542	39,475	Shipping Guarantee
			300	25,942	Letter of Credit
			65,822	101,798	Post Import Finance
			(3,157)	2,838	(Overdraft)/Current A/C Balance
	Chairman	Singer (Sri Lanka) Ltd.	300,000	50,000	Short-Term Loan
			184,834	409,302	Term Loan
			11,421	—	Shipping Guarantee
			130	11,434	Letter of Credit
			17,841	20,470	Overdraft
			175,000	175,000	Non-quoted Debenture
	Director	Bata Shoe Company of Ceylon Ltd.	16,000	28,000	Short-Term Loan
			3,443	(628)	Current Account Balance/ (Overdraft)
L de Mel	Director	Cisco Specialty Packaging (Pvt) Ltd.	48,750	63,636	Project Loan
S R de Silva	Director	Lanka Walltiles Meepe (Pvt) Ltd.	4,108	—	Project Loan
			1,375	4,029	Operating Lease
	Director	Lanka Tiles Ltd.	2,828	3,074	Project Loan
G C B Wijeyesinghe	Director	Regnis (Lanka) Ltd.	30,976	52,633	Project Loan
			90,000	90,000	Short-Term Loan
			8,542	39,475	Shipping Guarantee
			300	25,942	Letter of Credit
			65,822	101,798	Post Import Finance
			(3,157)	2,838	(Overdraft)/Current A/C Balance
	Director	Singer (Sri Lanka) Ltd.	300,000	50,000	Short-Term Loan
			184,834	409,302	Term Loan
			11,421	—	Shipping Guarantee
			130	11,434	Letter of Credit
			17,841	20,470	Overdraft
			175,000	175,000	Non-quoted Debenture
	Director	Central Finance Co. Ltd.	400,000	400,000	Short-Term Loan

Name of Director	Relationship	Company	Balance as at 31.12.2006 Rs '000	Balance as at 31.12.2005 Rs '000	Nature of Transaction
S T Nagendra	Director	Acme Printing & Packaging Ltd.	35,817	30,735	Post Import Finance
			14,115	–	Shipping Guarantee
			35	37,386	Letter of Credit
			31,850	31,850	Short-Term Loan
			210	9,441	Shipping Guarantee
			113	22,201	Letter of Credit
	Director	Lanka Aluminium Industries Ltd.	800	66,318	Overdraft
			48,510	–	Packing Credit Loan
			528	514	Call Deposit
			22	–	Current Account Balance
			44	99	Current Account Balance
			4,608	–	Current Account Balance
	Director	Texlan Lanka Ltd.	121,042	138,542	Project Loan
			226	121,065	Letter of Credit
			2,124	779	Overdraft
			21,553	15,658	Packing Credit Loan
			775	1,257	Overdraft
	Chairman	Classic Teas (Pvt)Ltd.			
Ravi Thambiayah	Director	Royal Ceramics Lanka Ltd.	47,115	–	Project Loan

45.3 Transactions with related companies, where the abovementioned Directors are also Directors of such Companies are disclosed in Note 46.2.

46. RELATED PARTY TRANSACTIONS

46.1 Transactions with Key Management and their close Family Members

Key management includes the members of the Board of Directors of NDB Bank and the key employees of NDB Bank holding Directorships in NDB Group Companies. NDB Bank carries out transactions with the key management and their related concerns in the ordinary course of its business on an arm's length basis at commercial rates except the loans that the key management have availed under the loan schemes uniformly applicable to all the staff at concessionary rates.

46.1.1 Key management of NDB Bank and their close family members had the following accounts/deposits with NDB Bank as at 31 December.

	2006 Rs '000	2005 Rs '000
Savings Deposits	1,509	2
Demand Deposits	147	87
Call Deposits	4,016	–
RFC - USD	4,975	–

46.1.2 Compensation for Key Management

Compensation paid by NDB Bank for key management amounted to Rs 37.8 mn during the year 2006 (Rs 29.4 mn in 2005)

46.2 Transactions with Related Companies

NDB Bank had the undermentioned financial dealings during the year with the following Subsidiaries and Associates of NDB Bank. The following Members of the Key Management were also Directors of the Group companies of NDB Bank as indicated below:

Company	Relationship	Member of the Key Management	Position	Amount 2006 Rs '000	Amount 2005 Rs '000	Details of Financial Dealings
Ayojana Fund (Pvt) Ltd.	Associate	N S Welikala A R Gunasekara G C B Wijeyesinghe	Director Director Director	–	25,000	NDB Bank contributed a sum of Rs 200 mn in the previous financial years to the Ayojana Fund (Pvt) Ltd., set up jointly with the Commonwealth Development Corporation. This was structured in the form of an interest free loan in terms of the shareholders' agreement. The balance outstanding of Rs. 25 mn was settled during the year.
Capital Development and Investment Company Ltd.	Subsidiary	Lal de Mel N S Welikala A R Gunasekara S N Jayasinghe (up to 31.01.2006)	Chairman Director Director Director	354,752 1,380 2,137 881,171 139,038 156,512 6,837	23,208 1,380 139,738 – 2,607 22,824 18,475	Dividend received from the Company Management fees received by NDB Bank Cash Balance at NDB Bank REPO Investments of the Company at NDB Bank Interest paid by NDB Bank on Short-term Investments Loan Settlement received by NDB Bank Interest received on loan balances
Development Holdings (Pvt) Ltd.	Subsidiary	N S Welikala Lal de Mel A R Gunasekara S N Jayasinghe	Director Director Director Director	200,000 30,000 5,010 8,027 1,384 27 28,871 1,356 11,813	200,000 40,687 4,620 8,027 1,377 31 92,164 27,547 10,435	Investment in Preference Shares by NDB Bank Preference Dividend received by NDB Bank Management Fees received by NDB Bank Rent paid by NDB Bank Electricity expenses reimbursed by NDB Bank Water expenses reimbursed by NDB Bank REPO Investments/call deposits of the Company in NDB Bank Cash Balance at NDB Bank Interest paid by NDB Bank on Short-term Investments
Maldives Finance Leasing Company (Pvt) Ltd.	Associate	N S Welikala	Director	1,663 9,222	309 6,792	Inter-Company balance receivable by NDB Bank Dividend received by NDB Bank
NDBS Stock Brokers (Pvt) Ltd.	Subsidiary	S K Wickremesinghe N S Welikala Lal de Mel S N Jayasinghe	Chairman Director Director Director	2,124 2,121 (268,373)	2,124 5,790 744,067	Rent received by NDB Bank Brokerage paid by NDB Bank (Payments)/receipts made by NDB Bank for purchases/sales
NDB Investment Bank Ltd.	Subsidiary	S K Wickremesinghe N S Welikala Lal de Mel Ajith Wickremaratne Eran Wickramaratne	Chairman Director Director Director Director	2,027 39,505	2,027 10,554	Rent received by NDB Bank Dividend received by NDB Bank
NDB Industrial Estates (Pvt) Ltd.	Subsidiary	Ajith Wickremaratne	Director	34,584	39,458	Inter-Company balance receivable by NDB Bank

46.3 Contribution to Pension Fund

NDB Bank contributed Rs 17.8 mn to the pension fund in year 2005.

There was no contribution made in 2006, as the current year's amortization of the actuarial gain and expected returns on assets were more than the cost of benefits this year.

47. COMPLETION OF INITIAL ACCOUNTING FOR BUSINESS COMBINATIONS

NDB Bank took over the assets and liabilities of NDB Bank Ltd. with effect from 1 August 2005. The initial accounting for business combinations was determined provisionally as at 31 December 2005 in which the combination was effected as the fair values to be assigned to the acquiree's identifiable assets, liabilities or contingent liabilities was accounted for by using provisional values.

As required by Sri Lanka Accounting Standard No. 25, Business Combinations PricewaterhouseCoopers were appointed to independently determine the fair value of the assets and liabilities taken over from NDB Bank Ltd. on 1 August 2005. They have confirmed that the excess over the identifiable assets and liabilities taken over from NDB Bank Ltd. on 1 August 2005 amounted to Rs 552 mn. Out of this amount the customer base taken over from NDB Bank Ltd. on 1 August 2005 amounted to Rs 173 mn. This amount was written off in full in the Income Statement in 2005. The balance goodwill of Rs 381 mn for which a full provision has been made against equity, will be tested for impairment annually. Accordingly, the previous year's figures have been restated.

48. RESTATEMENT OF CERTAIN PRIOR YEAR FIGURES

NDB Bank has restated certain prior year figures due to adoption of revised SLAS, and as a result of completing the initial accounting for Business Combinations. The effect is summarized below:

48.1 Effect on Adoption of Revised SLAS - 14, Income Taxes

NDB Bank has decided to adjust the transitional liability/asset with retrospective effect in accordance with the standard. The effect on the Financial Statements is given in Note 29 to these Financial Statements.

48.2 Completion of Initial Accounting for Business Combinations

The effect on the Financial Statements is summarized in Note 47 to these Financial Statements.

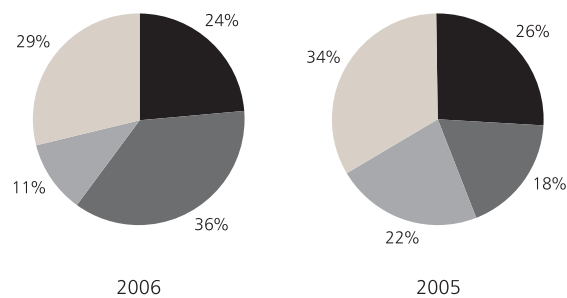
48.3 Certain ratios and disclosures in the Financial Statements have been restated taking the above effect into consideration.

NDB Bank

	2006 Rs '000	%	2005 Rs '000	%
VALUE ADDED				
Gross Income	6,888,379		4,288,138	
Cost of Borrowings and Services	(3,883,533)		(2,241,608)	
Provision for Losses	(3,559)		(171,786)	
	3,001,287		1,874,744	
DISTRIBUTION OF VALUE ADDED				
To Employees				
Remuneration and Benefits	722,400	24	499,308	26
To Government				
Income Tax	1,081,403	36	437,327	18
To Providers of Capital				
Dividend to Shareholders	327,422	11	322,500	22
Retained in the Business				
Retained Profit	677,575	23	483,327	27
Depreciation	192,487	6	132,282	7
	870,062	29	615,609	34
	3,001,287	100	1,874,744	100

Distribution of Value Added

%



■ To Employees ■ To Providers of Capital
 ■ To Government ■ For Expansion and Growth

1. Stock Exchange

The Consolidated Income Statement for the year ended 31 December 2006 and the Balance Sheet of NDB Bank and the NDB Group as at that date have been submitted to the Colombo Stock Exchange within three months of the Balance Sheet date.

2. Registered Ordinary Shareholders as at 31 December 2006

			Resident			Non-Residents			Total	
No. of Shares	No.		Shares	%	No.	Shares	%	No.	Shares	%
Individuals										
0 -	500	4,645	862,552	1.05	40	8,349	0.01	4,685	870,901	1.06
501 -	1,000	976	713,534	0.87	11	8,037	0.01	987	721,571	0.88
1,001 -	5,000	993	2,018,239	2.47	17	40,275	0.05	1,010	2,058,514	2.51
5,001 -	10,000	109	752,048	0.92	7	47,042	0.06	116	799,090	0.98
10,001 -	20,000	50	673,288	0.82	1	11,571	0.01	51	684,859	0.84
20,001 -	30,000	10	239,795	0.29	–	–	–	10	239,795	0.29
30,001 -	40,000	4	138,499	0.17	1	30,802	0.04	5	169,301	0.21
40,001 -	50,000	5	210,162	0.26	–	–	–	5	210,162	0.26
50,001 -	100,000	5	330,948	0.40	1	73,000	0.08	6	403,948	0.49
100,001 -	1,000,000	1	125,287	0.15	–	–	–	1	125,287	0.15
1,000,001 & Over	–	–	–	–	3	7,854,250	9.59	3	7,854,250	9.59
SUB-TOTAL		6,798	6,064,352	7.40	81	8,073,326	9.85	6,879	14,137,678	17.27
Corporate										
0 -	500	166	28,509	0.03	2	726	–	168	29,235	0.04
501 -	1,000	49	37,679	0.05	2	1,579	–	51	39,258	0.05
1,001 -	5,000	87	211,798	0.25	1	3,000	–	88	214,798	0.26
5,001 -	10,000	16	120,485	0.15	1	5,052	0.01	17	125,537	0.15
10,001 -	20,000	25	346,937	0.42	–	–	–	25	346,937	0.42
20,001 -	30,000	6	156,903	0.19	3	82,000	0.10	9	238,903	0.29
30,001 -	40,000	5	166,994	0.20	1	32,303	0.04	6	199,297	0.24
40,001 -	50,000	2	88,200	0.11	1	47,800	0.06	3	136,000	0.17
50,001 -	100,000	6	404,350	0.49	1	98,200	0.12	7	502,550	0.61
100,001 -	1,000,000	4	1,020,600	1.24	10	4,461,560	5.45	14	5,482,160	6.70
1,000,001 & Over	–	4	17,547,757	21.43	4	15,590,825	19.04	8	33,138,582	40.48
SUB-TOTAL		370	20,130,212	24.56	26	20,323,045	24.82	396	40,453,257	49.42
TOTAL		7,168	26,194,564	31.96	107	28,396,371	34.67	7,275	54,590,935	66.69

Notes on unregistered/unallotted shares

Out of the total issued share capital of 81,855,385 shares, 27,264,450 shares representing 33.31% are either not registered or unallotted, the details of which are given below:

1. 7,854,250 Bonus shares which were issued in 2006, remain unallotted.
2. Four shareholders of 12,208,500 shares of the issued capital are not registered in the books of NDB Bank and as such are not members of NDB Bank.
3. 7,201,700 shares of the issued capital are pending registration.

3. Share Valuation

The market value of the National Development Bank Ltd. ordinary shares on 29 December 2006 was Rs 201.00 per share. The highest and lowest values recorded during this 12 month period were Rs 228.00 on 9 November 2006 and Rs 144.25 on 20 June 2006 respectively.

4. Directors' Interest in Shares of NDB Bank as at 31 December 2006

Name	No. of Shares	
	As at 31.12.2006	As at 31.12.2005
S K Wickremesinghe	450	300
H D S Amarasuriya	9,075	3,950
A R Gunasekara	883	589
G C B Wijeyesinghe	-	-
A A Pio (<i>resigned w.e.f. 15 October 2006</i>)	-	-
N S Welikala	-	-
S R de Silva	-	-
Lal de Mel	15,541	10,361
S T Nagendra	4,575	3,050
R B Thambiayah (<i>appointed w.e.f. 6 February 2006</i>)	-	N/A
R W A Vokes (<i>appointed w.e.f. 11 December 2006</i>)	-	N/A
U L Kadurugamuwa (<i>resigned w.e.f. 23 January 2006</i>)	-	N/A

5. Twenty Largest Shareholders as at 31 December 2006

Name	No. of Shares	%
Bank of Ceylon	8,185,538	10.00
Jaya Investments Ltd.	8,098,000	9.89
Seylan Bank Ltd./Asia Fort Asset Management (Pvt) Ltd.	5,131,300	6.27
Employees' Provident Fund	3,937,500	4.81
HSBC Intl Nominees Ltd.-BPSS LUX - Aberdeen Global Asia Pacific Fund	3,025,725	3.70
Sri Lanka Insurance Corporation Ltd. - General Fund	2,926,044	3.57
Citibank London S/A RBS AS DP FOR FS Asia Pacific	2,319,700	2.83
HSBC Intl Nominees Ltd.-BPSS - LDN - Aberdeen Asia Pacific Fund	2,147,400	2.62
NDB - ESOP	2,062,425	2.52
Waldock Mackenzie Ltd./Investor Access Equities (Pvt) Ltd.	2,026,700	2.48
Employees' Trust Fund Board	1,132,500	1.38
HSBC Intl Nominees Ltd./HSBC Bank PLC-CMG - First State Global Umbrella Fund	937,500	1.15
HSBC Intl Nominees Ltd.-SSBT - The Local Government Pensions Institution	713,550	0.87
HSBC Intl Nominees Ltd.-BPSS LDN - Aberdeen Investment Fund ICVC Aberdeen - Emerging Markets Fund	637,500	0.78
HSBC Intl Nominees Ltd./SSBT Lloyds TSB Group Pension TR (No. 1) Ltd.	481,200	0.59
HSBC Intl Nominees Ltd.-SSBTL - Aberdeen New Dawn Investment Trust	450,000	0.55
Waldock Mackenzie Ltd./Asia Fort Asset Management Private Ltd.	381,400	0.47
HSBC Intl Nominees Ltd.-SNFE - Aberdeen Pacific Equity Fund	356,100	0.44
HSBC Intl Nominees Ltd.-SSBTL - Aberdeen Asia Smaller Companies Investment Trust	325,000	0.40
Richard Pieris & Co. Ltd. Account No. 1	272,900	0.33
Total	45,547,982	55.65

Percentage of Shares held by the Public - 97.44%

NDB Group Income Statement

Rs mn	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006
Income										
Total Income	3,565.5	4,053.0	4,600.2	5,512.2	6,525.5	5,971.3	6,071.0	5,868.9	7,116.0	8,208.8
Interest Income	3,234.4	3,560.6	4,183.3	4,896.4	5,810.3	5,041.3	4,666.5	4,397.9	5,035.3	6,075.6
Interest Expenses	2,128.0	2,492.0	3,219.3	3,662.2	4,369.7	3,380.6	2,465.4	2,151.8	2,342.0	3,223.0
Net Interest Income	1,106.4	1,068.6	964.0	1,234.2	1,440.6	1,660.7	2,201.1	2,246.1	2,693.3	2,852.6
Other Income	331.1	492.4	417.0	615.8	715.2	930.0	1,404.5	1,471.0	2,080.7	2,133.2
Net Income	1,437.5	1,561.0	1,380.9	1,850.0	2,155.8	2,590.7	3,605.6	3,717.1	4,774.0	4,985.8
Less: Operating Expenses										
Personnel Costs	124.8	199.9	247.8	289.0	382.1	412.7	588.0	916.3	1,131.5	830.0
Provision for Bad & Doubtful Debts and Fall in Value of Investments	156.0	159.9	19.0	547.9	526.8	476.8	787.0	278.6	153.5	13.4
Other Administrative & General Expenses	116.6	187.1	243.0	300.1	534.4	520.9	817.6	1,266.9	1,473.3	929.5
Total Operating Expenses	397.4	546.9	509.8	1,137.1	1,443.3	1,410.5	2,192.5	2,461.8	2,758.3	1,772.9
Less: Exceptional Items	—	—	—	—	—	—	—	—	171.8	—
Operating Profit	1,040.1	1,014.1	871.1	712.9	712.4	1,180.2	1,413.1	1,255.4	1,843.9	3,212.9
Share of Associate Companies Profit	19.2	32.3	106.5	124.8	72.4	113.7	113.2	31.3	21.7	214.5
Profit Before Taxation	1,059.3	1,046.4	977.6	837.7	784.8	1,293.9	1,526.3	1,286.6	1,865.6	3,427.4
Taxation	(332.0)	(232.5)	(232.9)	(281.9)	(226.2)	(251.0)	(305.2)	(481.1)	(593.0)	(1,220.4)
Profit After Taxation	727.3	813.9	744.7	555.8	558.6	1,042.9	1,221.1	805.5	1,272.6	2,206.9
Minority Interest	(4.0)	(11.3)	(31.4)	(6.7)	40.1	(112.3)	(98.0)	(102.4)	(236.6)	(17.4)
Profit Attributable to Group	723.3	802.6	713.3	549.1	598.7	930.6	1,123.1	703.0	1,036.0	2,030.5
Earnings per Share *	8.8	9.8	8.7	6.7	7.3	11.4	13.7	8.6	12.7	24.8
Dividends (Rs mn) - Proposed/Paid	232.9	232.9	241.9	241.9	456.9	295.6	309.1	309.1	322.5	327.4
Dividends per Share - Proposed/Paid	6.5	6.5	4.5	4.5	8.5	5.5	5.8	5.8	6.0	4.0
Dividend Cover	3.1	3.4	2.9	2.3	1.3	3.1	3.6	2.3	3.2	6.2

* Adjusted for 2006 Bonus Issue.

NDB Group Balance Sheet

Rs mn	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006
ASSETS										
Cash & Short-Term Funds	4,304.5	1,379.4	745.6	1,305.8	3,037.7	5,937.7	12,440.7	14,101.5	2,098.8	4,467.2
Balances with Central Bank	—	—	—	—	—	—	—	—	818.7	1,575.3
Investments	2,889.4	3,940.7	4,154.1	4,093.3	5,016.0	3,828.6	5,726.0	5,633.6	19,078.0	12,170.2
Bills of Exchange	—	—	—	—	—	—	—	943.4	970.8	1,591.9
Loans & Advances	17,044.0	23,749.4	28,692.0	29,514.7	27,035.4	24,364.4	20,783.2	31,833.4	35,274.5	39,377.2
Lease Rentals & Receivables	804.1	1,050.6	1,711.3	4,253.4	3,504.3	2,884.7	573.3	609.4	731.3	1,449.1
Investments in Associate Companies	821.8	677.3	977.3	410.2	454.0	798.6	413.1	225.1	241.2	1,179.0
Property & Equipment	143.2	207.3	315.0	1,646.1	1,747.1	1,667.8	1,166.5	1,658.0	1,162.0	691.5
Investment Property	—	—	—	—	—	—	—	—	1,040.9	1,200.0
Other Assets	577.6	782.3	982.8	965.6	1,815.7	889.0	1,865.4	2,445.6	3,006.3	1,276.2
Intangible Assets	(3.6)	36.4	27.9	(53.4)	(43.6)	2.9	904.9	1,535.1	872.7	—
Total Assets	26,581.0	31,823.4	37,606.0	42,135.8	42,566.5	40,373.7	43,873.1	58,985.0	65,295.2	64,977.5
LIABILITIES										
Borrowings	19,694.0	24,616.9	29,813.3	33,129.7	32,506.0	30,250.4	25,847.6	26,881.2	27,798.9	29,203.5
Deposits with Customers	—	—	—	—	—	—	—	11,085.1	13,953.7	21,161.1
Non-Life Insurance Reserves	—	—	—	—	—	—	420.8	485.8	858.8	—
Long-Term Insurance Fund	—	—	—	—	—	—	6,612.8	7,985.4	9,238.2	—
Taxation	456.8	336.6	333.7	480.2	401.0	550.1	350.8	300.1	220.4	640.4
Other Liabilities	1,439.4	1,171.9	1,258.1	1,807.1	2,259.6	1,397.2	1,997.5	2,770.1	2,847.0	1,983.7
Dividend Payable	236.1	234.2	243.5	244.1	245.8	300.2	4.6	7.5	8.0	107.9
Total Liabilities	21,826.3	26,359.6	31,648.6	35,661.1	35,412.4	32,498.0	35,234.1	49,515.2	54,924.9	53,096.6
SHAREHOLDERS' FUNDS										
Share Capital	358.3	358.3	358.3	537.5	537.5	537.5	537.5	537.5	545.7	818.6
Share Premium	91.7	91.7	91.7	91.7	91.7	91.7	91.7	91.7	214.4	214.4
Statutory Reserves	—	358.3	358.3	537.5	537.5	537.5	537.5	546.5	545.7	818.6
Revaluation Reserve	—	—	—	—	131.7	131.7	—	86.2	—	—
Revenue Reserves	4,141.2	4,352.5	4,824.0	4,654.3	4,839.7	5,524.8	6,730.5	7,114.7	7,849.7	8,715.2
Total Shareholders' Funds	4,591.2	5,160.8	5,632.3	5,821.0	6,138.1	6,823.2	7,897.1	8,376.5	9,155.4	10,566.6
Minority Interest	163.5	303.0	325.1	653.7	1,016.0	1,052.6	741.9	1,093.2	1,214.9	1,314.2
Total Funds Employed	4,754.7	5,463.8	5,957.4	6,474.7	7,154.0	7,875.8	8,639.0	9,469.8	10,370.3	11,880.9
Total Liabilities & Funds Employed	26,581.0	31,823.4	37,606.0	42,135.8	42,566.5	40,373.7	43,873.1	58,985.0	65,295.2	64,977.5
Return on Average Assets (%)	3.1	2.8	2.2	1.4	1.3	2.5	3.2	1.6	2.0	3.1
Return on Equity (%)	16.6	16.5	13.3	9.7	10.0	14.4	15.3	8.6	14.3	21.0
Return on Equity (%) (Excluding exceptional items)	16.6	16.5	13.3	9.7	10.0	14.4	15.3	8.6	14.3	10.5
Book Value per Share (Rs.)	85.42	96.02	103.34	108.30	114.20	126.94	146.92	155.84	159.60	129.09
Book Value per Share (Rs.) (Excluding exceptional items)	85.42	96.02	103.34	108.30	114.20	126.94	146.92	155.84	159.60	116.68

Notice of Meeting

Notice is hereby given that the Second (2nd) Annual General Meeting of the National Development Bank Limited (NDB Bank) will be held at Oak Room, Cinnamon Grand Hotel (formally 'Colombo Plaza Hotel'), Colombo, at 11.00 a.m. on the Twenty Sixth (26th) day of April, Two Thousand and Seven (2007) and the business to be brought before the meeting will be:

1. To lay before the members to be received and adopted by them the Report of the Directors of NDB Bank, the Balance Sheet, the Income Statement and the Auditors' Report relating to the year ended 31 December 2006.
2. To re-elect Directors in terms of Section 87 and 94 of the Memorandum and Articles of Association of NDB Bank:
Mr H D S Amarasuriya
Mr A R Gunasekara
Mr S T Nagendra
Mr R W A Vokes
3. To declare a Dividend as recommended by the Directors.
4. To reappoint Messrs Ernst & Young, Chartered Accountants, as Auditors of NDB Bank and authorize the Board of Directors to determine their remuneration.
5. To determine the remuneration payable to the Directors.
6. To approve under the Companies Donations Act No. 26 of 1951 the donations made by NDB Bank for the financial year 2006.
7. To authorize the Board of Directors to determine donations for the financial year 2007 under the Companies Donations Act No. 26 of 1951.

By Order of the Board

Mrs C L Jayawardena

Board Secretary

19 March 2007

Notes:

1. *A member entitled to attend and vote at the meeting is entitled to appoint a proxy to attend and vote in his/her/its stead.*
2. *A proxy need not be a member of NDB Bank. The Form of Proxy is sent herewith.*
3. *The instruments appointing proxies must be deposited at the Head Office of NDB Bank, at No. 40, Navam Mawatha, Colombo 2 not later than 48 hours prior to the time appointed for the holding of the meeting in accordance with Article 71 of the Memorandum and Articles of Association of National Development Bank Limited.*
4. *Members/proxies attending the meeting are requested to bring their National Identity Cards.*

NATIONAL DEVELOPMENT BANK LIMITED

I/We.....

(NIC/s of

..... being a member/members of

National Development Bank Ltd. (the 'NDB Bank') hereby appoint

1.

Holder of NIC No.

or failing him/her

2. Mr. S K Wickremesinghe (Chairman of NDB Bank) of Colombo or failing him one of the Directors of NDB Bank, as my/our proxy

to represent me/us and to vote for me/us and on my/our behalf at the Second Annual General Meeting of NDB Bank to be held

on 2007 and at any adjournment thereof and at every poll which may be taken in consequence thereof.

As witness I/We have set my/our hand/s hereunto this day of Two Thousand and Seven (2007).

.....
Signature of the Member/Members

.....
Common Seal
(If applicable)

Instructions for Completion of the Form of Proxy

1. In order to appoint a proxy, this form duly completed together with any Power of Attorney under which it is signed, must be deposited at the Registered Office of the NDB Bank, at No. 40, Navam Mawatha, Colombo 2, not later than forty-eight (48) hours prior to the time appointed for the holding of the meeting.
2. The proxy appointed need not to be a shareholder of NDB Bank.
3. In the case of a corporate member, the proxy must be executed under its common seal or by its authorized attorney.
4. The first joint holder shall have the power to sign the proxy without the concurrence of the other joint holder/s.
5. The full name and the registered address of the member appointing the proxy should be legibly entered in the Form of Proxy.

Corporate Information

Name

National Development Bank Ltd.
(NDB Bank, formerly National Development Bank of Sri Lanka)

Legal Form

Incorporated in Sri Lanka under the Companies Act No. 17 of 1982 and also regulated under the Banking Act No. 33 of 1988 as amended from time to time.

Statutory Status

The National Development Bank of Sri Lanka (NDB) was originally set up as a wholly state-owned institution by an Act of Parliament in January 1979. Following a change of ownership structure in 1993, 61% of the share capital of NDB was transferred to private ownership. In 1997, NDB was privatized further by the early conversion of its convertible debentures and the disposal of the resulting shares. This reduced the Government's direct shareholding to 12.2%. Thereafter, a further 2.56% was allocated for the Employee Share Option Scheme. In April 2000, NDB issued a further 17,916,667 shares in the ratio of 1:2 as Bonus Shares thereby increasing its total issued share capital to 53,750,000 shares.

In 2005, pursuant to the provisions of the National Development Bank of Sri Lanka (Consequential Provisions) Act No. 1 of 2005 a company by the name 'National Development Bank Ltd.' (NDB Bank) was incorporated for the purposes of taking over the business of NDB Accordingly, on the 15th of June 2005, the NDB Bank was incorporated and with effect from that date the National Development Bank of Sri Lanka Act No. 2 of 1979 was repealed save and except for certain provisions contained therein.

On the 1st of August 2005 the Central Bank of Sri Lanka granted a commercial banking licence to the new company whilst withdrawing the specialized banking licence that was held by it and on the same day the

business operations of NDB Bank Ltd. (NBL) was taken over by NDB Bank. In view of this the shareholders of NBL were issued with shares of NDB Bank at the ratio of 1 NDB Bank share for every 5.6 shares of NBL held by them. This resulted in the increase of the issued capital of NDB Bank to 54,570,257 shares. In 2006, NDB Bank approved a bonus share issue at the ratio of 1 new share for every 2 shares held by the shareholders and accordingly the capital of NDB Bank was further increased by another 27,285,128 shares. The present issued share capital of NDB Bank is Rs 818,553,850/- consisting of 81,855,385 ordinary shares of Rs 10/- each. The shares of NDB Bank are continued to be quoted on the Colombo Stock Exchange.

Head Office/Registered Office

40, Navam Mawatha, Colombo 2
Tel: 2437701, 2437350, 2323966
Fax: 2341044, 2440262
Telex: 21399 NDB CE

Board of Directors

S K Wickremesinghe (Chairman)
N S Welikala (Chief Executive)
H D S Amarasuriya
S R de Silva
L de Mel
G C B Wijeyesinghe
A R Gunasekara
S T Nagendra
R B Thambiayah (appointed w.e.f. 6 February 2006)
A A Pio (resigned w.e.f. 15 October 2006)
U L Kadurugamuwa (resigned w.e.f. 23 January 2006)
R W A Vokes (appointed w.e.f. 11 December 2006)

Audit Committee

G C B Wijeyesinghe (Chairman)
L de Mel
A R Gunasekara
R B Thambiayah

Human Resources Committee

H D S Amarasuriya (Chairman)
S R de Silva
A R Gunasekara
A A Pio (resigned w.e.f. 15 October 2006)
S T Nagendra

Nomination Committee

S K Wickremesinghe (Chairman)
H D S Amarasuriya
G C B Wijeyesinghe
L de Mel
S R de Silva

Credit Committee

L de Mel (Chairman)
S R de Silva
R B Thambiayah
S T Nagendra

Strategic Issues Committee

S K Wickremesinghe (Chairman)
G C B Wijeyesinghe
A R Gunasekara
H D S Amarasuriya
A A Pio (resigned w.e.f. 15 October 2006)

Subsidiary Companies as at 31.12.2006

Capital Development & Investment Co. Ltd.
Development Holdings (Pvt) Ltd.
NDB Industrial Estates (Pvt) Ltd.
NDBS Stock Brokers (Pvt) Ltd.
NDB Venture Investments (Pvt) Ltd.
NDB Investment Bank Ltd.
Aviva NDB Finance Lanka (Pvt) Ltd. (up to 31 January 2006)

Associate Companies as at 31.12.2006

Ayojana Fund (Pvt) Ltd.
Maldives Finance Leasing Co. (Pvt) Ltd.
Aviva NDB Finance Lanka (Pvt) Ltd. (from 1 February 2006)

Stock Exchange Listing

The shares of NDB Bank are listed with the Colombo Stock Exchange

Company Secretary

C L Jayawardena
Attorney-at-Law

Audit ors

Ernst & Young
201, De Saram Place
Colombo 10

Principal Correspondent Banks

ABN Amro Bank
Citibank
Deutsche Bank Trust Company
HSBC Bank
HypoVereinsbank Group
Standard Chartered Bank

Senior Management

Director/Chief Executive
N S Welikala

Deputy Chief Executive

E Wickramaratne

Vice President - SME & Corporate Business Development

R Bibile

Vice President - Risk Management, Credit Administration & Special Projects

N I R de Mel

Vice President - Information Technology

S Dissanayake

Vice President - Group Audit & Compliance

S N Jayasinghe

Vice President - Legal and Company Secretary

C L Jayawardena

Vice President - Treasury

N Ratnayake

Vice President - Operations

K Weerasuriya

Vice President - Consumer Banking & Marketing

I A Wickramasinghe

Vice President - Corporate Banking

A Wickramaratne



www.ndbbank.com