NATIONAL DEVELOPMENT BANK PLC

ANNUAL REPORT 2012

A step change in strategy leads to a quantum leap in fortunes

BIG
BETTER
BOLD

NDB Group is creating a new path to the future…Bigger, Better and Bolder than ever before.

Breaking new ground as a forerunner in the Sri Lankan financial services, the NDB Group has proved itself to be a very high quality service provider with a wide array of product offerings backed by a diversified talent pool and a unique knowledge hub: poised for national development. The Group understands the diverse needs of its clientele and is committed to continuously provide advice and tailor-made solutions through warm and friendly customer service. NDB Group, fortified with a strong capital base is empowered for bold yet responsible and accountable financial services to its customers.

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.

Our Values

Integrity, Care, Passion, Teamwork and Service guide us in our vision to be a world-class Sri Lankan Bank.

"AA (lka) Fitch Rating"

Registered Name: National Development Bank PLC
Trade Name: NDB bank
Company Registration No: PQ 27

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Financial Highlights

	BANK			GROUP		
	2012	2011	% Change	**2012**	2011	% Change
(Rs mn)						
Total income	**20,125**	13,534	49	**26,192**	14,667	79
Net interest income	**5,674**	4,562	24	**5,896**	4,909	20
Net operating income	**8,709**	6,640	31	**14,887**	8,010	86
Profit before Financial Services VAT	**4,607**	3,110	48	**10,391**	4,030	158
Profit after tax	**2,924**	1,831	60	**8,932**	2,763	223
Profit attributable to equity shareholders	**2,924**	1,831	60	**8,854**	2,527	250
Shareholders' funds	**14,942**	12,675	18	**24,883**	16,925	47
Deposits from customers	**107,601**	82,094	31	**107,394**	82,094	31
Borrowings	**34,933**	39,178	(11)	**34,893**	37,951	(8)
Total assets	**163,474**	138,423	18	**174,103**	142,588	22
Gross loans and advances	**123,424**	104,155	17	**123,471**	104,226	17
Non-performing loans	**1,558**	1,364	14	**1,558**	1,364	14
Dividends - Interim	**821**	575	43	**821**	575	43
Dividends - Final	**–**	658	(100)	**–**	658	(100)
(%)						
Return on average equity	**21.17**	15.01	41	**42.35**	15.69	170
Return on average assets	**1.94**	1.50	29	**5.59**	2.01	178
Non-performing loans ratio	**1.31**	1.35	(3)	**1.31**	1.33	(2)
Cost to income ratio	**46.54**	52.62	(12)	**30.10**	50.25	(40)
Effective overall tax rate	**36.53**	41.13	(11)	**18.26**	39.64	(54)
Capital adequacy - Tier I (minimum ratio of 5%)	**11.16**	9.98	12	**18.76**	14.24	32
Tier I & II (minimum ratio of 10%)	**12.41**	11.26	10	**20.71**	15.83	31
Liquidity ratio - DBU (minimum ratio of 20%)	**22.02**	22.54	(2)	**22.02**	22.54	(2)
FCBU (minimum ratio of 20%)	**24.92**	28.49	(13)	**24.92**	28.49	(13)
(Rs)						
Earnings per share (basic)	**17.81**	11.15	60	**55.31**	15.79	250
Earnings per share (diluted)	**17.80**	11.15	60	**55.29**	15.78	250
Dividends per share - Interim	**5.00**	3.50	43	**5.00**	3.50	43
Dividends per share - Final	**–**	4.00	(100)	**–**	4.00	(100)
Book value per share	**91.00**	77.19	18	**151.54**	103.08	47
Market value per share (31 December)	**137.90**	138.10	(0)	**137.90**	138.10	(0)
(Times)						
Debt/equity	**9.54**	9.81	(3)	**5.87**	7.29	(19)
Total leverage	**10.94**	10.92	0	**7.00**	8.42	(17)
Interest cover	**1.50**	1.67	(10)	**1.52**	1.73	(12)

Operational Highlights

- Group's share of profits attributable to shareholders increased significantly by 250% to Rs 8.8 bn

  (page 226)

- Group's capital base improved remarkably to reach Rs 27.9 bn as at end of 2012

  (page 322)

- Completed the sale of shareholding in AVIVA NDB Holdings to insurance giant AIA, entered into a long term Bancassurance relationship with AIA and acquired 100% of the largest Wealth Management company in Sri Lanka

  (page 40)

- Customer deposits base of the Bank reached Rs. 107.6 bn, recording a growth rate of 31%

  (page 228)

- NPL ratio continued to improve, reaching 1.31% as at end of 2012, compared to 1.35% a year ago

  (page 84)

- Group ROE improved to 42.35% in comparison to 15.69% in 2011

  (page 4)

- The branch network expanded to 69 by the end of 2012

  (page 264)

- Recorded a landmark in the history of the country's debt market with NDB Capital Holdings launch of a family of fixed income indices for the Sri Lankan market, to measure the performance of government securities of selected maturities

  (page 41)

- Became the first Investment Bank in the country to be named the "Best Investment Bank in Sri Lanka" by the prestigious Euromoney magazine

  (page 87)

- Was acclaimed as one of the "Top Ten Best Corporate Citizens of Sri Lanka" and won two awards at the Best Corporate Citizens Awards 2012

  (page 89)

- Was named the 'Best Commercial Bank in Sri Lanka' by World Finance, UK

  (page 88)

- Received an award for the organization with the most innovative HR practices at the 'HR Leadership Awards' held in Dubai

  (page 89)

- Introduced many innovative propositions, including Hire Purchase facilities without the need for guarantors and down payments, NDB Real Saver, pre-approved loans, six year leases and 365-day leasing desk.

  (pages 49 to 51)

Positioned to grow and prosper
in a truly sustainable manner

2012 was a groundbreaking year for NDB achieving most of its strategic aspirations. Our financial results are outstanding and NDB is on a stronger footing to seize the abundant opportunities at hand and to grow and prosper in a truly sustainable manner.

Chairman's Letter

Dear Shareholders,

2012 was a groundbreaking year in which the Bank achieved most of its strategic aspirations and also laid the foundation for continuous above industry growth rates vis-a-vis a 5 year strategic plan leading onto 2017. When organizations sing praise we must recognize the substantial contributions made by our customers and employees from managerial to grass root.

Customers are our 'profit centres'. In response, our aspiration is to uplift the service standards of our branches towards a nation-wide premier service. Indicators that our customer base has widened through new customers and migrations bear testimony that we are now on the 'way'. With this intent we hope to create a revelation through endorsements at the periphery of the market, where lies the latent potential for new capital formation.

Under the able guidance of our Chief Executive Officer, we have succeeded in synergising our top management from diverse functional areas into one. As an universal bank like no other, cross selling opportunities abound to be captured within our walls through synergy. Intra-Departmental connectivity has begun to reawaken and enliven this process.

Then at the grass root level, our youthful officers, both men and women, are equally motivated to work energetically and passionately and go beyond their call of duty, marking a clear differentiation across the heartland of the nation at branches and distant markets.

These human assets are not visible under the microscope of a Balance Sheet, nevertheless will configure into producing seamlessly outstanding results over the life time of the strategic plan. 'The wheels have begun to turn'.

Financial Results, Major Divestments and their Unfolding

Our financial results are outstanding. Most budgeted numbers realised, every key ratio improved upon even after eliminating substantial gains emerging from the divestment of AVIVA NDB Insurance.

While not wishing to dwell on the financials as they appear elsewhere in this report in analytical format, I need to touch base on selected headlines to catch your attention.

- Significant capital gains from the divestment of AVIVA NDB Insurance has strengthened our capital base and the Bank will now be able to approach the upcoming Basel III requirements in comfort.
- Simultaneously while divesting from NDB AVIVA Insurance Company, we were able to sign a 20 year agreement for bank assurance with the new owners AIA enabling our core bancassurance business to remain undisturbed despite the disposal of the investment.

Chairman's Letter

- Furthermore we purchased the AVIVA share of NDB AVIVA Wealth Management which now becomes a 100% subsidiary of NDB Capital Holdings PLC (99.5% owned by NDB) while signing a similar agreement which enables us to manage the insurance funds of the new owners, AIA. These transactions will further strengthen the investment banking arm of the Group which is poised to deliver a substantial component of the Group's bottom line growth during the tenure of the 5 year plan.
- Our management team analyses environmental trends, risks and key ratios on a weekly basis. This enables your Bank to continuously strengthen the Balance Sheet while successfully managing selected key ratios in the Financial Statements such as Net Interest Income margins now at 3.75% and Non-Performing Loans ratio (NPL) now at 1.3% by proactively anticipating the vagaries of the environment. Both ratios are on the upside of market trends amidst a slowing economy causing consternation to the financial sector.

The Economy

The most relevant event was the completion of Sri Lanka's Stand-By Arrangement (SBA) facility with the International Monetary Fund (IMF) which was successfully completed with the release of the 9th tranche in July 2012. The SBA which was signed off in July 2009 marked the longest engagement Sri Lanka had with the IMF and the outlay of approximately US$ 2,548 mn was the single largest facility Sri Lanka ever obtained from a multilateral institution in its recorded history. What the SBA programme achieved was to rebuild external reserves, strengthen the fiscal position, maintain monetary stability and fortify the domestic financial system during a turbulent post-war period when the economy averaged a growth of 8% per annum and tended towards overheating. This was also an endorsement for future stability of the economy, eliminating any aberrations that prevailed hitherto.

Challenges 2012

Among the challenges faced by the Bank was an imposition of credit limits to 18% of the outstandings of the previous year's debt book, placed on the entire financial sector by the Central Bank with a view to reigning in the growing trade deficit caused by accelerated import growth. Despite our Non-Performing loans ratio (NPL) being lowest in the industry at 1.3% this controls mechanism which was in the best interest of stabilising the economy, compelled us to lend selectively and quell demand patterns from a debt hungry market.

The Bank also faced challenges attributable to a widely fluctuating exchange risk vis-à-vis the dollar and other traded currencies. Leading from its substantial US Dollar trading and trade finance operations, the Bank remains exposed to exchange rate risk on assets and liabilities denominated in foreign currencies if the rupee was to fluctuate.

The debt ceiling has now been removed and is unlikely to be imposed this year. Currency remains vulnerable due to our overdependence on exports to USA and the European Community where recovery is expected to be slower than for the rest of the world. The stability of the currency will depend on to what extent the 'Invisible exports' can compensate for the trade deficit of around US$ 9 bn estimated for 2013.

Strategic Direction

As the demographics unfold, increasing urbanization and growing prosperity of the hinterland is now a recognizable reality. Perhaps the increase in inward remittances of expatriate workers having surpassed US$ 6 bn per annum paves the way for a greater distribution of wealth across the nation while preventing migration of the rural masses towards the metropolis, a malaise that torments neighbouring Asian countries. The Central Bank's policy directive to open two branches in the outer provinces to every one in the prosperous Western Province has also been instrumental in taking banking infrastructure towards the periphery.

- In this background we have identified the need to rapidly open branches in economically viable centres and access emerging capital formation with a view to increasing our customer base. While we are at 70 branches today, unfolding of the strategic plan envisages an increase to 120 by 2017 with 'windows' and service centres providing basic support services.
- Following growing prosperity of the rural and suburban sectors is the increasing potential of the small and medium enterprise (SME), particularly in the newly identified economic areas. Our Bank began its life in the development realm. We are well-versed in attuning our initiatives towards SMEs. Each of our 70 branches are now equipped with a SME desk while we have opened regional SME service centres in key towns to further develop the SME sector.
- At the base of the pyramid we disburse micro loans to cottage industries and inculcate savings habits among recipients after each new branch opening, catalysing a link between the bank and village. Uplifting of the rural masses pave the way for diversifying the Bank's customer base and expanding market scope and is a successful new initiative with limited risk accompanied by high loyalty.

Chairman's Letter

- Leasing and pawning are growing sectors for the banking community and pursued eagerly by us. Leasing is the fastest method of owning a commercial vehicle while pawning though frowned upon in certain quarters, is the only collateral for a bridging loan for a vast majority of the populace who would otherwise fall into the prey of the unscrupulous money lender. Strong competition is emerging from the leasing and finance company sectors which is overextending towards a likely fallout if not checked. While trading on common grounds with similar products, the banking sector needs to differentiate from these uncertainties by clear positioning of corporate and brand imagery to avoid been pulled into the 'vortex' following a market set back.
- On the investment banking axis new capital derived from the AVIVA NDB Insurance sale will be put to use shortly. Among the possibilities for new business is expanding our portfolio to venture capital, private equity investment and related areas of capital structuring. Private equity is virgin territory in our market today and NDB Investment Bank who has pioneered many new initiatives is ideally placed to enter this lucrative business as the 'first on line'.
- Our strategic alliance with DBS Bank Singapore in 2011 is already bearing fruit with support for major IPOs, debt structuring and loan syndication and gives us space to expand our consumer base across borders to expose our portfolio of products into the outer world. Similar alliances are being sought after in other Asian territories where investment banking has matured to fulfilment in markets which are showing interest in Sri Lanka's growing prosperity and emerging potential.
- To drive all these initiatives forward, the Bank has successfully integrated three different stand-alone IT systems into a single all encompassing systems engine for speedy and accurate decimation of information. The perseverance and dedication of our IT team to speed up the implementation by several months from the initial deadline is greatly appreciated by all. We will rely on them to be in the forefront of these new vistas through 'Information engineering'.

Shareholders and Investors

Monitoring of capital adequacy ratios at tier one capital dissuades the banking sector from payment of interim dividends. Since 2010, we have been able to declare interim dividends based on the strength of our cash flows and balance sheet and this will be an ongoing policy favouring our shareholders.

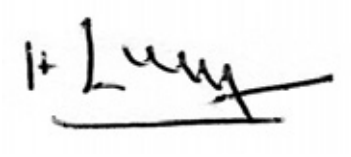
To strengthen our connectivity with shareholders and the financial sector we have introduced an investor forum this year where we will be meeting key shareholders, stockbrokers and financial analyst biannually. The first of such events was concluded successfully in February 2013 giving an insight into the strategic directions proposed by the Bank as it enters an exciting period in its history.

Acknowledgement

On behalf of the Board of Directors, I thank our valued shareholders for the trust and confidence placed in us, the CEO, management and staff for so passionately implementing the stated goals of the organization and delivering marvellous results. Our Board members are derived from diverse functional areas and bring their varied experiences to the table and I wish to thank them for the significant contributions they have made in positioning the Bank to be a dynamic organization in the making.

I wish NDB continued success in all its future endeavours.

Sincerely



Hemaka Amarasuriya
Chairman

13 February 2013

Geared to offer bigger, better and bolder solutions

As Sri Lanka continues to grow as a formidable force in the new Asian economy, NDB remains committed to deliver on its promises to all partners of its success; enhanced, enlightened and empowered to offer bigger, better and bolder solutions to our diverse clientele.

Chief Executive Officer's Review

Expanding Our Horizons on a Solid Foundation

As major global economies gather momentum towards recovery, the post-conflict landscape has opened new vistas of growth and opportunity for Sri Lanka as an emerging Asian economy.

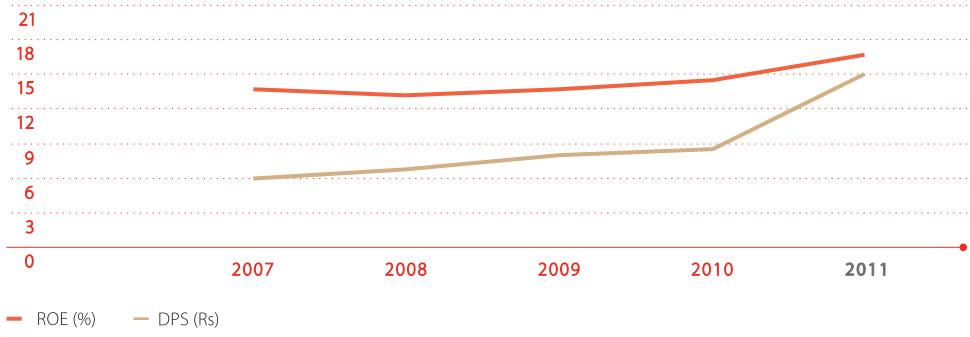
Today, we stand confident as a nation eager to make our own footprint in the new Asia. It is with much optimism that I boldly envision an era of ambitious and unprecedented growth and economic prospects for Sri Lanka in the years ahead. I am justifiably proud that, NDB Group's operating results in 2012 records the best in its history. The year was characterized by significant achievements across each of our diversified operating groups which is truly embedded in the profit attributable to our valued shareholders, which reached Rs 8.8 bn; a growth of 250%, the highest ever. It is remarkable to note that, the Team NDB reached such unprecedented heights in performance whilst maintaining financial strength and flexibility, managing risk prudentially, and investing for the future growth. The clarity of our business strategy individually as a bank and jointly as an unparalleled financial conglomerate could be attributed as the prime ingredient of our continued success story.

Our strength in terms of capital, liquidity and funding has fortified our stability as an indomitable player in the Sri Lankan financial arena. At a group level, our Core Tier I Capital Adequacy Ratio stands at 18.8% complemented by a strong liquidity pool, shielding us from volatile macroeconomic conditions.

While it is customary to use many metrics to manage and measure the business, return on equity is considered as the most significant financial measure that correlates most closely with shareholder value in the context of NDB. Our ambition to achieve a 20% return enabled us to make meticulous and disciplined choices over the year under review resulting in a ROE of 21.2% to our valued shareholders.

Our solid foundation, cemented by our strong capital base has undoubtedly expanded our horizons. We strongly believe in our ability to achieve higher returns through aggressive performance, intensified cost reduction drives and disciplined approach to capital and funding costs.

EFFECTIVE RETURNS TO SHAREHOLDERS
(Rs/%)



Chief Executive Officer's Review

Creating Sustainable Value to Our Society

Responsible corporate citizenship is deeply entrenched with the vision, mission and values of NDB. We have long recognized that banks need to become better citizens and that our ability to do this is critical to generate long-term value for all stakeholders and the society in general. This is not philanthropy - it is our ethos; we firmly believe in harnessing the unique skills and resources of our diversified group to deliver real commercial benefits which create sustainable value for our society. Our focus on nurturing and sustaining an entrepreneurial spirit across all segments of Sri Lankan society has paid rich dividends. We have made firm progress on our Citizenship agenda in 2012 propagating the cause of financial inclusion and empowerment spanning across all segments of the Sri Lankan society. During the year under review, we disbursed Rs 8 bn new loans to SME's in Sri Lanka whilst creating linkages between the producer and the distributor. Besides promoting and nurturing SMEs that form the backbone of any growing economy, we aggressively expanded into infrastructure and project financing activities, as we consciously contributed towards capital formation within the country - a vital ingredient in promoting investments. The Team NDB made all this possible, including a commitment to create over 1,000 apprenticeships; which indeed is a remarkable feat by any standard. Our commitment to this endeavour was accorded many accolades on the national platform where we were ranked amongst the top ten corporate citizens in the country .

Positioning NDB as a Distinctive Brand

Our 2012 results confirm that we are well-positioned to evolve as a distinctive brand. The confidence is attributable to our strong Balance Sheet, clear strategy, prudential risk management practices and above all a deep understanding of the pulse of our nation which stems from its roots as a development finance institution.

As we reach significant milestones of our journey, our aspirations remain both ambitious and optimistic. Our vision is entrenched with the importance of maintaining strong core capabilities while investing in the quality and knowledge of our key resource: the Team NDB. In keeping with the spirit of customer service excellence, we are constantly focused on sharpening our processes and technology to provide our diverse clientele a unique blend of services to meet their evolving needs.

Our confidence to perform rests on the professionalism, commitment and the passion of our team. Every member of the Team NDB - from senior management to investment professionals to front-line bankers - is well-poised and committed to deliver on our ambition. Our investment in the skills to sustain the anticipated long-term growth and more particularly to attract, nurture and retain the best talent in the market would continue as a priority.

Keeping Pace with Accelerated Growth

Our ambitious journey rests on five strategic imperatives in the medium term which focuses on fortifying and strengthening the Bank to keep pace with the projected accelerated growth:

- Optimize Balance Sheet and capital allocation.
- Drive profitability.
- Enhance core competencies and strengthen platforms.
- Undertake measured investments in growth areas.
- Create value through group synergies.

Optimizing the Balance Sheet continues as a top priority for NDB. During 2012, many initiatives were undertaken to improve the funding position through well-positioned and accelerated deposit drives. It is anticipated that the loans to deposits ratio would be further improved in 2013 through our continuous focus and efforts in that direction. The aforesaid initiatives would be further cemented through diversification of its funding channels and emphasis on reducing the cost of funds.

Nurturing and Promoting Entrepreneurial Spirit

The SME segment will continue as a key priority sector in 2013 in line with the national economic strategy. Promoting entrepreneurship at grass root level and financial inclusion for all Sri Lankans through empowerment and sustainability will be rated high in our agenda which would be propagated through our initiatives to drive productivity, innovation and capability upgrading; to tap opportunities for growth and to create a conducive business environment for SMEs. In this regard, we are greatly encouraged by the commitment extended by the Government in its 2013 Budget to raise over 10 year tenure long-term foreign development finance up to US$ 250 mn to provide long-term funding for SMEs, plantations, construction and other manufacturing industries and the assurance of the government to underwrite the exchange risk of such borrowing as an incentive to promote such much desired capital formation. Such incentives, supplemented by the proposed tax incentives would enable the domestic entrepreneurs to access long term funds at concessionary rates to meet their funding requirements. The retail bank will focus on geographic expansion and further penetration to new markets with the optimal channel, service and product mix besides making access to finance more convenient. Financing of infrastructure projects in newly opened up North and East Provinces of the country will undoubtedly rank as a priority in the near future.

Chief Executive Officer's Review

Driving Profitability Across all Segments

NDB intends to drive profitability across business segments while recognizing and appreciating the cross selling and fee-based income opportunities within the Group. The Bank will focus on enhancing the customer service proposition, while reducing cost base by optimizing its infrastructure. Under the Corporate Banking segment, developing comprehensive client solutions leveraging the expertise across the Group in Treasury and Markets, Wealth Management and Investment Banking would enable us to penetrate new territories and market segments.

The envisaged expansion of geographical reach and increasing business volumes would necessitate enhanced support functions and strengthening of client service platforms. In this respect, streamlining of processes and empowerment of staff at ground level while adhering to prudential risk management and mitigation practices would be continued.

During the year under review, NDB raised its capital position through a strategic divestment of a 49% stake of AVIVA to earn a gain of Rs 6 bn. Seizing similar avenues of opportunity that are likely to be opened up with the resurgence of the economy, the Bank will continue to actively evaluate investment opportunities on its own accord or through subsidiaries and associate companies of the Group. Given the strong capital position of the Bank, NDB will seek meaningful investments in both organic and inorganic growth, regionally besides strategic alliances in selective regions.

Surpassing the Boundaries of Conventional Banking

The highly competitive market reflecting the sophistication of the needs of our customers has necessitated innovative, customized solutions that cater to the diverse range of personal and corporate needs. In this regard, the synergy between the Bank and Group constituents would continue to add value and strengthen the NDB's service proposition to surpass the norm of conventional banking services creating new dimensions in the Sri Lankan Banking Industry.

Stakeholders of Our Growth

I take this opportunity to thank the Chairman and the Board of Directors for their valuable contribution and direction throughout the year under review and convey my gratitude and appreciation to the Team NDB of the Bank and the Group for their unstinted support, dedication and commitment. Over the years Team NDB has managed to sharpen their competitive edge, overcome challenges and exploit opportunities successfully which indeed is commendable.

I am also much obliged to the customers for their trust and confidence placed on the Bank and the shareholders for their co-operation. I also extend my gratitude to the regulators for their expert advice and guidance throughout the year under review. I warmly look forward for the same patronage to pursue growth in the ensuing year.

Committed to Deliver on Our Promises

In line with the national objectives, to transform Sri Lanka as an upper middle income country by reaching a Per Capita income of US$ 4,000 and US$ 100 bn GDP by 2016, we are confident that we have the right strategy; supported by a performance driven culture, an innovative range of products as well as people with the right attitude to deliver consistent and sustainable value to our customers and other stakeholders who have partnered in our growth.

As Sri Lanka continues to grow as a formidable force in the new Asian economy, NDB remains committed to deliver on its promises to all partners of its success; enhanced, enlightened and empowered to offer bigger, better and bolder solutions to our diverse clientele.

Russell De Mel
Chief Executive Officer

13 February 2013

Management Discussion and Analysis

Big

Breaking new ground as a forerunner in the Sri Lankan financial services industry with an unparalleled product and service offering, diversified talent pool and knowledge hub; poised for national development.

☑

Better

Understanding the diverse needs of a varied clientele; committed to provide tailor made solutions through superior customer service.

☑

Bold

Venturing into new territories fortified with a strong capital base; empowered for bold yet responsible and accountable banking.

☑

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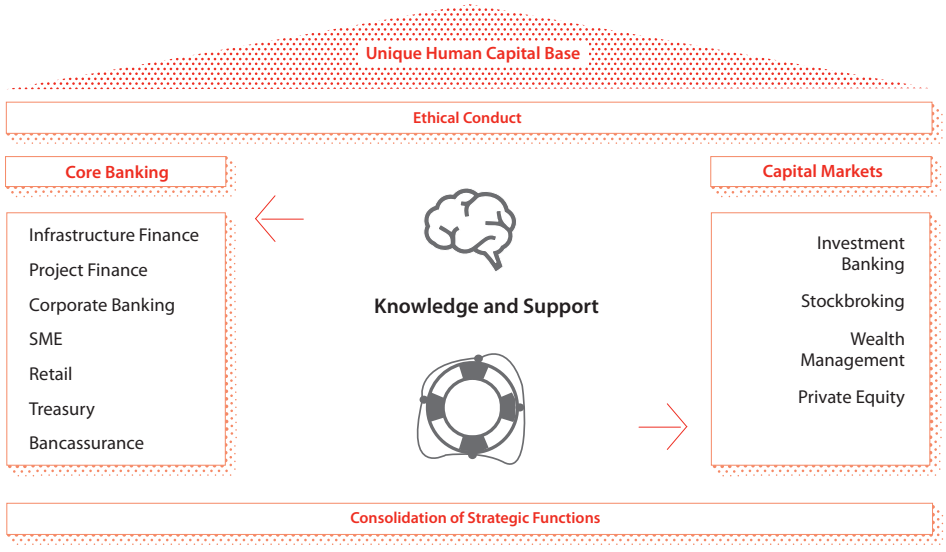
→ INTRODUCTION

The Knowledge Bank



NDB Group has emerged as a unique financial conglomerate harnessing the collective strengths of diversified service and product offerings through the synergy of its many subsidiaries. Its impressive human capital base supplemented by a prudential credit culture and entrenched business ethics has undoubtedly propelled the Group as a forerunner in the national economic resurgence.

The product offering of the Group, has been innovative and client-centric in a bid to cater to all segments of the Sri Lankan society. Our financial solutions vary from simple minor savings accounts to capture major national infrastructure projects. Our clientele ranges from the highest strata of the Sri Lankan society to the dairy farmers of a remote village and beyond the shores of Sri Lanka to mark our footprint in the Maldives and Bangladesh offering world class financial propositions staying true to its image as a 'Universal Banking' conglomerate. From a management perspective, being a universal banking group affords NDB many advantages, such as added heft in negotiations, the ability to exploit economies of scale and a common platform from which to cross-sell its wide array of products and services.

The unique structure of the Group combines synergy with operational independence for its members: National Development Bank (the Parent Company), the Capital Markets Cluster comprising NDB Investment Bank (NDBIB), NDB Stockbrokers, NDB Wealth Management (Formerly NDB AVIVA Wealth Management). These two giant pillars stand firmly on a solid foundation of consolidated strategic functions such as Human Resources, Information Technology and Finance. The two pillars are interlinked by the ethical conduct of a unique human capital base. Inter-dependence between the two pillars is created by knowledge and support. NDB Group is thus uniquely positioned as 'The Knowledge Bank'.

Strategic alliance with DBS, the largest bank in Singapore and a leading financial services group in Asia, gives NDBIB access to foreign high-net-worth individuals and institutions who form a broad potential customer base across 15 markets and 200 branches in Asia. Such alliances bear ample testimony for the wide spectrum of linkages that range from international development funds and other large international lenders to correspondent banks with which NDB has funds-transfer.

The Red Carpet for All

There is a red carpet welcome for just about anyone with any need in the way of financial solutions. NDB Group truly is a financial service provider for all

→ THE RED CARPET FOR ALL

Irrespective of the nature, size and complexity of the financial requirements, NDB Group is well-equipped to offer appropriate, cost-effective, custom-tailored solutions, making it a one-stop-shop for the various business and personal financial requirements that arise throughout a project/ personal life cycle.

The Bank's project-finance expertise has been instrumental in the execution of most of the largest and most critical infrastructure projects undertaken in Sri Lanka during the last thirty years. The post-war economic resurgence has regenerated continued confidence and commitment of NDB in promoting industrial, agricultural and commercial development both as a catalyst and a partner.

NDB offers transaction-banking solutions to the nation's largest corporates as well as to middle market players, in a harmonious synergy with the Group's investment-banking services. These services are promoted through the NDB 'Capital Markets Cluster', a group of subsidiaries and Parent-Company divisions that offer product portfolios in equity, debt financing and insurance, advisory services to the corporate sector, and value additions such as private wealth management and equity research at the retail end of the customer spectrum.

Balancing this presence at the high table of national finance, NDB is deeply committed to the cause of 'financial inclusion', the principle that all Sri Lankans, irrespective of the modesty of their income or social status, deserve access to the financial services. The confidence placed on this segment has positioned NDB among the pioneers to finance the small and medium-scale enterprise (SME) sector. In 2012, NDB reaffirmed its commitment to the sector, through recognition of this target market as a priority sector in the Bank's business strategy. Such prioritization of the SME sector reaffirms NDB's commitment towards national call for development and economic growth to the furthest, least-developed parts of the country.

For the middle market segment, which traditionally constitutes the bulk of personal finance clientele in Sri Lanka, NDB has refocused its retail-banking strategy to capture unexploited market segments, further broadening its footprint and fine-tuning its products and services to gain customer confidence.

The broad strategic parameters of NDB's business growth could be identified as sustainability and inclusiveness. The red carpet must accommodate people from all walks of life and must sustain adversity.

By broadening our horizons to encompass potentially, all Sri Lankans as well as numerous market segments overseas (particularly regional markets like South and Southeast Asia), we stand committed to our ambitions on inclusiveness and sustainability - raising our earning potential, spreading credit and other risks, adding operational capabilities and creating synergies ripe for exploitation.

We are optimistic to deliver on our ambition.

Management Discussion and Analysis

Corporate Banking Group

Project and Infrastructure Financing Division Fulfilling a triple role in a growing economy

Project and infrastructure financing plays an important role in sustainable economic development of developing countries and Sri Lanka is no exception. NDB's Project and Infrastructure Financing Division has been playing a triple role as a catalytic financier, knowledge disseminator and development partner since its inception in 1979 as a specialised project finance institution. With the public and private investment in commerce and infrastructure seeing an exponential increase after the cessation of a 30-year internal war, NDB's Project and Infrastructure Financing Division seized this opportunity to strengthen and expand its business through increased presence across new business segments and new markets, despite the challenges of a high-interest-rate regime and a highly competitive environment.

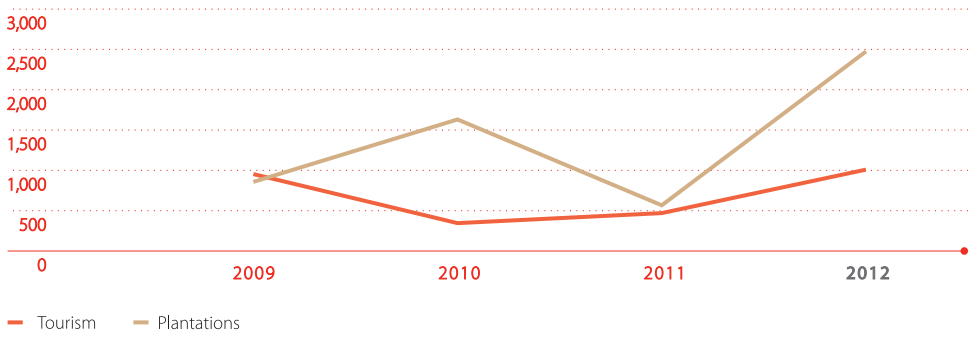
Broadening the spectrum to capture wider market segments

The business grew through increased Net Core Banking Revenue, despite the moderate growth of its portfolio. While focusing on revenue growth, attention was also paid to maintain portfolio quality. Despite the risks associated with term loans granted, the Division was able to maintain its Non-Performing Loans ratio well below 1%, amongst the lowest in the industry. This performance reflects the Bank's success in improving the risk profile, strengthening the credit culture, driving sector diversification and execution of relationship oriented business strategies.

NDB enhanced its reach through increased customer penetration, broadening its spectrum to capture all market segments without confining to the premier corporates. Further, bold initiatives were taken during the year under review to explore the possibilities of geographical diversification locally and overseas for project financing. The Bank in partnership with a Sri Lankan company financed a venture beyond the shores of Sri Lanka. In this direction, NDB's contribution is significant in the energy and plantation sectors in fulfilling a dual role as a project partner and a catalytic financier to Sri Lankan entities establishing business overseas. Locally, the Division financed two hotel projects in the Eastern Province, becoming a pioneer to assist such projects in the east.

NDB endeavoured in continuing its assistance to key economic sectors such as Plantation and Tourism as depicted in the graph below:

APPROVAL OF LOANS FOR KEY ECONOMIC SECTORS (2009-2012)
(Rs mn)



Emphasis was placed on social and environmental sustainability by strictly adhering to the guidelines of the Environmental and Social Management System (ESMS). In order to improve compliance with regard to ESMS, initiatives were undertaken to improve effectiveness and the stability of the system with technical assistance from Deutsche Investitions - und Entwicklungsgesellschaft mbH (DEG), Germany.

Bold and Aggressive initiatives for the future

With the strong capital base forming the foundation for the Balance Sheet growth, the Bank has formulated its strategy for the next few years to expand its business in project and infrastructure financing significantly. In order to achieve this objective, bold strategic initiatives are to be implemented shortly to expand its reach, product offering and service efficiency.

Promoting overseas lending, financing infrastructure projects and promoting fee-based advisory and consultancy services are the new initiatives identified to ensure exponential Balance Sheet growth supported by the strong capital base of the Bank.

With the support extended to the premier development financiers in the country through the Government Budget Proposals for 2013 by facilitating to source overseas funds for project financing, NDB intends to reach a wider customer base representing diverse markets both geographically and sectorally.

Financing of long-term projects through enhanced product offerings including participation in debt market instruments such as rated debentures, structured debt facilities, syndicated term financing and preference share investments will enable the Bank to expand its presence in national development endeavours. In addition, widening its product spectrum through the introduction of fee-based consultancy and advisory services has been envisaged. Enhancing customer convenience will be achieved by way of improved service efficiency and excellence through process improvements for speedy delivery, shared knowledge of a multi-disciplinary team of professionals and value added through the ESMS. The Bank will continue to contribute towards national economic development in a significant manner through these endeavours, which supports growth potential of booming economic sectors.

Management Discussion and Analysis

With the availability of new funding lines and exciting post-war economic revival, NDB will continue to explore the opportunities of expansion both locally and overseas. Under this strategy, financing of projects in newly opened and fast growing Northern and Eastern provinces will be a priority and a key initiative. In addition, the aggressive measures to establish its global presence in emerging economies of Asian and African continents will enable the Bank to make an impression as the preferred project financier for projects promoted by Sri Lankan entrepreneurs beyond Sri Lankan shores.

Wind Power Project in Kalpitiya

Hydro Power Project in Galle

Commercial Banking Division

The Commercial Banking Division continued to demonstrate strong operating performance and broad based growth, despite the challenges within the Banking industry and those arising out of developments in the local and global economy.

The asset portfolio grew by an impressive 24% which was achieved through nurtured relationships, innovative products and customized solutions to meet the varying financial needs of our distinctive clientele. Despite the above impressive growth, the Non-Performing Loan (NPL) ratio was retained at less than 1%, one of the lowest in the industry. Net income from commercial banking operations grew by 26%, contributing substantially to the bottom line of the Bank. Given the emphasis placed by the Bank on the aggressive growth of liabilities during the year under review, the liability base of Commercial Banking operations grew by 38% funding 47% of its own asset book.

In June 2012, the commercial banking operations received ISO 9001:2008 certification for internal policies and procedures, an endorsement of the strong systems underlying the superior service standards offered to our clientele which is attributable to the expertise and professionalism of our experienced staff.

Mr. Batuvita Sumanasiri, the Business Manager of Systems and Services Certification at SGS Lanka officially handing over the Certification to Mr. Amal Yapa, Assistant Vice-President of Corporate Banking

Management Discussion and Analysis

Emphasis on Improved Trade Services

In keeping with the initiatives of the Bank, a key strategy for 2013 would be to drive the changes required to improve the trade services offered considering that most of the clientele are export/ import oriented which would be achieved through improved transaction turnaround times and the provision of advisory services.

Over the past years, cash management has grown to become a key contributor to the liability growth of NDB. This success is mainly attributed to the superior customer service, treasury supported financial advice provided to customers in liability management and the Electronic Banking platform which provides online, real-time solutions for transaction banking. New features would be added during the year to improve the system further.

In furtherance of the above objectives, the Bank will provide Islamic Banking services during the year and thereby offer 'Shariah' compliant financial solutions to meet the diverse needs of our customers. The Bank is in the process of setting up the infrastructure, systems and procedures in this regard.

Nurturing the Middle Market

Currently, the Bank's Commercial Banking clientele consists of top end corporates and the middle-market companies in Sri Lanka. Over the years, NDB has nurtured and groomed many middle market entities to bloom into large corporates in a diversified arena i.e. agriculture, construction, manufacturing, local trade, imports, exports etc.

The middle market segment constitutes a substantial portion of the Sri Lankan economy and is a key contributor to its growth consisting of corporates which have grown and matured beyond the SME segment and are in need of more complicated banking solutions. This unexploited market segment with many sub-segments is earmarked to be explored by the Bank through the provisions of structured financial solutions to identified sub-segments.

Sponsorship of the 'Most outstanding Exporter - Sector Wise' category of the Annual NCE Export Awards 2011

The incentives of the 2013 Budget Proposals would undoubtedly propel NDB to promote long-term funding to middle market segments in plantations, construction and manufacturing sectors. Complementing the initiatives taken by the project and infrastructure finance division, the Commercial Banking operations unit too would proactively seek opportunities to provide working capital solutions to clients in overseas markets - initially in countries where Sri Lankan entrepreneurs have established businesses.

SME Banking

The year 2012 marked the beginning of many groundbreaking initiatives by NDB to support the SME sector. Amongst such initiatives the tri-lingual quarterly publication 'Siya Savi' launched in 2012 is noteworthy. The publication strives to add value through the dissemination of the much needed entrepreneurship education to this sector while recongizing and appreciating our own SME clientele who have made great strides in their respective businesses. Most articles appearing in this publication are authored by NDB staff members.

Regional technical advisory training provided to the SMEs also proved our commitment towards this priority sector. During the year under review, 16 technical advisory programmes with the participation of over 1000 entrepreneurs were held island-wide, drawing resource personnel from the Central Bank, local universities and our own expertise. These programmes were financed by NDB in collaboration with International Finance Corporation (IFC) and World Bank.

Establishment of SME centres equipped with state-of-the-art facilities to support the SME entrepreneurs also marked a significant feature in the 2012 SME business agenda bearing further testimony of NDB's commitment to this sector. The centres are now fully-operational with dedicated staff to provide the entrepreneurs with required advisory and financial support. The centres also enable computer access for personal browsing providing a wide array of information including training modules for interested entrepreneurs. IFC works in close collaboration with NDB in providing access to important sources of information and development banking sites through these IT facilities.

The SME banking clientele of NDB based on estimates accounts for 35,000 jobs in 2012, compared to the 2011 estimate of over 21,000. Similarly, the SME customer turnover generation is estimated at Rs 201 bn in 2012 compared to Rs 96 bn in 2011 which could be attributable to the financial assistance and customer acquisition by NDB. During the year under review, total facilities approved to this vital sector exceeded Rs 8 bn covering a wide array of industries including agriculture, trading, exports, imports, fisheries and tourism. NDB will continue to support the national cause of supporting the SME development in the country.

Despite the challenging economic environment, NDB's efforts to maintain superior credit quality has paid rich dividends with its SME portfolio recording a NPL ratio of 2.2% in 2012 as against the 3.24% in 2011. This commendable achievement could be attributable primarily to the expertise and experience of the staff in understanding the pulse of this sector, leading to superior customer origination.

Management Discussion and Analysis

NDB's unique channel financing value propositions in managing customer receivables via in house developed technological solutions such as 'Receivable Management System' (RMS) and 'PO Management System' (POMS) have contributed towards superior service excellence to our clientele.

During the year under review, NDB made optimum use of concessionary funding/credit lines from donor agencies and Government, i.e. DEG, SMEDEF, RFPL, Sawbhagya, Dasuna and SMILE II Revolving. Almost the entirety of the Government sanctioned IFA had been utilized to fund the SMEs totalling to over Rs 480 mn during the year 2012.

SME Workshop in Minuwangoda

SME Business in Hambantota funded by NDB

Performance Overview

SME Banking portfolio of NDB grew by 32% during the year 2012, with an improved NPL ratio of 2.2% as opposed to 3.24% in the preceding year. The Provincial distribution of the portfolio is in line with the GDP distribution of the country, Western Province being the dominant beneficiary. The Bank's SME portfolio is well-diversified with the largest contributor being the service sector, which consists of 23% of the portfolio. However since service sector is further distributed across 15 sub-sectors, the concentration risk could be deemed minimal.

Strategic Focus

Given the passion and the commitment of the Bank towards national development, NDB now envisages supporting the microfinance sector as part of its core banking activities within the ambit of the SME business proposition. The creation of wealth and providing hope for a bright future to this underserved yet deserving segment are the underlying themes behind the microfinance business proposition of the Bank. The envisaged strategy would focus on capacity building and empowerment of the bottom end of the pyramid whilst providing financial assistance irrespective of availability of collateral.

In line with the global sustainability agenda, NDB believes in the concept of triple bottom line, by focusing on people and the planet in addition to profits. Through NDB's '*Divi Aruna*' (awakening of lives) programme, the Bank has been able to achieve the above objectives. Amongst the industries supported during 2012 were fisheries, clay pottery, shoe manufacturing, vegetable cultivation, tea smallholders, dairy, sweet meat industry, weaving of handbags etc. NDB actively participates in the '*Divi Neguma*' programme initiated by the Ministry of Traditional Industries and Small Enterprise Development supporting the national cause of entrepreneurship development at grass root level. Focusing on the capacity building gaps, NDBs '*Jeevana*' livelihood scheme attempts to empower the youth by providing skills training and development in selected vocations.

SME Centre Opening in Kurunegala

Management Discussion and Analysis

As a strong advocate of the ESMS (Environmental and Social Management System) policies, NDB ensures responsible lending by meeting the internationally accepted norms in analyzing projects giving due consideration to preserving the planet by minimizing wastage and carbon emission. High emphasis is placed in ensuring that projects funded are in strict compliance with the standards set out by the relevant 'Environment Protection Authorities'.

As part of its sustainability programme NDB encourages all business lines to participate in socially responsible activities as a valued and respected corporate citizen. Accordingly island-wide programmes have been conducted with the participation of all Retail and SME staff members across the country emphasizing on children, women and differently abled.

NDB is optimistic that SMEs will form the backbone of the future economic growth of Sri Lanka, in line with the Government's commitment to support the sector. In the foregoing scenario, NDB will endeavour to expand its geographical reach in order to build and sustain stronger local economies.

Retail Banking

NDB continues to be a comprehensive financial solutions provider of the Sri Lankan consumer catering to a myriad of personal financial needs of a diverse clientele. Despite the macroeconomic stresses, retail-banking performance of NDB continued to maintain momentum which was achieved through appropriate pricing strategies and superior product innovation. Strategic product innovations in 2012 included the introduction of pre-approved loans, six-year leases and the setting-up of a 365-day leasing desk. Supplementing the leasing business, NDB also made its first foray into Hire Purchase lending during 2012.

During the year under review, NDB maintained its reputation for superior asset quality management recording a NPL ratio of 2.26% despite a high interest-rate regime and the restrictively regulated credit environment which prompted a strategy of asset consolidation.

While our asset strategy emphasised consolidation, our deposit strategy proved otherwise. The deposit portfolio of SME and Retail Banking grew by an unprecedented Rs 19.4 bn, which is a year on year deposit growth of 33%.

NDB undertook several strategic initiatives and promotions to mobilise deposits such as the re-launch of the popular *Badu Malla* promotion and the introduction of new savings schemes such as Savings Star Plus and NDB Real Saver.

Fee-driven businesses, such as remittances and credit/debit cards, indicated steady progress. It is envisaged that the remittance offering would be moulded into a strong brand to emerge as a frontrunner in the retail-banking business.

Network Expansion

In line with the Bank's commitment to promote economic growth outside the Western Province in 2012, NDB opened branches in Ambalangoda, Hambantota, Alutgama, Chunnakam, Dambulla, Embilipitiya, Hambantota, Kaduruwela and Nawalapitiya recording a total of 69 branches including two new branches in the Western Province namely Kaduwela and Minuwangoda. The location of the new branches was strategically placed in view of the fact that the GDP contribution from the rest of the country is gradually overtaking that of the Western Province. Committed to a strong national presence, NDB will continue with its geographical expansion in the coming years.

Branch Opening at Minuwangoda

Deposits

The deposit-mobilisation strategy for 2012 focused on a more advisory theme where depositors were encouraged to manage their own finances through incentives and products such as Real Saver. The above strategy was in line with the initiatives already taken by the Bank to inculcate a saving habit amongst all Sri Lankans thus contributing towards the Government's goal of increasing national savings. The said initiatives resulted in attracting savings deposits over Rs 4 bn.

Overall, the retail and SME deposit base of NDB grew by Rs 19.4 bn during the year under review, which is an increase of 33% over the previous year. In comparison, the average deposit growth rate for the entire banking industry stood at 17.1%.

Management Discussion and Analysis

Loans and Advances

With foreign reserves being depleted by growing imports and declining exports, the Central Bank moved to adjust the balance of payments by raising the official interest rate, mopping up liquidity in the market and placing specific lending growth ceilings on banks. This resulted some declining of demand for credit, which was aggravated by increased import duties, especially on vehicles. Vehicle registrations fell by 50% over the previous year. Under these conditions, an increase of 29% in the leasing asset book was commendable. The main contributors to the increase in retail assets were pawning and auto financing products.

Home Loans

During the year under review, NDB refocused its market segment to the lower income segment to support the personal housing needs rather than housing for investment purposes. The average size of a housing loan stood at Rs 1.7 mn in 2012 bearing ample testimony to the conscious efforts made by the Bank to channel more granular facilities. Emphasis was also placed in financing housing loan facilities for non-resident Sri Lankans under the theme 'a nest in your own motherland'. Despite the many challenges in the market, the Housing non-performing loans portfolio recorded a ratio of 1.15%, perhaps one of the lowest in the industry.

Personal Loans

The personal loan portfolio of the Bank remained stable although growth was curtailed by the high interest-rate regime and a lack of appetite for long-term investment opportunities amongst retail customers. The demand for personal financing was primarily derived from customers who wished to consolidate their liabilities and ease personal cash flows. While the number of loans processed remained the same the average size of a loan reduced dramatically. Notwithstanding these changes in customer behaviour, portfolio quality was maintained at the highest level and the NPL ratio stood at 1.48% at year end.

Promotional and merchandising efforts continued to focus on the convenience of the Dream Maker personal-loan product, which boasts of a three-hour approval process for targeted segments.

Auto Finance and Leasing

Defying the constraints faced in automobile sales and leasing industry, NDB's leasing portfolio grew by 25% over the previous year and now stands at Rs 7.3 bn emerging as the key contributor to the growth momentum of retail banking during the year under review.

The above feat was attributable to the strategic partnerships with industry leaders i.e. Sathosa Motors, Toyota Lanka, United Motors, Unimo Enterprises in addition to a multitude of retail dealers. These partnerships were actively promoted through advertising, outdoor and direct-marketing campaigns in the year under review. Another contributor to portfolio growth was the introduction of hire purchase facilities for registered vehicles revolutionizing the traditional norms of the leasing industry, by removing the need for down-payment and guarantor requirements for hire purchase contracts. Such innovative measures together with customized repayment terms, discounted insurance premiums and minimal documentation contributed towards the growth in volume and pull new clients.

In addition to the steady growth, the Bank boasts one of the best leasing portfolios in the industry in terms of quality, recording a NPL ratio of 1.97%.

Pawning

Considered a key contributor to the retail growth strategy the Pawning portfolio grew by over 35% in 2012 and currently stands at Rs 3.7 bn. The Bank currently offers the pawning product island-wide where noticeably large contributions are made by the branches located in the Northern and the Eastern Provinces.

Remittances

In keeping with the macroeconomic trends, Remittance business value increased by 35% in 2012, main contributor being Western Union Money Transfer Service. It is encouraging to observe increased demand in the remittance services from Middle Eastern countries, Europe, Scandinavian countries and Australia, dense with expatriate Sri Lankan population.

In Italy, NDB conducted a successful promotional campaign, *Ithaliye Thagi Pita Thagi*, based on its popular *Thagi Pita Thagi* domestic promotion, offering prizes to savings and FD account holders and to recipients of remittances originated via National Exchange Company in Italy.

Tie-up with Union Chemists to provide Western Union Services

Bancassurance

Subsequent to a strategic divestment of the NDB Group during the last quarter of 2012, Aviva NDB was reconstituted as AIA PLC. Despite the change of ownership and name NDB was successful in securing a twenty-year agreement with AIA for the distribution of bancassurance services in Sri Lanka reaffirming its long-term commitment towards the insurance sector.

Management Discussion and Analysis

Privilege Banking

NDB Privilege Banking provides a unique personalized wealth-management proposition to affluent personal-banking clientele evolving to be a truly comprehensive, global service provider, offering investments in derivatives and structured products as well as equity investments and private placements through the NDB Group companies. NDB's value proposition in this respect has attracted many clients even off the shores of Sri Lanka, infusing valuable foreign investment while boosting country's balance of payment.

Amongst the many promotional initiatives undertaken by Privilege Banking during 2012, was the sponsorship of the annual American Chamber of Commerce golf tournament - the highlight of the year's golfing calendar in Sri Lanka, which was being held for the thirteenth successive year. As a 'platinum' sponsor for the event, NDB Privilege Banking gained recognition within the targeted market segment while also contributing towards the education and welfare of the children of caddies living in the vicinity of the Royal Colombo Golf Club.

Participants at the Amcham Golf Tournament

Telemarketing and 24x7 Call Centre

Exponential growth of the branch network and the product offering in recent years has promoted the Bank to introduce the 24x7 Call Centre which recorded an increase of 24% in incoming call volumes in 2012 as against the preceding year.

The Bank's telemarketing team continues routine and specialised promotional activities in addition to conducting surveys of strategic importance based on the needs of the Bank.

Operational Improvements and Risk Management

Heavy emphasis was placed on operational process improvements and credit risk management to keep pace with increasing business volumes and expanding geographical reach. In this respect, most outstanding was the streamlining of process flows and delegation of authority to empower ground level staff with more decision-making authority. Constant attention is paid on operational risk management, with a special focus on branch banking and product delivery channels; thereby minimizing potential losses and reinforcing the Bank's commitment towards maintaining quality. Monthly reviews of all SME and Retail banking related operational matters are carried out under the purview of Vice-President - Retail and SME Banking.

Synergies with Group Companies

Building on the strength of the Group companies, Stockbroking counters were opened at NDB branches in Gampaha and Galle during the year by NDB Stockbrokers. High-net-worth clientele in these localities were rendered expert advice on wealth management and wealth creation products, resulting in significant cross-sales to branch customers. In addition, our individual and corporate clientele have also benefited through the advisory services provided by NDB Investment Bank and NDB's own Project Finance Division.

SME and Retail Banking: The Outlook

Despite the challenging macroeconomic environment, the future for SME and Retail sector indicates great potential for growth. Rising per-capita GDP and lower unemployment (currently measured at 3.9%) foreshadow consumption growth and increased demand for credit. With the removal of the current credit ceiling and the advent of overseas funding opportunities outlined in the National Budget Proposals - evidence of a Government policy favourable to business and particularly to SMEs - the picture can only improve. Even the stagnant global economy is showing signs of revival, though recovery is still a long way off. Meanwhile, growth in inward remittances, tourist arrivals and investment opportunities supplemented by Government concessions to selected industries, will drive GDP growth and create significant opportunities for banks.

Re-emphasizing its commitment to the SME and Retail Banking sector, NDB will continue to drive growth in these areas through aggressive channel expansion (both in the conventional branch network as well as in alternate distribution and customer-contact channels), new value-added product propositions and service offerings supplemented by streamlined business processes to ensure customer satisfaction.

Management Discussion and Analysis

The Bank will also leverage on the national efforts to encourage the savings habit by becoming the flag-bearer for this worthy national cause. Great strides have been already taken in this direction through the introduction of the Real Saver product in 2012 and the publication of its *Ithuru Karana Maga* ('The Way to Save') booklet in 2011. The Bank will strive to outpace the impressive momentum created in deposits mobilization in 2012, during 2013 as well.

The growth in deposits will also be complemented by equally aggressive growth in assets, especially in SME finance. In this regard, special emphasis will be placed on nationally-declared priority areas such as agriculture, tourism, construction, trading and exports. New SME centres on the same lines of those already set up in 2012 will be established island-wide in 2013, while the Bank's programme of technical-assistance seminars for entrepreneurs will be intensified.

In addition to the intensified focus on the SME sector, Leasing, pawning and consumer finance will also be growth areas for NDB in 2013.

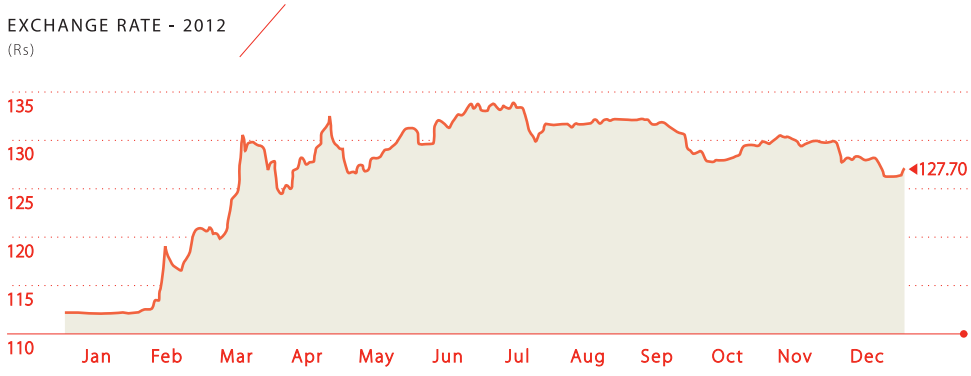
Treasury

The Operating Environment

Economic activity in Sri Lanka was somewhat constrained through the year by high interest rates and a number of other internal and external factors. Inflation pressures and excessive credit growth in 2011 prompted the Central Bank to tighten monetary policy and impose a credit ceiling on banks and other lenders in 2012. The rupee fell significantly against the US Dollar, while the Colombo Stock Exchange experienced a steady decline until September.

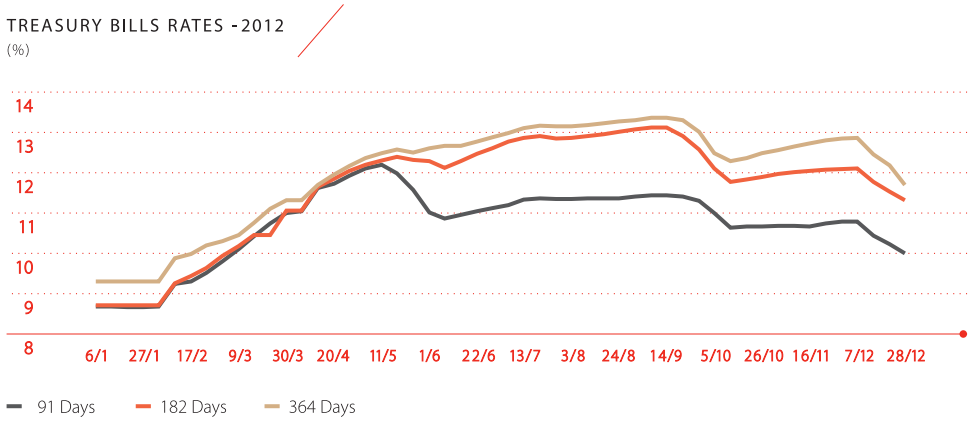
There was a significant depreciation of the Sri Lankan Rupee against the US Dollar during the first two quarters after the Central Bank ceased to intervene in the forex market. This move was welcomed by market participants, and the rupee was held relatively stable through the third and fourth quarters, ending the year at 127.70 making an overall annual depreciation of 12%. The national trade deficit narrowed by 4.1% for the year on the back of a 5.8% decline in imports, despite a general failure by exporters to take advantage of the weaker currency. The balance of payments also showed a surplus at the end of September, which the Central Bank attributed to workers' remittances, tourism and capital inflows.

Under the prevailing operating environment NDB's Treasury Division continued to meet not only the Bank's funding needs but also managing volatility in terms of interest and exchange rate changes besides meeting its own revenue targets.



In addition to imposing a credit ceiling, the Central Bank moved to tighten monetary policy twice in the first half of the year. Treasury Bill and Bond rates moved rapidly higher until September, then fell sharply due to foreign fund inflows. Rates at year's end for 3-month, 6-month and 12-month T-Bills were 10.00%, 11.32% and 11.69% respectively.

Exchange Rate Movement for the Year



Following unprecedented growth in 2009 and 2010, when it was ranked among the best-performing exchanges in the world, the Colombo Stock Exchange experienced a general decline, with prices, new listings and trading activity all on the downtrend. The All Share Price Index (ASPI), which stood at 6,074 on 1 January, fell to 4,737 on 6 June 2012 before rallying modestly in September to closing the year at 5,643 - a fall of around 7%. A variety of domestic and external factors contributed to this disappointing performance, from world economic recession to rising domestic interest rates (which resulted in retail investors shifting their assets from equity investments to relatively risk-free instruments such as short-term T- bills and Fixed Deposits).

Management Discussion and Analysis

Performance Review

NDB's Treasury continued to be a market-maker in the inter-bank spot and forward markets, which conferred on the Bank a pricing advantage in rates for both export and import customers. The revenue recorded in trading activities was commendable contributing positively to Bank's overall profitability. Supplementing its routine business, Treasury performed a unique role in providing advisory services to clients on market movements thereby improving business volumes through competitive pricing.

The role of Treasury in sourcing local and foreign funds through financial institutions and multilateral organizations became vital to keep pace with the asset growth of the Bank. In June 2012, NDB Treasury successfully raised US$ 50 mn through a syndicated 18-month loan - the first ever syndicated loan with a tenor in excess of 12 months to be raised by a local bank.

NDB Treasury was able to realize substantial gains from its debt-trading operations despite the upward movement in interest rates which adversely impacted operations in Government Securities. During the year under review, NDB Treasury formulated the necessary framework to introduce an asset-and-liability management desk to manage Balance-Sheet mismatches.

Outlook

With revived confidence, we expect more stability in both interest and exchange rates in year 2013. The Government's challenging target of achieving a budget deficit of 5.8% of GDP, through a growth target of 7.5% will undoubtedly open up ample opportunities to the banking sector to flourish alongside the anticipated economic growth. NDB Treasury will contribute towards this vital growth through mobilization of non-traditional funds mainly through foreign sources.

Support Services

Information Technology

Strengthened Information and Communications Platform

In keeping with the spirit of our process and service transformation aimed at superior customer service excellence, Information Technology (IT) department continued to execute on the technology blueprint for NDB's business strategy.

Year 2012 could be considered as a year of consolidation in line with the implementation of the new core banking platform in October 2011. This enabled NDB to strengthen system and network operations monitoring, improve connectivity to all regions and a high availability computing platform; much needed in this competitive Banking Industry. We are also continuing to strengthen our network security and technology operations by on-boarding peripheral applications.

Having created new dimensions in money transfer services, our customers now enjoy the ability of transferring money via VISA money transfer facility which will allow them to transfer funds in real time to any corner of the world which is a pioneering effort by a Sri Lankan bank. In order to cater to the fast growing online payments market, the Bank has implemented the VBV (Verified by Visa) facility to its customers to enable them to perform secure online transactions from their debit and/ or pre paid cards. SMS alerts for Credit Cards and Online VBV Transactions are now available for customers as a value-added service.

During the year under review, NDB launched the INSIGHT Platform to facilitate the pro-active, efficient and dynamic delivery of Management Information which will help the business in Regulatory Reporting, Risk Management, Customer Relationship Management and overall generation of Business Intelligence such as Trend Analysis and Forecasting etc. NDB has already initiated a project to virtualize the non-core-business application servers and will continue to evaluate techniques such as desktop virtualization and storage virtualization to manage our costs and reap better benefits in line with the diversification of the Bank's business.

In our attempts to pursue growth in a disciplined and judicious manner, the Bank successfully conducted a full scale disaster recovery simulation for the first time since moving to the new core banking platform, to test its DR capabilities in an unforeseen event and to complement its business continuity plan.

Consolidation of the Internet Banking platform took place during the period under review enabling Corporate, Retail and E-remittance clients to experience more facilities.

NDB envisages to upgrade the data centre to a 'Tier III' standard data centre while improving data integration, unified communication, collaboration and multi-party conferencing by converging into Voice Over IP (VOIP) in a bold effort to facilitate better and effective communication

Abiding by the spirit of responsible corporate citizenship NDB IT has been spearheading a widespread office environmental sustainability programme with key initiatives including virtualization, e-statement generation and paper recycling for better energy conservation and waste management which will continue in the forthcoming year.

Management Discussion and Analysis

Performance of Group Companies

NDB Capital Holdings

Creating New Frontiers in Capital Markets

NDB Group marked a new era in the financial services industry in Sri Lanka with the re-launch of Capital Development and Investment Company PLC as NDB Capital Holdings PLC (NCAP) in June 2012, as a full service investment bank under a new management led by a team of capital market experts. In order to facilitate this new strategy, NDB Investment Bank Ltd. (NDBIB), NDB AVIVA Wealth Management Ltd. (NWM) and NDB Stockbrokers (Pvt) Ltd. (NDBS) were clustered under the NCAP umbrella. During the year, NCAP sold its direct and indirect holdings in Aviva NDB Insurance PLC to American International Assurance Company Ltd. (AIA) of Hong Kong, thus realizing a six-fold capital gain amounting to Rs 6,693 mn. Furthermore, NCAP increased its stake in NWM to 100% and the company was rebranded as NDB Wealth Management Ltd.

NCAP's fee-based investment banking operations are facilitated through NDBIB, the flagship company of the Capital Markets Cluster, which is the market leader in both debt and equity structuring and placements. NCAP provides wealth management services to clients through NWM, the largest private sector wealth management company in Sri Lanka with over 20 years of industry experience and over Rs 57 bn in assets under management. NCAP's stockbroking operations are conducted through NDB Stockbrockers, one of the foremost brokering companies in the country that offers high-end research and brokerage services to both Sri Lankan and foreign investors in the CSE. Despite the dismal performance of the CSE and the tight money market conditions which adversely affected the business, the NCAP group companies outperformed the competition.

Creating a landmark in the history of debt markets in Sri Lanka, NCAP launched a family of bond indices for Government Securities in partnership with CRISIL Ltd., India. The indices were aptly co-branded as NDBIB-CRISIL and offered indices for 91-day, 364-day, 3-year and 5-year Government Securities.

The Governor of Central Bank speaking at NDB Capital Holdings' launch of Bond indices

With its diverse portfolio of service offerings comprising of investment banking, wealth management and stock brokering, NCAP envisages to cater to the growing needs of the Sri Lankan corporate sector and the capital markets. While maintaining its flagship status in the above mentioned business lines, NCAP also holds private equity investments amounting to approximately Rs 125 mn. NCAP has geared itself to cater to the escalating demand for private equity during this phase of growth in Sri Lanka through aggressive private equity portfolio expansion.

NDB Investment Bank Fortified through International Accolade

Befitting its status as Sri Lanka's premier investment bank, NDBIB outperformed its peers in an extremely challenging macroeconomic environment. Qualitatively, NDBIB rose to unprecedented heights, concluding several landmark mergers and acquisition deals, raising a total of Rs. 16 bn in debt and equity, and exploring new avenues in fund raising. Whilst adding superior value to its clientele through fee-based advisory services, NDBIB during the year focused substantially in training and skills development. With these changes, the company is now well poised to benefit from a cyclical upturn. Bearing testimony of its achievements, NDBIB was named the 'Best Investment Bank in Sri Lanka' by Euromoney, the first time an investment bank in Sri Lanka has received any such international accolade.

Management Discussion and Analysis

The year saw only three IPOs on the Colombo Stock Exchange, the largest two of which - Access Engineering PLC and Mackwoods Energy PLC - were managed by NDBIB. Corporate advisory activity was more intense during the year under review. The company successfully completed two large M&A transactions in the manufacturing and fashion-retail sectors, demonstrating its growing capabilities in this area. Numerous valuation assignments were carried out for firms in the leisure, hydropower, financial services and manufacturing sectors in addition to the advisory assignments undertaken on behalf of one of the large state-owned entities and a leading consumer-goods manufacturer.

Debt financing of over Rs. 12.5 bn was secured from the banking and finance sector and from the capital markets despite difficulties that arose due to the high interest-rate regime and the credit ceiling of 18% stipulated by the Central Bank for banking institutions. The largest credit and debit card receivables securitization, a product introduced to the market by NDBIB last year, was concluded successfully for one of the leading retail chains, raising Rs 2 bn with the participation of a syndicate of banks and financial institutions. NDBIB's client portfolio was further expanded with the addition of new clientele from the food and beverage, plantations and diversified holdings sectors.

While NDB continued to participate in IPOs, debt financing and M&A transactions carried out by NDBIB, there was a significant upsurge in interaction amongst the businesses within the investment-banking cluster. i.e., between NDBIB and NDBS in relation to M&A transactions on the CSE.

With the Government offering concessions to encourage the listing of both debt and equity on the CSE, and relaxing exchange control regulations for firms raising foreign currency debt, it is envisaged that 2013 is likely to witness a resurgence in the Sri Lankan capital markets and NDBIB is poised to enjoy a fruitful year, with a healthy portfolio of debt and equity deals already in the pipeline.

NDB Stockbrokers
Leveraging on the Group Strength

Measures introduced to stabilize the economy had a positive impact in regaining investor sentiment on the CSE. Foreign inflows picked up significantly and a recovery was perceptible in September as interest rates, inflation and exchange rates steadied. Positive measures introduced in the Budget, augurs well for the future of Sri Lanka's capital markets. Better performance of the CSE is anticipated in 2013, gathering momentum towards mid-year.

Despite the stagnant investment climate, NDBS continued its efforts to expand the geographical reach. Two new service centres were opened in Gampaha and Galle as part of a strategy of leveraging the NDB branch network to broaden the retail base and creating cross-sell opportunities. In furtherance of its attempts to create customer awareness on wealth creation, several presentations on capital markets and investment were made to audiences around the country.

The company's specialized sales team continued to market financial products structured by firms and divisions in the Capital Markets Cluster, while also seeking to boost revenues by facilitating placements in private equity deals. Further, synergies emerged subsequent to the restructuring of the 'Capital Markets Cluster' (see the section on NDB Capital Holdings above). Such a resource base undoubtedly places NDBS at a significant edge over its competition to emerge as a market leader. Endorsing its emphasis on the qualitative aspects of business, the research team was strengthened to cater to a growing portfolio of foreign, institutional and high-net-worth individual investors.

'Invest Sri Lanka' the first-ever overseas investor forum held in Malaysia under the auspices of NDBS was a landmark event of the year, showcasing Sri Lanka and profiling prominent listed Sri Lankan companies to foreign investors. The forum was succeeded by the investor conference in Singapore organized by our strategic partner, DBS Bank. Many such investment forums and conferences have been planned for 2013 as the company seeks greater penetration in the foreign markets.

Management Discussion and Analysis

NDB Stockbrokers opens Branch in Gampaha

NDB Wealth Management
Emphasis on Operational Efficiency

Building on the concept of wealth management, NWM continued to offer sophisticated, innovative, customized financial planning and management services to Sri Lankan savers and Investors. The services of NWM encompasses discretionary portfolio management (for institutional and individual high-net-worth investors), private wealth management for individuals, and mutual funds for the retail market. During the year under review, the company obtained an Investment Manager Licence from the Securities and Exchange Commission in addition to being a licensed unit trust management company. NWM has successfully secured a long-term agreement to manage the Insurance funds of the Sri Lankan operations of AIA.

Enhancing its operational efficiency and excellence in customer service through industry best practices in respect of compliance and reporting, NWM invested in state-of-the-art wealth-management software in 2012. The new software provides institutional and high net-worth clients with accounting reports or online access to portfolio information while facilitating the introduction of new products/solutions.

The 'Eagle Gilt Edged Fund', a fund dedicated to investment in Government Securities received an AAA credit rating from ICRA Lanka, one of the leading credit rating agencies and a subsidiary of Moody's. The 'Eagle Gilt Edged Fund' is the first-ever mutual fund to be rated in the Sri Lankan market.

Under the 'myeaglefunds' umbrella, two new mutual funds were launched in 2012. The 'Eagle Money Fund" invests exclusively in short-term Government Securities, while "Eagle Money Plus" invests in short-term corporate debt. Both products are designed to cater to the short-term savings and liquidity management needs of corporate and retail clientele. Several other innovative products and services are in the offing for 2013.

NDB Capital (Bangladesh) Offering High-end Investment Banking Solutions

NDB Capital, which commenced operations in 2009, is the only international merchant bank in Bangladesh. With the acquisition of a controlling interest in this firm by NDB, NDB Capital is provided with the dual advantage of access to the technical expertise of NDBIB, supplemented by a wealth of indigenous knowledge and contacts through its Bangladeshi joint-venture partners; thus offering high-end investment banking services to the Bangladeshi capital market.

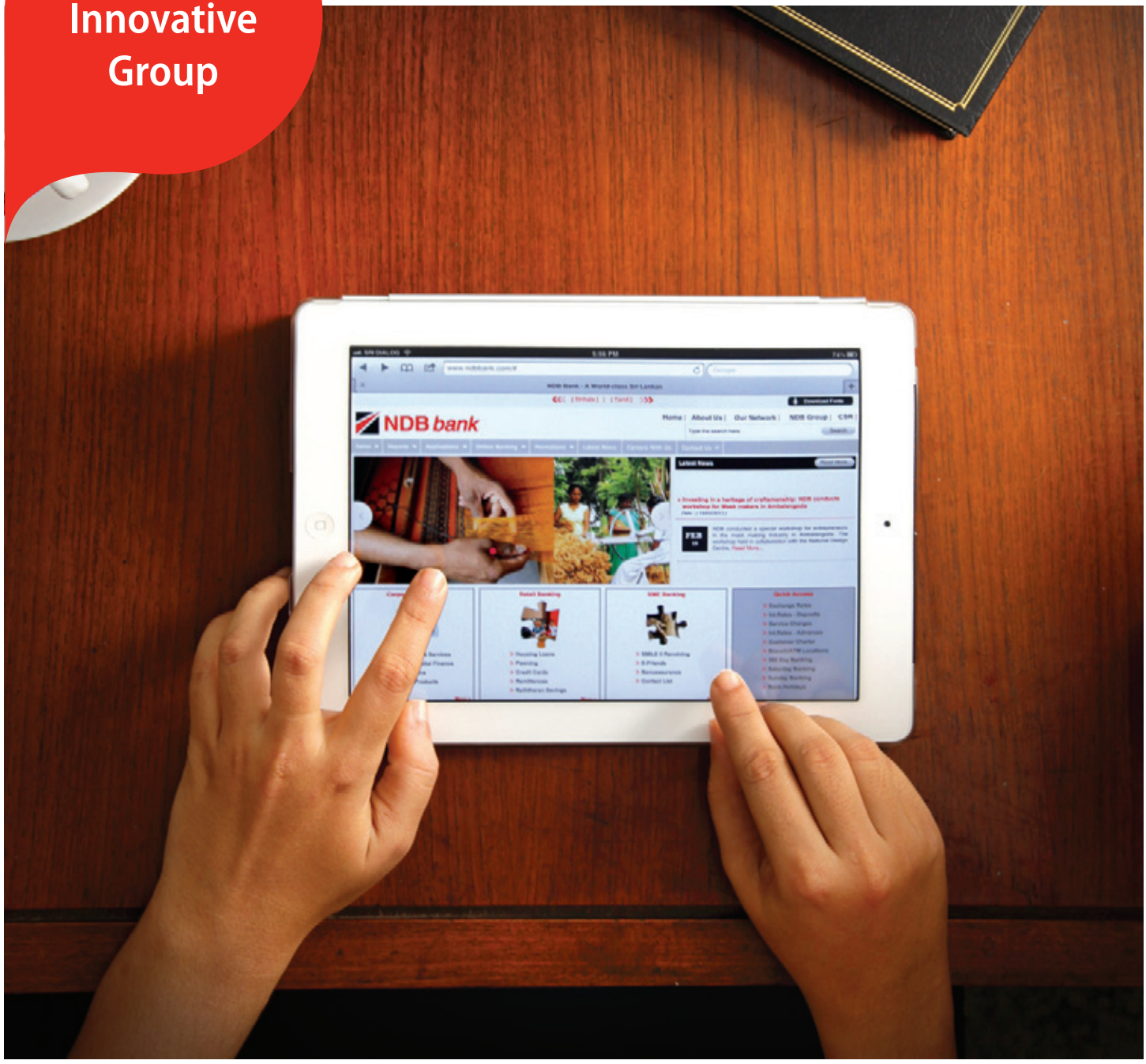
2012 was a difficult year for the Bangladesh economy. Volatility with low turnover experienced by the Bangladeshi capital markets during the year saw the Dhaka Stock Exchange General Index at 4,219 on 30 December compared to 5,352 on 1 January (a fall of 21%); thus making capital-market transactions extremely difficult to execute.

Bangladeshi regulators sent mixed signals through their monetary-policy decisions, resulting in an abrupt increase in interest rates and an acute liquidity crisis. The situation was aggravated by increased Government borrowing from banks, while gas and power shortages in the country further discouraged investment. In the foregoing scenario, several debt raising transactions which had been mandated for NDB Capital have been slowed down.

On a more positive note, NDB Capital, although a relative newcomer to the Bangladesh market, increased its presence and visibility through networking and promotional activities in a bid to ensure a steady flow of business in the ensuing year. The company foresees better prospects in 2013 through the execution of mandates already signed with a number of reputable local firms, primarily for debt financing.

The innovative spirit runs so strong in the NDB Group, that they seem to be able to embrace any situation… any character and personality…and deliver premium, 'out of the box' solutions…at will.

Quite an Innovative Group



QUITE AN INNOVATIVE GROUP

Brand Building

NDBs transformation and consolidation into a fully-fledged commercial bank has earned a ranking amongst the Top Fifteen brands in Brand Finance Lanka's annual ranking for the year 2012. The brand presence was further affirmed by the 'Brand Excellence Award' earned by NDB at the 2012 CMO Asia Awards in Singapore, in the category of banking, financial services and insurance.

Such achievements were feasible through many ambitious brand building initiatives undertaken by the NDB Group during the year. The most outstanding contribution in promoting entrepreneurial excellence amongst Sri Lankan businessmen was the Asia Pacific Entrepreneurship Awards held in partnership with the Malaysia Business Council and Ceylon Chamber of Commerce in 2012 where NDB was the principal sponsor. The joint venture was a pioneering project in many respects.

Significant amongst the brand building initiatives undertaken by NDB during the year was the Poson Vandana savings mobilization and safety campaign jointly conducted with AVIVA NDB Insurance, where awareness of safety during the pilgrim season to the historic shrines of Anuradhapura was coupled with a savings promotional campaign. The highlight of the promotion was the provision of free transportation by rail between Anuradhapura and Mihintale, to over fifty thousand pilgrims. NDB staff were deployed aboard the train, as well as at Anuradhapura and Mihintale railway stations, to spread the savings message through presentations and the distribution of over 50,000 copies of *Ithuru Karana Maga* booklets. Filled with excited passengers, the brilliantly co-branded train was a highly visible part of the Poson festivities. In addition, the Bank also sponsored the publication and distribution of a booklet of *gatha* (Buddhist devotional verses) amongst the pilgrims.

Optimizing the full potential of Sri Lankan youth, the EDEX Education and Careers Fair 2012 received active collaboration from NDB for the fifth consecutive year. As a participative sponsor at Sri Lanka's largest higher education and career fair held in Colombo and Kandy, the Bank reiterated its auxiliary efforts towards youth empowerment.

The AmCham-RCGC Golf Tournament organized by the American Chamber of Commerce, a much lauded event in Colombo's golfing calendar which also encompasses a philanthropic emphasis was sponsored by NDB in 2012, positioning its commitment to sports and recreational activity while reiterating its pledge towards community development through active participation.

Poson Vandana

Management Discussion and Analysis

Tikiri Peya Children's Promotion

Media Advertising and Brand Visibility

Lanka Market Research Bureau studies revealed improvements in overall spontaneous awareness of the brand and a total awareness level above 90% in key regions across the country during the year under review. Such increase in NDB's brand awareness levels could be attributed to the mass promotional activities conducted by the bank island-wide in addition to its highly visible presence in print and electronic media in all national languages. The brand visibility was further enhanced through equally vigorous outdoor presence through billboards, branch branding and branded street name boards throughout the country.

Adding more flavour to the promotional and publicity initiatives undertaken by the bank were customized events and campaigns that increased the awareness levels of the NDB brand within the targeted geographies. Branch openings were announced to the public by advertising on national media, while localized efforts such as door-to-door promotions and feet-on-the-street publicity gathered momentum for the new branches to commence operations on a high note.

Strategic Product Marketing

NDB Savings Star Plus

Bearing testimony to its commitment to inculcate a savings culture amongst all Sri Lankans, NDB Savings Star Plus account was introduced in 2012 as an innovative extension which assures a high interest yield in comparison to any other savings product. The product is structured with an interest rate that increases *pro rata* to the balance in the account. Savings Star Plus account holders also enjoy the convenience of account access through more than thousand ATMs island-wide, as well as through all NDB branches across the country.

NDB Real Saver

In line with the national policy of promoting the savings habit amongst all Sri Lankans, NDB spearheaded its national savings drive through *Ithuru Karana Maga* ('The Way to Save'), a booklet that explains the concept and offers practical saving tips as well as ways to conserve national resources, time and the environment by optimizing energy and water use and practising economical household habits.

Building on the *Ithuru Karana Maga* concept during the year under review, NDB presented Sri Lankans with a unique new proposition designed to inculcate a regular savings habit through NDB Real Saver account which yields double the applicable interest on the account balance if a predetermined minimum monthly deposit is made regularly. The launch of this revolutionary saving product was backed by an intensive communications campaign on print and electronic media together with direct marketing, point-of-sale advertising at NDB branches and outdoor advertising.

NDB Real Saver has gained popularity and confidence amongst Sri Lankan public through its innovative yet simple product features while also ensuring the much needed CASA build-up. The product will be further enhanced in a bid to build on NDB's commitment towards the national cause of cultivating a savings culture.

NDB Real Saver

NDB Children's Savings

Nurturing the savings habit in the future generation of Sri Lanka, NDB Children's Savings Accounts offer a free life and permanent disability insurance cover for the account holder's parent or guardian coupled with an attractive gift-offering.

An innovative promotion for young savers was conducted at NDB's Rajagiriya branch in 2012, where the Bank hosted young savers for an open day of fun filled activity and learning focusing on the savings habit. Events of similar nature emphasizing on youth and children have been planned island-wide in 2013.

Management Discussion and Analysis

Children Savings Promotion in Rajagiriya

Product Promotions

Savings Mobilization

Commitment of the NDB staff was captured to the maximum through an internal Staff-Get Member drive conducted in 2012 to mobilize growth of the Savings Star, Savings Star Plus, Current Accounts and Children's Savings Accounts. An ambitious internal promotional campaign was launched to encourage and motivate staff at all levels.

NDB Leasing Riya Pola

NDB Leasing and United Motors PLC joined hands to conduct the first-ever grand automobile fair or *Riya Pola* in Negombo during the year 2012. The event presented a unique experience to its visitors, enabling them to inspect, inquire about or simply admire a wide range of commercial and personal motor vehicles on display. An extensive publicity campaign was launched locally, in order to create awareness on the event and the unique features of the NDB Leasing product.

The growth of the auto finance portfolio was further supplemented by joint promotions conducted under exclusive partnership agreements with leading auto mobile vendors such as Sathosa Motors, Toyota Lanka and United Motors during the year.

'NDB Riya Pola'

Public Relations and Corporate Communications

All marketing initiatives undertaken by the Bank during the year were aptly supported by media releases, media conferences and other PR-based vehicles. In comparison to 2011, visibility of NDB in the public media (By the value of PR activities carried out) increased by 58%, exceeding a value of Rs 30 mn. As a result the Brand managed to secure a total share of voice of 9.6% in comparison to the industry in 2012.

NDB Group's Capital Adequacy Ratio is top of the range, Its 'CAR' at 20.71% signifies stability, the ability to take risk and the capacity for expansion. This is a key strength which allows them to drive change.

One of the best 'CARs' in Sri Lanka!

→ ONE OF THE BEST 'CARS' IN SRI LANKA

Capital Management

A Highly Capitalized Group in Financial Services

The Importance of Capital

Capital Adequacy Ratio (CAR) indicates the entity's capacity to meet credit risks, operational risks, market risks, etc. It also serves to restrain unjustified asset expansion by limiting gearing in terms of risk-weighted assets (a CAR of 10% effectively limits the acquisition of risk-weighted assets to ten times the available capital). A bank with a high CAR can withstand relatively greater losses arising from declines in asset value. The Central Bank of Sri Lanka prescribes the minimum capital resources to be held by banks against these risks. Since January 2008, CBSL has required banks to compute this minimum capital cushion following the internationally-adopted Basel II guidelines.

The primary role of capital is to act as a buffer against possible future losses. The cushion must be large enough to compensate both depositors and senior lenders while still leaving the bank to be able to meet the demands of business. Whenever the world experiences an economic downturn, with its inevitable repercussions on the banking system, we are reminded of the need for strongly capitalized financial institutions. Banks with low levels of equity capital and highly variable operating earnings are especially vulnerable in times of financial distress. More recently, the growing diversity and complexity of risks to which banks are exposed have underlined the need for adequate capital resources. Strongly capitalized banks have greater financial flexibility, enabling them to take full advantage of growth opportunities. From an economic perspective, a banking sector with a strong capital base is better able to supply credit to businesses and fund investment opportunities that encourage growth and create employment, while a weak banking sector inevitably leads to credit and liquidity shortfalls in the financial markets and hobbles the productive capacity of a country's economy. Such large scale implications further explain why regulators have a strong interest in issues of capital adequacy and allocation, and why they focus so much effort on capital regulation.

Provided it has the right human resources, a strongly capitalized bank is better able to promote innovation in the form of new products and services, distribution channels and improved internal processes. Managers are better able to focus on building business rather than on financial difficulties, generating more value for shareholders - and thus attracting more capital resources to the Bank.

NDB Group is a well-structured financial services conglomerate with a capital base of Rs 27.93 bn which indicates a significant increase of Rs 9.50 bn during the year under review. The Group's commercial banking arm, NDB increased its core capital (which represents the value created to its shareholders) by Rs 2.60 bn during the year through increased profitability and a well-managed portfolio. NDB's capital adequacy ratio stood at 12.41% as at 31 December 2012, and recorded an improvement of 1.15% points over the ratio of 11.26% as at the previous year end. The Bank's improved CAR of 12.41% undoubtedly paves way for future expansion supplemented by the strong capital base of the Group.

Management Discussion and Analysis

Gearing and Risk

The return on assets enjoyed by financial institutions is relatively low, hovering around 2%, while among non-financial businesses it can be as high as 20%. However, shareholders expect comparable Returns On Equity (ROE) irrespective of what business they invest in. Financial institutions thus resort to high levels of gearing in order to compensate for their lower asset returns and generate ROEs comparable with those earned by companies in other industries. But higher levels of gearing invariably increase the risks to which the Bank is exposed. The banking industry is highly regulated world over in order to avoid the temptation of over-gearing. The regulatory framework includes stringent capital adequacy requirements which enable bankers to avoid or manage risk while still achieving acceptable returns on equity for shareholders.

Indicators of Stability and Solvency

Apart from its CAR, the Bank monitors several other indicators to measure stability and solvency. These are shown in the accompanying table, with the 2012 figures for the Bank and industry.

	Bank	Industry
Return on Equity (%)	21.2	20.6
On-Balance Sheet Gearing (Times)	9.5	10.1
Equity to Assets (%)	9.1	8.5
Gross NPL to Equity (%)	10.4	26.0
Net NPL to Equity (%)	3.9	15.1
Specific Provision Cover (%)	62	42

Capital Management

Increasingly stringent and complex regulations relating to capital, the growing power of regulators and a regulatory CAR of 10% have made capital the main factor limiting the growth of banks. Banking is fast becoming a capital intensive business, and good capital management is imperative if a bank is to enjoy profitability and growth. Unfortunately, capital is an expensive form of funding and needs to be carefully managed through optimal structuring and reallocation, frequent monitoring, and managing the returns thereon to meet shareholders' expectations.

NDB's capital-management policy is based on these considerations. Periodic evaluations on the adequacy and the structure of the current capital 'cushion' is undertaken by the Board and management with emphasis on business strategy, risk profile and future capital needs. Stress-testing exercises are performed periodically in compliance with CBSL guidelines. For additional prudence, the Bank's internal capital targets are generally set above the statutory minimal.

Notwithstanding the above, the Bank continues to seek new avenues and opportunities to enhance revenue from fee-based activities, which do not require the maintenance of a capital cushion.

The dividend policy of the Bank is based on balancing shareholder expectations with the need to meet the capital demands of future growth which is evidenced in its record of dividend distribution. The prudential practices in dividend policy have enabled the Bank to build a loyal shareholder base which can be relied upon for future capital infusion.

Economic Capital

Economic capital is the amount of capital that a bank needs to ensure that it stays solvent. Economic capital is calculated internally and is the amount of capital the Bank should have to support any risks it encounters. The concept of economic capital differs from regulatory capital in the sense that regulatory capital is the mandatory capital the regulators require to be maintained while economic capital is the best estimate of required capital that banks use internally to manage their own risk and to allocate the cost of maintaining regulatory capital among different units within the organization. In order to ensure banks have sufficient economic capital, the financial regulators have introduced a measurement termed as 'Capital Adequacy' or the measurement of 'Regulatory Capital'. This is in the context of fractional reserve banking and is usually expressed as a capital adequacy ratio that must be held compared to the amount of money that is lent out. These requirements are put into place to ensure that these institutions are not participating or holding investments that increase the risk of default and that they have enough capital to sustain operating losses while still honouring withdrawals.

Accordingly, NDB enjoys a very strong economic capital base, whilst maximizing shareholder return expectations and has maintained sufficient capital over the years to enable future growth opportunities.

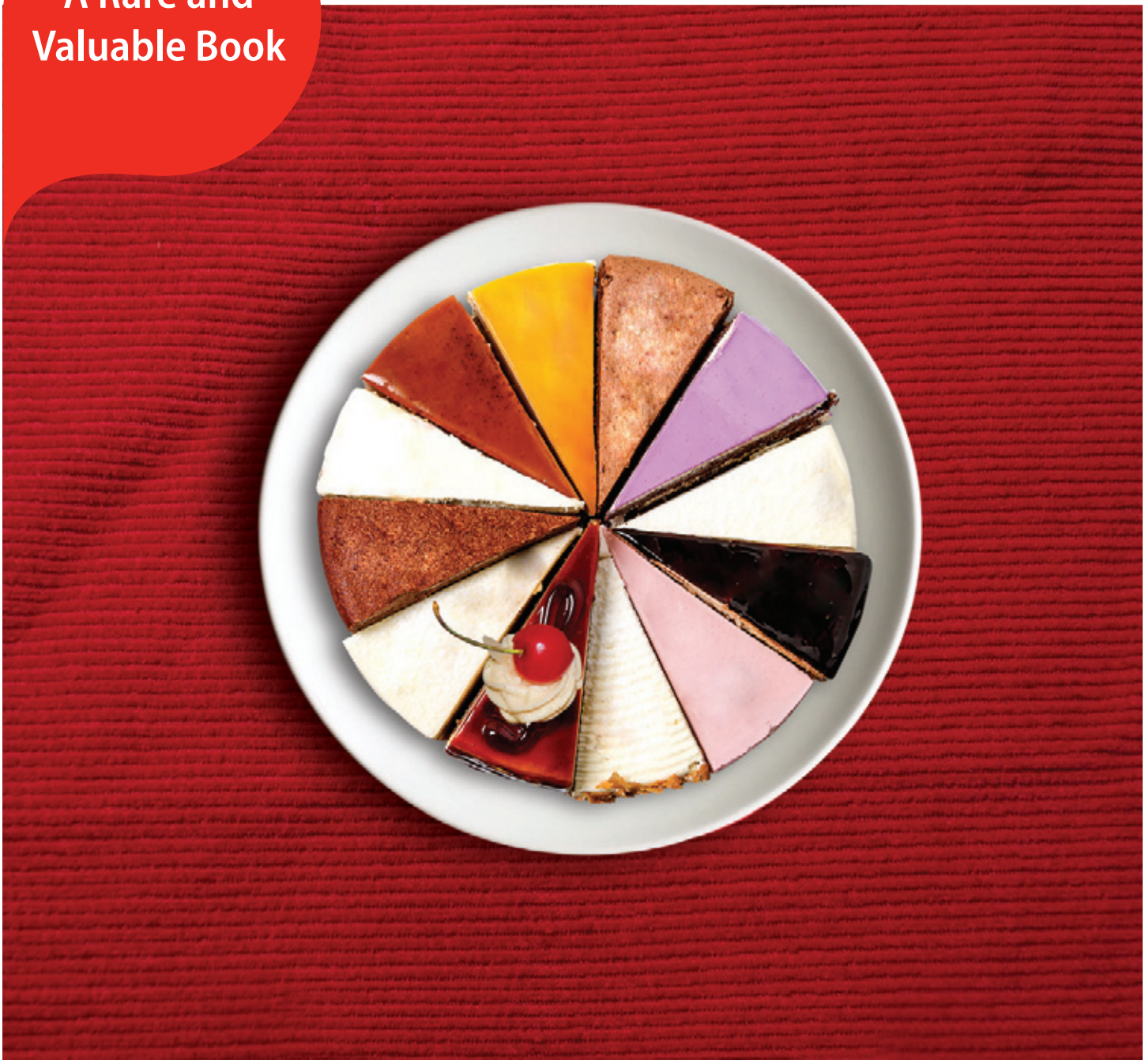
Strength in Depth

A robust Balance Sheet and liquidity in depth indicate the strength of NDB Group and illustrate its capacity to seize strategic growth opportunities. Among Sri Lankan banking institutions, the Group stands in a unique position, since its investment-banking arm and its fully-owned subsidiaries are fee-based businesses for which the operating capital requirements are minimal. The challenge for the Group is to ensure that capital and liquidity from these operations are transferred to the Bank to be utilized in funding strategic growth and optimizing returns to shareholders.

A detailed computation of the CAR of the NDB Group and the Bank is given on pages 319 to 323.

NDB's portfolio quality is the best in the Industry with a very low NPL ratio of 1.31%.

A Rare and Valuable Book



Risk Management

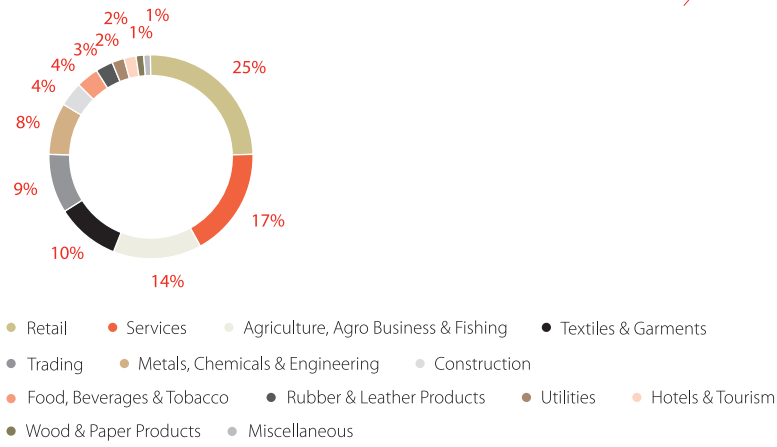
The quality and diversity of NDB's asset portfolio bears testimony to prudential risk management and business practices adopted. NDB's non-performing assets portfolio stood below the industry average throughout the year under review.

Portfolio Quality Highlights

Portfolio Diversification

NDB maintains a well-diversified loans and advances portfolio by placing maximum exposure limits on individual sectors and borrowers in a bid to lower its risk profile and enhance asset quality. The loans and advances portfolio is divided into 12 sectors, with a maximum limit of 15% of total Bank exposure. The retail sector is further dissected, with caps set for every product. The pie chart below indicates the sectorial distribution of assets as at 31 December 2012.

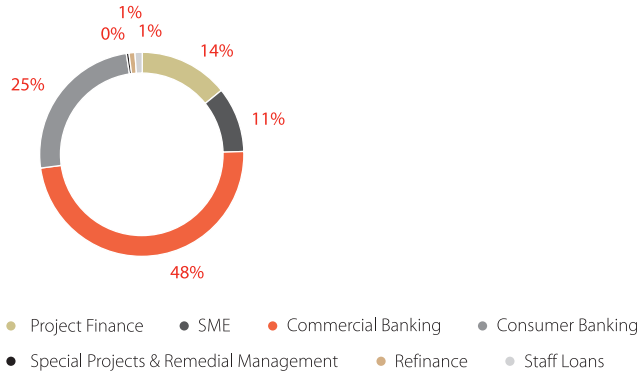
SECTOR-WISE DISTRIBUTION OF PORTFOLIO AS AT 31 DECEMBER 2012



Despite the concentration in commercial banking business, the portfolio illustrates the ongoing growth momentum in consumer-banking assets as a percentage of the total portfolio, in line with the Bank's long-term focus on Retail and SME business.

Management Discussion and Analysis

DIVISION-WISE BREAKDOWN OF PORTFOLIO AS AT 31 DECEMBER 2012



Concentrations

Single Borrower/Group

In keeping with the prudential risk management practices - Single borrower and Group exposure limits are more stringent than those set by the Central Bank. As at December 2012, the Top Ten Exposures accounted for only 15% of the total portfolio and the Top Twenty Clients for only 29%. The aggregate of exposures exceeding 15% of the capital base was 256%, well within the internal limits.

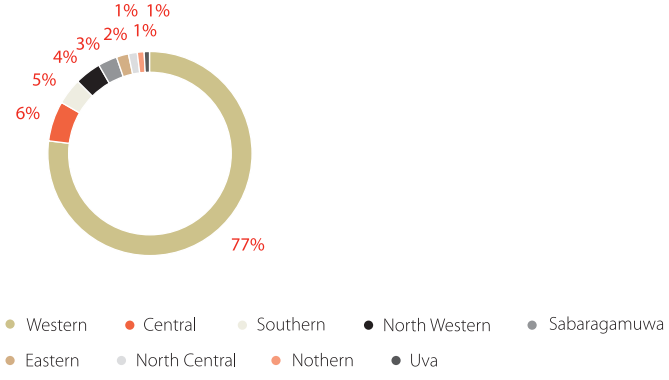
Sectoral

The Herfindhal-Hirshmen Index (HHI) is used to determine the Bank's sector-concentration risk, which is monitored on a quarterly basis. NDB's HHI has declined over the years, and stood at 0.1405 on 31 December indicating a lower credit concentration risk.

Sector	HHI Score as at 31.12.2012
Agriculture Agro Business and Fishing	0.0192
Food, Beverages and Tobacco	0.0013
Hotels and Tourism	0.0003
Metals, Chemicals and Engineering	0.0071
Retail	0.0617
Rubber and Leather Products	0.0007
Services	0.0290
Textiles and Garments	0.0099
Wood and Paper Products	0.0002
Utilities	0.0005
Construction	0.0014
Trading	0.0091
Miscellaneous	0.0001
Total	0.1405

Geographical Concentration

GEOGRAPHICAL CONCENTRATION OF PORTFOLIO AS AT 31 DECEMBER 2012



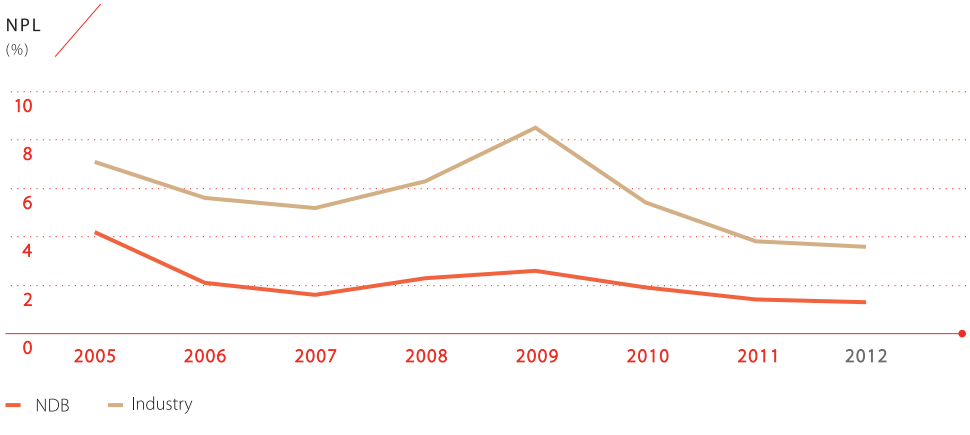
Bank's portfolio was mainly concentrated in Western Province.

Provisioning Policy

In compliance with the requirement stipulated by SLAS 44 and 45, the Bank has identified the probable factors to assess objective evidence on account of individually significant loans and parameters for impairment on a collective basis. Further the Bank also maintains provision records in accordance with the Prudential Guidelines for Licensed Banks issued by the Central Bank. Under three categories, i.e., General provision, Specific provision and Judgmental provision.

Asset Quality

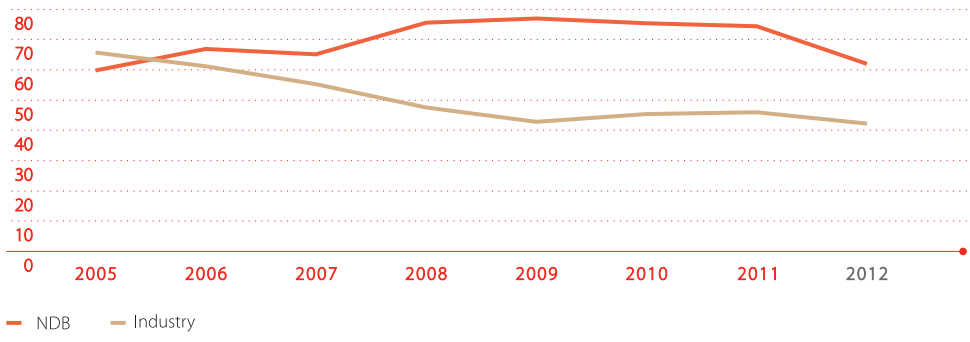
NPL Analysis



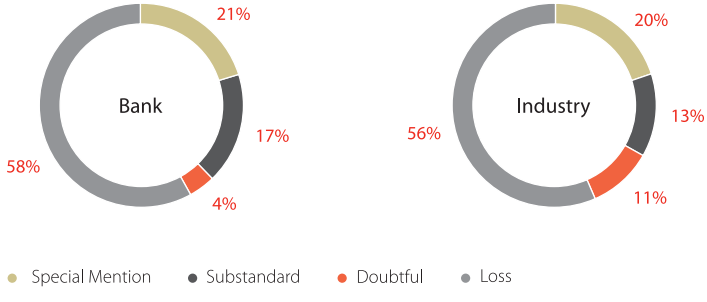
Management Discussion and Analysis

NPLs and Specific Provisioning

SPECIFIC PROVISION ON NPLs



COMPOSITION OF NPLs - BANK VS INDUSTRY



Despite the low NPL base, the Bank's provision cover is higher than that of the industry since the NPL portfolio is concentrated in loss category, requiring higher provisioning. The comparatively low base of cash-backed and pawning portfolios has mandated, a higher percentage of the Bank's performing portfolio being subjected to general provisioning.

Pre- and Post-Sanctioning Assessment

The credit culture of the Bank is based on three interdependent principles: independence, the 'four-eye principle' (meaning that at least two officers must sign a credit proposal) and service function.

Though credit risk is mitigated through demands for collateral, lending decisions are mainly based on credit evaluations carried out by the Bank's relationship managers and then reviewed/approved by the designated approving authority/Group Risk Management. The financial performance of borrowers is continuously monitored and frequently reviewed. Risk Management functions closely with the Bank's business lines throughout the credit appraisal process adding value. A post-sanction review and monitoring mechanism ensures that credit quality is not compromised. Deteriorating credits and other early warning signals are identified and closely monitored.

An independent credit audit unit monitors staff compliance in relation to the approval processes and evaluates the adequacy of controls while identifying areas for risk mitigation and process improvement.

Delegation of Authority

The Board of Directors has delegated approval authority to the CEO, with authority to redelegate limits to the Executive Credit Committees and the Business Lines. Approval limits are based on the individual staff member's experience, the facility type, value and type of collateral and the client's credit rating. Currently, four executive credit committees are functional, each with purview over the main business lines of the Bank. The delegated authority limits are reviewed periodically in line with the business strategy.

Regulatory Developments

Credit risk is the largest contributor to overall exposure and bears the highest risk-related capital charge. Advanced approaches to capital computation for credit risk will have a direct impact in reducing capital requirements. In furtherance of these objectives the Bank has decided to invest in a credit- and market-risk-management solution. In addition to facilitating obligor and facility ratings, risk-based pricing, etc., the proposed solution will also automate and optimize the capital computation process. On the same lines, the Bank has developed an Internal Capital Adequacy Assessment Process (ICAAP) in compliance with the Central Bank directive on 'Integrated Risk Management Framework'.

Outlook

NDB will continue to maintain superior asset quality through prudential risk mitigation and operational processes whilst focusing on growth sectors of the economy.

To keep pace with the revival of the economy and Bank's commitment to cater to a wide clientele spanning across all geographies risk processes will be further refined with credit models subject to periodic revalidation, regular portfolio stress tests, and appropriate internal and external training for the business line involved at various stages of the credit process.

NDB Group, with its roots in Development Banking, continues to foster National Development. Its uniquely talented human resources base, the wide array of financial solutions and commitment to promote entrepreneurship, can realize all your dreams, be it a cottage industry or a gigantic infrastructure investment.

Got the Wheels for the Long Haul

→ THEY GOT THE WHEELS FOR THE LONG HAUL

The Bank recognizes three categories of corporate social responsibility - strategic, philanthropic and operational. Focusing on long-term social and economic value, the strategic CSR initiatives of the Bank are in the areas of education and entrepreneurship. Integrating these initiatives with the Company's business objectives NDBs goal is to promote national economic growth. Philanthropic initiatives focus on uplifting society's most vulnerable where the commitment to social responsibility also informs our behaviour as an employer. Operational initiatives concentrate on how we manage the wider social and environmental impacts of what we do with a focus on optimizing resource utilization and minimizing the negative impacts of the Bank's operations.

The Roots of Responsibility

An ethical approach to doing business, one that shows consideration for others, for the communities that surround us and for the environment, has been shown over and over again to make good business sense in the long term. Since NDB is in business for the long haul, the Bank's policy is to maintain the highest levels of integrity, responsibility and accountability in its operations and conduct.

The Corporate Governance Section of this report (pages 176 to 199) outlines the principles, systems and procedures set in place to ensure full and constant compliance with this policy. The Compliance Policy and Code of Conduct of the Bank clearly state the standards of responsibility and ethical conduct expected of NDB employees in their professional capacity.

Responsible Lending

At NDB, incorporating environmental and social due diligence into the lending process is a key aspect of the Bank's social responsibility efforts, This effort is supported by the Bank's 'Environmental and Social Management System' (ESMS) which is in operation since 2008. The ESMS is used to identify and asses environmental and social risks of the projects and businesses the Bank finances, where the identified risks are addressed at an early stage of credit evaluation. Businesses and projects must be compliant with all relevant environmental and social laws and regulations to qualify for the Bank's funding. In addition, the Bank encourages customers to approach sustainability issues on a 'best efforts' basis with the support of the ESMS.

The objectives of the ESMS are -

- to identify and assess adverse environmental and social outcomes of the project or business,
- to avoid or to minimize, mitigate or compensate for these outcomes,
- to promote improved environmental and social performance in the businesses and projects to which we lend through the effective use of suitable management systems.

ESMS is an integral part of the Bank's credit policy and the credit evaluation process in long-term lending. A five-member, cross-functional team is responsible for day-to-day ESMS operations and all relevant staff are familiar with its requirements.

Socially Responsible Products

NDB holds to a strategic CSR policy of supporting education and entrepreneurship. Many of the Bank's products are designed in conformity with this policy, yielding benefits for our customers that go beyond mere financial aspects. A few examples are given below:

NDB Jeevana Livelihood Training/Loan Scheme

Sri Lanka was experiencing three decades long civil war which ended in the year 2009 opening numerous livelihood development opportunities for displaced and affected people in the Northern and the Eastern Provinces of Sri Lanka. Both public and private sector involvement in the ensuing developmental effort in the two provinces created vacancies for a large number of skilled jobs but unfortunately there appeared to be a large vacuum in sourcing skilled workers.

Identifying this gap NDB commenced a project in these regions offering unemployed youth aged 18-35 training opportunities in sectors the Bank has identified as having long-term employment potential, such as hospitality, motor mechanics, construction and nursing. The Bank provides the required uniforms, tool kits etc., for training free of charge and also assists the youth with improving their English language skills. With the success of the project in the North and the East the project was expanded to the South and will be further expanded to other areas as per the need.

Considering that the students are from rural areas and are not familiar with banking products and dealing with banks, NDB formulated this project so that it would bring greater benefits to the youth. Thus financial inclusion was brought in as another aspect of this project and the project included a loan component where the selected students are granted a loan covering the training cost together with a monthly stipend to cover travelling, food costs etc. The loan repayments commence once the students successfully complete the training programme. Through this mechanism the students learn how to save, how to operate a bank account, how to obtain a loan, the discipline of timely repayments and overall how to liaize with a bank for their financial needs. Another objective of the Bank was that the students should feel that they earned this opportunity themselves by paying for this, which would give them a sense of satisfaction and pride as well as inculcate values such as integrity, care and passion which are the very values the Bank lives by. Anything given free soon loses its value, whereas anything a person works hard for will never lose its value it would only grow in value.

Jeevana Livelihood Training Programme

Divi Aruna Loan Scheme

Divi Aruna empowers small entrepreneurs across the country, enriching and building opportunity for them and for the communities in which they live. The loan scheme with flexible repayment terms, attractive pricing and the convenience of ATM accessibility targets fisheries, small agricultural and dairy enterprises and small-scale industries.

A special feature of the *Divi Aruna* scheme is its built-in savings component. A regular cash deposit is set aside from the loan principal and invested in the borrower's savings account. This promotes the saving habit and helps customers maintain financial responsibility in a sector where circumstances often make this difficult for borrowers.

NDB *Divi Aruna* Embilipitiya

SME Banking

A pioneer of SME financing in Sri Lanka, NDB Bank believes that a culture of enterprise is key to sustainable development. The Bank has to date financed over 100,000 ventures and created over a million employment opportunities islandwide. More information on NDB's support for SMEs appears on page 27 of this report.

Strategic CSR

The Bank's strategic CSR focus is education and entrepreneurship. To this end, NDB has established an Endowed Chair in Entrepreneurship at the University of Moratuwa and also supports a programme that allows enterprising undergraduates to try their hand at starting and running a business while still at university. Key CSR initiatives under education include the English communication programme for secondary school teachers and the library project.

NDB Chair of Entrepreneurship

To help promote understanding between the very diverse worlds of academia and industry, the Bank endowed a Chair of Entrepreneurship at the University of Moratuwa, the first such tenured position in Sri Lankan academia. The University's first Professor of Entrepreneurship was Professor A K W Jayawardena, who accepted the chair in September 2010. With his appointment as Vice Chancellor of the University of Moratuwa, Senior Fellow Nishantha Nanayakkara who is also an entrepreneur and a one-time client of the Bank, accepted the chair in October 2012.

The main objects of the endowment are four in number -

1. To develop an entrepreneurship culture within the University
2. To develop entrepreneurship-education programmes and teach entrepreneurship
3. To undertake research and develop a research base in entrepreneurship
4. To help the University produce job creators

Entrepreneurship Training for University Students

In partnership with the University of Moratuwa and the Young Entrepreneurs Sri Lanka (YESL) organization, NDB sponsored a course of entrepreneurship training for university students - the first such effort directed at this group.

The Young Entrepreneurs Business Programme provides students with training on practical business, economics and entrepreneurship concepts and, gives them an opportunity to set up and operate their own businesses. Training, provided by the YESL, covers all aspects of running a business, from formulating a business plan through registration and setting-up, operations, marketing, etc., all the way to liquidation. The project cycle is 8-10 months, though successful businesses are encouraged to continue. During this time, the aspiring entrepreneurs acquire practical, first-hand experience of the world of business and the responsibilities of management.

Signing of the Agreement with University of Moratuwa

English Communication Programme for Secondary School Teachers

In an effort to mobilize the strategic view on sustainability, NDB joined hands with the British Council of Colombo on a special project to enhance the teaching skills of Secondary English Language Teachers of Government Schools; thereby increasing the standard of English teaching in Sri Lanka. The programme was conducted in several parts of the North-Western Province in partnership with the Ministry of Education and the Provincial Education Department. English teachers from several Government schools in the region, nominated by the provincial department were enrolled in the 50-hour Master Training Course. The course concluded with an award ceremony where 120 English Teachers passed out with Certificates in Secondary English Language Teaching (CiSELT), a qualification validated by the British Council.

English is the universal tongue of the current global marketplace and has become the passport to wealth and opportunity, an essential requirement for almost every profession. Proficiency of this universal language is critical for the success of businesses and the economic progress of the nation. Therefore today, English language has become an essential component in a child's curriculum and the foundation is set at an early age at school. Teachers who nurture our children play a pivotal role in setting high standards of language proficiency in our future generation. With initiatives such as this programme NDB strives to empower the teachers in the country to provide a higher quality education and thereby raise the bar for education in Sri Lanka. This initiative helps to uplift the standard of education and make a positive contribution towards this national endeavour.

Award ceremony - English Communication Programme for Secondary School Teachers in the North Western Province

Library Project

Good English-language skills are both widely desired by Sri Lankans and recognized by policymakers as the key to developing of a globally competitive labour force. NDB, promotes the improvement of English through reading in partnership with the Asia Foundation donating educational volumes in English to schools across the island. This on-going project is carried out through the Bank's branch network since 2008, helping to build good Bank-community relations. The books donated include volumes of general interest as well as texts on subjects such as mathematics, science, health, natural history and geography. Advanced texts in mathematics, science, natural history and other subjects were also donated for the benefit of the pupils in higher grades. Books were donated to over 40 schools in the year under review.

Green Financing

Lending for Renewable Energy, Pollution Abatement and Pollution Control

The Bank's Renewable Energy for Rural Economic Development Project (RERED) loan scheme offers financing for renewable-energy projects that will replace and help conserve non-renewable resources, often reducing pollution and negative environmental effects at the same time.

The E-Friends loan scheme is an external line of credit promoted by the Bank and specifically dedicated to funding pollution abatement and control. Loans are offered for 'end-of-pipe' effluent treatment and emissions control installations. The scheme also funds workplace safety measures, particularly with regard to the control of hazardous substances and noise, as well as the relocation of highly polluting industries to special estates equipped with waste treatment facilities, the treatment facilities themselves, and the purchase of pollution-control equipment. Funds under this loan scheme are presently fully committed.

NDB also funded the country's first ever commercial wind power project in 2009 with two more projects funded thereafter, as well as a number of mini-hydropower projects.

Customer Satisfaction

Business sustainability depends on satisfied customers. NDB monitors customer satisfaction with annual surveys, undertaken on behalf of the Bank by Lanka Market Research Bureau (LMRB). A dedicated Customer Quality Champion is tasked with improving process efficiency and implementing continuous improvement across all customer touchpoints. Systematic improvements in customer-service standards and the efficiency of branch operations were undertaken during the year under review. All front-line staff at NDB are trained in good customer interaction and continuously monitored to ensure positive customer outcomes at each interaction. An online complaints and suggestions tracking system helps ensure that all customer concerns and complaints are addressed and appropriate action is taken to the best of the Bank's ability. In addition, customers are regularly canvassed at point of delivery to assess their levels of satisfaction. Feedback received is passed through the appropriate channels for decision and action.

Realizing Operational Synergies

Several cross-functional teams, their members drawn from various companies within the Group, are tasked with identifying strategic initiatives for value creation, product innovation and synergies between Group companies, divisions, etc. These teams both operationalize and drive Group strategy through the implementation of key initiatives across business sectors and customer segments, developing customized products and channels and leveraging the Bank's competitive strengths.

NDB encourages staff innovation and idea-sharing through an IT-based 'suggestion generator', IdeaXpress. All employees have access to this application, through which they share innovative ideas and customer insights with their colleagues and superiors.

Operational CSR

Energy-Saving Measures and Renewable Energy Use

To save on operating costs, preserve valuable resources and help control carbon emissions, NDB has taken a number of steps to reduce its energy use. NDB's energy-conservation measures are based on an energy audit carried out by Lanka Transformers in 2009. Energy use across the Bank network is monitored daily at NDB and monthly comparisons are undertaken to identify deviations from the conservation regime.

Specific measures taken to save energy at NDB are discussed below:

Air Conditioning

In a tropical climate, office air conditioning consumes more energy than any other requirement. NDB uses the most efficient type of air conditioning system, a chilled-water-based central plant, at its head office. The plant can be switched off ½ hour before the end of the working day without compromising customers' and employees' comfort. Currently, the practice is to shut down this unit at 4.30 pm on every working day.

The plant is not activated on weekends. Departments such as IT, Administration, Marketing, Sales and the Call Centre, which need climate control even at these times, use a backup split-type unit. Further savings are effected by adjusting temperature settings to suit the ambient weather and temperature conditions, for example during the rainy season.

Lighting

Magnetic ballasts on all fluorescent light fixtures were replaced with electronic ones in 2011. The most energy-intensive fixtures were replaced with energy-saving units that deliver higher lighting output in relation to energy consumption while actually improving visibility.

NDB also practises the simplest and most effective conservation method of all: ensuring that all lighting and air conditioning in customer service areas is switched off once the Bank is closed to customers for the day.

Other Conservation Measures

- Capacitor banks have been installed to reduce peak power demand, smoothing out power 'spikes' and avoiding unnecessary electricity drawdown.
- Power factor correction instruments have been installed in most of the Bank's UPS units.
- Many vehicles in the Bank's fleet have been converted to run on LP gas, significantly improving NDB's carbon footprint.
- The Head Office colour scheme emphasises light, reflective colours, reducing the need for artificial lighting.
- The Bank's standby generators are used only during power-supply interruptions.

Waste Reduction and Recycling

The Bank also has in place a broad range of measures to control waste and recycle materials.

Significant among these are -

- Taxi pooling - Following an internal study of vehicle use, mainly taxicabs, for official purposes, a number of cost savings was effected by 'pooling' cabs for late-working employees travelling in the same direction after hours.
- Waste Paper Recycling - Waste paper generated as part of the Bank's day-to-day operations is recycled under contract with Neptune Papers, a recycling company. In 2012, 26,316 kg of waste paper was recycled, a carbon-equivalent saving in greenhouse gas emissions of 26,316 kg. This was the equivalent of
  - 447 Fully Grown Trees
  - 836,322 Litres of water
  - 105,264 kwh of Electricity
  - 46,185 Litres of Oil
  - 79 Cubicmeter of Landfill
- Paperless Operations - NDB also promotes a paperless culture. Employees are encouraged to use electronic communications, online approvals and other web-based applications, printing out documents only if hard copies are strictly necessary.

Process Innovation

NDB makes further resource savings by developing process improvements. Automated document workflows both minimise paper usage and greatly improve turnaround time. Paperwork generated by the automated credit-approval system, for example, is nearly zero. Approvals, disbursements, memos etc., are all processed online.

Disposable Assets

Obsolete physical assets, such as computers and furniture that are still in working condition are donated to deserving institutions.

Under the Lexmark Recycling Programme, used toner cartridges from the Bank's Lexmark printers are collected and recycled by the brand agents. Similarly, mobile phones supplied to employees are recycled, along with their used batteries, by the telecom service provider, which has its own recycling programme to take care of this type of hazardous waste.

Assets that are beyond use or repair are disposed of responsibly. For example, used computers are disposed of to parts recyclers. The Central Environmental Authority has provided a list of electronic-waste-disposal firms of certified repute, and the Bank is taking steps to ensure that all unusable electronic assets are disposed of exclusively through these firms in the future.

Philanthropic CSR

The Prevention of Child Abuse Trust

Child abuse is a social evil all over the world, taking different forms in different cultures. NDB is committed to the elimination of this evil in Sri Lankan society through the Prevention of Child Abuse Trust (PCAT), which was founded in 1997. The Trust comprises of volunteers and the Bank's CEO, with many internal volunteers assisting with the activities related to the Trust. Working closely with the Department of Probation and Child Care, the Trust is committed to help eradicate child abuse by raising awareness of the problem. The Trust conducts awareness programmes for parents, school teachers, school principals and other caregivers in regions where a high incidence of child abuse has been reported. Special awareness programmes are also held for children.

These programmes are aimed at educating participants on what constitutes child abuse, its effects and how to deal with it. Topics discussed include methods of prevention, action in case of an incident, legal issues, and available resources such as help centres for children. All programmes are conducted by qualified resource personnel from the Department of Probation and Child Care. The Trust has also conducted training programmes for caregivers. A unique feature was the Art Therapist programme conducted for the teachers, social workers and counsellors. This unique programme conducted by a renowned international art therapist is specially designed for social workers, caregivers and teachers who deal with abused children and is a very successful indirect method which deals with the sub conscious mind. Most often children are reluctant to talk about traumatic experiences. However they express their feelings better through art and play display. Thus NDB sponsored the Art Therapist programme with a vision to equip caregivers to assist abused children in their healing process and help them move beyond their traumatic experience into a better future.

Awareness Programme on Prevention of Child Abuse

NDB Bank Cancer Aid Trust Fund

NDB launched the NDB Bank Cancer Aid Trust Fund in 2007 in partnership with the National Cancer Hospital at Maharagama. The objectives of the Fund are to provide financial and related assistance to cancer patients who are unable to afford treatment and help maintain the well-being of patients undergoing treatment at the country's cancer hospitals. A substantial amount has been spent to date on the purchase of essential surgical and therapeutic equipment; in the year under review, NDB contributed a total of Rs 2.0 mn to the Fund.

Supporting Orphans

In partnership with the Women's Development Federation, Hambantota, the Bank provides a monthly stipend to forty deeply impoverished children orphaned by the 2004 tsunami. The sum goes towards their education, health and nourishment. Previously, the Bank opened savings accounts for these unfortunate children, granting them a measure of future financial security.

Solar Study Lamps for Students

With the end of the military conflict numerous persons were displaced. After being released from the camps these families returned to destroyed homes, schools, and livelihoods. In this climate, there were thousands of children attempting to prepare for the O/Level and A/Level Examinations. The majority were struggling to study in temporary shelters or damaged housing with no access to electricity, using either candles or kerosene lamps. The use of candles and kerosene lamps in these temporary homes made of cadjan also creates a dangerous situation. In many instances the family is so poor they do not have the money to purchase lamps/candles for their children. Despite these difficulties, education accorded a very high priority. Poor quality lighting from kerosene lamps creates difficult and unhealthy conditions for studying. In contrast solar-powered LED study lamps offer a uniform bright lighting ideal for studying. However purchasing such a device was not a possibility to these students. Addressing this need NDB donated 1,500 solar lamps to students identified by the Bank's Branch in Vavuniya.

Donation of Solar Lamps

Employee Volunteerism

At NDB, sustainability is deemed as a strategic priority and the Bank continuously endeavours to foster sustainability across all its business decisions and activity. In setting this philosophy into action, NDB ranks 'Responsible Behaviour' as an integral element of the Bank and promotes an altruistic culture amongst its employees by encouraging employee volunteerism to make meaningful benefactions to the society. We share below the highlights of the projects carried out by our very own employees.

Staff Voulnteerism - Refurbishing the Schools Furniture at Tissa Maha Vidyalaya Trincomalee - Treasury, Cards and Privilege Banking Team

Staff Volunteerism - Spending time with the Visually Differently abled - Administration and Marketing Team

A Truly Empathic Team

An NDB'er is a special kind of person - a person with empathy who can visualise needs and offer one-of-a-kind service level - across the Board.

→ A TRULY EMPATHIC TEAM

NDB's winning formula centres on the commitment and the passion of its employees who are the key drivers of NDB's business strategy. Based on this presumption, NDB HR continuously strives to exceed the expectations of its stakeholders by providing superior HR solutions.

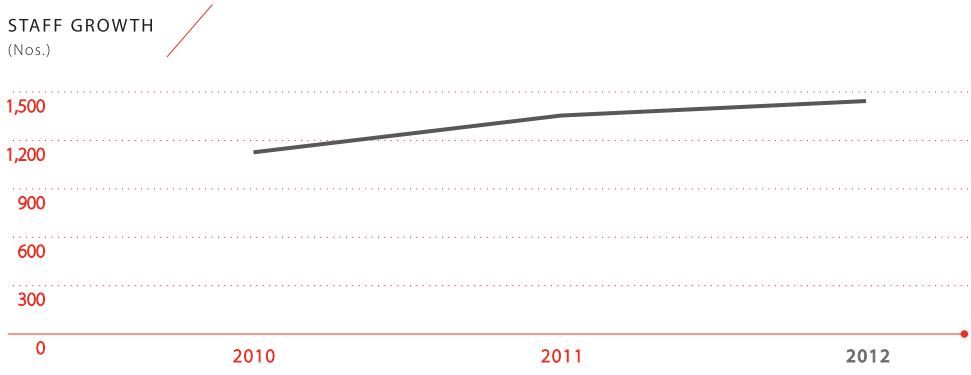
Operational Excellence → Value Creator → Most Respected Function → Employer of Choice

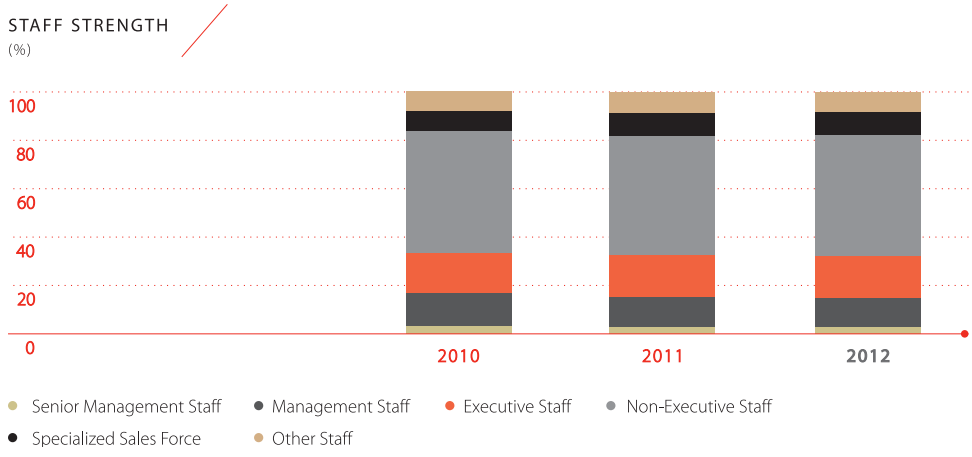
NDB also believes that success in the future depends on being lean, agile and spirited in a resource-challenged world. On this premise NDB HR has continued to give priority for strategic focus on talent management and organizational capability development while systematizing and controlling the cost of transactional work. Over the period of the past three years, NDB HR has transformed itself to an integral function that innovates better through operational excellence and takes full advantage of our strengths and opportunities to project.

Managing Diversity

Managing diversity focuses on maximizing the ability of all employees to contribute to our goals irrespective of the different ethnic backgrounds, religions and ages into one cohesive and productive group. Managing diversity therefore has evolved to be a part of NDB's culture and we take pride in our achievements as we celebrate our differences.

Today the NDB family comprises over 1,400 employees with a staff growth of 30% year on year as illustrated below:





NDB boasts of a unique blend of employees which is becoming increasingly diverse, with a greater number of Non-Executives and over 71% of professionally qualified staff.

For the year under review, NDB recorded 61% of male employees and 39% of female employees for whom identical working conditions have been offered irrespective of gender differences.

Seeking the Right Talent for the Right Job at the Right Time

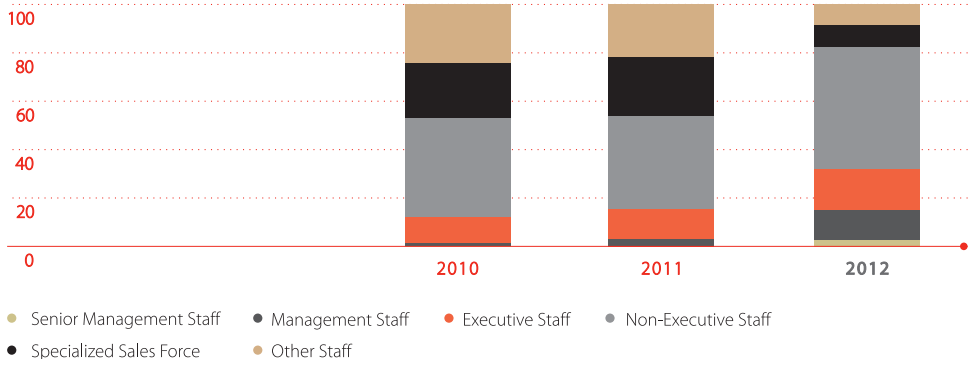
Attracting, developing and retaining talent has been the prime focus in reaching our Group's ambitions which is achieved through constant audit of the skills and leadership needed across every cluster.

We adopt a strategic orientation to the recruitment process which is designed to identify, develop and retain people with outstanding talent considering the long-term needs of the organization. Being an equal opportunity employer that thrives on a culture of meritocracy, priority is given to internal candidates in filling positions thereby extending our employees the opportunity to climb their career ladders.

The infusion of fresh talent has received much deliberation at NDB. Hence, career fairs, recruitment drives in the North and the East, unique management trainee recruitment initiatives have been implemented from time to time. During the year under review, leading tertiary institutions in the country were explored to source credit officers thereby, infusing new blood and new thinking to the organization in a changing, growing, diversifying business context.

Thus, it is evident that we maintain a balance of internal and external selection. Equal opportunities for both internal and external applicants are applied in a transparent manner.

STAFF RECRUITMENTS
(%)

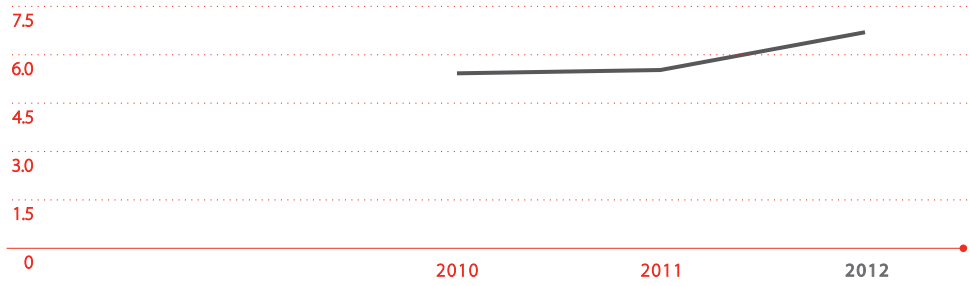


Harnessing Talent

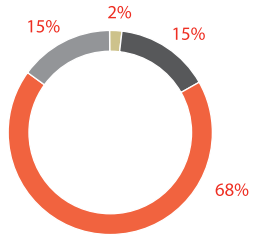
Continuous learning has been considered as an enduring process at NDB. Encouragement is extended to optimize and sharpen individual strengths and talents to maximum in furtherance of career prospects.

It is noteworthy that in 2012, NDB's average training days stood well above the industry average recording an increase of 21% year on year to 6.7 days per employee. During the year under review, an impressive figure of 321 training programmes were conducted at NDB.

AVERAGE TRAINING DAYS PER EMPLOYEE (2010-2012)
(Days)

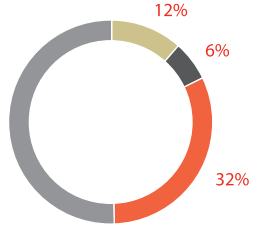


TRAINING OPPORTUNITIES



Foreign Training · In house - Foreign Faculty Brought Down · In house - Other · Local Training

NUMBER OF TRAINING PROGRAMMES



Foreign Training · In house - Foreign Faculty Brought Down · In house - Other · Local Training

It is with pride that we publish that nearly 567 employees being 50% of the permanent cadre of NDB have had the opportunity to experience foreign faculty driven training programmes from leading international training institutions during 2012.

IT Team on an Experiential Learning Programme

Fostering on the concept of an "University Within" working environment, NDB created history by partnering with the Institute of Bankers of Sri Lanka, an apex banking body to offer unique training programmes such as Diploma in Credit Management, Diploma in Treasury and Risk Management, Certificate Course in Branch Operations and Certificate Course in Branch Banking exclusively for NDBers internally. Over the past 2 years, over 20% of our permanent employees have obtained these qualifications amidst their busy work commitments through this endeavour, which is noteworthy.

An Inspring Moment - IBSL Certification

NDB e Learning platform extends our employees the opportunity to learn at their own pace and convenience, irrespective of the geographical restrictions with no interference to their work responsibilities with real time evaluations. This empowers the employees to take control of their own development.

Subsequent to the establishment of this Knowledge Management System the necessary infrastructure and training was extended to staff to optimize the benefits of the system. Simultaneously, processes were also established for users to complete modules within a specified period, face assessments and win awards. During the year under review, 825 employees benefitted from e Learning-based programmes. NDB's concept of e Learning is to support employees in career advancement without making it mandatory. It was encouraging to note that staff response to e Learning has been substantial recording a high percentage of 70% of staff utilization of the platform for training and knowledge sharing.

Further, NDB possesses a state-of-the-art training centre which records over 75% utilization rate inclusive weekends bearing further testimony to the staff and management commitment on learning and development.

Performance Culture - Encouraging Exceptional Performance

Encouraging every employee to grow to his or her full potential has been emphasized resulting in a promotion rate of 16%-20%. The new performance-based reward structure recognizes people not only with operational excellence but also with entrenched values. The performance appraisal process was revisited in 2012 with the assistance of external consultants 'Towers Watson' in response to the feedback received through employee satisfaction surveys.

Compensation and its interconnectivity to talent and performance management have been under serious consideration during the year 2012. On this premise to encourage exceptional performance, the existing variable pay scheme was revisited and a new scheme will be implemented effective in 2013 in a bid to be on par with industry practices.

Nurturing Unity and Family Spirit

Camaraderie, togetherness and team spirit are fostered through the events organized by the Staff Recreation Club and NDB HR emphasizing on the physical, mental and emotional well-being of its employees.

In furtherance of the initiatives designed to improve the health, safety and well-being of our staff, NDB also extends a wide array of recreational activities to enable employees pursue their interests and find ways to unwind.

In keeping with the Asian traditions, the family unit has been extended pride of place in our recreational and social activities. Therefore, most of our social events are open to families. During the year under review, special events such as the Kiddie's Art Competition, the British Council Communication and Presentation skills workshop for NDB Juniors, '*Lama Lokaya*'-an awareness programme on child protection rights highlights some of the planned events in our calendar. NDB HR will continue to introduce and implement better initiatives to create a fulfilling and contended work environment.

From Vision to Reality

Over the years, NDB HR has outlived its traditional role of being an administrator of HR functions to be an active crusader of the Bank's business strategy. The accolades that NDB HR has been recognized with, bear ample testimony to this success story.

ISO 9001:2008 Certification

NDB HR created history by being the first HR department in the banking industry to obtain ISO 9001:2008 certification for all processes and procedures relating to HR functionalities.

Financial Review

Financial Performance

The Bank and the NDB Group performed exceptionally well in 2012, as a result of a favourable macro economic environment. The Bank was able to achieve these commendable results amidst a highly competitive interest rate environment that prevailed during the year and the ceiling on credit growth of 18% imposed by the Central Bank of Sri Lanka.

The performance of the Bank and the Group for the year ended 31 December 2012 is summarized below:

	BANK			GROUP		
All figures in Rs mn	**2012**	2011	Var %	**2012**	2011	Var %
Net interest income	**5,674**	4,561	24	**5,896**	4,909	20
Core banking profits	**3,883**	3,298	18	**3,883**	3,298	18
Net operating income	**8,709**	6,640	31	**14,887**	8,010	86
Profit before Financial Services VAT	**4,607**	3,110	48	**10,391**	4,030	158
Profit after tax	**2,924**	1,831	60	**8,932**	2,763	223
Profit attributable to shareholders	**–**	–	–	**8,854**	2,527	250

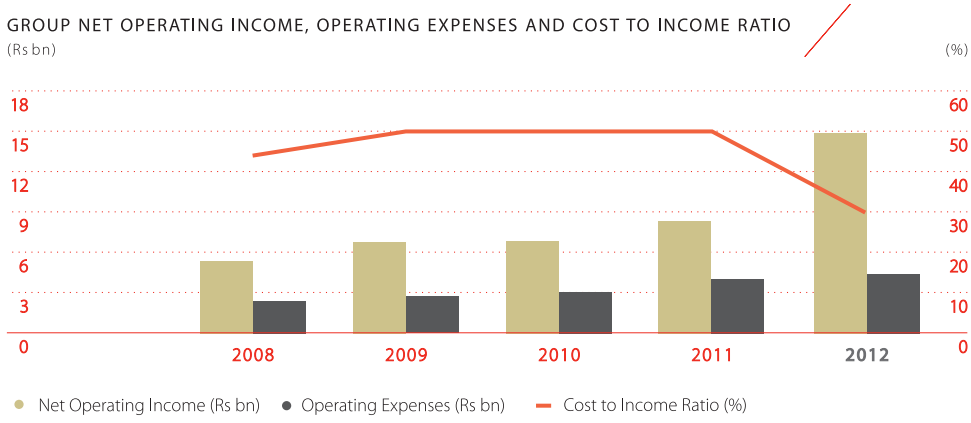
The Bank's Profit before Financial Services VAT and the Profit after Tax grew significantly by 48% and 60% respectively over 2011, with its asset base recording an increase of 18% over 31 December 2011. However, it is noteworthy to mention that the share of profits available for shareholders at the Group level increased significantly by 250% to Rs 8.8 bn due to the capital gain of Rs 6.0 bn generated as a result of the divestment of the investment in AVIVA NDB Insurance PLC to American International Assurance (AIA) Company Ltd. of Hong Kong during the fourth quarter of 2012, the details of which are given below.

The strategic rearrangement within the Group that took place during the year resulted in the divestment of NDB's investments of NDB Investment Bank Ltd., NDB Stock Brokers (Pvt) Ltd. and of the 5% direct holding in AVIVA NDB Insurance PLC, to NDB Capital Holdings PLC (formerly known as Capital Development and Investment Company PLC). Following this strategic rearrangement of investments within the Group, NDB entered into a Share Sale and Purchase Agreement with AIA Group Ltd. (AIA), headquartered in Hong Kong, whereby NDB Group agreed to sell its shareholding in the AVIVA NDB Holdings Lanka (Private) Ltd. to AIA. Through the transaction which reached finality in December 2012, NDB Group earned a net receipt of US$ 59 mn. With the aim of continuing to provide a wide array of financial services under one roof, NDB also entered into an exclusive Bancassurance Agreement with AIA for a period of 20 years. Pursuant to this transaction, NDB entered into a second transaction to purchase the balance of the shareholding of NDB AVIVA Wealth Management Ltd. from AIA. NDB Capital Holdings which now owns 100% of the Wealth Management arm of the Group will be able to harness the strengths of its portfolio, thus consolidating its position as the market leader in Wealth Management in Sri Lanka.

Financial Review

Accordingly, the results of NDB Investment Bank Ltd., NDB Stock Brokers (Pvt) Ltd., NDB Capital Holdings PLC, Development Holdings (Pvt) Ltd., NDB Capital Ltd. (Bangladesh) and NDB Wealth Management Ltd., representing the spectrum of Group businesses, have been consolidated.

GROUP NET OPERATING INCOME, OPERATING EXPENSES AND COST TO INCOME RATIO



Net Interest Income (NII)

NDB's NII of Rs 5,674 mn increased by 24% over the previous year. The Bank was able to achieve this growth with conscious monitoring of the yields of the lending products and the product mix in a highly competitive interest rate environment. The Bank's Net Interest Margin (NIM) increased from 3.70% in 2011 to 3.76% in 2012, whilst there was a marginal decline in NIMs in the industry. At the NDB Group level, contribution to NII primarily came from the interest income from surplus funds earned by the Group companies.

Net Operating Income

The Net Operating Income, which includes NII, fees, commissions, trading income and equity income adjusted for impairment losses increased by 31% at Bank level and 86% at NDB Group level over the previous year. Net Trading Income of the Bank which consists of forex income and trading income from equities increased significantly by 78% primarily due to the devaluation of the Sri Lankan Rupee against foreign currencies. Other Operating Income of the Group included the capital gain of Rs. 6 bn earned from the divestment of the investment in AVIVA NDB Insurance PLC to American International Assurance Company Limited of Hong Kong during the fourth quarter of 2012.

Operating Expenses

Operating expenses of Rs 4,496 mn of NDB Group recorded an increase of only 13% over the previous year, out of which the Bank's operating expenses increased by only 16% despite the Bank increasing its branch network by 9 during the year. NDB's good cost management practices resulted in the Cost to Income Ratio of 49% improving from 52% in 2011 and compares well with the industry average.

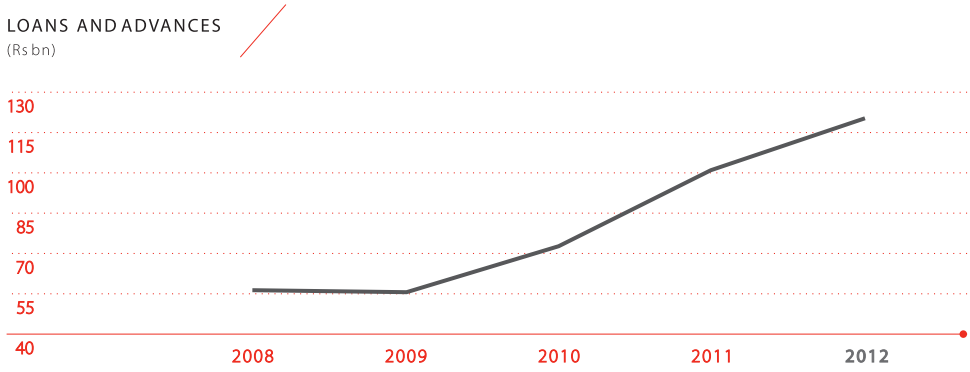
Impairment Charges for Loans and Other Losses

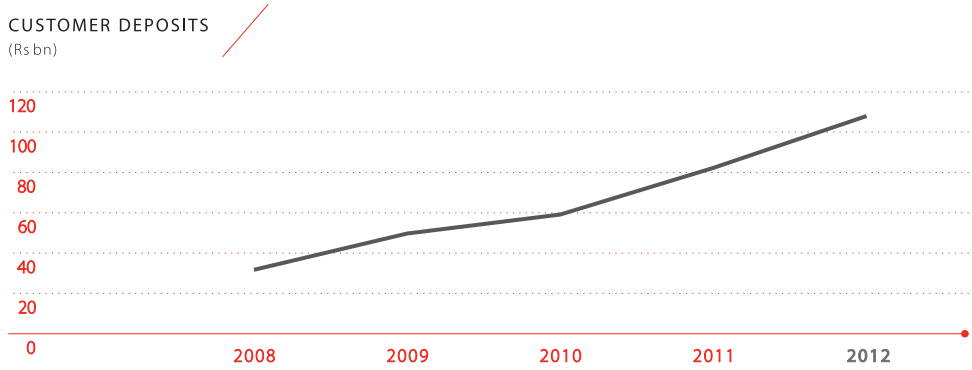
The provision made for impairment and other losses was Rs 106 mn as compared with Rs 68 mn for the previous year. The Bank's impairment provision includes a specific provision based on risk assessments on individual loans and a collective provision made considering the economic factors relevant to each portfolio segment and is in line with the Sri Lanka Accounting Standards adopted by the banks in 2012. Settlements made by borrowers and improved performance levels of the respective borrowers was considered in assessing the risk level of each borrower.

Portfolio Growth

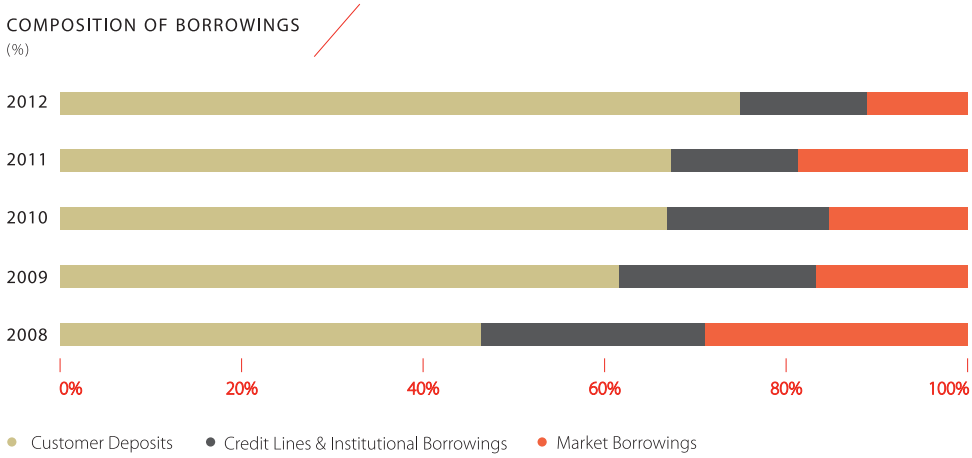
The Bank's gross loans and advances were Rs 120 bn as at 31 December 2012 and recorded a growth of 17% over the previous year mainly on account of growth in the SMEs, agriculture and the service sectors through the branch network of the Bank spread across the country. The growth level in loans and advances is in line with the credit ceiling imposed by the regulator in 2012.

The Bank's customer deposits also grew significantly by 31% from Rs 82 bn as at 31 December 2011 to Rs 108 bn as at 31 December 2012. These growth levels are commendable as compared to the lower industry growth of 17% for the year. The Bank's savings deposits increased by Rs 7 bn and accordingly the CASA improved to 25% in 2012 as compared to 24% in 2011, despite the low CASA trend in the industry. The composition of customer deposits on the total borrowings of the Bank also improved to 75% from 67% as at the previous year end. The Advances to Deposits Ratio (ADR), including the credit lines improved to 105% as compared to 111% as at 31 December 2011.



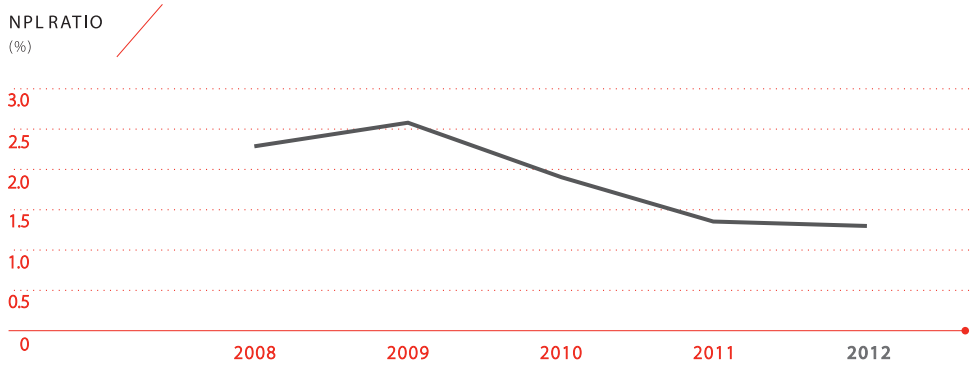


Financial Review



Asset Quality

The Bank continued to implement prudent measures and proactive practices to maintain the quality of its loan book throughout the year. The NPLs to the gross lending portfolio improved to 1.31% as at 31 December 2012 from 1.35% as at 31 December 2011. The Bank's ratio of 1.31% compares well with the industry NPL ratio of 3.6% as at 31 December 2012. The NPL cover as at 31 December 2012 was 62% with an industry NPL cover of 42% as at 31 December 2012.



Capital Adequacy

The Bank's core capital and the capital base as at 31 December 2012 were Rs 13.5 bn and Rs 15.0 bn respectively. The Tier I and II ratio of the Bank was 12.41% as compared with 11.26% for the previous year. The improvement in the core capital of the Bank, which represents shareholder value created, of Rs 2.5 bn attributed to improved profitability, supported by a well-managed Balance Sheet.

With the strategic rearrangements that took place within the Group during the year, the NDB Group's Core Capital and the Capital base improved significantly to Rs 25.3 bn and Rs 28.0 bn respectively as at 31 December 2012. Accordingly NDB Group's Tier I and Tier I & II ratio were 18.76% and 20.71% as at 31 December 2012, and indicate the future growth potential of the Group with this strong capital base.

Regulatory Developments

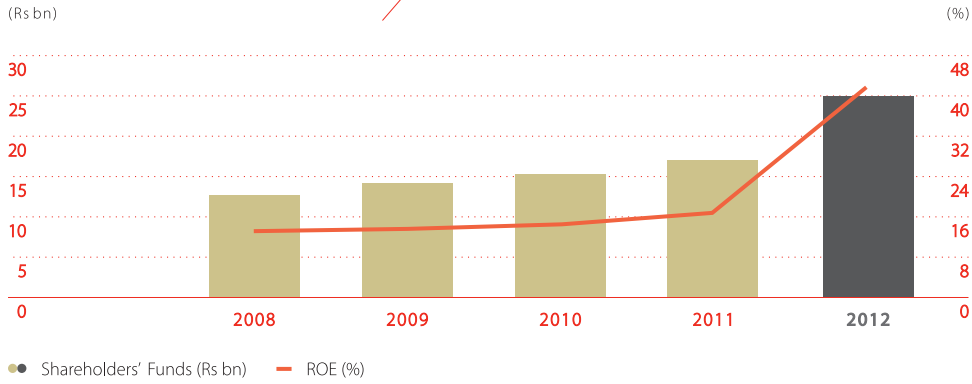
The Bank is substantially in compliance with all the Directions and complies with the daily, monthly and quarterly reporting requirements of the Central Bank.

Key Performance Indicators

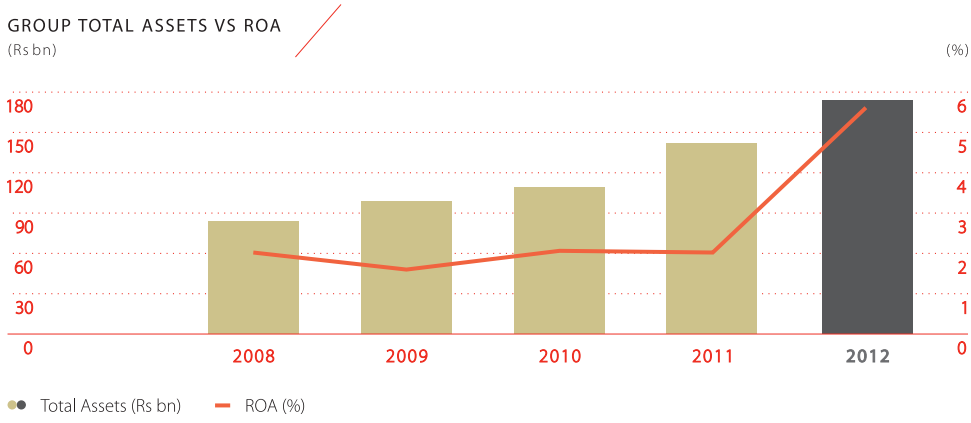
The Bank's earnings per share for the year improved to Rs 17.81 from Rs 11.15 from the previous year. The Bank's return on equity for the year was 21.1% as compared with 15.0% in 2011.

The Group earnings per share for the year increased significantly to Rs 55.31 as compared to Rs 15.79 as a result of the capital gain of Rs 6 bn earned on the divestment of the investment in AVIVA NDB Insurance PLC. Accordingly the Group's return on equity for the year too increased substantially to 42.35% as compared to 15.69% for 2011.

GROUP SHAREHOLDERS' FUNDS VS ROE



Financial Review



Share Price

The share price of NDB closed at Rs 137.90 in 2012 as compared to Rs 138.10 in 2011, in a stagnant equity market environment that prevailed during the year. The share price of the Bank has been maintained throughout the year despite the decline in the ASPI of 7% over the last year.

The Price/Book Value (PBV) at the year end was 0.91 times compared with 1.34 times at the previous year end. The PE ratio for the year 2012 was 2.56 times as compared to 8.97 times for 2011 and the improvement of the ratio was primarily due to the increased profitability of the NDB Group.

Post-Balance Sheet Events

There have been no other significant events subsequent to the Balance Sheet date that require disclosure in the Financial Statements.

Achievements

→ AWARDS AND RECOGNITION

NDB received significant local and global acclaim during 2012. The prestigious awards and recognition we received further reiterate the high level of competence, agility, strength and stability of NDB and fortifies its exciting journey towards excellence in the coming year, which is anticipated to be a year of quantum leap and growth for the Bank.

We present an account of these awards, the criteria upon which they were awarded and pen sketches of the awarding body, among other details.

CMO Asia Award for Excellence in Branding and Marketing

NDB was presented the Award for Brand Excellence in Banking, Financial Services and Insurance (BFSI) at the CMO Asia Awards 2012. This was the second consecutive year in which NDB was awarded by the CMO, and we were also the only Sri Lankan Bank to be recognized at the CMO Awards, which was held for the 3rd consecutive year.

Asia's Awards for Brand Excellence are adjudged by the Global Research Cell of the CMO Council - its members control over USD 200 bn in marketing spend - which identifies brands that perform within their respective markets based on market dominance, brand longevity, goodwill, customer loyalty and market acceptance.

For the best brand category, NDB was in great company, rubbing shoulders with renowned brands such as Adidas, Coca-Cola, Fonterra Brands, Nestle, Nokia, Hewlett Packard, Starbucks, Thai Airways and Proctor & Gamble.

Euromoney Awards for Excellence 2012

NDB Investment Bank Ltd. (NDBIB) was adjudged the 'Best Investment Bank in Sri Lanka' at the Awards for Excellence 2012 bestowed by Euromoney, the world's premier financial markets magazine.

This was a historic achievement for NDBIB as well as the country since it is the first time Euromoney has ever recognized an investment bank in Sri Lanka, for any award. It is also the first time an investment bank in the country has received an international accolade for excellence.

Euromoney Magazine has been the voice of international capital markets for over 40 years, offering unique coverage on the banking sector and global equity, bond and foreign exchange markets. Its Annual Awards for Excellence Programme has been running for 22 years and forms a benchmark for financial institutions featuring high quality products and services across all areas of commercial and investment banking. The selection criteria of Best Investment Bank Awards are based on both quantitative and qualitative factors over the preceding twelve-month period. Euromoney's awards for excellence cover more than 20 global product categories and best-in-class awards by region and country.

Achievements

LACP Vision Awards 2011

NDB's Annual Report 2011 gained noteworthy global acclaim being ranked amongst the World's Top 100 as well as Asia Pacific's Top 50, whilst winning two Platinum Awards and one Gold Award at the Vision Awards 2011 conducted by the League of American Communications Professionals (LACP).

The Vision Awards is one of the world's largest and most prestigious competitions assessing annual reporting from all over the globe.

NDB won the Platinum Award for the Best Annual Report in the commercial bank category. NDB also grabbed the Gold Award for the Most Improved Annual Report across all categories worldwide along with the Platinum Award for the Most Improved Annual Report across all categories in the Asia Pacific region this year.

According to the rankings of LACP, NDB was placed 6th amongst the Top 50 Annual Reports of the Asia Pacific Region and 32nd amongst the Top 100 Annual Reports of the world. This world ranking is a prestigious win for NDB as it places Sri Lanka in prime position in the rankings, surpassing such global giants as Boeing Corporation, WPP, Daimler AG, China Telecom and Commerzebank AG; all of whose annual reports were also ranked among the global top 100.

World Finance Names NDB the 'Best Commercial Bank in Sri Lanka'

The UK-based World Finance magazine rated NDB as the 'Best Commercial Bank in Sri Lanka'.

World Finance is a highly acclaimed international business journal that is renowned globally for its accuracy, credibility and wide readership.

The prestigious accolade was awarded in recognition of the Bank's commitment to continued excellence and superior service to its customers. The award appraised excellence achieved by banks against several criteria, which include; overall performance, financial ratios, variety and clarity of products and services, corporate governance, alternative financial products offering, parallel market interaction and competitive strategy.

HRM Awards 2012

NDB was presented the HR Masters Silver Award at the HRM Awards 2012 conducted by the Association of Human Resource Professionals (HRP) in Sri Lanka. The HRM Awards is the flagship event of the HRP Association, which rewards the nation's best HR practices while assessing, recognizing and felicitating the best HRM systems and processes in Sri Lankan organizations.

This is a pioneering effort which signifies NDB's long-term commitment towards the development of its Human Resource and has placed the Bank in the top bracket, amidst multinationals as well as local blue-chips that were among the other recipients of the Silver Award.

Achievements

ASIAN HR Leadership Award for Innovative HR Practices

NDB received an award for the organization with the most innovative HR practices, at the ASIAN HR Leadership Awards held on 25 September 2012 in Dubai, UAE. The Asian Leadership Awards are made in recognition of continuous commitment to best practices and innovative HR strategies.

The strategic partners of this initiative are the World HRD Congress and CMO Asia while 'Stars of the Industry Group' was the research partner. These awards celebrate the spirit of achievement and excellence in businesses in Asia.

Business Today Top 25 Corporates 2012

NDB was yet again positioned amongst 'Sri Lanka's Top 25' corporates by Business Today magazine which recognizes and rewards Sri Lankan corporate entities for their exceptional performance throughout the previous year. The awards are strictly based on the published financial information and other indicators of companies listed on the Colombo Stock Exchange in the year 2011/12.

NDB was ranked 18th this year.

NDB Amongst the 10 Best Corporates in Sri Lanka

NDB gained significant acclaim for its commitment towards sustainability and CSR at the recently concluded 'Best Corporate Citizens (BCC) Awards 2012' hosted by the Ceylon Chamber of Commerce. The Bank won the Award for the Best Corporate Citizen in the category of 'Corporates with a turnover below Rs 15 bn' and was recognized as one of the '10 Best Corporate Citizens' for 2012 along with leading multinationals and blue-chip companies in the country. NDB also won a Special Merit Award for its 'Jeevana Livelihood Development Scheme' under the Best CSR Projects Category.

Hosted by the Ceylon Chamber of Commerce, the BCC awards raise awareness on the importance of corporate social responsibility and strategic corporate sustainability within the business community, promoting and encouraging these practices amongst the corporate sector.

The Best Corporate Citizens Awards 2012 acknowledged NDB's display of exemplary corporate citizenship while appraising the Bank's take on social responsibility that goes far beyond philanthropy.

Team NDB - Winner of IPM's Great HR Debate 2012

Our team NDB secured the winner's title at the final round of the Great HR Debate by knocking out the defending champions Nations Trust Bank. The Great HR Debate, an inter organizational debating competition hosted by the Institute of Personnel Management (IPM), was the concluding event at the International HR Conference 2012, which was held on 26 and 27 July at Water's Edge.

Board of Directors

Board of Directors

Board of Directors

01. Hemaka Amarasuriya

Chairman

Mr Amarasuriya brings to NDB an impressive range of management, industrial, marketing and business skills from his tenure as Chairman of the industrial and retailing conglomerate Singer Group and his experience on the Boards of such companies as Regnis Lanka and Bata Shoe Company of Ceylon. He also brings with him substantial experience in international management as a former Senior Vice-President of Singer Asia Ltd. and Retail Holdings Ltd., USA and as Chairman of the Singer Worldwide Business Council. As a Chartered Accountant and a Chartered Marketer, he has used his wide experience in the business world to add value to whatever institution he serves.

02. Ashok Pathirage

Deputy Chairman

Mr Pathirage co-founded Softlogic in 1991 and has served the Softlogic Group as the Managing Director from its inception. He was appointed as the Chairman of the Group in 2000.

He is the Managing Director of Asiri Hospital Holdings PLC and is the Chairman of other hospitals in the group. He is also the Chairman of Softlogic Capital PLC, Asian Alliance Insurance PLC and Softlogic Finance PLC besides being the Chairman of many other Group Companies that operate in Leisure, Retail, Automobile and ICT sectors.

He also serves as the Chairman of NDB Capital Holdings PLC.

He started his career at a leading blue chip company in Sri Lanka and has over 25 years of experience in senior managerial capacity in the Information Technology industry and in the business world.

03. Russell De Mel

Director/Chief Executive Officer

Mr de Mel has been with NDB for over 30 years, largely in the field of Corporate Banking. Prior to his appointment as CEO he served as Vice-President - Head of the Corporate Banking Group and as Vice-President - Head of Group Risk Management.

During the initial phase of his career at NDB he has held many key positions in the field of Project and Infrastructure Finance. Over the last two decades he has been actively associated with some of the key commercial projects NDB partnered with both local and foreign investors. He also played a leading role in the privatization of the plantation sector. As Head of Group Risk Management he was instrumental in realigning the risk management function within the NDB Group. Currently, he sits on several Boards of the NDB Group companies.

Mr de Mel is a Fellow of the Chartered Institute of Management Accountants, UK.

Board of Directors

04. Trevine Jayasekara
Director

Mr Jayasekara is the Group Finance Director of Brandix Lanka Ltd. and is responsible for the overall finance function of the Group, as well as its related support functions. Mr Jayasekara brings with him a wealth of experience in international banking and finance, having worked at Arab Bank Ltd. in Bahrain, Deutsche Bank, Colombo and Aitken Spence & Co. He is a Fellow Member of The Institute of Chartered Accountants of Sri Lanka and an Associate Member of the Chartered Institute of Management Accountants, UK. He is a Non-Executive Director of Lanka Ventures Ltd.

05. Sarath Wikramanayake
Director

Mr Wikramanayake is a Chartered Accountant. He has worked with the Bank of Butterfield, a Bermuda-based international bank for 19 years, where he reached the position of Executive Vice-President. Since returning to Sri Lanka, he has been the Chief Executive Officer of Union Assurance Ltd. and the President of the Insurance Association of Sri Lanka in 2002. He is currently engaged in providing consultancy services to the Financial Services and ICT Industries. In addition to his role as a Director of National Development Bank PLC, Mr Wikramanayake is also a Director to several other companies including NDB Capital Holdings PLC, Orient Finance PLC, NDB Investment Bank Ltd. and NDB Wealth Management Ltd.

06. Mrs Kimarli Fernando
Director

Mrs Fernando is an Attorney-at-Law, and also a Barrister-at-Law, Lincoln's Inn, UK. She holds LL.B. (Hons.), from London School of Economics and Political Science, London, UK and successfully completed the Postgraduate Certificate Course in Human Resources Management at the Postgraduate Institute of Management (PIM), Sri Lanka.

Counting over 21 years of experience in the Banking Industry in Sri Lanka and Germany, Mrs Fernando was seconded to Deutsche Bank, Frankfurt and thereafter worked at Standard Chartered Bank. She joined Pan Asia Bank as a Director in March 2008 and functioned as the Chief Executive Officer of the Bank until 2009 when she was also Director of Lanka Clear (Pvt) Ltd., Director and Management Committee Member of Waters Edge and Member, Sri Lanka Bankers' Association. Currently, whilst serving as a Director of National Development Bank PLC, she also serves as a Director of L B Finance PLC, Valibel One PLC and Lewis Brown & Co. (Pvt) Ltd.

Board of Directors

07. Anura Siriwardena
Director

Mr Siriwardena holds a B.Sc. in Biological Sciences from University of Kelaniya and an MBA from the Postgraduate Institute of Management of the University of Sri Jayewardenepura, Sri Lanka. He is a Member of numerous professional bodies, including the Sri Lanka Institute of Marketing, the Sri Lanka Institute of Biology and the Sri Lanka Association for the Advancement of Sciences. Mr Siriwardena was the past Chairman and Chief Executive Officer of the Independent Television Network Ltd., Secretary to the Ministry of Coorperatives and Internal Trade and Secretary to the Ministry of Coconut Development and Janatha Estate Development. He currently functions as the Secretary - Industry and Commerce of the Ministry of Industry and Commerce of the Government of Sri Lanka. Mr. Siriwardena is a Platinum Honour Awardee of the Postgraduate Institute of Management Alumni Association for his outstanding performance in the field of Management.

08. Ms G D Chandra Ekanayake
Director

Ms Ekanayake is a nominee of the Ministry of Finance and Planning. She has been a Member of the Sri Lanka Administrative Service since 1984. Presently, she is the Director General of the Department of National Budget of the Ministry of Finance and Planning. Previously, she has held senior positions in the Treasury as Director - Economic Affairs, Controller of Insurance, Additional Director General - Department of External Resources and Director General - Department of Trade, Tariff and Investment Policy over a span of approximately 25 years service. Ms Ekanayake holds a Science Special Degree from the University of Kelaniya, an MBA from the Postgraduate Institute of Management, Sri Lanka and Diploma in the fields of Development Planning Techniques, International Relations and Economic Development.

09. Sujeewa Rajapakse

Director

Mr Rajapakse is the Managing Partner of BDO Partners, a firm of Chartered Accountants and counts over 28 years of experience with the firm. He is a Fellow of The Institute of Chartered Accountants of Sri Lanka and holds a Master's in Business Administration from the Postgraduate Institute of Management of the University of Sri Jayawardenapura.

Today, Mr Rajapakse serves as the President of The Institute of Chartered Accountants of Sri Lanka (ICASL) and is a Technical Advisor of the South Asian Federation of Accountants and the Confederation of Asia Pacific Accountants. He is currently serving as a Non-Executive Independent Director at Asian Alliance PLC and also a Board Member at the National Institute of Business Management (NIBM), Postgraduate Institute of Management (PIM), Securities Exchange Commission (SEC) and the Sri Lanka Accounting and Auditing Monitoring Board (SLAAMB) as an ex-officio nominated by ICASL. He is also serving as a Committee Member of the Monetary Policy Consultative Committee of the Central Bank of Sri Lanka.

He has held numerous honorary positions over the years and has functioned as a Board Member of First Capital Group and the Treasurer of Sri Lanka Cricket.

The Leadership Team

Ishani Senaweera
Vice-President
Head of Human Resources

Niran Mahawatte
Vice-President
Head of Treasury

Lionel Wickramasinghe
Head of Project Finance

Nirmala Rayen
Vice-President
Head of Group Risk Management

Raj Aboobucker
Vice-President
Head of SME and Retail Banking

Dhanan Senathirajah
Vice-President
Head of Finance & Planning

Faizan Ozman
Chief Financial Officer

Vajira Kulatilleke
Chief Executive Officer
NDB Capital Holdings PLC

Chrishanthi Jayawardena
Chief Operating Officer

Indrajit Wickramasinghe
Chief Operating Officer

The Leadership Team

Russell de Mel
Director/Chief Executive Officer

Ruwani De Silva
Assistant Vice-President
Head of Audit

Buwanekabahu Perera
Vice President
Head of Corporate Banking

Sujeewa Dissanayake
Vice-President
Head of Information Technology

Bank Management Committee

Murray Fernandesz
Assistant Vice President
Head of Sales and Marketing Treasury

Rivindu Nanayakkara
Assistant Vice President
Head of Trade Finance

Amal Yapa
Assistant Vice President
Corporate Banking

Delrene Seneviratne
Assistant Vice President
Head of Retail/SME Credit and Micro Finance Strategy

Bank Management Committee

Yasas Hewage
Assistant Vice-President
Head of Channels and Retail/SME Business Development

Melody Wickramanayake
Assistant Vice-President
Head of Legal

Sunil Karunaratne
Assistant Vice-President
Head of High Networth Segments and Group Products

Sithambaram Sri Ganendran
Assistant Vice-President
Head of Operational Risk

Group Management Team

Prasansani Mendis
Chief Executive Officer
NDB Stockbrokers (Pvt) Ltd.

Faizan Ozman
Chief Financial Officer
NDB

Vajira Kulatilleke
Chief Executive Officer
NDB Capital Holdings PLC

Quazi Arif
Chief Executive Officer
NDB Capital Ltd. - Bangladesh

Russell de Mel
Director/Chief Executive Officer
NDB Group

Group Management Team

Chrishanthi Jayawardena
Chief Operating Officer
NDB

Darshan Perera
Chief Executive Officer
NDB Investment Bank Ltd.

Saeed Reza
Managing Director & Acting Chief Executive Officer
Maldives Finance Leasing Company (Pvt) Ltd.

Indrajit Wickramasinghe
Chief Operating Officer
NDB

Prabodha Samarasekara
Chief Executive Officer
NDB Wealth Management Ltd.

Sustainability Report

Message from the CEO

The banking sector plays an integral role in the economy and is linked to every segment of human activity. As such banks play a very significant role in the planet's sustainability and are in a strategic position to act as influential change agents. At NDB we look at the big picture and operate in a manner that benefits all our stakeholders. 'Sustainability is a Lifestyle' is the core of the Bank's sustainability strategy, reflecting the manner in which the Bank operates, where sustainability is embedded in every decision taken and every activity carried out, and where every employee is encouraged to live these values. Sustainability has often been referred to as 'corporate citizenship', 'corporate responsibility' and by many other diverse terms. To us at NDB, sustainability simply means Integrity, Care, Passion, Teamwork and Service, the core values that the Bank lives by. In embedding and integrating sustainability into its business operations, the Bank takes every measure to fulfil its vision of creating sustainable shared value by delivering social, environmental and economic benefits across the stakeholder spectrum. The Bank's sustainability goals include ethical business practices, good governance, the minimizing of its carbon footprint, the fostering of a sustainability culture throughout the organization and the implementation of CSR initiatives that promote national economic growth and uplift the most vulnerable in society.

It is our belief that a robust economy is essential for the well-being of each individual. Stimulating sustainable economic growth contributes to poverty alleviation as well as a higher standard of living and overall well-being. Key aspects that drive a sustainable and robust economy are Entrepreneurship and Education. It is with this view that NDB has focussed on Entrepreneurship and Education as our strategic CSR initiatives.

In 2012, the Bank expanded into new regions and areas, introduced innovative products and strengthened the SME sector, which is considered the growth engine of the economy. The Bank opened 5 dedicated SME centres, conducted special SME workshops in several key regions and contributed significantly to financial inclusion and livelihood development of youth. The Bank's microfinance scheme '*Divi Aruna*' and the '*Jeewana Livelihood Development Scheme*' were key initiatives in our financial inclusion and livelihood development initiatives. Thus, the Bank promoted entrepreneurship development at every level, integrating this goal into the Bank's sustainability agenda. Whilst promoting entrepreneurship at the business level, the Bank also contributed to entrepreneurship development at the academic level. Bridging industry and academia, the Bank in partnership with the University of Moratuwa was successful in introducing entrepreneurship into the curriculum of the University. This effort was further strengthened by including a practical element where students were given the opportunity of forming and operating their own companies. The success and the interest generated clearly revealed that creating awareness and imparting knowledge and guidance, broadened the vision of these students. Whereas earlier, their ultimate goal had been to find employment, the entrepreneurship training embedded in them fostered the vision of starting up their own enterprises, which, in the course of operation would create employment opportunities for many others. For some others, this training was a moulding process which would undoubtedly help them become better employees...better 'internal customers'...or to coin a phrase, 'intra-preneurs'.

The lifetime benefits of education have long being recognized by economists. More recently, research findings have testified to the personal and social benefits and positive outcomes of education, particularly with regard to reduction of crime, improved health, lower mortality rates and increased political participation. At NDB we believe that a good education is the passport to success in every area of a person's life. An area of key focus in our initiatives to support education is the 'English Communication Programme' for secondary school teachers which the Bank conducted for teachers in rural schools in the North-Western Province. This learner-centred, activity based programme proved very valuable for teachers in rural areas who have little exposure to new methods and trends of teaching. The teachers themselves expressed their gratitude and were confident that this training which was of great benefit to them would continue to benefit many future batches of students who would study under them.

As we stride confidently into the future, proud possessors of a stable foundation and an exceptional talent pool, the Bank foresees more prospects for growth and excellence in all three areas of sustainability - profit, planet and people. Embracing and pursuing a holistic approach to sustainability the Bank is committed to enhancing economic growth whilst delivering innovative solutions and upholding environmental and social responsibility.

Russell de Mel
Chief Executive Officer

13 February 2013

Sustainability Report

Profiling the Bank

The National Development Bank PLC has its origins in 1979 when under the National Development Bank of Sri Lanka Act No. 02, our predecessor the National Development Bank of Sri Lanka was established. In 2005, through the provisions of another Act of Parliament, a company by the name of 'National Development Bank Ltd.' was incorporated under the Companies Act No. 17 of 1982 for the purposes of taking over the business of National Development Bank of Sri Lanka. Thereafter on 4th July 2007 in terms of the new Companies Act No. 07 of 2007, National Development Bank Ltd. was re-registered as National Development Bank PLC bearing registration No. PQ 27.

The principal activities of NDB lie in the areas of commercial banking, development financing, merchant banking, investment banking, leasing, housing finance, venture capital, stockbroking, wealth management, property investment and insurance.

Our services in these areas are accesible to customers through the Bank, its subsidiaries and associate companies. For a complete list of our subsidiaries and associates, please refer to 'NDB Group Companies' appearing on pages 200 to 203 of the Annual Report.

Although the Bank operates a subsidiary company in Bangladesh, its main enterprise is conducted within Sri Lanka. Therefore this Report will be confined to its operations in Sri Lanka

We also draw your kind attention to the Corporate Information provided on pages 332 and 334 of the Report, which provides further insight into salient features of the Bank.

The Bank's wide ranging product portfolio is channelled through four main areas of enterprise - *SME Banking, Retail Banking, Corporate Banking and Project Financing.*

Product Portfolio

- Loans for SME - Long-Term Loans (Concessionary Interest Rates)
- Short-Term Working Capital Loans
- Distributor Finance Facilities
- Supplier Banking Products
- Funding Importers & Exporters

- Current Accounts
- Savings Accounts
- Children's Savings Accounts
- NRFC/RFC Accounts
- Fixed Deposits
- Housing Loans
- Education Loans
- Personal Loans
- Leasing Facilities
- Credit Cards
- Debit Cards
- Pawning Services
- Western Union Money Transfer Services
- Raththaran Ithurum
- Internet Banking
- Bancassurrance

- Overdrafts
- Trade Products
- Money Market
- Cash Management Products
- Electronic Banking Platform, eWindow Facilitates the Payment Module

- Term Loans
- Securitization
- Guarantee Facilities
- Merchant Banking

1. Ordinary Share Investments
2. Preference Share Investments
3. Debentures
4. Advisory Services
5. Underwriting
6. Arranging Syndications

Sustainability Report

These products and services are made easily available via the Bank's Branch Network and Automated Distribution systems such as ATMs, Internet Banking, our Website, Telemarketing, Call Centre, a Mobile Commerce Application EZPay and our unique 'Feet on the Street' Sales force.

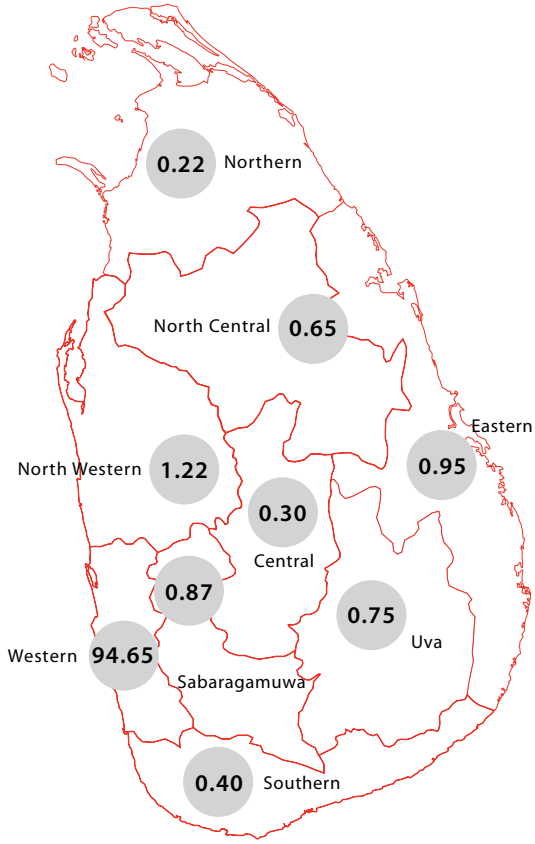
These channels are all managed by the Bank.

The Bank opened 9 new branches during 2012 in Hambantota, Kaduwela, Embilipitiya, Aluthgama, Kaduruwela, Nawalapitiya, Chunnakam, Minuwangoda and Dambulla.To date, NDB PLC operates island-wide, with 69 branches located in every province and district of the country.

Our total cadre as at 31 December 2012 stood at 1,447. Equity as at the same date amounted to Rs 15 bn. (Gross Income - Rs 20 bn, Total capitalization - Rs 22.6 bn, Total Assets - Rs 163.5 bn.)

Product and Service Impact

Percentage of the portfolio for business lines by specific region.



Note: The majority of the projects listed under the Western Province are located outside the Western Province and is categorized under this province since the registered office is located in the Western Province.

Percentage of the portfolio for business lines by size.

Size	%
Large	61.19
SME	38.75
Micro	0.06
	100.00

NDB has been instrumental in devising a new financial structure for the Un-Habitat programme seeking out and developing mechanisms to mobilize domestic savings and capital for affordable housing. The Bank continues to manage this fund with a sum of over Rs 27 mn guaranteed in the year 2012. The Bank also promotes livelihood development with special emphasis on inculcating the savings habit and financial inclusion (details on MDA page 65).

Monetary Value of Products and Services Designed to Deliver a Specific Environmental Benefit for each Business Line Broken Down by Purpose

The Bank promotes 'Green Financing' with many products designed to deliver specific environmental benefits such as pollution control, resource saving, renewable energy etc. (details on MDA page 65). A sum of over Rs 7.2 bn has been allocated under this segment with a portfolio balance of Rs 1.1 bn as at 31 December 2012.

Coverage and Frequency of Audits to Assess Implementation of Environmental and Social Policies and Risk Assessment Procedures

The Banks environmental and social management system (ESMS) is used to identify and assess environmental and social risks to which the projects and businesses it finances may incur, and addresses these risks at an early stage of credit evaluation (details on MDA page 63). The ESMS covers project lending for sectors which have been pre-identified in the policy as critical. Projects which fall under these sectors are assessed for environmental and social risks with frequent follow up throughout the loan cycle.

Percentage and Number of Companies held in the Institution's Portfolio with which the Reporting Organization has Interacted on Environmental or Social Issues

In relation to the above identified sectors, the % of facilities assessed under ESMS is 7% of the Bank's loan portfolio.

Sustainability Report

Accolades Received During the Year (2.10)

This subject is covered in detail in the chapter titled 'Achievements' appearing on page 87 of this Annual Report.

Parameters of this Sustainability Report

This is the Bank's second Sustainability Report to be published according to the guidelines of the GRI. It is our resolve to report as fully and transparently as possible and to be more inclusive and comprehensive with each passing year.

To further illustrate what we mean - in 2010/11, we provided information on 23 indicators, some of which were partially reported on. For the current year, we made provisions to be able to enhance our reporting to cover 24 indicators.

The Bank has adopted the sustainability data measurement techniques, basis of calculations and assumptions as stipulated in the GRI 3.1 framework.

A comprehensive Table of Standard Disclosures in the context of GRI appear on pages 145 and 150.

Our reporting period is from 1 January 2012, to 31 December 2012, whilst this report will appear annually.

Should you have any queries as to this Report and its contents, you may contact
Ms Sharon De Silva - Manager
Telephone : +94 11 2448448 Ext. 3130
Fax : +94 11 2341048
E-mail : sharon.desilva@ndbbank.com

Governance at NDB

The Bank has in place an exemplary regime of governance. Whilst this subject is covered extensively in the section entitled 'Corporate Governance' which appears elsewhere in this Annual Report, it may be pertinent to highlight a few key areas which have relevance to sustainability.

The highest governance body which oversees the management of the Bank is the Board of Directors. The Board meets regularly and ensures that the Bank adheres to the regulatory framework applicable to it and that all business conducted by the Bank is in full compliance with these regulations.

Delegation levels are ascribed to employees and to the subcommittees of the Board to ensure that the Bank remains at all times in compliance with regulatory requirements in the course of conduct of its business activities.

The Chair of the Board of Directors is a Non-Executive Director. The Board is comprised of nine Directors eight of whom are Non-Executive members and in terms of gender, count two females and six males.

The chart appearing below highlights the composition of Board and Board Committees as at 31 December 2012:

Board/Committee	No. of Members	Non-Executive Directors	Independent Directors*
Main Board	9	8	4
Audit Committee	5	5	2
Integrated Risk Management Committee	8**	3	1
Strategic Issues Committee	7	7	4
Remuneration and Human Resources Committee	6	6	4
Nomination Committee	5	5	3
Corporate Governance and Legal Affairs Committee	4	3	2

* *Independent Directors have been identified according to the criteria given in the Banking Act Direction No. 11 of 2007 on Corporate Governance issued to Licensed Commercial Banks. The Licensed Commercial Banks have been exempted from complying with Section 7.10 (Corporate Governance) of the continuous listing requirements under CSE Listing Rules.*

*** Includes Head -Group Risk, Head - Market Risk, Head -Operational Risk and Head - Strategic Risks, who are not Directors.*

Good governance practice invariably requires that an establishment ensures a free flow of views and information between the entity and its shareholders and employees.

At the Bank, the Board/Board committees members interact with employees at the monthly Board meetings and at committee meetings which are held regularly. At such meetings, employee's feedback and recommendations are put forward for the consideration and approval of the Board.

Our shareholders are entitled to timely and pertinent information on the financial performance of the Bank. In order to foster open dialogue, the CEO and Chairman maintain an effective communication with key shareholders providing opportunities for them to make recommendations and express views regarding the performance and strategic direction of the Bank.

All shareholders are free to contact the Chairman/CEO directly through written communications, meetings or through the Bank's website on 'contact@ndbbank.com'.

The Bank also has an ongoing programme of stakeholder engagement - the chart below gives salient details:

List of stakeholder groups engaged by the organization	Basis for identification and selection of stakeholders with whom to engage
Shareholders	To ensure that their expectations are met.
Directors	To ensure that stakeholder expectations are met.
Employees	Loyalty, Commitment and Motivation. To create a great place to work and also to ensure that employees' values are aligned with corporate values. Moreover, as NDB is in the service industry, we ensure to create a unique value proposition in the industry through our staff.
Depositors	To attract new depositors and to maintain loyalty.
Multilateral Lending Agencies	To keep them updated about the Bank and to report on progress.
Regulator - Central Bank of Sri Lanka	Close working relationship and compliance.
Auditors	Compliance.
Market Analysts	To keep them informed of the Bank's performance.
Suppliers	Close working relationship.
Local and Foreign Correspondent Banks	Maintain a good relationship.
Government Agencies - such as Inland Revenue Department, Registrar of Companies, Colombo Stock Exchange, etc.	Compliance.
Sri Lanka Accounting and Auditing Standards Monitoring Board	Compliance.
Rating Agencies	Compliance.

The measure of true sustainability of an organization necessitates a review of its strategy and enterprise against a tripodal base of Economic, Environmental and Social parameters.

We now present an account of the Bank's achievements from these three perspectives, elicited in response to GRI indicators.

From an Environmental Perspective

Today, the whole world is pre-occupied with the subject of energy - the usage, conservation and replenishment of existing sources and the search for viable and sustainable alternative/new sources. The sustainability of businesses and indeed, the planet itself, hinges on how successful we are in finding solutions to this subject.

The Bank plays a key role in the Nation's Energy Sector.

NDB has been actively engaged in funding mini-hydro power projects since 1997 and has been a Participating Credit Institution (PCI) in the World Bank's Energy Services Delivery (ESD) project and the Renewable Energy for Rural Economic Development (RERED) project. We have placed enormous emphasis on the development of alternative sources of energy through participation in these programmes - particularly in renewable energy processes such as mini-hydro power, wind, biomass and the like. NDB has supported the development of environment-friendly solutions to support the energy demands of Sri Lanka by offering concessionary funding to potential developers through various funding lines.

Thus, NDB has played a a dominant role in the renewable energy sector and pioneered the following projects in Sri Lanka in the past:

- Financed some of the country's maiden mini-hydro projects after the liberalization of the Power Sector.
- Financed the first grid connected dendro power project in Sri Lanka.
- Operated as the apex body administering the pollution control and energy efficiency improvement credit line provided by the Japanese Bank for International Co-operation.
- Was one of the leading participating financial institutions of the World Bank funded credit schemes for the upliftment and enhancement of the Renewable Energy Sector of Sri Lanka
- Co-financed the first commercial wind power project in Sri Lanka

Over the years, NDB has financed 26 mini-hydro projects, with a total capacity of 74.83 MW where the aggregate amount financed was Rs 2,789 mn. We have also financed 4 out of the 8 wind projects which operate in the country today, with a total capacity of 35.2 MW, where the aggregate amount financed was Rs 1,588 mn.

In the table appearing below, we present a detailed account of NDB's own track record in terms of energy consumption and conservation as well as other initiatives the Bank has taken in terms of awareness and energy conservation:

Energy Consumption in 2012

Month	Nawam Mawatha Building	Dharmapala Mawatha Building	
January	148,960.00	71,850.00	
February	136,630.00	62,150.00	
March	152,820.00	73,560.00	
April	134,580.00	66,550.00	
May	159,220.00	75,920.00	
June	145,330.00	70,330.00	
July	147,530.00	74,190.00	
August	146,620.00	73,300.00	
September	142,090.00	71,640.00	
October	149,150.00	75,610.00	
November	137,440.00	69,490.00	
December	132,250.00	66,970.00	
Total	1,732,620.00	851,560.00	
Average	144,385.00	70,963.33	
Total Consumption (NM+DM)		2,584,180.00	Kwh(Units)
Average Consumption (NM+DM)		215,348.33	Kwh(Units)

***** Excluding the consumption of NDB branches*

Energy Saving Projects

#	Initiative in Brief	Description/Benefit	Expected Implementation Date
1	Optimal utilization of Chilled water Plant	Reduce the additional consumption used by the Package type AC units	In Progress
2	Upgrading of Capacitor Bank	Reduce the Maximum Demand of the Building	Implemented
3	Energy Saving Lighting Improvement	All Magnetic ballasts were replaced by Electronic ballasts	Implemented
4	Improvement of existing City water pumps(Hydro pneumatic Pumps)	Save additional energy consumed by the water pumps	Immediately
6	Down time of the Chiller Plant- 4.30 pm everyday	1/2 hr Energy saving from Central Chiller Plant	Implemented
7	Reduce the running hours of pumps (AC)-After office hours	Reduce energy consumption	Implemented
8	Pilot Project for LED light fittings at Palawatta Branch	Reduce energy consumption	Implemented
9	Energy saving light fittings for outdoor Lighting (Security area)	Reduce energy consumption	Implemented
	Other Initiatives		
11	Awareness of the staff - energy saving	Reduce energy wastage	In Progress
12	Monitoring daily energy usage in the building	Identify the wastage/leakages etc.	Implemented
13	Monitoring of branch energy consumption at night	Daily energy monitoring by branch manager for night time unit consumptions	In Progress
14	Installation of light fittings to Sign board with less consumption	Reduce energy consumption	In Progress
15	Duration of sign board lighting reduced (7.00 pm - 10.00 pm)	Reduce energy consumption	In Progress
16	Reduced elevator running hours	Reduce the energy	Implemented
17	Polished Aluminum Parabolic light Fittings are used with Fluorescent Tubes	80% Energy saving. Minimum No. of fittings for an any area	Implemented
21	Light coloured finishes are to be used in floors, walls and ceiling	Artificial lighting will be minimized	In Progress
22	Keep AC units running at comfortable temperature levels	Set the temperature of the units at 22 Celsius (Avr. Ambient temperature)	Implemented

NEPTUNE RECYCLERS
EVERYDAY IS AN EARTH DAY

January 18, 2013

The Manager,
National Development Bank,
Nawam Mawatha,
Colombo 02.

Dear Sir/Madam,

Thank You for Shredding Your Confidential Documents with Neptune Recyclers.

We hereby confirm the collection and shredding of 26,316 kg of Waste Paper/confidential documents from 01st Of January 2012 to 31st of December 2012 from National Development Bank.

We thank you for using our shredding service to dispose off your waste papers in an environmentally friendly manner which not only saves precious Natural Resources, but also assists your organization in securely disposing your confidential documents at no charge to you. If every company in Sri Lanka thought as you do, our country would definitely be a better place to live for you and me.

The above paper that was provided by you for re-cycling has approximately saved:

- 447 Fully Grown Trees
- 46,185 Liters of Oil
- 105,264 kwh of Electricity
- 836,322 Liters of Water
- 79 Cubic meter of Land fill
- And Reduce Green House Gas Emission by 26,316 kg of Carbon Equivalent.

Whilst thanking you for your generous consideration in saving the environment we assure you of quality service at all times. Should you require further information or clarifications, please feel free to contact us on 0777-915153 or 011-3038877 at any given time.

Thanking you.
Yours Sincerely,

NEPTUNE RECYCLERS

Mohamed Sakkhaf
Assistant Manager - Recycling Solutions

a member of exp

NEPTUNE PAPERS (PVT) LTD
164 2/2 Old Kandy Road, Peliyagoda, Sri Lanka.
Telephone: (011) 3038877 Fax: (011) 4657018 Email: ecosave@npl.lk
www.recyclesrilanka.com

Employment and Employee

As one of the best financial conglomerates in Sri Lanka we offer people with talent, passion and integrity some of the best personal advancement and career opportunities. The data we present below stands testimony to NDB's goal - to provide premium employment and decent work avenues together with career and personal advancement.

Staff Statistics - Trend - By Designation

Designation	2010 %	2011 %	2012 %
Senior Management Staff	3	3	3
Management Staff	14	12	12
Executive Staff	16	17	17
Non-Executive Staff	51	49	51
NDB Bank Staff	84	81	83
Specialized Sales Force	8	10	9
Other Staff	8	9	8
Overall Staff	100	100	100
Permanent Staff	85	84	85
Contract Staff	15	16	15

Staff Statistics - Trend - By Gender

Designation	Female %	Male %
Senior Management Staff	39	61
Management Staff	34	66
Executive Staff	31	69
Non-Executive Staff	46	54
NDB Bank Staff	41	59
Specialized Sales Force	100	0
Other Staff	38	62
Overall Staff	41	59

Sustainability Report

The NDB's attrition rates have always been positive and have consistently remained below industry levels.

Attrition - By Gender

Gender	Staff No.	Staff %
Female	24	42
Male	33	58
Total	57	100

Turnover Rate - 5%

Recruitments

Designation	Staff %
Senior Management Staff	0.3
Management Staff	1
Executive Staff	6
Non-Executive Staff	37.7
NDB Bank Staff	45
Specialized Sales Force	28
Other Staff	27
Overall Staff	100

Beyond basic remuneration, full-time employees of the Bank receive a package of benefits.

The health, safety and well-being of staff is a prime consideration at the Bank. NDB have thus been at great pains to ensure that our occupational safety and health policy is an integral part of our work environment.

An important adjunct in this area is security. By security we mean the protection of facilities and equipment from unauthorized access and the protection of employees whilst at work. Further we ensure that our employees are educated on health and safety issues.

Occupational Injuries

In accordance with NDB's Business Continuity Plan (BCP) there is a dedicated team of specialists tasked with handling, the business continuity plan, first aid as well as psychological first aid requirements in emergency situations.

Currently, there are 25 BCP Co-ordinators, 50 first aiders at our Head Office and 53 trained specialists stationed within our branch network.

Similarly the psychological first aid team is a cross functional team consisting of 25 trained specialists. First Aid/ Psychological First Aid programmes are conducted annually.

Therefore, it is evident that over 10% of the employees represent the formal joint management - worker health and safety committees.

The Levels at which the committees typically operates; the committees consists of employees from all levels ranging from Junior Executives to Managers.

Rates of Injuries and Lost days

No. of Employees	Days
4	24

NDB HR has taken commendable steps in looking after its employees' well-being in the belief that a healthy body and mind will have a positive impact on their professional and personal lives. In addition to the comprehensive gymnasium, initiatives are designed to improve the health, safety and well-being of its people at work, NDB also offers a number of recreational activities to help employees pursue their interests and find ways to unwind. Such as NDB Health Week, Work Life Balance Week, *Lama Lokaya* an awareness session on child protection rights, Fitathon, Aerobics, Yoga and Social Dancing sessions. These awareness sessions, health screening and checkups have been truly beneficial to the employees as well as their family members.

Training is a *sine qua non* at NDB. Whilst we have an emancipated and comprehensive training programme that is enacted across all grades of the organization, we also believe that training philosophy and strategies should be revisited from time to time in order to incorporate the new trends and challenges in the environment and the necessary skills needed to face them.

Training opportunities are extended to all staff to maximize their skills and competencies in order to meet organizational needs as well as facilitate personal growth, thereby providing challenging careers to employees.

For the year under review, as at 31 December 2012, the training days per person ratio stood at 6.7 days per employee.

Sustainability Report

By Gender

Category	Sum of No.of Training Days
Female	3,412.88
Male	5,540.26
Grand Total	8,953.13

By Location

Region	Sum of No. of Training Days
Region 1	854.50
Region 2	616.25
Region 3	780.63
Region 4	332.75
Region 5	676.50
Region 6	919.25
Region 7	1,229.00
Head Office	3,544.25
	8,953.13

For Branches coming under each Region refer Branch Network on Page .....

Band	Designation	Sum of No. of Training Days		Grand Total	Average per Person	Sum of No. of Training Hours		Grand Total	Average per Person
		Female	Male			Female	Male		
0	BDA/BDO/SBDA/ Consultant/TBA/ Agency Staff/Intern	1,151	1,547	2,698	10.66	9,208	12,376	21,584	85.31
1	VP	13	37	50	4.53	106	293	399	36.27
2	AVP	79	124	203	6.76	632	991	1,623	54.10
3	Manager 1	112	133	244	6.11	893	1,062	1,955	48.88
4	Manager 2	104	146	249	4.71	831	1,164	1,995	37.64
5	Deputy Manager	170	444	614	7.30	1,358	3,550	4,908	58.43
6	Assistant Manager	218	453	671	6.78	1,744	3,623	5,367	54.21
7	Officer	254	773	1,027	7.03	2,034	6,181	8,215	56.27
8	Senior Associate	314	803	1,117	7.30	2,513	6,426	8,939	58.42
9	Associate 1	547	635	1,182	4.27	4,379	5,078	9,457	34.14
10	Associate 2	451	447	898	3.04	3,605	3,578	7,183	24.35
Grand Total		3,413	5,540	8,953	6.75	27,303	44,322	71,625	54.02

Building capability has also posed a unique set of challenges to NDB. Accordingly the skill set that is needed to run the business has changed and those needs had to be met through carefully laid out measures.

Thus, the learning plans have been developed based on intense discussions with Senior Management in meeting evolving business and development needs of the organization. As the retail arm of the business grew rapidly, NDB recruited a dedicated trainer to meet the specific learning needs of the business. New technical skills that were needed was given using multitude of resources - the dedicated trainer, internal resource persons who were trained as 'train the trainers' and by getting down external faculties including foreign faculties to run programmes tailor-made for NDB. The foreign faculties were brought down since NDB wanted to be abreast of regional and global trends as well. These were strengthened by 'awareness training' on related areas in order to broaden the learning base. These were further strengthened by soft skills including team-building exercises to bring people from diverse cultures together and managerial skills development at different levels for Senior, Middle and Junior Management.

Management skill development happened at different levels as mentioned above with refresher programmes built to those - the latest being a mini MBA programme. The foreign faculties brought down are from places like Singapore and India who were in the calibre of Singapore Institute of Management and CRISIL India. NDB ran at least 3-4 programmes using foreign faculties a year. By 2010, NDB tied up with IBSL to impart Banking knowledge on a continuous basis based on modular programmes to existing staff and the new staff that is joining the Bank in large numbers. NDB also tied up with IBSL to run Diploma programmes in order to impart technical knowledge that is required. This is a pioneering effort for a local Bank in Sri Lanka as per the IBSL.

With the ceasefire and peace declaration opportunities on the horizon with new business opportunities yielded , NDB started imparting Tamil language skills to its staff. Further, in order to meet the business needs NDB taught languages like Italian to enable staff to be on top of business. NDB's commitment to building capability and learning and development is such, that during difficult times when the Senior Management decided to forfeit its salary increments, the learning budget was not slashed. However, being conscious of escalating costs, HR took steps to find alternate funding sources and managed to get reimbursements for some of the training programmes conducted.

NDB HR also took steps to have its own Training Centre which is a 'Business Centre' so that no resources need to be dedicated to external sources. Today, HR is proud to own a state-of-the-art Training Centre. The Training Centre currently has a utilization rate of over 75% including week-ends. This talks volumes and justifies the fact that a dedicated Training Centre at NDB has paid-off dividends, with the additional positive of training costs coming down.

The data presented below illustrate the diversity within our HR base in terms of age and gender spread.

Sustainability Report

Age Analysis - Overall

Range	2010	2010 %	2011	2011 %	2012	2012 %
18 - 20 Years	19	2	18	1	3	0.2
21 - 30 Years	504	52	715	58	751	56.6
31 - 40 Years	294	30	342	28	368	27.7
41 - 50 Years	116	12	128	10	158	11.9
51 - 55 Years	30	3	31	2	37	2.8
56 Years and above	9	1	9	1	11	0.8
	972	100	1,243	100	1,328	100.0

Gender Analysis

Designation	Female %	Male %
Senior Management Staff	39	61
Management Staff	34	66
Executive Staff	31	69
Non-Executive Staff	47	53
NDB Bank Staff	41	59
Specialized Sales Force	15	85
Other Staff	38	62
Overall Staff	39	61

NDB seeks to build its own unique culture and set of values within all its employees. This begins at the beginning, where all new recruits undergo a compulsory corporate induction programme and they are familiarized with the main aspects of the policies and procedures governing organizational ethics and practices. This is an ethos inculcating process; one which enshrines desired attributes in terms of business morality and respect for human rights among many others.

As part of our welfare initiatives, NDB HR provides a broad range of training and assistance that supports lifelong learning and transition support. These programmes develop knowledge, competencies and learning that collectively benefit our employees. Wealth management programmes, Debt management sessions covered in NDB work-life balance week, the recently held Asian Alliance Insurance briefing sessions are few of such examples.

	%		Ratio	
Category	Male	Female	Male	Female
Senior Management Staff	65	35	1	0.5
Management Staff	64	36	1	0.6
Executive Staff	67	33	1	0.5
Non-Executive Staff	56	44	1	0.8
Overall	63	37	1	0.6

NDB and Society

One of the foundational qualities in any sustainable enterprise is 'responsibility'. The Bank takes this word very seriously, as we consider how responsible our products and services are vis-à-vis society and its best interests. In that light, we choose carefully the areas we will engage in the course of our business.

The Bank makes every effort to link its business operations to strategic sustainability activities. With a renewed focus on SME development, a host of support activities were conducted for the relevant stakeholders who included customers, employees and the community.

A key initiative with regard to the community and customers was the SME training programme which the Bank conducted for entrepreneurs in SME hubs in the main regions. The participants included existing as well as potential customers including customers of the local Chambers of Commerce. The programmes covered a diverse range of business related subjects including business management, business planning, financial management, working capital management, human resource management, marketing, taxation, accounting and taxation, leadership on motivation and planning, positive thinking, management of investments and new business in Sri Lanka.

The Bank adopts a pragmatic approach in executing these programmes where each regional programme is customized according to the geographic region and the industries represented at these different forums. Furthermore, the participants can choose from a list of subjects on offer and assign priority in terms of the subjects they wish to follow. Thereafter, the subjects for the programme are decided based on the need of the participants. The resource persons include industry specialists as well as experienced personnel of the Bank who shared their knowledge and expertize with the entrepreneurs.

Whilst providing a forum for the entrepreneurs to network and share views with each other this initiative also gives them an opportunity to gain a clear understanding with regard to the products and services on offer and identify the most suitable SME Banking solutions that meet their individual business needs. These regional education programmes equip the entrepreneurs with the competencies and proficiencies required to sustain and grow their business operations.

The Bank conducted 16 programmes in 2012 benefitting over 1,000 entrepreneurs.

Sustainable Lending

The Bank's 'Environmental and Social Management Policy' which was implemented in 2008 plays a central role in the Bank's lending policy. This ensures that funding is made available only for projects that comply with the approved standards. This comprehensive policy which includes an environmental guideline, an environmental management system and a governance model, integrates environmental impact considerations into business decisions across the Company. The policy's exclusion list cites industries engaged in illegal activities, industries that pollute the environment with no proper pollution control methods, industries involved in manufacturing and selling arms and production or activities involving harmful or exploitative forms of forced labour/ child labour among others.

Projects deemed eligible but which do not comply with the guidelines are accommodated only if the identified risks are mitigated.

Training in 'Green Financing'

A vital part of the Bank's training includes improving knowledge in green financing where employees are trained on how to appraise a credit facility based on all three sustainability aspects; economic, environmental and social. A special certification programme was conducted on Environmental Appraisal on Financing Industries and Projects where employees are given the know-how to incorporate environmental and social considerations in business processes.

For the year in review, the bank trained 50 employees under the specialized training for green financing.

Anti-Corruption

As a responsible Bank, we shun bribery and corruption in all its forms.

The Bank compliance policy covers the aspect of bribery and corruption. A yearly review is conducted across the organization where the risk is assessed individually.

The Bank is also in the process of formulating a revised and more comprehensive compliance policy.

All new recruits undergo a compulsory corporate induction programme and they are familiarized with the main aspects of the anti-corruption policies and procedures.

The Bank takes prudent measures to train the employees on this aspect, taking every measure to inculcate a culture of ethics governed by integrity and high moral standards. As an intensive and proactive measure Mr. Simon Culhane of the Chartered Institute of Investments and Securities - United Kingdom was brought in and all the management cadre employees were exposed to a one-off training session on 'Integrity at Work' during 2012.

This preventive action has resulted in a 'zero incident' record.

The Bank supports and assists policy development whenever the Banks opinion is sought. The Bank has shared its expertise and knowledge and given feedback on diverse aspects including banking, legal and listing on the stock exchange.

Satisfying the Customer

Ultimately, our entire effort is for one purpose only - to satisfy and exceed customer expectations. This is the pivotal point from which all else flows.

The frontline staff at NDB are continuously monitored and provided training to cover any identified gaps thus ensuring improved customer satisfaction at all touch points of the Bank.

The Bank conducted a customer satisfaction survey annually for the period 2008 to 2010, with the assistance of Lanka Market Research Bureau (LMRB). A consistent pattern of growth unfolds, which is encouraging - customer satisfaction ratings for 2008, 2009 and 2010 were 69.76%, 75.40% and 75.40% respectively.

A structured, comprehensive research programme was mapped out with LMRB in 2012 and will be implemented in 2013.

A dedicated customer service official of the NDB monitors and identifies the service delivery gaps across all touch points of the Bank and provides recommendations for service recovery and monitors the implementation of these activities from end to end.

NDB maintains a comprehensive online complaint management system where complaints are resolved within a stipulated time frame based on the nature and complexity of the complaint.

Continuous improvement continues to flow, based on the feedback received in customer surveys and from ongoing customer feedback on products and services.

Several cross functional teams have been appointed from within the Group with the objective of identifying strategic initiatives for value creation, product innovation and synergy across the Group towards building the NDB Brand. These teams play a pivotal role in triggering the overall Group strategy through the implementation of key initiatives across customer segments via customized products and channels, whilst leveraging the Bank's competitive strengths and market dynamics.

NDB encourages continuous innovation through its automated, suggestion generating system - 'IdeaXpress' - which is an IT tool that can be accessed by all employees in the Bank in order to share innovative ideas and customer insight.

Satisfying the customer requires that the Bank is scrupulously fair and transparent in all its communications, whether it be in its marketing communications with them, adherence to pertinent regulations and other such areas.

In compliance with the Customer Charter laid out by the Central Bank of Sri Lanka, the Bank has made the following arrangements to ensure product ownership with regard to marketing communication.

- Details of products offered at branches could be found on printed material such as leaflets, posters and the like, prominently displayed at branches for easy access.
- Details of all products are also available on the Bank's website along with the details of relevant contact persons, thus providing the customer easy access to information.
- A 24 hour Customer Service Hotline also serves customers every day, throughout the year.

All the systems we have in place, together with sound and ethical strategy and enterprise of the Bank have ensured that NDB has not recorded any transgressions, violations or breach of regulations concerning responsible customer communication.

The Selected Performance Information

Product and Service Impact

At NDB, incorporating environmental and social due diligence into the lending process is a key aspect of the Bank's social responsibility efforts. This effort is supported by the Banks 'Environmental and Social Management System' (ESMS) which is in operation since 2008. The ESMS is used to identify and assess environmental and social risks of the projects and businesses the Bank finances, where the identified risks are addressed at an early stage of credit evaluation. Businesses and projects must be compliant with all relevant environmental and social laws and regulations to qualify for the Banks funding. In addition, the Bank encourages customers to approach sustainability issues on a 'best efforts' basis with the support of ESMS.

The objectives of ESMS are -

- to identify and assess adverse environmental and social outcomes of the project or business,
- to avoid or to minimize, mitigate or compensate for these outcomes,
- to promote improved environmental and social performance in the businesses and projects to which we lend through the effective use of suitable management systems.

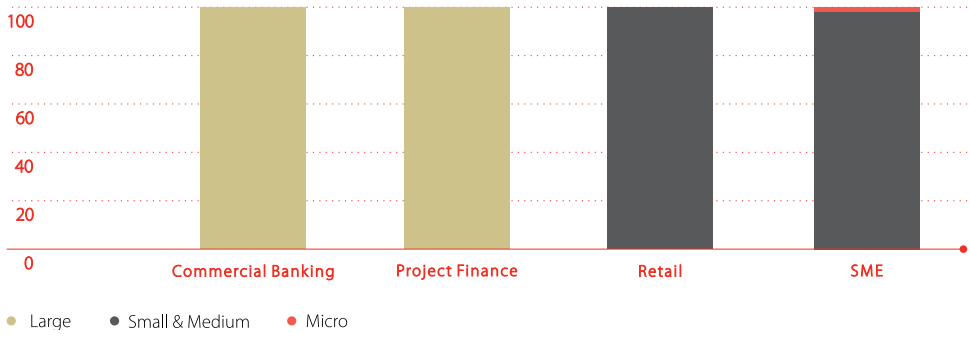
ESMS is an integral part of the Bank's credit policy and the credit evaluation process in long-term lending. A five-member, cross-functional team is responsible for day-to-day ESMS operations and all relevant staff are familiar with its requirements.

Percentage of the Portfolio for Business Lines by Specific Region, Size (E.g. Micro/SME/Large) and by Sector (FS 6)

Province	SME	Project Finance	Retail	Commercial Banking
Western	55.39	65.14	67.84	100
Eastern	5.88	1.82	4.28	–
Southern	10.40	2.84	4.59	–
Northern	2.67	–	2.96	–
Central	6.77	10.57	5.81	–
North-Western	8.29	5.55	7.37	–
North-Central	2.29	0.17	2.67	–
Sabaragamuwa	7.00	8.92	2.86	–
UVA	1.31	4.99	1.62	–
Total	100.00	100.00	100.00	100.00

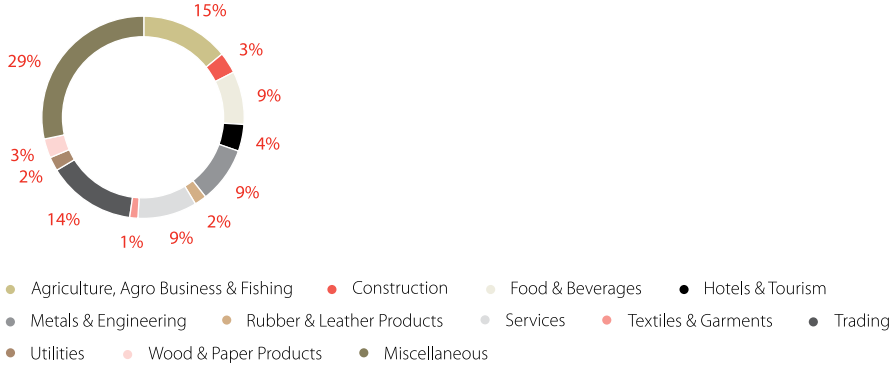
Sustainability Report

PERCENTAGE OF THE PORTFOLIO FOR BUSINESS LINES BY SPECIFIC SIZE
(%)

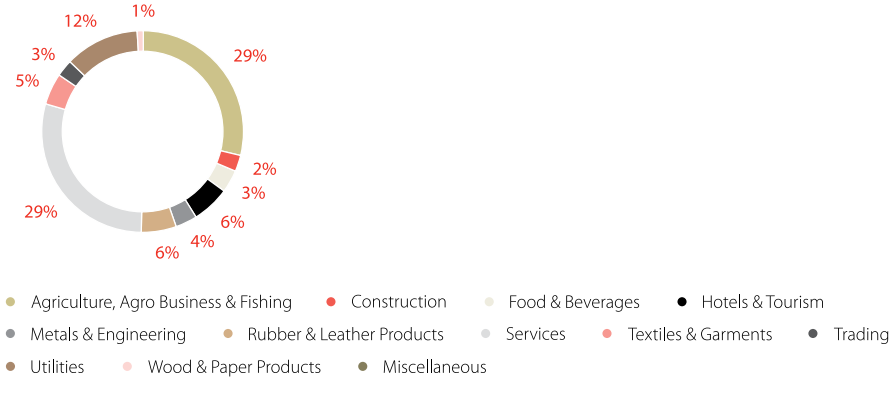


Percentage of the Portfolio for Business Lines by Specific Sector

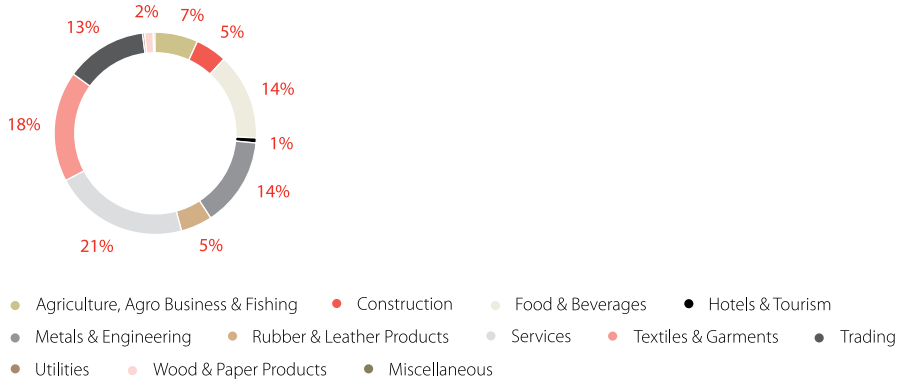
SME



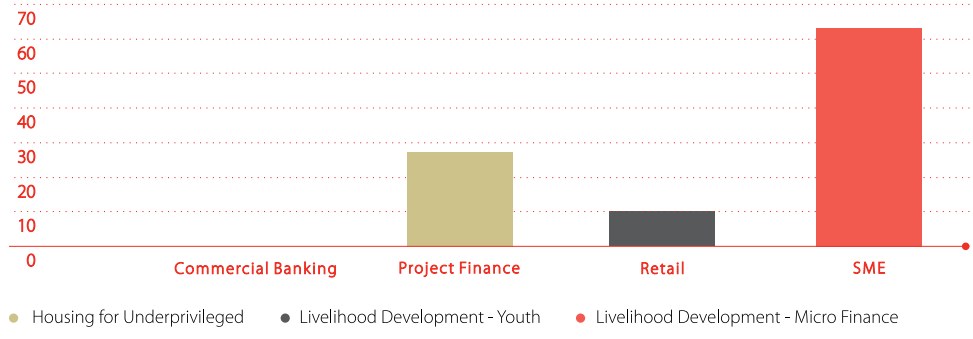
PROJECT FINANCE

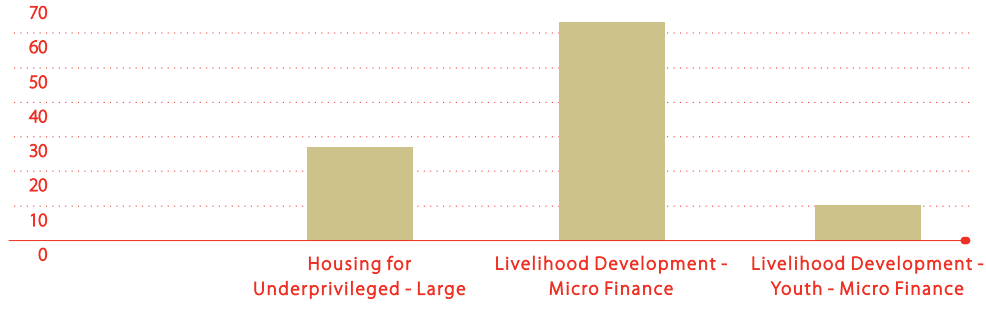


COMMERCIAL BANKING UNIT



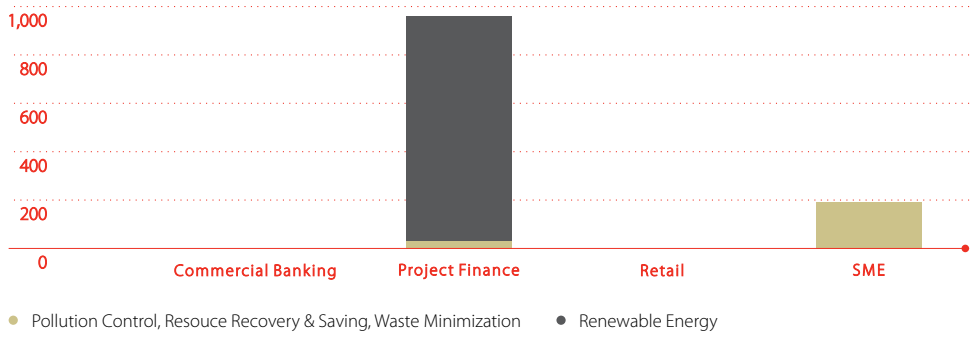
Monetary Value of Products and Services Designed to Deliver a Specific Social Benefit for Each Business Line Broken Down by Purpose (FS 7)





Sustainability Report

Monetary Value of Products and Services Designed to Deliver a Specific Environmental Benefit for Each Business Line Broken Down by Purpose (FS8)



Direct Economic Value Generated and Distributed, Including Revenues, Operating Costs, Employee Compensation, Donations and Other Community Investments, Retained Earnings, and Payments to Capital Providers and Governments (EC 1)

Value Added Statement

	2012	%	2011	%
Value Added				
Gross Income	20,124,990		13,533,769	
Cost of borrowings and services	(12,974,606)		(8,291,042)	
Impairments charges for loans and other assets	(106,112)		(67,789)	
Value addition	7,044,272		5,174,938	
Distribution of Value Added				
To Employees				
Remuneration and benefits	2,172,740	31	1,838,184	36
To Government				
Taxes	1,682,953	24	1,279,321	25
To Providers of Capital				
Dividends to shareholders	656,696	9	879,833	17
Retained in the Business				
Retained profit	2,350,046	33	999,313	19
Depreciation	181,837	3	178,287	3
	2,531,883	36	1,177,600	23
	7,044,272	100	5,174,938	100

Environmental

Initiatives to Provide Energy-efficient or Renewable Energy-based Products and Services, and Reductions in Energy Requirements as a Result of these Initiatives. (EN 6)

The addition of Green Energy to the National Grid as a result of the Banks renewable energy-based products and services.

Projects Funded	Capacity (MW)
Wind Projects	35.2
Hydro Projects	74.83

Total Workforce by Employment Type, Employment Contract and Region, Broken down by Gender (LA 1)

Total Workforce Broken Down by Gender

Designation	Female	Male	Grand Total	Female %	Male %
CEO		1	1		
Chief Financial Officer		1	1		
Chief Operating Officer	1	1	2		
Vice-President	2	5	7		
Assistant Vice-President	13	17	30		
Senior Management Staff	16	25	41	39	61
Manager 1	19	21	40		
Manager 2	17	36	53		
Deputy Manager	25	59	84		
Management Staff	61	116	177	34	66
Assistant Manager	32	67	99		
Officer	34	95	129		
Management Trainee	11	6	17		
Executive Staff	77	168	245	31	69
Senior Associate	55	98	153		
Associate 1	138	139	277		
Associate 2	147	148	295		
Assistant	1	5	6		
Non-Executive Staff	341	390	731	47	53
NDB Bank Staff	495	699	1,194	41	59
Business Development Officer	2		2		
Business Development Associate	14	103	117		
Senior Business Development Associate	4	9	13		
Specialized Sales Force	20	112	132	15	85
Senior Management on Contract		10	10		
Trainee Banking Assistants	22	18	40		
Interns	9	4	13		
Outsourced Staff	15	43	58		
Other Staff	46	75	121	38	62
Total	561	886	1,447	39	61

Sustainability Report

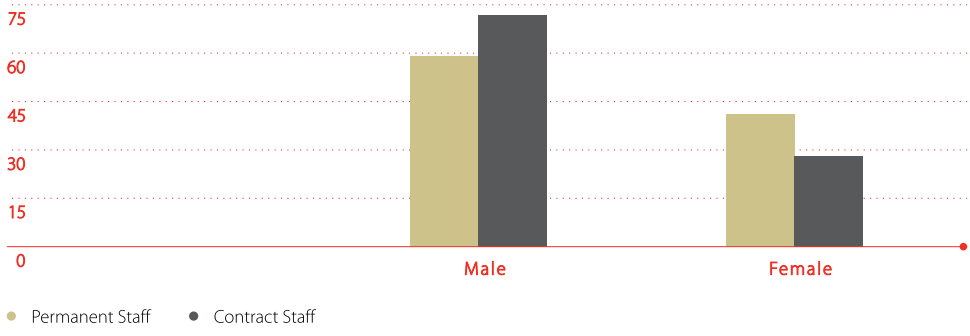
Employment Contract by Gender

	Staff		
Employment Category	Male No.	Female No.	Total No.
Permanent Staff	669	460	1,129
Contract Staff	144	55	199
	813	515	1,328

Percentage of Employment by Gender

	Staff		
Employment Category	Male %	Female %	Total %
Permanent Staff	59	41	100
Contract Staff	72	28	100
Total	61	39	100

EMPLOYMENT CATEGORY - BY GENDER
(%)



Total No. of Permanent Employees Broken Down by Employment Type and Gender

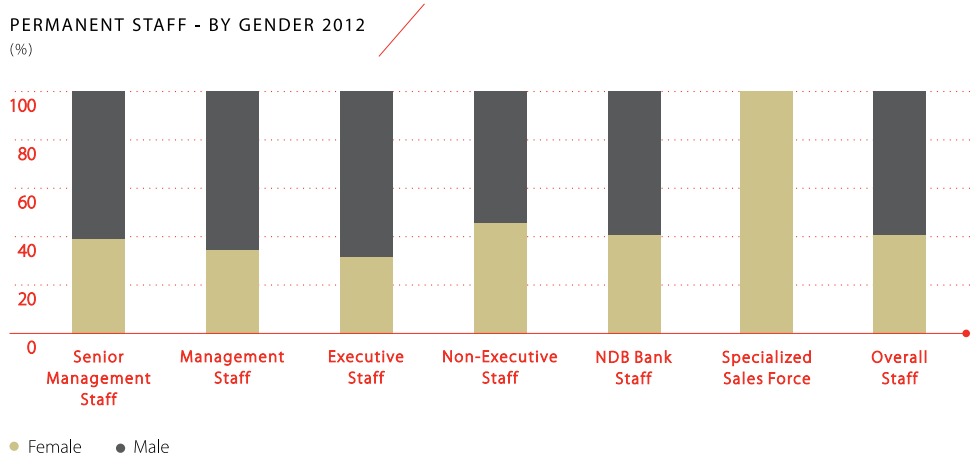
Designation	Female	Male	Grand Total	Female %	Male %
CEO		1*	1		
Chief Financial Officer		1	1		
Chief Operating Officer	1*	1	2		
Vice-Presidents	2	5	7		
Assistant Vice-Presidents	13	17	30		
Senior Management Staff	**16**	**25**	**41**	**39**	**61**
Manager 1	19	21	40		
Manager 2	17	36	53		
Deputy Manager	25	59	84		
Management Staff	**61**	**116**	**177**	**34**	**66**
Assistant Manager	32	67	99		
Officer	34	95	129		
Management Trainee	11	6	17		
Executive Staff	**77**	**168**	**245**	**31**	**69**
Senior Associate	55	98	153		
Associate 1	138	139	277		
Associate 2	111	119	230		
Assistant	1	5	6		
Non-Executive Staff	**305**	**361**	**666**	**46**	**54**
NDB Bank Staff	**459**	**670**	**1,129**	**41**	**59**
Business Development Officer	2		2		
Specialized Sales Force	**2**	**0**	**2**	**100**	**0**
	461	670	1,131	41	59

**Employees holding key positions who are on long-term contract.*

Sustainability Report

Employment Category	Female %	Male %	Total %
Senior Management Staff	39	61	100
Management Staff	34	66	100
Executive Staff	31	69	100
Non Executive Staff	46	54	100
NDB Bank Staff	41	59	100
Specialized Sales Force	100	0	100
Overall Staff	41	59	100

Permanent Staff - By Gender

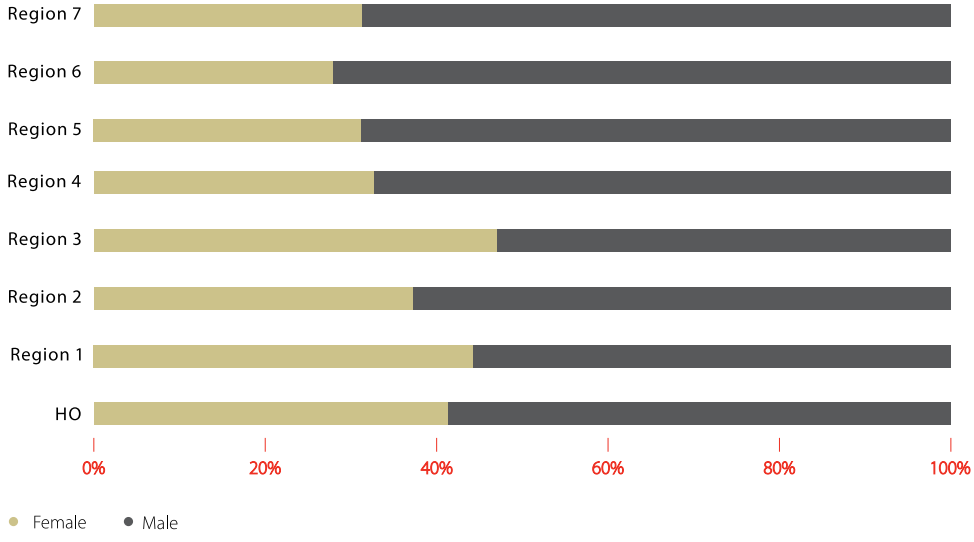


By Region and Gender

Overall Staff Details	Staff		
Location	Female No.	Male No.	Total No.
Head Office	353	502	855
Region 1	35	44	79
Region 2	25	42	67
Region 3	33	37	70
Region 4	19	39	58
Region 5	29	64	93
Region 6	30	77	107
Region 7	37	81	118
Total	561	886	1,447

Overall Staff Details	Staff		
Location	Female %	Male %	Total %
Head Office	41	59	100
Region 1	44	56	100
Region 2	37	63	100
Region 3	47	53	100
Region 4	33	67	100
Region 5	31	69	100
Region 6	28	72	100
Region 7	31	69	100
Total	39	61	100

PERCENTAGE OF STAFF BY REGION BY GENDER
(%)



Sustainability Report

Total Number and Rate of New Employee hires and Employee Turnover by Age Group, Gender and Region (LA 2)

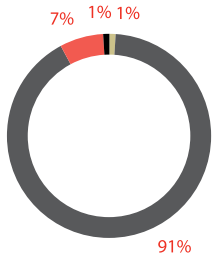
Recruitments - By Gender

Gender	Staff No.	Staff %
Female	123	37
Male	207	63
Total	330	100

RECRUITMENTS - BY GENDER

Female Male

RECRUITMENTS - BY AGE

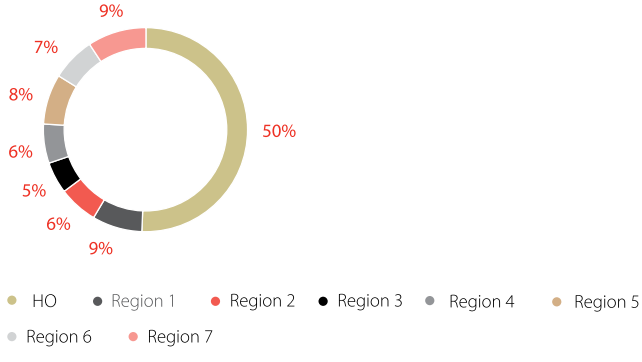


20-30 Years 30-40 Years 40-50 Years 50-60 Years

Recruitments - By Location

Location	Staff No.	Staff %
Head Office	165	50
Region 1	28	8
Region 2	20	6
Region 3	18	5
Region 4	19	6
Region 5	28	8
Region 6	22	7
Region 7	30	9
Total	330	100

RECRUITMENTS BY LOCATION - 2012



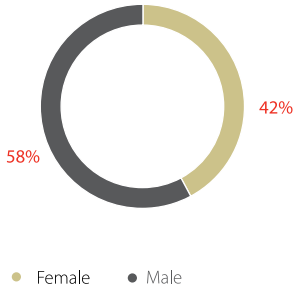
Sustainability Report

Attrition - By Gender

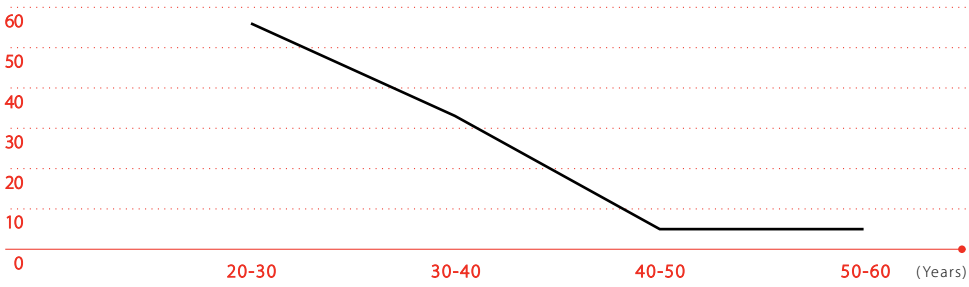
Gender	No.	%
Female	24	42
Male	33	58
Total	57	100

Rate - 5%

ATTRITION - BY GENDER - 2012

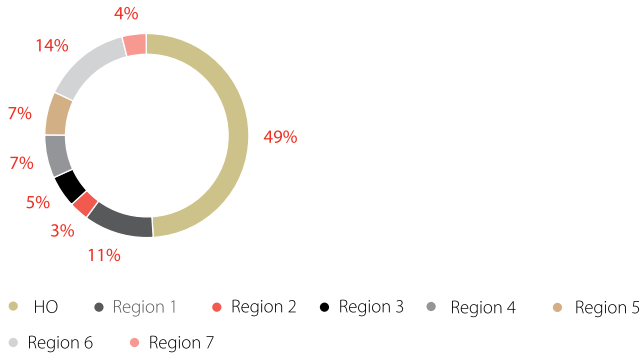


ATTRITION - BY AGE (2012)
(%)



NDB's attrition rates have always been positive and consistently remained below industry levels.

ATTRITION BY LOCATION - 2012



Benefits Provided to Full-Time Employees that are not Provided to Temporary or Past-Time Employees, by Significant Locations of Operations (LA 3)

Beyond basic remuneration, full-time employees of the Bank receive a package of benefits. Staff loans are granted to employees in three main categories - housing, vehicle and sundry, with a view to improving their living standards. With effect from November 2010, employees were given the option of combining their staff housing loan and vehicle loan entitlements to fund a single need - either to meet housing requirements or to acquire a vehicle. The greater diversity of its workforce made the Bank realize that an equally diverse set of needs exists towards the enhancement of the quality of life. Therefore the Bank believes that this policy revision would assist employees in prioritizing their needs and help them to acquire assets that are in line with their expectations.

Within the package of benefits are also Critical Illness Cover, In-house OPD Facilities and Insurance for instances of hospitalization. The insurance covers health care as well as disability coverage.

All female employees who have no children or one child is entitled for 84 days maternity leave and any female employee who already has two or more children is entitled for 42 days of maternity leave. At NDB employees are also given the opportunity to utilize their medical as well as vacation leave together with the maternity leave entitlement.

Male employees are not yet entitled for paternity leave at NDB as this concept is yet to be reviewed by the regulatory authorities in Sri Lanka.

Based on this compensation philosophy the Bank continues to reward staff with potential on the short term and keeps them engaged over a longer period of time through incentive plans such as the Equity-Linked Compensation Plan (ELCP). Equity-Linked Compensation Plan is another significant long-term incentive plan introduced for the Senior Management and reports to Senior Management who are at the strategic decision-making table. This initiative aims at aligning shareholder and management interests, retention of key/critical talent of the Bank, rewarding high potentials in creating a performance-driven culture and attracting high calibre talent essential to enable the Bank's growth objectives. Whilst all these were done to encourage good performance, steps were taken to manage poor performance as well in the spirit of bringing about a "performance-driven culture".

The following summary depicts the entitlements of a permanent employee and an employee on contractual basis:

Permanent Employees	Contract Employees
Vehicle Loan	Not Applicable
Housing Loan	Not Applicable
Sundry Loan	Not Applicable
Medical Insurance	Covered but entitlement differs
EPF/ETF	EPF/ETF
Gratuity	On principle staff not retained longer than 4 years on contractual basis
Leave	Entitlement differs
Overtime	Not Applicable
Allowances (Risk Allowance/Accommodation Allowance/Holiday Allowance)	Travelling Allowance - Conditions apply
Leave encashment (NDB Employees)	Not Applicable
Cafeteria/Gymnasium/Library	Cafeteria/Gymnasium/Library
Recreation Club Activities	Recreation club activities
Club Memberships and Subscriptions	Not Applicable
Training and Foreign Training Opportunities	In-house training opportunities

Composition of Governance Bodies and Breakdown of Employees per Category According to Gender, Age Group, Monitory Group Membership, and Other Indicators of Diversity (LA 13)

- Percentage of individuals with the HR governance bodies.

  The HR subcommittee consists of 5 members including the Chief Executive Officer, 2 Chief Operating Officers, Chief Financial Officer and the Vice-President Human Resources.

Over 50 - 2 - 40%	2 - Female Employees
30 - 50 - 3 - 60%	3 - Male Employees

- Remuneration and Human Resources Committee

  The Remuneration and Human Resources Committee consists of 6 Directors out of which -

Over 50 - 4 - 67%	1 - Female member
30 - 50 - 2 - 33%	5 - Male members

Society

Percentage of Operations with Implemented Local Community Engagement, Impact Assessments, and Development Programmes (SO 1)

The Bank engages the local community wherever possible and during the last financial year 23% of the CSR projects implemented were done with local community engagement. These development projects are closely monitored by the Bank with regular follow-up conducted by the Bank's staff which includes the closest Branch. The impact assessments are conducted by the Bank's staff, where they visit the project after completion. The staff reviews the project with the main stakeholders, obtaining feedback from them and any concerns raised are addressed.

The impact of operations on the communities are assessed and monitored by the Bank's staff which includes the branch staff. The staff visits the project initially to assess the need. During this visit the staff speak to the main stakeholders and obtain the required information. For example if the need is to renovate a school building, the staff inspect the site and assess the requirement. Thereafter depending on the need a professional valuation is carried out with quotations etc. obtained. Once the project and cost is approved the work would commence. During implementation the staff would visit the project several times and assess the work done. Progress reports would also be obtained from the main stakeholder, for example if the project is to renovate a school building the principal or one of the coordinating teachers would send regular progress reports. The staff would also be in constant contact with the stakeholder and on call to handle any situations or issues that arise. Once the project is completed the staff would visit the site again and ensure that the work has been completed as per the requirements. Thereafter the staff handover the project and keep a close follow-up on the project. Site visits are conducted and the staff would keep in contact with the stakeholders.

Examples of feedback obtained by an external party for previous CSR projects conducted for schools are given below:

Behavioural Changes and Skills Development

Ms Kumari, the Biology Teacher at S D S Jayasinghe College - *"After the renovation of the lab, the students' knowledge about the subject has increased and the number of A/L students selecting biology has doubled and both A/L and O/L students look forward to coming for lab sessions."* According to an A/L student, Isuru Chathuranga, who does biology as his primary A/L subject, *"Now the teachers don't have to keep demonstrating the practicals. The students have the chance to do practicals on their own. The subject is now more interesting and understandable."* Both students and teachers agreed on the fact that the students have a better knowledge about the subject and its practical side as well.

Ms Ramani, who is in charge of the newly built home science room in Dharmashoka Vidyalaya explained, that the students are very interested in the subject and even male students show an interest to cook. According to her, before the home science room was constructed, students and teachers had to go to the science lab for cookery lessons, but the teachers did not like this because it was very risky to handle the gas cooker where there are chemicals. Therefore, they had to take the gas cylinder outside, which took half of the period, and by that time, there was not much time left for the lesson. Ms Ramani is now very happy because of the fact that they have a seperate home science room and said, *"Now we have more time to teach the students rather than preparing for lessons throughout half of the period"*. A Grade 8 student Sanduni, who uses the home science room for the subject practical and technical skills said, *"We are very happy with the facilities given and we love to cook food and share it"*.

According to the Principal at Dharmashoka Vidyalaya, another behavioural change that could be seen in the school is that the students are more involved in the lessons and stay in their class rooms. She further explained, *"Before we got water facilities, we could see students here and there all the time, even between lessons, going in search of water"*. One student recalled, *"We had to go all the way to the nearest temple to collect water"*.

Vice-Principal of a Roman Catholic School said, *"It is easy to control the students now, because in their free time, they tend to go to the library and borrow a book and read, rather than running here and there"*. And she said, with a smile on her face, that though the children are better behaved, they tend to sneak into the play area. The Principal at the school said, *"The children are eager to come to school every day to play in their new play area and to get books from the library"*. She explained that most of the children in this school are from underprivileged families nearby, and do not have any proper place to play or study at home. After the changes introduced to the school by the Bank, the students' attendance has increased and the teachers are well-motivated to teach as the environment in the school has become more suitable for teaching.

The teachers at a Roman Catholic Primary School further explained that, out of the activities which are essential for the skills development of students in grade one and two, 80% are outdoor activities and 20% are indoor activities. According to the rules and regulations of the primary education, a play area in a school is mandatory for these outdoor activities. Thus, the play area has immensely helped for skill development of the students. The reading skills of the students too have increased, due to the regular use of the library.

Though most of the beneficiaries admitted that there are behavioural changes, some said these changes have only helped to make their day-to-day lives easier and others said these changes did influence their lives to a certain extent. It was understood through interviewing children especially, that their home lives have changed. One student from the Dharmashoka Vidyala said, *"Now I help my mother to cook at home from the knowledge I gathered through home science lessons".* Another primary student from the Roman Catholic School said, *"I borrow a book from the school library everyday and read it with my younger sister".*

Percentage of Employees Trained in Organization's Anti-corruption Policies and Procedures (SO 3)

100% - All new recruits undergo a compulsory corporate induction programme and they are familiarized with the main aspects of the policies and procedures governing organizational ethics and practices. Anti-corruption policies are covered during these sessions.

Product Responsibility

Practices Related to Customer Satisfaction, Including Result of Surveys Measuring Customer Satisfaction (PR 5)

Ultimately, our entire effort is for one purpose only - to satisfy and exceed customer expectations. This is the pivotal point from which all else flow.

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NDB maintains a comprehensive online complaint management system where complaints are resolved within a stipulated time frame based on the nature and complexity of the complaint.

Continuous improvement continues to flow, based on the feedback received in customer surveys and from ongoing customer feedback on products and services.

Several cross functional teams have been appointed from within the Group with the objective of identifying strategic initiatives for value creation, product innovation and synergy across the Group towards building the NDB Brand. These teams play a pivotal role in triggering the overall Group strategy through the implementation of key initiatives across customer segments via customized products and channels, whilst leveraging the Bank's competitive strengths and market dynamics.

NDB encourages continuous innovation through its automated, suggestion generating system - 'IdeaXpress' - which is an IT tool that can be accessed by all employees in the Bank in order to share innovative ideas and customer insight.

Satisfying the customer requires that the Bank is scrupulously fair and transparent in all its communications, whether it be in its marketing communications with them, adherence to pertinent regulations and other such areas.

In compliance with the Customer Charter laid out by the Central Bank of Sri Lanka, the Bank has made the following arrangements to ensure product ownership with regard to marketing communication:

- Details of products offered at branches could be found on printed material such as leaflets, posters and the like, prominently displayed at branches for easy access.
- Details of all products are also available on the Bank's website along with the details of relevant contact persons, thus providing the customer easy access to information.
- A 24-hour Customer Service Hotline also serves customers every day, throughout the year.

All the systems we have in place, together with sound and ethical strategy and enterprise of the Bank have ensured that NDB has not recorded any transgressions, violations or breach of regulations concerning responsible customer communication.

Programme for Adherence to Laws, Standards and Voluntary Codes Related to Marketing Communications Including Advertising, Promotion and Sponsorship (PR 6)

All marketing communications and branding activity are conducted in compliance with the NDB Communications Policy, which is an internal document that provides guidelines for conducting communication activity in adherence to laws and accepted standards governing the industry and voluntary codes set by the Bank.

The Communication Policy encourages effective internal and external communications of corporate information in relation to the Bank, covering all stakeholders including staff, customers, creditors, shareholders, partners, general public and regulators. The policy covers objectives, division of responsibilities and general guidelines for communicating with various target groups. The main purpose of the Communication Policy is to establish guidelines for presenting the Bank to current and potential stakeholders, both internally and externally.

The Communication Policy encompasses the following aspects:

1. The communication of public and non-public information.
2. Communications with media, shareholders, regulators and other stakeholder groups.
3. Business communication and usage of email, etc.
4. Social media activity (such as: involvement in online conversations about the Bank, expressing of opinions with regard to the Bank, posting pictures of the Bank interior or exterior, etc.).
5. Fraud and confidentiality and protecting of confidential information.

The policy is recommended and endorsed by the Board of Directors of the Bank and is made available to all staff members via the Bank's intranet portal.
The Policy is reviewed annually or as and when the need arises to do so.

*** The Bank has not provided any product or service that has been banned or deemed inappropriate. The Bank's range of products and services are all accepted by the related regulatory bodies governing the industry (Central Bank of Sri Lanka, Securities and Exchange Commission, Colombo Stock Exchange and other Regulatory authorities including but not being limited to the Registrar General's Department).*

Total Number of Incidents of non-compliance with Regulations and Voluntary codes concerning Marketing Communications, Including Advertising, Promotion, and Sponsorship by type of outcomes (PR 7)

There were no incidents of non-compliance with regulations and voluntary codes concerning marketing communications, including advertising, promotion and sponsorship by type of outcomes during the reporting period.

Sustainability Report

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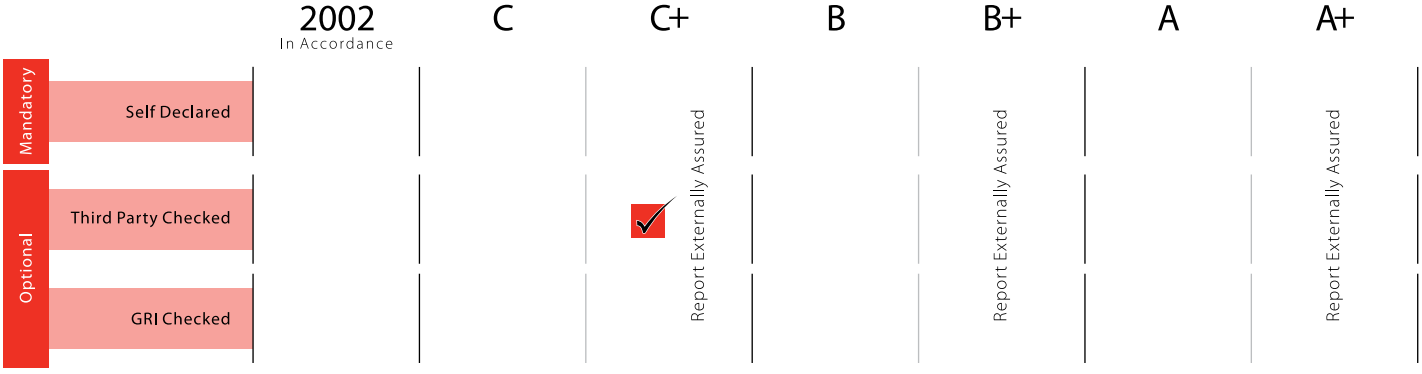

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INDEPENDENT LIMITED ASSURANCE REPORT TO NATIONAL DEVELOPMENT BANK PLC

On the Sustainability Report for the Year ended 31 December 2012

Introduction

We were engaged by the Board of Directors of National Development Bank PLC to provide limited assurance on the following sustainable development performance indicators ("the selected performance information") as set out on pages 125 to 143 of the National Development Bank PLC 2012 Annual Report ("the Report").

Management's Responsibility and the Criteria Applied

Management is responsible for the preparation and presentation of the Report in accordance with the GRI Sustainability Reporting Guidelines as described in the Report, and the information and assertions contained within it; for determining the National Development Bank PLC's objectives in respect of sustainable development performance and reporting, including the identification of stakeholders and material issues; and for establishing and maintaining appropriate performance management and internal control systems from which the reported performance information is derived.

Our Responsibilities and Compliance with SLSAE 3000

Our responsibility is to carry out a limited assurance engagement and to express a conclusion based on the work performed. We conducted our engagement in accordance with Sri Lanka Standard on Assurance Engagements SLSAE 3000: Assurance Engagements other than Audits or Reviews of Historical Financial Information, issued by the Institute of Chartered Accountants of Sri Lanka.

Summary of Work Performed

A limited assurance engagement on a sustainability report consists of making inquiries, primarily of persons responsible for the preparation of information presented in the sustainability report, and applying analytical and other evidence gathering procedures, as appropriate. These procedures included:

- Inquiries of management to gain an understanding of National Development Bank PLC processes for determining the material issues for National Development Bank PLC key stakeholder groups.
- Interviews with relevant staff at business unit level responsible for providing the information in the Report.
- Inquiries about the design and implementation of the systems and methods used to collect and process the information reported, including the aggregation of data into information as presented in the Report.
- Comparing the information presented in the Report to corresponding information in the relevant underlying sources to determine whether all the relevant information contained in such underlying sources has been included in the Report.
- Reading the information presented in the Report to determine whether it is in line with our overall knowledge of, and experience with, the sustainability performance of National Development Bank PLC.

The extent of evidence gathering procedures performed in a limited assurance engagement is less than that for a reasonable assurance engagement, and therefore a lower level of assurance is provided.

Our Conclusion

Based on the procedures performed, as described above, nothing has come to our attention that causes us to believe that the above selected performance information in the Report is not prepared, in all material respects.

CHARTERED ACCOUNTANTS
Colombo
22nd February 2013

KPMG, a Sri Lankan Partnership and a member firm of the KPMG network of independent member firms affiliated with KPMG International cooperative ("KPMG International"), a Swiss entity.

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C.P. Jayatilake FCA
Ms. S. Joseph FCA
S.T.D.L. Perera FCA
Ms. M.P. Perera FCA
T.J.S. Rajakarier FCA
Ms. S.M.B. Jayasekara ACA
G.A.U. Karunaratne ACA
P.Y.S. Perera FCA
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W.K.D.C. Abeyrathne ACA
R.M.D.B. Rajapakse ACA

Principals - S.R.I. Perera ACMA, LLB, Attorney-at-Law, H.S. Goonewardene ACA

Risk Management

Overview

The recent misfortunes in financial and non-financial firms and in Governmental agencies point up the need for more stringent risk management practices. Financial misadventures are hardly a new phenomenon, but the rapidity with which economic entities can get into trouble is. As such, one of the key challenges faced by the financial sector today is to strike a balance between risks and return. The ability of a Bank to take strategic initiatives within pre-defined and consistent risk framework can be considered as a speciality that can make a distinction for a bank and ensure safety for all the stakeholders in today's competitive market. Thus risk management is an integral part of banking business.

The global economic crisis has provided an opportunity for a fundamental restructuring of the approach to risk and regulation in the financial sector.

The Board is required to define the risk appetite for the Bank and is responsible for the activities and overall performance of the Bank. This risk appetite supports effective decision-making, capital allocation and is central to embedding risk management in business decisions and risk reporting across the Bank.

Recent Learnings and Risk Management

Rapid economic development and change of business in both local and global economies provide opportunities but at the same time is a challenging task under risky economic environment. A sound and accurate risk management process is an essential part of our business norm to deliver superior shareholder value by accomplishing an appropriate degree of trade-off between risk and return.

During 2012 the financial markets were dominated by concerns over sovereign debt default risk within the peripheral Eurozone countries and possible impact across core Eurozone countries. Middle East turmoil, fiscal deficit of US economy and the perception that the world economic recovery remained fragile and continued to cause concerns.

The rapid depreciation of the Rupee with the cessation of Central Bank intervention in the domestic forex market in early 2012 exposed the Banks to highly volatile market conditions as a result of forex dealers adjusting to the vibrant market-driven policy framework.

Within the challenging economic and financial environment, we actively managed our risk profile by close monitoring of portfolios and reducing exposures to the most likely areas of stress. Our top and emerging risk monitoring framework supports our approach to forward looking risk identification and focus on appropriate stress tests required to evaluate the potential impact of emerging scenarios.

A strong and pervasive integrated risk management culture provides a bank with a sound foundation of risk management framework consistent with the Bank's objectives, risk tolerance, control standards and management philosophy. In risk management, robustness is more important than sophistication. In an organization everyone is, a risk manager - or should be - and organizations need dynamic risk officers to direct and embed a culture of risk management across the organization.

The objectives of the risk management frame work are -

1. To establish common principles, standards to identify, measure and manage all risks and to inform behaviour across the Bank.
2. Provide a shared framework and language to improve awareness of risk management processes.
3. To provide clear accountability and responsibility for risk management.

Integrated Risk Management at NDB

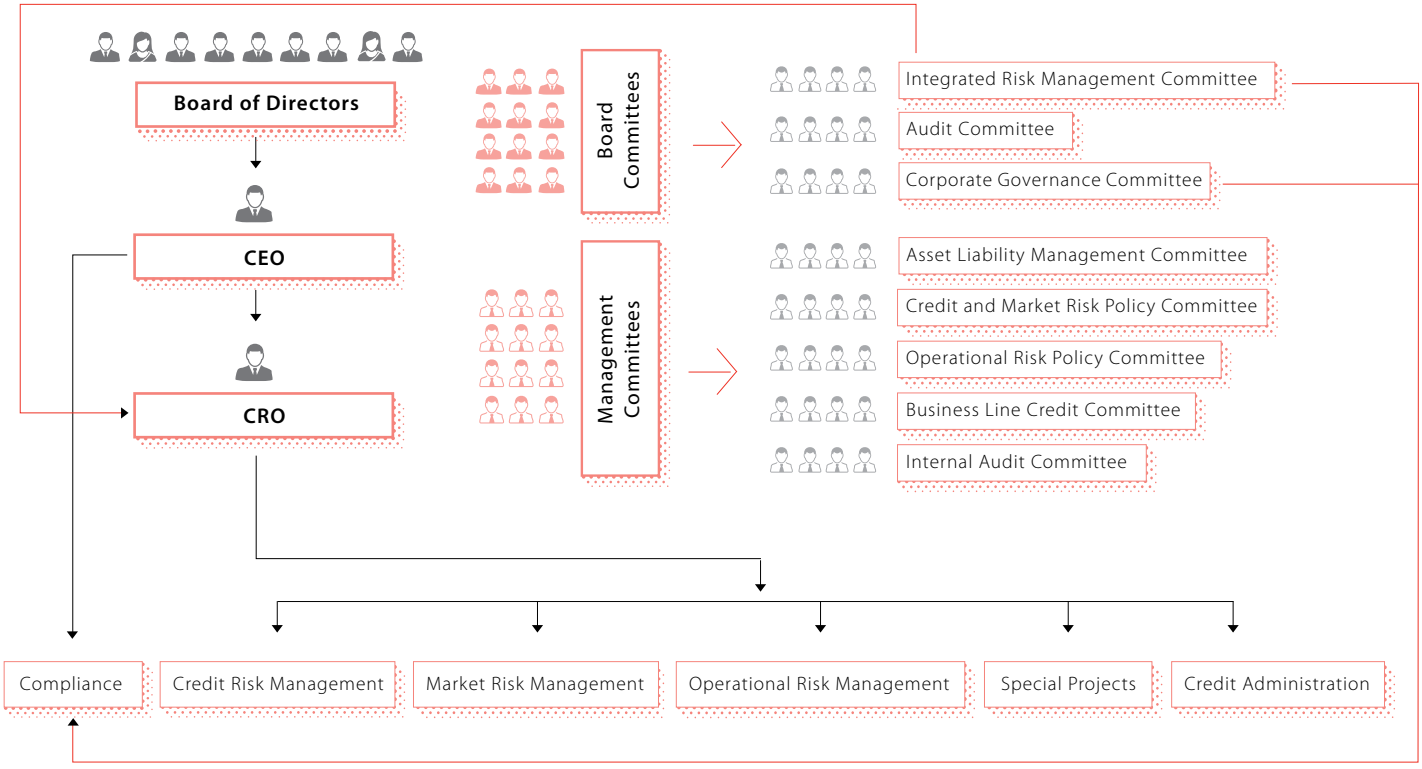
NDB promotes a strong risk management culture supported by a robust risk governance structure. The Bank's Risk Management Unit is assigned with the responsibility to design and operate the Bank's integrated risk-management process and is independent of the Bank's business units. Its risk management framework is integrated with the Bank's strategy and business planning processes. An integrated risk capital framework is consistently applied across all business units to protect its capital base and support effective capital management. Maintaining our capital strength and strong liquidity position is the main focus through our risk appetite framework. We ensure that our portfolios/exposures remain aligned to our risk appetite and strategy whilst proactively managing our risks supported by strong forward looking risk identification.

Management committees in operation together with the Board subcommittees (as detailed below) undertakes this task by supporting business decisions in an objective manner and ensures alignment of risk/reward within business strategy.

- Board Integrated Risk Management Committee (IRMC)
- Board Audit Committee (BAC)
- Corporate Governance and Legal Affairs Committee
- Asset Liability Management Committee (ALCO)
- Credit and Market Risk Policy Committee (CMRPC)
- Operational Risk Policy Committee (ORPC)
- Credit Committees for each business Line
- Internal Audit Committee

Risk Management

Risk Governance Structure



The Board Integrated Risk Management Committee (IRMC) meets quarterly to review and assess the Bank's overall risks and to focus on policy recommendations and strategies in an integrated manner. The IRMC Charter was formulated in line with the regulatory guidelines and is approved by the Board of Directors.

The Board Audit Committee is entrusted with the responsibility of ensuring the Bank's compliance with its internal and external regulatory guidelines and meets on a quarterly basis to address, assess and recommend management action on any matters of concern.

The Bank's Assets and Liabilities Committee (ALCO) reviews all market and liquidity-related exposures, on a monthly basis and decisions are made to facilitate the business requirements and make investment/policy decisions. These decisions are further reviewed/approved at IRMC and the Board.

The Credit and Market Risk Policy Committee and Operational Risk Policy Committee are in operation to formulate policies and to focus more clearly on defined risk areas. These committees comprise of the CEO, COO, CRO, CFO and the Heads of Business Units, Treasury and representatives of the Group Risk Management. The committees meet regularly to review the Bank's risk policy framework, overall performance and the potential risks faced by specific lines of business and support functions.

There are four credit committees representing separate business lines and members comprise of senior officers of business units and risk management The committees meet on a weekly/ monthly basis to assist in the process of pre-clearance of large credits, approvals, reviewing portfolio and watch listed clients etc.

Our proactive approach towards risk identification and mitigation has given us the ability to absorb shocks arising from financial and economic stress scenarios and be more resilient and competitive in the market.

The Bank thrives on innovation to deliver new products which would cater to the growing and evolving needs of our customers. Risk management is a key aspect of product development and all new products are supported by products programmes which are reviewed and approved by all stakeholders including the compliance unit prior to the launch. These product programmes are reviewed independently by Internal Audit and are subject to annual review.

The Bank recognizes the different types of risk, based on the origin and nature and manage each risk area with diligence. These risks could be mainly categorized as follows:

- Credit risk
- Market risk
- Liquidity risk
- Operational risk
- Strategic risk
- Legal Risk
- Reputational risk

Credit Risk

Credit risk is the risk of financial loss if a customer or counterparty fails to meet a payment obligation under a contract. It arises principally from direct lending, trade finance and leasing business, and also from Off-Balance Sheet products such as letters of credit and guarantees. Credit risk generates the largest regulatory capital requirement of the risks we incur. The Bank manages the credit risk in the entire portfolio as well as individual credits or transactions with a view to minimise the non-performing loans and also to manage any concentrations as well as to maximise returns.

Risk Management

Credit Risk Management at NDB

Credit risk management reviews and manages the credit process from origination to collection. NDB has a well-defined credit policy approved by the Board of Directors. It defines the

- credit culture of the Bank,
- target markets for lending,
- prohibited lending which the Bank under no circumstances will entertain due to either the very high risks involved in such proposals and/or its negative social/ethical consideration,
- acceptable risk parameters,
- remedial and recovery actions.

The following principles guide credit risk management across the Bank:

- Diligently manage its risk asset portfolio to ensure that the risk of excessive concentration to any industry, sector or individual customer is minimized;
- Ensure that exposures to any industry or customer are determined by the regulatory guidelines, clearly defined internal policies, debt service capability and Balance Sheet management guidelines;
- Extend credit to only suitable and well-identified customers and never where there is any doubt as to their ethical standards and record;
- Never extend credit where the source of repayment is unknown or speculative nor where the purpose/destination of funds is undisclosed;
- Never take a credit risk where ability of the customer to meet obligations is based on the most optimistic forecast of events. Risk considerations shall have priority over business and profit considerations;
- Ensure that the primary source of repayment for each credit is from an identifiable cash flow from the counterparty's normal business operations or other financial arrangements; the realization of security remains a fall-back option;
- Adopt a pricing mechanism that reflects variation in the risk profile of various exposures to ensure that higher risks are compensated by higher returns;
- Ensure that products to be sold in the retail market are backed by approved product programmes;
- Avoid all conflict of interest situations and report all insider-related credits to appropriate bodies;
- The financial performance of borrowers is to be continuously monitored and frequently reviewed, as is the manner in which the borrower operates his accounts.

Governance - Delegation of Authority

Final authority and responsibility for all activities that expose the Bank to credit risk rests with the Board of Directors and the Board of Directors has delegated approval authority to the CEO, with authority to re-delegate limits to the Executive Credit Committees and the Business Lines. All approval limits are name specific and are based on the individual experience, facility type, collateral in order to ensure accountability and mitigate any judgmental errors. There are four Executive Credit Committees representing the four Business Lines and these committees comprise senior officers of business units as well as Risk Department. The delegated authority limits are reviewed periodically and the Bank follows the 'four-eyes principle' (i.e., minimum of two officers signing a credit proposal). Lending decisions are based on detailed credit evaluation carried out by Relationship Managers and reviewed/approved by designated approving authority/ Risk Management.

Strategy and Priority

The credit risk management strategy ties into the overall corporate strategy and is focused on making the Bank a clear leader in sound risk management practices. This is governed by the following:

- High-quality assets measured by the following Key Performance Indicators:
  1. Ratio of non-performing loans to total loans;
  2. Ratio of loan loss provision to gross non-performing loans.
- Financial and prudential ratios should be at a level more conservative than the regulatory requirements and better than the average of benchmark banks.

Asset Quality

Risk management works closely with the Bank's business units at every stage of the credit process, from facility origination to approval to collections, adding value as appropriate and developing the proposal in terms of risks, mitigants and returns. A post-sanction review and monitoring mechanism is in place to ensure quality of credit is not compromised. Any deteriorating credits with emphasis on internal and external early warning signals are identified and such accounts are "Watch Listed". The Watch Listed clients are monitored closely with quarterly reports submitted to the Executive Credit Committee. Further, based on the Watch Lists the Bank assesses the portfolio at risk in the event, such accounts deteriorates further. Non-performing assets are identified at an early stage, enabling management to take action as appropriate.

This process has enabled the Bank to control and maintain a low NPL ratio of 1.3% when compared to the industry ratio of 3.6%.

Non-performing accounts have been recognized, classified and provisions made as appropriate in line with the Prudential Guidelines, giving loan loss coverage of 100%.

Non-performing exposures are defined as exposures with past due obligations >90 days. Loans move from performing status to substandard, doubtful and loss, depending on objective criteria based on the number of days past due as shown below:

	December 2012 Rs Mn
Performing	115,683
Non-performing	1,558
Special mention	317
Substandard	270
Doubtful	66
Loss	905
Total	117,241

Non-performing loans/total loans ratio for the period was 1.3%.

Impairment as per SLAS 44 and 45

In line with the requirements of SLAS 44 and 45 the Bank has identified the probable factors to assess objective evidence on account of individually significant loans and parameters for impairment on a collective basis. The Bank has also engaged an external party to assist with the initial transition. Further, the new Credit Rating System to be implemented will facilitate the Credit Impairment Calculations.

Collateral Policy

Collateral policy differs from business line to business line according to the products offered. Borrower's cash flows and income-generating capacity is the prime consideration. Collateral is only a second way out.

The main types of collateral taken by the Bank are immovable and movable property mortgages, cash deposits and corporate and personal guarantees. It is the Bank's policy to be on a *pari passu* status with other lenders. This position would change only if supported by strong financials of the entity financed. This policy is mainly applicable to corporate clients. Facilities under Product Programmes are governed by guidelines given in such individual programmes.

In instances where facilities are granted without collateral the Bank ensures that its position will not be subordinated to other creditors interests. In such instances, the Bank generally requires either a negative pledge agreement not to encumber any assets without prior permission of the Bank or a *pari pasu* clause, whereby the debtor will treat the Bank equally with respect to collateral with all current and future lenders.

The Bank has a panel of valuers who have been selected based on the criteria set out by Regulator. The Bank ensures that the valuations are carried out and reviewed as follows:

Facilities in NPL

- For facilities granted against residential property occupied by the borrower for residential purposes: every four years.
- For all other NPL facilities: every three years.

Performing facilities

- Watch listed clients with working capital facilities - every three years
- Single 'A' rated clients with working capital facilities - every five years

No value is considered if valuations are not in line with the time frames set out as per the Regulatory Guidelines.

Internal Risk Ratings of Obligors

The credit portfolio of the Bank is risk-rated using an internally-developed system that takes into account quantitative as well as qualitative factors. The rating scale ranges from Triple A to B4 and the ratings of every obligor is reviewed at least annually or more frequently if required. This rating system is used as a guide for account monitoring, provisioning/collective impairment, granting delegated authority and pricing. Based on the year-end figures the portfolio is concentrated in the 'Single A' category which represents a quality portfolio.

The Bank has also initiated steps to revise the current practice of rating with a more robust risk rating system which will have the capability of predicting the Probability of Default (PD) of the borrower. This would facilitate to measure the profile of the credit portfolio in an objective manner.

Prudential Limits

The industry and portfolio limits are set by the Board of Directors on the recommendation of the Risk Department. Credit risk management monitors compliance with approved limits.

The process of setting the limits is as follows:

The Bank engages in a detailed portfolio plan annually. In drawing up the plan, the Bank reviews the macroeconomic factors, identifies the growth sectors of the economy and conducts a risk rating of the sectors to determine its acceptable target market industries and exception. The Bank's target loan portfolio is then distributed across acceptable target market industries, strategic business units and approved product programmes -

- Substantial Exposure Limit - Aggregate large exposure limit of not more than 500% of the Bank's capital base.
- Industry/Economic Sector Limits - Exposure to any single industry of not more than 15% of its loan exposure.
- Single Obligor Limits - Limits are imposed on loans to individual borrowers. The regulatory lending limit is 30% of its Capital Base. However, the internal guidance limit is set at 25% of Capital Base to create a prudent buffer.
- Group Obligor Limits - Limits are imposed on loans to group of companies/individuals. The regulatory lending limit is 40% of its Capital Base dependent on the rating of bank client and capital ratios of the Bank. However, the integral guidance limit is set at 37% of Capital Base to create a prudent buffer.
- Prudential Group Exposure Limit - Given the possible impact to a 'Group of Related Parties', in an event of a management failure and the possible impact to the Group, the Bank has put in place an 'Internal Prudential Group Exposure Limit'. Under this arrangement, a 'related party' includes a company, an individual, a firm/partnership etc. When considering a group of related parties, in addition to the substantial interest through shareholding (direct shareholding), indirect shareholding and the management control is also identified if the majority of the Directors are nominated by one another or the management is otherwise controlled by the other.

Market Risk

Market risk is the risk in movements in market factors such as foreign exchange rates, interest rates, equity prices, credit spreads and commodity prices, that could reduce our income or the value of our portfolios.

Financial institutions are exposed to market risk in a variety of ways. Exposure may be explicit in portfolios of securities, equities and other actively-traded instruments, or it may be implicit - manifesting itself, for example, as interest-rate risk arising from a mismatch of loans and deposits.

Exposures to market risk in portfolios are of two fold:

- Trading Portfolios - Positions arising from market-making and position-taking and others designated as marked to market.
- Non-Trading Portfolios - Positions that primarily arise from the interest rate management of our retail and commercial banking assets and liabilities, financial investments designated as available for sale and held to maturity.

The associated market risks are:

- Exchange risk, the risk that foreign exchange rates and/or the implied volatility will change.
- Interest rate risk, the risk that interest rates and/or the implied volatility will change.
- Equity risk, the risk that stock prices and/or the implied volatility will change.
- Commodity risk, the risk that commodity prices and/or implied volatility will change.

Market Risk Management at NDB

Our objective is to manage and control market risk exposures in order to optimise return on risk whilst ensuring that the Bank is not exposed to unexpected losses.

Market risk in 2012 was managed against a backdrop of global economic slowdown, the fiscal deficit of the US and concerns over European sovereign debt and its contagion effects. Funding and capital concerns relating to financial institutions also dominated in Europe. All these factors triggered high levels of volatility in the financial markets where we continued to selectively manage our exposures to countries/regions with high vulnerability and adjusted our risk appetite and exposures to mitigate any adverse consequences.

During the highly volatile conditions in the foreign exchange market and the depreciating scenario of the Rupee, we managed our forex exposures and open positions effectively maximizing the market potential within our risk parameters and to the best interest of the Bank.

Bank's comprehensive risk management framework covers the market, liquidity, asset and liability risks and proactively manages the exposures against the pre-defined risk parameters.

Risk Management

Prudential internal limits have been defined for liquidity risks, price risks, exchange risks and asset/liability risks for close monitoring of exposures. All exposure limits are linked to the Bank's capital base to ensure adequate and efficient capital allocation/planning. These limits are subject to annual review and are approved by the Board.

Additionally, sensitivity analysis, stress tests, scenario analysis and mark to market exercises are carried out on products, portfolios and Balance Sheet on a regular basis as forward looking analytical tools for managing exposures.

Sensitivity Analysis

Daily sensitivity analysis is carried out on major foreign currency Net Open Positions (NOP) giving positive and negative shocks to the spot rates to determine the impact on the P/L. Bank's Balance Sheet too is subject to sensitivity analysis based on the duration of its interest sensitive assets and liabilities which is carefully managed within the set limit.

Exchange rate sensitivity of major foreign currency open positions as at 31 December 2012.

		LKR Depreciate ←				→ LKR Appreciate		
Spot Rate Shocks		-5.0%	-2.5%	-1.0%	**Spot Rate**	1.0%	2.5%	5.0%
Currency	Net Open Position							
USD	(4,798,911)	(30,653,046)	(15,326,523)	(6,130,609)	**127.75**	6,130,609	15,326,523	30,653,046
GBP	(27,854)	(288,835)	(144,417)	(57,767)	**207.39**	57,767	144,417	288,835
EUR	260,501	2,199,826	1,099,913	439,965	**168.89**	(439,965)	(1,099,913)	(2,199,826)
JPY	6,232,700	458,960	229,480	91,792	**1.47**	(91,792)	(229,480)	(458,960)
AUD	157,014	1,042,539	521,270	208,508	**132.80**	(208,508)	(521,270)	(1,042,539)
Total		(27,240,555)	(13,620,277)	(5,448,111)		5,448,111	13,620,277	27,240,555

The possible impact of exchange rate movements on the NOP of major Foreign Currency Positions are monitored to evaluate the impact on the P/L and ensure it is within acceptable levels.

Interest Rate Sensitivity of the Balance Sheet as at 31 December 2012.

Modified Duration and Price Sensitivity of Assets and Liabilities

As at 31.12.2012	Duration	Total Balance LKR mn	Price Sensitivity DEC
Assets:			
Overdrafts - LKR	2.02	18,547	374.65
Short-Term Loans	0.12	13,983	16.68
Project Loans Fixed	1.46	11,115	162.16
Refinance Loans	1.83	1,384	25.38
Securitization Loans	0.35	6,582	23.04
Post-Import Finance - LKR	0.12	10,123	12.26
Fixed Retail Loans	1.18	1,061	12.54
Fixed DM Loan	1.70	5,598	95.17
Raththaran Loans	0.50	138	0.69
Vishmitha/Cash Back	1.47	853	12.52
Fixed Housing Loans	3.00	4,915	147.68
Variable DM Loans	0.40	4,515	18.06
Staff Loans	2.00	1,215	24.31
Pawning	0.46	3,706	17.14
AF Lease	1.25	5,831	72.88
Hire Purchase	1.45	468	6.79
Deposits Placed - LKR	0.16	1,875	3.01
Investments in Treasury Bills	0.27	3,600	9.64
Investments in Treasury Bonds	1.22	15,506	189.47
Investments in T Bills Trading	0.71	487	3.45
Investments in T Bonds Trading	0.58	577	3.32
Reverse Repos	0.01	3,098	0.25
Total assets			1,231.09

Risk Management

As at 31.12.2012	Duration	Total Balance LKR mn	Price Sensitivity DEC
Liabilities:			
Demand Deposits - LKR	1.39	8,429	117.31
Savings Deposits - LKR	3.25	10,726	349.03
Call Deposits - LKR	3.18	1,097	34.93
Margin Deposits - LKR	3.36	105	3.53
Term Deposits - LKR	0.48	58,862	282.54
Repurchase Agreements	0.09	12,348	10.98
Borrowings LKR	0.01	1,550	0.16
Borrowings Other	1.69	2,188	37.02
Credit Lines Fixed	3.10	7,761	240.59
Credit Lines Variable	3.10	2,641	81.87
Debentures	2.80	400	11.20
Total liabilities			1,169.15
Net Price Sensitivity			61.90
Limit			150.00

Modified Duration - Measurement of the portfolio to a 1% change in interest rates.
Price Sensitivity - Sum of value change in each portfolio due to a 1% change in interest rates.

The price sensitivity of the Balance Sheet was managed with in the pre-defined risk parameters whilst maximizing the market potential on interest sensitive assets and liabilities.

Stress Testing/Scenario Analysis

Bank's net foreign currency position is tested on a daily basis under three stressed scenarios giving adverse shocks of 5%,10% and 15% to the exchange rate to arrive at the maximum loss scenarios the Bank is exposed and is monitored against the limits set. Stress tests on liquidity are being carried out to ensure liquidity under stressed scenarios.

Limit is set at the minimum level of shock (Scenario 1) as an early warning where the Bank will take action to ensure that it does not surpass the first level of shock and reach worse case scenarios.

Bank's foreign currency Net Open Position stress test results as at 31 December 2012.

	Net Position (in USD) as at 31.12.12	Scenario 1	Scenario 2	Scenario 3	Limit on Scenario 1 (In LKR)
Magnitude of Shock (Adverse)	–	5%	10%	15%	
Spot Rate movement	127.75	134.14	140.53	146.91	
Position - Profit/Loss	(4,245,014)	(27,115,029)	(54,230,057)	(81,345,086)	(102 mn)

The stress results of the Bank's overnight Net Open Position is managed well within the risk limit and monitored on a daily basis.

Liquidity Stress Test Results as at 31 December 2012.

Stress Testing for Liquidity Risk

Banks Average Liquid Asset Ratio for the month - 23.6

Stress Testing on Liquid Asset Ratio

		Magnitude of Shocks on Liquid Asset Ratio		
Scenario No.	Stress Scenarios**	5%	10%	15%
		Revised LAR. after Relevant Shocks		
1	Adverse Impact on MM & Institutional Borrowings/Drop in Market Liquidity	22.94	22.23	21.51
2	Run Down on CASA & Time Deposits	20.76	17.67	14.32
3	Impact on Total Liquid Liabilities	20.01	16.03	11.64

The Bank managed to maintain a healthy Liquid Asset Ratio well above the regulatory limit of 20% on a daily basis throughout the year and the stress results are being evaluated on a regular basis.

Mark to Market Exercise

Trading portfolios of Securities (Treasury Bills/Bonds), Equity and Foreign Currency Options are subject to mark to market exercise on a daily basis and are monitored against the set stop loss limits. Prompt management action is taken where necessary ensuring minimum loss situations to the portfolios.

Clear segregation of duties has been established between different business units ensuring prudent control and monitoring mechanisms. The Treasury Front Office reports to CEO and Treasury Back Office reports to Head of Operations. The Market Risk unit reports directly to the CRO who is a member of Bank's Assets and Liabilities Committee (ALCO). All senior level staff attached to Market Risk, Treasury Front Office and Treasury Back Office have obtained the internationally recognized ACI qualification offered by the Financial Markets Association, as required by the CBSL directives and are competent in their job profile.

The Assets and Liabilities Committee (ALCO), comprising senior management staff from the Treasury, risk management, finance and all business units of the Bank together with the market Risk management unit responsible for the supervision and management of market risk. The ALCO meets on a monthly basis and whenever circumstances demand. Its main responsibilities are:

- to decide on the required maturity profile and mix of incremental assets and liabilities;
- to monitor the structure and composition of the Bank's assets and liabilities and decide on product pricing for deposits and advances;
- to articulate the interest rate view of the Bank and decide on future business strategy;
- to review and articulate funding policy;
- to decide the transfer pricing policy of the Bank;
- to evaluate risks involved in launching new products.

ALCO is the governing body for market risk, liquidity risk and asset liability risk management and the implementation of the Bank's risk management policies, procedures and systems is delegated to the Head of Market Risk Management who reports to the Chief Risk Officer. Market and liquidity risks are addressed at ALCO on a monthly basis and at Board IRMC level on quarterly basis.

The market risk management in the Bank is evolving very fast and there is greater emphasis on strengthening systems and people with adequate training and system support.

Liquidity Risk

Liquidity risk arises due to unmatched maturities of assets and liabilities, that hinders honouring commitments as and when they fall due or will have to do so at an excessive cost. Thus the overall funding strategy takes into consideration both timing and size of business and investment together with the various sources of funding.

Effective liquidity risk management is essential to maintain the confidence of depositors and counterparties as well as to ensure that the Bank's core businesses continue to generate revenue, even under adverse conditions.

Liquidity Risk Management at NDB

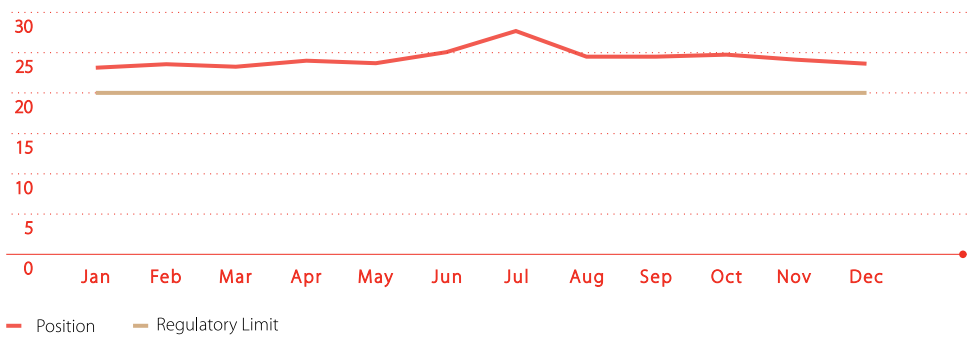
The objective of our liquidity framework is to ensure that all anticipated funding commitments can be met when due and allow us to withstand liquidity stresses whilst maintaining our business profile. It is designed to be adaptable to changing business models, market and regulations.

The Bank maintains a well-articulated liquidity risk management policy, which drives the level of liquidity risk exposures and determine the business size and maturities which ensures that it has at all times sufficient liquidity to meet its financial obligations at a fair market price.

Our principle mechanism for implementation of the liquidity policy is to maintain the Bank's liquid assets to liabilities ratio above the regulatory defined ratio of 20%. Our internally set prudential liquidity limits/ratios would give us early warnings of any areas of concern.

Bank's Liquidity Ratio Trend 2012

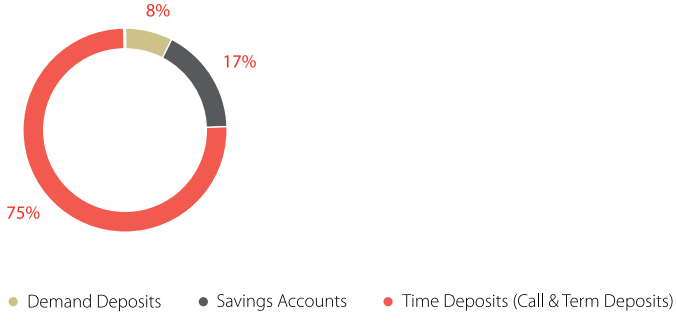
STATUTORY LIQUID ASSET RATIO MAINTENANCE - 2012



Through the Deposit Concentration Policy requirements we ensure that the Bank is not relying on a limited number of depositors or funding sources. The top 20 depositors account for only 17% of the total deposit portfolio whilst top 10 depositors account 11% as at end December 2012 which reflects the granularity of our deposit base.

Product-wise Deposit Concentration as at 31 December 2012.

TOTAL DEPOSIT CONCENTRATION



The liquidity positions of the Bank strengthened in 2012 with the inflows of customer deposits and maintained good access to wholesale markets. Our Advances to Deposit Ratios (ADR) improved considerably compared to the previous year with the aggressive deposit mobilization campaigns. During 2012, customer deposits grew by 31%. Our stable funding ratio which reflects the measure of advances to core funding recorded a ratio of 85% as at 31 December 2012 reflecting the strong liquidity profile of the Balance Sheet. The Bank will continue to focus liability generation, which will be necessary precondition for significant asset growth.

A satisfactory trade-off between liquidity and profitability is maintained by categorizing liquidity shortfalls in the Balance Sheet into suitable time buckets, placing exposure limits on each time bucket to monitor the liquidity mismatch gaps. These limits correspond to the liquidity available to NDB through various fund providers, at an agreed level of confidence.

We have carefully assessed and revised our Balance Sheet maturity mismatch limits in order to optimize market opportunities which are being effectively managed by our Asset Liability Management Desk (ALM Desk) which was set up in 2012 within the Treasury function. Separate gap limits are set for the local currency and foreign currency Balance Sheets based on the size and the nature of the Bank's Balance Sheet.

The Bank is equipped with a comprehensive Liquidity Contingency Funding Plan (LCFP) linked to the Business Continuity Plan, which is in line with the regulatory guidelines. The LCFP clearly defines the responsibilities of the Liquidity Management Team and ensures the business continuity through close monitoring of the Bank's liquidity position against the predefined liquidity risk trigger points. Trigger points have been defined taking into consideration the Bank specific and systemic triggers which would cause a liquidity crisis. Action Plans are set out under each level of liquidity crisis (Mild, Moderate, Severe) with responsibilities assigned to a Liquidity Management Team nominated from all areas of business to ensure that all stakeholders of the Bank are safeguarded.

Market & Liquidity Risk Reporting

- Daily market risk report on foreign exchange to Treasury, Finance and GRM
- Daily limit exception report to Treasury and GRM
- Market liquidity and Bank's open exposure report to ALCO and Treasury
- Monthly market risk reports on foreign exchange, liquidity, deposit concentration, country exposure reports to ALCO
- Monthly ALM reports to ALCO
- Quarterly market, ALM and liquidity reports to CMRPC and IRMC
- Quarterly risk assessment report to the Board

Operational Risk

Operational risk is the risk of loss resulting from inadequate or failed internal processes, people, systems and external events. This definition includes legal risk but excludes reputational risk and strategic risk. Therefore, in line with the Basel II risk management framework and best practices, operational risk in the Bank is composed of the following risk types: operations risk, legal risk, regulatory compliance risk, financial crime risk, people risk, property, technology, vendor, financial, and environmental risk.

Operational Risk Management at NDB

Operational risk is recognized as a distinct risk category which the Bank strives to manage within acceptable levels through sound operational risk management practices. The Bank's approach to managing operational risk is to adopt practices that are most appropriate and relevant considering the organizational maturity and business environment.

Operational risk exposure is managed through comprehensive set of internal controls and management processors that cover risk assessment (Identification, description and estimation), risk evaluation, reporting, mitigation, residual risk reporting and monitoring and control associated with our business operations as an ongoing activity. Further, the Bank recognizes the significance of operational risk, which is inherent in all areas of our business.

The Bank's risk framework defines the minimum requirements for operational risk management and is supported by specific policies and procedures. Business units implement the Bank's risk framework, policies and procedures but may customize these to better suit their unique environments.

Business unit/line management as the first line of defence is ultimately responsible for managing risks that arise within the scope of their respective areas. Both centralized and decentralized operational risk management functions are independent from business line management and work-in partnership as the second line of defence. Their role is to monitor, manage and report on risks to ensure operational risk exposure remains within the policy parameters as mandated by the Senior Management and the Board of Directors. These independent functions are also responsible for developing and implementing the operational risk management framework and for promoting sound risk management practices across the Bank. Internal Audit is the Bank's third line of defence and performs an independent review of the operational risk management framework, policies and practices to ensure that operational risk practices are adequate, comprehensive, consistent and efficiently implemented.

The objective in managing operational risk is to improve the efficiency and effectiveness of the Bank's resources, minimize losses whilst utilizing opportunities.

The Bank continues to manage operational risk on the Basic Indicator Approach (BIA) in accordance with the Regulator's guidelines and has commenced parallel computation of capital in terms of The Standardized Approach with effect from December 2011.

Risk Management

Operational Risk Management Function

The Bank's operational risk management function is independent of the businesses, branches, departments/business units, control and support units and reports to the Chief Risk Officer.

The Bank has a comprehensive insurance policy as a measure to mitigate risks. This falls within the framework of risk mitigation and control which in turn is an integral component of the risk management framework of the Bank. This policy will be reviewed and further enhanced in the near future.

The core responsibility of the Bank's Operational Risk Management function is the development and implementation of operational risk management across the Group.

This entails:

- reviewing operational risk management policies, standards, processes and procedures;
- developing and driving implementation and maintenance of the operational risk management framework;
- developing and distributing tools, techniques, methodologies, common risk language, risk frameworks, analysis, reports, communication and training;
- co-ordinating, aggregating and facilitating operational risk management activities across the Bank;
- monitoring the operational risk profile, including accumulation of risk, trends, and risks from internal and external market changes;
- escalating high-priority issues to Senior Management and the Board of Directors through the Integrated Risk Management Committee;
- collating, challenging and reporting on aggregate risk profile, control effectiveness and actions to the Integrated Risk Management Committee;
- analyzing business units, branches, departments and support units' operational risk to derive emerging risk themes for the Bank;
- liaising with external parties, e.g. regulators, analysts, External Auditors, etc. on the Bank's operational risk management practices.

Managing Operational Risk

Operational risk management forms part of the day-to-day responsibilities of management at all levels. Qualitative and quantitative methodologies and tools are applied to identify and assess operational risks and to provide management with information for determining appropriate mitigating measures.

These tools include:

- Operational Loss Reporting Template
  This is for reporting urgent and significant operational loss events those have to be escalated to relevant senior management stakeholders without having to wait for the monthly risk reporting cycle. Examples of significant operational loss events are: cash shortages, fraud and losses, etc…
- Internal Loss Database
  Collection of operational risk/loss events categorized according to the Basel II business lines and operational risk event types;
- Risk and Control Self-Assessment (RCSA)
  A process to analyze business activities and identify operational risks that could affect the achievement of business objectives.

  An effective risk and control self-assessment process is a key component of developing a risk profile and understanding the residual risk;
- Key Operational Risk Controls (KORC)
  The Key Operational Risk Controls (KORCs) framework provide an overview of the key risks associated with process scopes and the expected key controls to mitigate these risks. As such they are fundamental to develop operational risk management in the Bank as well as to realize qualification for the Advanced Measurement Approaches for measuring operational risk;
- Key Risk Indicators (KRI)
  KRIs are used to manage operational risk on an ongoing basis. Key risk indicators contribute to the development of a risk profile. The main purpose is to assist management by providing an early warning indicator of potential risk exposures and/or a potential breakdown of controls.

The Bank has implemented a software-based solution to assist in the management of operational risk. The tools for operational risk identification, assessment and monitoring will be made operational through the said software during the coming months.

Risk Management

Operational Losses for 2012

LOSS EVENT TYPES

External Fraud Execution, Delivery and Process Management

The majority of operational losses were caused by external frauds. Credit card frauds and submission of counterfeit foreign currency drafts through our customers into the banking system contributed to the majority of the external frauds.

Outsourcing Arrangements

The Bank has entered into outsourcing agreements due to the specialization required for certain functions of branch operations, marketing, human resources, administration, card operations, IT, pawning, central processing unit and auto finance. It has been cost effective to outsource such areas of expertise. The Regulator has issued guidelines on the activities which are allowed to be outsourced and within these parameters an in depth screening process as enumerated below is carried out prior to selecting the service provider.

The Bank looks at its structure and ownership, its capacity, capability and authorization to carry out the outsourced activity. In addition the Company's personnel are reviewed to ensure they have adequate training, skills and experience to understand the nature of the service and manage the risks. The risk management systems of the service provider are also looked at.

The Bank is concerned and committed to ensuring that the outsourced parties continue to uphold and extend the high standard of customer care and service excellence that has become synonymous with NDB, hence due diligence tests are routinely carried out to assess the performance of these outsourced parties.

A comprehensive cost benefit analysis is performed and the benefit is evaluated against the risk of outsourcing. The tests would assess the quality of service, any breach of contract, identify if price caps and performance guarantees are in place. They would also ensure that the risks/interactions/ disruptions related to the outsourcing activity are being identified.

Business Continuity Management

As an integral component of the Bank's risk management framework, the Bank has deployed a Business Continuity Plan enabling it to possess adequate preparedness to continue its business in the event of a disaster. This plan is not only designed to comply with Central Bank of Sri Lanka's requirements but also with best practices promoted by Disaster Recovery Institute International of USA. The Bank's business continuity strategy is structured to ensure strong central monitoring and reporting and decentralized execution, and is supported by a robust governance process.

The plan developed contains four different areas which include, Recovery Plans, Emergency Response Plans, Support Plans and Management System Plans. The Business Continuity Plans so developed are backed by redundant infrastructure to support key services, core systems and critical business processes.

The plan is approved by the Integrated Risk Management Committee of the Bank and its implementation is being coordinated via the operational risk unit of the Bank. The Bank has appointed a disaster management team representing critical business units and officers who manage resources required for disaster recovery. The disaster management team consists of three layers, where the Incident Commander occupies the top most layer, the team leaders the second layer and the team members who will man the continuity of operations and recovery form layer three.

The Bank gives primary importance to ensuring safety of its customers, staff, contractors and other visitors. In this regard the Bank not only has an able emergency response team but also a team dedicated to support people and families affected.

Management plans within the BCP spells out the tools and processes required to maintain the continued effectiveness of the plan. Business Continuity Plan is being periodically reviewed to accommodate organizational changes and is being subjected to regular drills and testing. A full BCP activation drill covering all the critical operations was carried out successfully during the review period from our disaster recovery site. This simulation exercise was carried out with the participation of staff from each critical operational area while other department staff continued their operations from their respective work places.

In addition to the above, the Bank has conducted 64 functional drills, two call tree drills and two evacuation drills during the review period. The Business Continuity Plan processes were audited and necessary corrective actions were taken.

Risk Management

Compliance Function

NDB has established a permanent and effective compliance function in line with the Directions issued by the Central Bank of Sri Lanka and the recommendations made by the Basel Committee on Bank Supervision on `Compliance and compliance function in Banks'. A dedicated compliance department headed by a senior officer, independently monitors adherence to all applicable laws, regulations and statutory requirements and reports to the Integrated Risk Management Committee and the Corporate Governance and Legal Affairs Committees. Quarterly reports are submitted to the Integrated Risk Management Committee confirming compliance with the Bank's Compliance Policy and Code of Conduct in addition to compliance with external laws and regulations. These reports are also tabled quarterly at Board meetings for the information of the Directors.

NDB has effective processes in place to ensure compliance with applicable laws and regulations pertaining to the banking industry (including the Anti-Money Laundering Act No. 5 of 2006 and related acts, Companies Act No. 07 of 2007, and the Listing Rules of the Colombo Stock Exchange). The Compliance Department ensures that compliance reports are submitted to the Central Bank of Sri Lanka confirming the Bank's compliance with Central Bank Regulations and Guidelines.

Group Risk Management

Group risk management process has evolved with the development of appropriate risk reporting and parameters including reputational risk, legal risk to capture NDB Group company risk profiles and probable impact on Bank's reputation/financial performance.

The Key Risk Indicators/Key Performance Indicators of the Group companies are monitored and reported to Board subcommittee on integrated risk management on a monthly/quarterly basis for their review. Further, the Bank's Group Risk Management Team is a party to the approval process of credits, pre-clearance of product papers/underwriting standards of specific companies.

Outlook

Given the opportunities presented in the post-war era, the Bank has been very aggressive in pursuing business. Emphasis has been given to SME, retail and project finance in support of the development objectives of the country. Risk has facilitated this process by reviewing existing policies and procedures within acceptable risk parameters and strengthening the post sanction monitoring process.

The credit process will be enhanced to address prevailing challenges, while credit models to be implemented will be subjected to periodic validation for the purpose of obtaining necessary assurances. Portfolio stress tests will be adopted as appropriate, to consider implications of scenarios that may seem relatively unlikely but could pose serious risks to the institution if they crystallize.

The Bank will continue to focus on the growth sectors of the economy through strategic portfolio planning, supported by sound risk identification, measurement, control, monitoring and reporting.

Basel II Compliance and Capital Management

Currently, the Bank is applying the Standardized Approach for Credit Risk, Standardised Measurement Approach for Market Risk and Basic Indicator Approach for Operational Risk in computing the minimum capital requirements as per CBSL Regulations. As at 31 December 2012 the Bank's Pillar II Capital Adquacy Ratio (CAR) stands at 12.4%.

Credit risk is the largest contributor in the over all risk exposure of the Bank and bears the highest risk related capital charge. The Bank at present possesses a quality portfolio and moving into advanced approaches of capital computation for credit risk would facilitate minimizing the capital requirements. This requires the sophisticated systems and methodologies in quantification and monitoring of risk. Understanding this, Bank has initiated steps to invest in a credit and market risk management solution. The system would facilitate the obligor and facility ratings, risk based pricing, market VaR calculation would also automate the capital computation process. This would allow the Bank to optimize collateral allocation and thereby take maximum use of its capital. In line with the Central Bank directions on Integrated Risk Management Framework which recognizes the responsibility of Bank Management in developing an Internal Capital Adequacy Assessment Process and setting capital targets that are commensurate with the Bank's risk profile and the control environment, the Bank has commenced the process of developing an Internal Capital Adequacy Assessment Process (ICAAP) assessing the Bank's overall adequacy of capital.

The Bank continues to maintain capital over and above the minimum levels required. Stress tests are carried out periodically for various risks faced by the Bank to assess the impact of these on capital allocation. Accordingly the Bank's Stressed CAR on Pillar I and Pillar II risks stand at 11.2% as at 31 December 2012 and the results of same are presented to the Board Subcommittee on integrated risk. The Bank continue to exceed the Central Bank requirement for minimum capital even under the stressed conditions considered, thereby protecting shareholder interest and enhancing the financial strength and stability of the Bank.

In Sri Lanka, the local regulator is yet to issue guidelines on implementation of Basel III. Basel III stresses that it is critical that Bank's risk exposures are backed by a high quality capital base. A key element of the new definition of capital is the greater focus on common equity, the highest quality component of a Bank's capital. The guideline stipulates that banks need to maintain a common equity capital ratio of 4.5%, a capital conservation buffer of 2.5%, Tier I capital ratio of 6% and a total capital ratio of 8%, by 1 January 2019. The minimum ratio for total capital plus conservation buffer as at 1 January 2019 has to be 10.5%. Though the international guideline provide for a transition period, the Bank as at 31 December 2012, exceeded these requirements demonstrating that its quality and quantity of capital is sufficient to ensure resilience in times of stress.

Basel III also stresses that a strong liquidity base is of equal importance. Recognizing this the Bank monitors its liquidity risk closely with liquidity risk parameters and adequate stress testing. The Bank also has a detailed Liquidity Contingency Funding Plan approved by the Board Integrated Risk Management Committee.

The Bank's good risk management practices would facilitate the move towards Basel III with confidence.

Corporate Governance

The Corporate Governance Report

Dear Stakeholder,

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

In order to implement good Corporate Governance practices there has to be commitment on the part of the Board to foster the development of best practices in Corporate Governance. Board composition is a critical factor which impacts the Corporate Governance process.

The Bank has over the years recommended members to the Board based on the contribution they would make towards the achievement of the Bank's current and future business activities.

Further, collectively the Directors have the appropriate skills, experience and a clear understanding of their role in Corporate Governance enabling them to make an effective contribution to the Bank.

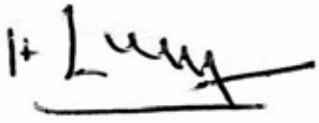
Our vision to be a world class Sri Lankan, captures our commitment to achieve excellence in all spheres and motivates our staff to strive for distinction in our service to customers and stakeholders. At NDB, staff are encouraged and motivated to adhere to ethical practices.

We at NDB are governed by our core values of integrity, care, passion, teamwork and service. The employees are required to live the values and 20% weightage is assigned to the said values in the overall performance assessment.

The performance of employees is assessed based on how well they have applied the core values in their day-to-day tasks. We serve our customers with professionalism, innovation and creativity. Above all, we endeavour never to lose the human touch. At NDB, we have used Corporate Governance as a competitive advantage to achieve future sustainability.

In our commitment to ensure that adherence to good Corporate Governance practices are a cornerstone of our business activities, we have reviewed and amended our internal Code of Corporate Governance to be in line with the international best practices.

As good Corporate Governance is evolutionary in nature, we continue to improve and adapt our Corporate Governance practices and frameworks so that we can meet demands and grasp new opportunities.



Hemaka Amarasuriya
Chairman

Kimarli Fernando
Chairperson
Corporate Governance and
Legal Affairs Committee

13 February 2013

Corporate Governance

Our Highlights

- Reviewed the internal Code of Corporate Governance in line with best practices
- Focused on growth whilst strengthening governance practices
- NDB received the following key awards:
  - NDB Annual Report 2011 was awarded with 5 prestigious international awards and rankings at the League of American Communication Professionals (LACP) Vision Awards 2011
  - Best Corporate Citizen in the category of enterprises with a turnover below Rs 15 bn at the Best Corporate Citizens (BCC) Awards 2012 hosted by The Ceylon Chamber of Commerce
  - NDB was rated as the 'Best Commercial Bank 2012' in Sri Lanka by World Finance magazine
  - NDB was adjudged winner of the Silver Award at the HRM Awards 2012 organized by the Association of Human Resource Professionals

Our Priorities for 2013

- Focused, aggressive growth plan in keeping with the opportunities and the growth momentum of the country
- Focused attention on SME and project financing to support the growth in the real economy
- Continue to review the internal Code of Corporate Governance in keeping with the changing environment
- Leverage on synergies of the Group to deliver a one stop shop to the customer

Corporate Governance Structure

National Development Bank PLC is a public quoted company incorporated under the Companies Act No. 07 of 2007. NDB being a Licensed Commercial Bank is also governed by the Banking Act No. 30 of 1988 (as amended) and the Directions issued by the Central Bank of Sri Lanka.

The Board of NDB has the overall responsibility and accountability for the management of the affairs of the Bank, maintenance of prudent risk management mechanisms, safeguarding stakeholder rights and above all ensuring the safety and soundness of the Bank. To this end the Board has appointed a management team ably led by the Chief Executive Officer (CEO).

The Board has delegated some of its functions to six Board sub committees chaired by Non-Executive Directors. However, a formal schedule of matters has been reserved specifically for the decision of the Board.

The Board of NDB provides effective leadership within a framework of prudent and effective controls for the operations of the Bank. The Board leads by example in establishing professional standards and corporate values for the Bank and ensures that its obligations to its shareholders and other stakeholders are understood and met.

Whilst the CEO and senior management are responsible for recommending the strategic direction of the Bank, the Board constructively challenges and helps the development of proposals on strategy. The Board decides the strategic direction, vision and mission of the Bank and ensures that they are kept under review.

The Board regularly reviews the progress of the Bank against financial objectives and business strategy.

Board's Structure and Composition

The Board comprises nine Directors as at end December 2012, eight of whom, including the Chairman, are Non-Executive Directors. Of the nine Directors four are independent. The CEO of NDB, functions as the only ex-officio Director.

Directors

The authority of the Directors is exercised at Board meetings. The Board of Directors act effectively as a team, having collectively the necessary skills, experience and knowledge to ensure sound management of the Bank. Non-Executive Directors who are not employees of NDB, contribute a balance of financial and banking experience together with business experience and skills. They are from both the private and public sectors, who constructively challenge proposals on strategy and monitor performance of the Bank against set goals and targets. The Directors have unlimited access to management and information.

The filling of vacancies of Directors by the Board is made on the recommendation of the Nominations Committee of the Board, based on guidelines approved by the Board. Additionally, in recommending the appointment of Non-Executive Directors, the Nominations Committee ensures that these Directors are persons of repute with credible track records who demonstrate ethical leadership keeping in mind NDB's values and culture.

The Board has delegated its authority in operational areas to the senior management, within clearly defined limits. The management works through a number of internal committees as shown in the diagram on page 179.

Board Meetings

The Board has met fifteen times during the financial year under review. The table given on page 199 shows the attendance of each Director at meetings of the Board including meetings of Board sub committees.

Chairman and CEO

The roles of Chairman and CEO are held by two individuals to ensure separation of responsibilities. This requirement is clearly embodied in the internal Code of Corporate Governance and the Articles of the Bank.

Key Functions of the Chairman

The Chairman -

- provides leadership to the Board;
- ensures that the Board works effectively and discharges its responsibilities; and
- ensures that all key and appropriate issues are discussed by the Board in a timely manner.

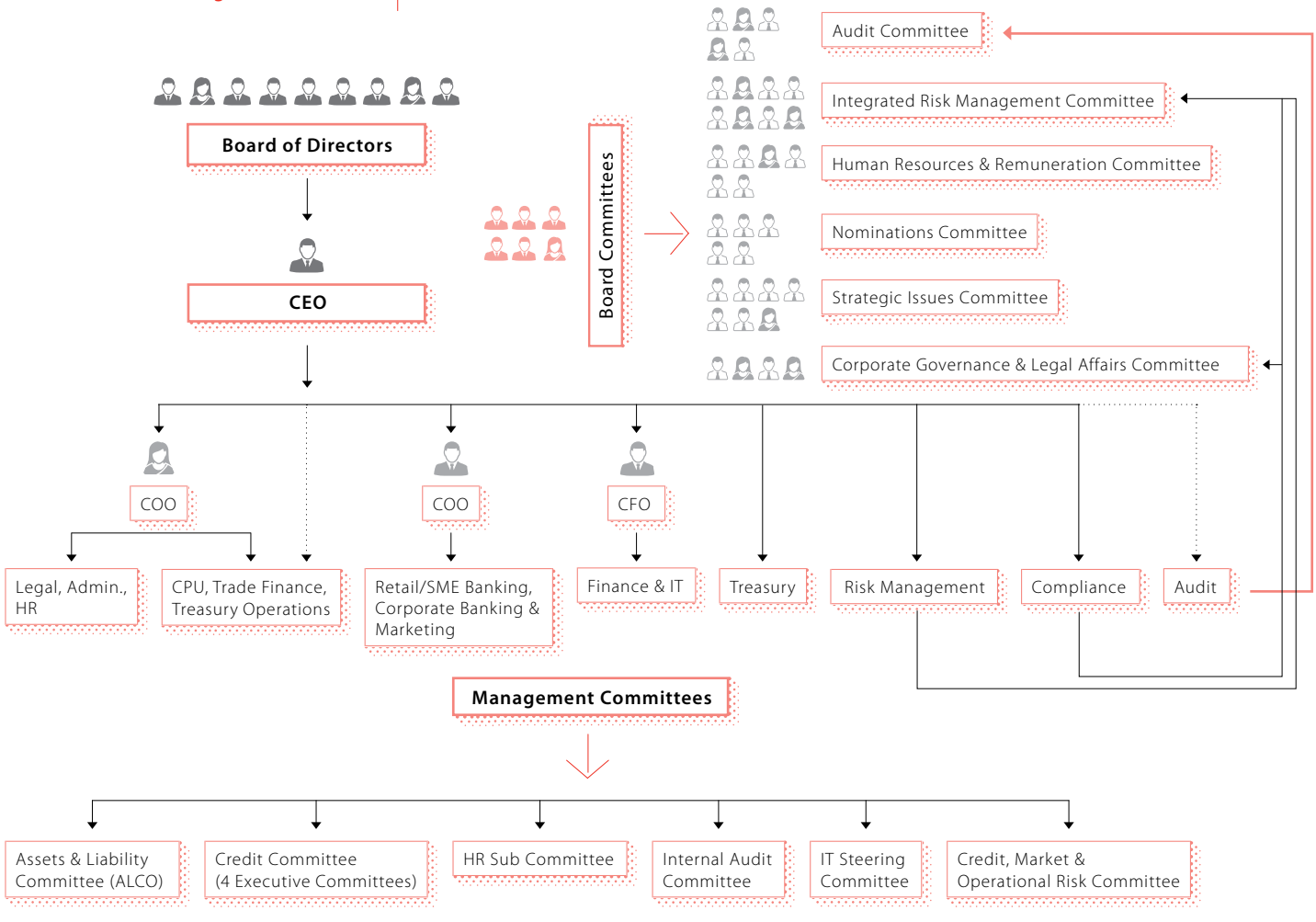
The Chairman is not involved in the day-to-day operations of the Bank, but functions in such a way so as to ensure that the Board is in control of the overall affairs of the Bank and fully alert to its obligations towards its stakeholders.

Key Functions of the CEO and Key Management Personnel (KMP)

The CEO and KMP are responsible for -

- developing and recommending the strategic direction of the Bank for consideration and approval by the Board;
- formulating appropriate short, medium and long-term corporate plans and budgets;
- monitoring the performance of the Bank against plans and budgets;
- identifying, assessing, managing and monitoring of risks;
- developing, operating and monitoring the system of internal control and providing assurance to the Board;
- providing the Board with accurate, timely, clear and pertinent information, in particular about the Bank's performance;
- preparing complete and accurate Financial Statements and disclosures in accordance with financial reporting standards, which present a fair view of the Bank's performance and financial position.

Organization Chart



Code of Ethics

In terms of the Bank's Compliance Policy/Code of Conduct, all employees are required to adhere to high standards of ethical and professional conduct. This code has been communicated to all staff, who are required to observe high standards of personal integrity when conducting both the Bank's business and their own private financial affairs.

Regulations and Supervision

The Monetary Board of the Central Bank of Sri Lanka issued Banking Act Direction No. 11 of 2007 (as amended) on Corporate Governance for Licensed Commercial Banks. Compliance with this Direction commenced from 1 January 2008 onwards and all Licensed Commercial Banks were required to be fully compliant with the provisions of the Direction by or before 1 January 2009, except where extended compliance dates were specifically provided. NDB complies with the said Directions on Corporate Governance and the table containing the degree of compliance with explanatory comments thereon is given on pages 181 to 190.

NDB being committed to the high standards of Corporate Governance is also guided by the Code of Best Practice on Corporate Governance issued jointly by the Securities and Exchange Commission and The Institute of Chartered Accountants of Sri Lanka. Further, NDB has been exempted by the Colombo Stock Exchange, from the requirement to comply with Section 7.10 (Corporate Governance) of the Continuous Listing Requirements under the Colombo Stock Exchange Listing Rules.

Banking Act Direction No. 11 of 2007 on Corporate Governance

NDB's adherence to the Corporate Governance Directions, contained in the Banking Act Direction No. 11 of 2007 (as amended) issued by the Monetary Board of the Central Bank of Sri Lanka with explanatory comments thereon is set out as follows:

Rule No.	Principle	Compliance Status	Comments
3(1) Responsibilities of the Board 3(1)(i)	The Board shall strengthen the safety and soundness of the Bank by ensuring the implementation of the following:		
	(a) Approve and oversee the Bank's strategic objectives and corporate values and ensure that these are communicated throughout the Bank	Compliant	Board has approved the strategic objectives and corporate values and communicated same, as required by the Direction.
	(b) Approve the overall business strategy of the Bank	Compliant	Overall business strategy and risk management policy and procedures have been approved as required by the Direction.
	(c) Identification of the principal risks and implementation of appropriate systems	Compliant	The Board has identified key risks of the Bank and approved the relevant policies for management of such risks. The function of management of risks has been delegated to the Integrated Risk Management Committee.
	(d) Approve the implementation of a policy of communication with all stakeholders	Compliant	The Communication Policy has been approved by the Board and communicated to staff.
	(e) Review the adequacy and the integrity of the Bank's internal control systems and management information systems	Compliant	Adequacy and the integrity of the Bank's internal control systems and management information systems are reviewed by the Board Audit Committee.

Rule No.	Principle	Compliance Status	Comments
	(f) Identify and designate key Management Personnel, as defined in the International Accounting Standards	Compliant	Process is reviewed periodically.
	(g) Define the areas of authority and key responsibilities for the Board Directors themselves and for the Key Management Personnel	Compliant	The responsibilities of the Directors and KMP have been set out in the internal Code of Corporate Governance.
	(h) Ensure that there is appropriate oversight of the affairs of the Bank by Key Management Personnel	Compliant	The Board interacts with KMP from time to time at Board meetings and through reports tabled at Board meetings. There is oversight by the six Board Committees.
	(i) Periodically assess the effectiveness of the Board Directors' own governance practices	Compliant	Self-assessments of Directors have been obtained for the year 2012.
	(j) Ensure that the Bank has an appropriate succession plan for Key Management Personnel	Compliant	The Bank has in place a succession planning process, which is periodically reviewed.
	(k) Meet regularly, on a needs basis, with the Key Management Personnel to review policies, establish communication lines and monitor progress towards corporate objectives	Compliant	Directors meet KMP at monthly Board meetings and at Board Committee meetings on a continuous basis and the requirement of the Direction is complied with.
	(l) Understand the regulatory environment and ensure that the Bank maintains an effective relationship with regulators	Compliant	CEOs of Banks meet with the Central Bank officials monthly at the Managers Meeting and at other meetings between CBSL officials and with the SLBA. Further, Directors of all Banks are invited for a meeting with CBSL annually. KMP also maintain a dialogue with regulators on a continuous basis.

Rule No.	Principle	Compliance Status	Comments
	(m) Exercise due diligence in the hiring and oversight of External Auditors	Compliant	Audit Committee Charter includes the functions of hiring and overseeing of External Auditors. External Auditors attend all Audit Committee meetings by invitation and there is continuous dialogue with External Auditors.
3(1)(ii)	The roles of the Chairman and CEO	Compliant	There is a clear division of responsibilities between the Chairman and the CEO by defining the roles of the Chairman and the CEO.
3(1)(iii)	Board meetings	Compliant	There have been fifteen Board Meetings during 2012. The attendance of Directors for Board and committee meetings is set out in the table on page 199.
3(1)(iv)	Board to ensure that arrangements are in place for Directors to include matters and proposals in the agenda	Compliant	This is a requirement of the internal Code of Corporate Governance. A Director is free to bring up any matter at Board meetings.
3(1)(v)	Notice of Board meetings	Compliant	Notice and agenda are issued to Directors 7 days in advance of the Board meeting.
3(1)(vi)	Non-attendance by Directors	Compliant	Company Secretary monitors the attendance register to ensure compliance.
3(1)(vii)	Appointment of a Company Secretary	Compliant	A person with the specified qualifications has been appointed. The Company Secretary is responsible to the Board for ensuring that Board procedures are followed and that applicable laws, rules and regulations are complied with.
3(1)(viii)	Access to the advice and services of the Company Secretary	Compliant	All Directors have access to the advice and services of the Company Secretary.
3(1)(ix)	Board meeting minutes	Compliant	Detailed Board minutes, as appropriate, are made available to Directors.

Corporate Governance

Rule No.	Principle	Compliance Status	Comments
3(1)(x)	Minutes to be in detail	Compliant	The minutes contain adequate details appropriate to the matters dealt with. The minutes are also read together with the corresponding Board papers, which supplement the information in the minutes.
3(1)(xi)	Independent professional advice at Bank's expense	Compliant	The Directors are aware of this service and have obtained professional advice during the year.
3(1)(xii)	Avoid conflicts of interest	Compliant	The Directors have been informed of the requirements. Furthermore, this requirement is also laid down in the Bank's internal Code of Corporate Governance. Annually, a declaration is obtained from the Directors confirming whether they have avoided conflicts of interest.
3(1)(xiii)	Formal schedule of matters	Compliant	A formal schedule of matters has been specifically reserved for the decision of the Board.
3(1)(xiv)	Insolvency	Compliant The situation has not arisen	A Solvency Statement is prepared quarterly and tabled at the Integrated Risk Management Committee and the Board.
3(1)(xv)	Capital Adequacy Ratio	Compliant	The Bank is in compliance with Capital Adequacy requirements stipulated by the Central Bank.
3(1)(xvi)	Corporate Governance Report	Compliant	The requirement is complied by this Report.
3(1)(xvii)	Self-assessment	Compliant	An evaluation is done annually by Directors based on a format which would constitute the scheme.

Rule No.	Principle	Compliance Status	Comments
3(2) Composition of the Board			
3(2)(i)	Number of Directors	Compliant	The Board comprised nine Directors as at 2012 year end.
3(2)(ii)	Period of service of a Director	Compliant	This is monitored by the Company Secretary to ensure compliance.
3(2)(iii)	Appointment of an employee as a Director	Compliant	The CEO is the only employee on the Board. The number of Executive Directors does not exceed one-third of the Directors on the Board.
3(2)(iv)	Independent Non-Executive Directors	Compliant	Four of the eight Non-Executive Directors as at year end 2012 were independent. The number of independent Non-Executive Directors exceeds one-third of the total number of Directors on the Board.
3(2)(v)	Appointment of an alternate Director	Compliant	The Company Secretary monitors this to ensure compliance.
3(2)(vi)	Non-Executive Directors with credible track records, necessary skills and experience	Compliant	The Directors are eminent persons with knowledge, expertise and experience in different business sectors including leadership in public listed companies.
3(2)(vii)	Number of Non-Executive Directors required to form a quorum	Compliant	Attendance of Directors is monitored by the Company Secretary who ensures compliance with this Direction.
3(2)(viii)	Details of Directors	Compliant	The Directors' Profiles and composition of the Board are published in the Annual Report.
3(2)(ix)	Appointment of new Directors	Compliant	The Board has approved guidelines for the Nominations Committee to recommend new Directors to the Board.
3(2)(x)	Appointment to fill a casual vacancy	Compliant	Appointment to fill a casual vacancy is made by the Board. A person so appointed could be elected as a Director at the next Annual General Meeting. Central Bank approval is obtained in terms of the Banking Act for the appointment of Directors.

Corporate Governance

Rule No.	Principle	Compliance Status	Comments
3(2)(xi)	Resignation or removal of a Director	Compliant	The reason for resignation is given.
3(2)(xii)	Appointment of a Director/ employee to another bank	Compliant	None of the Directors or employees of the Bank have been appointed as Directors of other Banks.
3(3) Criteria to Assess the Fitness and Propriety of Directors			
3(3)(i)	Directors over 70 years of age	Compliant	This is monitored by the Company Secretary to ensure compliance.
3(3)(ii)	Holding of office in more than 20 companies	Compliant	This is monitored by the Company Secretary to ensure compliance.
3(4) Management Function Delegated by the Board			
3(4)(i)	Delegation arrangements	Compliant	Delegation papers are prepared in detail and presented to the Board. Terms of Reference of Board Committees are approved by the Board.
3(4)(ii)	Extent of delegation	Compliant	By delegating the Board does not lose the authority to deal with matters that have been delegated when necessary.
3(4)(iii)	Review of delegation process	Compliant	Delegation of authority is reviewed from time to time.
3(5) The Chairman and Chief Executive Officer			
3(5)(i)	Separation of roles of the Chairman and CEO	Compliant	There is a clear division of responsibilities between the Chairman and the CEO in terms of the internal Code of Corporate Governance.
3(5)(ii)	Chairman to be a Non-Executive Director and preferably an Independent Director	Compliant	The Chairman is a Non-Executive, independent Director and therefore, the appointment of an independent Director as the Senior Director does not arise.
3(5)(iii)	Relationship between Chairman and CEO and other Directors	Compliant	Based on the annual declarations and affidavits provided by the Directors, there is no relationship between the Chairman and CEO and among the members of the Board.

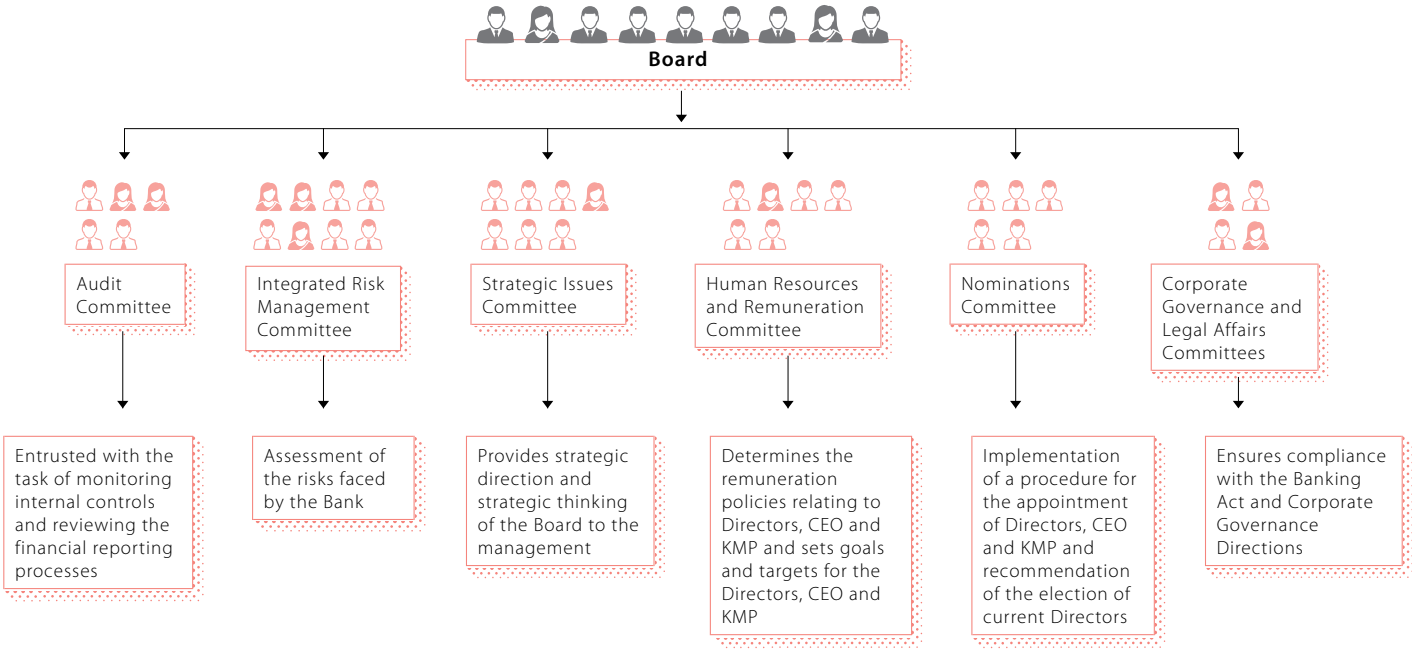
Rule No.	Principle	Compliance Status	Comments
3(5)(iv)	Role of the Chairman	Compliant	The Chairman is responsible for the running of the Board, preserves order and ensures that proceedings at meetings are conducted in a proper manner. Further, he ascertains the views of the Directors on the issues being discussed before decisions are taken.
3(5)(v)	Primary responsibilities of the Chairman	Compliant	The key functions of the Chairman are included in the internal Code of Corporate Governance.
3(5)(vi)	Briefing on issues arising at Board meetings	Compliant	The Directors are adequately briefed in the course of discussions by the Chairman, CEO and officers of the management in respect of matters that are taken up by the Board. Board papers containing information are normally circulated among the Directors in advance.
3(5)(vii)	Board to act in the best interest of the Bank	Compliant	The Chairman ensures that all members effectively participate as a team in Board decisions.
3(5)(viii)	Effective contribution of Non-Executive Directors and constructive relations between Executive and Non-Executive Directors	Compliant	The Chairman ensures that the Non-Executive Directors actively contribute to the decisions of the Board and a climate of mutual trust and respect exists between the Board and the CEO.
3(5)(ix)	Chairman not to engage in executive duties whatsoever	Compliant	In terms of the internal Code of Corporate Governance the Chairman is not involved in the day-to-day operations of the Bank.
3(5)(x)	Effective communication with shareholders	Compliant	The Chairman together with the CEO ensure effective communication with stakeholders and that members of the Board are apprised of the views of major investors and other key stakeholders.
3(5)(xi)	CEO to be the apex executive-in-charge of the daily operations and business	Compliant	In terms of the internal Code of Corporate Governance the CEO and Senior Management are responsible for providing the leadership, expertise and professional environment within the Bank for the implementation of the Board's policies and the achievement of the Bank's goals and objectives.

Corporate Governance

Rule No.	Principle	Compliance Status	Comments
3(6) Board Appointed Committees			
3(6)(i)	Four Board-Appointed committees	Compliant	The Board has appointed a Corporate Governance and Legal Affairs Committee (CGLA) and a Strategic Issues Committee in addition to the four Board committees mentioned in the Direction. Please refer pages 191 to 198 for details.
3(6)(ii)	Board Audit Committee - composition and responsibilities	Compliant	Please refer pages 191 to 193.
3(6)(iii)	Human Resources and Remuneration Committee - composition and responsibilities	Compliant	Please refer page 196. This is being reviewed on an ongoing basis.
3(6)(iv)	Nominations Committee - composition and responsibilities	Compliant	Please refer page 197.
3(6)(v)	Integrated Risk Management Committee - composition and responsibilities	Compliant	Please refer pages 193 and 194.
3(7) Related Party Transactions			
3(7)(i), (ii), (iii)	Avoid conflicts of interest in related party transactions and favourable treatment	Compliant	When entering into related party transactions, the Bank is governed by the Banking Act and Regulations issued thereunder. The Bank's internal Code of Corporate Governance has laid down provisions regarding conflicts of interest and procedure to be followed in the event of a conflict of interest. The policies and procedures relating to related party transactions have been improved in the current year and will be reviewed and strengthened on an ongoing basis.

Rule No.	Principle	Compliance Status	Comments
3(7)(iv)	Accommodation to Directors and/or their close relations	Compliant	When accommodation is granted to Directors and their close relations, the requirements of the Banking Act and Directions are complied with.
3(7)(v)	Appointment of a Director subsequent to granting of facilities	Compliant	The requirements of the Banking Act and Directions have been complied with.
3(7)(vi)	Accommodation to employees	Compliant	Accommodation to employees is based on specific schemes that have been formulated.
3(7)(vii)	Remission of accommodation/ interest due on facilities under 3(7)(v) and 3(7)(vi)	Compliant	The situation has not arisen.
3(8) Disclosures			
3(8)(i)	Publication of annual and quarterly Financial Statements	Compliant	
3(8)(ii)	Minimum disclosure requirements in the Annual Report		
	(a) Annual Audited Financial Statements to be prepared in line with applicable accounting standards and regulatory requirements	Compliant	Please refer "Statement of Directors' Responsibilities" on page 216.
	(b) Confirmation from Directors on the effectiveness of the internal control mechanism over the financial reporting system and compliance with accounting principles and regulatory requirements	Compliant	Please refer "Directors Statement on Internal Control over Financial Reporting" on pages 217 to 219.
	(c) External Auditors' certification on the internal control mechanism referred to in 3(8)(ii)(b) above	Compliant	Please refer "Independent Assurance Report" on page 220.

Rule No.	Principle	Compliance Status	Comments
	(d) Details of Directors, Directors' transactions with the Bank and total of fees/ remuneration paid by the Bank	Compliant	Please refer 'Board of Directors' on pages 90 to 94, "Directors' Interest in Contracts with National Development Bank PLC" on pages 214 and 215 and page 212 for Directors' Remuneration.
	(e) Total net accommodation to related parties included as a percentage of the Bank's regulatory capital	Compliant	Please refer pages 314 to 317.
	(f) Aggregate values of remuneration paid to and transactions with key management personnel	Compliant	Please refer page 315.
	(g) External Auditors' certification of the compliance with the Corporate Governance Directions	Compliant	All the findings of the "Factual Findings Report" of auditors issued under "Sri Lanka Related Services Practice statement 4750" have been incorporated in the Annual Corporate Governance Report.
	(h) Report of compliance with prudential requirements, regulations, laws and internal controls and rectification measures	Compliant	Please refer page 216.
	(i) Lapses in the Bank's risk management or non-compliance with these directions, pointed out by the Director of Bank Supervision and directed by the Monetary Board to be disclosed to the public	Compliant	The situation has not arisen.



Board Committees

The Board of Directors has appointed six committees to oversee specific areas as given in the diagram above. The Chairman of each Board sub committee is a Non-Executive Director and reports to the Board on the activities of the committees.

Each Board sub committee has been given 'Terms of Reference' by the Board, terms of which are reviewed as per the terms of reference.

Appointment of the members to Board committees are decided by the Board.

Board Sub Committees

The composition and workings of these committees are elaborated in the table below:

Committee/Composition as at 31 December 2012	Scope of the Board Committee/Principal Activities carried out during the year
Audit Committee: Mr T L F W Jayasekara* Mr D S P Wikramanayake Mr S Rajapakse Ms G D C Ekanayake Ms K Fernando	The Audit Committee is entrusted with the task of monitoring the internal controls, systems and processes of the Bank. It also serves as an effective forum for the Board of Directors in discharging their responsibilities and is empowered to review and monitor the financial reporting process of the Bank and to provide additional assurance on the reliability of Financial Statements through a process of independent and objective reviews.

Committee/Composition as at 31 December 2012	Scope of the Board Committee/Principal Activities carried out during the year
	For the year ended 31 December 2012, the Audit Committee comprised of five Non-Executive Board members. Amongst its other functions, the Audit Committee Charter empowers the Audit Committee to examine any matters relating to the financial affairs of NDB and to review the adequacy of internal control procedures, coverage of internal and external audit plans, disclosure of accounting policies etc. NDB has an effective and independent Internal Audit function, covering operational, financial, credit and Information Security Audits. The Head of Internal Audit reports to the Chairman of the Audit Committee, who carries out the performance evaluation of the former. The Committee ensures that the audit function is independent of the activities it audits and that impartiality is maintained with due professional care being exercised when carrying out its duties. The internal audit plan and results of the internal audit process is reviewed by the Committee and where necessary, it is ensured that appropriate actions are taken on the recommendations of the Internal Audit Department. The Committee also provides a forum for the impartial review of the regular internal audit reports and investigation reports and takes into consideration the major findings and recommendations stated therein, relating to significant business risks and control issues suggesting appropriate remedial measures where necessary. The Committee also reviews and monitors the External Auditor's independence and objectivity and the effectiveness of the audit processes in accordance with the applicable standards and best practices. Before the audit commences, the nature and scope of the external audit is discussed including an assessment of the Bank's compliance with the relevant directions in relation to Corporate Governance, the management's internal controls over financial reporting and the preparation of Financial Statements for external purposes in accordance with relevant accounting principles and reporting obligations. The Committee also reviews the external Auditor's management letter and management's response thereto.

Committee/Composition as at 31 December 2012	Scope of the Board Committee/Principal Activities carried out during the year
	The Committee reviews the Financial Statements of the Bank, its annual report, accounts and disclosures and significant financial reporting judgements contained therein, before submission to the Board, focusing particularly on major judgemental areas, any changes in accounting policies and practices, significant adjustments arising from the audit, going concern assumption and compliance with the relevant accounting standards and other legal requirements. During the year, eight Audit Committee meetings were held with due notice of issues to be discussed, recording its conclusions in discharging its duties and responsibilities. The minutes of the Committee meetings were formalised and made available to the Board of Directors for their information.
Integrated Risk Management Committee: Mr D S P Wikramanayake* Mr H D S Amarasuriya Ms G D C Ekanayake Mr N I R de Mel Mr F Ozman (CFO) Ms Nirmala Rayen (Head - Group Risk Management) Ms C Chandrapala (Head - Market Risk) Mr S S Ganendran (Head - Operational Risk)	The Integrated Risk Management Committee was formed in June 2008 replacing the Risk & Credit Committee of the Board, in compliance with the Section 3 (6) of Direction No. 11 of 2007, on the subject 'Corporate Governance for Licensed Commercial Banks in Sri Lanka'. The Committee consists of three Non-Executive Directors, the Chief Executive Officer, Head Group Risk, Head of Operational Risk, Head of Market Risk and Head of Strategic Risk(CFO). In addition, key members of the staff participate at the meetings as appropriate. **IRMC Committee Meetings** The Committee held four meetings on a quarterly basis during the year under review to discuss the normal scope of work. The attendance of Committee Members at meetings is given on page 199 of the Annual Report. The minutes of the Committee meetings were made available to the Board of Directors for their information and necessary action and were affirmed by the Board.

Committee/Composition as at 31 December 2012	Scope of the Board Committee/Principal Activities carried out during the year
	Scope of Duties The main responsibility of the Committee is to assess risks faced by the Bank covering mainly credit, market, liquidity, operational and strategy. In fulfilling its duties, the Committee covers the following areas: • Review the quality of the portfolio on a business line basis, product, groups, sectors, trends in NPL, capital adequacy and stress tests on capital adequacy. • Review adequacy of provisions and approve the charge/ release for the period. • Review liquidity position, impact on market volatility, performance of equity portfolio, country exposures. • Review progress on operational risk roll-out throughout the organization. • Review of Business Continuity Plans. • Assess adequacy and effectiveness of all Executive Credit Committees, Policy Committees on Credit, Market and Operational Risk and ALCO • Compliance with the local laws and regulations etc. • Propose appropriate corrective action to mitigate specific risks in case such risks are beyond prudent levels agreed upon based on internal and regulatory requirements. • Review and approve the new products developed prior to roll out. • Review and approve policies relating to the risk categories. A risk assessment report is submitted to the Board of Directors on a quarterly basis, within one week of the Committee meeting.

Committee/Composition as at 31 December 2012	Scope of the Board Committee/Principal Activities carried out during the year
Strategic Issues Committee: Mr H D S Amarasuriya* Mr A K Pathirage Ms K Fernando Mr T L F W Jayasekara Mr S Rajapakse Mr H A Siriwardena Mr D S P Wikramanayake	The Strategic Issues Committee was formed in 2005. The Committee consists of seven Non-Executive Directors. The Committee was set-up to examine and evaluate strategic issues of a regular as well as an ad hoc nature and recommend any action the Board should take. The Committee was set up to serve as a catalyst as well as to monitor the development and implementation of the Bank's business strategies. The Committee assists the Board in maintaining an interactive strategic planning process with the management. This includes review and assessment of business strategy plans developed by the management and approved by the Board. **Committee Meetings** The Committee meets as and when necessary and as such there was one meeting of the Committee during the year under review. The Chairman of the Committee is the Chairman of the Board. The majority of the Committee members are independent directors of the Bank. The Chief Executive Officer and the management may be present at meetings of the Committee. The minutes of the Committee meetings would be made available to the Board of Directors for their information and necessary action. **Scope of Duties** The main responsibilities of the Committee are- • To provide strategic direction and strategic thinking of the Board to the management in the development and implementation of the Bank's strategic plan; • Together with the management to develop the Bank's strategy and its implementation; • To review and assess the formulation and the implementation of strategic plans developed by the management and approved by the Board; To review and evaluate strategic issues and plans of subsidiary companies of the NDB Group to ensure that the same are in line with the strategic initiatives and strategic direction of the Bank.

Committee/Composition as at 31 December 2012	Scope of the Board Committee/Principal Activities carried out during the year
Human Resources and Remuneration Committee: Mr H D S Amarasuriya* Mr A K Pathirage Ms K Fernando Mr T L F W Jayasekara Mr S Rajapakse Mr H A Siriwardena	The Human Resources and Remuneration Committee was formed in 2003. The Committee consists of six Non-Executive directors. The Committee was set up to determine the human resources and remuneration policies (salaries, allowances and other financial payments) relating to Directors, the CEO and KMP. The Committee also evaluates the performance of the CEO and the KMP against the set targets and goals periodically and determines the basis for revising remuneration benefits and other payments of performance based incentives. **Committee Meetings** The Committee held four meetings during the year under review. The attendance of Committee Members at meetings is given on page 199 of the Annual Report. The minutes of the Committee meetings were made available to the Board of Directors for their information and necessary action and were affirmed by the Board. **Scope of Duties** The main responsibilities of the Committee are to recommend to the Board the apportionment of the remuneration, perquisites and benefits of Non-Executive Directors including the Chairman out of a total sum determined for the purpose by the shareholders in terms of the Bank's Articles and to recommend to the Board the remuneration payable to the Executive Directors and the CEO of the Bank in terms of the Bank's Articles. The Committee is in the process of documenting the goals and targets for Directors and formulating the remuneration policy for Directors.

Committee/Composition as at 31 December 2012	Scope of the Board Committee/Principal Activities carried out during the year
Nominations Committee: Mr H D S Amarasuriya* Mr A K Pathirage Mr T L F W Jayasekara Mr S Rajapakse Mr H A Siriwardena	The Nominations Committee was formed in 2007. The Committee consists of five Non-Executive Directors. The Committee was set up to identify individuals qualified to become members of the Board and to recommend to the Board the nominees for the next Annual General Meeting. **Committee Meetings** The Committee held four meetings during the year under review. The minutes of the Committee meetings were made available to the Board of Directors for their information and necessary action and were affirmed by the Board. **Scope of Duties** The main responsibilities of the Committee are- • Implement a procedure to select/appoint Directors, the CEO and KMP; • To consider and recommend (or not recommend) the election of current Directors, taking into account the performance and contribution made by the Director concerned towards the overall discharge of the Board's responsibilities. To set up the criteria such as qualifications, experience, key attributes required for eligibility to be considered for appointment or promotion to the post of CEO and the Key Management positions.

Committee/Composition as at 31 December 2012	Scope of the Board Committee/Principal Activities carried out during the year
Corporate Governance and Legal Affairs Committee: Ms K Fernando* Ms G D C Ekanayake Mr H A Siriwardena Mr N I R de Mel	NDB has continuously emphasized the need for good business practices and governance structures. The importance of structures and processes have been a key factor in the success of business as it brings in better risk management practices through enhanced accountability and transparency. The Corporate Governance and Legal Affairs Committee was formed in the year 2007. The principal purposes of the Committee are to assist the Board of Directors of NDB in defining the Governance Role, improving Board processes and ensuring effective governance. In addition to the powers and responsibilities expressly delegated to the Committee, the Committee may also exercise any other powers and carry out any other responsibilities delegated to it by the Board from time to time consistent with the Bank's Articles of Association (Constitution) and applicable laws and regulations. The Committee consists of three Non-Executive Directors and the CEO. In addition, key members of the staff participate at the meetings as appropriate. **CGLA Committee Meetings** The Committee held two meetings, during the year under review. The attendance of Committee Members at meetings is given on page 199 of the Annual Report. **Scope of Duties** The Committee is mandated with the task of assisting the Board in ensuring compliance with the Companies Act No. 07 of 2007, the Banking Act Directions on Corporate Governance, the Bank's internal Code of Corporate Governance and all rules, regulations and guidelines issued by regulatory authorities relating to Corporate Governance for licensed commercial banks and reviewing, on a regular basis, the overall Corporate Governance of the Bank including its Constitution, the CGLA Charter and the internal Code of Corporate Governance and recommending improvements as appropriate.

**Chairman of the Committee*

Structure and Composition of the Main Board, Board Committees as at end 2012 and the attendance of each Director is set out in the table below:

Name of Director	Category	Main Board		Audit Committee		Integrated Risk Management Committee		Strategic Issues Committee		Human Resources and Remuneration Committee		Nominations Committee		Corporate Governance and Legal Affairs Committee	
Committee/ Composition		*E	*A	*E	*A	*E	*A	*E	*A	*E	*A	*E	*A	*E	A*
H D S Amarasuriya (Chairman)	Non-Executive Independent	15	15			4	4	1	1	4	4	4	4		
Mr A K Pathirage (Deputy Chairman)	Non-Executive Non-Independent	15	14					1	1	4	4	4	4		
N I R de Mel (CEO)	Executive Non-Independent	15	12	8	7	4	3							2	2
T L F W Jayasekara	Non-Executive Independent	15	11	8	8			1	0	4	4	4	2		
D S P Wikramanayake	Non-Executive Non-Independent	15	15	8	6	4	3	1	0						
K Fernando	Non-Executive Independent	15	14	8	5			1	1	4	3			2	2
H A Siriwardena	Non-Executive Independent	15	13					1	0	4	2	4	4	2	2
G D C Ekanayake	Non-Executive Non-Independent	15	14	8	6	4	4							2	2
S Rajapakse	Non-Executive Non-Independent	15	14	8	8			1	0	4	4	4	4		

**E - Eligible to attend* **A - Attended*

NDB Group Companies

NDB Capital Holdings PLC
(Formerly known as Capital Development and Investment Company PLC

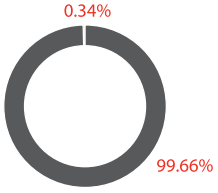
40, Navam Mawatha, Colombo 02.
Tel: +94 11 2300385-90

(Venture Capital)

NDB Group's Investment	Rs 2,331 mn
Profit after Tax (Group)	Rs 6,584 mn
Net Assets (Group)	Rs 11,557 mn

Directors:
A K Pathirage - Chairman
D S P Wikramanayake
N I R de Mel
Aruni Rajakarier
M Arsakularatne (Appointed w.e.f. 18.12.2012)
I A Wickramasinghe
C V Kulatilaka
N Wadugodapitiya (Resigned w.e.f. 18.01.2012)

NDB's direct holding - 99.6%



NDB Others

NDB Investment Bank Ltd.

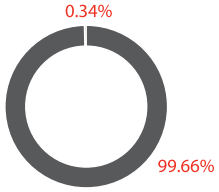
40, Navam Mawatha, Colombo 02.
Tel: +94 11 2300385

(Investment Banking)

NDB Group's Investment	Rs 290 mn
Profit after Tax	Rs 59 mn
Net Assets	Rs 334 mn

Directors:
D S P Wikramanayake - Chairman
N I R de Mel
C V Kulatilaka
D G Perera
S Peiris

NDB's indirect holding - 99.6%



NDB Others

NDB Stockbrokers (Pvt) Ltd.

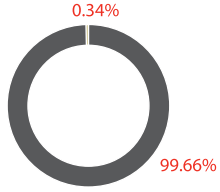
40, Navam Mawatha, Colombo 02.
Tel: +94 11 2131000

(Stockbroking)

NDB Group's Investment	Rs 292 mn
Profit after Tax	–
Net Assets	Rs 284 mn

Directors:
S R de Silva - Chairman
N I R de Mel
C V Kulatilaka
I A Wickramasinghe
S N Jayasinghe (Resigned w.e.f. 23.03.2012)

NDB's indirect holding - 99.6%



NDB Others

NDB Group Companies

Development Holdings (Pvt) Ltd.

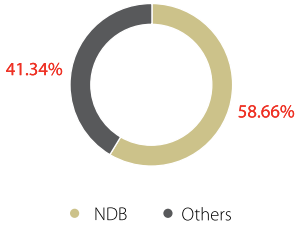
42, Navam Mawatha, Colombo 02.
Tel: +94 11 2436279

(Property Development)

NDB Group's Investment	Rs 228 mn
Profit after Tax	Rs 99 mn
Net Assets	Rs 1,830 mn

Directors:
Mrs C L Jayawardena
Mrs D Seneviratne
J Ratnayake
Ms S Weerakoon
S Wijesinghe
Mrs P K Sumithrarachchi
I A Wickramasinghe (Appointed w.e.f. 22.06.2012)
S Rajapakse (Appointed w.e.f. 28.09.2012)
E D K Weerasuriya (Resigned w.e.f. 31.05.2012)
S N Jayasinghe (Resigned w.e.f. 29.02.2012)
H A Siriwardena (Appointed on 12.03.2012 and resigned on 30.07.2012)

NDB's direct holding - 58.66%



NDB Capital Ltd.

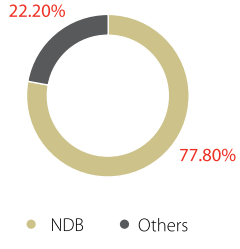
Bilquis Tower (5th Floor), Plot No. 06,
Gulshan No. 02, Dhaka, Bangladesh
Tel: +88 02 9888626, +88 02 9888979
Fax: +88 02 9888906

(Investment Banking)

NDB Group's Investment	Rs 131 mn
Profit after Tax	Rs (37) mn
Net Assets	Rs 106 mn

Directors:
H D S Amarasuriya - Chairman
A M Khan
C M Alam
C V Kulatilaka
K Jayawardana
Mrs Z Chowdhury
H F Choudhury
Q G R Arif - MD (Appointed w.e.f. 25.01.2012)

NDB's direct holding - 78%



Ayojana Fund (Pvt) Ltd.

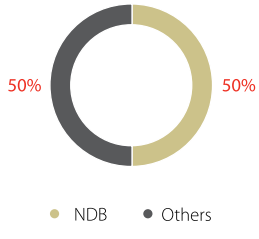
1st Floor, Parkway Building
48 1/1, Park Street, Colombo 02.
Tel: +94 11 2307230

(Venture Capital)

NDB Group's Investment	Rs 0.1 mn
Profit after Tax	–
Net Assets	–

The Company is under liquidation and Mr. Thomas Prins of CAS Corporate Services (Pte.) Ltd. has been appointed as liquidator.

NDB's direct holding - 50%



NDB Group Companies

NDB Wealth Management Ltd.
(Formerly known as NDB AVIVA Wealth Management Ltd.)

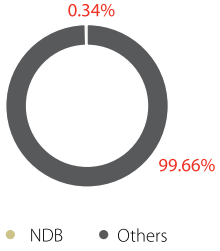
No. 42, Navam Mawatha, Colombo 02.
Tel: +94 11 2303232

(Wealth Management)

NDB Group's Investment	Rs 412 mn
Profit after Tax	Rs 48 mn
Net Assets	Rs 275 mn

Directors:
D S P Wikramanayake - Chairman
C V Kulatilaka
T R Ramachandran (Resigned w.e.f. 05.12.2012)
N I R de Mel
D U R Wijesinghe (Resigned w.e.f. 05.12.2012)

NDB's indirect holding - 99.66%



NDB Venture Investments (Pvt) Ltd.

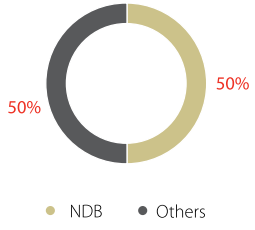
1st Floor, Parkway Building
48 1/1, Park Street, Colombo 02.
Tel: +94 11 2307230

(Venture Capital)

NDB Group's Investment	Rs 19 mn
Profit after Tax	–
Net Assets	Rs 67 mn

The Company is under liquidation and Mr Thomas Prins of CAS Corporate Services (Pte.) Ltd. has been apponted as the liquidator.

NDB's direct holding - 50%



Maldives Finance Leasing Company (Pvt) Ltd.

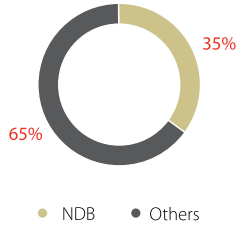
04-01 Aage,
No. 12, Boduthakurufaanu Magu, Male' 20-094,
Republic of Maldives
Tel: +(960) 3315605/3315606
Fax: (960) 3315608

(Leasing)

NDB Group's Investment	Rs 165 mn
Profit after Tax	Rs (42) mn
Net Assets	Rs (18) mn

Directors:
M H Maniku
N I R de Mel
A A Abdulla
H Afeef
H Rasheed
A Noordeen
S Reza (ex-officio)

NDB's direct holding - 35%



AVIVA NDB Holdings Lanka (Pvt) Ltd.
(Group Company upto 5 December 2012)

No. 75, Kumaran Ratnam Road, Colombo 02.
Tel: +94 11 2310000

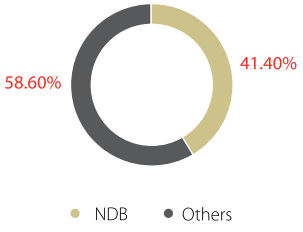
(Holding Company of AVIVA NDB Insurance PLC)

NDB Group's Investment	–
Profit after Tax	Rs 969 mn
Net Assets	Rs 4,145 mn

Directors:

H T Phong - Chairman (Appointed w.e.f. 04.12.2012)
R Bates (Appointed w.e.f. 04.12.2012)
M Ramachandran (Appointed w.e.f. 04.12.2012)
S Machell - Chairman (Resigned w.e.f. 04.12.2012)
R J Donaghy (Resigned w.e.f. 04.12.2012)
T R Ramachandran (Resigned w.e.f. 04.12.2012)
N I R de Mel (Resigned w.e.f. 05.12.2012)
D S P Wikramanayake (Resigned w.e.f. 05.12.2012)

NDB's indirect holding - 41.40%



AVIVA NDB Insurance PLC
(Group Company upto 5 December 2012)

No. 75, Kumaran Ratnam Road, Colombo 02.
Tel: +94 11 2310000

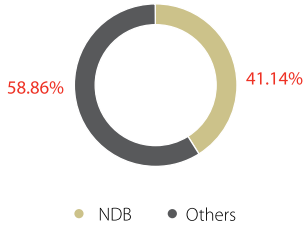
(Insurance)

NDB Group's Investment	–
Profit after Tax	Rs 780 mn
Net Assets	Rs 4,063 mn

Directors:

T R Ramachandran - Chairman
(Resigned w.e.f. 04.12.2012)
S Rouf - Managing Director
D Sooriyaarachchi
D Hope (Resigned w.e.f. 01.04.2012)
N Majmudar (Resigned w.e.f. 17.12.2012)
N I R de Mel (Resigned w.e.f. 05.12.2012)
D S P Wikramanayake (Resigned w.e.f. 05.12.2012)
L de Mel (Resigned w.e.f. 26.03.2012)
I A Wickramasinghe (Resigned w.e.f. 08.02.2012)
H A Siriwardena (Appointed w.e.f. 08.02.2012 & Resigned w.e.f. 05.12.2012)

NDB's indirect holding - 41.14%



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Financial Calendar 2012

Interim Quarterly Unaudited Reports for 2012

March - 15 May 2012*

June - 15 August 2012*

September - 14 November 2012*

December - 26 February 2013*

Meetings

First Annual General Meeting - 26 April 2006

Second Annual General Meeting - 26 April 2007

Third Annual General Meeting - 29 April 2008

Fourth Annual General Meeting - 30 March 2009

Fifth Annual General Meeting - 30 March 2010

Sixth Annual General Meeting - 30 March 2011

Seventh Annual General Meeting - 30 March 2012

Eighth Annual General Meeting - 28 March 2013

* Published in the newspapers

Annual Report of the Directors on the State of Affairs of National Development Bank PLC

The Directors of the National Development Bank PLC (NDB) have pleasure in presenting their Report on the State of Affairs of NDB together with the Audited Financial Statements for the year ended 31 December 2012.

The Audited Financial Statements were approved by the Board of Directors at a Board meeting held on 13 February 2013.

Principal Activities

The principal activities of NDB and NDB Group are described under Note 1 to the Financial Statements on page 264.

Details of the NDB Group companies indicating NDB's own holding in key companies is shown on pages 200 to 203.

Vision, Mission and Values

The Vision, Mission and Values of NDB are given on page 2 of this Report.

Review of Business

The Chairman's Letter, the Chief Executive Officer's Review, the Financial Review and the Operations Review which form an integral part of the Directors' Report on the State of Affairs of NDB, contain a detailed description of the operations of NDB during the year ended 31 December 2012 and contain a fair view of NDB's affairs.

Directors' Responsibility for Financial Reporting

The Directors are responsible for the preparation of the Financial Statements of NDB 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. 07 of 2007, the Banking Act No. 30 of 1988 (as amended), the Listing Rules of the Colombo Stock Exchange and the Direction on Corporate Governance for Licensed Commercial Banks issued by the Central Bank of Sri Lanka.

The Directors are satisfied that the Financial Statements, presented on pages 226 to 318 inclusive, give a true and fair view of the state of affairs of NDB and the NDB Group as at 31 December 2012 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.

Annual Report of the Directors on the State of Affairs of National Development Bank PLC

Corporate Governance

The Directors are responsible for the governance of NDB including the establishment and maintenance of NDB'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 and that the internal control systems referred to above are effective.

A description of NDB's Corporate Governance Practices is set out on pages 176 to 199.

Profits and Reserves

The NDB Group's profit before Financial Services VAT including that of its subsidiaries and its share of profit from associate companies amounted to Rs 10,830 mn (compared to Rs 4,360 mn in 2011). After deducting Rs 1,898 mn (compared to Rs 1,597 mn in 2011) for taxation, the profit after tax for the year amounted to Rs 8,932 mn (compared to Rs 2,763 mn in 2011).

NDB's profit before Financial Services VAT amounted to Rs 4,607 mn (compared to Rs 3,110 mn in 2011). After deducting Rs 1,683 mn (compared to Rs 1,279 mn in 2011) for taxation, the profit after tax for the year amounted to Rs 2,924 mn (compared to Rs 1,831 mn in 2011).

Details are given in the Income Statement on page 226.

Details of the reserves are shown in the Statement of Changes in Equity on page 230.

Shares and Shareholders

NDB had 8,374 registered shareholders as at 31 December 2012. The distribution, public holding, 20 largest shareholders and the share price during 2012 are set out in page 326 of this Annual Report.

Strategic Change

In December 2012, NDB's subsidiary, NDB Capital Holdings PLC divested its shareholding in AVIVA NDB Holdings Lanka (Pvt) Ltd. and AVIVA NDB Insurance PLC realizing a capital gain of Rs 6.0 bn.

Dividend

NDB paid a final dividend of Rs 4.00 per share for the year ended 31 December 2011, and an interim dividend of Rs. 5.00 per share for the year ended 31 December 2012. In declaring the dividends the Directors ensured due compliance by NDB of the solvency provisions contained in the Companies Act No. 07 of 2007. These dividends were partly paid out of dividends received and partly out of taxable profits, the latter being subject to withholding tax.

Annual Report of the Directors on the State of Affairs of National Development Bank PLC

Property, Plant & Equipment and Depreciation

Details of the property, plant & equipment of NDB, additions made during the year and the depreciation charges for the year are shown in Note 32 to the Financial Statements on page 279.

Donations

No donations to external charitable or political organizations were made by NDB during the year, except for the following:

	Amount Rs
NDB Bank Cancer Aid Trust Fund	500,000
Tsunami Orphans	200,000
The Ceylon School for the Deaf and Blind	200,000
The Children's Heart Project of Sri Lanka	200,000
Victoria Home for Incurables	200,000
Ranaviru Rehabilitation Fund	200,000
Martin Wickramasinghe Trust	200,000
Lanka Alzheimer's Foundation	150,000
The Ceylon Association for the Mentally Retarded	100,000
Society for the Uplift and Rehabilitation of Leprosy Patients	100,000
Lt. General Denzil Kobbekaduwa Trust	100,000
The National Institute of Mental Health	100,000
Missionaries of Charity	100,000
Leonard Cheshire Disability Resource Center	75,000
Sri Lanka Sumithrayo	75,000
Prithipura Infant Home	50,000
Educate a Child Trust	50,000
Prisoners Welfare Association - Sri Lanka	50,000
Zonta Club	50,000
English Communication Programme	2,979,900
Library Project for Rural Schools	600,000
Jeevana Livelihood Development	188,608
Endowed Chair in Entrepreneurship - University of Moratuwa	3,019,510
Department-wise CSR Activities	2,050,000
Other Donations	1,902,124
Total	13,440,142

The Sustainability Report of NDB is given on pages 102 to 151 of the Annual Report.

Annual Report of the Directors on the State of Affairs of National Development Bank PLC

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.

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

Post-Balance Sheet Events

There have been no events subsequent to the Balance Sheet date that require disclosure.

Stated Capital and Debentures

The stated capital of NDB at the beginning and end 2012 of the year was Rs 1,093,094,670/-.

In 2011, NDB privately placed rated subordinated unsecured unlisted redeemable debentures having an aggregate face value of Rs 400,000,000/-. The proceeds of these debentures were utilized for lending purposes. The details of the said debentures are as follows:

Date	Amount Rs	Number of Debentures	Value Rs	Redemption	Rate of Interest
30 June 2011	1,000 each	110,000	110,000,000	30 June 2016	03 months gross TBR + 1.00% per annum
22 July 2011	1,000 each	290,000	290,000,000	30 June 2016	03 months gross TBR + 1.00% per annum

Directorate

In terms of the provisions of the Articles of Association of NDB, the Board of Directors, as at 31 December 2012, consisted of nine (09) Directors, including the Chairman and was made up as follows:

- Seven (07) Directors have been appointed by the shareholders;
- One Director has been appointed as a representative of the Ministry of Finance and;
- The Chief Executive Officer is an ex-officio Director, with voting rights.

The list of Directors who held office during the year under review and changes thereto are given on page 332.

In terms of the provisions of the Articles of Association of NDB, one-third of the elected Directors shall retire from office and new Directors will be elected at each Annual General Meeting of NDB. Accordingly, Mr D S P Wikramanayake and Mr H A Siriwardena will retire and stand for re-election by the shareholders at the Annual General Meeting of NDB.

Annual Report of the Directors on the State of Affairs of National Development Bank PLC

Compliance by the Board of Directors of the Banking Direction No. 11 of 2007 on Corporate Governance for Licensed Commercial Banks in Sri Lanka issued by the Central Bank of Sri Lanka is set out in pages 181 to 190 of the Annual Report. In terms thereof the classification of directors as executive, non-executive, independent and non-independent as at 31 December 2012 is given below:

Name of director	Independent/ Non-Independent	Executive/ Non-Executive
H D S Amarasuriya	Independent	Non-Executive
A K Pathirage	Non-Independent	Non-Executive
N I R de Mel (CEO)	Non-Independent	Executive
T L F Jayasekara	Independent	Non-Executive
D S P Wikramanayake	Non-Independent	Non-Executive
Ms K Fernando	Independent	Non-Executive
H A Siriwardena	Independent	Non-Executive
Ms G D C Ekanayake	Non-Independent	Non-Executive
S Rajapakse	Non-Independent	Non-Executive

In terms of an approval received from the Board of Directors of the Colombo Stock Exchange on 30 March 2010, Licensed Commercial Banks have been granted a total exemption from the requirement to comply with Section 7.10 (Corporate Governance) of the Continuing Listing Requirements under the CSE Listing Rules with effect from 1 January 2010.

Interest Register

The Bank, as per the Companies Act No. 07 of 2007, maintains the Interest Register. All Directors have made declarations as provided for in Section 192 (2) of the Companies Act aforesaid. The related entries were made in the Interest Register during the year under review. The share ownership of Directors is indicated elsewhere in this Report. Entries were made in the Interest Register on share disposals, Directors' interest in contracts, remuneration paid to the Directors etc. The Interest Register is available for inspection as required under the Companies Act.

Directors' interests in contracts or proposed contracts with the Company, both direct and indirect are disclosed on pages 214 and 215 of this Annual Report. These interests have been declared at Directors' Meetings. As a practice, Directors have refrained from voting on matters in which they were materially interested. Directors have no direct or indirect interest in any other contract or proposed contract with the Company.

Annual Report of the Directors on the State of Affairs of National Development Bank PLC

Directors' Emoluments

Directors' fees and emoluments, in respect of the Group and NDB for the financial year ended 31 December 2012 are as follows:

	NDB	Group
Directors' Fees and Emoluments (Rs mn)	45,740	46,710

Insurance and Indemnity

Pursuant to a decision of the Board, NDB obtained an Insurance Policy to cover Directors' liability.

Directors' Shareholdings

Shareholdings of the Directors in NDB as at the year-end and their corresponding holdings as at the end of the previous year are as shown on page 325 of this Annual Report.

Directors' Interests in Debentures

There were no debentures registered in the name of any Director as at the beginning and at the end of the year.

Board Sub committees

There are six permanent committees of the Board, namely, Integrated Risk Management Committee, Audit Committee, Strategic Issues Committee, Remuneration and Human Resources Committee, Nominations Committee and Corporate Governance and Legal Affairs Committee. Details of the members of these six committees are given on page 332.

Auditors

The Financial Statements for the year ended 31 December 2012 have been audited by Messrs Ernst & Young, Chartered Accountants.

Fees to Auditors

The fees paid to Auditors during the year was Rs 7.2 mn (2011 - Rs 6.0 mn) for audit work and Rs 0.7 mn for non-audit work (2011 - Rs 0.9 mn).

Annual Report of the Directors on the State of Affairs of National Development Bank PLC

Reappointment of Auditors

The Auditors have indicated their willingness to offer themselves for reappointment. The Board Audit Committee and the Board of Directors have recommended the reappointment of the Auditors. A resolution appointing Messrs Ernst & Young as Auditors and authorizing the Directors to fix their remuneration will be proposed at the Annual General Meeting.

As required by the Companies Act No. 07 of 2007, the Board of Directors hereby acknowledge the contents of this report

For and on behalf of the Board,

H D S Amarasuriya
Chairman

N I R de Mel
Chief Executive Officer

S A Ranasinghe
Secretary to the Board

13 February 2013

Directors' Interests in Contracts with National Development Bank PLC

	Relationship	Accommodation Granted/Deposits	Balance Outstanding as at 31.12.2012 Rs '000	Balance Outstanding as at 31.12.2011 Rs '000
(a) Mr H D S Amarasuriya				
Singer (Sri Lanka) PLC	Chairman	Deposits & Investments	–	13,338
		Loans/Advances	319,740	150,000
		Off-Balance Sheet Accommodations	128,917	112,918
Singer Finance (Lanka) PLC	Chairman	Deposits & Investments	524	198
Regnis Lanka PLC	Chairman	Deposits & Investments	1,456	6,554
		Loans/Advances	83,766	88,461
		Off-Balance Sheet Accommodations	29,952	76,434
Regnis Appliances (Pvt) Ltd.	Chairman	Loans/Advances	51,893	646
		Off-Balance Sheet Accommodations	169,120	265,479
Bata Shoe Co. of Ceylon Ltd.	Director	Deposits & Investments	799	11
ACL Cables PLC	Director	Deposits & Investments	1,691	–
		Loans/Advances	3,159	10,885
		Off-Balance Sheet Accommodations	–	67,921
C W Mackie PLC	Director	Deposits & Investments	2,007	1,837
		Loans/Advances	–	218,620
		Off-Balance Sheet Accommodations	92,119	–
(b) Mr A K Pathirage				
Softlogic Holdings PLC	Chairman/Managing Director	Deposits & Investments	53,161	1,155
		Loans/Advances	500,000	500,536
Uni Walkers (Pvt) Ltd.	Chairman/Managing Director	Loans/Advances	144,957	141,562
		Off-Balance Sheet Accommodations	19,144	6,317
Asiri Central Hospitals PLC	Chairman/Managing Director	Loans/Advances	18,750	23,750
Central Hospital Ltd.	Chairman/Managing Director	Loans/Advances	–	41,560
Softlogic Capital PLC	Chairman	Deposits & Investments	–	2,637
		Loans/Advances	450,114	450,000
Softlogic Communications (Pvt) Ltd.	Chairman	Deposits & Investments	6,558	6,797
		Loans/Advances	409,386	421,698
		Off-Balance Sheet Accommodations	9,619	2,591
Softlogic Information Technologies (Pvt) Ltd.	Chairman	Deposits & Investments	2,283	220
		Loans/Advances	22,359	–
		Off-Balance Sheet Accommodations	29,839	–
Softlogic International (Pvt) Ltd.	Chairman	Deposits & Investments	9,565	–
Asian Alliance Insurance PLC	Chairman	Deposits & Investments	17	–
Asiri Hospital Holdings PLC	Managing Director	Deposits & Investments	200,779	2,895
NDB Capital Holdings PLC	Chairman	Deposits & Investments	3,973	637,388

Directors' Interests in Contracts with National Development Bank PLC

	Relationship	Accommodation Granted/Deposits	**Balance Outstanding as at 31.12.2012 Rs '000**	Balance Outstanding as at 31.12.2011 Rs '000
(c) Mr N I R De Mel				
NDB Investment Bank Ltd.	Director	Deposits & Investments	**11,419**	163,309
		Loans/Advances	**2**	–
NDB Capital Holdings PLC	Director	Deposits & Investments	**3,973**	637,388
Maldives Finance Leasing Company Ltd.	Director	Deposits & Investments	**1**	144
NDB Wealth Management Ltd.	Director	Deposits & Investments	**7**	153
NDB Stockbrokers (Pvt) Ltd.	Director	Deposits & Investments	**–**	141,524
(d) Ms K Fernando				
L B Finance PLC	Director	Deposits & Investments	**275**	441
		Loans/Advances	**750,600**	1,145,700
(e) Mr D S P Wikramanayake				
NDB Wealth Management Ltd.	Director	Deposits & Investments	**7**	153
NDB Investment Bank Ltd.	Director	Deposits & Investments	**11,419**	163,309
		Loans/Advances	**2**	–
NDB Capital Holdings PLC	Director	Deposits & Investments	**3,973**	637,388
Orient Finance PLC	Director	Loans/Advances	**273,078**	–
(f) Mr T L F Jayasekera				
Brandix Lanka Ltd.	Director	Deposits & Investments	**–**	1,118
Ceylease Financial Services Ltd.	Director	Deposits & Investments	**102**	56
		Loans/Advances	**250,000**	191,868
(g) Mr S Rajapakse				
Asian Alliance Insurance PLC	Director	Deposits & Investments	**17**	–
Development Holdings (Pvt) Ltd.	Director	Deposits & Investments	**213,103**	–

Statement of Directors' Responsibilities

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

It is also the responsibility of the Directors to ensure that NDB 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. 07 of 2007 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 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 pages 221 to 224 of this Report.

Messrs Ernst & Young, Chartered Accountants have been made available with all records of NDB 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 225 of this Report.

The NDB has also complied with the prudential requirements, regulations, laws and internal controls and there were no material non-compliances.

By Order of the Board,

Mrs. Shehani Ranasinghe
Secretary to the Board

13 February 2013

Directors' Statement on Internal Control Over Financial Reporting

Responsibility

In line with the Banking Act Direction No. 11 of 2007, Section 3 (8) (ii) (b), the Board of Directors presents this report on Internal Control over Financial Reporting.

The Board of Directors ('Board') is responsible for the adequacy and effectiveness of the internal control mechanism in place at National Development Bank PLC, ('the Bank'). In considering such adequacy and effectiveness, the Board recognizes that the business of banking requires reward to be balanced with risk on a managed basis and as such the internal control systems are primarily designed with a view to highlighting any deviations from the limits and indicators which comprise the risk appetite of the Bank. In this light, the system of internal controls can only provide reasonable, but not absolute assurance, against material misstatement of financial information and records or against financial losses or fraud.

The Board has established an ongoing process for identifying, evaluating and managing the significant risks faced by the Bank and this process includes enhancing the system of internal controls over financial reporting as and when there are changes to business environment or regulatory guidelines.

The process is regularly reviewed by the Board and is in accordance with the Guidance for Directors of Banks on the Directors' Statement on Internal Control issued by the Institute of Chartered Accountants of Sri Lanka. The Board has assessed the internal control over financial reporting taking into account principles for the assessment of internal control system as given in that guidance.

The Board is of the view that the system of internal controls over financial reporting in place is sound and adequate to provide reasonable assurance regarding the reliability of financial reporting, and that the preparation of Financial Statements for external purposes is in accordance with relevant accounting principles and regulatory requirements.

The management assists the Board in the implementation of the Board's policies and procedures on risk and control by identifying and assessing the risks faced and in the design, operation and monitoring of suitable internal controls to mitigate and control these risks.

Key Features of the Process Adopted in Applying and Reviewing the Design and Effectiveness of the Internal Control System over Financial Reporting

The key processes that have been established in reviewing the adequacy and integrity of the system of internal controls with respect to financial reporting include the following:

Various Committees are established by the Board to assist the Board in ensuring the effectiveness of the Bank's daily operations and that the Bank's operations are in accordance with the corporate objectives, strategies and the annual budget as well as the policies and business directions that have been approved.

Directors' Statement on Internal Control Over Financial Reporting

- The Internal Audit Department of the Bank checks for compliance with policies and procedures and the effectiveness of the internal control systems on an ongoing basis using samples and rotational procedures and highlights significant findings in respect of any non-compliance. Audits are carried out on all units and branches, the frequency of which is determined by the level of risk assessed, to provide an independent and objective report. The annual audit plan is reviewed and approved by the Board Audit Committee. Findings of the Internal Audit Department are submitted to the Board Audit Committee for review at their periodic meetings.

- The Board Audit Committee of the Bank reviews internal control issues identified by the Internal Audit Department, regulatory authorities and management, and evaluate the adequacy and effectiveness of the risk management and internal control systems. They also review the internal audit functions with particular emphasis on the scope of audits and quality of internal audits. The minutes of the Board Audit Committee meetings are forwarded to the Board of the Bank on a periodic basis. Further details of the activities undertaken by the Audit Committee of the Bank are set out in the Audit Committee Report on pages 221 to 224.

In assessing the internal control system over financial reporting, identified officers of the Bank collated all procedures and controls that are connected with significant accounts and disclosures of the Financial Statements of the Bank. These in turn were observed and checked by the Internal Audit Department for suitability of design and effectiveness on an ongoing basis.

As the current year was the first year of adopting new Sri Lanka Accounting Standards comprising LKAS and SLFRS, processes to comply with new requirements of recognition, measurement, classification and disclosure are being introduced, and as at Balance Sheet date were not fully completed. The assessment did not include subsidiaries of the Bank.

Confirmation

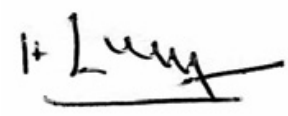
Based on the above processes, the Board confirms that the financial reporting system of the Bank has been designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes and has been done in accordance with Sri Lanka Accounting Standards and regulatory requirements of the Central Bank of Sri Lanka.

Directors' Statement on Internal Control Over Financial Reporting

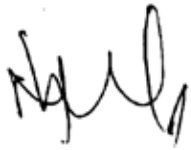
Review of the Statement by External Auditors

The External Auditors have reviewed the above Directors' Statement on Internal Control over financial reporting included in the Annual Report of the Bank for the year ended 31 December 2012 and reported to the Board that nothing has come to their attention that causes them to believe that the statement is inconsistent with their understanding of the process adopted by the Board in the review of the design and effectiveness of the internal control over financial reporting of the Bank.

By order of the Board.



H D S Amarasuriya
Chairman



Trevine Jayasekara
Chairman - Audit Committee

N I R de Mel
Chief Executive Officer

13 February 2013

Independent Assurance Report

ERNST & YOUNG

Chartered Accountants
201 De Saram Place
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Colombo 10
Sri Lanka

Tel : +94 11 2463500
Fax Gen : +94 11 2697369
Tax : +94 11 5578180
eysl@lk.ey.com

INDEPENDENT ASSURANCE REPORT TO THE BOARD OF DIRECTORS OF NATIONAL DEVELOPMENT BANK PLC

Report on the Directors' Statement on Internal Control over Financial Reporting

We were engaged by the Board of Directors of National Development Bank PLC ("Bank") to provide assurance on the Directors' Statement on Internal Control over Financial Reporting ("Statement") included in the annual report for the year ended 31 December 2012.

Management's Responsibility

Management is responsible for the preparation and presentation of the Statement in accordance with the "Guidance for Directors of Banks on the Directors' Statement on Internal Control" issued in compliance with section 3(8)(ii)(b) of the Banking Act Direction No. 11 of 2007, by the Institute of Chartered Accountants of Sri Lanka.

Our Responsibilities and Compliance with SLSAE 3050

Our responsibility is to issue a report to the board on the Statement based on the work performed. We conducted our engagement in accordance with Sri Lanka Standard on Assurance Engagements (SLSAE) 3050 - Assurance Report for Banks on Directors' Statement on Internal Control issued by the Institute of Chartered Accountants of Sri Lanka.

Summary of Work Performed

We conducted our engagement to assess whether the Statement is supported by the documentation prepared by or for directors; and appropriately reflected the process the directors have adopted in reviewing the system of internal control over financial reporting of the Bank.

The procedures performed were limited primarily to inquiries of company personnel and the existence of documentation on a sample basis that supported the process adopted by the Board of Directors.

SLSAE 3050 does not require us to consider whether the Statement covers all risks and controls or to form an opinion on the effectiveness of the Bank's risk and control procedures. SLSAE 3050 also does not require us to consider whether the processes described to deal with material internal control aspects of any significant problems disclosed in the annual report will, in fact, remedy the problems.

Our Conclusion

Based on the procedures performed, nothing has come to our attention that causes us to believe that the Statement included in the annual report is inconsistent with our understanding of the process the Board of Directors has adopted in the review of the design and effectiveness of internal control over financial reporting of the Bank.

(Sgd.)
13 February 2013
Colombo

Partners: A D B Talwatte FCA FCMA M P D Cooray FCA FCMA R N de Saram ACA FCMA Ms. N A De Silva ACA Ms. Y A de Silva FCA W R H Fernando FCA FCMA W K B S P Fernando FCA FCMA A P A Gunasekera FCA FCMA A Herath FCA D K Hulangamuwa FCA FCMA LLB (Lond) H M A Jayesinghe FCA FCMA Ms. A A Ludowyke FCA FCMA Ms. G G S Manatunga ACA N M Sulaiman ACA ACMA B E Wijesuriya ACA ACMA

Audit Committee Report

Purpose and Terms of Reference

The purpose of the Board Audit Committee is to assist the Board of Directors in its general oversight of financial reporting, internal controls and functions relating to internal and external audit. The Charter of the Board Audit Committee, which is periodically reviewed and revised with the concurrence of the Board of Directors, clearly defines the Terms of Reference of the Committee. The Audit Committee Charter was approved by the Board in June 2010 and reviewed in November 2011. The Committee is responsible to the Board of Directors and reports on its activities regularly. The composition requirements, roles and functions of the Committee, are set out in the Banking Act Direction No. 11 of 2007 on 'Corporate Governance for Licensed Commercial Banks in Sri Lanka' (hereinafter referred to as the Direction), 'Rules on Corporate Governance under Listing Rules of the Colombo Stock Exchange' and 'Code of Best Practice on Corporate Governance' issued jointly by the Institute of Chartered Accountants of Sri Lanka and the Securities and Exchange Commission of Sri Lanka.

Committee Composition

The Audit Committee comprised of five Non-Executive Directors for the year, of which two were Independent Directors. The Chairman of the Audit Committee is an Independent Director and a Fellow Member of the Institute of Chartered Accountants of Sri Lanka, while the other members of the Committee are also from specialist financial/auditing backgrounds.

The following Directors serve/served on the Audit Committee:

Mr Trevine Jayasekara	Chairman
Mr Sarath Wikramanayake	Non-Executive Director
Mrs Kimarli Fernando	Non-Executive Director
Ms G D Chandra Ekanayake	Non-Executive Director
Mr Sujeewa Rajapakse	Non-Executive Director

Brief profiles of the members are given on pages 92 to 94 of the Annual Report.

Responsibilities of the Audit Committee

- Monitors the integrity of the Financial Statements
- Oversees the internal control systems including reviewing their effectiveness
- Monitors and reviews the effectiveness of the internal audit function
- Reviews the Company's financial and accounting policies and practices
- Advises the Board on the appointment of the External Auditor and is responsible for oversight and remuneration of the External Auditor

Audit Committee Report

Meetings

The Audit Committee met eight times during the year. Attendance by the Committee Members at each of these meetings is given in the table on page 199 of the Annual Report.

The Chief Executive Officer attended the meetings of the Committee by invitation. The Head of Internal Audit, the Chief Financial Officer, Head of Group Risk and the two Chief Operating Officers also attended the meetings. Other officials were invited to attend the meetings on a need basis. On the invitation of the Committee, the Engagement Partner of the Bank's External Auditors, Messrs Ernst & Young attended all the meetings during the year. The Audit Committee met the External Auditors twice during the year, without the presence of the CEO and the Corporate Management, to ensure that there was no limitation of scope in relation to the audit and to allow for full disclosure of any incidents which could have had a negative impact on the effectiveness of the external audit, and concluded that there were no cause for concern.

Financial Reporting

The Committee assists the Board to discharge their responsibility in the preparation of Financial Statements that reflect a true and fair view on the financial position and performance in accordance with the Bank's accounting records and as per the requirements of the Sri Lanka Accounting Standards. The Committee reviews -

- The adequacy and effectiveness of the Internal Control Systems and Procedures to provide reasonable assurance that all transactions are accurately and completely recorded in the books of account.
- The effectiveness of the Financial Reporting Systems in place to ensure reliability of the information provided to the stakeholders.
- The Bank's financial and accounting policies and practices.
- The processes by which compliance with Sri Lanka Accounting Standards and other regulatory provisions relating to financial reporting and disclosures are ensured.
- The Annual Report and Accounts and the Interim Financial Statements prepared for publication, prior to submission to the Board.

Having assessed the prevailing Internal Control Systems and Procedures, the Committee is of the view that adequate controls and procedures are in place to provide reasonable assurance that the Bank's assets are safeguarded and that the financial position of the Bank is well-monitored and accurately reported.

Risks and Internal Controls

During the year, the Committee reviewed the effectiveness of the Bank's Internal Control System and the CEO's quarterly confirmation on the internal control environment. Additionally, the Committee also assessed the effectiveness of the Bank's internal controls over financial reporting as of 31 December 2012, as required by the Banking Act Direction No. 11 of 2007, Corporate Governance for Licensed Commercial Banks in Sri Lanka, Subsection 3(8)(ii)(b), based on the "Guidance for Directors of Banks on the Directors' Statement on Internal Control" issued by the Institute of Chartered Accountants of Sri Lanka. The result of the assessment is given on page 217 to 219, "Directors' Statement on Internal Control" in the Annual Report. The External Auditors have issued an Assurance Report on Directors' Statement on Internal Controls. The report is given on page 220 of the Annual Report.

Audit Committee Report

Internal Audit

During the year, the Audit Committee reviewed the independence, objectivity and performance of the internal audit function and the adequacy of its resources. The Internal Audit Plan was reviewed and approved by the Committee and the findings of the internal audits completed and their evaluation of the Bank's internal control systems were reviewed. They also reviewed updates on audit activities and the adequacy of coverage of the approved audit plan, the results of any unsatisfactory audits, the action plan to address these areas and the implementation status. Audit findings presented in the reports are prioritized based on the level of risk.

Internal Audit Charter

The internal audit function is governed by the Internal Audit Charter which defines the scope, functions, authority, responsibility, reporting, external relationship management and ethics that assist and direct/guide the Internal Audit Department to discharge its function independently. The Internal Audit Charter was last reviewed and approved in November 2011.

External Audit

The Audit Committee undertook the annual evaluation of the independence and objectivity of the External Auditor and the effectiveness of the audit process.

The Committee met with the External Auditor during the year to discuss their audit approach and procedures, including matters relating to the scope of the audit and Auditor's independence. The Lead Audit Partner is required to be rotated every five years in order to ensure the independence of the Auditor and to comply with the requirements of the Banking Act Direction No. 11 of 2007, Corporate Governance for Licensed Commercial Banks in Sri Lanka.

The Committee reviewed the audited Financial Statements with the External Auditor who is responsible for expressing an opinion on its conformity with the Sri Lanka Accounting Standards.

The Committee reviewed the Management Letter for the year 2011, issued by the External Auditor with the management responses thereto.

The Audit Committee was of the view that the Non-Audit Services provided by the External Auditor were not within the category of services identified as prohibited under -

1. The guidelines issued by the Central Bank of Sri Lanka for External Auditors, relating to their statutory duties in terms of Section 39 of the Banking Act No. 30 of 1988 and its amendments thereto.
2. The guidelines for Listed Companies on Audit and Audit Committees issued by the Securities and Exchange Commission of Sri Lanka.

The Audit Committee recommends to the Board of Directors that Messrs Ernst & Young, Chartered Accountants, be reappointed for the financial year ending 31 December 2013, subject to the approval of the shareholders at the next Annual General Meeting.

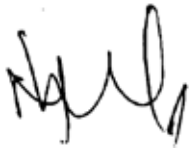
Audit Committee Report

Whistle-Blowing

The Bank's Whistle-Blowing Policy is intended to serve as a channel of corporate fraud risk management. The policy will allow any team member who has a legitimate concern on an existing or potential "wrong doing", done by any person within the Bank, to come forward voluntarily, and bring such concern to the notice of an independent designated authority. Concerns raised are investigated and the identity of the person raising the concern is kept confidential, as even anonymous complaints are looked at.

Evaluation of the Board Audit Committee

The Audit Committee conducted a self-review of its effectiveness for the year and concluded that its performance was effective.



Trevine Jayasekara
Chairman of the Audit Committee

13 February 2013

Independent Auditors' Report

ERNST & YOUNG

Chartered Accountants
201 De Saram Place
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Sri Lanka

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eysl@lk.ey.com

INDEPENDENT AUDITORS' REPORT TO THE SHAREHOLDERS OF NATIONAL DEVELOPMENT BANK PLC

Report on the Financial Statements

We have audited the accompanying financial statements of National Development Bank PLC ("Bank"), the consolidated financial statements of the Bank and its subsidiaries, which comprise of the statements of financial position as at 31 December 2012, and the income statements and statements of comprehensive income, statements of changes in equity and cash flow statements for the year then ended, and a summary of significant accounting policies and other explanatory notes.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with Sri Lanka Accounting Standards. This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

Scope of Audit and Basis of Opinion

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with Sri Lanka Auditing Standards. Those standards require that we plan and perform the audit to obtain reasonable assurance whether the financial statements are free from material misstatement.

An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting policies used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

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, the Bank maintained proper accounting records for the year ended 31 December 2012 and the financial statements give a true and fair view of the Bank's financial position as at 31 December 2012 and its financial performance and cash flows for the year then ended in accordance with Sri Lanka Accounting Standards.

In our opinion, the consolidated financial statements give a true and fair view of the financial position as at 31 December 2012 and its financial performance and cash flows for the year then ended, in accordance with Sri Lanka Accounting Standards, of the Bank and its subsidiary dealt with thereby, so far as concerns the shareholders of the Bank.

Report on Other Legal and Regulatory Requirements

These financial statements also comply with the requirements of Sections 151(2) and 153(2) to 153(7) of the Companies Act No. 07 of 2007.

(Sgd.)
13 February 2013
Colombo

Partners: A D B Talwatte FCA FCMA M P D Cooray FCA FCMA R N de Saram ACA FCMA Ms. N A De Silva ACA Ms. Y A de Silva FCA W R H Fernando FCA FCMA W K B S P Fernando FCA FCMA A P A Gunasekera FCA FCMA A Herath FCA D K Hulangamuwa FCA FCMA LLB (Lond) H M A Jayesinghe FCA FCMA Ms. A A Ludowyke FCA FCMA Ms. G G S Manatunga ACA N M Sulaiman ACA ACMA B E Wijesuriya ACA ACMA

Income Statement

		BANK			GROUP		
For the year ended 31 December	Note	2012 Rs '000	2011 Rs '000	Change %	2012 Rs '000	2011 Rs '000	Change %
Interest income	2	16,983,637	11,387,683	49	17,149,866	11,654,594	47
Interest expenses	3	11,309,774	6,826,023	66	11,254,042	6,745,376	67
NET INTEREST INCOME		5,673,863	4,561,660	24	5,895,824	4,909,218	20
Net Fee and commission income	4	1,133,603	1,150,401	(1)	1,643,583	1,916,230	(14)
Net trading income/(expenses)	5	1,010,276	568,196	78	1,272,496	448,396	184
Other operating income	6	997,474	427,489	133	6,126,547	647,785	846
Total operating income		8,815,216	6,707,746	31	14,938,450	7,921,629	89
Impairment charges/(reversal) for loans and other losses	7	106,112	67,789	57	51,379	(88,492)	158
Net operating income		8,709,104	6,639,957	31	14,887,071	8,010,121	86
LESS: OPERATING EXPENSES							
Personnel expenses	8	2,172,740	1,838,184	18	2,333,325	2,117,613	10
Depreciation of property, plant & equipment		181,837	178,287	2	205,161	198,556	3
Amortization of intangible assets		82,783	48,328	71	95,786	51,411	86
Other operating costs		1,664,833	1,465,019	14	1,861,926	1,612,976	15
Total operating expenses		4,102,193	3,529,818	16	4,496,198	3,980,556	13
OPERATING PROFIT BEFORE VALUE ADDED TAX (VAT)	9	4,606,911	3,110,139	48	10,390,873	4,029,565	158
Value Added Tax (VAT) on financial services		(622,286)	(504,960)	23	(622,287)	(504,960)	23
OPERATING PROFIT AFTER VALUE ADDED TAX (VAT)		3,984,625	2,605,179	53	9,768,586	3,524,605	177
Share of associate companies' profit	10	–	–	–	438,720	330,793	33
PROFIT BEFORE TAXATION		3,984,625	2,605,179	53	10,207,306	3,855,398	165
Taxation	11	(1,060,667)	(774,361)	37	(1,275,367)	(1,092,517)	17
PROFIT FOR THE YEAR		2,923,958	1,830,818	60	8,931,939	2,762,881	223
PROFIT ATTRIBUTABLE TO EQUITY HOLDERS OF THE PARENT		2,923,958	1,830,818	60	8,853,821	2,527,473	250
Non-Controlling Interests		–	–	–	78,118	235,408	(67)
		2,923,958	1,830,818	60	8,931,939	2,762,881	223
Earnings per share (in Rs)	12	17.81	11.15	–	55.31	15.79	–
Dividend per share (in Rs)	13	5.00	7.50	–	–	–	–

Significant Accounting Policies and Notes to the Financial Statements disclosed on pages 233 to 318 are an integral part of these Financial Statements.

13 February 2013

Statement of Comprehensive Income

	BANK			GROUP		
For the year ended 31 December	**2012 Rs '000**	2011 Rs '000	Change %	**2012 Rs '000**	2011 Rs '000	Change %
Profit for the year	**2,923,958**	1,830,818	60	**8,931,939**	2,762,881	223
Total other comprehensive income/(expenses)	**–**	–	–	**–**	–	–
Total comprehensive income for the year	**2,923,958**	1,830,818	60	**8,931,939**	2,762,881	223
ATTRIBUTABLE TO:						
Equity holders of the parent	**2,923,958**	1,830,818	60	**8,853,821**	2,527,473	250
Non-controlling interests	**–**	–	–	**78,118**	235,408	(67)
	2,923,958	1,830,818	60	**8,931,939**	2,762,881	223

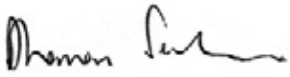
Statement of Financial Position

		BANK				GROUP			
As at 31 December	Note	**2012 Rs '000**	2011 Rs '000	Change %	As at 1 January 2011 Rs '000	**2012 Rs '000**	2011 Rs '000	Change %	As at 1 January 2011 Rs '000
ASSETS									
Cash and cash equivalents	14	**3,480,395**	2,395,152	45	2,224,459	**3,634,983**	2,518,840	44	2,508,470
Balances with Central Bank	15	**6,074,792**	4,614,170	32	3,077,406	**6,074,792**	4,614,170	32	3,077,406
Placements with banks	16	**3,559,354**	517,833	587	–	**3,559,354**	517,833	587	–
Securities purchased under resale agreements	20	**3,324,868**	911,709	265	2,154,637	**3,324,868**	911,709	265	2,154,637
Financial assets held for trading	17	**982,967**	7,106,148	(86)	7,961,585	**982,967**	7,106,148	(86)	8,186,934
Derivative financial instruments	18	**1,706,372**	1,402,305	22	140,565	**1,706,372**	1,402,305	22	140,565
Other financial assets held for trading	19	**–**	233,771	(100)	368,650	**10,411,658**	2,086,525	399	1,851,984
Loans and advances to banks	21	**1,183,343**	1,640,462	(28)	1,816,744	**1,183,343**	1,640,462	(28)	1,816,744
Loans and advances to customers	22	**109,602,523**	93,094,783	18	65,011,952	**109,649,198**	93,166,027	18	65,044,918
Lease rentals receivables	24	**6,389,837**	4,649,610	37	2,412,200	**6,389,837**	4,649,610	37	2,412,200
Other financial assets classified as loans and receivable	25	**3,121,163**	1,255,099	149	7,926,285	**3,764,025**	2,563,186	47	9,178,507
Financial assets - held to maturity	26	**19,257,271**	15,566,201	24	7,273,278	**19,223,228**	15,666,201	23	7,679,622
Financial assets - available for sale	27	**66,714**	88,648	(25)	4,790	**173,541**	186,475	(7)	6,774
Investments in subsidiary companies	28	**2,641,178**	2,770,540	(5)	2,770,540	**–**	–	–	–
Investments in associate companies	29	**18,525**	286,898	(94)	452,460	**33,301**	1,796,695	(98)	1,762,589
Other assets	30	**936,485**	782,002	20	492,296	**1,154,688**	962,764	20	690,990
Intangible assets	31	**272,314**	278,633	(2)	206,720	**318,723**	318,347	–	210,300
Property, plant & equipment	32	**856,195**	828,754	3	650,433	**1,222,500**	1,185,259	3	707,727
Investment properties	33	**–**	–	–	–	**1,295,693**	1,295,693	–	1,200,000
Goodwill									4,330
Total assets		**163,474,296**	138,422,718	18	104,945,000	**174,103,071**	142,588,249	22	108,634,697
LIABILITIES									
Due to Banks	34	**2,319,984**	5,923,527	(61)	570,385	**2,319,984**	5,923,527	(61)	570,385
Securities sold under repurchase agreements	20	**12,515,861**	11,360,101	10	12,351,199	**12,515,861**	10,132,841	24	11,474,836
Derivative financial instruments	18	**1,736,838**	1,022,462	70	–	**1,736,838**	1,022,462	70	–
Due to customers	35	**107,600,583**	82,094,320	31	60,532,985	**107,393,866**	82,094,320	31	60,532,985
Debt securities issued and other borrowed funds	36	**17,841,963**	19,466,302	(8)	13,960,910	**17,802,038**	19,466,303	(9)	13,960,910
Tax liabilities		**656,211**	304,662	115	452,497	**633,838**	355,976	78	573,416
Other liabilities	37	**3,525,882**	3,106,318	14	2,668,372	**3,657,375**	3,285,805	11	2,824,765
Subordinated term debts	38	**2,254,699**	2,428,012	(7)	2,625,243	**2,254,699**	2,428,012	(7)	2,625,243
Deferred Tax	39	**79,874**	41,875	91	59,256	**79,120**	41,122	92	59,753
Total liabilities		**148,531,895**	125,747,579	18	93,220,847	**148,393,619**	124,750,368	19	92,622,293

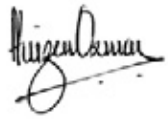
Statement of Financial Position

		BANK				GROUP			
As at 31 December	Note	**2012 Rs '000**	2011 Rs '000	Change %	As at 1 January 2011 Rs '000	**2012 Rs '000**	2011 Rs '000	Change %	As at 1 January 2011 Rs '000
EQUITY ATTRIBUTABLE TO EQUITY HOLDERS OF PARENT									
Stated capital	40	**1,093,095**	1,093,095	–	1,093,095	**863,937**	863,937	–	863,937
Statutory reserve fund	41	**878,718**	878,718	–	878,718	**878,718**	878,718	–	878,718
Investment Fund	42	**924,333**	386,825	139	–	**924,333**	386,825	139	–
Retained Earnings	43	**12,046,255**	10,316,501	17	9,752,340	**22,216,055**	14,795,649	50	13,552,666
		14,942,401	12,675,139	18	11,724,153	**24,883,042**	16,925,129	47	15,295,321
Non-controlling interests		**–**	–	–	–	**826,410**	912,752	(9)	717,083
Total equity		**14,942,401**	12,675,139	18	11,724,153	**25,709,452**	17,837,881	44	16,012,404
Total liabilities and total equity		**163,474,296**	138,422,718	18	104,945,000	**174,103,071**	142,588,249	22	108,634,697
Commitments and contingencies	49	**158,740,820**	145,667,380	9	95,704,093	**158,740,820**	145,667,380	9	95,704,093

These Financial Statements are in compliance with the requirements of the Companies Act No. 07 of 2007.

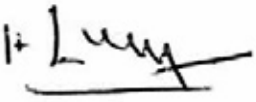


D Senathirajah
Vice-President - Finance & Planning



Faizan Ozman
Chief Financial Officer

The Board of Directors is responsible for the preparation and presentation of these Financial Statements.
Signed for and on behalf of the Board.



H D S Amarasuriya
Chairman

N I R De Mel
Chief Executive Officer

S A Ranasinghe
Company Secretary

13 February 2013

Significant Accounting Policies and Notes to the Financial Statements disclosed on pages 233 to 318 are an integral part of these Financial Statements.

Statement of Changes in Equity

	Attributable to Equity Holders of the Parent						
For the year ended 31 December	Stated Capital	Statutory Reserve Fund	General Reserve	Investment Fund	Retained Profit	Non-Controlling Interests	Total
	Rs '000	Rs '000	Rs '000	Rs '000	Rs '000	Rs '000	Rs '000
BANK							
Balance as at 1 January 2011	1,093,095	878,718	5,805,707	–	3,946,633	–	11,724,153
Profit for the year	–	–	–	–	1,830,818	–	1,830,818
Transfer to Investment fund	–	–	–	386,825	(386,825)	–	–
Dividends paid	–	–	–	–	(879,832)	–	(879,832)
Balance as at 31 December 2011	1,093,095	878,718	5,805,707	386,825	4,510,794	–	12,675,139
Balance as at 1 January 2012	1,093,095	878,718	5,805,707	386,825	4,510,794	–	12,675,139
Profit for the year	–	–	–	–	2,923,958	–	2,923,958
Transfer to investment fund	–	–	–	537,507	(537,507)	–	–
Dividends paid	–	–	–	–	(656,696)	–	(656,696)
Balance as at 31 December 2012	**1,093,095**	**878,718**	**5,805,707**	**924,332**	**6,240,549**	**–**	**14,942,401**
GROUP							
Balance as at 1 January 2011	1,093,095	878,718	5,805,707	–	7,620,922	717,083	16,115,525
Adjustment for Employee Share Ownership Plan (ESOP)	(229,158)	–	–	–	126,037	–	(103,121)
Balance as at 1 January 2011 restated	863,937	878,718	5,805,707	–	7,746,959	717,083	16,012,404
Exchange gain from valuation of foreign associate	–	–	–	–	(17,832)	(1,988)	(19,820)
Transfer to investment fund	–	–	–	386,825	(386,825)	–	–
Profit for the year	–	–	–	–	2,527,473	235,408	2,762,881
Dividends paid	–	–	–	–	(879,833)	(37,751)	(917,584)
Balance as at 31 December 2011	863,937	878,718	5,805,707	386,825	8,989,942	912,752	17,837,881
Balance as at 1 January 2012	863,937	878,718	5,805,707	386,825	8,989,942	912,752	17,837,881
Exchange gain from valuation of foreign associate	–	–	–	–	18,824	2,960	21,784
Transfer to Investment Fund	–	–	–	537,507	(537,507)	–	–
Effect of change in the holding in group companies	–	–	–	–	(258,037)	(130,086)	(388,123)
Profit for the year	–	–	–	–	8,853,821	78,118	8,931,939
Dividends paid	–	–	–	–	(656,696)	(37,333)	(694,029)
Balance as at 31 December 2012	**863,937**	**878,718**	**5,805,707**	**924,332**	**16,410,347**	**826,411**	**25,709,452**

Cash Flow Statement

		BANK		GROUP	
For the year ended 31 December	Note	2012 Rs '000	2011 Rs '000	2012 Rs '000	2011 Rs '000
Cash flows from operating activities					
Interest received		16,317,018	11,391,173	16,568,884	11,572,159
Fee-based income received		2,387,630	1,156,265	2,538,084	1,680,745
Dividend income received		126,648	311,124	162,855	132,595
Other income received		312,746	980,565	651,633	1,446,844
Interest paid		(9,918,252)	(6,215,430)	(9,917,401)	(6,215,430)
Personnel costs paid		(876,337)	(1,704,905)	(1,031,225)	(1,958,117)
General expenses paid		(2,721,155)	(1,506,478)	(2,910,189)	(1,827,087)
Operating profit before changes in operating assets and liabilities	a	5,628,298	4,412,314	6,062,641	4,831,709
Net increase in loans and advances		(17,298,517)	(30,164,965)	(17,298,517)	(30,164,965)
Net increase in deposits from customers		24,739,780	20,946,521	24,739,780	20,946,521
Net (increase)/decrease in other receivables		341,737	(784,843)	339,100	(680,499)
Net increase/(decrease) in other liabilities		63,941	207,653	(41,960)	174,920
Net cash inflow/(outflow) from operating activities before taxation		13,475,249	(5,383,320)	13,801,044	(4,892,314)
Financial Services VAT paid		(569,106)	(578,869)	(569,106)	(578,869)
Income taxes paid		(671,119)	(939,576)	(832,895)	(1,075,328)
Net cash provided by/(used in) operating activities		12,235,014	(6,901,765)	12,399,043	(6,546,511)
Cash flows from investing activities					
Net increase in investments -					
Government treasury bills and bonds		(2,064,075)	453,245	(2,064,075)	452,718
Disposal of subsidiaries/associates		884,951	–	7,654,287	–
Change in other investments		192,500	45,558	(6,620,816)	(408,461)
Securities sold under repurchase agreements		1,105,367	(931,621)	1,105,366	(833,656)
Net due to/(from) related companies		256	(17,872)	256	(17,872)
Expenditure on property and equipment		(295,273)	(476,801)	(325,078)	(525,150)
Proceeds from sale of property and equipment		22,111	17,959	23,278	18,594
Net cash used in investing activities		(154,163)	(909,532)	(226,780)	(1,313,827)
Cash flows from financing activities					
(Decrease)/Increase in borrowings		(5,330,589)	10,601,672	(5,330,589)	10,619,505
Dividend paid		(1,162,876)	(575,246)	(1,223,388)	(661,174)
Net cash provided by/(used in) financing activities		(6,493,465)	10,026,426	(6,553,977)	9,958,331
Net increase/(decrease) in cash and cash equivalents		5,587,386	2,215,129	5,618,286	2,097,993
Cash and cash equivalents at the beginning of the year		7,527,155	5,312,026	7,650,843	5,552,850
Cash and cash equivalents at the end of the year	b	13,114,541	7,527,155	13,269,129	7,650,843

Cash Flow Statement

	BANK		GROUP	
For the year ended 31 December	**2012 Rs '000**	2011 Rs '000	**2012 Rs '000**	2011 Rs '000
Note a				
Reconciliation of Operating profit				
Profit before taxation	**4,606,912**	3,110,139	**10,390,872**	4,029,564
Add/(less)				
Accrued interest on loans and advances	**(667,925)**	2,964	**(667,925)**	2,964
Accrued interest on interest rate swap	**1,306**	48,543	**1,306**	48,543
Accrued interest on deposits & borrowings	**1,391,522**	610,593	**1,391,522**	610,593
Profit on disposal of fixed assets	**(12,384)**	(17,807)	**(12,384)**	(17,807)
Depreciation of property, plant & equipment	**264,620**	226,615	**300,947**	249,966
(Gain)/loss on mark to market valuation on shares	**(51,427)**	74,787	**(51,427)**	194,589
Capital (gain)/loss on sale of shares	**(575,649)**	8,076	**(5,790,875)**	8,076
Sales proceeds on sale of shares	**325,130**	188,799	**579,881**	107,853
Accrued general expenses	**220,026**	71,761	**(150,710)**	65,805
Provision for investment	**48,500**	165,562	**(6,233)**	9,281
Impairment of financial assets	**57,612**	(97,773)	**57,612**	(97,773)
Deferment of equity linked compensation plan	**20,055**	20,055	**20,055**	20,055
Change in the fair value of investment property	**–**	–	**–**	(400,000)
Operating profit before changes in operating assets and liabilities	**5,628,298**	4,412,314	**6,062,641**	4,831,709
Note b				
Reconciliation of cash and cash equivalents				
Cash and short-term funds	**7,039,749**	2,912,985	**7,194,337**	3,036,673
Balances with Central Bank	**6,074,792**	4,614,170	**6,074,792**	4,614,170
	13,114,541	7,527,155	**13,269,129**	7,650,843

Significant Accounting Policies and Notes to the Financial Statements disclosed on pages 233 to 318 are an integral part of these Financial Statements.

Significant Accounting Policies

1. Corporate Information

National Development Bank PLC together with its subsidiaries provides retail, corporate banking and investment banking services. National Development Bank is the Ultimate Parent of the Group.

National Development Bank PLC is a listed limited liability company incorporated and domiciled in Sri Lanka. Its registered office is at No. 40, Navam Mawatha, Colombo 2, Sri Lanka.

The Financial Statements of National Development Bank PLC for the year ended 31 December 2012 was authorized for issue in accordance with a resolution of the Board of Directors on 13 February 2013.

2. Accounting Policies

2.1 Basis of Preparation

For all periods up to and including the year ended 31 December 2011, the Bank and the Group prepared its Financial Statements in accordance with Sri Lanka Accounting Standards effective as at 31 December 2011. These Financial Statements for the year ended 31 December 2012 represents first time adoption of Sri Lanka Accounting Standards comprising SLFRS/LKAS effective 1 January 2012. Accordingly, the NDB Group has prepared Financial Statements which comply with SLFRS/LKAS applicable for periods ending on or after 1 January 2012, together with the comparative period data as at and for the year ended 31 December 2011, as described in the Accounting Policies. In preparing these Financial Statements, the Group's opening statement of financial position was prepared as at 1 January 2011, the Group's date of transition to SLFRS. Refer Note 2.5 on page 257 for information on how the Group adopted SLFRS.

The Consolidated Financial Statements have been prepared on a historical cost basis, except for the following material items in the Statement of Financial Position:

- Investment properties which are measured at fair value
- Available for sale Financial Assets which are measured at fair value
- Derivative financial instruments which are measured at fair value
- Other financial assets and liabilities held for trading which are measured at fair value
- Financial assets and liabilities designated at fair value through profit or loss which are measured at fair value

2.1.1 Functional and Presentation Currency

The Consolidated Financial Statements are presented in Sri Lankan Rupees and all values are rounded to the nearest thousand Rupees, except when otherwise indicated.

2.1.2 Statement of Compliance

The Statement of Financial Position, Statement of Comprehensive Income, Statement of Changes in Equity and Statement of Cash Flows together with Accounting Policies and Notes, (Financial Statements), i.e., Consolidated Financial Statements of NDB Group as at 31 December 2012 and for the year then ended, have been prepared in accordance with Sri Lanka Accounting Standards (SLFRS) issued by The Institute of Chartered Accountants of Sri Lanka. The preparation and presentation of these Financial Statements are in compliance of the Companies Act No. 07 of 2007. The presentation of these Financial Statements are also in compliance with the requirements of Banking Act No. 30 of 1988 and amendments thereto.

2.1.3 Presentation of Financial Statements

The Bank and the Group present its Statement of Financial Position broadly in order of liquidity. The contractual maturities of the assets and liabilities of the Bank is presented in Note 48 to the Financial Statements.

2.1.4 Materiality and Aggregation

In compliance with LKAS 01 on Presentation of Financial Statements, each material class of similar items is presented separately in the Financial Statements. Items of dissimilar nature or functions are presented separately, unless they are immaterial.

Financial assets and financial liabilities are offset and the net amount reported in the Consolidated Statement of Financial Position only when there is a legally enforceable right to offset the recognized amounts and there is an intention to settle on a net basis, or to realize the assets and settle the liability simultaneously.

Income and expenses are not offset in the Consolidated Income Statement unless required or permitted by any accounting standard or interpretation, and as specifically disclosed in the Accounting Policies of the Bank.

Basis of Consolidation

The Consolidated Financial Statements comprise the Financial Statements of the Bank and its subsidiaries for the year ended 31 December 2012. The Financial Statements of National Development Bank PLC's subsidiaries are prepared for the same reporting year as National Development Bank PLC , using consistent Accounting Policies.

All intra-group balances, income and expenses and unrealised gains and losses resulting from intra-group transactions are eliminated in full in preparing the Consolidated Financial Statements.

Subsidiaries are fully-consolidated from the date on which control is transferred to the Bank. Control is achieved where the Bank has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities.

Non-controlling interests represent the portion of profit or loss and net assets of subsidiaries not owned, directly or indirectly, by the Bank.

Non-controlling interests are presented separately in the Consolidated Income Statement and within equity in the Consolidated Statement of Financial Position, but separate from Parent shareholders' equity. Any losses applicable to the non-controlling interests are allocated against the interests of the non-controlling interest even if this results in a deficit balance. Acquisitions of non-controlling interests are accounted for using the Parent entity extension method, whereby the difference between the consideration and the fair value of the share of the net assets acquired is recognized as equity.

2.2 Significant Accounting Judgments, Estimates and Assumptions

In the process of applying Group Accounting Policies, management is required to make judgments, which may have significant effects on the amounts recognized in the Financial Statements. Further, management is also required to consider key assumptions concerning the future and other key sources of estimation uncertainty at the Balance Sheet date that have significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year. The key significant accounting judgments, estimates and assumptions involving uncertainty are discussed below, whereas the respective carrying amounts of such assets and liabilities are as given in related Notes.

2.2.1 Judgments

Taxation

The Group is subject to income taxes and other taxes including VAT on financial services. Significant judgement is required to determine the total provision for current, deferred and other taxes pending the issue of tax guidelines on the treatment of the adoption of SLFRS in the Financial Statements and the taxable profit for the purpose of imposition of taxes. Uncertainties exist, with respect to the interpretation of the applicability of tax laws, at the time of the preparation of these financial statements. The Group recognized assets and liabilities for current, deferred and other taxes based on estimates of whether additional taxes will be due. Where the final tax outcome of these matters is different from the amounts that were initially recorded, such differences will impact the income, deferred and tax amounts in the period in which the determination is made.

2.2.2 Estimates and Assumptions

Going Concern

The Board of Directors of the Bank has made an assessment of its ability to continue as a going concern and is satisfied that it has the resources to continue in business for the foreseeable future. Furthermore, Board of Directors is not aware of any material uncertainties that may cast significant doubt upon the Bank's ability to continue as a going concern. Therefore, the Financial Statements continue to be prepared on the going concern basis.

Fair Value of Financial Instruments

Where the fair values of financial assets and financial liabilities recorded on the Statement of Financial Position cannot be derived from active markets, they are determined using a variety of valuation techniques that include the use of mathematical models. The inputs to these models are derived from observable market data where possible, but if this is not available, judgment is required to establish fair values.

Impairment losses on Loans and Advances

The Bank and the Group review their individually-significant loans and advances at each statement-of-financial-position date to assess whether an impairment loss should be recorded in the Income Statement. In particular, management's judgment is required in the estimation of the amount and timing of future cash flows when determining the impairment loss. These estimates are based on assumptions about a number of factors and actual results may differ, resulting in future changes to the allowance.

Loans and advances that have been assessed individually and found not to be impaired are assessed together with all individually insignificant loans and advances in groups of assets with similar risk characteristics. This is to determine whether provision should be made due to incurred loss events for which there is objective evidence, but the effects of which are not yet evident. The collective assessment takes account of data from the loan portfolio such as loan ownership type, levels of arrears, industries etc. and judgements on the effect of concentrations of risks and economic data (including levels of unemployment, Inflation rate, interest rates, exchange rates). The impairment loss on loans and advances is disclosed in more detail in Note 22 and Note 24.

Impairment of Available for Sale Investments

The Group reviews its debt securities classified as available for sale investments at each reporting date to assess whether they are impaired. This requires similar judgment as applied to the individual assessment of loans and advances.

The Bank also records impairment charges on available for sale equity investments when there has been a significant or prolonged decline in the fair value below their cost. The determination of what is 'significant' or 'prolonged' requires judgment. In making this judgment, the Bank evaluates, among other factors, historical share price movements and duration and extent to which the fair value of an investment is less than its cost.

Deferred Tax Assets

Deferred tax assets are recognized for all deductible temporary differences and unused tax losses where applicable, to the extent that it is probable that taxable profit will be available against which such items can be deducted in the future. Significant management judgment is required to determine the amount of deferred tax assets that can be recognized, based upon the likely timing and level of future taxable profits together with future tax planning strategies.

Defined Benefit Plans

The cost of the defined benefit plans (gratuity and pension plan) is determined using an actuarial valuation. The actuarial valuation involves making various assumptions which may differ from actual developments in the future. These include the determination of discount rates, expected rates of return on assets, future salary increases, mortality rates and future pension increases. Due to the long-term nature of these plans, such estimates are subject to significant uncertainty. All assumptions are reviewed at each reporting date. The assumptions used to arrive in defined benefit obligation reported in Financial Statements are disclosed in Note 37.1.

Distinction Between Investment Properties and Owner-Occupied Properties

The NDB Group determines whether a property qualifies as investment property by considering whether the property generates cash flows largely independently of the other assets held by the entity. Owner-occupied properties generate cash flows that are attributable not only to property but also to other assets used in the production or supply process.

Some properties comprise a portion that is held to earn rentals or for capital appreciation and another portion that is held for use in the production or supply of goods or services or for administrative purposes. If these portions can be sold separately (or leased out separately under a finance lease), Group accounts for the portions separately. If the portions cannot be sold separately, the property is accounted for as investment property only if an insignificant portion is held for use in the production or supply of goods or services or for administrative purposes. Group considers each property separately in making its judgment.

2.3 Summary of Significant Accounting Policies

2.3.1 Financial Instruments - Initial Recognition and Subsequent Measurement

(a) Date of Recognition

All financial assets and liabilities are initially recognized on the trade date, i.e., the date that the Group becomes a party to the contractual provisions of the instrument. This includes purchases or sales of financial assets that require delivery of assets within the time frame generally established by regulation or convention in the market place.

(b) Initial Measurement of Financial Instruments

The classification of financial instruments at initial recognition depends on their purpose and characteristics and the management's intention in acquiring them. All financial instruments are measured initially at their fair value plus transaction costs, except in the case of financial assets and financial liabilities recorded at fair value through profit or loss.

(c) Derivatives Recorded at Fair Value through Profit or Loss

The Group uses derivatives such as interest rate swaps, forward foreign exchange contracts and options on interest rates. Derivatives are recorded at fair value and carried as assets when their fair value is positive and as liabilities when their fair value is negative. Changes in the fair value of derivatives are included in 'Net trading income'.

(d) Financial Assets held for Trading

Financial assets held for trading are recorded in the Statement of Financial Position at fair value. Changes in fair value are recognized in 'Net trading income'. Interest and dividend income or expense is recorded in 'Net trading income' according to the terms of the contract, or when the right to the payment has been established.

Included in this classification are debt securities, equities that have been acquired principally for the purpose of selling or repurchasing in the near term.

(e) Available for Sale Financial Investments

Available for sale investments include equity and debt securities. Equity investments classified as available for sale are those which are neither classified as held for trading nor designated at fair value through profit or loss.

Debt securities in this category are intended to be held for an indefinite period of time and may be sold in response to needs for liquidity or in response to changes in the market conditions.

The Group has not designated any loans or receivables as available-for-sale. After initial measurement, available-for-sale financial investments are subsequently measured at fair value.

Unrealized gains and losses are recognized directly in equity (Other comprehensive income) in the 'Available for sale reserve'. When the investment is disposed of, the cumulative gain or loss previously recognized in equity is recognized in the Income Statement in 'Other operating income'. Where the Group holds more than one investment in the same security, they are deemed to be disposed of on a first-in-first-out basis. Interest earned whilst holding available for sale financial investments is reported as interest income using the Effective Interest Rate (EIR).

Dividends earned whilst holding available for sale financial investments are recognized in the Income Statement as 'Other operating income' when the right of the payment has been established. The losses arising from impairment of such investments are recognized in the Income Statement in 'Impairment losses on financial investments' and removed from the 'Available for sale reserve'.

(f) Held to Maturity Financial Investments

Held to maturity financial investments are non-derivative financial assets with fixed or determinable payments and fixed maturities, which the Group has the intention and ability to hold to maturity. After initial measurement, held-to-maturity financial investments are subsequently measured at amortized cost using the EIR, less impairment. Amortized cost is calculated by taking into account any discount or premium on acquisition and fees that are an integral part of the EIR.
The amortization is included in 'Interest and similar income' in the Income Statement.

If the Group were to sell or reclassify more than an insignificant amount of held to maturity investments before maturity (other than in certain specific circumstances), the entire category would be tainted and would have to be reclassified as available for sale. Furthermore, the Bank would be prohibited from classifying any financial asset as held-to-maturity during the following two years.

(g) Financial Assets classified as Loans and Receivables

Financial Assets classified as Loans and Receivables includes non-derivative financial assets with fixed or determinable payments that are not quoted in an active market, other than:

- Those that the Group intends to sell immediately or in the near term and those that the Group, upon initial recognition, designates as at fair value through profit or loss
- Those that the Group, upon initial recognition, designates as available for sale
- Those for which the Group may not recover substantially all of its initial investment, other than because of credit deterioration

After initial measurement, amounts 'Due from banks' and 'Loans and advances to customers' are subsequently measured at amortized cost using the EIR, less allowance for impairment. Amortized cost is calculated by taking into account any discount or premium on acquisition and fees and costs that are an integral part of the EIR. The amortization is included in 'Interest and similar income' in the Income Statement. The losses arising from impairment are recognized in the Income Statement in 'Credit loss expense'.

(h) 'Day 1' Difference for Staff Loans

All staff loans granted at below market interest rates were recognized at fair value. The difference between the fair value and the amount disbursed were treated as day 1 difference and amortized as staff cost over the loan period by using effective interest rate. The staff loans were subsequently measured at amortized costs.

(i) Other Financial Liabilities

Financial instruments issued by the Bank that are not designated at fair value through profit or loss, are classified as other financial liabilities, where the substance of the contractual arrangement results in the Bank having an obligation either to deliver cash or another financial asset to the holder, or to satisfy the obligation other than by the exchange of a fixed amount of cash or another financial asset for a fixed number of own equity shares.

Other financial Liabilities include, deposits from customers, amount due to banks, borrowings from bank and others and debentures.

After initial measurement, other financial liabilities are subsequently measured at amortized cost using the EIR. Amortized cost is calculated by taking into account any discount or premium on the issue and costs that are an integral part of the EIR.

2.3.2 Derecognition of Financial Assets and Financial Liabilities

(a) Financial assets

A financial asset (or, where applicable a part of a financial asset or part of a group of similar financial assets) is derecognized when -

- The rights to receive cash flows from the asset have expired,
- The Group has transferred its rights to receive cash flows from the asset or has assumed an obligation to pay the received cash flows in full without material delay to a third party under a 'pass-through' arrangement; and either,
- The Group has transferred substantially all the risks and rewards of the asset, or
- The Group has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset.

When the Group has transferred its rights to receive cash flows from an asset or has entered into a pass-through arrangement, and has neither transferred nor retained substantially all of the risks and rewards of the asset nor transferred control of the asset, the asset is recognized to the extent of the Group's continuing involvement in the asset. In that case, the Group also recognizes an associated liability. The transferred asset and the associated liability are measured on a basis that reflects the rights and obligations that the Group has retained. Continuing involvement that takes the form of a guarantee over the transferred asset is measured at the lower of the original carrying amount of the asset and the maximum amount of consideration that the Bank could be required to repay.

(b) Financial liabilities

A financial liability is derecognized when the obligation under the liability is discharged or cancelled or expires. Where an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is treated as a derecognition of the original liability and the recognition of a new liability. The difference between the carrying value of the original financial liability and the consideration paid is recognized in profit or loss.

2.3.3 Securities Purchased Under Reverse Repurchase Agreements

Securities sold under agreements to repurchase at a specified future date are not derecognized from the Statement of Financial Position as the Bank retains substantially all of the risks and rewards of ownership. The corresponding cash received is recognized in the Consolidated Statement of Financial Position as an asset with a corresponding obligation to return it, including accrued interest as a liability within 'securities purchased under Repurchase Agreements', reflecting the transaction's economic substance as a loan to the Bank. The difference between the sale and repurchase prices is treated as interest expense and is accrued over the life of agreement using the EIR.

2.3.4 Securities Sold Under Repurchase Agreements

Securities purchased under agreements to resell at a specified future date are not recognized in the Statement of Financial Position. The consideration paid, including accrued interest, is recorded in the Statement of Financial Position, within 'securities sold under Repurchase Agreements', reflecting the transaction's economic substance as a loan by the Bank. The difference between the repurchase and resale prices is recorded in 'Net Interest income' and is accrued over the life of the agreement using the EIR.

2.3.5 Determination of Fair Value of Financial Instruments

The fair value for financial instruments traded in active markets at the reporting date is based on their quoted market price without any deduction for transaction costs.

For all other financial instruments not traded in an active market, the fair value is determined by using appropriate valuation techniques. Valuation techniques include the discounted cash flow method, comparison with similar instruments for which market observable prices exist, options pricing models, credit models and other relevant valuation models.

Certain financial instruments are recorded at fair value using valuation techniques in which current market transactions or observable market data are not available. Their fair value is determined using a valuation model that has been tested against prices or inputs to actual market transactions and using the Bank's best estimate of the most appropriate model assumptions.

An analysis of fair values of financial instruments and further details as to how they are measured are provided in Note 45.

2.3.6 Impairment of Financial Assets

(a) Loans and advances

Losses for impaired loans are recognized promptly when there is objective evidence that impairment of a loan or portfolio of loans has occurred. Impairment allowances are calculated on individual loans and on groups of loans assessed collectively. Impairment losses are recorded as charges to the Income Statement. The carrying amount of impaired loans on the Balance Sheet is reduced through the use of impairment allowance accounts. Losses expected from future events are not recognized.

Individually assessed loans and advances

For all loans that are considered individually significant, the Bank assesses on a case-by-case basis at each Balance Sheet date whether there is any objective evidence that a loan is impaired. The criteria used to determine that there is such objective evidence include:

- known cash flow difficulties experienced by the borrower;
- past due contractual payments of either principal or interest;
- breach of loan covenants or conditions;
- the probability that the borrower will enter bankruptcy or other financial realisation; and
- a significant downgrading in credit rating by an external credit rating agency.

For those loans where objective evidence of impairment exists, impairment losses are determined considering the following factors:

- Bank's aggregate exposure to the customer;
- the viability of the customer's business model and their capacity to trade successfully out of financial difficulties and generate sufficient cash flow to service debt obligations;
- the amount and timing of expected receipts and recoveries;
- the extent of other creditors' commitments ranking ahead of, or *pari passu* with, the Bank and the likelihood of other creditors continuing to support the Bank;
- the complexity of determining the aggregate amount and ranking of all creditor claims and the extent to which legal and insurance uncertainties are evident;
- the realisable value of security (or other credit mitigants) and likelihood of successful repossession;
- the likely deduction of any costs involved in recovery of amounts outstanding;
- the ability of the borrower to obtain, and make payments in, the currency of the loan if not denominated in local currency

Impairment losses are calculated by discounting the expected future cash flows of a loan at its original effective interest rate and comparing the resultant present value with the loan's current carrying amount. The impairment allowances on individually significant accounts are reviewed more regularly when circumstances require. This normally encompasses reassessment of the enforceability of any collateral held and the timing and amount of actual and anticipated receipts. Individually assessed impairment allowances are only released when there is reasonable and objective evidence of a reduction in the established loss estimate.

Collectively assessed loans and advances

Impairment is assessed on a collective basis in two circumstances:

- To cover losses which have been incurred but have not yet been identified on loans subject to individual assessment; and
- For homogeneous groups of loans that are not considered individually significant.

Incurred but not yet identified impairment

Individually assessed loans for which no evidence of loss has been specifically identified on an individual basis are grouped together according to their credit risk characteristics for the purpose of calculating an estimated collective loss. This reflects impairment losses that the Bank has incurred as a result of events occurring before the date of the Statement of Financial Position, which the Bank and the Group are not able to identify on an individual loan basis, and that can be reliably estimated. These losses will only be individually identified in the future. As soon as information becomes available which identifies losses on individual loans within the Group, those loans are removed from the Group and assessed on an individual basis for impairment.

The collective impairment allowance is determined after taking into account:

- historical loss experience in portfolios of similar credit risk; and
- management's experienced judgment as to whether current economic and credit conditions are such that the actual level of inherent losses at the date of the Statement of Financial Position is likely to be greater or less than that suggested by historical experience.

Homogeneous groups of loans and advances

Statistical methods are used to determine impairment losses on a collective basis for homogeneous groups of loans. Losses in these groups of loans are recorded on an individual basis when individual loans are written off, at which point they are removed from the group.

Two alternative methods are used to calculate historical loss experience on a collective basis:

- *When the group of loan by nature long term, the Group uses probability of default method*
  Under this methodology the movement in number of customers into non-performing categories over the periods are used to estimate the amount of loans that will eventually be written off as a result of the events occurring before the date of the Statement of Financial Position which the group is not able to identify on an individual loan basis, and that can be reliably estimated.
- *When the group of loan by nature short term, the Bank uses net flow rate method*
  Under this methodology the movement in the outstanding balance of customers into different age categories over the periods are used to estimate the amount of loans that will eventually be written off as a result of the events occurring before the date of the Statement of Financial Position which the group is not able to identify on an individual loan basis, and that can be reliably estimated.

Under both methodologies, loans are grouped into ranges according to the number of days in arrears and statistical analysis is used to estimate the likelihood that loans in each range will progress through the various stages of delinquency, and ultimately prove irrecoverable.

Current economic conditions and portfolio risk factors are also evaluated when calculating the appropriate level of allowance required to cover inherent loss.

These additional macro and portfolio risk factors may include:

- recent loan portfolio growth and product mix,
- unemployment rates, Gross Domestic Production (GDP) growth, inflation
- exchange rates, interest rates
- changes in Government laws and regulations

Write-off of loans and advances

Loans (and the related impairment allowance accounts) are normally written off, either partially or in full, when there is no realistic prospect of recovery. Where loans are secured, this is generally after receipt of any proceeds from the realization of security.

Reversals of impairment

If the amount of an impairment loss decreases in a subsequent period, and the decrease can be related objectively to an event occurring after the impairment was recognized, the excess is written back by reducing the loan impairment allowance account accordingly. The write back is recognized in the Income Statement.

The Bank assesses at each reporting date, whether there is any objective evidence that a financial asset or a group of financial assets is impaired. A financial asset or a group of financial assets is deemed to be impaired if, and only if, there is objective evidence of impairment as a result of one or more events that have occurred after the initial recognition of the asset (an 'incurred loss event') and that loss event (or events) has an impact on the estimated future cash flows of the financial asset or the group of financial assets that can be reliably estimated.

(b) Financial assets carried at amortized cost

For financial assets carried at amortized cost (such as amounts due from banks, loans and advances to customers as well as held to maturity investments), the Bank first assesses individually whether objective evidence of impairment exists for financial assets that are individually significant, or collectively for financial assets that are not individually significant. If the Bank determines that no objective evidence of impairment exists for an individually assessed financial asset, it includes the asset in a group of financial assets with similar credit risk characteristics and collectively assesses them for impairment. Assets that are individually assessed for impairment and for which an impairment loss is, or continues to be, recognized are not included in a collective assessment of impairment.

If there is objective evidence that an impairment loss has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future expected credit losses that have not yet been incurred). The carrying amount of the asset is reduced through the use of an allowance account and the amount of the loss is recognized in the Income Statement. Interest income continues to be accrued on the reduced carrying amount and is accrued using the rate of interest used to discount the future cash flows for the purpose of measuring the impairment loss. The interest income is recorded as part of 'Interest and similar income'.

Loans together with the associated allowance are written off when there is no realistic prospect of future recovery and all collateral has been realized or has been transferred to the Bank. If, in a subsequent year, the amount of the estimated impairment loss increases or decreases because of an event occurring after the impairment was recognized, the previously recognized impairment loss is increased or reduced by adjusting the allowance account. If a future write-off is later recovered, the recovery is credited to the 'Credit loss expense'.

The present value of the estimated future cash flows is discounted at the financial asset's original EIR. If a loan has a variable interest rate, the discount rate for measuring any impairment loss is the current EIR. The calculation of the present value of the estimated future cash flows of a collateralized financial asset reflects the cash flows that may result from foreclosure less costs for obtaining and selling the collateral, whether or not foreclosure is probable.

For the purpose of a collective evaluation of impairment, financial assets are grouped on the basis of the Bank's internal credit grading system, that considers credit risk characteristics such as asset type, industry, geographical location, collateral type, past-due status and other relevant factors.

Future cash flows on a group of financial assets that are collectively evaluated for impairment are estimated on the basis of historical loss experience for assets with credit risk characteristics similar to those in the group.

Historical loss experience is adjusted on the basis of current observable data to reflect the effects of current conditions on which the historical loss experience is based and to remove the effects of conditions in the historical period that do not exist currently.

Estimates of changes in future cash flows reflect, and are directionally consistent with, changes in related observable data from year to year (such as changes in unemployment rates, property prices, commodity prices, payment status, or other factors that are indicative of incurred losses in the Group and their magnitude). The methodology and assumptions used for estimating future cash flows are reviewed regularly to reduce any differences between loss estimates and actual loss experience.

See Note 7 for details of impairment losses on financial assets carried at amortized cost, Notes 22 and 24 for an analysis of the impairment allowance on loans and advances by class.

(c) Available for sale financial investments

For available for sale financial investments, the Bank assesses at each reporting date whether there is objective evidence that an investment is impaired. In the case of debt instruments classified as available for sale, the Bank assesses individually whether there is objective evidence of impairment based on the same criteria as financial assets carried at amortized cost. However, the amount recorded for impairment is the cumulative loss measured as the difference between the amortized cost and the current fair value, less any impairment loss on that investment previously recognized in the Income Statement. Future interest income is based on the reduced carrying amount and is accrued using the rate of interest used to discount the future cash flows for the purpose of measuring the impairment loss.

The interest income is recorded as part of 'Interest and similar income'. If, in a subsequent period, the fair value of a debt instrument increases and the increase can be objectively related to a credit event occurring after the impairment loss was recognized in the Income Statement, the impairment loss is reversed through the Income Statement.

In the case of equity investments classified as available for sale, objective evidence would also include a 'significant' or 'prolonged' decline in the fair value of the investment below its cost.

(d) Rescheduled loan facilities

Where possible, the Bank seeks to restructure loans rather than to take possession of collateral. This may involve extending the payment arrangements and the agreement of new loan conditions. Once the terms have been renegotiated, any impairment is measured using the original EIR as calculated before the modification of terms and the loan is no longer considered past due. Management continually reviews renegotiated loans to ensure that all criteria are met and that future payments are likely to occur. The loans continue to be subject to an individual or collective impairment assessment, calculated using the loan's original EIR.

(e) Collateral

The Bank seeks to use collateral, where possible, to mitigate its risks on financial assets. The collateral comes in various forms such as cash, securities, letters of credit/guarantees, real estate, receivables, inventories, other non-financial assets and other credit enhancements.

2.3.7 Impairment of Non-Financial Assets Other than Goodwill

NDB Group 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 Group makes an estimate of the asset's recoverable amount. An asset's recoverable amount is the higher of an asset's or cash-generating unit's fair value less costs to sell and its value in use 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.

2.3.8 Offsetting Financial Instruments

Financial assets and financial liabilities are offset and the net amount reported in the Statement of Financial Position if, and only if, there is a currently enforceable legal right to offset the recognized amounts and there is an intention to settle on a net basis, or to realize the asset and settle the liability simultaneously. This is not generally the case with master netting agreements, therefore, the related assets and liabilities are presented gross in the Statement of Financial Position.

2.3.9 Business Combinations and Goodwill

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 (negative goodwill) 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 the 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 or more frequently if events or changes in circumstances indicate that the carrying value may be impaired.

For the purpose of impairment testing, goodwill acquired in a business combination is, from the acquisition date, allocated to each of the 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.

Carrying amount of the goodwill arising on acquisition of subsidiaries is presented as an intangible and the goodwill on an acquisition of an equity accounted investment in investment in associates is included in the carrying value of the investment.

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.

2.3.10 Investment in an Associate

The Group's investment in its associate is accounted for using the equity method. An associate is an entity in which the Group has significant influence. Under the equity method, the investment in the associate is carried on the Statement of Financial Position at cost plus post acquisition changes in the Group's share of net assets of the associate. Goodwill relating to the associate is included in the carrying amount of the investment and is neither amortized nor individually tested for impairment.

The Income Statement reflects the Group's share of the results of operations of the associate. When there has been a change recognized directly in the equity of the associate, the Group recognizes its share of any changes and discloses this, when applicable, in the Statement of Changes in Equity. Unrealized gains and losses resulting from transactions between the Group and the associate are eliminated to the extent of the interest in the associate.

The Group's share of profit of an associate is shown on the face of the Income Statement. This is the profit attributable to equity holders of the associate and, therefore, is profit after tax and non-controlling interests in the subsidiaries of the associate.

The Financial Statements of the associate are prepared for the same reporting period as the Group. When necessary, adjustments are made to bring the Accounting Policies in line with those of the Group.

After application of the equity method, the Group determines whether it is necessary to recognize an additional impairment loss on its investment in its associate. The Group determines at each reporting date whether there is any objective evidence that the investment in the associate is impaired. If this is the case, the Group calculates the amount of impairment as the difference between the recoverable amount of the associate and its carrying value and recognizes the amount in the 'share of profit of an associate' in the Income Statement.

Upon loss of significant influence over the associate, the Group measures and recognizes any retaining investment at its fair value. Any difference between the carrying amount of the associate upon loss of significant influence and the fair value of the retained investment and proceeds from disposal is recognized in profit or loss.

2.3.11 Property, Plant and Equipment

(a) Basis of recognition

Property, plant and equipment are recognised if it is probable that future economic benefits associated with the asset will flow to the Group and the cost of the asset can be reliably measured.

(b) Basis of measurement

An item of Property, Plant and Equipment that qualifies for recognition as an asset is initially measured at its cost. Cost includes expenditure that is directly attributable to the acquisition of the assets and subsequent cost as explained below. The cost of self constructed assets includes the cost of the materials and direct labour, any other cost directly attributable to bringing the assets to a working condition for its intended use and cost of dismantling and removing the old items and restoring site on which they are located. Purchased software which is integral to the functionality of the related equipment is capitalized as part of computer equipment.

(c) Subsequent cost

There are costs that are recognized in the carrying amount of an item if it is probable that the future economic benefits embodied within that part will flow to the Group and it can be reliably measured.

(d) Depreciation

Depreciation is calculated on a straight-line basis over the useful life of the assets, commencing from when the assets are available for use. The estimated useful lives of the assets are as follows:

Buildings/Improvements	20 years - 40 years
Motor vehicles	4 years
Furniture and office equipment	5 years

Depreciation is provided proportionately for the completed number of months the asset is in use, if it is purchased or sold during the financial year.

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

(e) Derecognition

An item of Property, Plant and Equipment is derecognized upon disposal or when no future economic benefits are expected. Any gain or loss arising on derecognition of the asset (calculated as the difference between the net disposal proceeds and the carrying amount of the asset) is included in the Income Statement in the year the asset is derecognized.

2.3.12 Intangible Assets

The Group's intangible assets include the value of computer software and work in progress. An intangible asset is recognized only when its cost can be measured reliably and it is probable that the expected future economic benefits that are attributable to it will flow to the Group.

Intangible assets acquired separately are measured on initial recognition at cost. 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.

Intangible assets are amortized using the straight-line method to write down the cost over its estimated useful economic lives as given below:

Computer software	5 years

Intangible assets are derecognized on disposal or when no future economic benefits are expected. Any gain or loss arising on derecognition of an intangible asset are measured as the difference between the net disposal proceeds and the carrying amount of the asset is included in the Income Statement in the year the asset is derecognized.

2.3.13 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 Statement of Financial Position include total lease payments due net of unearned interest income not accrued to revenue and allowance for impairment.

2.3.14 Investment Property

Properties held to earn rental income and properties held for capital appreciations have been classified as investment property. Investment properties are initially recognized at cost. Subsequent to the initial recognition, the investment properties are stated at fair values, which reflect market conditions at the date of the Statement of Financial Position. Gains or losses arising from changes in the fair values are included in the Income Statement in the year in which they arise.

Cost includes expenditure that is directly attributable to the acquisition of the investment property. The cost of self-constructed investment property includes the cost of materials and direct labour, any other costs directly attributable to bringing the investment property to a working condition for their intended use.

Investment properties are derecognized when disposed of or permanently withdrawn from use because no future economic benefits are expected. Any gains or losses on retirement or disposal are recognized in the Income Statement in the year of retirement or disposal.

An external, independent valuer, having appropriate recognized professional qualifications and recent experience in the location and category of property being valued, values the Group's investment property every 3 years. In financial periods within that period the fair value is determined by the Directors.

2.3.15 Taxation

(a) Domestic Banking Unit and Foreign Currency 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 10 of 2006 and amendments thereto, at the rate of 28% for both on-shore domestic banking unit and on shore foreign currency banking unit transactions (2011 - 28%).

(b) Deferred tax

Deferred tax is provided on temporary differences at the date of the Statement of Financial Position 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 utilized 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 Statement of Financial Position 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 Statement of Financial Position 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.

Deferred income tax assets and liabilities are measured at the tax rates that are expected to apply to the year when the asset is realized or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted at the date of the Statement of Financial Position.

(c) Value Added Tax on financial services

The basis for the computation of value added tax on financial services is the accounting profit before emoluments paid to employees and income tax, which is adjusted for the depreciation computed on prescribed rates. The amount of value added tax charged at 12% in determining the profit for the period is given in the Income Statement.

2.3.16 Financial Guarantees

In the ordinary course of business, the Bank gives financial guarantees, consisting of letters of credit, guarantees and acceptances. Financial guarantees are initially recognized in the Financial Statements (within 'other liabilities') at fair value, being the premium received.

Subsequent to initial recognition, the Bank's liability under each guarantee is measured at the higher of the amount initially recognized less cumulative amortization recognized in the Income Statement, and the best estimate of expenditure required to settle any financial obligation arising as a result of the guarantee.

The premium received is recognized in the Income Statement in 'Net Fees and Commission Income' on a straight line basis over the life of the guarantee.

2.3.17 Pensions and Retirement Benefits

The Bank operates an approved employee non-contributory pension Plan for the payment of pensions to members of its permanent staff who qualify for such payments when retiring. Employees who joined since 1999 are not covered under the said pension scheme. These employees are entitled to retirement gratuity as explained in Note 8 on page 266. Up to 31 December 2002, annual contributions to the pension plan was payable by the 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.

The costs of retirement gratuities are determined by a qualified actuary using projected unit credit method. This item is stated under other liabilities in the Statement of Financial Position. Actuarial gains and losses are recognized as income or expense when the net cumulative unrecognized actuarial gains or losses at the end of the previous reporting period exceeded 10% of the defined benefit obligation at the date and recognized over the expected average working lives of employees participating in the plan of the defined benefit obligation at that date, in accordance with the Corridor Method.

Employees are eligible for Employees' Provident Fund contributions and Employees' Trust Fund contributions in accordance with the respective statutes and regulations. The Bank contributes 15% and 3% of gross salaries of employees to the Bank's Employees' Provident Fund and the Employees' Trust Fund respectively. Group companies contributes 12% and 3% to Central Bank of Sri Lanka for eligible employees for Employees' Provident Fund contributions and Employees' Trust Fund contributions respectively.

2.3.18 Provisions

Provisions are recognized when the Group has a present obligation (legal or constructive) as a result of a past event, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation.

2.3.19 Equity-Linked Compensation Plan

On 1 July 2010, shareholders of the Bank approved an Equity Linked Compensation Plan (ELCP), to enable the management staff in the rank of Assistant Vice-President and above of the Bank to take part in the voting ordinary share capital of the Bank, subject to certain limits, terms and conditions. A total quantum of 2,455,661 shares of the Bank which is equivalent to a maximum of 3% of the present voting share capital of the Bank is to be issued to the ELCP. Half of such shares are to be awarded as share options and the other half as Share Grants in equal proportions. The issue of shares for the ELCP will take place over five years commencing July 2010. Each of the five tranches would amount to a maximum of 0.6% of the voting shares. Subsequent to the subdivision of the Bank's ordinary shares in the proportion of one share for every ordinary share in issue, which was approved at the Annual General Meeting held on 30 March 2011, the total quantum of shares has now increased to 4,911,322 shares.

Details of the Share Options and the Share Grants are given in Note 47 to the Financial Statements.

The cost of equity-settled transactions is recognized, together with a corresponding increase in equity, over the period in which the performance and/or service conditions are fulfilled, ending on the date on which the relevant employees become fully entitled to the award ('the vesting date'). The cumulative expense recognized for equity-settled transactions at each reporting date until the vesting date reflects the extent to which the vesting period has expired and the Bank's best estimate of the number of equity instruments that will ultimately vest.

The Income Statement expense or credit for a period is recorded in 'Personnel expenses' and represents the movement in cumulative expense recognized as at the beginning and end of that period.

2.3.20 Dividends on Ordinary Shares

Dividends on ordinary shares are recognized as a liability and deducted from equity when they are approved by the Board of Directors.

2.3.21 Equity Reserves

The reserves recorded in equity (Other comprehensive income) on the Group's Statement of Financial Position include -

- 'Available for sale' reserve, which comprises changes in fair value of available for sale investments.
- 'Foreign currency translation reserve', which is used to record exchange differences arising from the translation of the net investment in foreign operations.

2.3.22 Foreign Currency Translation

(a) Transactions in foreign currencies are initially recorded using the closing exchange rate of the functional currency ruling at the date of the transaction.

Monetary assets and liabilities denominated in foreign currencies are re-translated at the middle exchange rate of the functional currency ruling at the date of the Statement of Financial Position. 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.

(b) Transactions of the Foreign Currency Banking Unit

These have been recorded in accordance with Note (a) above. Net gains and losses are dealt within the Income Statement.

(c) Forward exchange contracts are valued at the forward market rates prevailing at the date of the Statement of Financial Position. Profits and losses on such transactions are dealt within the Income Statement.

(d) Liabilities in respect of foreign currency borrowings guaranteed by the Government of Sri Lanka are not translated at rates of exchange prevailing at the date of the Statement of Financial Position, 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. The Bank pays a premium to the Government of Sri Lanka for bearing such risk.

(e) As at the reporting date, the assets and liabilities of overseas subsidiaries/associates are translated into the Bank's presentation currency at the rate of exchange ruling at the Statement of Financial Position 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.

(f) 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', respectively.

2.3.23 Recognition of Income and Expenses

Revenue is recognized to the extent that it is probable that the economic benefits will flow to the Group and the revenue can be reliably measured. The following specific recognition criteria must also be met before revenue is recognized:

(a) Interest and similar income and expense

For all financial instruments measured at amortized cost, interest-bearing financial assets classified as available for- sale and financial instruments designated at fair value through profit or loss, interest income or expense is recorded using the EIR. EIR is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument or a shorter period, where appropriate, to the net carrying amount of the financial asset or financial liability. The calculation takes into account all contractual terms of the financial instrument (for example, prepayment options) and includes any fees or incremental costs that are directly attributable to the instrument and are an integral part of the EIR, but not future credit losses.

The carrying amount of the financial asset or financial liability is adjusted if the Group revises its estimates of payments or receipts. The adjusted carrying amount is calculated based on the original EIR and the change in carrying amount is recorded as 'Interest and similar income' for financial assets and Interest and similar expense for financial liabilities.

Once the recorded value of a financial asset or a group of similar financial assets has been reduced due to an impairment loss, interest income continues to be recognized using the rate of interest used to discount the future cash flows for the purpose of measuring the impairment loss.

(b) Dividend income

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

(c) Income from fee-based activities

Fees for underwriting, advisory work, loan syndication, management of funds and all other fees and commissions are recognized on an accrual basis. Fees charged on guarantee/bid bonds are recognized on an accrual basis over the period the service is performed.

(d) Net trading income

Results arising from trading activities include all gains and losses from changes in fair value and related interest income or expense and dividends for financial assets and financial liabilities held for trading.

(e) Expenditure recognition

Operating 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 and Equipment in a state of efficiency has been charged to income in arriving at the profit for the year.

2.3.24 Cash and Cash Equivalents

Cash and cash equivalents comprise of cash balances, short-term funds and balances with Central Bank of Sri Lanka. The cash flow statement has been prepared by using 'The Direct Method', whereby gross cash receipts and gross cash payments of operating activities, investing and financing activities have been recognized.

2.3.25 Segment Reporting

A segment is a distinguishable component of the NDB Group that is engaged in providing services (Business Segment) or in providing services within a particular economic environment (Geographical Segment) which is subject to risks and rewards that are different from those of other segments.

In accordance with the Sri Lanka Accounting Standard No. 28 on Segment Reporting, segmental information is presented in respect of the NDB Group. The NDB Group's segmental reporting is based on the following operating segments: Banking, Investment Banking, Property Development, and Others. Segment results, assets and liabilities include items directly attributable to a segment, as well as those that can be allocated on a reasonable basis.

Inter-segment transactions are accounted for at fair market prices charged to inter-bank counterparts for similar services. Such transfers are eliminated on consolidation.

2.4 Standards Issued But Not Yet Effective

Standards issued but not yet effective up to the date of issuance of the Consolidated Financial Statements are set out below along with details of SLFRS which will have a future effect on the Accounting Policies adopted by the Group.

(i) SLFRS 9 - Financial Instruments: Classification and Measurement

SLFRS 9, as issued reflects the first phase of work on replacement of LKAS 39 and applies to classification and measurement of financial assets and liabilities.

(ii) SLFRS 13 - Fair Value Measurement

SLFRS 13 establishes a single source of guidance under SLFRS for all fair value measurements. SLFRS 13 provides guidance on all fair value measurements under SLFRS.

SLFRS 9 and SLFRS 13 will be effective for financial periods beginning on or after 1 January 2015 and 2014 respectively.

In addition to the above, following standards have also been issued and will be effective for financial periods beginning on or after 01 January 2014.

SLFRS 10 - Consolidated Financial Statements
SLFRS 11 - Joint Arrangements
SLFRS 12 - Disclosure of Interests in Other Entities

The Group will adopt these standards when they become effective. Pending a detailed review, the financial impact is not reasonably estimable as at the date of publication of these Financial Statements.

2.5 First-Time Adoption of SLFRSs and LKASs

The Group adopted Sri Lanka Accounting Standards comprising LKAS and SLFRS effective 1 January 2012. Prior to the adoption of SLFRS, the Group prepared it's Consolidated Financial Statements in accordance with previous Sri Lanka Accounting Standards. The Group prepared its opening SLFRS Consolidated Financial Statements as at 1 January 2011, the date of transition to SLFRS which forms the starting point for the group's financial reporting under SLFRS. These Consolidated Financial Statements have been prepared in accordance with the Accounting Policies described in Note 2 on page 233.

In preparing these Consolidated Financial Statements, the Group has applied the requirements of SLFRS1 - First-time adoption of Sri Lanka Accounting Standards, including retrospective application of SLFRS effective for the Group on adoption, unless otherwise indicated. The resulting adjustments are described below.

First-Time Adoption of SLFRS

Reconciliation of Equity as at 1 January 2011 (Date of transition to SLFRS)

		BANK				GROUP			
	Note	SLAS* Rs '000	Reclassifi-cation Rs '000	Remeasure-ments Rs '000	SLFRS as at** 1 January 2011 Rs '000	SLAS* Rs '000	Reclassifi-cation Rs '000	Remeasure-ments Rs '000	SLFRS as at** 1 January 2011 Rs '000
ASSETS									
Cash and cash equivalents		2,191,431	33,028	–	2,224,459	2,475,443	33,028	–	2,508,471
Balances with Central Bank		3,077,406	–	–	3,077,406	3,077,406	–	–	3,077,406
Securities purchased under resale agreement	A	1,984,200	169,204	1,233	2,154,637	2,085,264	68,140	1,233	2,154,637
Financial assets held for trading		7,782,587	179,525	(526)	7,961,585	8,007,936	179,525	(525)	8,186,935
Derivative financial instruments	B	–	90,715	49,849	140,565	–	90,715	49,849	140,565
Other financial assets held for trading		368,650	–	–	368,650	832,427	1,019,557	–	1,851,984
Bills of exchange		3,266,461	(3,266,461)	–	–	3,266,461	(3,266,461)	–	–
Loans and advances to banks		–	1,816,744	–	1,816,744	–	1,816,744	–	1,816,744
Loans and advances to customers	D	63,813,641	1,449,717	(251,406)	65,011,952	64,837,507	458,815	(251,405)	65,044,917
Lease rentals receivable		2,326,989	–	85,211	2,412,200	2,326,989	–	85,211	2,412,200
Other financial assets classified as loans and receivable		–	7,926,285	–	7,926,285	–	9,178,507	–	9,178,507
Financial assets - held to maturity	C	15,222,142	(7,948,864)	–	7,273,278	16,740,026	(9,060,404)	–	7,679,622
Financial assets - available for sale		–	4,790	–	4,790	–	6,774	–	6,774
Investments in subsidiary companies		2,770,540	–	–	2,770,540	–	–	–	–
Investments in associate companies		452,460	–	–	452,460	1,762,589	–	–	1,762,589
Other assets	E	625,256	(454,683)	321,723	492,296	997,327	(628,060)	321,722	690,989
Intangible assets		206,720	–	–	206,720	210,299	–	–	210,299
Property, plant & equipment		650,433	–	–	650,433	707,727	–	–	707,727
Investment properties		–	–	–	–	1,200,000	–	–	1,200,000
Goodwill		–	–	–	–	4,330	–	–	4,330
Total assets		104,738,916	–	206,084	104,945,000	108,531,731	(103,120)	206,085	108,634,697

** Based on Sri Lanka Accounting Standards ('SLAS') at 1 January 2011 (Date of transition).*

***Based on Sri Lanka Accounting Standards comprising LKAS and SLFRS ('SLFRS') at 1 January 2011 (Date of transition).*

		BANK				GROUP			
	Note	SLAS* Rs '000	Reclassifi-cation Rs '000	Remeasure-ments Rs '000	SLFRS as at** 1 January 2011 Rs '000	SLAS* Rs '000	Reclassifi-cation Rs '000	Remeasure-ments Rs '000	SLFRS as at** 1 January 2011 Rs '000
LIABILITIES									
Due to Banks		–	570,385	–	570,385	–	570,385	–	570,385
Securities sold under repurchase agreements	F	12,174,293	176,906	–	12,351,199	12,174,293	(699,457)	–	11,474,836
Due to customers	G	59,363,660	1,223,604	(54,279)	60,532,985	59,363,660	1,223,603	(54,278)	60,532,985
Debt securities issued and other borrowed funds		16,937,822	(2,976,912)	–	13,960,910	16,061,460	(2,100,550)	–	13,960,910
Tax liabilities	J	361,370		91,127	452,497	482,289	–	91,127	573,416
Other liabilities		3,784,732	(1,168,431)	52,073	2,668,374	3,941,122	(1,168,431)	52,074	2,824,765
Dividends payable		450,793	(450,793)	–	–	450,793	(450,794)	–	–
Subordinated term debts		–	2,625,243	–	2,625,243	–	2,625,243	–	2,625,243
Deferred Tax	J	59,256	–	–	59,256	59,753	–	–	59,753
Total liabilities		93,131,926	–	88,921	93,220,847	92,533,369	–	88,923	92,622,293
EQUITY ATTRIBUTABLE TO EQUITY HOLDERS OF PARENT									
Stated capital		1,093,095	–	–	1,093,095	1,093,095	(229,158)	–	863,937
Statutory reserve fund		878,718	–	–	878,718	878,718	–	–	878,718
Retained Earnings	H	9,635,177	–	117,163	9,752,340	13,309,466	126,038	117,163	13,552,666
		11,606,990	–	117,163	11,724,153	15,281,279	(103,120)	117,163	15,295,321
Non-controlling interests		–	–	–	–	717,083	–	–	717,083
Total equity		11,606,990	–	117,163	11,724,153	15,998,362	(103,120)	117,163	16,012,404
Total liabilities and equity		104,738,916	–	206,084	104,945,000	108,531,731	(103,120)	206,086	108,634,697

** Based on Sri Lanka Accounting Standards ('SLAS') at 1 January 2011 (Date of transition).*

***Based on Sri Lanka Accounting Standards comprising LKAS and SLFRS ('SLFRS') at 1 January 2011 (Date of transition).*

First-Time Adoption of SLFRS

Reconciliation of Equity as at 31 December 2011

		BANK				GROUP			
	Note	SLAS* Rs '000	Reclassifi-cation Rs '000	Remeasure-ments Rs '000	SLFRS as at** 31 December 2011 Rs '000	SLAS* Rs '000	Reclassifi-cation Rs '000	Remeasure-ments Rs '000	SLFRS as at** 31 December 2011 Rs '000
ASSETS									
Cash and cash equivalents		3,225,999	(830,847)	–	2,395,152	3,349,687	(830,847)	–	2,518,840
Balances with Central Bank		4,614,170	–	–	4,614,170	4,614,170	–	–	4,614,170
Placements with banks		–	517,833	–	517,833	–	517,833	–	517,833
Securities purchased under resale agreement	A	911,709	–	–	911,709	911,709	–	–	911,709
Financial assets held for trading		7,058,269	47,879		7,106,148	7,058,269	47,879	–	7,106,148
Derivative financial instruments	B	–	1,400,999	1,306	1,402,305	–	1,400,999	1,306	1,402,305
Other financial assets held for trading		233,771	–	–	233,771	543,809	1,542,716	–	2,086,525
Bills of exchange		3,824,828	(3,824,828)	–	–	3,824,828	(3,824,828)	–	–
Loans and advances to banks		–	1,640,462	–	1,640,462	–	1,640,462	–	1,640,462
Loans and advances to customers	D	91,510,422	2,184,366	(600,004)	93,094,783	92,678,865	1,087,166	(600,004)	93,166,026
Lease rentals receivable		4,508,959	–	140,651	4,649,610	4,508,959	–	140,651	4,649,610
Other financial assets classified as loans and receivable		–	1,252,104	2,994	1,255,099	–	2,560,191	2,994	2,563,186
Financial assets - held to maturity	C	16,383,363	(817,161)	–	15,566,202	18,168,909	(2,502,708)	–	15,666,201
Financial assets - available for sale		–	88,648	–	88,648	–	186,475	–	186,475
Investments in subsidiary companies		2,770,540	–	–	2,770,540	–	–	–	–
Investments in associate companies		286,898	–	–	286,898	1,796,695	–	–	1,796,695
Other assets	E	1,406,665	(1,011,030)	386,367	782,002	1,853,741	(1,277,343)	386,366	962,764
Intangible assets		278,633	–	–	278,633	318,347	–	–	318,347
Property, plant & equipment		828,754	–	–	828,754	1,185,259	–	–	1,185,259
Investment property		–	–	–	–	1,295,693	–	–	1,295,693
Total assets		137,842,980	648,425	(68,687)	138,422,718	142,108,940	547,995	(68,687)	142,588,249

** Based on Sri Lanka Accounting Standards ('SLAS') at 31 December 2011.*

***Based on Sri Lanka Accounting Standards comprising LKAS and SLFRS ('SLFRS') at 31 December 2011.*

		BANK				GROUP			
	Note	SLAS* Rs '000	Reclassifi-cation Rs '000	Remeasure-ments Rs '000	SLFRS as at** 31 December 2011 Rs '000	SLAS* Rs '000	Reclassifi-cation Rs '000	Remeasure-ments Rs '000	SLFRS as at** 31 December 2011 Rs '000
LIABILITIES									
Due to Banks		–	5,923,527	–	5,923,527	–	5,923,527	–	5,923,527
Securities sold under repurchase agreements	F	11,242,671	117,430	–	11,360,101	11,242,671	(1,109,830)	–	10,132,841
Derivative financial instruments	B	–	1,022,462	–	1,022,462	–	1,022,462	–	1,022,462
Due to customers	G	80,310,181	1,862,355	(78,216)	82,094,320	80,310,181	1,862,355	(78,216)	82,094,321
Debt securities issued and other borrowed funds		27,913,530	(8,447,229)	–	19,466,302	26,686,271	(7,219,968)	–	19,466,303
Tax liabilities	J	213,535	–	91,127	304,662	264,849	–	91,127	355,976
Other liabilities		4,557,003	(1,502,751)	52,066	3,106,318	4,736,410	(1,502,671)	52,066	3,285,805
Dividends payable		755,381	(755,381)	–	–	755,381	(755,381)	–	–
Subordinated term debts		–	2,428,012	–	2,428,012	–	2,428,012	–	2,428,012
Deferred Tax	J	112,108	–	(70,233)	41,875	111,353	–	(70,231)	41,122
Total liabilities		125,104,410	648,425	(5,256)	125,747,579	124,107,117	648,507	(5,256)	124,750,368
EQUITY ATTRIBUTABLE TO EQUITY HOLDERS OF PARENT									
Stated capital		1,093,095	–	–	1,093,095	1,093,095	(229,158)	–	863,937
Statutory reserve fund		878,718	–	–	878,718	878,718	–	–	878,718
Investment Fund		386,825	–		386,825	386,825	–	–	386,825
Retained Earnings	H	10,379,932	–	(63,431)	10,316,501	14,730,509	128,577	(63,437)	14,795,649
		12,738,570	–	(63,431)	12,675,139	17,089,147	(100,581)	(63,437)	16,925,129
Non-controlling interests		–	–	–	–	912,675	76	–	912,752
Total equity		12,738,570	–	(63,431)	12,675,139	18,001,823	(100,506)	(63,437)	17,837,881
Total liabilities and equity		137,842,980	648,425	(68,687)	138,422,718	142,108,940	547,995	(68,687)	142,588,249

** Based on Sri Lanka Accounting Standards ('SLAS') at 31 December 2011.*

***Based on Sri Lanka Accounting Standards comprising LKAS and SLFRS ('SLFRS') at 31 December 2011.*

Significant Accounting Policies

First-Time Adoption of SLFRS

Reconciliation of Income for the year ended 31 December 2011

		BANK				GROUP			
	Note	SLAS* Rs '000	Reclassifi–cation Rs '000	Remeasure–ments Rs '000	31 December 2011** Rs '000	SLAS* Rs '000	Reclassifi–cation Rs '000	Remeasure–ments Rs '000	31 December 2011** Rs '000
Interest income	C & D	11,337,032	–	50,651	11,387,683	11,541,126	62,176	51,292	11,654,594
Interest expenses	G	6,849,961	–	(23,937)	6,826,023	6,769,314	–	(23,938)	6,745,376
NET INTEREST INCOME		4,487,071	–	74,589	4,561,660	4,771,812	62,176	75,230	4,909,218
Net fee and commission income		–	1,150,401	–	1,150,401	–	1,916,227	–	1,916,230
Net trading income/(expenses)	B	–	616,214	(48,017)	568,196	–	496,414	(48,017)	448,396
Other operating income	D	2,194,098	(1,766,610)	–	427,489	3,157,621	(2,510,999)	1,158	647,785
Total operating income		6,681,169	–	26,572	6,707,746	7,929,433	(36,182)	28,371	7,921,629
Impairment charges/(Reversal) for loans and other losses		(160,727)	–	228,516	67,789	(317,008)	–	228,516	(88,492)
Net operating income		6,841,896	–	(201,944)	6,639,957	8,246,441	(36,182)	(200,145)	8,010,121
LESS: OPERATING EXPENSES									
Personnel expenses	D	1,704,906	84,389	48,889	1,838,184	1,976,398	91,166	50,049	2,117,612
Staff retirement benefits		84,389	(84,389)	–	–	91,166	(91,166)	–	–
Depreciation of property plant & equipment		–	178,287	–	178,287	–	198,556	–	198,556
Amortization of intangible assets		–	48,328	–	48,328	–	51,411	–	51,411
Other operating costs	E	1,691,634	(226,615)	–	1,465,019	1,901,099	(286,149)	(1,974)	1,612,976
Total operating expenses		3,480,929	–	48,889	3,529,818	3,968,663	(36,182)	48,075	3,980,556
OPERATING PROFIT BEFORE VALUE ADDED TAX (VAT)		3,360,967	–	(250,833)	3,110,139	4,277,778	–	(248,220)	4,029,565
Value Added Tax (VAT) on Financial Services	J	–	(504,960)	–	(504,960)	–	(504,960)	–	(504,960)
OPERATING PROFIT AFTER VALUE ADDED TAX (VAT)		3,360,967	(504,960)	(250,833)	2,605,179	4,277,778	(504,960)	(248,220)	3,524,605
Share of associate companies' profit		–	–	–	–	330,793	–	–	330,793
PROFIT BEFORE TAXATION		3,360,967	(504,960)	(250,833)	2,605,179	4,608,571	(504,960)	(248,220)	3,855,398
Taxation	J	(1,349,554)	504,960	70,233	(774,361)	(1,667,710)	504,960	70,233	(1,092,517)
PROFIT FOR THE YEAR		2,011,413	–	(180,600)	1,830,818	2,940,861	–	(177,987)	2,762,881
PROFIT ATTRIBUTABLE TO EQUITY HOLDERS OF THE PARENT		2,011,413	–	(180,600)	1,830,818	2,705,530	–	(178,064)	2,527,473
Non-Controlling Interests		–	–	–	–	235,331		77	235,408
		2,011,413	–	(180,600)	1,830,818	2,940,861	–	(177,987)	2,762,881
Earnings Per Share									
Basic Earnings Per Share		12.25			11.15	16.48			15.39
Dividend Per Share		7.5							

** Based on Sri Lanka Accounting Standards ('SLAS') at 31 December 2011*

***Based on Sri Lanka Accounting Standards comprising LKAS and SLFRS ('SLFRS') at 31 December 2011*

2.5.1 Notes to the Reconciliation of Equity as at 1 January 2011, 31 December 2011 and Income Statement for the year ended 31 December 2011

(A) Reverse Repurchase Agreements

On adoption of SLRFS, the interest income on reverse repurchase agreements is recognized based on an effective interst rate (EIR) method.

(B) Derivative Financial Instruments

The fair value of derivative instruments is recognized as per the SLFRS on the Statement of Financial Position. That was not recognized under SLAS.

(C) Financial Assets Held to Maturity

Financial assets where the Group has the ability and intention to hold to maturity were classified as held to maturity and measured at amortized cost using effective interest rate method.

(D) Loans and Advances to Customers

Previous SLAS required provision for impairment of receivables to consist of both a specific amount for incurred losses and general amount for expected future losses. SLFRS does not permit recognition of impairment for expected future losses and instead assessed on a collective as well as individual basis, based on objective evidence that there has been an impairment.

Based on SLFRS, all loans granted to staff of the Group at concessionary rates are initially recognized at fair value. Subsequent interest thereon was recognized on EIR. Day 1 difference is treated as pre-paid staff cost and amortized over the remaining tenor of the loan.

(E) Other Assets

SLFRS requires total lease payments under operating leases be recognized as an expense on a straight-line basis over the lease term.

(F) Repurchase Agreements

On adoption of SLFRS, the interest expense on repurchase contracts is recognized based on an EIR method.

(G) Amounts due to Customers

On adoption of SLFRS, the interest expense on amounts due to customers (deposits) is recognized based on an EIR method.

(H) Reserves

The net effect of adoption of SLFRS as of the transition date of 1 January 2011 is recorded through 'Retained Earnings'.

(I) Statement of Cash Flows

The transition from SLAS to SLFRS did not have a material impact on the Statement of Cash Flows.

(J) SLFRS Tax

This represents the effect on taxes arising on adjustments following the adoption of Sri Lanka Accounting Standards. Pending the issue of tax guidelines, such impact on taxes has been assessed based on the currently applicable tax laws and regulations.

Notes to the Financial Statements

1. Incorporation, Principal Activities and Significant Changes in the Group Structure

The National Development Bank of Sri Lanka was incorporated under the National Development Bank of Sri Lanka Act No. 02 of 1979. In 2005, pursuant to the provisions of the National Development Bank of Sri Lanka (Consequential Provisions) Act No. 01 of 2005, a company by the name of 'National Development Bank Limited' 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. 02 of 1979 was repealed except for certain provisions contained therein.

In terms of the new Companies Act No. 07 of 2007, the name of the Bank was changed as 'National Development Bank PLC'. The Bank was re-registered in terms of the new companies regime on 4 July 2007 and was assigned with PQ 27 as the new Registration Number.

The Bank is listed on the Colombo Stock Exchange. The registered office of the Bank and its principal place of business is situated at No. 40, Navam Mawatha, Colombo 2.

The principal activities of the Bank, its subsidiaries and associate companies (NDB), consist of the business of commercial banking, development financing, merchant banking, investment banking, leasing, housing finance, venture capital, stockbroking, wealth management and property investment.

The number of staff employed by NDB as at 31 December 2012 was 1,447 (2011 - 1,357).

The number of branches of NDB as at 31 December 2012 was 69 (2011 - 60).

	BANK		GROUP	
	2012 Rs '000	2011 Rs '000	**2012 Rs '000**	2011 Rs '000
2. Interest Income				
Loans and advances - due from banks	**105,400**	131,370	**105,400**	131,370
Loans and advances to customers	**13,227,224**	8,467,524	**13,231,487**	8,471,053
Lease rentals receivables	**819,472**	489,580	**819,472**	489,580
Money market lending	**309,346**	120,021	**337,064**	171,451
Reverse repurchase agreements	**252,473**	22,980	**252,473**	22,980
Financial investments held for trading	**107,238**	139,685	**214,210**	292,236
Financial investments held for maturity	**1,399,424**	1,962,122	**1,399,424**	1,972,868
Other Interest income from Government Securities	**763,060**	54,401	**790,336**	103,056
	16,983,637	11,387,683	**17,149,866**	11,654,594
3. Interest Expenses				
Due to banks	**444,581**	372,459	**444,581**	372,459
Securities lent and repurchase agreements	**1,398,432**	923,460	**1,398,432**	923,460
Due to customers	**7,853,381**	4,227,557	**7,853,381**	4,227,557
Debt issued and other borrowed funds	**1,613,380**	1,302,547	**1,557,648**	1,221,900
	11,309,774	6,826,023	**11,254,042**	6,745,376

	BANK		GROUP	
	2012 Rs '000	2011 Rs '000	2012 Rs '000	2011 Rs '000
4. Net Fee and Commission Income				
Management fees	4,995	7,740	–	–
Fee and commission income - loans & other products	1,128,608	1,142,661	1,643,583	1,916,230
Net fee and commission income	1,133,603	1,150,401	1,643,583	1,916,230
5. Net Trading Income				
Foreign exchange income	976,401	760,123	976,401	760,122
Equities	238	(100,055)	9,099	(219,854)
Debt securities	33,637	(43,855)	286,996	(43,855)
Other interest rate instruments	–	(48,017)	–	(48,017)
	1,010,276	568,196	1,272,496	448,396

'Foreign Exchange' income includes gains and losses from spot and forward contracts and other currency derivatives.

'Equities' Income includes the results of buying and selling, and changes in the fair value of equity securities. 'Debt securities' income includes the results of buying and selling and changes in the fair value of debt securities and debt securities sold short as well as the related interest income and expense. The results of trading money market instruments and interest rate swaps, are recorded under 'Other Interest Rate Instruments'.

	BANK		GROUP	
	2012 Rs '000	2011 Rs '000	2012 Rs '000	2011 Rs '000
6. Other Operating Income				
Dividend income from securities				
- Quoted investments	–	8,837	–	15,352
- Non-quoted investments	30,950	44,875	40,496	116,068
Dividend income from subsidiaries/associates				
- Quoted investments	–	179,194	–	–
- Non-quoted investments	95,699	78,217	–	–
Capital gains from sale of securities	91,122	(110)	91,122	(110)
Capital gains from sale of group investments	535,716	17,300	5,750,942	17,300
Non-trading foreign exchange income	218,830	64,979	218,830	64,979
Revaluation gain on investment properties	–	–	–	400,000
Others	25,157	34,197	25,157	34,196
	997,474	427,489	6,126,547	647,785

	BANK		GROUP	
	2012 Rs '000	2011 Rs '000	2012 Rs '000	2011 Rs '000
7. Impairment Charges/(Reversal) for Loans and Other Losses				
Loans and receivables				
Long-term loans	(96,318)	(448,129)	(96,318)	(448,129)
Medium and short-term loans	43,024	62,561	43,024	62,561
Overdrafts	128,985	355,013	128,985	355,013
Trade finance loans	(65,265)	5,993	(65,265)	5,993
Consumer loans	(25,920)	16,169	(25,920)	16,169
Housing loans	32,826	(21,949)	32,826	(21,949)
Pawning	(26,893)	(753)	(26,894)	(753)
Staff loans	677	(2,012)	677	(2,012)
Leases	66,496	(64,666)	66,496	(64,666)
Investment securities	48,500	165,562	(6,233)	9,281
Total	106,112	67,789	51,379	(88,492)

8. Personnel Expenses				
Remuneration	1,843,769	1,498,315	2,044,332	1,769,808
Contribution to defined benefit plan				
Pension fund (Note 8.1)	22,706	36,304	29,253	43,082
Gratuity (Note 8.2)	40,960	48,084	40,960	48,084
Share based payments	20,054	20,055	20,054	20,055
Others	245,251	235,426	198,726	236,584
Total	2,172,740	1,838,184	2,333,325	2,117,613

8.1 Pension Fund

The 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 refer Accounting Policy 2.3.17.

The amount funded since the inception of the Plan is the amount recognized as an expense over the respective periods. The adequacy of the contributions was reviewed by an actuary as at 31 December 2012.

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, which has been estimated at 12% (2011 - 10%) and the rate of increase in salaries, which have been estimated at 10% (2011 - 9%).

The actuarial experience losses or gains have been recognized in line with the corridor method over the expected future working life of the participants.

Accordingly, the provision made for pension liability was Rs 22.7 mn as at 31 December 2012 (Rs 36.3 mn in 2011)

The Pension Plan is fully funded.

8.2 Gratuity

Provisions for retirement gratuities have been made based on the actuarial valuation carried out as at 31 December 2012. Please refer Note 37 (1) for detailed disclosure and assumptions on the retirement benefit liability.

	BANK		GROUP	
	2012 Rs '000	2011 Rs '000	**2012 Rs '000**	2011 Rs '000
9. Operating Profit Before Value Added Tax				
Status after charging,				
Directors' emoluments	**45,740**	35,952	**46,710**	36,923
Auditors' remuneration	**7,188**	5,903	**8,773**	7,223
Legal expenses	**12,051**	14,753	**13,908**	16,106
Office administration and establishment expenses	**876,351**	764,388	**1,015,955**	868,701
Others	**745,783**	662,446	**798,860**	702,446

		GROUP	
	Percentage Holding 2012/2011	**2012 Rs '000**	2011 Rs '000
10. Share of Associate Companies' Profit/(Loss) before Taxation			
Ayojana Fund (Pvt) Ltd. (under liquidation)	50.00%	**–**	–
Maldives Finance Leasing Co (Pvt) Ltd.	35.00%	**(14,683)**	(125,152)
NDB Venture Investments (Pvt) Ltd. (under liquidation)	50.00%	**–**	4,177
AVIVA NDB Insurance PLC (Note 10.1)	41.14%	**440,000**	430,724
AVIVA NDB Finance Lanka (Pvt) Ltd. (Note 10.1)	41.42%	**13,403**	21,044
		438,720	330,793

10.1 On 27 September 2012, the Bank (NDB) and NDB Capital Holdings PLC entered into a Share Sale and Purchase Agreement with American International Assurance Company Ltd. (AIA) of HongKong to divest the 41.56% shareholding in AVIVA NDB Holdings and 5% of AVIVA NDB Insurance PLC. Accordingly, on 5 December 2012 the divestment of these resulted in a capital gain of Rs 5.8 bn to the NDB Group.

11. Taxation

The components of income tax expense for the years ended 31 December 2012 and 2011 are:

		BANK		GROUP	
	Note	2012 Rs '000	2011 Rs '000	2012 Rs '000	2011 Rs '000
Current tax expenses					
Income tax expense		1,039,602	790,450	1,039,602	790,450
Adjustment in respect of current income tax of prior years		(16,935)	1,294	(16,935)	1,294
		1,022,667	791,744	1,022,667	791,744
Income tax of subsidiary companies		–	–	74,853	146,480
Income tax of associate companies		–	–	139,847	172,928
	a	1,022,667	791,744	1,237,367	1,111,152
Deferred tax expense					
Temporary differences	b	38,000	(17,383)	38,000	(18,635)
Total tax charged to the Income Statement		1,060,667	774,361	1,275,367	1,092,517
Effective tax rate (%)		23	25	12	27

Reconciliation of the total tax expense

(a) Income tax

Profit before tax	4,606,911	3,110,139	10,390,873	4,029,565
Income tax for the period (Accounting profit @ applicable tax rate)	1,289,935	870,838	3,342,894	1,274,867
Tax effect of exempt income	(269,649)	(100,520)	(2,107,123)	(114,908)
Adjustment in respect of current income tax of prior period	(16,935)	1,294	(16,935)	1,294
Add: Tax effects of expenses that are not deductible for tax purposes	606,972	391,951	612,837	391,951
(Less): Tax effects of expenses that are deductible for tax purposes	(625,679)	(490,247)	(632,338)	(490,247)
Tax effect of leasing/tax losses	38,023	118,428	38,032	48,195
Tax expenses for the period	1,022,667	791,744	1,237,367	1,111,152

(b) Deferred tax

The following table shows deferred tax recorded on the statement of financial position in other assets and other liabilities and changes recorded in the income tax expense:

	Deferred Tax Assets 2012	Deferred Tax Liabilities 2012	Income Statement 2012	Deferred Tax Assets 2011	Deferred Tax Liabilities 2011	Income Statement 2011
BANK						
Provisions	(6,991)	–	5,106	(12,097)	–	86,416
Other temporary differences	(208,706)	295,572	32,894	(158,946)	212,918	(103,799)
Total	(215,697)	295,572	38,000	(171,043)	212,918	(17,383)
GROUP						
Provisions	(6,991)	–	5,106	(12,097)	–	86,416
Other temporary differences	(209,783)	295,894	32,894	(160,878)	214,096	(105,051)
Total	(216,774)	295,894	38,000	(172,975)	214,096	(18,635)

12. Earnings Per Share

The basic earnings per share for 2012 and 2011 have been calculated by dividing the profit attributable to ordinary shareholders by the weighted average number of ordinary shares outstanding during the year as required by the Sri Lanka Accounting Standard No. 33 (LKAS. 33) on 'Earnings per Share'.

	BANK		GROUP	
	2012	2011	2012	2011
Amount used as the numerator				
Profit attributed to ordinary shareholders (Rs '000)	2,923,958	1,830,818	8,853,821	2,527,473
Amount used as the denominator				
Ordinary shares in issue for basic EPS calculation	164,201,902	164,201,902	160,068,176	160,068,176
Weighted average number of ordinary shares as at the Balance Sheet date for basic EPS calculation	164,201,902	164,201,902	160,068,176	160,068,176
Weighted average basic earnings per share (Rs)	17.81	11.15	55.31	15.79
Weighted average number of ordinary shares as at the Balance Sheet date for Basic EPS calculation	164,201,902	164,201,902	160,068,176	160,068,176
Effect of outstanding share option scheme	54,847	55,479	54,847	55,479
Number of ordinary shares including share option	164,256,749	164,257,381	160,123,023	160,123,655
Weighted average number of ordinary shares as at the Balance Sheet date for diluted EPS calculation	164,256,749	164,257,381	160,123,023	160,123,655
Weighted average diluted earnings per share (Rs)	17.80	11.15	55.29	15.78

13. Dividends Paid and Proposed

The Bank paid an interim dividend of Rs 5.00 per share for the year ended 31 December 2012. (2011 - Rs. 3.50). A final dividend of Rs 4.00 per share for the year ended 31 December 2011, was paid in 2012.

	BANK			GROUP		
	2012 Rs '000	2011 Rs '000	1 Jan 11 Rs '000	**2012 Rs '000**	2011 Rs '000	1 Jan 11 Rs '000
14. Cash and Cash Equivalents						
Cash in hand	**1,546,788**	1,140,934	241,385	**1,546,864**	1,140,997	241,448
Dues from banks	**1,933,607**	1,254,218	1,983,074	**2,088,119**	1,377,843	2,267,022
	3,480,395	2,395,152	2,224,459	**3,634,983**	2,518,840	2,508,470
15. Balances with Central Bank						
Statutory balances with Central Bank of Sri Lanka	**6,074,792**	4,614,170	3,077,406	**6,074,792**	4,614,170	3,077,406
	6,074,792	4,614,170	3,077,406	**6,074,792**	4,614,170	3,077,406

Balances with Central Bank include the cash balance that is required as per the provisions of Section 93 of the Monetary Law Act. The minimum cash reserve requirement was 8.0% of the rupee deposit liabilities as at 31 December 2012 (8.0% as at 31 December 2011). 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.

	BANK			GROUP		
	2012 Rs '000	2011 Rs '000	1 Jan 11 Rs '000	**2012 Rs '000**	2011 Rs '000	1 Jan 11 Rs '000
16. Placements with Banks						
Placements with Banks	**3,559,354**	517,833	–	**3,559,354**	517,833	–
17. Financial Assets Held for Trading						
Treasury bills	**448,489**	3,105,847	3,404,406	**448,489**	3,105,847	3,629,755
Treasury bonds	**534,478**	4,000,301	4,557,179	**534,478**	4,000,301	4,557,179
	982,967	7,106,148	7,961,585	**982,967**	7,106,148	8,186,934

	BANK & GROUP					
	Financial Assets 2012 Rs '000	**Financial Liabilities 2012 Rs '000**	Financial Assets 2011 Rs '000	Financial Liabilities 2011 Rs '000	Financial Assets 2010 Rs '000	Financial Liabilities 2010 Rs '000
18. Derivative Financial Instruments						
Derivatives Held for Trading						
Interest rate swaps	–	–	1,306	–	–	–
Currency options	–	–	13,901	–	–	–
Forward Foreign Exchange contracts	**1,706,372**	**1,736,838**	1,387,098	1,022,462	140,565	–
	1,706,372	**1,736,838**	1,402,305	1,022,462	140,565	–

	BANK			GROUP		
	2012 Rs '000	2011 Rs '000	2010 Rs '000	**2012 Rs '000**	2011 Rs '000	2010 Rs '000
19. Other Financial Assets Held for Trading						
Equity securities	–	233,771	368,650	**123,717**	543,809	832,427
Investment in unit trusts	–	–	–	**10,287,941**	1,542,716	1,019,557
	–	233,771	368,650	**10,411,658**	2,086,525	1,851,984
20. Repurchase Agreements						
Securities purchased under resale agreements	**3,324,868**	911,709	2,154,637	**3,324,868**	911,709	2,154,637
Securities sold under repurchase agreements	**12,515,861**	11,360,101	12,351,199	**12,515,861**	10,132,841	11,474,836
21. Loans and Advances to Banks						
Gross loans and receivables	**1,183,343**	1,640,462	1,816,744	**1,183,343**	1,640,462	1,816,744
(Less): allowances for impairment losses	–	–	–	–	–	–
Net loans and advances to banks	**1,183,343**	1,640,462	1,816,744	**1,183,343**	1,640,462	1,816,744

Notes to the Financial Statements

	BANK			GROUP		
	2012 Rs '000	2011 Rs '000	2010 Rs '000	2012 Rs '000	2011 Rs '000	2010 Rs '000
22. Loans and Advances to Customers						
Gross loans and receivables (Note 22.1)	**112,475,910**	95,902,772	67,639,422	**112,522,586**	95,974,016	67,672,388
(Less): Allowances for impairment losses (Note 22.4)	**2,873,387**	2,807,989	2,627,470	**2,873,387**	2,807,989	2,627,470
Net loans and advances to customer	**109,602,523**	93,094,783	65,011,952	**109,649,198**	93,166,027	65,044,918
22.1 Loans and advances to customers - by product						
Long-term loans	**21,235,303**	23,951,494	17,376,969	**21,235,303**	23,952,758	17,376,971
Medium and Short-term loans	**20,325,610**	15,290,882	11,138,081	**20,325,610**	15,290,882	11,138,081
Overdrafts	**18,634,753**	14,409,916	8,775,492	**18,634,753**	14,408,653	8,775,492
Trade Finance loans	**31,171,501**	22,331,054	16,564,527	**31,171,501**	22,331,054	16,564,526
Consumer loans	**11,341,513**	11,203,238	7,654,032	**11,341,513**	11,203,238	7,654,032
Housing loans	**4,972,040**	5,134,789	4,497,903	**4,972,040**	5,134,789	4,497,903
Pawning	**4,011,455**	2,873,588	1,122,657	**4,011,455**	2,873,588	1,122,657
Staff loans	**783,735**	707,811	509,761	**830,411**	779,054	542,726
Gross loans and advances	**112,475,910**	95,902,772	67,639,422	**112,522,586**	95,974,016	67,672,388
22.2 Loans and advances to customers - by currency						
Loans and advances - LCY	**84,641,250**	72,713,320	48,538,595	**84,687,926**	72,784,563	48,571,561
Loans and advances - FCY	**27,834,660**	23,189,452	19,100,827	**27,834,660**	23,189,453	19,100,827
	112,475,910	95,902,772	67,639,422	**112,522,586**	95,974,016	67,672,388

22.3. Loans and Advances to Customers - By Industry

	2012		2011		2010	
	Rs mn	%	Rs mn	%	Rs mn	%
Food, beverages and tobacco	**3,868**	**3.4**	9,220	9.6	2,654	3.9
Agriculture, agro-business and fisheries	**16,611**	**14.8**	15,665	16.3	16,521	24.4
Textiles and garments	**11,800**	**10.5**	9,007	9.4	8,500	12.6
Wood and paper products	**1,608**	**1.4**	547	0.6	592	0.9
Leather and plastic products	**2,794**	**2.5**	1,064	1.1	1,327	2.0
Metals, chemicals and engineering	**9,783**	**8.7**	9,061	9.4	8,456	12.5
Hotels and Tourism	**2,080**	**1.8**	753	0.8	361	0.5
Utilities	**2,591**	**2.3**	434	0.5	545	0.8
Construction and Housing Finance	**9,649**	**8.6**	7,812	8.1	4,721	7.0
Services	**17,380**	**15.5**	17,954	18.7	11,004	16.3
Transport	**734**	**0.7**	1,716	1.8	1,678	2.5
Consumer	**32,721**	**29.1**	17,903	18.7	10,725	15.9
Other	**857**	**0.7**	4,767	5.0	555	0.7
	112,476	**100.0**	95,903	100.0	67,639	100.0

22.4 Impairment for Loans and Advances to Customers

	BANK & GROUP								
	Long-term Loans Rs '000	Medium and Short-term Loans Rs '000	Overdrafts Rs '000	Trade Finance Loans Rs '000	Consumer Loans Rs '000	Housing Loans Rs '000	Pawning Rs '000	Staff Loans Rs '000	Total Rs '000
At 1 January 2012	1,041,179	423,704	588,409	457,317	273,052	18,787	72	5,471	2,807,989
Charges for the year (Note 7)	(96,319)	43,024	128,984	(65,264)	(25,920)	30,173	(24,290)	677	(8,885)
Amounts written-off	(48,619)	(12,406)	–	–	–	(127)	–	–	(61,152)
Other movements	34,142	(5,233)	80,451	(32,993)	33,023	(6,070)	32,115		135,435
At 31 December 2012	930,383	449,089	797,844	359,060	280,155	42,763	7,947	6,148	2,873,387
Individual Impairment	245,289	210,753	371,506	148,983	–	–	2,654	–	979,186
Collective Impairment	685,094	238,336	426,338	210,077	280,155	42,763	5,293	6,148	1,894,201
At 31 December 2012	930,383	449,089	797,844	359,060	280,155	42,763	7,947	6,148	2,873,387
Gross amount of loan individually determined to be impaired, before deduction of individually assessed impairment allowance	1,620,989	571,330	500,925	345,773	–	–	47,869	–	3,086,886

	BANK & GROUP								
	Long-term Loans Rs '000	Medium and Short-term Loans Rs '000	Overdrafts Rs '000	Trade Finance Loans Rs '000	Consumer Loans Rs '000	Housing Loans Rs '000	Pawning Rs '000	Staff Loans Rs '000	Total Rs '000
At 1 January 2011	1,279,621	303,938	259,007	558,093	197,567	21,761	–	7,483	2,627,469
Charges for the year	(448,129)	62,561	355,013	5,993	16,169	(21,948)	(753)	(2,012)	(33,106)
Amounts written-off	(6,237)	(10,693)	–	–	–	–	–	–	(16,930)
Other movements	215,924	67,898	(25,611)	(106,769)	59,316	18,974	825	–	230,556
At 31 December 2011	1,041,179	423,704	588,409	457,317	273,052	18,787	72	5,471	2,807,989
Individual Impairment	286,222	213,984	335,269	151,579	–	–	–	–	987,053
Collective Impairment	754,957	209,720	253,140	305,738	273,052	18,787	72	5,471	1,820,936
At 31 December 2011	1,041,179	423,704	588,409	457,317	273,052	18,787	72	5,471	2,807,989
Gross amount of loan individually determined to be impaired, before deduction of individually assessed impairment allowance	630,171	488,599	527,005	1,662,438	–	–	–	–	3,308,213

23. Loans granted by utilizing the Funds in the Investment Fund Account

The above long-term loans include Rs 799 mn of loans disbursed by utilizing the Investment Fund Account Balance.

	Bank & Group								2010
Sector	Interest Rates %	Tenure (Years)	Number of Loans Granted	Total 2012 (Rs. '000)	Interest Rates %	Tenure (Years)	Number of Loans Granted	Total 2011 (Rs. '000)	Total 2010 (Rs. '000)
(a) Cultivation of agriculture/ plantation crops			23	101,927			6	67,302	–
(b) Factory/mills modernization			40	217,966			14	70,248	–
(c) Small and medium enterprises	11.0 - 18 .0	5-6	72	369,092	11.1 - 14.3	5-6	16	142,887	–
(d) Information technology and BPO			1	2,093			1	2,200	–
(e) Education			1	4,250			–	–	–
(g) Construction of hotel			14	104,042			–	–	–
			151	799,370			37	282,637	–

	BANK			GROUP		
	2012 Rs '000	2011 Rs '000	2010 Rs '000	2012 Rs '000	2011 Rs '000	2010 Rs '000
24. Lease Rentals Receivable						
Gross loans and receivables	9,764,885	6,611,411	3,137,682	9,764,885	6,611,411	3,137,682
(Less): Allowance for impairment losses (Note 24.1)	49,735	56,448	16,894	49,734	56,448	16,894
(Less): Unearned income	3,325,314	1,905,353	708,588	3,225,314	1,905,353	708,588
Net loans and receivables	6,389,837	4,649,610	2,412,200	6,389,837	4,649,610	2,412,200

	BANK & GROUP	
	2012 Rs '000	2011 Rs '000
24.1 Allowance for Impairment Losses		
At 01 January	56,448	16,895
Charges for the year (Note 07)	66,496	(64,665)
Amounts written-off	(5,618)	–
Other movement	(67,591)	104,218
At 31 December	49,735	56,448
Individual impairment	–	–
Collective impairment	49,735	56,448
	49,735	56,448
Gross amount of loan individually determined to be impaired, before deduction of individually assessed impairment allowance	19,697	–

	Up to 1 year Rs '000	1 to 5 years Rs '000	More than 5 years Rs '000	Total 2012 Rs '000
24.2 Maturity of Lease Rentals Receivable of the Bank				
Total rentals receivable	845,012	8,644,413	288,343	9,777,768
Interest in suspense	(57,714)	(4,825)	(78)	(62,617)
Unearned income	(86,089)	(3,115,193)	(124,032)	(3,325,314)
Net rentals receivable	701,209	5,524,395	164,233	6,389,837

	BANK			GROUP		
	2012 Rs '000	2011 Rs '000	2010 Rs '000	**2012 Rs '000**	2011 Rs '000	2010 Rs '000
25. Other Financial Assets Classified as Loans and Receivables						
Sri Lanka Development Bonds	**2,981,123**	924,604	559,028	**2,981,123**	924,604	559,028
Redeemable Cumulative Preference Shares	**140,040**	330,495	520,000	**140,040**	375,495	610,000
Investment in Securitization	**–**	–	–	**642,862**	1,263,087	1,162,222
Central Bank Securities	**–**	–	6,847,257	**–**	–	6,847,257
	3,121,163	1,255,099	7,926,285	**3,764,025**	2,563,186	9,178,507
26. Financial Assets - Held to Maturity						
Treasury Bills	**3,476,192**	462,379	2,165,409	**3,500,061**	462,379	2,165,409
Treasury Bonds	**15,781,079**	14,318,987	4,363,763	**15,616,573**	14,318,987	4,670,106
Sovereign Bonds	**–**	784,835	744,106	**–**	784,835	744,107
Debentures	**–**	–	–	**106,594**	100,000	100,000
	19,257,271	15,566,201	7,273,278	**19,223,228**	15,666,201	7,679,622
27. Financial Assets - Available for Sale						
Non quoted ordinary shares	**4,790**	4,790	4,790	**111,617**	102,617	6,774
Investment Fund Account (Note 27.a)	**61,924**	83,858	–	**61,924**	83,858	–
	66,714	88,648	4,790	**173,541**	186,475	6,774

Notes to the Financial Statements

		BANK & GROUP		
		2012		2011
	Maturity Date	Rate of Interest %	Rs '000	Rs '000
27.a Investment Fund Account				
Treasury Bills	Feb.-April 2013	10.5 -13.5	61,924	83,858
			61,924	83,858

	Percentage Holding %	Cost 2012 Rs '000	Directors' Valuation/ Market Value 2012 Rs '000	Percentage Holding %	Cost 2011 Rs '000	Directors' Valuation/ Market Value 2011 Rs '000	Percentage Holding %	Cost 2010 Rs '000	Directors' Valuation/ Market Value 2010 Rs '000
28. Investments in Subsidiary Companies									
NDB Capital Holdings PLC	99.66	2,330,855	19,063,550	99.66	2,330,855	12,149,626	99.66	2,330,855	5,749,391
Development Holdings (Pvt) Ltd.	58.61	228,150	1,072,860	58.61	228,150	1,060,291	58.61	228,150	817,438
NDB Investment Bank Ltd.	–	–	–	100	53,922	287,885	100	53,922	147,650
NDB Stock Brokers (Pvt) Ltd.	–	–	–	100	26,940	297,914	100	26,940	237,661
NDB Capital Ltd.	77.80	130,673	82,216	77.80	130,673	130,673	77.80	130,673	130,673
Less: Provision made for impairment of investments	–	(48,500)	–	–	–	–	–	–	–
		2,641,178	20,218,625		2,770,540	13,926,389		2,770,540	7,082,813

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

28.2 The Directors' valuation of investments in subsidiary companies has been carried out on a net assets basis except for investments in quoted companies, which are at the market value as at the Balance Sheet date.

28.3 As explained in 28.2, NDB Capital Holdings PLC has been valued at the market price as at the Balance Sheet date. The Company's shares are traded and the market price is driven by the non-controlling shareholders of only 0.4%.

28.4 The Bank's 99.6% owned subsidiary Capital Development and Investment Company PLC (CDIC), approved a business plan to position itself as a diversified financial services conglomerate with ultimate exposure to investment banking (both regionally and in Sri Lanka), stock broking, wealth management, private equity investments and the insurance sectors. Accordingly, in March 2012, CDIC acquired full ownership of NDB Investment Bank and 5% holding in AVIVA NDB Insurance PLC which was directly held by the Bank, to compliment its investments in AVIVA NDB Insurance PLC and NDB AVIVA Wealth Management Ltd. Further in April 2012, the shares of the Bank's fully-owned subsidiary NDB Stock Brokers (Private) Ltd. was also transferred to CDIC in line with this business plan. Following this strategic restructuring of the Group's corporate equity holdings, CDIC was relaunched under a new corporate identity named NDB Capital Holdings PLC.

	Percentage Holding %	Cost 2012 Rs '000	Directors' Valuation 2012 Rs '000	Percentage Holding %	Cost 2011 Rs '000	Directors' Valuation 2011 Rs '000	Percentage Holding %	Cost 2010 Rs '000	Directors' Valuation 2010 Rs '000
29. Investments in Associate Companies									
(A) Bank									
Ayojana Fund (Pvt) Ltd. (Under Liquidation)	50	100	–	50	100	–	50	100	–
Maldives Finance Leasing Co. (Pvt) Ltd.	35	165,462	–	35	165,462	–	35	165,462	145,300
NDB Venture Investments (Pvt) Ltd. (Under Liquidation)	50	18,525	33,301	50	18,525	33,301	50	18,525	29,124
AVIVA NDB Insurance PLC	5	–	–	5	268,373	371,100	5	268,373	420,000
Less: Provision made for Impairment of Investments		(165,562)	–		(165,562)	–		–	–
		18,525	33,301		286,898	404,401		452,460	594,424

	Percentage Holding %	As at 01.01.2012 Rs '000	Provisions/ Disposals Rs '000	Exchange Gain on Valuation Rs '000	Profit net of Dividend Received Rs '000	As at 31.12.2012 Rs '000	As at 31.12.2011 Rs '000	As at 31.12.2010 Rs '000
(B) Group								
Maldives Finance Leasing Co. (Pvt) Ltd.	35	–	6,234	8,450	(14,684)	–	–	145,299
NDB Venture Investments (Pvt) Ltd.	50	33,301	–	–	–	33,301	33,301	29,124
AVIVA NDB Insurance PLC	41.14	1,374,393	(1,374,393)	–	–	–	1,374,393	1,197,027
AVIVA NDB Finance Lanka (Pvt) Ltd.	41.41	389,001	(613,712)	–	224,711	–	389,001	391,139
		1,796,695	(1,981,871)	8,450	210,027	33,301	1,796,695	1,762,589

	2012 Rs '000	2011 Rs '000	2010 Rs '000
(C) Summarized Financial Information of the NDB Group's Investment in its Associates			
Total Assets	15,516,824	15,758,076	13,918,595
Total Liabilities	14,112,316	14,338,047	12,541,906
Net Assets	1,404,509	1,420,028	1,376,689
Revenue	4,142,957	4,146,227	6,406,529
Profits	438,720	330,793	294,784

(D) On 27 September 2012, the Bank (NDB) and NDB Capital Holdings PLC entered into a Share Sale and Purchase Agreement with American International Assurance Company Ltd. (AIA) of Hongkong to divest the 41.56% shareholding in AVIVA NDB Holdings and 5% of AVIVA NDB Insurance PLC. Accordingly, on 5 December 2012 the divestment of these resulted in a capital gain of Rs 5.8 bn to the NDB Group.

	BANK			GROUP		
	2012 Rs '000	2011 Rs '000	2010 Rs '000	2012 Rs '000	2011 Rs '000	2010 Rs '000
30. Other Assets						
Sundry Receivables	597,359	544,832	272,163	880,842	794,134	555,332
Payments in Advance	257,820	144,150	114,653	273,846	168,630	135,658
Employee Share Ownership Plan (ESOP)	80,205	91,663	103,121	–	–	–
Group Balance Receivable	1,101	1,357	2,359	–	–	–
	936,485	782,002	492,296	1,154,688	962,764	690,990

The ESOP represents the written down value of the NDB shares paid for by the 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.

	BANK			GROUP		
	2012 Rs '000	2011 Rs '000	2010 Rs '000	2012 Rs '000	2011 Rs '000	2010 Rs '000
31. Intangible Assets						
31.1 Computer Software						
Cost/Valuation						
As at 1 January	598,196	385,141	338,859	641,457	389,185	350,960
Additions during the Year	87,062	213,055	46,282	106,746	252,272	49,690
Transfers/Adjustments	(199,489)	–	–	(199,476)	–	(11,465)
As at 31 December	485,769	598,196	385,141	548,727	641,457	389,185
Depreciation/Amortization						
As at 1 January	329,984	281,656	245,726	333,531	282,120	257,233
Charge for the Year	82,783	48,328	35,930	95,785	51,411	36,352
Transfers/Adjustments	(199,312)	–	–	(199,312)	–	(11,465)
As at 31 December	213,455	329,984	281,656	230,004	333,531	282,120
Written-Down Value						
As at 31 December	272,314	268,212	103,485	318,723	307,926	107,065
31.2 Software Under Development						
Cost/Valuation						
As at 1 January	10,421	103,235	54,250	10,421	103,235	54,250
Additions during the Year	7,935	8,190	50,294	7,935	8,190	50,294
Transfers/Adjustments	(18,356)	(101,004)	(1,309)	(18,356)	(101,004)	(1,309)
As at 31 December	–	10,421	103,235	–	10,421	103,235
Net Book Value of Total Intangible Assets	272,314	278,633	206,720	318,723	318,347	210,300

	Land and Buildings Rs '000	Motor Vehicles Rs '000	Furniture and Equipment Rs '000	Work-in-Progress Rs '000	Total Rs '000
32. Property, Plant & Equipment					
32.1 Bank					
(a) Cost					
Freehold Assets [Note 32.2]					
As at 1 January 2012	743,890	173,742	1,317,188	9,480	2,244,300
Additions during the Year	41,909	50,438	135,765	80,176	308,288
Disposals during the Year	(2,037)	(51,689)	(459,285)	–	(513,011)
Transfers/Adjustments	–	–	–	(89,656)	(89,656)
As at 31 December 2012	783,762	172,491	993,668	–	1,949,921
(b) Depreciation/Amortization					
Freehold Assets					
As at 1 January 2012	352,667	109,459	953,420	–	1,415,546
Charge for the Year	47,255	25,808	108,580	–	181,643
On Disposals	(1,372)	(46,834)	(455,257)	–	(503,463)
As at 31 December 2012	398,550	88,433	606,743	–	1,093,726
Written Down Value as at 31 December 2012 (a) - (b)	**385,212**	**84,058**	**386,925**	–	**856,195**
Written Down Value as at 31 December 2011	391,223	64,283	363,768	9,480	828,754
Written Down Value as at 31 December 2010	377,719	41,164	216,986	14,564	650,433

Location	Extent (Perches)	Cost or Revaluation of Land Rs '000	Buildings (Square Feet)	Cost or Revaluation of Buildings Rs '000	Total Value Rs '000	Accumulated Depreciation Rs '000	Written Down Value Rs '000	As a % of Total Cost
32.2 Freehold Land and Building								
Head Office - Dharmapala Mawatha								
No. 103 A, Dharmapala Mawatha, Colombo 07	20.00	164,857	3,766	20,185	185,042	2,100	182,942	58.2
Head Office - Nawam Mawatha								
No. 40, Nawam Mawatha, Colombo 02	1.43	159	8,842	388,491	388,650	257,230	131,420	41.8
	21.43	165,016	12,608	408,676	573,692	259,330	314,362	100.0
Add: Improvement to Buildings of the Bank Branches					210,070	139,220	70,850	
Written Down Value as at 31 December 2012					783,762	398,550	385,212	

	Land and Buildings Rs '000	Motor Vehicles Rs '000	Furniture and Equipment Rs '000	Work-in-Progress Rs '000	Total Rs '000
32.3 Group					
(a) Cost					
Freehold Assets					
As at 1 January 2012	1,048,247	258,315	1,492,905	(2,159)	2,797,308
Additions during the Year	41,859	28,715	138,695	91,815	301,084
Disposals during the Year	(2,037)	(53,725)	(459,689)	–	(515,451)
Transfers/Adjustments	–	–	–	(89,656)	(89,656)
As at 31 December 2012	1,088,069	233,305	1,171,911	–	2,493,285
(b) Depreciation/Amortization					
Freehold Assets					
As at 1 January 2012	352,677	133,134	1,126,238	–	1,612,049
Charge for the Year	47,245	32,956	84,425	–	164,626
On Disposals	(1,372)	(48,870)	(455,648)	–	(505,890)
As at 31 December 2012	398,550	117,220	755,015	–	1,270,785
Written Down Value as at 31 December 2012 (a) - (b)	**689,519**	**116,085**	**416,896**	**–**	**1,222,500**
Written Down Value as at 31 December 2011	695,570	125,180	366,668	(2,159)	1,185,259
Written Down Value as at 31 December 2010	377,719	64,636	250,808	14,564	707,727

	GROUP		
	2012 Rs '000	2011 Rs '000	2010 Rs '000
33. Investment Properties			
Balance as at 1 January	**1,295,693**	1,200,000	1,200,000
Change in the Fair Value during the Year	**–**	400,000	–
Transferred to Property, Plant & Equipment	**–**	(304,307)	–
Balance as at 31 December	**1,295,693**	1,295,693	1,200,000

The Investment Property is owned by Development Holdings (Pvt) Ltd., a subsidiary of the Bank, whose principal activity is renting out premises for commercial use.

Investment Properties are stated at fair value, which has been determined based on valuations performed by a professional valuer on the basis of an open market value, supported by market evidence.

	BANK			GROUP		
	2012 Rs '000	2011 Rs '000	2010 Rs '000	2012 Rs '000	2011 Rs '000	2010 Rs '000
34. Due to Banks						
Amounts due to Foreign Banks	132,445	48,178	84,982	132,445	48,178	84,982
Money Market Borrowings	2,187,539	5,875,349	485,403	2,187,539	5,875,349	485,403
	2,319,984	5,923,527	570,385	2,319,984	5,923,527	570,385
35. Due to Customers						
Savings Deposits	18,023,160	11,299,306	10,094,596	18,023,160	11,299,306	10,094,596
Time Deposits	81,648,029	63,361,906	42,913,031	81,441,312	63,361,906	42,913,031
Demand Deposits	7,742,146	7,059,107	7,301,268	7,742,146	7,059,107	7,301,268
Margins	143,600	312,007	189,676	143,600	312,007	189,676
Other Deposits	43,648	61,994	34,414	43,648	61,994	34,414
	107,600,583	82,094,320	60,532,985	107,393,866	82,094,320	60,532,985

	2012 Rs '000	2011 Rs '000	2010 Rs '000
36. Debt Securities Issued and Other Borrowed Funds			
(a) Bank			
Government of Sri Lanka Loans under ADB, IDA, KFW and JBIC Credit Lines	7,762,298	9,473,226	10,536,326
Other Government of Sri Lanka Loans	885,011	1,069,800	1,406,924
Foreign Borrowings	2,690,692	3,886,161	1,135,542
Local Borrowings	5,579,551	4,112,797	360,956
Debentures (Note 36.1)	924,411	924,318	521,162
	17,841,963	19,466,302	13,960,910

36.1 Debentures

As at 31 December 2012 debentures consisted of 400,000 unlisted unsecured redeemable debentures of Rs 1,000/- each issued by the Bank in 2011 and of 500,000 debentures issued in 2005 details are given below:

	Interest Payable	Issue Date	Maturity Date	Value as at 31st December		
				2012 Rs '000	2011 Rs '000	2010 Rs '000
Floating Rate Debenture						
2011 - 2016 - 3-month TB rate (gross) +1% p.a.	Quarterly	30.06.2011	30.06.2016	**110,000**	110,000	–
2011 - 2016 - 3-month TB rate (gross) +1% p.a.	Quarterly	18.07.2011	30.06.2016	**50,000**	50,000	–
2011 - 2016 - 3-month TB rate (gross) +1% p.a.	Quarterly	19.07.2011	30.06.2016	**40,000**	40,000	–
2011 - 2016 - 3-month TB rate (gross) +1% p.a.	Quarterly	21.07.2011	30.06.2016	**200,140**	200,213	–
				400,140	400,213	–
Fixed Rate Debenture						
2005 - 2013 - 10.13% p.a.	Semi Annually	23.03.2005	24.01.2013	**524,271**	524,105	521,162
				924,411	924,318	521,162

	2012 Rs '000	2011 Rs '000	2010 Rs '000
(b) Group			
Government of Sri Lanka Loans Under ADB, IDA, KfW and JBIC Credit Lines	**7,762,298**	9,473,226	10,536,326
Other Government of Sri Lanka Loans	**885,011**	1,069,800	1,406,882
Foreign Borrowings	**2,690,692**	3,886,161	1,109,500
Local Borrowings	**5,569,626**	4,142,798	387,040
Non-Quoted Debentures	**894,411**	894,318	521,162
	17,802,038	19,466,303	13,960,910

	BANK			GROUP		
	2012 Rs '000	2011 Rs '000	2010 Rs '000	2012 Rs '000	2011 Rs '000	2010 Rs '000
37. Other Liabilities						
Accrued Expenses	421,203	302,587	290,156	436,911	339,917	345,317
Retirement benefit liability (Note 37.1)	122,192	94,106	55,702	129,850	203,481	98,486
Other liabilities	2,982,487	2,709,625	2,322,514	3,090,614	2,742,407	2,380,962
	3,525,882	3,106,318	2,668,372	3,657,375	3,285,805	2,824,765

37.1 The movement in the retirement benefit liability of Bank is given below:

	2012 Rs '000	2011 Rs '000	2010 Rs '000
Present Value of defined benefit obligation	146,953	131,554	139,879
Outstanding balance of transition (Liability)/Asset	–	(3,840)	(7,682)
Unrecognised net actuarial (Loss) or gain	(24,761)	(33,608)	(76,495)
Retirement benefit liability as at 31 December	122,192	94,106	55,702

(a) Messrs Piyal S Goonethilleke and Associates, a firm of professional actuaries has carried out an independent actuarial valuation of the Defined Benefit Plan - Gratuity and accordingly compatible assumptions have been used in determining the cost of retirement benefits.

(b) The key assumptions used by the Actuary include the following:

	2012	2011	2010
Rate of interest	12%	10%	10%
Rate of salary increase	10%	9%	12%
Retirement age	55-60 years	55-60 years	55-60 years

(c) The transitional liability of Rs 19.2 mn on the adoption of SLAS 16 (Employee Benefits) is expensed on a straight-line basis over five years from the date of adoption.

Notes to the Financial Statements

38. Subordinated Term Debts

						BANK			GROUP		
	Repayment Terms	Issued Date	Maturity Date	Rate of Interest %	Amount FCY	2012 Rs '000	2011 Rs '000	2010 Rs '000	2012 Rs '000	2011 Rs '000	2010 Rs '000
Nederlandse Financierings Maatschappij Voor Ontwikkelingslanden N.V. (FMO)											
FMO Loan 1 -	Semi annually	20 Jan. 2006	1 Oct. 2015	AWPR +5%	EUR 7,500,000	**573,879**	760,699	956,961	**573,879**	760,699	956,961
FMO Loan 11	Semi annually	18 Dec. 2007	15 Oct. 2017	Avg (6 months AWPR, 6 months T Bill rate) + 3%	USD 15,000,000	**1,680,820**	1,667,313	1,668,282	**1,680,820**	1,667,313	1,668,282
						2,254,699	2,428,012	2,625,243	**2,254,699**	2,428,012	2,625,243

	Statement of Financial Position						Income Statement					
	BANK			GROUP			BANK			GROUP		
	2012 Rs '000	2011 Rs '000	2010 Rs '000	2012 Rs '000	2011 Rs '000	2010 Rs '000	2012 Rs '000	2011 Rs '000	2010 Rs '000	2012 Rs '000	2011 Rs '000	2010 Rs '000
39. Deferred Taxation												
Deferred Tax Liabilities												
Accelerated Depreciation for Tax Purposes	**57,013**	40,108	27,731	**57,335**	41,286	31,402	**16,905**	12,378	969	**16,048**	9,884	6,076
Finance Leases	**238,568**	172,810	177,179	**238,568**	172,810	177,179	**65,758**	(4,370)	16,980	**65,758**	(4,369)	16,980
	295,581	212,918	204,910	**295,903**	214,096	208,581	**82,663**	8,008	17,949	**81,806**	5,515	23,056
Deferred Tax Assets												
Defined Benefit Plans	**34,214**	26,350	19,496	**35,290**	28,280	22,671	**(7,864)**	(6,854)	(4,307)	**(7,008)**	(5,611)	(7,481)
C/F loss on leasing business	**104,269**	62,363	27,643	**104,269**	62,363	27,643	**(41,905)**	(34,720)	(11,660)	**(41,905)**	(34,720)	(11,660)
Loss on other operations	**70,233**	70,233	–	**70,233**	70,233	–	**–**	(70,233)	–	**–**	(70,233)	–
Provision for bad and doubtful debts	**6,991**	12,097	98,515	**6,991**	12,098	98,514	**5,106**	86,416	80,580	**5,107**	86,416	80,580
	215,707	171,043	145,654	**216,783**	172,974	148,828	**(44,663)**	(25,391)	64,613	**(43,806)**	(24,148)	61,439
							38,000	(17,383)	82,562	**38,000**	(18,633)	84,495
Net deferred tax liability/(Asset)	**79,874**	41,875	59,256	**79,120**	41,122	59,753						

	2012		2011		2010	
	Number	Value Rs '000	Number	Value Rs '000	Number	Value Rs '000
40. Stated Capital						
40.1 Issued and Fully Paid - Bank						
Balance as at 1 January	**164,201,902**	**1,093,095**	82,100,951	1,093,095	81,855,385	1,032,931
Issue of shares under the Equity Linked Compensation Plan (Note 40.3)	–	–	–	–	245,566	60,164
Subdivision of shares - Scrip Issue (Note 40.4)	–	–	82,100,951	–		
Balance as at 31 December	**164,201,902**	**1,093,095**	164,201,902	1,093,095	82,100,951	1,093,095

	2012		2011		2010	
	Number	Rs '000	Number	Rs '000	Number	Rs '000
40.2 Issued and Fully Paid - Group						
Balance as at 1 January	**160,068,176**	**863,937**	80,034,088	863,937	81,855,385	1,032,931
Issue of shares under the Equity Linked Compensation Plan (Note 40.3)	–	–	–	–	245,566	60,164
Subdivision of Shares (Scrip Issue) (Note 40.4)	–	–	80,034,088	–	–	–
Adjustment on Employee Share Ownership Plan	–	–	–	–	(2,066,863)	(229,158)
Balance as at 31 December	**160,068,176**	**863,937**	160,068,176	863,937	80,034,088	863,937

40.3 Equity Linked Compensation Plan

The Bank obtained approval of the shareholders at an Extra Ordinary General Meeting held in April 2010, to enable the management staff in the rank of Assistant Vice-President and above of the Bank to take part in the voting ordinary share capital of the Bank, subject to certain limits, terms and conditions. Accordingly, the ELCP will create a maximum of 3% of the ordinary voting shares, half of such shares are to be awarded as share options and the other half as share grants in equal proportions. Each of the five tranches would amount to a maximum of 0.6% of the voting shares.

Accordingly, on 6 July 2010, 245,566 shares were issued to the Trustees of the ELCP grant scheme, being the first tranche under the share grant scheme. This share issue resulted in the increase of the stated capital of the Bank from Rs 1,032.9 mn to Rs 1,093.1 mn and the number of shares from 81,855,385 to 82,100,951 during the year 2010.

40.4 Subdivision of Shares (Scrip Issue)

At the Annual General Meeting held on 30 March 2011, the shareholders of the Bank approved to increase the number of existing ordinary shares amounting to 82,100,951 by subdividing the said existing ordinary shares in the proportion of one share for every ordinary share in issue so that the number of ordinary shares representing the Stated Capital of the Bank be increased to 164,201,902. Accordingly, the number of shares as at 31 December 2011 was 164,201,902.

41. Statutory Reserve Fund

The 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 76 (1) and is maintained under Section 20 of the Banking Act No. 30 of 1988.

	BANK			GROUP		
	2012 Rs '000	2011 Rs '000	2010 Rs '000	**2012 Rs '000**	2011 Rs '000	2010 Rs '000
Balance as at 1 January	**878,718**	878,718	818,554	**878,718**	878,718	818,554
Transfer from revenue reserves	**–**	–	60,164	**–**	–	60,164
Balance as at 31 December	**878,718**	878,718	878,718	**878,718**	878,718	878,718

42. Investment Fund Account

Transfers to Investment Fund Account 2011 Government Budget

As proposed in the 2011 Government Budget as and when taxes are paid after 1 January 2011, licensed banks must make transfers to the Investment Fund Account to build up a permanent fund within the Bank. Accordingly such account has been established and operated based on the guideline on the operation of the investment fund account issued by Central Bank of Sri Lanka on 29 April 2011 with the Concurrence of the Commissioner General of Inland Revenue.

i. 8% of the profits calculated for the payment of Value Added Tax (VAT) on Financial Services on dates as specified in the VAT Act for payment of VAT.

ii. 5% of the profit before tax calculated for payment of income tax purposes on dates specified in Section 113 of the Inland Revenue Act for the self-assessment payment of tax.

	BANK			GROUP		
	2012 Rs '000	2011 Rs '000	2010 Rs '000	**2012 Rs '000**	2011 Rs '000	2010 Rs '000
Balance as at 1 January	**386,825**	–	–	**386,825**	–	–
Transfer from revenue reserves	**537,508**	386,825	–	**537,508**	386,825	–
Balance as at 31 December	**924,333**	386,825	–	**924,333**	386,825	–

	General Reserves Rs '000	Retained Profit Rs '000	Total Rs '000
43. Revenue Reserves			
(a) Bank			
As at 1 January 2012	5,805,707	4,510,793	10,316,500
Profit after taxation	–	2,923,958	2,923,958
Transferred to investment fund	–	(537,507)	(537,507)
Dividends paid	–	(656,696)	(656,696)
As at 31 December 2012	5,805,707	6,240,548	12,046,255

	General Reserves Rs '000	Retained Profit Rs '000	Total Rs '000
(b) Group			
As at 1 January 2012	5,805,707	8,989,942	14,795,649
Exchange gain from valuation of foreign associate	–	18,824	18,824
Transferred to investment fund	–	(537,507)	(537,507)
Change in the holding in Group companies	–	(258,037)	(258,037)
Profit after taxation	–	8,853,821	8,853,821
Dividends paid	–	(656,696)	(656,696)
As at 31 December 2012	5,805,707	16,410,347	22,216,054

44 . Measurement of Financial Instruments

	HFT Rs '000	HTM Rs '000	L & R Rs '000	AFS Rs '000	Others Rs '000	Total Rs '000
(a) Bank - Current Year (2012)						
Cash and Cash equivalents	–	–	3,480,395	–	–	3,480,395
Balances with Central Bank	–	–	6,074,792	–	–	6,074,792
Placements with banks	–	–	3,559,354	–	–	3,559,354
Securities purchased under resale agreements	–	–	3,324,868	–	–	3,324,868
Financial assets held for trading	982,967	–	–	–	–	982,967
Derivative financial instruments	1,706,372	–	–	–	–	1,706,372
Other financial assets held for trading	–	–	–	–	–	–
Loans and advances to banks	–	–	1,183,343	–	–	1,183,343
Loans and advances to customers	–	–	109,602,523	–	–	109,602,523
Lease rentals receivable	–	–	6,389,837	–	–	6,389,837
Other Financial Assets classified as loans and receivable	–	–	3,121,163	–	–	3,121,163
Financial assets - held to maturity	–	19,257,271	–	–	–	19,257,271
Financial assets - available for sale	–	–	–	66,714	–	66,714
Total Financial Assets	2,689,339	19,257,271	136,736,275	66,714	–	158,749,599
Investments in subsidiary companies	–	–	–	–	2,641,178	2,641,178
Investments in associate companies	–	–	–	–	18,525	18,525
Other assets	–	–	–	–	936,486	936,486
Intangible assets	–	–	–	–	272,314	272,314
Property, plant & equipment	–	–	–	–	856,195	856,195
Total Assets	2,689,339	19,257,271	136,736,275	66,714	4,724,699	163,474,296

	HFT Rs '000	Amortized Cost Rs '000	Others Rs '000	Total Rs '000
Liabilities				
Due to Banks	–	2,319,984	–	2,319,984
Securities sold under repurchase agreements	–	12,515,861	–	12,515,861
Derivative financial instruments	1,736,838		–	1,736,838
Due to customers	–	107,600,583	–	107,600,583
Debt securities issued and other borrowed funds	–	17,841,963	–	17,841,963
Subordinated Term debts	–	2,254,699	–	2,254,699
Total Financial Liabilities	1,736,838	142,533,090	–	144,269,928
Tax liabilities	–	–	656,211	656,211
Other liabilities	–	–	3,525,882	3,525,882
Deferred Tax	–	–	79,874	79,874
Total liabilities	1,736,838	142,533,090	4,261,966	148,531,895

	HFT Rs '000	HTM Rs '000	L & R Rs '000	AFS Rs '000	Others Rs '000	Total Rs '000
(b) Group - Current Year (2012)						
Cash and Cash equivalents	–	–	3,634,983	–	–	3,634,983
Balances with Central Bank	–	–	6,074,792	–	–	6,074,792
Placements with banks	–	–	3,559,354	–	–	3,559,354
Securities purchased under resale agreements	–	–	3,324,868	–	–	3,324,868
Financial assets held for trading	982,967	–	–	–	–	982,967
Derivative financial instruments	1,706,372	–	–	–	–	1,706,372
Other financial assets held for trading	10,411,658	–	–	–	–	10,411,658
Loans and advances to banks	–	–	1,183,343	–	–	1,183,343
Loans and advances to customers	–	–	109,649,198	–	–	109,649,198
Lease rentals receivable	–	–	6,389,837	–	–	6,389,837
Other financial assets classified as loans and receivable	–	–	3,764,025	–	–	3,764,025
Financial assets - held to maturity	–	19,223,228	–	–	–	19,223,228
Financial assets - available for sale	–	–	–	173,541	–	173,541
Total Financial Assets	13,100,997	19,223,228	137,580,399	173,541	–	170,078,171
Investments in subsidiary companies	–	–	–	–	–	–
Investments in associate companies	–	–	–	–	33,301	33,301
Other assets	–	–	–	–	1,154,688	1,154,688
Intangible assets	–	–	–	–	318,723	318,723
Property, plant & equipment	–	–	–	–	1,222,500	1,222,500
Investment properties	–	–	–	–	1,295,693	1,295,693
Total Assets	13,100,997	19,223,228	137,580,399	173,541	4,024,905	174,103,071

	HFT Rs '000	Amortized Cost Rs '000	Others Rs '000	Total Rs '000
Liabilities				
Due to Banks	–	2,319,984	–	2,319,984
Securities sold under repurchase agreements	–	12,515,861	–	12,515,861
Derivative financial instruments	1,736,838	–	–	1,736,838
Due to Customers	–	107,393,866	–	107,393,866
Debt securities issued and other borrowed funds	–	17,802,038	–	17,802,038
Subordinated Term debts	–	2,254,699	–	2,254,699
Total Financial Liabilities	1,736,838	142,286,448	–	144,023,286
Tax liabilities	–	–	633,838	633,838
Other liabilities	–	–	3,657,375	3,657,375
Deferred Tax	–	–	79,119	79,120
Total Liabilities	1,736,838	142,286,448	4,391,865	148,393,619

Notes to the Financial Statements

	HFT Rs '000	HTM Rs '000	L & R Rs '000	AFS Rs '000	Others Rs '000	Total Rs '000
(a) Bank - Previous Year (2011)						
Cash and Cash equivalents	–	–	2,395,152	–	–	2,395,152
Balances with Central Bank	–	–	4,614,170	–	–	4,614,170
Placements with banks	–	–	517,833	–	–	517,833
Securities purchased under resale agreements	–	–	911,709	–	–	911,709
Financial assets held for trading	7,106,148	–	–	–	–	7,106,148
Derivative financial instruments	1,402,305	–	–	–	–	1,402,305
Other financial assets held for trading	233,771	–	–	–	–	233,771
Loans and advances to banks	–	–	1,640,462	–	–	1,640,462
Loans and advances to customers	–	–	93,094,783	–	–	93,094,783
Lease rentals receivable	–	–	4,649,610	–	–	4,649,610
Other financial assets classified as loans and receivable	–	–	1,255,099	–	–	1,255,099
Financial assets - held to maturity	–	15,566,201	–	–	–	15,566,201
Financial assets - available for sale	–	–	–	88,648	–	88,648
Total Financial Assets	8,742,224	15,566,201	109,078,819	88,648	–	133,475,892
Investments in subsidiary companies	–	–	–	–	2,770,540	2,770,540
Investments in associate companies	–	–	–	–	286,898	286,898
Other assets	–	–	–	–	782,002	782,002
Intangible assets	–	–	–	–	278,633	278,633
Property, plant & equipment	–	–	–	–	828,754	828,754
Total Assets	8,742,224	15,566,201	109,078,819	88,648	4,946,827	138,422,719

	HFT Rs '000	Amortized Cost Rs '000	Others Rs '000	Total Rs '000
Liabilities				
Due to banks	–	5,923,527	–	5,923,527
Securities sold under repurchase agreements	–	11,360,101	–	11,360,101
Derivative financial instruments	1,022,462	–	–	1,022,462
Due to customers	–	82,094,320	–	82,094,320
Debt securities issued and other borrowed funds	–	19,466,302	–	19,466,302
Subordinated Term debts	–	2,428,012	–	2,428,012
Total Financial Liabilities	1,022,462	121,272,261	–	122,294,724
Tax liabilities	–	–	304,662	304,662
Other liabilities	–	–	3,106,320	3,106,318
Deferred Tax	–	–	41,875	41,875
Total Liabilities	1,022,462	121,272,261	3,452,857	125,747,579

	HFT Rs '000	HTM Rs '000	L & R Rs '000	AFS Rs '000	Others Rs '000	Total Rs '000
(b) Group - Previous Year (2011)						
Cash and Cash equivalents	–	–	2,518,840	–	–	2,518,840
Balances with Central Bank	–	–	4,614,170	–	–	4,614,170
Placements with banks	–	–	517,833	–	–	517,833
Securities purchased under resale agreements	–	–	911,709	–	–	911,709
Financial assets held for trading	7,106,148	–	–	–	–	7,106,148
Derivative financial instruments	1,402,305	–	–	–	–	1,402,305
Other financial assets held for trading	2,086,525	–	–	–	–	2,086,525
Loans and advances to banks	–	–	1,640,462	–	–	1,640,462
Loans and advances to customers	–	–	93,166,027	–	–	93,166,027
Lease rentals receivable	–	–	4,649,610	–	–	4,649,610
Other financial assets classified as loans and receivable	–	–	2,563,186	–	–	2,563,186
Financial assets - held to maturity	–	15,666,201	–	–	–	15,666,201
Financial assets - available for sale	–	–	–	186,475	–	186,475
Total Financial Assets	10,594,978	15,666,201	110,581,837	186,475	–	137,029,491
Investments in subsidiary companies	–	–	–	–	–	–
Investments in associate companies	–	–	–	–	1,796,695	1,796,695
Other assets	–	–	–	–	962,764	962,764
Intangible assets	–	–	–	–	318,347	318,347
Property, plant & equipment	–	–	–	–	1,185,259	1,185,259
Investment property	–	–	–	–	1,295,693	1,295,693
Total Assets	10,514,367	15,666,201	110,581,837	186,475	5,558,758	142,588,249

	HFT Rs '000	Amortized Cost Rs '000	Others Rs '000	Total Rs '000
Liabilities				
Due to Banks	–	5,923,527	–	5,923,527
Securities sold under repurchase agreements	–	10,132,841	–	10,132,841
Derivative financial instruments	1,022,462	–	–	1,022,462
Due to customers	–	82,094,320	–	82,094,320
Debt securities issued and other borrowed funds	–	19,466,303	–	19,466,303
Subordinated term debts	–	2,428,012	–	2,428,012
Total Financial Liabilities	1,022,462	120,045,002	–	121,067,465
Tax liabilities	–	–	355,976	355,976
Other liabilities	–	–	3,285,807	3,285,805
Deferred Tax	–	–	41,122	41,122
Total Liabilities	1,022,462	120,045,002	3,682,905	124,750,368

45. Fair Value of Financial Instruments

Financial Instruments Recorded at Fair Value

The following is a description of how fair values are determined for financial instruments that are recorded at fair value using valuation techniques. These incorporate the Bank's estimate of assumptions that a market participant would make when valuing the instruments.

Financial Assets Held for Trading

Financial assets held for trading consist of quoted equity securities and Government debt securities. Quoted equity securities are valued using market price published by the Colombo Stock Exchange. Government debt securities are valued using discounted cash flow techniques which incorporate market interest rate for similar investments.

Financial Derivatives

Financial derivatives are valued using valuation techniques which consider current market interest rates, forward interest rates and spot and forward exchange rates.

Determination of Fair Value and Fair Value Hierarchy

The Bank uses the following hierarchy for determining and disclosing the fair value of financial instruments by valuation technique:

Level 1: quoted (unadjusted) prices in active markets for identical assets or liabilities.

Level 2: other techniques for which all inputs which have a significant effect on the recorded fair value are observable, either directly or indirectly.

Level 3: techniques which use inputs that have a significant effect on the recorded fair value that are not based on observable market data.

The following table shows an analysis of financial instruments recorded at fair value by level of the fair value hierarchy:

	BANK			
31 December 2012	Level 1 Rs '000	Level 2 Rs '000	Level 3 Rs '000	Total Rs '000
Financial Assets				
Financial Assets held for trading				
Treasury Bills	448,489	–	–	448,489
Treasury Bonds	534,478	–	–	534,478
Derivative financial instruments				
Forward foreign exchange contracts	–	1,706,372	–	1,706,372
Total financial assets	**982,967**	**1,706,372**	**–**	**2,689,339**
Derivative financial instruments				
Forward foreign exchange contracts	–	1,736,838	–	**1,736,838**
Total financial liabilities	**–**	**1,736,838**	**–**	**1,736,838**

	BANK			
31 December 2011	Level 1 Rs '000	Level 2 Rs '000	Level 3 Rs '000	Total Rs '000
Financial Assets				
Financial Assets held for trading				
Treasury Bills	3,105,847	–	–	3,105,847
Treasury Bonds	4,000,301	–	–	4,000,301
Other financial assets held for trading				
Equity securities	233,771	–	–	233,771
Derivative Financial Instruments				
Interest rate swaps	–	1,306	–	1,306
Currency options	–	13,901	–	13,901
Forward foreign exchange contracts	–	1,387,098		1,387,098
Total financial assets	**7,106,148**	**1,636,076**	**–**	**8,742,224**
Derivative financial instruments				
Forward foreign exchange contracts	–	1,022,462	–	1,022,462
Total financial liabilities	**–**	**1,022,462**	**–**	**1,022,462**

Notes to the Financial Statements

	GROUP			
31 December 2012	Level 1 Rs '000	Level 2 Rs '000	Level 3 Rs '000	Total Rs '000
Financial Assets				
Financial Assets held for Trading				
Treasury Bills	448,489	–	–	448,489
Treasury Bonds	534,478	–	–	534,478
Other Financial Assets held for Trading				
Equity securities	123,717	–	–	123,717
Investment in unit trusts	10,287,941	–	–	10,287,941
Derivative Financial Instruments				
Forward Foreign exchange contracts	–	1,706,372	–	1,706,372
Total financial assets	**982,967**	**12,118,030**	**–**	**13,100,997**
Derivative Financial Instruments				
Forward Foreign exchange contracts	–	1,736,838	–	**1,736,838**
Total financial liabilities	**–**	**1,736,838**	**–**	**1,736,838**

	GROUP			
31 December 2011	Level 1 Rs '000	Level 2 Rs '000	Level 3 Rs '000	Total Rs '000
Financial Assets				
Financial Assets held for Trading				
Treasury Bills	3,105,847	–	–	3,105,847
Treasury Bonds	4,000,301	–	–	4,000,301
Other Financial Assets held for Trading				
Equity securities	543,809	–	–	543,809
Investment in unit trusts	1,542,716	–	–	1,542,716
Derivative Financial Instruments				
Interest rate swaps	–	1,306	–	1,306
Currency options	–	13,901	–	13,901
Forward Foreign exchange contracts	–	1,387,098		1,387,098
Total financial assets	**7,106,148**	**3,488,830**	**–**	**10,594,978**
Derivative Financial Instruments				
Forward Foreign exchange contracts	–	1,022,462	–	1,022,462
Total financial liabilities	**–**	**1,022,462**	**–**	**1,022,462**

Set out below is a comparison, by class, of the carrying amounts and fair values of the Bank's financial instruments that are not carried at fair value in the Financial Statements. This table does not include the fair values of non-financial assets and non-financial liabilities.

	2012		2011	
	Carrying Amount Rs '000	Fair Value Rs '000	Carrying Amount Rs '000	Fair Value Rs '000
Financial Assets				
Cash and cash equivalents	3,480,395	3,480,395	2,395,152	2,395,152
Balances with Central Bank	6,074,792	6,074,792	4,614,170	4,614,170
Placements with banks	3,559,354	3,559,354	517,833	517,833
Financial assets held for trading	982,967	982,967	7,106,148	7,106,148
Derivative financial instruments	1,706,372	1,706,372	1,402,305	1,402,305
Other financial assets held for trading	–	–	233,771	233,771
Securities purchased under resale agreements	3,324,868	3,324,868	911,709	911,709
Loans and advances to banks	1,183,343	1,029,596	1,640,462	1,640,462
Loans and advances to customers	109,602,523	105,501,130	93,094,783	91,717,841
Lease rentals receivables	6,389,837	5,601,146	4,649,610	4,423,656
Other financial assets classified as loans and receivables	3,121,163	3,121,163	1,255,099	1,298,288
Financial assets - Held to maturity	19,257,271	17,346,778	15,566,201	15,388,935
Financial assets - Available-for-sale	66,714	66,714	88,648	88,648
Total financial assets	158,749,598	151,795,275	133,475,892	131,738,918
Financial Liabilities				
Due to banks	2,319,984	2,319,984	5,923,527	5,923,527
Derivative financial instruments	1,736,838	1,736,838	1,022,462	1,022,462
Securities sold under repurchase agreements	12,515,861	12,515,861	11,360,101	11,360,101
Due to customers	107,600,583	104,231,973	82,094,320	79,521,844
Debt securities issued and other borrowed funds	17,841,963	17,841,963	19,466,302	19,466,302
Subordinated term debts	2,254,699	2,254,699	2,428,012	2,428,012
Total financial liabilities	144,269,927	140,901,317	122,294,724	117,294,236

Fair Value of Financial Assets and Liabilities Not Carried at Fair Value

The following describes the methodologies and assumptions used to determine fair values for those financial instruments which are not already recorded at fair value in the Financial Statements:

Assets for which Fair Value Approximates Carrying Value

For financial assets and financial liabilities that have a short-term maturity (less than three months) it is assumed that the carrying amounts approximate their fair value. This assumption is also applied to demand deposits, and savings accounts without a specific maturity.

Fixed Rate Financial Instruments

The fair value of fixed rate financial assets and liabilities carried at amortized cost are estimated by comparing market interest rates when they were first recognized with current market rates for similar financial instruments. The estimated fair value of fixed interest-bearing deposits is based on discounted cash flows using prevailing money market interest rates for debts with similar credit risk and maturity. For quoted debt issued the fair values are determined based on quoted market prices. For those notes issued where quoted market prices are not available, a discounted cash flow model is used based on a current interest rate yield curve appropriate for the remaining term to maturity and credit spreads. For other variable rate instruments, an adjustment is also made to reflect the change in required credit spread since the instrument was first recognized.

46. Risk Management

46.1 Introduction

Risk Management Structure

The Board of Directors is responsible for the overall risk management approach and for approving the risk management strategies and principles.

The Board Integrated Risk Management Committee (IRMC) which is a subcommittee of the Board meets quarterly to review and assess the Bank's overall risks and to focus on policy recommendations and strategies in an integrated manner. The IRMC Charter was formulated and approved by the Board of Directors.

The Bank's Assets & Liabilities Committee (ALCO) reviews all market and liquidity related exposures, excesses on a monthly basis and decisions are made to facilitate the business requirements. These decisions are further reviewed at IRMC and reviewed by the Board.

The Credit and Market Risk Policy Committee and Operational Risk Policy Committee are in operation to formulate policies and to focus more clearly on defined risk areas. These committees comprise of the CEO, COO, CFO, the heads of business units, Treasury and representatives of the Group Risk Management. The committees meet regularly to review the Bank's risk policy framework, overall performance and the potential risks faced by specific lines of business and support functions.

Bank Treasury is responsible for managing the Bank's assets and liabilities and the overall financial structure. It is also primarily responsible for the funding and liquidity risks of the Bank.

Risk Measurement and Reporting Systems

Monitoring and controlling risks is primarily performed based on limits established by the Bank. These limits reflect the business strategy and market environment of the Bank as well as the level of risk that the Bank is willing to accept, with additional emphasis on selected industries.

Information compiled is examined and processed in order to analyze, control and identify risks on a timely basis. This information is presented and explained to the Board subcommittee for Integrated Risk Management and heads of each business division. The report includes aggregate credit exposure based on business lines, product, group and industry concentrations, NPL movements, liquidity ratios, maturity gap analysis, price sensitivity, stress tests. The Committee also assesses the appropriateness of the provision for credit losses on a quarterly basis. The Board of Directors receives a comprehensive risk report once a quarter which is designed to provide all the necessary information to assess and conclude on the risks of the Bank.

Risk Concentration

Concentrations arise when a number of counterparties are engaged in similar business activities, or activities in the same geographical region, or have similar economic features that would cause their ability to meet contractual obligations to be similarly affected by changes in economic, political or other conditions. Concentrations indicate the relative sensitivity of the Bank's performance to developments affecting a particular industry or geographical location.

46.2 Credit Risk

Credit risk is the risk that the Bank will incur a loss because its customers or counterparties fail to discharge their contractual obligations. The bank manages and controls credit risk by setting limits on the amount of risk it is willing to accept for individual/ group counterparties and for geographical and industry concentrations, and by monitoring exposures in relation to such limits.

The Bank has established a credit quality review process to provide early identification of possible changes in the creditworthiness of counterparties. Counterparty limits are established by the use of a internally-designed credit risk classification system, which assigns each counterparty a risk rating. Risk ratings are subject to regular revision. The credit quality review process aims to allow the Bank to assess the potential loss as a result of the risks to which it is exposed and take corrective action.

Credit Risk Management verifies and manages the credit process from origination to collection. NDB Bank has a well-defined credit policy approved by the Board of Directors. It defines the -

- credit culture of the Bank
- specify target markets for lending
- specify prohibited lending which the Bank under no circumstances will entertain
- set acceptable risk parameters
- set remedial and recovery actions

The principles guiding the credit risk management across the Bank is given on page 156.

Risk management works closely with the Bank's business units at every stage of the credit process, from facility origination to approval to collections, adding value as appropriate and developing the proposal in terms of risks, mitigants and returns. A post-sanction review and monitoring mechanism is in place to ensure quality of credit is not compromised. Any deteriorating credits with emphasis on internal and external early warning signals are identified and such accounts are 'Watch Listed'. The Watch Listed clients are monitored closely with quarterly reports submitted to the Executive Credit Committee. Further, based on the Watch Lists the Bank assesses the portfolio at risk in the event, such accounts deteriorates further. Non-performing assets are identified at an early stage, enabling management to take action as appropriate.

Impairment Assessment

For accounting purposes, the Bank uses an incurred loss model for the recognition of losses on impaired financial assets. This means that losses can only be recognized when objective evidence of a specific loss event has been observed. Triggering events include the following:

- Significant financial difficulty of the customer
- A breach of contract such as a default of payment
- Where the Bank grants the customer a concession due to the customer experiencing financial difficulty
- It becomes probable that the customer will enter bankruptcy or other financial reorganization
- Observable data that suggests that there is a decrease in the estimated future cash flows from the loans

Individually Assessed Allowances

The Bank determines the allowances appropriate for each individually significant loan or advance on an individual basis if there is any objective evidence of a loss based on the above. Items considered when determining allowance amounts include the sustainability of the counterparty's business plan, its ability to improve performance if it is in a financial difficulty, projected receipts and the expected payout should bankruptcy arise, the availability of other financial support, the realizable value of collateral and the timing of the expected cash flows. Impairment allowances are evaluated at each reporting date, unless unforeseen circumstances require more careful attention.

Collectively-Assessed Allowances

Allowances are assessed collectively for losses on loans and advances that are not individually significant (including personal loans, leases and pawning) and for individually significant loans and advances that have been assessed individually and found not to be impaired.

The Bank generally bases its analyses on historical experience and market factors. These factors include, depending on the characteristics of the individual or collective assessment: unemployment rates, current levels of bad debts, changes in laws, changes in regulations, and other relevant consumer data. The Bank may use the aforementioned factors as appropriate to adjust the impairment allowances.

Allowances are evaluated separately at each reporting date with each portfolio. The collective assessment is made for groups of assets with similar risk characteristics, in order to determine whether provision should be made due to incurred loss events for which there is objective evidence, but the effects of which are not yet evident in the individual loans assessments. The collective assessment takes account of data from the loan portfolio (such as loan types, industry codes, internal risk ratings and level of arrears).

Analysis of Gross Exposure on Credit Risk and Impairment

The table below shows the credit quality by class of asset for all financial assets exposed to credit risk, based on the Bank's classification of assets. The amounts presented are gross of impairment allowances.

			Past Due but not Impaired*						
Products	Note	Neither Past Due Nor Impaired* Rs mn	Less than 3 months Rs mn	3-6 months Rs mn	6-12 months Rs mn	12-18 months Rs mn	Over 18 months Rs mn	Individually Impaired Rs mn	Total Rs mn
Bank									
Cash and cash equivalents	14	3,480	–	–	–	–	–	–	3,480
Balances with Central Bank	15	6,075	–	–	–	–	–	–	6,075
Placements with banks	16	3,559	–	–	–	–	–	–	3,559
Securities purchased under resale agreements	20	3,325	–	–	–	–	–	–	3,325
Financial assets held for trading	17	983	–	–	–	–	–	–	983
Derivative financial instruments	18	1,706	–	–	–	–	–	–	1,706
Other financial assets held for trading	19	–	–	–	–	–	–	–	–
Loans and advances to banks	21	1,183	–	–	–	–	–	–	1,183
Loans and advances to customers	22	89,803	15,289	656	2,901	832	1,646	1,349	112,476
Lease rentals receivable	24	6,336	3,158	52	31	5	183	–	9,765
Other financial assets classified as loans and receivables	25	3,121	–	–	–	–	–	–	3,121
Financial assets - held to maturity	26	19,257	–	–	–	–	–	–	19,257
Financial assets - available for sale	27	67	–	–	–	–	–	–	67

			Past Due but not Impaired*						
Products	Note	Neither Past Due Nor Impaired* Rs mn	Less than 3 months Rs mn	3-6 months Rs mn	6-12 months Rs mn	12-18 months Rs mn	Over 18 months Rs mn	Individually Impaired Rs mn	Total Rs mn
Group									
Cash and cash equivalents	14	3,635	–	–	–	–	–	–	3,635
Balances with Central Bank	15	6,075	–	–	–	–	–	–	6,075
Placements with banks	16	3,559	–	–	–	–	–	–	3,559
Securities purchased under resale agreements	20	3,325	–	–	–	–	–	–	3,325
Financial assets held for trading	17	983	–	–	–	–	–	–	983
Derivative financial instruments	18	1,706	–	–	–	–	–	–	1,706
Other financial assets held for trading	19	9,781	–	–	–	–	–	–	10,412
Loans and advances to banks	21	1,183	–	–	–	–	–	–	1,183
Loans and advances to customers	22	89,849	15,289	656	2,901	832	1,646	1,349	112,522
Lease rentals receivable	24	6,336	3,158	52	31	5	183	–	9,765
Other financial assets classified as loans and receivables	25	3,764	–	–	–	–	–	–	3,764
Financial assets - held to maturity	26	19,223	–	–	–	–	–	–	19,223
Financial assets - available for sale	27	174	–	–	–	–	–	–	174

** Collective impairment allowances are made for 'neither past due nor impaired' and 'past due but not impaired' loans.*

Industry Analysis Risk Concentration

The Bank's concentrations of risk are managed by client/counterparty and by industry sector.

The following tables show the risk concentration by industry:

As at 31 December 2012	Financial Services Rs '000	Government Rs '000	Consumer Rs '000	Retail and Wholesale Rs '000	Construction Rs '000	Manufacturing Rs '000	Service Rs '000	Total Rs '000
Bank								
Financial Assets								
Cash and Cash Equivalents								
Cash in hand	1,546,788	–	–	–	–	–	–	1,546,788
Dues from banks	1,933,607	–	–	–	–	–	–	1,933,607
	3,480,395	–	–	–	–	–	–	3,480,395
Balances with Central Bank	–	6,074,792	–	–	–	–	–	6,074,792
Placements with banks	3,559,354	–	–	–	–	–	–	3,559,354
Financial Assets Held for Trading								
Treasury Bills	–	448,489	–	–	–	–	–	448,489
Treasury Bonds	–	534,478	–	–	–	–	–	534,478
	–	982,967	–	–	–	–	–	982,967
Derivative Financial Instruments								
Forward foreign exchange contracts	1,706,372	–	–	–	–	–	–	1,706,372
	1,706,372	–	–	–	–	–	–	1,706,372
Securities purchased under resale agreements	3,324,868	–	–	–	–	–	–	3,324,868
Loans and Advances to Banks	1,183,343	–	–	–	–	–	–	1,183,343
Loans and Advances to Customers								
Gross loans and receivables	13,202,534	–	11,386,699	22,823,870	18,831,013	33,420,267	12,811,527	112,475,910
(Less): Allowance for impairment losses	(375,678)	–	(196,711)	(396,948)	(507,165)	(1,175,192)	(221,693)	(2,873,387)

As at 31 December 2012	Financial Services Rs '000	Government Rs '000	Consumer Rs '000	Retail and Wholesale Rs '000	Construction Rs '000	Manufacturing Rs '000	Service Rs '000	Total Rs '000
	12,826,856	–	11,189,988	22,426,922	18,323,848	32,245,075	12,589,834	109,602,523
Lease Rentals Receivables								
Gross loans receivables	135,775	–	–	4,455,006	1,385,779	1,654,863	2,133,463	9,764,886
(Less) Unearned income	(46,236)			(1,517,099)	(471,910)	(563,544)	(726,525)	(3,325,314)
(Less) Collective impairment charges	(692)	–	–	(22,690)	(7,058)	(8,429)	(10,866)	(49,735)
	88,847	–	–	2,915,217	906,811	1,082,890	1,396,072	6,389,837
Other Financial Assets Classified As Loans and Receivable								
Sri Lanka Development Bonds	–	2,981,123	–	–	–	–	–	2,981,123
Redeemable cumulative preference shares	–	–	–	–	–	–	140,040	140,040
	–	2,981,123	–	–	–	–	140,040	3,121,163
Financial Investments - Held to Maturity								
Treasury Bills	–	3,476,192	–	–	–	–	–	3,476,192
Treasury Bonds		15,781,079	–	–	–	–	–	15,781,079
	–	19,257,271	–	–	–	–	–	19,257,271
Financial Investments - Available for Sale								
Non-quoted ordinary shares	–	–	–	–	–	–	4,790	4,790
Investment fund account	–	61,924	–	–	–	–	–	61,924
	–	61,924	–	–	–	–	4,790	66,714
	26,170,032	29,358,077	11,189,988	25,342,139	19,230,659	33,327,966	14,130,736	158,749,599

Notes to the Financial Statements

As at 31 December 2012	Financial Services Rs '000	Government Rs '000	Consumer Rs '000	Retail and Wholesale Rs '000	Construction Rs '000	Manufacturing Rs '000	Service Rs '000	Total Rs '000
Group								
Financial Assets								
Cash and Cash equivalents								
Cash in hand	1,546,864	–	–	–	–	–	–	1,546,864
Dues from Banks	2,088,119	–	–	–	–	–	–	2,088,119
	3,634,983	–	–	–	–	–	–	3,634,983
Balances with Central Bank	–	6,074,792	–	–	–	–	–	6,074,792
Placements with banks	3,559,354	–	–	–	–	–	–	3,559,354
Financial Assets Held for Trading	–	–	–	–	–	–	–	–
Treasury Bills	–	448,489	–	–	–	–	–	448,489
Treasury Bonds	–	534,478	–	–	–	–	–	534,478
	–	982,967	–	–	–	–	–	982,967
Derivative Financial Instruments								
Forward foreign exchange contracts	1,706,372	–	–	–	–	–	–	1,706,372
	1,706,372	–	–	–	–	–	–	1,706,372
Other Financial Assets Held for Trading								
Equity Securities	123,717	–	–	–	–	–	–	123,717
Investment in Unit Trusts	10,287,941	–	–	–	–	–	–	10,287,941
	10,411,658	–	–	–	–	–	–	10,411,658
Securities purchased under resale agreements	3,324,868	–	–	–	–	–	–	3,324,868
Loans and advances to banks	1,183,343	–	–	–	–	–	–	1,183,343
Loans and advances to customers								
Gross loans and receivables	13,202,532	–	11,386,699	22,870,543	18,831,013	33,420,267	12,811,527	112,522,586
(Less): Allowance for impairment losses	(375,679)	–	(196,711)	(396,948)	(507,165)	(1,175,192)	(221,693)	(2,873,388)
	12,826,853	–	11,189,988	22,473,595	18,323,848	32,245,076	12,589,835	109,649,198

As at 31 December 2012	Financial Services Rs '000	Government Rs '000	Consumer Rs '000	Retail and Wholesale Rs '000	Construction Rs '000	Manufacturing Rs '000	Service Rs '000	Total Rs '000
Lease Rentals Receivables								
Gross loans and receivables	135,775	–	–	4,455,006	1,385,779	1,654,863	2,133,463	9,764,886
(Less) Unearned Income	(46,236)	–	–	(1,517,099)	(471,910)	(563,544)	(726,525)	(3,325,314)
(Less) Collective impairment charges	(692)	–	–	(22,690)	(7,058)	(8,429)	(10,866)	(49,735)
	88,847	–	–	2,915,217	906,811	1,082,890	1,396,072	6,389,837
Other Financial Assets Classified as Loans and Receivable								
Sri Lanka Development Bonds	–	2,981,123	–	–	–	–	–	2,981,123
Redeemable cumulative preference shares	–	–	–	–	–	–	140,040	140,040
Investment in securitization	642,862	–	–	–	–	–	–	642,862
	642,862	2,981,123	–	–	–	–	140,040	3,764,025
Financial Investments - Held to Maturity								
Treasury Bills	–	3,500,061	–	–	–	–	–	3,500,061
Treasury Bonds	–	15,616,573	–	–	–	–	–	15,616,573
Debentures	106,594	–	–	–	–	–	–	106,594
	106,594	19,116,635	–	–	–	–	–	19,223,228
Financial Investments - Available for sale								
Non-quoted ordinary shares	–	–	–	–	–	–	68,201	68,201
Investment fund account	43,412	61,924	–	–	–	–	–	105,336
	43,412	61,924	–	–	–	–	68,201	173,537
	37,529,145	29,217,441	11,189,988	25,388,812	19,230,659	33,327,966	14,194,147	170,078,163

Commitments and Guarantees

To meet the financial needs of customers, the Bank enters into various irrevocable commitments and contingent liabilities. Even though these obligations may not be recognized on the Statement of Financial Position, they do contain credit risk and are therefore part of the overall risk of the Bank.

The table below shows the Bank's maximum credit risk exposure for commitments and guarantees.

The maximum exposure to credit risk relating to a financial guarantee is the maximum amount the Bank would have to pay if the guarantee is called upon.

	2012 Rs mn	2011 Rs mn
Guarantees & Bonds	**9,120**	7,731
Shipping guarantees	**3,668**	6,893
Advanced documents endorsed	**1,571**	2,123
LCs	**7,168**	8,955
Acceptances	**5,866**	5,918
Undrawn ODs & credit cards	**5,839**	4,911
Commitments	**43,598**	28,176
Forex	**81,910**	80,960
Total	**158,740**	145,667

46.3 Liquidity Risk and Funding Management

Liquidity risk is defined as the risk that the Bank will encounter difficulty in meeting obligations associated with financial liabilities that are settled by delivering cash or another financial asset. Liquidity risk arises because of the possibility that the Bank might be unable to meet its payment obligations when they fall due under both normal and stress circumstances. To limit this risk, management has arranged diversified funding sources in addition to its core deposit base, and adopted a policy of managing assets with liquidity in mind and monitoring future cash flows and liquidity on a daily basis.

The Bank has developed internal control processes and is equipped with a comprehensive Liquidity Contingency Funding Plan (LCFP) linked to the Business Continuity Plan, which is in line with the regulatory guidelines. The LCFP clearly defines the responsibilities of the Liquidity Management Team and ensures the business continuity through close monitoring of the Bank's liquidity position against the pre-defined liquidity risk trigger points. Trigger points have been defined taking into consideration the Bank specific and systemic triggers which would cause a liquidity crisis. Action Plans are set out under each level of liquidity crisis (Mild, Moderate, Severe) with responsibilities assigned to a Liquidity Management Team nominated from all areas of business to ensure that all stakeholders of the Bank are safeguarded.

The Bank maintains a portfolio of marketable and diverse assets that are assumed to be easily liquidated in the event of an unforeseen interruption of cash flow. In addition, the Bank maintains a statutory deposit with the Central Bank of 8% of customer deposits.

In accordance with the Bank's policy, the liquidity position is assessed/stressed and managed under a variety of scenarios, giving due consideration to stress factors relating to both the market in general and specifically to the Bank. The most important of these is to maintain limits on the ratio of net liquid assets to customer liabilities, to reflect market conditions. Net liquid assets consist of cash, short-term bank deposits and liquid debt securities available for immediate sale.

Liquidity Ratios

Liquid Asset Ratio

The Bank defines liquid assets for the purposes of the liquidity ratio as cash balances, short-term interbank deposits and highly-rated debt securities available for immediate sale and for which a liquid market exists. The Bank is expected to maintain a minimum Liquid Asset Ratio of 20% on a daily basis. An internally set prudential liquid asset ratio on top of the regulatory requirement level ensures that the Bank is maintaining adequate liquidity buffer throughout the year.

	2012 %
Year end	24.92
Maximum	27.67
Minimum	23.17
Average	24.35

Advances to Deposit Ratio (ADR Ratio)

The Bank stresses the importance of current accounts and savings accounts as sources of funds to finance lending to customers. They are monitored using the advances to deposit ratio, which compares loans and advances to customers as a percentage of core customer current and savings accounts, together with term funding with a remaining term to maturity in excess of one year. Loans to customers that are part of reverse repurchase arrangements, and where the Bank receives securities which are deemed to be liquid, are excluded from the advances to deposits ratio. Due to the fact that the Bank has been a Development Bank, the Balance Sheet Structure has resulted in an ADR ratio higher than the industry norm. The Bank is consciously managing same with adequate measures to improve the ratio gradually. Continuous growth in the deposit base has resulted in bringing the ADR ratio in line with the approved limit.

Advances to Deposit Ratios

	2012 %
Year end	105.0
Maximum	107.7
Minimum	102.4
Average	105.4

Net Loans to Total Assets

The consistency in the Net Loans to Total Assets Ratio of the Bank reflects that the Bank has maintained the share of loans and advances in total asset base focusing mainly on Loans and Advances.

Net Loans to Total Assets Ratio During the Year	2011 December	2012 March	2012 June	2012 September	2012 December
Net Loans (Rs mn)	99,384	103,964	99,615	111,782	117,151
Total Assets (Rs mn)	138,797	143,756	138,366	159,004	163,474
Ratio (%)	71.60	72.32	71.99	70.30	71.66

Liquidity Risk and Funding Management

The table below summarizes the maturity profile of the undiscounted cash flows of the bank's financial assets and liabilities as at 31 December 2012.

Liquidity Mismatch Report Maturities of Undiscounted Cash Flows of Financial Assets and Liabilities

	On Demand Rs mn	Trading Derivatives Rs mn	Less than 3 months Rs mn	3 - 12 months Rs mn	1 - 5 years Rs mn	Over 5 Years Rs mn	Total Rs mn
Assets:							
Cash and Cash equivalents	3,480,395	–	–	–	–	–	3,480,395
Balances with Central Bank	6,074,792	–	–	–	–	–	6,074,792
Placements with Banks	–	–	3,533,292	80,796	–	–	3,614,088
Financial Assets held for trading	–		255,275	603,965	201,444	–	1,060,684
Derivative Financial Instruments	–	1,706,372	–	–	–	–	1,706,372
Securities purchased under resale agreements	–	–	3,324,868	–	–	–	3,324,868
Loans and advances to banks	–	–	191,615	460,677	816,726	1,334	1,470,352
Loans and advances to customers	–	–	68,161,319	18,595,307	33,182,867	8,887,742	128,827,235
Lease rentals receivables	–	–	878,738	1,942,782	5,488,402	25,000	8,334,922
Other Financial Assets classified as loans and receivable	–	–	3,000,181	–	–	–	3,000,181
Financial assets - Held to Maturity	–	–	4,834,000	6,293,000	10,969,000	–	22,096,000
Financial assets - Available for sale	–	–	66,714	–	–	–	66,714
Total Financial Assets	9,555,187	1,706,372	84,246,003	27,976,526	50,658,439	8,914,075	183,056,603
Financial Liabilities:							
Due to Banks	1,682,521	637,463	–	–	–	–	2,319,984
Derrivative Financial Instruments	–	1,736,838	–	–	–	–	1,736,838
Securities sold under repurchase agreements	–	–	2,571,929	10,107,646	–	–	12,679,575
Due to Customers	–	–	70,611,726	34,699,328	3,484,738	–	108,795,791
Debt Securities issued and other borrowed funds	–	–	7,509,125	1,875,490	6,256,251	1,094,023	16,734,889
Subordinated term debts	–	–	–	–	3,176,025	–	170,840
Total Financial Liabilities	1,682,521	2,374,301	80,692,780	46,682,464	12,917,014	1,094,023	142,437,917

Contractual Maturities for Contingencies

The table below summarises the maturity profile of the Bank's Contingent liabilities as at 31 December 2012.

	On Demand Rs '000	Less than 3 months Rs '000	3 - 12 months Rs '000	1 - 5 years Rs '000	Over 5 Years Rs '000	Total Rs '000
Undisbursed financing commitments	5,838,596	42,207,558	14,271	695,133	681,706	49,437,265
Guarantees	3,893,151	3,611,044	4,906,953	1,891,829	56,412	14,359,389
Commitments on account of letter of credit	494,795	6,000,394	664,348	8,424	–	7,167,961
Forward exchange contracts	–	44,473,483	37,039,657	397,150	–	81,910,289
Acceptances	–	4,772,503	1,093,413	–	–	5,865,916
	10,226,543	101,064,981	43,718,642	2,992,536	738,118	158,740,820

46.4 Market risk

Market risk is the risk that the fair value or future cash flows of financial instruments will fluctuate due to changes in market variables such as interest rates, foreign exchange rates and equity prices. The Bank classifies exposures to market risk into either trading or non-trading portfolios and manages each of those portfolios separately. The market risk for the trading portfolio is managed and monitored based on a mark to market computation and duration analysis that reflects the portfolio volatility and the market sensitivity.

Mark to Market Exercise - Trading

Trading portfolios of Securities (Treasury Bills/Bonds), Equity and Foreign Currency Options are subject to mark to market exercise on a daily basis and are monitored against the set stop-loss limits. Prompt management action taken where necessary ensuring minimum loss situations to the portfolios.

Mark to market results are being monitored against the Board approved stop-loss limit on a daily basis and reviewed at monthly ALCO and the Integrated Risk Management Committee on a quarterly basis to assess the portfolio performance and investment decisions.

46.4.1 Interest Rate Risk

Interest rate risk arises from the possibility that changes in interest rates will affect future cash flows or the fair values of financial instruments. The Board has established limits on the non-trading interest rate gaps for stipulated periods. The Bank's policy is to monitor positions on a daily basis and hedging strategies are used to ensure positions are maintained within the established limits.

The following table demonstrates the sensitivity to a reasonably possible change in interest rates, with all other variables held constant, of the Bank's Income Statement

The sensitivity of the Income Statement is the effect of the assumed changes in interest rates on the profit or loss for a year, based on the interest rate sensitive assets and liabilities as at 31 December 2012.

	Increase/(Decrease) in basis points	Sensitivity of profit or loss Rs mn	Sensitivity of Equity Rs mn
Trading	+ 100/(100)	6.64/6.64	(6.64)/6.64

46.4.2 Currency Risk

Currency risk is the risk that the value of a financial instrument will fluctuate due to changes in foreign exchange rates. The Board has set limits on positions by currency. In accordance with the Bank's policy, positions are monitored on a daily basis and hedging strategies are used to ensure positions are maintained within established limits.

The table below indicates the currencies to which the Bank had significant exposure at 31 December 2012 on its currency exposures. The analysis calculates the sensitivity of each currency position to the increase in exchange rate against the LKR with all other variables held constant, on the Income Statement and equity. A negative amount in the table reflects a potential net reduction in Income Statement or equity, while a positive amount reflects a net potential increase depending on the side of the currency position. An equivalent decrease in below currencies against the LKR would have resulted in an equivalent but opposite impact.

Change in currency rate in %

Currency	%	Effect on Profit 2012 Rs '000	Effect on Equity 2012 Rs
USD	2.50	(15,327)	(15,327)
GBP	2.50	(144)	(144)
EUR	2.50	1,100	1,100

Equity Price Risk

Equity price risk is the risk that the fair value of equities decreases as the result of changes in the level of equity indices and individual stocks. The non-trading equity price risk exposure arises from equity securities classified as available for sale. The Bank was insensitive to the equity price changes since the Bank did not carry an equity portfolio as at 31 December 2012

Prepayment Risk

Prepayment risk is the risk that the Bank will incur a financial loss because its customers and counterparties repay or request repayment earlier than expected, such as fixed rate mortgages when interest rates fall.

The Bank uses regression models to project the impact of varying levels of prepayment on its net interest income. The model makes a distinction between the different reasons for repayment (e.g., relocation, refinancing and renegotiation) and takes into account the effect of any prepayment penalties.

46.5 Country Risk

Country risk is the risk that an occurrence within a country could have an adverse effect on the Bank directly by impairing the value of the Bank or indirectly through an obligor's ability to meet its obligations to the Bank. Generally, these occurrences relate, but are not limited to: sovereign events such as defaults or restructuring; political events such as contested elections; restrictions on currency movements; non-market currency convertibility; regional conflicts; economic contagion from other events such as sovereign default issues or regional turmoil; banking and currency crisis; and natural disasters.

Geographical Analysis - Bank

31 December 2012	Sri Lanka Rs '000	Europe Rs '000	America Rs '000	Asia Rs '000	Oceania Rs '000	Total Rs '000
Cash and Cash equivalents	1,678,833	346,098	1,137,254	237,112	81,099	3,480,395
Balances with Central Bank	6,074,792	–	–	–	–	6,074,792
Placements with banks	3,559,354	–	–	–	–	3,559,354
Securities purchased under resale agreements	3,324,868	–	–	–	–	3,324,868
Financial assets held for trading	982,967	–	–	–	–	982,967
Derivative financial instruments	1,706,372	–	–	–	–	1,706,372
Loans and advances to banks	1,183,343	–	–	–	–	1,183,343
Loans and advances to customers	109,602,523	–	–	–	–	109,602,523
Lease rentals receivables	6,389,837	–	–	–	–	6,389,837
Other financial assets classified as loans and receivable	3,121,163	–	–	–	–	3,121,163
Financial assets - held to maturity	19,257,271	–	–	–	–	19,257,271
Financial assets - available for sale	66,714	–	–	–	–	66,714
Investments in subsidiary companies	2,641,178	–	–	–	–	2,641,178
Investments in associate companies	18,525	–	–	–	–	18,525
Other assets	936,485	–	–	–	–	936,485
Intangible assets	272,314	–	–	–	–	272,314
Property, plant & equipment	856,195	–	–	–	–	856,195
Total Assets	161,672,734	346,098	1,137,254	237,112	81,099	163,474,296

Geographical Analysis - Group

31 December 2012	Sri Lanka Rs '000	Europe Rs '000	America Rs '000	Asia Rs '000	Oceania Rs '000	Total Rs '000
Cash and Cash equivalents	1,833,420	346,098	1,137,254	237,112	81,099	3,634,983
Balances with Central Bank	6,074,792	–	–	–	–	6,074,792
Placements with banks	3,559,354	–	–	–	–	3,559,354
Securities purchased under resale agreements	3,324,868	–	–	–	–	3,324,868
Financial assets held for trading	982,967	–	–	–	–	982,967
Derivative financial instruments	1,706,372	–	–	–	–	1,706,372
Other financial assets held for trading	10,411,658	–	–	–	–	10,411,658
Loans and advances to banks	1,183,343	–	–	–	–	1,183,343
Loans and advances to customers	109,649,198	–	–	–	–	109,649,198
Lease rentals receivables	6,389,837	–	–	–	–	6,389,837
Other financial assets classified as loans and receivable	3,764,025	–	–	–	–	3,764,025
Financial assets - held to maturity	19,223,228	–	–	–	–	19,223,228
Financial assets - available for sale	173,541	–	–	–	–	173,541
Investments in associate companies	33,301	–	–	–	–	33,301
Other assets	1,154,688	–	–	–	–	1,154,688
Intangible assets	318,723	–	–	–	–	318,723
Property, plant & equipment	1,222,500	–	–	–	–	1,222,500
Investment properties	1,295,693	–	–	–	–	1,295,693
Total Assets	172,382,606	346,098	1,137,254	237,112	81,099	174,103,071

	2012 Rs '000	2011 Rs '000
47. Share-Based Payments to Key Management Personnel		
Share Grant		
No. of ordinary shares held [Refer Note (a)]	**209,848**	209,848
Dividends paid (in Rs '000)	**755**	1,127
No. of cumulative grants allocated under the Equity Linked Compensation Plan (ELCP) Tranche 1 (6 July 2010)	**209,848**	209,848

Share Option

As at 31 December 2010, the eligible members of the staff were allocated share options as follows:

209,848 ordinary shares at a price of Rs 124.21 each, was vested on 6 July 2011 and exercisable before 30 June 2014.

Note (a)

At the Annual General Meeting held on 30 March 2011, the shareholders of the Bank approved to increase the number of existing ordinary shares amounting to 82,100,951 by subdividing the said existing ordinary shares in the proportion of one share for every ordinary share in issue so that the number of ordinary shares representing the Stated Capital of the Bank be increased to 164,201,902. Accordingly, the number of shares of the share grant and the share option as at 31 December 2011 and 31 December 2012 was 209,848.

48. Maturity Analysis

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:

	Within 12 Months Rs '000	After 12 Months Rs '000	Total Rs '000
Cash and cash equivalents	3,480,395	–	3,480,395
Balance with Central Bank	6,074,792	–	6,074,792
Placements with banks	3,559,354	–	3,559,354
Securities purchased under resale agreements	3,324,868	–	3,324,868
Assets held for trading	982,967	–	982,967
Derivative financial Instruments	1,706,372	–	1,706,372
Loans and advances to banks	567,608	615,735	1,183,343
Loans and advances to customers	78,753,164	30,849,359	109,602,523
Lease rentals receivables	2,287,859	4,101,978	6,389,837
Other financial assets classified as loans and receivables	48,623	3,072,540	3,121,163
Financial assets - held to maturity	9,704,863	9,552,408	19,257,271
Financial assets - available for sale	66,714	–	66,714
Investments in subsidiary companies	–	2,641,178	2,641,178
Investments in associate companies	–	18,525	18,525
Group balances/Other Assets	936,485	–	936,485
Intangible assets	–	272,314	272,314
Property, plant & equipment	–	856,195	856,195
Total assets	111,494,064	51,980,232	163,474,296
Liabilities			
Due to banks	2,319,984	–	2,319,984
Securities sold under repurchase agreements	12,513,817	2,044	12,515,861
Derivatives financial instruments	1,736,838	–	1,736,838
Due to customers	104,525,878	3,074,705	107,600,583
Debt securities issued and other borrowed funds	8,730,100	9,111,863	17,841,963
Tax liabilities	656,211	–	656,211
Other liabilities	3,525,882	–	3,525,882
Subordinated term debts	577,999	1,676,700	2,254,699
Deferred tax	–	79,874	79,874
Total liabilities	134,586,709	13,945,186	148,531,895
SHAREHOLDERS FUNDS			
Stated capital	–	1,093,095	1,093,095
Statutory reserve fund	–	878,718	878,718
Investment fund	–	924,333	924,333
Revenue reserves	–	12,046,255	12,046,255
Minority interests	–	–	–
Total funds employed	–	14,942,401	14,942,401
Total liabilities and funds employed	–	–	–
As at 31 December 2012	134,586,709	28,887,587	163,474,296

49. Commitment and Contingencies

49.1 Business Commitments

In the normal course of business, the 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:

	BANK			GROUP		
	2012	2011	2010	**2012**	2011	2010
	Rs '000	Rs '000	Rs '000	**Rs '000**	Rs '000	Rs '000
Undisbursed financing commitments	**49,437,265**	33,086,804	21,495,867	**49,437,265**	33,086,804	21,495,867
Guarantees	**14,359,389**	16,747,134	7,919,207	**14,359,389**	16,747,134	7,919,207
Commitments on account of letters of credit	**7,167,960**	8,955,288	6,197,540	**7,167,960**	8,955,288	6,197,540
Forward exchange contracts	**81,910,290**	80,959,785	56,226,251	**81,910,290**	80,959,785	56,226,251
Acceptances	**5,865,916**	5,918,369	3,865,228	**5,865,916**	5,918,369	3,865,228
	158,740,820	145,667,380	95,704,093	**158,740,820**	145,667,380	95,704,093

49.2 Litigation against the Bank

In the normal course of business, the 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 thirty five clients/third parties have filed cases against the Bank preventing the sale of assets mortgaged to the Bank. The 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 the Bank.

49.3 Rs 165 mn was provided during the year ended 31 December 2011 in respect of the impairment of the Bank's investment in Maldives Finance Leasing Company Ltd., which is disclosed in the Income Statement under Provision/(Release) for the fall in value of investment securities. Further, the Bank has provided letters of comfort for the borrowings undertaken by the Company. Accordingly, the probable liability in the event the Company fails to meet its debt obligations amounts to Rs 18 mn as at the Balance Sheet date.

50. Post-Balance Sheet Events

There have been no events subsequent to the end of the reporting period that require disclosure.

51. SEGMENTAL ANALYSIS - GROUP

	Banking		Capital Markets		Property Investment		Others		Consolidated	
For the year ended 31 December	**2012**	2011	**2012**	2011	**2012**	2011	**2012**	2011	**2012**	2011
	Rs '000	Rs '000	**Rs '000**	Rs '000	**Rs '000**	Rs '000	**Rs '000**	Rs '000	**Rs '000**	Rs '000
Revenue										
External income	**19,468,265**	13,487,317	**5,897,725**	946,580	**123,646**	494,613	**610,059**	(365,653)	**26,099,695**	14,562,857
Inter-segment income	**–**	–	**51,794**	62,723	**41,001**	41,424	**–**	–	**92,795**	104,147
Total income	**19,468,265**	13,487,317	**5,949,519**	1,009,303	**164,647**	536,037	**610,059**	(365,653)	**26,192,490**	14,667,004
Segment expenses	**(15,413,846)**	(10,177,421)	**(332,705)**	(408,921)	**(61,300)**	(41,818)	**6,233**	(9,281)	**(15,801,618)**	(10,637,441)
Segment results	**4,054,419**	3,298,270	**5,616,814**	295,684	**103,346**	494,219	**616,292**	189,605	**10,390,872**	4,029,561
Share of associate companies profit before taxation	**–**	–	**–**	4,177	**–**	–	**438,719**	326,616	**438,719**	330,793
Taxation									**(1,275,367)**	(1,092,514)
VAT on financial services									**(622,286)**	(504,960)
Profit after taxation									**8,931,939**	2,762,881
Other information										
Segment assets	**163,474,297**	137,151,887	**8,921,190**	2,392,997	**1,674,283**	1,246,671	**–**	–	**174,069,770**	140,791,555
Investment in associates	**–**	–	**–**	–	**–**	–	**33,301**	1,796,694	**33,301**	1,796,694
Consolidated total assets									**174,103,071**	142,588,249
Segment liabilities	**148,283,244**	124,476,747	**73,581**	182,907	**36,795**	90,714	**–**	–	**148,393,619**	124,750,368
Consolidated total liabilities									**148,393,619**	124,750,368
Segmental Cash flows										
Cash flows from operating activities	**12,235,016**	(6,876,411)	**(95,356)**	49,066	**(712)**	17,882	**260,095**	262,952	**12,399,043**	(6,546,511)
Cash flows from investing activities	**(154,163)**	(909,533)	**196,967**	(97,156)	**37,493**	18,899	**(307,077.76)**	(326,038)	**(226,781)**	(1,313,828)
Cash flows from financing activities	**(6,493,464)**	10,044,260	**(11,907)**	(8,546)	**(36,781)**	(36,781)	**(11,825)**	(40,602)	**(6,553,977)**	9,958,331

52. Related Party Disclosures

52.1 Parent and Ultimate Control Party

The Bank does not have an identifiable Parent of its own.

52.2 Transactions with Key Management and their Close Family Members

Related parties include Key Management Personnel defined as persons having authority and responsibility for planning, directing and controlling the activities of the Bank and its subsidiaries.

Key Management Personnel include the members of the Board of Directors of the Bank, key employees who are holding directorships in subsidiary companies and other key employees who meet the criteria mentioned above.

The Bank carries out transactions with 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.

	2012 Rs '000	2011 Rs '000
52.2.1 Compensation of Key Management Personnel of the Bank		
Short-term employee benefits	**193,331**	111,603
Post-employment benefits (defined contribution)	**7,258**	6,301
Share-based payments (Note 52.2.1.1)	**755**	1,127
	201,344	119,031

In addition to the salaries, the Bank has also provided non-cash benefits such as vehicle, insurance for Key Management Personnel in line with the approved benefit plan of the Bank.

	2012 Rs '000	2011 Rs '000
52.2.1.1 Share-Based Payments to Key Management Personnel		
Share Grant		
No. of ordinary shares held [Note (a)]	**209,848**	209,848
Dividends paid (in Rs '000)	**755**	1,127
No of cumulative grants allocated under the Equity Linked Compensation Plan (ELCP) Tranche 1 (6 July 2010)	**209,848**	209,848

Share Option

As at 31 December 2010, the eligible members of the staff were allocated share options as follows:

209,848 ordinary shares at a price of Rs 124.21 each, was vested on 6 July 2011 and exercisable before 30 June 2014.

Note (a)

At the Annual General Meeting held on 30 March 2011, the shareholders of the Bank approved to increase the number of existing ordinary shares amounting to 82,100,951 by subdividing the said existing ordinary shares in the proportion of one share for every ordinary share in issue so that the number of ordinary shares representing the Stated Capital of the Bank be increased to 164,201,902. Accordingly, the number of shares of the share grant and the share option as at 31 December 2011 and 31 December 2012 was 209,848.

52.2.2 Key management of the Bank and their close family members had the following transactions with the Bank as at 31 December.

	2012 Rs '000	2011 Rs '000
As at		
Residential mortgages	**39,913**	24,807
Credit cards	**1,042**	210
Other loans and advances	**24,395**	15,856
Deposits placed	**228,488**	59,248
For the year		
Interest income	**5,322**	1,171

52.2.3 Transactions involving entities which are controlled/significantly influenced by Key Management Personnel and their close family members.

	31.12.2012 Rs '000	31.12.2011 Rs '000
As at		
Loans and advances	2,767,736	1,579,178
Guarantees/LCs	130,830	66,237
Deposits placed	2,139,049	13,705
For the year		
Interest Income	361,382	104,709
Interest Expense	42,053	1,208
Other Income	10,536	4,659

52.2.4 Direct and Indirect accommodation to Key Management Personnel and their close family members & entities that have significant influence.

Direct and indirect accommodation as a % of the Bank's regulatory capital	19.82	13.62

52.3 Transactions with the Government of Sri Lanka and its Related Entities

A number of entities in which the Government of Sri Lanka has an interest, have a significant interest in the Bank.

The Bank enters into transactions, arrangements and agreements with Government of Sri Lanka and its related entities. The significant financial dealings during the year and as at the Balance Sheet date are as follows:

	31.12.2012 Rs '000
As at	
Loans and advances	2,579,503
Investment	3,224,905
Deposits	23,275
Repo borrowings	1,064,215
Borrowings	700,000
Credit lines	8,555,805
Guarantees	68,468
FX contracts	9,065,250
For the year	
Interest income	367,228
Interest expenses	979,404
Other income	826

Further transactions as detailed below, relating to the ordinary course of business, are entered into with the Government of Sri Lanka and its related entities;

Investments in Treasury Bills, Treasury Bonds
Payments of statutory rates and taxes
Payments for utilities mainly comprising of telephone, electricity and water
Payments for employment retirement benefits - ETF

During the year, the Government of Sri Lanka proposed in the Budget 2013 that certain identified financial institutions including NDB raise long-term foreign development finance up to US$ 250 mn each with a tenure of over 10 years, to provide long-term funding for SMEs, plantations, the construction industry and other manufacturing industries.

52.4 Transactions with Related Entities

52.4.1 The Bank had the undermentioned financial dealings during the year with the following subsidiaries and associates of the Bank.

	Subsidiaries of the Group*				Associates of the Group*			
	Balances as at end of the Year		Average Balance during the Year		Balances as at end of the Year		Average Balance during the Year	
	2012 Rs '000	2011 Rs '000	**2012 Rs '000**	2011 Rs '000	**2012 Rs '000**	2011 Rs '000	**2012 Rs '000**	2011 Rs '000
Loans and advances	**4**	1,263	**634**	674	**–**	453	**226**	7,968
Group company receivables	**1,100**	1,640	**1,370**	820	**–**	–	**–**	678
Deposits placed	**228,502**	1,254,506	**741,504**	1,115,181	**1**	378,800	**189,401**	380,999
Other payables	**2,862**	12,163	**7,512**	10,649	**–**	–	**–**	–
Investment in ordinary shares net of provision for impairment	**2,641,178**	2,770,540	**2,705,859**	2,770,540	**18,525**	286,898	**152,712**	369,679
Disposal of investments	**80,862**	–	**40,431**	–	**268,373**	–	**134,187**	–
Contingencies & commitments	**–**	–	**–**	–	**–**	285,000	**–**	142,500

	Subsidiaries of the Group* during the Year		Associates of the Group* during the Year	
	2012 Rs '000	2011 Rs '000	**2012 Rs '000**	2011 Rs '000
Income Statement				
Interest received/(paid) - net	**(48,282)**	(80,520)	**(22,060)**	(22,580)
Rent and utilities received	**15,477**	12,368	**2,590**	–
Rent and utilities paid	**(18,937)**	(15,582)	**–**	–
Management fees received	**5,788**	17,289	**–**	–
Front end fees received	**952**	5,876	**–**	–
Bancassurance income	**–**	–	**9,251**	27,018
Insurance paid	**–**	–	**(119,947)**	(61,248)
Claims received	**–**	–	**25,813**	28,167
Share brokerages paid	**(1,240)**	(927)	**–**	–
Dividends received	**95,698**	244,821	**–**	12,590
Capital gains received	**501,759**	–	**33,958**	17,300

** Refer Note 28 and Note 29 for details of subsidiary and associate companies.*

52.4.2 The Bank had the undermentioned financial dealings during the year with NDB Provident Fund:

	2012 Rs '000	2011 Rs '000
Deposits with the Bank	**22,908**	44,658
Interest paid on deposits during the year	**2,618**	1,052
Contribution made by the Bank	**138,864**	116,948
Investments in Government Securities	**401,941**	220,809

52.4.3 NDB Wealth Management Ltd., a subsidiary of the Bank had the under mentioned financial dealings with NDB Provident Fund:

	2012 Rs '000	2011 Rs '000
Portfolio balance as at 31 December managed on behalf of NDB Provident Fund	**933,491**	847,442

52.4.4 Direct and indirect accommodation of related companies

Direct and indirect accommodation of subsidiaries and associate companies as a % of the Bank's regulatory capital	**–**	0.01

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, its dealing operations and its human activities, technology and natural incidents. Central Bank of Sri Lanka has prescribed the minimum risk sensitive capital and effective from 1 January 2008 required the Bank to compute the minimum capital in accordance with the 'International Convergence of Capital Measurement and Capital Standards - a Revised Framework' (Basel II). The aim is to ensure minimum capital, commensurate with risks assumed by the Bank, is maintained as a buffer to absorb foreseeable future credit, market and operational losses.

Basis of Computation

The risks weights assigned to the On and Off-Balance Sheet assets and the composition of capital are prescribed by the Central Bank of Sri Lanka.

	BANK	
Capital Base as at 31 December	2012 Rs '000	2011 Rs '000
Tier I: Core Capital		
Stated capital	1,093,095	1,093,095
Statutory reserve fund	878,718	878,718
Published retained profits	6,240,549	4,510,794
General & other reserves	6,730,039	6,192,532
	14,942,401	12,675,139
Deductions - Tier I		
Intangible assets	272,314	278,634
50% investments in unconsolidated banking & financial subsidiaries	1,206,514	1,271,195
50% investments in capital of other banks & financial institutions	9,263	151,575
Total Tier I Capital	13,454,310	10,973,735
Tier II: Supplementary Capital		
General provision	528,401	460,873
Approved subordinated term debt	2,188,350	2,373,300
	2,716,751	2,834,173
Deductions - Tier II		
50% investments in unconsolidated banking & financial subsidiaries	1,206,514	1,271,195
50% investments in capital of other banks & financial institutions	9,263	151,575
	1,215,777	1,422,770
Eligible Tier II Capital	1,500,974	1,411,403
Capital Base	14,955,284	12,385,138

Capital Adequacy

Risk-Weighted Assets and Off-Balance Sheet Exposure

	BANK				
	Principal Amount of On-Balance Sheet Items		Risk Weights	Risk-Weighted Asset Amount	
	2012 Rs '000	2011 Rs '000	%	**2012 Rs '000**	2011 Rs '000
Cash, Treasury Bills & other securities with Central Bank	**29,542,462**	21,942,787	0	**–**	–
Loans against cash deposits & gold	**11,847,144**	7,546,053	0	**–**	–
Claims on banks	**6,719,738**	3,685,237	20-100	**1,673,817**	1,147,889
Claims on financial institutions	**10,811,311**	8,694,418	50-100	**7,156,750**	5,139,402
Loans secured by primary mortgages	**5,446,713**	5,505,536	50	**2,723,356**	2,752,768
Other claims	**89,027,408**	77,264,316	20-150	**82,465,798**	72,570,716
Property & equipment	**856,194**	828,754	100	**856,194**	828,754
Other receivables	**738,471**	1,124,870	100	**738,471**	1,124,870
Total assets considered for credit risk	**154,989,441**	126,591,971		**95,614,386**	83,564,399

Off-Balance Sheet Exposure

	BANK				
	Principal Amount of Off-Balance Sheet Items		Credit Conversion Factor	Credit Equivalent of Off-Balance Sheet Items	
	2012 Rs '000	2011 Rs '000	%	**2012 Rs '000**	2011 Rs '000
General guarantees of indebtedness	**6,304,827**	7,643,592	100	**6,304,827**	7,643,592
Standby LCs relating to particular transactions	**36,193**	18,844	50	**18,096**	9,422
Performance Bonds, Bid Bonds	**2,784,498**	2,210,523	50	**1,392,249**	1,105,262
Trade-related acceptances, advance documents endorsed	**7,370,072**	5,918,368	20	**1,474,014**	1,183,674
Shipping guarantees	**1,186,614**	2,297,673	20	**237,323**	459,535
Documentary letters of credit	**7,124,801**	8,936,444	20	**1,424,960**	1,787,289
Undrawn term loans	**1,399,849**	1,389,401	0, 20 & 50	**693,022**	694,701
FX contracts	**64,384,677**	66,149,182	2 & 5	**1,300,125**	1,385,674
Undrawn overdrafts	**5,838,596**	4,911,290	0	**–**	–
Other unutilized facilities	**42,198,820**	26,786,112	0, 20 & 50	**130,335**	1,010,873
Total Off-Balance Sheet exposure	**138,628,947**	126,261,429		**12,974,951**	15,280,022

Capital Adequacy

	2012 Rs '000	2011 Rs '000
Capital Charge for Market Risk		
Capital charge for interest rate risk	12,544	62,503
Capital charge for equity	–	37,758
Capital charge for foreign exchange & gold	158,255	123,778
Total capital charge for market risk	170,799	224,039
Total risk-weighted assets equivalent for Market Risk	1,707,988	2,240,390
Capital Charge for Operational Risk		
Gross Income:		
Year 1	5,653,829	5,411,883
Year 2	6,681,169	5,653,829
Year 3	8,148,959	6,681,169
Average gross income	6,827,985	5,915,627
Total capital charge for operational risk -15%	1,024,198	887,344
Total risk-weighted assets equivalent for operational risk	10,241,978	8,873,440
Total risk-weighted assets and Off-Balance Sheet exposure	120,539,303	109,958,251
Risk-Weighted Capital Ratios		
Tier I (Required statutory minimum ratio is 5%)	11.16%	9.98%
Tier I & Tier II (Required statutory minimum ratio is 10%)	12.41%	11.26%

	GROUP	
Capital Base as at 31 December	2012 Rs '000	2011 Rs '000
Tier I: Core Capital		
Stated capital	863,937	863,937
Statutory reserve fund	878,718	878,718
Published retained profits	16,410,347	8,989,942
General & other reserves	6,730,039	6,192,532
Minority interests	826,411	912,752
	25,709,452	17,837,881
Deductions - Tier I		
Intangible assets	318,723	318,347
50% investments in the capital of other banks and financial institutions	88,943	986,971
Total Tier I Capital	25,301,786	16,532,563

Capital Adequacy

	GROUP	
Capital Base as at 31 December	**2012 Rs '000**	2011 Rs '000
Tier II: Supplementary Capital		
General provision	**528,401**	460,873
Approved subordinated term debt	**2,188,350**	2,373,300
	2,716,751	2,834,173
Deductions - Tier II		
50% investments in the capital of other banks and financial institutions	**88,943**	986,971
Capital base	**27,929,594**	18,379,765

Risk-Weighted Assets and Off-Balance Sheet Exposure

	GROUP				
	Principal Amount of On-Balance Sheet Items		Risk Weights	Risk-Weighted Asset Amount	
	2012 Rs '000	2011 Rs '000	%	**2012 Rs '000**	2011 Rs '000
Cash, Treasury Bills & other securities with Central Bank	**29,542,538**	21,955,774	0	**–**	–
Loans against cash deposits & gold	**11,847,144**	7,546,053	0	**–**	–
Claims on banks	**6,874,251**	3,808,862	20-100	**1,722,775**	1,196,293
Claims on financial institutions	**11,171,411**	9,791,618	20-100	**7,370,650**	5,775,902
Loans secured by primary mortgage	**5,446,713**	5,505,536	50	**2,723,356**	2,752,768
Other claims	**99,252,404**	78,780,029	20-150	**92,690,794**	74,050,429
Property & equipment	**2,515,678**	2,480,961	100	**2,515,678**	2,480,961
Other receivables	**1,086,268**	1,571,939	100	**1,086,268**	1,571,939
Total assets considered for credit risk	**167,736,407**	131,440,772		**108,109,521**	87,828,292

Off-Balance Sheet Exposure

	Principal Amount of Off-Balance Sheet Items		Credit Conversion Factor	Credit Equivalent of Off-Balance Sheet Items	
	2012 Rs '000	2011 Rs '000	%	**2012 Rs '000**	2011 Rs '000
General guarantees of indebtedness	**6,304,827**	7,643,592	100	**6,304,827**	7,643,592
Standby LCs relating to particular transactions	**36,193**	18,844	50	**18,096**	9,422
Performance Bonds, Bid Bonds	**2,784,498**	2,210,523	50	**1,392,249**	1,105,262
Trade-related acceptances, advance documents endorsed	**7,370,072**	5,918,368	20	**1,474,014**	1,183,674
Shipping guarantees	**1,186,614**	2,297,673	20	**237,323**	459,535
Documentary letters of credit	**7,124,801**	8,936,444	20	**1,424,960**	1,787,289
Undrawn term loans	**1,399,849**	1,389,401	0, 20 & 50	**693,022**	694,701
FX contracts	**64,384,677**	66,149,182	2 & 5	**1,300,125**	1,385,674
Undrawn overdrafts	**5,838,596**	4,911,290	0	**–**	–
Other unutilized facilities	**43,473,820**	26,786,112	0, 20 & 50	**130,335**	1,010,873
Total Off-Balance Sheet exposure	**139,903,947**	126,261,430		**12,974,951**	15,280,022

	2012 Rs '000	2011 Rs '000
Capital Charge for Market Risk		
Capital charge for interest rate risk	**12,544**	62,503
Capital charge for equity	**13,268**	80,831
Capital charge for foreign exchange & gold	**158,255**	123,778
Total capital charge for market risk	**184,067**	267,112
Total risk-weighted assets equivalent for market risk	**1,840,666**	2,671,120
Capital Charge for Operational Risk		
Gross Income:		
Year 1	**6,744,675**	5,996,782
Year 2	**7,929,433**	6,744,675
Year 3	**9,192,963**	7,929,433
Average gross income	**7,955,690**	6,890,296
Total capital charge for operational risk -15%	**1,193,354**	1,033,544
Total risk-weighted assets equivalent for operational risk	**11,933,535**	10,335,445
Total risk-weighted assets and Off-Balance Sheet exposure	**134,858,673**	116,114,879
Risk-Weighted Capital Ratios		
Tier I (Required statutory minimum ratio is 5%)	**18.76%**	14.24%
Tier I & Tier II (Required statutory minimum ratio is 10%)	**20.71%**	15.83%

Economic Value Added Statement

	2012 Rs '000	%	2011 Rs' 000	%
Value Added				
Gross Income	20,124,990		13,533,769	
Cost of Borrowings and Services	(12,974,607)		(8,291,042)	
Impairments Charges for Loans and Other Assets	(106,112)		(67,789)	
Value Addition	7,044,272		5,174,938	
Distribution of Value Added				
To Employees				
Remuneration and Benefits	2,172,740	31	1,838,184	36
To Government				
Taxes	1,682,953	24	1,279,321	25
To Providers of Capital				
Dividend to Shareholders	656,696	9	879,833	17
Retained in the Business				
Retained Profit	2,350,046	33	999,313	19
Depreciation	181,837	3	178,287	3
	2,531,883	36	1,177,600	22
	7,044,272	100	5,174,938	100

Investor Information

1. Stock Exchange

The consolidated Income Statement for the year ended 31 December 2012 and the Balance Sheet of the Bank and the Group as at that date have been submitted to the Colombo Stock Exchange within three months of the Balance Sheet date.

2. Ordinary Shareholders as at 31 December 2012

Individuals

Range (Shareholdings)	No.	Resident Shares	%	No.	Non-Resident Shares	%	No.	Total Shares	%
1 - 1,000	5,268	1,867,058	1.14	65	32,832	0.02	5,333	1,899,890	1.16
1,001 - 10,000	2,128	6,492,962	3.95	58	258,771	0.16	2,186	6,751,733	4.11
10,001 - 100,000	291	7,380,635	4.49	21	600,786	0.37	312	7,981,421	4.86
100,001 - 1,000,000	18	3,166,546	1.93	0	0	0.00	18	3,166,546	1.93
1,000,001 Over	2	5,008,950	3.05	1	8,669,000	5.28	3	13,677,950	8.33
Sub Total	7,707	23,916,151	14.56	145	9,561,389	5.83	7,852	33,477,540	20.39

Corporate

Range (Shareholdings)	No.	Resident Shares	%	No.	Non-Resident Shares	%	No.	Total Shares	%
1 - 1,000	160	54,365	0.03	4	1,826	0.00	164	56,191	0.03
1,001 - 10,000	170	671,904	0.41	5	30,446	0.02	175	702,350	0.43
10,001 - 100,000	108	3,904,469	2.38	8	498,187	0.30	116	4,402,656	2.68
100,001 - 1,000,000	33	11,084,013	6.75	14	6,633,520	4.04	47	17,717,533	10.79
1,000,001 Over	12	75,299,582	45.86	8	27,346,050	16.65	20	102,645,632	62.51
Sub Total	483	91,014,333	55.43	39	34,510,029	21.01	522	125,524,362	76.44
Total	8,190	114,930,484	69.99	184	44,071,418	26.84	8,374	159,001,902	96.83

Notes on unregistered/unallotted shares

Out of the 164,201,902 shares in issue, 5,200,000 shares which were issued in 2006 representing 3.17% are not allotted.

3. Share Valuation

The market value of the National Development Bank PLC ordinary shares on 31 December 2012 was Rs 137.90 per share. The highest and lowest values recorded during this 12-month period were Rs 155.00 on 26 September 2012 and Rs 96.00 on 05 June 2012.

4. Directors' Interest in Shares of NDB

Name	No. of Shares as at 31 December 2012	Name	No. of Shares as at 31 December 2011
H D S Amarasuriya	28,150	H D S Amarasuriya	18,150
A K Pathirage	3,470,000	A K Pathirage	3,470,000
N I R de Mel (CEO)	7,116	N I R de Mel (CEO)	7,116
T L F Jayasekara	–	T L F Jayasekara	–
K Fernando	–	K Fernando	–
H A Siriwardena	–	H A Siriwardena	–
D S P Wikramanayake	–	D S P Wikramanayake	–
G D C Ekanayake	–	G D C Ekanayake	–
S Rajapakse	–	S Rajapakse	–

Investor Information

5. Twenty Largest Registered Shareholders

	As at 31 December 2012		As at 31 December 2011	
Name	No. of Shares	%	No. of Shares	%
1. Bank of Ceylon A/C 1	16,371,076	9.97	16,371,076	9.97
2. Employees' Provident Fund	15,810,248	9.63	14,408,400	8.77
3. Sri Lanka Insurance Corporation Ltd. - General Fund	9,388,488	5.72	9,388,488	5.72
4. Dr S Yaddehige	8,669,000	5.28	8,469,000	5.16
5. Sri Lanka Insurance Corporation Ltd. - Life Fund	7,805,426	4.75	7,805,426	4.75
6. HSBC International Nominees Ltd. - BPSS LUX - Aberdeen Global Asia Pacific Equity Fund	5,715,450	3.48	5,715,450	3.48
7. Employees' Trust Fund Board	5,303,700	3.23	5,284,700	3.22
8. HSBC International Nominees Ltd. - SNFE - NTAsian Discovery Master Fund	4,686,400	2.85	4,152,000	2.53
9. HSBC International Nominees Ltd. - MSNY - Bay Pond Partners LP	4,501,200	2.74	4,501,200	2.74
10. HSBC International Nominees Ltd. - BPSS LDN - Aberdeen Asia Pacific Fund	4,294,800	2.62	4,294,800	2.62
11. Hatton National Bank PLC A/C No. 1	4,282,200	2.61	4,282,200	2.61
12. NDB-ESOP	4,133,726	2.52	4,133,726	2.52
13. Asian Alliance Insurance PLC - Account Number 3/Life Shareholders Fund	3,500,000	2.13	–	–
14. Mr A K Pathirage	3,470,000	2.11	3,470,000	2.11
15. BNY-CF Ruffer Investment Funds: CF Ruffer Pacific Fund	3,000,000	1.83	3,000,000	1.83
16. Asian Alliance Insurance PLC - General Fund A/C 1	2,741,700	1.67	5,732,200	3.49
17. Asiri Hospital Holdings PLC	2,408,136	1.47	2,400,000	1.46
18. HSBC International Nominees Ltd. - MSNY - Bay Pond Investors (Bermuda) LP	2,045,200	1.25	2,045,200	1.25
19. DFCC Bank A/C 1	2,000,000	1.22	2,000,000	1.22
20. HSBC International Nominees Ltd. - BP2S London - Aberdeen Asia Smaller Companies Investment Trust	1,683,000	1.02	683,000	0.42
Total	111,809,750	68.10	108,136,866	65.87

Percentage of Shares held by the Public - 96.12%

6. Debenture Information

In 2011, NDB privately placed rated subordinated unsecured unlisted redeemable debentures having an aggregate face value of Rs 400,000,000/-. The proceeds of these debentures were utilized for lending purposes. The details of the said debentures are as follows:

Date	Amount Rs	Number of Debentures	Value Rs	Redemption	Rate of Interest
30 June 2011	1,000/- each	110,000	110,000,000	30 June 2016	03 months gross TBR + 1.00% per annum
22 July 2011	1,000/- each	290,000	290,000,000	30 June 2016	03 months gross TBR + 1.00% per annum

Ten Year Summary - Group Income Statement

Rs mn	2012	2011	2010	2009	2008	2007	2006	2005	2004	2003
Income										
Net Interest Income	**5,896**	4,909	4,163	4,233	3,787	3,522	2,853	2,693	2,246	2,201
Other operating Income	**9,042**	3,012	2,785	2,560	1,662	1,475	2,133	2,081	1,471	1,405
Total operating income	**14,938**	7,922	6,948	6,793	5,449	4,997	4,986	4,774	3,717	3,606
Impairment charges for loans and other losses	**51**	(88)	(172)	373	116	65	13	153	279	787
Net operating income	**14,887**	8,010	7,120	6,420	5,333	4,932	4,973	4,621	3,438	2,819
Less operating expenses										
Personnel costs	**2,333**	2,118	1,567	1,300	1,151	949	830	1,132	916	588
Other operating costs	**2,163**	1,863	1,496	1,370	1,237	1,104	930	1,645	1,267	818
Total operating expenses	**4,496**	3,981	3,063	2,670	2,388	2,053	1,760	2,777	2,183	1,406
Operating profit before share of associate companies profit before tax	**10,391**	4,030	4,057	3,750	2,945	2,879	3,213	1,844	1,255	1,413
Share of associate companies profit	**439**	331	295	526	172	179	214	22	31	113
Profit before taxation	**10,830**	4,360	4,352	4,276	3,117	3,058	3,427	1,866	1,286	1,526
Taxation	**(1,898)**	(1,597)	(2,175)	(2,154)	(1,409)	(1,421)	(1,220)	(593)	(481)	(305)
Profit after taxation	**8,932**	2,763	2,177	2,122	1,708	1,637	2,207	1,273	805	1,221
Minority interest	**(78)**	(235)	(73)	(37)	(103)	(115)	(176)	(237)	(102)	(98)
Profit attributable to Group	**8,854**	2,528	2,104	2,085	1,605	1,522	2,031	1,036	703	1,123
Earnings per share (Rs)	**55.31**	15.79	12.81	12.75	9.80	9.30	12.40	11.20	6.50	10.40
Final dividend (Rs mn) - proposed/paid	**821**	880	983	553	491	409	327	323	309	309
Interim dividend per share - paid (Rs)	**5.00**	3.50	4.00	–	–	–	–	–	–	–
Final dividend per share - paid (Rs)	**–**	4.00	4.50	8.00	6.75	6.00	4.00	6.00	5.75	5.75
Dividend cover (Times)	**10.78**	2.87	2.19	3.77	3.27	3.72	6.20	3.21	2.28	3.63

Ten Year Summary - Group Balance Sheet

Rs mn	2012	2011	2010	2009	2008	2007	2006	2005	2004	2003
Assets										
Liquid assets	**13,269**	7,651	5,586	8,243	5,883	7,748	6,042	2,917	14,101	12,441
Investments	**35,823**	27,359	20,021	32,128	18,509	14,701	12,170	19,078	5,633	5,726
Loans & advances	**120,986**	102,019	78,452	54,107	54,589	49,818	42,418	36,976	33,387	21,356
Investments in associate companies	**33**	1,797	1,763	1,724	1,393	1,210	1,179	241	225	413
Property & equipment	**1,541**	1,504	918	806	781	804	691	1,162	1,658	1,166
Investment properties	**1,296**	1,296	1,200	1,200	1,200	1,200	1,200	1,041	–	–
Other assets	**1,155**	962	691	1,074	925	662	1,277	3,008	2,446	1,866
Goodwill	**–**	–	4	4	–	–	–	873	1,535	905
Total assets	**174,103**	142,588	108,635	99,286	83,280	76,143	64,977	65,296	58,985	43,873
Liabilities										
Borrowings	**36,630**	38,973	28,631	29,561	34,993	34,147	29,204	27,799	26,881	25,848
Deposits with customers	**107,394**	82,094	60,533	49,948	31,091	25,624	21,161	13,954	11,085	–
Non-life insurance reserves	**–**	–	–	–	–	–	–	859	486	421
Long-term insurance fund	**–**	–	–	–	–	–	–	9,238	7,985	6,613
Taxation	**713**	397	633	560	352	522	640	220	300	351
Other liabilities	**3,657**	3,286	2,826	4,334	3,614	2,750	2,091	2,855	2,778	2,001
Total Liabilities	**148,394**	124,750	92,623	84,403	70,050	63,043	53,096	54,925	49,515	35,234
Shareholders' funds										
Stated capital	**864**	864	864	1,033	1,033	1,033	1,033	760	629	629
Statutory reserves	**879**	879	879	819	819	819	819	546	546	538
Revaluation reserve	**–**	–	–	–	–	–	–	–	86	–
Investment fund	**924**	387	–	–	–	–	–	–	–	–
Revenue reserves	**22,216**	14,795	13,552	12,345	10,811	9,833	8,715	7,850	7,116	6,730
Total shareholders' funds	**24,883**	16,925	15,295	14,197	12,662	11,685	10,567	9,156	8,377	7,897
Minority interests	**826**	913	717	686	568	1,415	1,314	1,215	1,093	742
Total funds employed	**25,709**	17,838	16,012	14,883	13,230	13,100	11,881	10,370	9,470	8,639
Total liabilities and funds employed	**174,103**	142,588	108,635	99,286	83,280	76,143	64,977	65,296	58,985	43,873
Return on average assets (%)	**5.59**	2.01	2.02	2.28	2.01	2.16	3.10	2.00	1.57	3.16
Return on equity (%)	**42.35**	15.69	14.26	15.52	13.18	13.67	21.00	14.30	8.64	15.26
Price earnings ratio (Times)	**2.56**	8.97	13.61	8.09	4.39	9.14	8.10	9.56	12.23	6.84
Book value per share	**151.54**	103.08	93.15	86.72	77.35	71.38	64.54	79.80	77.92	73.46

Branch Network

Region 1

Boralesgamuwa
Borella
Ja-ela
Kadawatha
Kandana
Kiribathgoda
Kotahena
Maharagama
Pettah
Wattala

Region 2

Boralasgamuwa
Athurugiriya
Homagama
Kohuwala
Malabe
Nugegoda
Pelawatte
Piliyandala
Rajagiriya
Kaduwela

Region 3

Colpetty
Colombo 7
Havelock Town
Moratuwa
Mt. Lavinia
Narahenpita
Navam Mawatha
Ratmalana
Wellawatte

Region 4

Ampara
Batticaloa
Chunnakam
Jaffna
Kalmunei
Trincomalee
Vavuniya

Region 5

Anuradhapura
Badulla
Bandarawela
Dambulla
Gampola
Kandy
Kaduruwela
Matale
Nawalapitiya
Pilimathalawa

Region 6

Negambo
Chillaw
Wennappuwa
Kurunegala
Kuliyapitiya
Minuwangoda
Kegalle
Gampaha
Nittambuwa
Puttalam
Wariyapola

Region 7

Akuressa
Aluthgama
Amabalangoda
Ambalantota
Avissawella
Embilipitiya
Galle
Hambantota
Horana
Kalutara
Matara
Mathugama
Panadura
Ratnapura

Glossary of Financial and Banking Terms

A

Accounting Policies
The specific principles, bases, conventions, rules and practices adopted by an entity in preparing and presenting Financial Statements.

Amortization
The systematic allocation of the depreciable amount of an intangible asset over its useful life.

Accrual Basis
Recognizing the effects of transactions and other events when they occur without waiting for receipt or payment of cash or its equivalent.

Associate
An entity, including an unincorporated entity such as a partnership, over which the investor has significant influence and that is neither a subsidiary nor an interest in a joint venture.

Available-for-sale
A debt or equity security that is purchased with the intent of selling before it reaches maturity, or selling prior to a lengthy time period in the event the security does not have a maturity.

B

Bonus Issue (Scrip Issue)
The issue of new shares to existing shareholders in proportion to their shareholdings. It is a process for converting a company's reserves (in whole or part) into issued capital and hence does not involve an infusion of cash.

C

Capital Adequacy Ratios
The relationship between capital and risk-weighted assets as defined in the framework developed by the Bank for International Settlements (BIS) and as modified by the Central Bank of Sri Lanka to suit local requirements.

Capital Reserves
Reserves identified for specific purposes and considered not available for distribution.

Commitments
Credit facilities approved but not yet utilized by the clients as at the Balance Sheet date.

Contingencies
A condition or situation existing at Balance Sheet date where the outcome will be confirmed only by occurrence or non-occurrence of one or more future events.

Cost to Income Ratio
Operating expenses excluding loan loss provision as a percentage of net income.

Corporate Governance
The process by which corporate entities are governed. It is concerned with the way in which power is exercised over the management and direction of entity, the supervision of executive actions and accountability to owners and others.

Correspondent Bank
A bank in a foreign country that offers banking facilities to the customers of a bank in another country.

Cash Equivalents
Short-term highly liquid investments that are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value.

Credit Risk
Credit risk or default risk is most simply defined as the potential that a borrower or counterparty will fail to meet its obligations in accordance with agreed terms and conditions.

Credit Ratings
An evaluation of a corporate's ability to repay its obligations or the likelihood of not defaulting, carried out by an independent rating agency.

D

Deferred Taxation
Sum set aside for tax in the Financial Statements that may become payable/ receivable in a financial year other than the current financial year.

Depreciation
The systematic allocation of the depreciable amount of an asset over its useful life.

Dividend Cover
Profit after tax divided by gross dividends. This ratio measures the number of times dividend is covered by current year's distributable profits.

Dividend Yield
Dividend earned per share as a percentage of its market value.

Documentary Credits
Commercial letters of credit provided for payment by a bank to the named beneficiary usually the seller of merchandise, against delivery of documents specified in the credit.

E

Earnings per Ordinary Share (EPS)
Profit attributable to ordinary shareholders divided by the number of ordinary shares in issue.

Effective Tax Rate
Provision for taxation excluding deferred tax divided by the profit before taxation.

Equity Method
This is a method of accounting whereby the investment is initially recognized at cost and adjusted thereafter for the post-acquisition changes in the investor's share of net assets of the investee. The profit or loss of the investor includes the investor's share of the profit or loss of the investee.

F

Fair Value
The amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction.

Financial Assets
Any assets that is cash, equity instrument of another entity, a contractual right to receive cash or contractual right to receive another financial asset from another entity.

Financial Liabilities
A contractual obligation to deliver cash or another financial asset to another entity or to exchange financial assets or financial liabilities with another entity under conditions that are potentially unfavourable to the entity.

Finance Lease
A contract whereby a lessor conveys to the lessee the right to use an asset for rent over an agreed period of time which is sufficient to amortize the capital outlay of the lessor. The lessor retains ownership of the asset but transfers substantially all the risks and rewards of ownership to the lessee.

Foreign Exchange Profit
Profit earned on foreign currency transactions arising from the difference in foreign exchange rates between the transaction/last Balance Sheet date and the settlement/Balance Sheet date. Also arises from trading in foreign currencies.

Forward Exchange Contract
Agreement between two parties to exchange one currency for another at a future date at a rate agreed upon today.

G

Group
A group is a parent and all its subsidiaries.

Guarantees
Three party agreement involving a promise by one party (the guarantor) to fulfil the obligations of a person owing a debt if that person fails to perform.

H

Held to Maturity
Investments and debt securities that a company has the ability and intent to hold until maturity.

Held for Trading
Debt and equity investments that are purchased with the intent of selling them within a short period of time (usually less than one year).

I

Impairment
This occurs when recoverable amount of an asset is less than its carrying amount.

Intangible Asset
An intangible asset is an identifiable non-monetary asset without physical substance.

Interest in Suspense
Interest suspended on non-performing loans and advances.

Glossary of Financial and Banking Terms

Interest Spread
Represents the difference between the average interest rate earned on interest-earning assets and the average interest rate paid on interest-bearing liabilities.

Investment Property
A real estate property that has been purchased with the intention of earning a return on the investment (purchase), either through rent (income), the future resale of the property, or both.

K

Key Management Personnel
Key management personnel are those persons having authority and responsibility for planning, directing and controlling the activities of the entity, directly or indirectly, including any Director (whether Executive or otherwise) of that entity.

L

Liquid Assets
Assets that are held in cash or in a form that can be converted to cash readily, such as deposits with other banks, Bills of Exchange and Treasury Bills & Bonds.

Impairment Charges for Loan Losses
Amounts set aside against possible losses on loans, advances and other credit facilities as a result of such facilities becoming partly or wholly uncollectible.

M

Market Capitalization
Number of ordinary shares in issue multiplied by the market value of a share as at a date.

Market Risk
This refers to the possibility of loss arising from changes in the value of a financial instrument as a result of changes in market variables such as interest rates, exchange rates, credit spreads and other asset prices.

Materiality
The relative significance of a transaction or an event, the omission or misstatement of which could influence the economic decisions of users of Financial Statements.

N

Net Assets Value per Ordinary Share
Shareholders' funds excluding preference shares, if any, divided by the number of ordinary shares in issue.

Net Interest Income (NII)
The difference between the amount a bank earns on assets such as loans and securities and the amount it pays on liabilities such as deposits, refinance funds and inter-bank borrowings.

Net Interest Margins (NIM)
Net interest income expressed as a percentage of average interest-earning assets.

Non-Controlling Interest
The interest of individual shareholders, in a company more than 50% of which is owned by a holding company.

Non-Performing Loans (NPLs)
A loan or an advance placed on cash basis (i.e. interest income is only recognized when cash is received) because, in the opinion of the management, there is reasonable doubt regarding the collectibility of principal or interest.

Non-Performing Loans Cover (NPL Cover)
Cumulative loan provision as a percentage of total non-performing loans (net of interest in suspense).

NPL Ratio
Total non-performing loans and advances (net of Interest in Suspense) divided by total loans and advances portfolio (net of Interest in Suspense).

O

Open Credit Exposure Ratio
Total net non-performing loans and advances expressed as a percentage of regulatory capital base.

Operational Risk
This refers to the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events.

P

Parent
A parent is an entity that has one or more subsidiaries.

Price Earnings Ratio (P/E Ratio)
Market price of a share divided by earnings per share.

Provision Cover
Total provisions for loan losses expressed as a percentage of net non-performing loans and advances before discounting for provisions on non-performing loans and advances.

R

Related Parties
Where one party has the ability to control the other party or exercise significant influence over the other party in making financial and operating decisions, directly or indirectly.

Return on Average Assets (ROA)
Profit after tax divided by the average assets.

Risk-Weighted Assets
On balance sheet assets and the credit equivalent of off-balance sheet assets multiplied by the relevant risk-weighting factors.

Repurchase Agreement
Contract to sell and subsequently repurchase securities at a specified date and price.

Reverse Repurchase Agreement
Transaction involving the purchase of securities by a bank or dealer and resale back to the seller at a future date and specified price.

Return on Average Equity (ROE)
Net profit for the year, less preference share dividends, if any, expressed as a percentage of average ordinary shareholders' equity.

Revenue Reserves
Reserves that are set aside for future distribution and investments.

S

Segmental Analysis
Analysis of financial information by segments of an entity specifically, the different industries and the different geographical areas in which it operates.

Shareholders' Funds
Total of stated capital and revenue reserves.

Single Borrower Limit (SBL)
33% of the regulatory capital base.

Statutory Reserve Fund
A capital reserve created as per the provisions of the Banking Act No. 30 of 1988.

Substance Over Form
The consideration that the accounting treatment and the presentation in Financial Statements of transactions and events should be governed by their substance and financial reality and not merely by legal form.

Subsidiary
An entity, including an unincorporated entity such as a partnership, which is controlled by another entity (known as the parent).

Swaps
The simultaneous purchase of an amount of a currency for spot settlement and the sale of the same amount of the same currency for forward settlement.

T

Tier I Capital
Core capital representing permanent shareholders' equity and reserves created or increased by appropriation of retained earnings or other surpluses.

Tier II Capital
Supplementary capital representing revaluation reserves, general provisions and other capital instruments, which combine certain characteristics of equity and debt such as hybrid capital instruments and subordinated term debts.

V

Value Added
Value of wealth created by providing banking and other related services, less the cost of providing such services.

Corporate Information

Name
National Development Bank PLC (The Bank was registered under the Companies Act No. 17 of 1982 and subsequently re-registered under the Companies Act No. 07 of 2007 on 4 July 2007).

Registration No.
PQ 27

Legal Form
Incorporated in Sri Lanka under the Companies Act No. 07 of 2007 and also regulated under the Banking Act No. 30 of 1988 as amended from time to time.

Head Office/Registered Office
40, Navam Mawatha, Colombo 2
Tel: 2448448
Fax: 2341044, 2440262
Telex: 21399 NDB CE
Web Page: www.ndbbank.com
E-mail: contact@ndbbank.com
VAT Registration No.: 409000266-7000
Credit Rating: AA(lka) Fitch Rating

Board of Directors
Mr H D S Amarasuriya (Chairman)
Mr A K Pathirage (Deputy Chairman)
Mr N I R de Mel (CEO)
Mr T L F Jayasekara
Mr D S P Wikramanayake
Mrs K Fernando
Mr H A Siriwardena
Ms G D C Ekanayake
Mr S Rajapakse

Integrated Risk Management Committee
Mr D S P Wikramanayake (Chairman)
Mr H D S Amarasuriya
Ms G D C Ekanayake
Mr N I R de Mel
Mrs N Rayen (Head - Group Risk)
Mr F Ozman (CFO)
Mr S S Ganendran (Head - Operational Risk)
Ms C Chandrapala (Head - Market Risk)

Audit Committee
Mr T L F Jayasekara (Chairman)
Ms G D C Ekanayake
Mr D S P Wikramanayake
Mr S Rajapakse
Mrs K Fernando

Strategic Issues Committee
Mr H D S Amarasuriya (Chairman)
Mr A K Pathirage
Mr T L F Jayasekara
Mrs K Fernando
Mr D S P Wikramanayake
Mr S Rajapakse
Mr H A Siriwardena

Remuneration & Human Resources Committee
Mr H D S Amarasuriya (Chairman)
Mr A K Pathirage
Mr S Rajapakse
Mrs K Fernando
Mr H A Siriwardena
Mr T L F Jayasekera

Nominations Committee
Mr H D S Amarasuriya (Chairman)
Mr A K Pathirage
Mr T L F Jayasekara
Mr H A Siriwardena
Mr S Rajapakse

Corporate Governance and Legal Affairs Committee
Mrs K Fernando (Chairperson)
Ms G D C Ekanayake
Mr H A Siriwardena
Mr N I R de Mel

Subsidiary Companies as at 31.12.2012
NDB Capital Holdings PLC
Development Holdings (Pvt) Ltd.
NDB Stockbrokers (Pvt) Ltd.
NDB Investment Bank Ltd.
NDB Capital Ltd. (Bangladesh)
NDB Wealth Management Ltd.
NDB Industrial Estates (Pvt) Ltd.

Associate Companies as at 31.12.2012
Maldives Finance Leasing Co. (Pvt) Ltd.
NDB Venture Investments (Pvt) Ltd.
Ayojana Fund (Pvt) Ltd.

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

Company Secretary
Mrs. Shehani Ranasinghe (Attorney-at-Law)

Auditors
Messrs Ernst & Young
201, De Saram Place, Colombo 10

Bankers
Hongkong & Shanghai Banking Corporation PLC
Citibank
Deutsche Bank AG
Standard Chartered Bank
ANZ
ICICI Bank
Uni Credit Bank AG
Nordea Bank Norge ASA
Bank of New Zealand
Commerz Bank AG

Corporate Information

Bank's History

In January 1979, an Act of Parliament, originally set up the predecessor of National Development Bank PLC, National Development Bank of Sri Lanka, as a wholly state-owned institution. Following a change of ownership structure in 1993, 61% of the share capital of the Bank was transferred to private ownership. In 1997, the Bank 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, the Bank 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 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 save and except for certain provisions contained therein.

On 29 July 2005, the Central Bank of Sri Lanka granted a commercial banking license to the new company whilst withdrawing the specialized banking license that was held by it and on the same day the business operations of NDB Bank Ltd. was taken over by National Development Bank Ltd. In view of this, the shareholders of NDB Bank Ltd. were issued with shares of National Development Bank Ltd. at the ratio of 1 National Development Bank Ltd. share for every 5.6 shares of NDB Bank Ltd. held by them. This resulted in the increase of the issued capital to 54,570,257 shares.

In 2006, the 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 the Bank was further increased by another 27,285,128 shares.

In July 2010, as per the Equity Linked Compensation Plan of the Bank, 245,566 ordinary shares were issued.

In April 2011, the Bank subdivided its existing ordinary shares amounting to 82,100,951 in the proportion of one ordinary share for every ordinary share in issue resulting in 164,201,902 ordinary shares in issue.

The present stated capital of the Bank is Rs 1,093,094,670/-. The shares of the Bank are continuously quoted on the Colombo Stock Exchange.

Pursuant to the provisions in the Companies Act No. 07 of 2007 the Bank was re-registered and is accorded with PQ 27 as the new registration number.

Notice of Meeting

Notice is hereby given that the Eighth (8th) Annual General Meeting of the National Development Bank PLC (NDB) will be held at the DHPL Auditorium, NDB EDB Tower, No 42, Navam Mawatha, Colombo 2 at 10.00 a.m. on the Twenty-Eighth (28th) day of March, Two Thousand and Thirteen (2013) and the business to be brought before the meeting will be:

1. To lay before the shareholders for consideration, the Annual Report for the year ended 31 December 2012.
2. To re-elect in terms of Article 42 of the Articles of Association Mr D S P Wikramanayake, who retires in terms of the said Article 42.
3. To re-elect in terms of Article 42 of the Articles of Association Mr H A Siriwardena, who retires in terms of the said Article 42.
4. To reappoint Messrs Ernst & Young, Chartered Accountants, as Auditors of the NDB as set out in Section 154 of the Companies Act No. 07 of 2007 and Section 39 of the Banking Act No. 30 of 1988 (as amended) and to fix the fees and expenses of such Auditors.
5. To determine the aggregate remuneration payable to Non-Executive Directors including the Chairman in terms of Article 58 of the Articles of Association of NDB and to authorize the Board of Directors to approve other remuneration and benefits to the Directors (including the remuneration of the Executive Director/s) in terms of Section 216 of the Companies Act No. 07 of 2007.
6. To authorize the Board of Directors to determine donations for the financial year 2013 under the Companies Donations Act No. 26 of 1951.

By Order of the Board,

Mrs. Shehani Ranasinghe
Secretary to the Board

Colombo
13 February 2013

Notes:

1. A shareholder entitled to attend and vote at the meeting is entitled to appoint a proxy holder to attend and vote in his/her stead.
2. A proxy holder need not be a shareholder of NDB.
3. The Form of Proxy is sent herewith. The completed Form of Proxy must be deposited at the Head Office of NDB, at No. 40, Navam Mawatha, Colombo 02 not later than 24 hours prior to the time appointed for the holding of the meeting in accordance with Article 29 of the Articles of Association of NDB.
4. Shareholders/Proxy holders attending the meeting are requested to bring their National Identity Cards.

Form of Proxy

National Development Bank PLC

I/We .....
(NIC/s .....) of .....
..... being a member/members of
National Development Bank PLC (the 'NDB') hereby appoint

1. .....
   holder of NIC No. ..... or failing him/her
2. Mr H D S Amarasuriya (Chairman of NDB) of Colombo or failing him,
   Mr A K Pathirage (Deputy Chairman of NDB) of Colombo or failing him,
   Mr T L F Jayasekara of Colombo or failing him,
   Mr D S P Wikramanayake of Colombo or failing him,
   Mrs K Fernando of Colombo or failing her,
   Mr H A Siriwardena of Colombo or failing him,
   Ms G D C Ekanayake of Colombo or failing her,
   Mr S Rajapakse of Colombo or failing him,
   Mr N I R de Mel (CEO of NDB) of Colombo

   as my/our proxy to represent me/us and to vote for me/us and on my/our behalf at the Eighth Annual General Meeting of NDB to be held on twenty-eighth (28th) day of March 2013 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 Thirteen (2013).

.....
Signature of the Member/Members

Instructions for Completion of the Form of Proxy

1. In order to appoint a proxy holder, 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, at No. 40, Navam Mawatha, Colombo 02, not later than twenty-four (24) hours prior to the time appointed for the holding of the meeting.
2. The Proxy Holder appointed need not to be a shareholder of the NDB.
3. In the case of a corporate member, the proxy must be executed under its common seal (if applicable) 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.

Circular to the Shareholders

Dear Shareholder/s,

The Annual Report - Year 2012

As you may be aware, in terms of the revised rules of the Colombo Stock Exchange (the 'CSE') a listed company may issue to its shareholders its Annual Report in a CD-ROM, provided that such company complies with the specified requirements listed in the said rules. An extract of these rules has been set out for the information of our shareholders, on the reverse of this letter.

In pursuance of the said Rules, it was proposed that commencing from the year 2011, the Annual Report of National Development Bank PLC (the 'Bank') will be issued to its shareholders in a CD-ROM, unless a shareholder makes a written request for a printed copy thereof. Where such written request is received by the Company it will send within eight (08) Market Days of such receipt to any requesting shareholder, a printed copy of the Annual Report.

We note from our records that we have not received, as at date, any communication from you requesting for a printed copy of the Annual Report of the Bank. Accordingly, we enclose herewith the said Report for the financial year ended 31 December 2012 contained in a CD-ROM.

If you should, however, still require a printed copy of the said Annual Report, please provide us with a written request therefor. You may for this purpose complete and forward to us the attached Request Form. We shall then, within eight (08) Market Days of the date of our receipt of your request forward to you, a printed copy of the said Annual Report.

In the event that you require assistance relating to the use of the enclosed CD-ROM, you may contact the following persons any time between 10.00 a.m. and 4.00 p.m. on any working day, on the following contact numbers:

Name	Contact Telephone Numbers
Romesh De Silva	011 2448448 Ext.: 3630
Kithunika Nawalage	011 2448448 Ext.: 3625
Mayomi Samarawickrama	011 2448448 Ext.: 3418
Teloma Rodrigo	011 2448448 Ext.: 3407

The Annual Report may also be accessed by shareholders at the Bank's web site - www.ndbbank.com

Shareholders are advised that the Notice convening the Annual General Meeting (AGM) of the Bank, and the related Form of Proxy are also enclosed and if any shareholder is unable to attend the AGM, please return the Form of Proxy to us duly completed, to reach us not later than 24 hours before the time fixed for the said meeting.

If you have any queries on this matter, please call Ms Mayomi Samarawickrama on telephone No. (0094) 11 2448448 (extension 3418), between 10.00 a.m. and 4.00 p.m. on any working day or via email to mayomi.samarawickrama@ndbbank.com.

By Order of the Board of National Development Bank PLC.

Shehani Ranasinghe
Secretary to the Board

Colombo
23 January 2013

Extract of Rule 7.5.b of the Revised Listing Rules of the Colombo Stock Exchange in relation to The Circulation of Annual Reports

"7.5 Circulation of Annual Report

b. Without prejudice to the other provisions relating to issuance of Annual Reports, a Listed Entity may issue its Annual Report in a CD-ROM to its shareholders provided that the Entity complies with the following:

   i. the Listed Entity shall provide a printed copy of the Annual Report to a shareholder, upon such shareholder's request in writing

   ii. the Listed Entity shall designate a person to attend to the shareholders' requests as stated in subparagraph (a) above;

   iii. the Listed Entity shall ensure that a printed copy of the Annual Report is forwarded to the shareholder requesting the Annual Report, within eight (08) Market Days from the date of receipt of the request;

   iv. the Listed Entity shall designate a person/s to answer queries from shareholders relating to the use of the CD-ROM.

   v. Together with the CD-ROM the Listed Entity shall issue a note to the shareholders containing the following statement/information;

      1. that the Listed Entity shall forward a printed copy of the Annual Report to the shareholder requesting such printed copy within eight (08) Market Days from the date of receipt of the written request; and

      2. the Listed Entity's web site and e-mail address, name/s of designate person/s attending to the shareholder's requests and queries and contact number/s; and

      3. a request form to enable the shareholder to request for a printed copy of the Annual Report, with the particulars of the Listed Entity's facsimile number and mailing address."

Request Letter

To:
Company Secretary
National Development Bank PLC
No. 40, Navam Mawatha
Colombo 2

Dear Madam,

National Development Bank PLC
Request for a Printed Copy of the Annual Report - 2012

With reference to the Circular to Shareholders dated 23 January 2013, I/we hereby request you to please forward to me/us a printed copy of the Annual Report of National Development Bank PLC for the year 2012, in addition to the said Report being issued to me/us in a CD-ROM.

Shareholder Details

Full Name of Shareholder _____

Shareholder's NIC/ Passport/
Company Registration No. _____

Shareholder's Address _____

_____

Shareholder's Folio No.
(Please refer to address label) _____

Contact Telephone Number _____

....
Signature *Date*

Notes:

1. Please complete the Request Letter by filling in legibly the required information, signing in the space provided and filling in the date of signature.
2. Please mail or deliver the completed Request Letter to the Board Secretary at the address given above or forward via facsimile to (0094) 11 2440196.
3. In the event the shareholder is a company, the Request Letter should be signed under its Common Seal or by a duly authorized officer of the Company.
4. In the case of joint holders, the Request Letter may be executed by the registered principal holder.
5. If you have any query regarding this Request Letter, please contact the following:

Name	Contact Telephone Numbers
Romesh De Silva	011 2448448 Ext.: 3630
Kithunika Nawalage	011 2448448 Ext.: 3625
Mayomi Samarawickrama	011 2448448 Ext.: 3418
Teloma Rodrigo	011 2448448 Ext.: 3407

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www.carbonfund.org

NATIONAL DEVELOPMENT BANK PLC

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Web: www.ndbbank.com