

HNB Finance PLC

HNB FINANCE

No. 168, Nawala Road, Nugegoda. Tel: 0112 17 62 62 Fax: 0112 17 62 63
E-mail: info@hnbfinance.lk Web: www.hnbfinance.lk

AUDITED FINANCIAL STATEMENTS AS AT 31ST MARCH 2021.
(PUBLICATIONS OF ANNUAL FINANCIAL STATEMENTS).

Income Statement

For the year ended 31 march	2021 (LKR'000)	2020 (LKR'000)
Gross Income	7,167,025	8,291,664
Interest income	6,478,389	8,105,612
Interest expenses	(3,521,400)	(3,719,331)
Net interest income	2,956,989	4,386,281
Fee and commission income	503,021	844,610
Fee and commission expenses	(96,509)	(160,405)
Net fee and commission income	406,512	684,205
Net interest, fee and commission income	3,363,501	5,070,486
Other Operating Income	185,615	219,915
Net mark to market valuation gain	391	178
Total operating income	3,549,507	5,290,579
Impairment Charges for Loans and Other Losses	(1,045,177)	(1,085,863)
Net operating income	2,504,330	4,204,716
Personnel expenses	(1,123,141)	(1,336,693)
Other expenses	(1,455,439)	(1,740,353)
Total operating Expenses	(2,578,580)	(3,077,046)
Operating Profit before Value Added Tax (VAT) , Nation Building Tax (NBT) and Debt Recovery Levy (DRL) on Financial Services	(74,250)	1,127,670
Value Added Tax (VAT) and Debt Recovery Levy (DRL) on financial services	122,057	(442,188)
Nation Building Tax (NBT) on financial services	-	(25,834)
Operating Profit after Value Added Tax (VAT) , Nation Building Tax (NBT) and Debt Recovery Levy (DRL) on Financial Services	(196,307)	659,648
Income tax expenses	72,694	(239,133)
Profit/(loss) for the year	(123,613)	420,515
Basic earnings per share	(0.07)	0.24

Statement of Financial Position

As at 31 March	2021 (LKR'000)	2020 (LKR'000)
ASSETS		
Cash and cash equivalents	645,636	1,502,773
Financial assets- Fair value through profit or loss	16,704	16,193
Financial assets at amortised cost -Loans and advances to customers	18,075,473	17,775,566
Financial assets at amortised cost - Lease rentals receivables and stock out on hire	10,296,416	9,942,882
Financial assets at amortised cost - Loans and advances to others	405,765	584,123
Financial assets measured at fair value through other comprehensive income	2,656	12,430
Financial assets at amortised cost - Debt and other instruments	3,482,765	4,231,143
Other Assets	460,829	421,097
Investment Properties	1,105,000	1,105,000
Intangible Assets	254,264	298,713
Property, Plant & Equipment	1,590,029	1,625,569
Right-of-use assets	257,471	286,728
Deferred Tax Assets	153,988	184,776
Total assets	36,746,995	37,986,993
LIABILITIES		
Financial Liabilities at Amortised cost - Due to Customers	28,046,962	27,528,790
Financial Liabilities at Amortised cost -Debt issued and other borrowed funds	2,636,573	3,822,043
Income Tax Payable	(8,393)	133,467
Value added tax payable	61,155	59,080
Other Liabilities	834,933	1,138,518
Retiring Benefit Obligation	280,858	260,518
Total liabilities	31,852,088	32,942,416
SHAREHOLDERS' FUND		
Stated Capital	223,545	223,545
General Reserve	82,898	82,898
Statutory Reserve Fund	1,091,098	1,091,098
Revaluation Reserve	600,739	591,714
Retained Earnings	2,896,626	3,055,321
	4,894,906	5,044,577
Total equity and liabilities	36,746,995	37,986,993

We, the undersigned, being the Managing Director/Chief Executive Officer and the Chief Operating Officer of HNB Finance PLC certify jointly that,

a) The above Statements have been prepared in compliance with the formats and definitions prescribed by the Central Bank of Sri Lanka.

b) The information contained in these Statements have been extracted from the Audited Financial Statements of HNB Finance PLC.

Signed - B.M.D.C Prabhath
Managing Director/Chief Executive Officer

29 June 2021

Signed - W.S.P Arangala
Chief Operating Officer

29 June 2021

Statement Of Other Comprehensive Income

Year ended 31 March	2021 (LKR'000)	2020 (LKR'000)
Profit/(loss) for the Year	(123,613)	420,515
Other Comprehensive Income for the Year, Net of Tax		
Other comprehensive income to be reclassified to profit or loss in subsequent periods		
Actuarial gain/(losses) on defined benefit plans	25,720	(7,507)
Deferred tax effect on actuarial gains/(losses) on defined benefit plans	(6,173)	2,102
Revaluation Reserve of free hold lands and buildings	-	-
Deferred tax effect on revaluation on lands and buildings	-	-
Pro. For Falling Market Valuation	(9,774)	-
Other Comprehensive Income for the Year, Net of Tax	9,773	(5,405)
Total Comprehensive Income for the Year	(113,841)	415,110

Selected Key Performance Indicators

	As at 31st March 2021		As at 31st March 2020	
	Required	Actual	Required	Actual
Regulatory Capital Adequacy (%)				
Tier 1 Capital Adequacy Ratio (%)	6.50	9.91	6.50	10.16
Total Capital Adequacy Ratio (%)	10.50	14.08	10.50	14.02
Capital Funds to Deposit Liabilities Ratio (%)	10.00	20.75	10.00	18.31
Liquidity (%)				
Available Liquid Assets to Required Liquid Assets (Minimum 100%)		225.36		178.65
Liquid Assets to External Funds		14.43		18.69
Quality of Loan Portfolio (%)				
Gross Non-Performing Loans Ratio (%)		17.68		16.41
Net-Non-Performing Loans Ratio (%)		4.23		2.07
Net-Non-Performing Loans to Core Capital Ratio (%)		34.25		19.08
Provision Coverage Ratio (%)		65.75		80.92
Profitability (%)				
Interest Margin		8.27		15.54
Return on Average Assets (Profit before tax) (%)		(0.33)		1.86
Return on Average Equity (profit after tax)(%)		(2.50)		8.69
Cost to Income Ratio		72.65		58.16
Memorandum Information				
No of Branches		70		69
External Credit Rating (Fitch Rating)		A		AA-



KPMG
(Chartered Accountants)
32A, Sir Mohamed Macan Markar Mawatha,
P. O. Box 186,
Colombo 00300, Sri Lanka.

Tel : +94 - 11 542 6426
Fax : +94 - 11 244 5872
+94 - 11 244 6058
Internet : www.kpmg.com/lk

To the Shareholders of HNB Finance PLC Report on the Audit of the Financial Statements

Opinion
We have audited the financial statements of HNB Finance PLC ("the Company"), which comprise the statement of financial position as at 31st March 2021, and the statement of income, statement of profit or loss and other comprehensive income, statement of changes in equity and statement of cash flows for the year then ended, and notes to the financial statements, including a summary of significant accounting policies set out on pages 6 to 89 in the financial statements.

In our opinion, the accompanying financial statements give a true and fair view of the financial position of the Company as at 31st March 2021, and of its financial performance and its cash flows for the year then ended in accordance with Sri Lanka Accounting Standards.

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

Emphasis of Matter - Restatement of comparative balances

We draw attention to Note 51 to the financial statements which indicates that the comparative balances presented as at and for the year ended 31st March 2020 have been restated and disclosed in these financial statements. Our opinion is not modified in respect of this matter.

Key Audit Matters
Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the financial statements of the current period. These matters were addressed in the context of our audit of the financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

1. Impairment Allowance for Loans, Advances and Lease Rentals Receivables
As disclosed in Notes 18 and 19 to the financial statements, the Company has recorded impairment allowance of Rs. 2,767 Mn relating to loans and advances to customers and Rs. 849 Mn relating to lease rentals receivables as at 31st March 2021.

The determination of provision for impairment allowances using the expected credit loss model is subject to a number of key parameters, key assumptions and judgments, including the identification of loss stages, probability of default (PD), loss given default (LGD), macroeconomic scenarios including their weighting and judgments from the use of data inputs required. These models are reliant on data and a number of estimates including the impact of multiple economic scenarios and other assumptions such as defining a significant increase in credit risk (SICR).

Management judgement is involved in the selection of those parameters and the application of assumptions. Additionally, the COVID-19 pandemic has led the Company to use assumptions regarding the economic outlook becoming more uncertain which, combined with varying government responses, increases the level of judgement required by the Company in calculating the ECL.

Impairment allowance for loans and advances and lease rentals receivables was considered as a key audit matter due to the significance to the financial statements, management assumption, judgements and estimation uncertainty associated with the impairment allowance calculation.

Our audit procedures included:

- Obtaining an understanding of and assessing the design, implementation and operating effectiveness of management's key internal controls related to the measurement of allowance for impairment.
- Evaluating the appropriateness of the accounting policies for ECL and underlying methodology applied based on the requirements of SLFRS 9 with our business understanding and industry practices.
- Evaluating the completeness of customers/facilities assessed individually based on the criteria set for the same and checking the accuracy of the provision for impairment for such identified individually significant exposures.
- Assessing the appropriateness of identified "risk elevated industries" by the management for the identification of SICR of the exposures due to the economic impact of COVID-19 Pandemic and independently calculating the stages of loans based on the set criteria for the collectively assessed exposures. Along with this, we reviewed the reasonableness of the Company's treatment for COVID-19 payment relief customers (moratorium/ debt concessions) in staging the exposure for the collective assessment.
- Assessing the appropriateness of key parameters and assumptions particularly related to the macroeconomic scenarios used in the expected credit loss model by considering the uncertainties pursuant to the COVID 19 outbreak.
- Evaluating the appropriateness and testing the mathematical accuracy of the estimation of allowance for impairment.
- Evaluating the completeness, accuracy and relevance of underlying data used for the calculation of impairment allowance on sample basis by agreeing to the source documents and IT systems.
- Assessing the adequacy and appropriateness of disclosures made in the financial statements with reference to the requirements of relevant accounting standards.

2. IT systems and controls over financial reporting

Risk Description
The Company's key financial accounting and reporting processes are highly dependent on the automated controls over the Company's information systems. Automated accounting procedures and IT environment controls, which include IT governance, controls over programme development and changes, access to programmes and data and IT operations, are required to be designed and to operate effectively to ensure accurate financial reporting.

System calculations including interest calculations and interfaces between business management systems and accounting systems are the significant areas which could result in the financial records being materially misstated.

We identified IT systems and controls over financial reporting as a key audit matter because the Company's financial accounting and reporting systems are fundamentally reliant on complex IT systems and control processes which are driven by significant transaction volumes caused by the size of the customer base.

We used our KPMG IT specialists to perform audit procedures to assess IT systems and controls over financial reporting, which included:

- Obtaining an understanding of and assessing the design, implementation and operating effectiveness of management key internal controls over the continued integrity of all major IT systems fundamental to dealing with the financial data, particularly financial reporting.
- Examining the framework of governance over the Company's IT organisation and the controls over programme development and changes, access to programmes and data and IT operations, including compensating controls where required.
- Evaluating the design, implementation and operating effectiveness of the significant accounts related IT process controls by assessing the operating effectiveness of IT application controls, assessing the operating effectiveness of certain automated controls and system calculations which are relevant to the Company's compliance activities.

- Assessing the availability and stability of key operating systems, taking into consideration the rapid development of businesses types and transaction volumes as well as IT projects that have an impact on the financial reporting process.
- Assessing the management's evaluation of access right granted and removed to applicants relevant to financial accounting and reporting systems.
- Testing preventative controls designed to enforce segregation of duties between users within particular systems.

Other Matter relating to comparative balances

The financial statements of the Company as at and for the year ended 31st March 2020, excluding the retrospective adjustments described in Note 51 to the financial statements, were audited by another auditor who expressed an unmodified opinion on those financial statements on 29th July 2020.

As part of our audit of the financial statements as at and for the year ended 31st March 2021, we also audited the retrospective adjustments described in Note 51 to the financial statements that were applied to restate the comparative information.

We were not engaged to audit, review, or apply any procedures to the comparative information, other than with respect to the retrospective adjustments described in Note 51. Accordingly, we do not express an opinion or any other form of assurance on comparative information. However, in our opinion, the retrospective adjustments described in Note 51 to the financial statements are appropriate and have been properly applied.

Other Information

Management is responsible for the other information. The other information comprises the information included in the annual report but does not include the financial statements and our auditor's report thereon. The annual report is expected to be made available to us after the date of this auditor's report.

Our opinion on the financial statements does not cover the other information and we will not express any form of assurance conclusion thereon.

Responsibilities of Management and Those Charged with Governance for the Financial Statements

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

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

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

Auditor's Responsibilities for the Audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with SLAuSs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

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

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

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

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

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

Report on Other Legal and Regulatory Requirements

As required by section 163 (2) of the Companies Act No. 07 of 2007, we have obtained all the information and explanations that were required for the audit and, as far as appears from our examination, proper accounting records have been kept by the Company.

CA Sri Lanka membership number of the engagement partner responsible for signing this independent auditor's report is 3029.

Chartered Accountants
Colombo, Sri Lanka
29th June 2021

M.R. Mhular FCA
T.S. Rajakarier FCA
Ms. S.M.S. Jayasinghe FCA
G.A.U. Kanunaratne FCA
R.H. Rajan FCA
A.M.S.P. Nalankkone ACA
P.V.S. Perera FCA
W.W.J.C. Perera FCA
W.K.G.C. Jayasinghe FCA
R.M.D.B. Rajapakse FCA
M.N.M. Shanee FCA
C.P. Jayatilake FCA
Ms. S. Joseph FCA
S.T.D.L. Peweera FCA
Ms. B.K.D.T.N. Rodrigo FCA
Ms. C.T.K.N. Perera FCA
Principals - S.R.L., Perera FCA/UKI, LL.B. Attorney-at-Law, H.S. Gooneratne ACA,
Ms. P.M.K.Sumanasekera FCA, W.A.A. Weerasinghe FCA, ACM, MRICS

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