

# Here, Now, Beyond.

HNB, supporting the DREAMS of a NATION





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# Chairperson's Message

Principle D.5



**“The Board, directly and through its Sub-Committees, considered actions to successfully face challenges, manage crisis and harness opportunities while recalibrating strategy, to protect and create value for the Bank and its stakeholders.”**

Dear Shareholders,

Good Corporate Governance is the bedrock for sustainable growth, and I am pleased to present the Corporate Governance Report for 2021.

## **OUR APPROACH TO CORPORATE GOVERNANCE**

The challenges presented by COVID-19 underscored the need for strong Corporate Governance. 2021 continued to test the rigour, resilience, and agility of our governance structures as we sought to drive sustainable growth for HNB in alignment with our Vision and Values, carefully balancing interests of our stakeholders.

The Governance Framework is designed to provide clear direction for responsive and informed decision-making setting the tone at

the top, benchmarked to best practice, the Framework sets out the Bank's commitment to high standards of Corporate Governance reinforced through accountability, strong risk and performance management, transparency, and effective and ethical leadership. We regularly review our framework to adapt to internal and external developments and ensure that it is fit for purpose.

Our Governance Framework references the principles of the Banking Direction No.11 of 2007 on Corporate Governance and the Code of Best Practice on Corporate Governance issued by the Institute of Chartered Accountants of Sri Lanka in 2017. Details of full compliance are set out on CG&RR pages 04 to 41.

## **DELIVERING ON STAKEHOLDER EXPECTATIONS**

The pandemic accelerated the shift towards a more integrated approach to value creation, embracing stakeholder inclusivity and factoring Environmental, Social and Governance (ESG) considerations into decision making. It underscored the need to engage proactively and deeply with diverse stakeholders, both internally and externally, to find win-win solutions, uplifting the socio-economic progress of people and entities as we move forward in step with each other. The Board welcomed the maturity achieved in key stakeholder engagement processes in 2021 despite the continuing challenges.

Internally, ensuring the health and safety of our employees and clients remained our key priority. Protecting jobs, zero wage cuts, mobility and virtual training and development were important concerns that enabled delivery of stakeholder expectations.

We continued to support our clients through this difficult period successfully steering many out of dependency on moratoria. The accelerated development and delivery of innovative digital products on secure platforms supported the digital migration of customers, taking the country towards a new era in financial services. Call centers and relationship management underpinned regular engagement with customers, serving as a key source for insights into issues impacting their progress. Continuous customer surveys conducted by a dedicated Customer Experience Division monitored customer satisfaction which provided insights into areas where we could improve services provided to them.

We also worked closely with the Government and Central Bank of Sri Lanka adapting to regulatory changes as the Government implemented policies to address urgent socioeconomic issues.

## **GOVERNANCE THROUGH THE PANDEMIC**

Clearly defined governance structures enabled the Board to maintain ongoing and effective oversight and leadership as the medium to long-term impacts of the pandemic unfold. The Board received regular updates supported by increased analysis and reporting on key issues affecting the Bank and its stakeholders. Compliance, risk management, recoveries,

and internal control remained key priorities. The Board, directly and through its Sub-Committees, considered actions to successfully face challenges, manage crisis and harness opportunities while recalibrating strategy, to protect and create value for the Bank and its stakeholders.

The increased volume and value of digital transactions, high levels of cybercriminal activities globally and the sophistication of tactics used was a key Board concern. We continue to invest in defending our systems to ensure the resilience of our critical systems, platforms and infrastructures against disruptive cyberattacks. The Board Audit Committee (BAC) and Board Integrated Risk Management Committee (BIRMC) increased the rigour of their oversight on the Bank's IT and the governance processes in place to ensure the efficient delivery of technology and cyber security strategies. Meanwhile, the Board Digital Banking Committee (BDBC) supported the acceleration in the launch of digital innovations and customer value propositions, to successfully increase the Bank's share of digital wallet.

We continue to nurture a culture of risk awareness, underpinned by our embedded risk governance frameworks and a strong focus on training all three lines of defense. The reduced impairment charges and a low Non-Performing Advances ratio reflect our proactive management of credit risk while the significantly lower number of operational risk incidents reflects the strengthening of internal controls, systems and processes. The Board Recoveries Committee continued to provide oversight to the monitoring, management and recovery of overdue loans, driving intensity and focus in managing credit risk and improving asset quality.

## BOARD CHANGES

The range and depth of skills and expertise on our Board has been invaluable as the Bank navigated the pandemic related risks and opportunities effectively. While Board gender diversity improved during the year, Board composition and succession continues to remain an area of focus, as the Board ensures that its composition remains diverse and relevant enabling the effective execution of duties.

On behalf of the Board, I extend my thanks and deep appreciation to, Mr Dinesh Weerakkody for his sound leadership during an unprecedented period in the Bank's history. It is with deep sorrow that we acknowledge the demise of my predecessor, Mr Nilanth De Silva in September 2021. We remember him for his insight and dedicated contribution to the Bank. Mr De Silva was appointed Chairman of HNB in July 2021 and prior to that served as an independent director from April 2015.

I take this opportunity to thank Dr Harsha Cabral, Mr Duliksha Soosaipillai and Mr Rusi Captain for their invaluable contribution to the Bank. We are grateful to Dr Harsha Cabral for having accepted the responsibility of Acting Chairman in April 2021, until a suitable candidate was appointed and to Mr Soosaipillai for his unstinted time and commitment to our Board and numerous Sub-Committees he served on. I thank Mr Devaka Cooray for his role as Senior Independent Director.

I am pleased to welcome Mr Osman Chandrawansa (Independent Non-Executive Director), Mr Rimoe Saldin (Non-Executive Director) and Mr Nihal Jayawardene PC (Non-Executive Director) to the Board. I also welcome Mr Rasitha Gunawardana (Independent Non-Executive Director) and Mr Kithsiri Gunawardana (Non-Executive Director), who have been appointed to the Board since the financial year end. Their appointments add to the Board's expertise and collective experience.

It was an honour to be appointed Chairperson of the Bank in September 2021. I am conscious of the responsibility that comes with the position particularly during this critical period and look forward to leading the Bank to greater heights.

## COMPLIANCE

The Board acknowledges its responsibility to ensure compliance with the laws of the country and have put in place structures, policies and processes to facilitate this. A dedicated Compliance Department reports directly to BIRMC on the subject and report to the Board on key matters. Diligent oversight and a compliance culture nurtured at the Bank support effective compliance with legal and regulatory requirements.

Our aspirations to reach increasingly high standards of ESG compliance takes the HNB Group to a dimension beyond regulatory compliance as we benchmark best practice across a number of topics which are important to the Bank and key stakeholders. I am also pleased to report that there were no deficiencies brought to the notice of the Board by regulators nor payment of fines related to regulatory non-compliance during 2021.

As required by the Code of Best Practice on Corporate Governance, I confirm that I am not aware of any material violations if any of the provisions embodied (i) in the Board Charter, by the Board of Directors of the Bank; or (ii) in the Bank's Codes of Conduct and Ethics, by any member of the Corporate Management team of Hatton National Bank PLC.

## BOARD APPRAISAL

In line with our commitment to adhere to best Corporate Governance practices, a Board effectiveness appraisal was conducted in the second half of 2021. Results were collated by the Company Secretary and made available to the Nomination Committee (NC) and discussed with the Board in May 2021. The outcome of the appraisal indicated that the performance of the Board met expectations. Areas identified for improvement were communicated to the Board.

## LOOKING AHEAD

We will continue to play a key role in providing guidance and oversight in pursuit of the Bank's strategic priorities, while managing the ongoing uncertainties associated with the pandemic. The Board will continue to review the Bank's governance structures to ensure they support effective and ethical leadership and foster sustainable growth while aligning to evolving best practice.



**Aruni Goonetilleke**  
Chairperson

Colombo, Sri Lanka  
18 February 2022

# Corporate Governance Report

## THE BOARD

Principle A.1, A.10

### Executive Directors

#### JONATHAN ALLES



Managing Director / Chief Executive Officer

- » Appointed MD/CEO - July 2013
- » Appointed Director - May 2013
- » Expertise - Banking and Finance



#### DILSHAN RODRIGO



Executive Director / Chief Operating Officer

- » Appointed Executive Director - July 2020
- » Appointed COO - July 2013
- » Expertise - Banking and Finance

### Chairperson

#### ARUNI GOONETILLEKE (MRS)



Chairperson (Independent, Non-Executive)

- » Appointed Chairperson - September 2021
- » Appointed to Board - April 2021
- » Expertise - Legal and Banking & Finance



### Non Executive Directors

#### DAMIEN FERNANDO



Non Executive Director

- » Appointed - October 2018
- » Expertise - Management and Finance



#### RIMOE SALDIN



Non Executive Director

- » Appointed - April 2021
  - » Appointed Alternate Director - July 2018
  - » Expertise - Management and Finance
- (Alternate Director to Rusi Captain from July 2018 to April 2021)



#### DR PRASAD SAMARASINGHE



Non Executive Director

- » Appointed - July 2019
  - » Expertise - Information Technology/ Telecommunication
- (Alternate Director to Damien Fernando)

#### NIHAL JAYAWARDENE PC



Non Executive Director

- » Appointed - August 2021
- » Expertise - Legal



## Independent Non Executive Directors



### AMAL CABRAAL

Independent Non Executive Director

- » Appointed - April 2014
- » Expertise - Management and Marketing



### MADU RATNAYAKE

Independent Non Executive Director

- » Appointed - October 2018
- » Expertise - Information Technology



### DEVAKA COORAY

Independent Non Executive Director

- » Appointed - July 2020
- » Expertise - Accounting and Finance



### OSMAN CHANDRAWANSA

Independent Non Executive Director

- » Appointed - April 2021
- » Expertise - Banking and Finance



## Company Secretary



### THUSHARI RANAWEERA (MRS)

- » Appointed - January 2012
- » Expertise - Legal



## 2021 HIGHLIGHTS

- » Maintained the rigour of oversight in managing the impact and risks on the Bank arising from the COVID-19 pandemic.
- » Approved the issue of Rs. 7 Bn Debentures in July 2021 to increase balance sheet stability and support organisation growth.
- » Improved gender diversity on the Board.
- » Gave oversight to the innovation technology and digital strategy of the Bank while enhancing system security and cyber safeguards.
- » Complied with all regulations and reporting requirements of CBSL responding proactively to the fast-evolving regulatory landscape.
- » Continued to give oversight to the effective monitoring, management and recovery of overdue loans through Board Recoveries Committee.
- » Continued to review the succession planning for the Board, Sub-Committee compositions, KMP including CEO/MD and COO and senior management of the Bank.

## RETIREMENTS/RESIGNATIONS

### DINESH WEERAKKODY

Independent Non-Executive Director

### DULIKSHA SOOSAIPIILLAI

Independent Non-Executive Director

### RUSI CAPTAIN

Non-Executive Director

### DR HARSHA CABRAL PC

Independent Non-Executive Director

### NILANTH DE SILVA

Independent Non-Executive Director

|       |   |
|-------|---|
| BAC   | Board Audit Committee                       |
| HRRC  | HR & Remuneration Committee                 |
| NC    | Nomination Committee                        |
| BIRMC | Board Integrated Risk Management Committee  |
| RPTRC | Related Party Transactions Review Committee |
| SIRC  | Strategy & Investment Review Committee      |

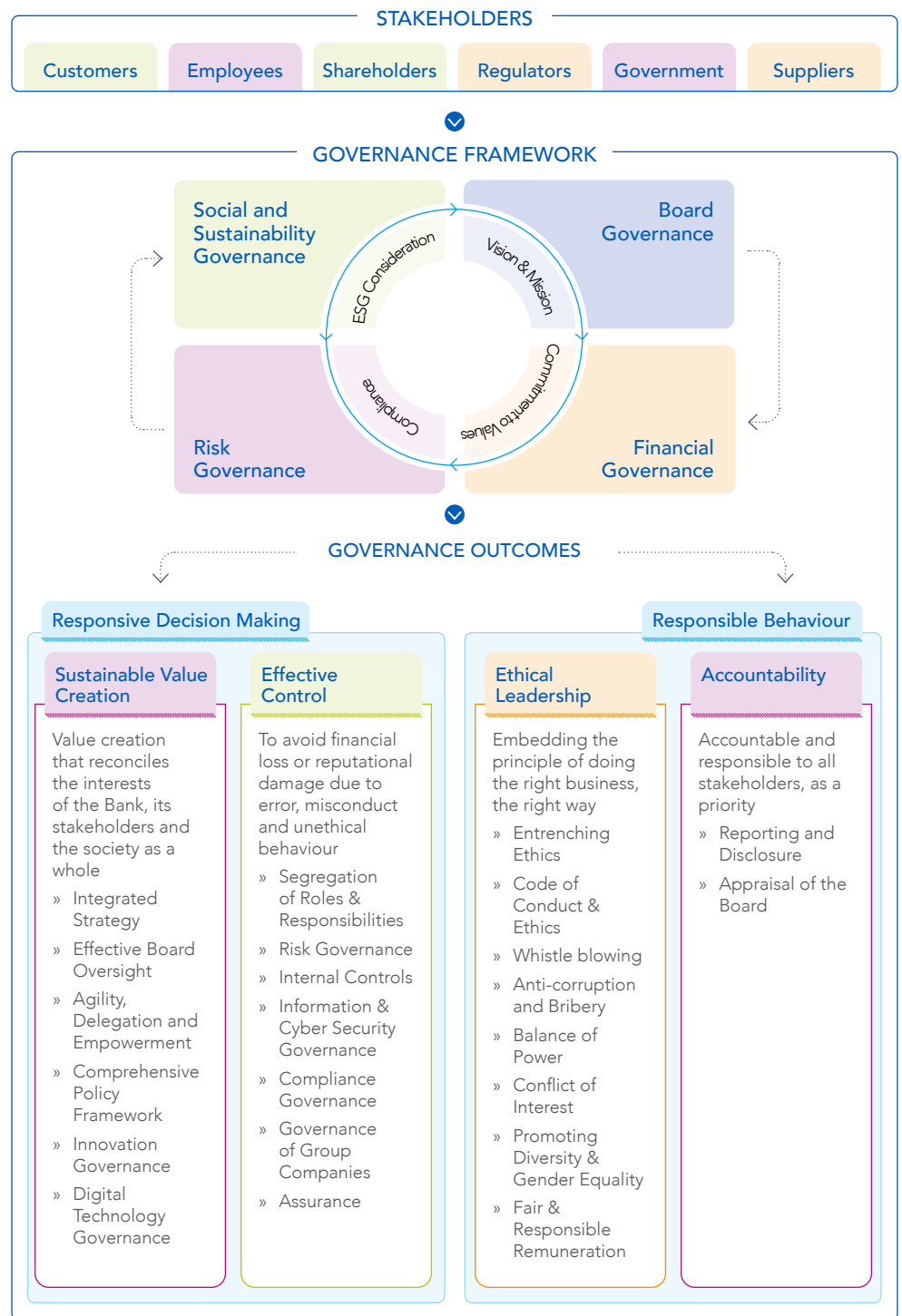
|                      |   |
|----------------------|---|
| PADC                 | Procurement & Assets Disposal Committee |
| BCC                  | Board Credit Committee                  |
| BRC                  | Board Recoveries Committee              |
| BDBC                 | Board Digital Banking Committee         |
| Chairman/Chairperson |   |

# Corporate Governance Report

## 1.0 GOVERNANCE FRAMEWORK

The COVID -19 pandemic and challenges of the socio-economic environment have highlighted the importance of our governance framework and operating practices. Strong leadership, checks and balances at all levels, a clear organisational structure with well-defined lines of responsibility, effective risk management and controls and a values driven ethical culture underpin robust governance structures that provide clear direction for quick and responsive decision-making and promotes responsible behaviour. Our framework supports integrated thinking and decision-making that reconciles the interests of the Bank, stakeholders and society in creating and protecting sustainable shared value.

The Board is the overall custodian of good Corporate Governance and is fully committed to realising the four governance outcomes of sustainable value creation, effective control, ethical leadership and accountability, as depicted in the diagram.





## 1.1 Sustainable Value Creation



- 1.1.1 Integrated Strategy
- 1.1.2 Effective Board Oversight
- 1.1.3 Agility, Delegation and Empowerment
- 1.1.4 Comprehensive Policy Framework
- 1.1.5 Innovation Governance
- 1.1.6 Digital Technology Governance

The Board provides effective oversight, in ensuring sustainable value creation. Our integrated approach reconciles the interests of the Bank, stakeholders and society while Environmental, Social and Governance (ESG) priorities are adopted into policy and strategy formulation.

During the year, our robust governance structures highlighted the resiliency of the Bank, and the ability to be responsive and adaptive in successfully facing challenges, managing crisis and harnessing opportunities. Innovation and digitalisation remain key priorities in driving competitiveness and ensuring our sustainable growth.

### 1.1.1 Integrated Strategy

Principle H.1

The Board provides effective oversight, in strategy formulation and implementation.

In deliberating strategy, the Board adopts a structured and systematic approach to manage our most significant Environmental, Social and Governance (ESG) impacts and addressing the material interests of our priority stakeholders. The Board considers Management updates on stakeholder engagement initiatives undertaken and through reports from Board Sub-Committees. Arising risks and opportunities are continuously assessed and tested against the Bank's vision and values, to ensure that the strategy remains relevant. Processes and systems ensure that the Bank delivers against this strategy.

During the year, the Board remained vigilant, engaging closely with Management in recalibrating the strategic priorities of the Bank to effectively manage crisis, drive resilience, enable recovery and promote long term value creation. Primary focus was on ensuring the health and safety of employees;

adhering to rapid regulatory changes, invoking business continuity plans; ensuring IT systems stability; and supporting clients in managing their finances through this difficult period. ESG practices adopted during the year and the value created are reported in a holistic manner in the Annual Integrated Report 2021.

### 1.1.2 Effective Board Oversight

Principles A.1, A.1.2, A.1.4

The Board plays a key role in creating sustainable value by approving strategy, setting policy, ensuring risk management and capital prudence, and overseeing the Bank's governance frameworks and control environment. The Board's functions and responsibilities are provided for in the Board Charter and defined by legislation.

During the year, the Board continued to take on a leading oversight role in steering the Bank through the pandemic. The Board's firm commitment is demonstrated through their active participation and attendance at Board and Sub-Committee meetings. The Board met more frequently this year (17 times) adopting a hybrid meeting format, where required.

The Bank's governance structure references the principles of the Banking Act, No.11 of 2007 on Corporate Governance and the Code of Best Practice on Corporate Governance issued by the Institute of Chartered Accountants of Sri Lanka in 2017. Details of compliance are set out on CG&RR pages 04 to 41. Respective principles of the Code of Best Practice on Corporate Governance complied with has also been signposted to the Report narrative, to provide further guidance on compliance.

The External Auditors, Messrs. KPMG, have performed procedures set out in Sri Lanka Standards on Related Service 4400 (SLSRS 4400) issued by Institute of Chartered Accountants of Sri Lanka to meet the compliance requirement of the Corporate Governance directive.

The Bank is exempted from disclosure of the CSE listing rules on Corporate Governance as the Bank complies with the Banking Act Direction No.11 of 2007 (as amended) on Corporate Governance for Licensed Commercial Banks in Sri Lanka.

# Corporate Governance Report

The Bank has obtained adequate insurance cover for the Board, Directors and KMP in accordance with the recommendations of the Nominations Committee. The Directors and Officers Liability Policy is renewed annually.

## Board Diversity

Principles A.4, A.5, A.5.1, A.5.2, A.5.3, A.5.4

The Board is well balanced. As at year end, eighty percent (80%) of Directors were Non-Executive and fifty percent (50%) of the Directors are Independent. Non-Executive Directors are eminent professionals in their respective fields. The Board's diversity as demonstrated in this report, has supported varied perspectives and objective evaluation of matters set before them. Leveraging different ideas, skill sets, and experiences the Board has guided the development of effective solutions in navigating the current challenges

Careful succession planning has ensured that the skills and experience of the Board remains relevant to the Bank's needs. The Board adopts a Skills Matrix to support Director recruitment and succession planning. Gender diversity improved with the appointment of Mrs Aruni Goonetilleke during the year.

## Independent Judgement

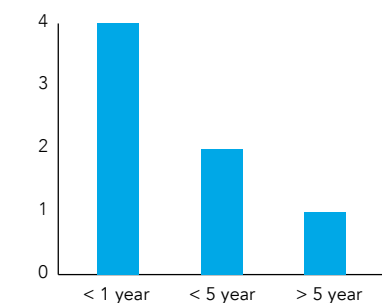
Principles A.1.5, A.5.5

Directors' exercise independent judgement in the effective discharge of duties, engaging in constructive Board discussions and objective evaluation of matters set before them. Directors' demonstrated independence in judgment and character is assessed by the Board as a whole, in the annual Board appraisal and feedback provided.



BOARD COMPOSITION

## Diversity of Non-Executive Tenure



Sufficiently balanced between continuity, new insights, and fresh perspectives.

## Diversity of Expertise



Experienced Board with an appropriate balance of knowledge and skills in areas relevant to the Bank.

"The fundamental role of the Board is to provide entrepreneurial and coherent leadership within a framework of prudent and efficient controls which enables risk to be assessed and managed."

Board Charter



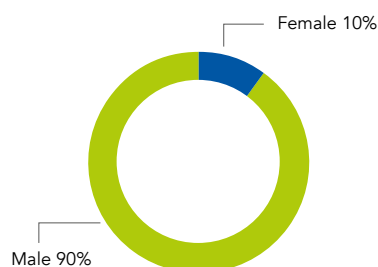
## KEY BOARD RESPONSIBILITIES

- » Provide strategic direction
- » Monitor implementation of strategy
- » Set corporate values and promote ethical behaviours
- » Establish systems of risk management, internal control and compliance
- » Determine Bank's risk appetite and be responsive to the needs of society with focus on environmental, social and ethical standards
- » Meet shareholders, employees and other stakeholder's obligations, balancing their interests in a fair manner
- » Present a balanced and understandable assessment of the Bank's position and prospects
- » Safeguard assets and ensure legitimate use
- » Assess effectiveness of the Board and Sub Committees through self-evaluation
- » Ensure succession planning and the continued ability of the Bank to operate without any disruption

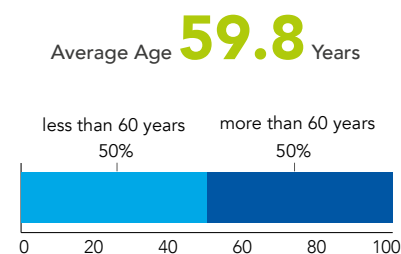
Principle D.1

## Board Gender Diversity

Improved Gender balance



## Diversity of Age



Well-represented, balance in experience and perspectives.



## CHANGES TO THE BOARD

### March 2021

- » Retirement of Mr Dinesh Weerakkody, (Chairman/INED) and Mr Duliksha Soosaipillai (INED) at the close of the AGM
- » Appointment of Dr Harsha Cabral PC (INED) as Acting Chairman

### April 2021

- » Appointment of Mrs Aruni Goonetilleke (NED), Mr Osman Chandarwansa (INED) and Mr Rimoe Saldin (NED) to the Board
- » Retirement of Mr Rusi Captain (NED)

### July 2021

- » Resignation of Dr Harsha Cabral (INED)
- » Appointment of late Mr Nilanth De Silva (INED) as Chairman

### August

- » Appointment of Mr Nihal Jayawardene (NED) to the Board

### September

- » Demise of Mr Nilanth De Silva (Chairman/INED)
- » Appointment of Mrs Aruni Goonetilleke (NED) as Chairperson and Mr Devaka Cooray (INED) as Senior Independent Director

### November

- » Change in status of Mrs Aruni Goonetilleke and Mr Amal Cabraal to Independent Non Executive Directors

### December

- » Resignation of Mr Devaka Cooray (INED) from his role as Senior Independent Director

## Appointments

- » The nomination of directors has been delegated to the Nomination Committee (NC), which recommends the appointment of new Directors for approval by the Board. Such appointments are formal and transparent, and the selection process is conducted under the guidance of an approved policy.
- » When nominating candidates, the NC considers the Board's Skill Matrix, the combined knowledge, experience and diversity of the Board in relation to the Bank's strategic plans, and feedback from the Board Appraisal.
- » On approval, names are referred to the Central Bank of Sri Lanka for approval as a "fit and proper" person, prior to appointment.
- » Appointments are communicated to the CSE and shareholders through press releases together with a brief resume of the Director disclosing relevant expertise, key appointments, shareholding and whether he is independent.
- » Four new directors were appointed to the Board to fill vacancies that arose in 2021. The Committee undertook a thorough process to identify and assess suitable candidates to fill the vacancies created, as disclosed under Succession Planning on CG&RR page 12.

## Re-election/Re-appointment

- » The Articles of Association of the Bank require 1/3 of the Non-Executive Directors to retire from office and stand for re-election by the shareholders at the subsequent Annual General Meeting, subject to completing three (3) years in office from his/her last date of re-election.
- » Mr Damien Fernando and Mr Madu Ratnayake will retire by rotation at the AGM under the Articles of the Association of the Bank and both directors will offer themselves for re-election from the support of the Board at the AGM to be held in March 2022.
- » Mrs Aruni Goonetilleke, Mr Osman Chandarwansa, Mr Rimoe Saldin and Mr Nihal Jayawardene were appointed to the Board in 2021 to fill casual vacancies. Further Mr Rasitha Gunawardana and Mr Kithsiri Gunawardana were appointed to the Board subsequent to the year end to fill casual vacancies. All six (6) Directors appointed to fill casual vacancies will offer themselves for re-election at the AGM to be held in March 2022.
- » The Nomination Committee assesses each Director for their interests, independence and active engagement, prior to recommendation to the Board for re-election.
- » No Director has served on the Board for more than three (3) years from the date of his last appointment, without being subject to re-election/re-appointment at an AGM of the Bank.

## Retirement/Resignation & Director Tenure

- » Director tenure is limited to a maximum term of nine (9) years and an age limit of up to seventy (70) years, whichever comes first in line with the provisions of the Banking Act Direction No.11 of 2007.
- » Resignations or removal of Directors if any, and the reasons are promptly informed to the regulatory authorities and shareholders as per CSE requirements together with a statement confirming whether or not there are any matters that need to be brought to the attention of shareholders.

# Corporate Governance Report

## Independence

- » For a Director to be deemed independent such Director should be independent of management and free of any business or relationship that could materially interfere with or could reasonably be perceived to materially interfere with the exercise of their unfettered and independent judgement.
- » Directors are deemed independent based on the criteria specified in the Banking Act Direction No.11 of 2007. All Directors submit annual declarations to this effect which are evaluated to ensure compliance with the criteria.

## Possess Financial Acumen

- » Directors possess financial acumen and knowledge gained through experience from leading large enterprises and professional backgrounds.

## Digital Savviness


- » Directors, Mr Madu Ratnayake and Mr Prasad Samarasinghe (Alternate Director to Mr Damien Fernando) are digital experts and enhance the Board's skills and knowledge base in technology and information governance, particularly given the Bank's strategic digital transformation combined with the rise in cyber threats that has accompanied the pandemic.

## Active Board Engagement












 Principles A.1, A.7, A.8

The pandemic has heightened the need for more effective management and has emphasized the importance of stronger Board engagement in and oversight of ESG issues. The HNB Board demonstrated their firm commitment to their fiduciary duties and responsibilities, through active participation and attendance in Meetings.

## Board Meetings

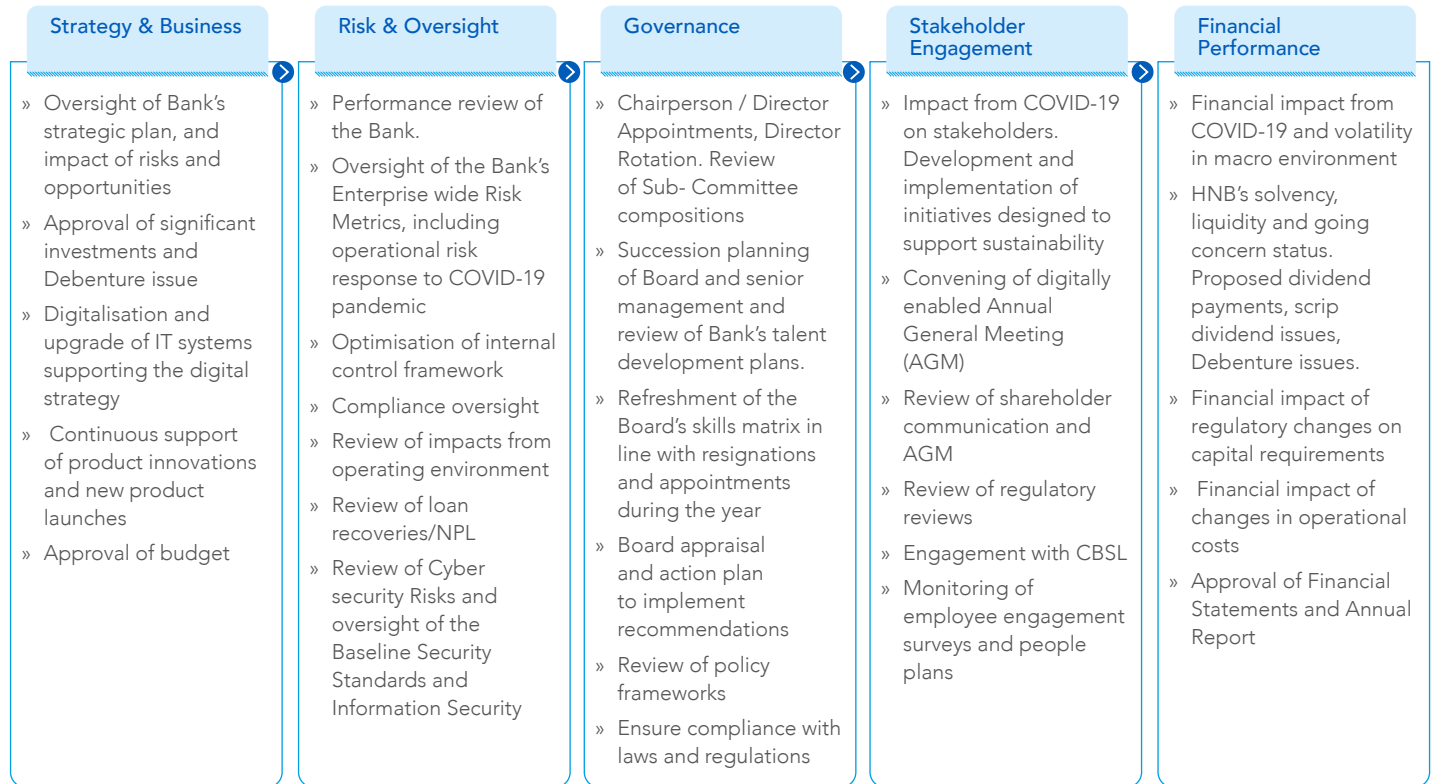
 Principles A.1.1, A.10

Board and Committee Meetings are held regularly, and the Directors ensure that they allocate sufficient time to discharge their duties effectively. Meetings are well chaired and meeting agendas, relevant. The Company Secretarial function supports the Board effectively.

| Board Member   | Date of Appointment to the Board | Board   | Board Audit Committee   | HR & Remuneration Committee   | Nomination Committee  | Board Integrated Risk Management Committee  | Related Party Transaction Committee   | Strategy & Investment Review Committee   | Procurement & Assets Disposal Committee | Board Credit Committee  | Board Recoveries Committee  | Board Digital Banking Committee   |
|--|----------------------------------|---|---|---|---|---|---|--|---|---|---|---|
| <b>Total Meetings Held</b>                                       |                                  | 17  | 8   | 4   | 6   | 10  | 4   | 7  | 11                                      | 5   | 10  | 29  |
| Mrs Aruni Goonetilleke   | 01st April 2021                  |  12/12 | *3  | 2/2   | 1/1   | 6/6   |   | 5/5  |   |  1/1 | 7/7   |   |
| Mr Nilanth De Silva<br>(Until his demise on 29th September 2021) | 30th April 2015                  | 12/12   | 5/5   | 0/1   | 3/3   |   | 2/2   |  |   | 4/4   | 8/9   |   |
| Mr Dinesh Weerakkody<br>(Retired w.e.f 30th March 2021)          | 29th June 2017                   | 5/5   |   | 1/1   | 2/2   |   |   |  |   |   |   |   |
| Mr Jonathan Alles  | 01st May 2013                    | 17/17   | *4  | *4  | *5  | 3/3   | **4/4   | *7   |   | *5  |   | 18/29   |
| Mr Rusi Captain<br>(Retired w.e.f 2nd April 2021)                | 02nd April 2012                  | **6/6   | **3/3   |   | **1/2   | **2/2   | **1/1   |  |   |   |   |   |
| Mr Amal Cabraal  | 01st April 2014                  | 17/17   |   | 4/4   | 3/3   |   |   |  7/7    |   | 5/5   |  10/10 |   |
| Mr Duliksha Soosaipillai<br>(Retired w.e.f 30th March 2021)      | 30th April 2015                  | 4/4   |   | 1/1   |   | 2/2   |   | 1/2  | 2/2                                     |   | 3/3   |   |
| Mr Damien Fernando   | 25th October 2018                | **17/17   | **4/5   |   |   | **10/10   |   | **7/7  | **11/11                                 |   | **5/5   | **27/29   |
| Mr Madu Ratnayake  | 25th October 2018                | 17/17   | 3/3   |  3/3 | 1/1   | *2,8/8  |   | 6/7  | 4/6                                     |   |   |  29/29 |
| Dr Harsha Cabral<br>(Resigned w.e.f 05th July 2021)              | 26th September 2019              | 8/8   |   |   | 5/5   |   |   |  |   | 2/2   | 6/6   |   |
| Mr Dilshan Rodrigo   | 01st July 2020                   | 16/17   | *8  |   |   | *10   |   | *6   | *11                                     | *5  | *9  | *14   |
| Mr Devaka Cooray   | 03rd July 2020                   | 17/17   |  8/8 |   |  1/1 | *9  |  2/2 |  | 6/8                                     | 5/5   |   |   |
| Mr Osman Chandrawansa  | 01st April 2021                  | 12/12   | 5/5   |   |   |   | 3/3   |  |   | 2/2   |   |   |
| Mr Rimoe Saldin  | 30th April 2021                  | 11/11   | 4/4   |   |   |  7/7 |   |  *2,7/7 |   |   |   |   |
| Mr Nihal Jayawardene   | 17th August 2021                 | 6/6   |   |   |   |   | 1/2   |  | 2/3                                     | 1/1   | 1/1   |   |

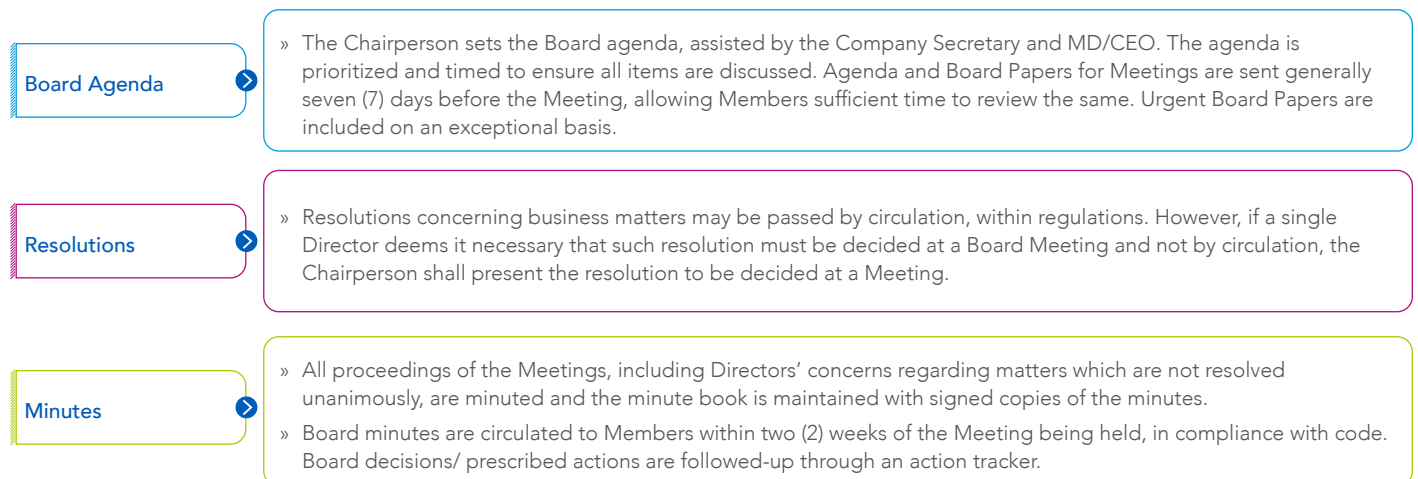
\* Meetings attended by invitation | \*\* Includes Meetings attended by an alternative Director |  Chairman/Chairperson as at 31st December 2021

## Board Focus Areas 2021



## Governance of Meetings

 Principles A.1.7, A.5.10, A.6



# Corporate Governance Report

## Informed Decision Making

Principles A.1.1, A.1.3, A.1.8, A.6

We believe “Better information means better decisions”. The Banks reporting and information systems ensures, the Board receives relevant and objective information, in a timely manner.

### Supply of Information

- » The Board pack, generally circulated seven (7) days in advance of a Board Meeting, provides comprehensive qualitative and quantitative information on matters to be raised at the Board Meeting. This includes reports on the Bank's performance against strategic value drivers and reports on key focus areas such as progress in implementation of Key Projects, the Bank's technology and digitalisation plans, quality of asset portfolio and loan recoveries, risk assessment and impact of COVID-19 on Bank's operations.
- » Further, Corporate Management and external experts make regular presentations regarding the business environment, strategy and operations of the Bank. Deep-dive sessions are held regularly on each business unit's performance supporting strategy development.

### Access to Information

- » Directors have unrestricted access to Executive Management, organisation information, as well as resources required to facilitate discharge of their duties. Access to external specialist advice is available to directors at the Bank's expense, co-ordinated through the Company Secretary. Copies of such advice obtained are circulated to Directors who request for it.

### Knowledge Development

- » On appointment, Directors are provided with a folder containing relevant governance information, including the Bank's founding documents, mandates, legislation and policies. Directors are apprised of the Bank's business and given an opportunity to meet with KMP and visit key branches.
- » Directors' understandings of key matters and risks for the business are supported on an ongoing basis. Board members undertake relevant training as appropriate. They are members of the Sri Lanka Institute of Directors and attend sessions from time to time. Directors also undertake other Continuous Professional Development (CPD) programmes in their personal capacity to update their knowledge on relevant and emerging topics.

## Succession Planning

The Nomination Committee is responsible for succession planning in ensuring continuity and strengthening of the collective skills and experience of the Board. The Nominations Committee continually assesses the Board and its Sub-Committees' composition, against the Board Skill Matrix, to align better to the Bank's strategic objectives, fill identified skills gaps and bring new perspectives to the Board.

During the year, four new Directors were appointed to the Board to fill vacancies that arose in 2021.

The Nomination Committee spent a considerable amount of time in identifying the most suitable candidates and building the right team to guide the Bank into the future. A background search was conducted on the potential candidate and their skills, experience, availability, possible conflicts of interest, likely fit as well as demonstrated integrity, proven leadership and other time commitments.

The Committee also continuously reviewed succession planning efforts at the level of Key

Management Personnel. Similarly, the Human Resources and Remuneration Committee reviewed in-depth the succession planning for identified critical roles of executive management and senior management of the Bank. These succession plans identified emergency successors and also ensured development plans are in place for successors. The respect Committees continue to monitor progress in this regard.

## Company Secretary

Principles A.1.4

The office of the Company Secretary is integral to the effective functioning of the Board. The Company Secretary Ms Thushari Ranaweera, Attorney-at-Law, guides the Board on the execution of their duties, keeping the Board aware of relevant changes in legislation and Corporate Governance best practice. All Directors have access to advise and services of Company Secretary. Appointment and removal of the Company Secretary is a matter for the Board.

### 1.1.3 Agility, Delegation and Empowerment

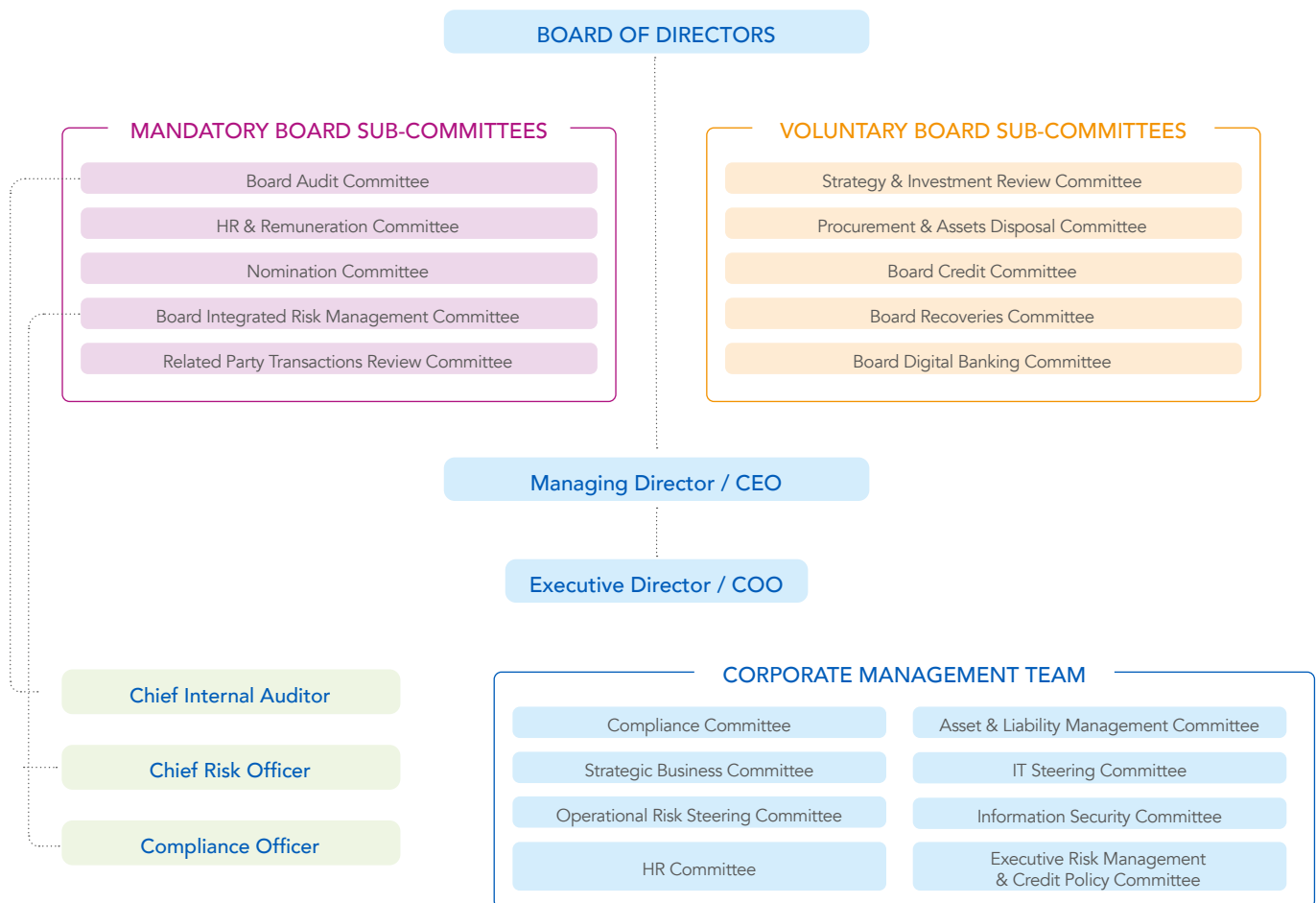
 Principle A.1.6

As the apex governance body, the Board holds ultimate responsibility for the performance and affairs of the Bank. The Board provides strategic direction and leadership and is assisted by ten (10) Board Sub-Committees. Daily management of the Bank and implementation of the Bank's strategic plan has been delegated to the Executive Management lead by the MD/CEO.

Roles and responsibilities are clearly defined by mandates and job descriptions.

Delegation of authority and responsibility within our Governance structures promotes in-depth focus on specific areas, assists with balance of power and the effective discharge of duties in the promotion of Bank's business. Also regular reporting on key matters enables effective oversight by the Board.

Our agility has been a key strength during the year. Close engagement between the Board, Sub-Committees and Executive Management, empowerment and regular reporting has enabled time-critical, informed decision making that has supported the Bank to move swiftly to deliver client specific solutions, capitalise on business opportunities or mitigate emerging threats.



# Corporate Governance Report

## Board Sub-Committees

 Principles A.10, B.1

Delegation of authority to Board Sub-Committees, enables the Main Board to allocate sufficient time to matters reserved for its decision making, while ensuring delegated matters receive in-depth focus. It also allows the Board to capitalise on the specific expertise of individual board members.

The Committees are governed by Board approved mandates. Committee Chairpersons are responsible for the effective functioning of the Committees and after each Committee meeting, the Chairpersons report on the proceedings to the Board, through the Committee minutes included in the Board papers. Please refer the Reports of the respective Committees given on IR pages 96 to 110 for an understanding of their key actions during the year.

### MANDATORY COMMITTEES

#### Board Audit Committee (BAC)

##### *Composition of Directors*

- » Mr Devaka Cooray (Chairman)
- » Mr Osman Chandrawansa
- » Mr Rimoe Saldin

##### *Areas of Oversight*

- » Integrity of financial reporting and disclosures
- » Internal controls and internal audit
- » External audit
- » Compliance

*Report Reference – IR page 106*

#### HR & Remuneration Committee (HRRC)

##### *Composition of Directors*

- » Mr Madu Ratnayake (Chairman)
- » Mr Amal Cabraal
- » Mrs Aruni Goonetilleke

##### *Areas of Oversight*

- » HR Policies including remuneration
- » Organisation values and Code of Conduct
- » Compliance with labour laws
- » HR Systems including performance evaluation, talent management, succession

*Report Reference – IR page 96*

#### Nomination Committee (NC)

##### *Composition of Directors*

- » Mr Devaka Cooray (Chairman)
- » Mrs Aruni Goonetilleke
- » Mr Madu Rathnayake

##### *Areas of Oversight*

- » Selection and appointment of Directors, MD/CEO and Key Management Personnel
- » Expertise gaps, succession, and re-election
- » Board Corporate Governance

*Report Reference – IR page 98*

#### Board Integrated Risk Management Committee (BIRMC)

##### *Composition of Directors*

- » Mr Rimoe Saldin (Chairman)
- » Mr Jonathan Alles
- » Mr Damien Fernando
- » Mr Madu Ratnayake

##### *Areas of Oversight*

- » Comprehensive Risk Management Framework
- » Risk measurement, monitoring and management
- » Compliance with regulatory and internal prudential requirements
- » Review Basel III implementation

*Report Reference – IR page 101*

#### Related Party Transactions Review Committee (RPTRC)

##### *Composition of Directors*

- » Mr Devaka Cooray (Chairman)
- » Mr Jonathan Alles
- » Mr Osman Chandrawansa
- » Mr Nihal Jayawardene

##### *Areas of Oversight*

- » Related Party Transaction Policy
- » Scrutiny of Related Party Transactions
- » Market disclosures on Related Party Transactions
- » Quarterly and annual disclosures of Related Party Transactions
- » Avoidance of conflict of interest

*Report Reference – IR page 109*

# 10

**BOARD SUB-COMMITTEES**



## DISCRETIONARY COMMITTEES

### Strategy & Investment Review Committee (SIRC)

#### Composition of Directors

- » Mr Amal Cabraal (Chairman)
- » Mr Damien Fernando
- » Mr Madu Ratnayake
- » Mrs Aruni Goonetilleke

#### Areas of Oversight

- » Review of economic climate, capital markets activity
- » Economic and monetary policy direction emerging trends and their potential/impact
- » Investment policy
- » Review Bank's investment portfolios and their performance

### Procurement & Asset Disposal Committee (PADC)

#### Composition of Directors

- » Mr Rimoe Saldin (Chairman)
- » Mr Damien Fernando
- » Mr Nihal Jayawardene

#### Areas of Oversight

- » Procurement and Disposal Policy
- » Approve procurements and disposal in line with delegation

### Board Credit Committee (BCC)

#### Composition of Directors

- » Mrs Aruni Goonetilleke (Chairperson)
- » Mr Amal Cabraal
- » Mr Devaka Cooray
- » Mr Osman Chandrawansa
- » Mr Nihal Jayawardene

#### Areas of Oversight

- » Credit Policy and Lending Guidelines
- » Credit risk control measures including pricing of credit risk
- » Performance of credit risk indicators
- » Formulate and periodically review the credit policy
- » Authorise credit facilities over and above the delegated limits of specified categories

### Board Recoveries Committee (BRC)

#### Composition of Directors

- » Mr Amal Cabraal (Chairman)
- » Mrs Aruni Goonetilleke
- » Mr Nihal Jayawardene

#### Areas of Oversight

- » Provide strategic direction for speedy recovery of defaulted facilities
- » Review effectiveness of recovery initiatives deployed
- » Ensure engagement of relevant stakeholders in the recovery process recommend credit and recovery capability requirements to ensure effective management of NPA and recoveries

### Board Digital Banking Committee (BDBC)

#### Composition of Directors

- » Mr Madu Ratnayake (Chairman)
- » Mr Jonathan Alles
- » Mr Damien Fernando

#### Areas of Oversight

- » Provide oversight to the timely and seamless implementation of Bank's proposed Digital Banking Platform/Layer including oversight on related investment components and initiatives
- » Creating a culture of prioritization of customer engagement
- » Escalation of issues to Board for urgent action



## DELEGATION OF AUTHORITY (DLA) FRAMEWORK

### Key Highlights

- » Regular reporting on key matters enables effective oversight by the Board.
- » Management is open and transparent with the Board and escalates concerns to its attention in the appropriate forums and in a timely manner.
- » The Board strives to create an effective balance between meeting the Board's oversight responsibilities and maintaining an entrepreneurial environment in which management can operate.
- » Roles are clearly defined (by mandates and job descriptions) and authority and responsibilities are effectively exercised.
- » Strategically aligned financial and non-financial Key Performance Indicators (KPI) drive performance and the achievement of objectives.
- » All functional departments are headed by competent individuals and are adequately resourced.
- » The Chief Internal Auditor reports directly to the BAC while the Chief Risk Officer and the Chief Compliance Officer report directly to BIRMC ensuring independence of these key functions.
- » Delegated Authority by the Board is reviewed periodically to ensure limits are aligned to the Bank's evolving needs and business context. The Company Secretary monitors the implementation of DLA.

# Corporate Governance Report

## Executive Management

Lead by the MD/CEO, the Executive Management implements corporate strategy and operates the Bank's business. The MD/CEO is supported by the Corporate Management Team (CMT) and Executive Committees. The CMT consists largely of department heads and meets regularly to discuss overall performance of the business, progress on strategic initiatives and top risks. The complementary skills and diverse experience of the CMT strengthens the Bank's ability to deliver on strategy.

Centralization of key operations into dedicated verticals under the transformational initiatives of 2019 and the resulting specialization of roles, has supported quick decision making at the right level of business by the people best placed to take them. Our Key Management Personnel (KMP) are empowered to take decisions within the defined framework and are expected to always act in accordance with the Bank's values and Code of Conduct.

Several Committees have also been established to facilitate co-operation across departments, healthy debate on matters considered critical for the Bank's operations and to improve efficacy in business matters.

All functional departments are headed by competent individuals and are adequately resourced.

### 1.1.4 Comprehensive Policy Framework

 Principle A.1.3

The Bank's strong policy framework serves as a guide to behaviour and decision making at all levels of the organisation. The framework facilitates compliance with laws and regulations while managing stakeholders' expectations and risk. Policy documents are typically modelled against international best practice, appropriate to the Bank's context.

During the year, the Bank commenced the review of its policies to rationalise and simplify the policy framework. The Anti-Corruption & Bribery, Whistle Blowing and Prevention of Harassment Policies were revised in 2021 to meet the evolving needs of the Bank.

### 1.1.5 Innovation Governance

The Bank's ability to continually innovate is critical to differentiate itself and drive competitive within the financial services industry. To this end, the Board has been proactive and enabled innovation from the top as one of its governance responsibilities which encourages a creative and flexible culture that promotes innovative thinking, while managing risk within the agreed appetite.

The Bank leverages digital innovation technology as a means to create and accelerate new opportunities, which trend has accelerated during the COVID-19 pandemic. During the year, we successfully rolled out innovative digital banking solutions that enhanced customer and employee experience while pursuing the Bank's digital transformation strategy. This included the expanded rollout of our digital wallet HNB SOLO and E Banking platform with additional features and functionalities integrated digital solutions such as the Habio Chatbox and the deployment of RPA, AI and cloud technologies that support advanced analytics and drive efficiencies.

### 1.1.6 Digital Technology Governance

 Principle G.1

The Board takes responsibility to implement an effective and properly resourced digital technology strategy. The Board ensures alignment of the IT strategy with the Bank's overall business strategy and monitors implementation against performance targets. The Board monitors and evaluates significant IT investment and expenditure. The Management keeps Board informed for the evolving regulations, governing technology adaption. Technology and information risk is integrated in the Bank's risk management as discussed in Information and Cyber Security Governance on CG&RR Page 18.

The presence of two technology experts on the Board, Mr Madu Ratnayake and Dr Prasad Samarasinghe, an alternative Director to Mr Damien Fernando, has served to enhance the Board's skills base and knowledge of technology governance.

In January 2020, the Board Digital Banking Committee was established to

"The Board would maintain a sound relationship with the executive management which would in turn assist the Board to develop structures, processes and practices that fit the Bank and its business needs."

*Board Charter*

lead implementation of the Bank's digital transformation project and ensure timely and seamless delivery of relevant and prioritized digital solutions. Under the purview of the Committee, the Bank was able to accelerate the delivery of banking solutions to customers through online, mobile and digital channels during the pandemic. Product rollout was prioritized on a needs basis and customized to offer digital solutions for differing customer segments, ranging from retail to SME. The Bank is well positioned to compete and gain an increased share of customers' wallets from these digital channels.

## 1.2 Effective Control



- 1.2.1 Segregation of Roles & Responsibilities
- 1.2.2 Risk Governance
- 1.2.3 Internal Controls
- 1.2.4 Information & Cyber Security Governance
- 1.2.5 Compliance Governance
- 1.2.6 Governance of Group Companies
- 1.2.7 Assurance

By maintaining and regularly reviewing the Bank's structures, systems, policies and procedures, effective control is exercised in avoiding financial loss or reputational damage due to error.

The Bank ensures appropriate and up to date internal financial and management controls are in place. Major risks to which the organisation is exposed including information security and cyber risk, are regularly identified and reviewed, and systems in place to manage those risks. All applicable legal and regulatory requirements are complied with.

### 1.2.1 Segregation of Roles & Responsibilities

*Principles A.2, A.3*

The role of the Chairman/Chairperson is distinct and separate from that of the MD/CEO. There is a clear division of responsibilities as mandated in the Board Charter. The delineation of roles and areas of responsibility within the Governance framework, recognises the independent roles and duties required to effectively govern the Bank, while ensuring no single person has unfettered decision-making powers.

#### Chairman/Chairperson

##### Role

- » Leads the Board, preserving good Corporate Governance and ensuring that it works effectively, acting in the best interests of the Bank at all times.

##### Responsibilities

- » Leading the Board in providing strategic oversight and providing leadership to the Board;
- » Ensuring effective, regular communication with shareholders and their views are communicated to the Board;
- » Ensuring Board's effectiveness, setting its agenda and chairing its Meetings;
- » Ensuring the provision of accurate, timely and clear information to Directors;
- » Ensuring that all Board members understand the information provided and discussed;
- » Ensuring implementation of Board decisions;
- » Ensuring effective communications with shareholders;
- » Facilitating coordination between Board Committees, especially between the Audit, Risk, Credit and Remuneration Committees;
- » Arranging regular evaluation of the performance of the Board, its Committees, and the individual Directors including the Chief Executive Officer;
- » Ensuring the Chief Risk Officer, the Head of Compliance and the Chief Internal Auditor have direct access to the Board;
- » Facilitating effective contribution of all Directors and ensuring constructive relations between Executive and Non-Executive Directors;
- » Addressing the development needs of individual Directors and the Board as a whole, in enhancing Boardroom capital.

#### Managing Director / Chief Executive Officer

##### Role

- » Accountable to the Board for exercise of authorities delegated and for the performance of the Bank.

##### Responsibilities

- » Ensuring proper succession planning of the Corporate Team and assessment of their performance;
- » Developing the Bank's strategy for consideration and approval by the Board;
- » Developing and recommending budgets to the Board to support the Bank's strategy;
- » Monitoring the performance and compliance with regulatory and policy framework and reporting to the Board;
- » Establishing an appropriate organisational structure for the Bank;
- » Setting the tone for ethical leadership and creating an ethical environment;
- » Ensuring a culture that is based on the Bank's values;
- » Ensuring that the Bank operates within the Board's stated risk appetite.

# Corporate Governance Report

## 1.2.2 Risk Governance

 Principle D.2

The overall risk profile of the Bank increased in the period under review, as the pandemic continued to weigh heavily on the economy and society. In response, the Bank enhanced its risk management capabilities to mitigate exposure as described in the Risk & Capital Review given on CG&RR Pages 42 to 87.

Our robust risk management system is governed by mandated Board and Management Committees with appropriate expertise. Through the Board Integrated Risk Management Committee (BIRMC) the Board oversees the Bank's Risk Management Framework (RMF) which includes identifying risks, developing risk strategy, formulating policies, setting procedures, establishing limits and managing exposures, among others. Our well-developed framework supports a consistent approach to risk and capital management. The risk department supports the BIRMC in execution of responsibilities.

During the year, the Board and BIRMC increased the rigor of their oversight functions to effectively and proactively manage risk. The Bank has remained resilient throughout the pandemic, confirming the Bank's strong risk culture.

## 1.2.3 Internal Controls

 Principle D.2

Combined with Risk management, the Board formulates and implements effective internal control systems to safeguard shareholder interests and the assets of the Bank, in meeting strategic objectives. These systems cover all controls, including financial, operational and compliance and are monitored and regularly reviewed for effectiveness by the Board. The Board Audit Committee assists in the discharge of its duties with regards to internal controls, supported by the Internal Audit Department. Details of the internal audit function and systems of internal control are explained in the Board Audit Committee Report given on IR Pages 106 to 108. The Board is satisfied with the integrity of financial information and the robustness of the internal controls and systems of the Bank.

## 1.2.4 Information and Cyber Security Governance

 Principles G.1, G.2, G.3, G.4, G.5

Information and Cyber Security (I&CS) risk remains inherently high as a result of the increase in volumes of digital transactions and remote working vulnerabilities amid the pandemic. High levels of cybercriminal activities globally and the sophistication of tactics used (i.e. phishing) remain a key concern. The Bank is committed to protecting its customers and invests extensively in the I&CS management systems. Information security governance and cyber risk are recurring items on the BIRMC and Board Meeting agendas.

The Information Security Committee (ISC) established under Central Bank of Sri Lanka (CBSL) guidelines, is charged with oversight responsibilities for information security and cyber risk management at corporate level. Key concerns are escalated to the Board.

In meeting the information security objectives and requirements of the Bank, governance structures, policy frameworks and competency of teams were strengthened, and surveillance and monitoring tools enhanced during the year. Key actions taken are described in Information & Cyber Risk on CG&RR pages 67 to 68 of the Risk & Capital Review. To date, I&CS has been well managed.

### Assurance

The Board obtains assurance of the I&CS management systems through annual audits performed for critical banking systems and in compliance with security standards and from independent assessments of specific projects on a needs basis. These are conducted by external auditors and cyber security experts.



## INFORMATION SECURITY POLICY STATEMENT

It is the policy of Hatton National Bank PLC that its information assets shall be protected from all threats identified, whether internal or external, advertent or inadvertent, such that the brand is protected; confidentiality of information is maintained; integrity of information can be relied upon; availability of information is ensured; and all legal, regulatory, statutory and contractual obligations are met.

## Chief Information Security Officer (CISO)

The CISO provides leadership to the Bank's overall information security function and has been responsible for establishing the information and cyber security strategy and formulating road maps for implementation. The CISO was appointed last year, following the Bank's decision to separate this critical role from the CRO, who was, until then, responsible for managing vulnerabilities within the Bank's IT on-premises and cloud infrastructures.

### 1.2.5 Compliance Governance

 Principle A.1.3

Responsibility and accountability for compliance management rests with the Board. Through the Board Integrated Risk Management Committee (BIRMC), the Board reviews the adequacy of the Bank's systems of governance and risk including ensuring that appropriate controls are in place to confirm compliance with applicable laws, regulations, codes of conduct and standards. Implementation of an effective compliance framework has been delegated to the Compliance Officer, who reports directly to the BIRMC, ensuring the independence of this key function.

During 2021, the Bank had to meet the rapidly evolving and increasingly stringent regulatory requirements, particularly following Government's efforts to introduce regulations and policies to manage the impact of the pandemic and the Central Bank of Sri Lanka (CBSL) intensified surveillance on financial crime, focused on Anti-Money Laundering and Countering the Financing of Terrorism (AML/ CFT) activities. The Bank remained extra vigilant, expanding the scope and rigor of processes to mitigate emerging threats and ensure compliance with regulations.

Continued investments in new systems and platforms such as the CBSL initiated GoAML system and International Transaction Reporting System (ITRS), digital tools including advanced analytics using Artificial Intelligence (AI) solutions, and set up of a Compliance Audit team strengthened the compliance function and improved efficacy in prevention, detection, and reporting.

The Bank maintains a zero tolerance approach for non-Compliance with the regulatory requirements.

### 1.2.6 Governance of Group Companies

The Board seeks to establish a common standard of Corporate Governance across Group subsidiaries and is guided by the Board approved Charter for Management/

Good Governance for Group Companies. Alignment of governance practices and processes is reinforced by the appointment of Bank Directors and/or Corporate Management Members to the Boards of subsidiaries. In strengthening the overview of Group subsidiaries, the MD/CEO meets with Subsidiary heads and KPI, on a quarterly basis.

### 1.2.7 Assurance

The Board ensures that assurance services and functions enable an effective control environment, and that support the integrity of information for internal decision making and of the Bank's external reports. The Board Audit Committee (BAC) on behalf of the Board reviews the plans and work outputs of both external and internal auditors, coordinating activities to adopt a combined assurance model.

The BAC is responsible for overseeing the adequacy of the performance of the internal audit function and of its resources. It reviews and approves the annual audit plan and reviews the significant issues raised during the internal audit processes and the adequacy of corrective action taken in response to such findings.

In respect of the external auditors and the external audit, BAC recommends the appointment of auditors to the shareholders and oversees the external audit process. The Committee remains satisfied with the independence, impartiality, competence, resources, service levels and objectivity of the External Auditor, Messrs. KPMG Chartered Accountants in rendering their services. Please refer the BAC Report on IR pages 106 to 108.

Further, the Bank's whistle-blower policy enables any internal and external stakeholder to inform the Bank of matters of concern that may require internal investigation.

# Corporate Governance Report

## 1.3 Ethical Leadership

 Principle D.5



- 1.3.1 Entrenching Ethics
- 1.3.2 Code of Conduct & Ethics
- 1.3.3 Whistleblowing
- 1.3.4 Anti-Corruption and Bribery
- 1.3.5 Balance of Power
- 1.3.6 Conflict of Interest
- 1.3.7 Promoting Diversity and Gender Equality
- 1.3.8 Fair and Responsible Remuneration

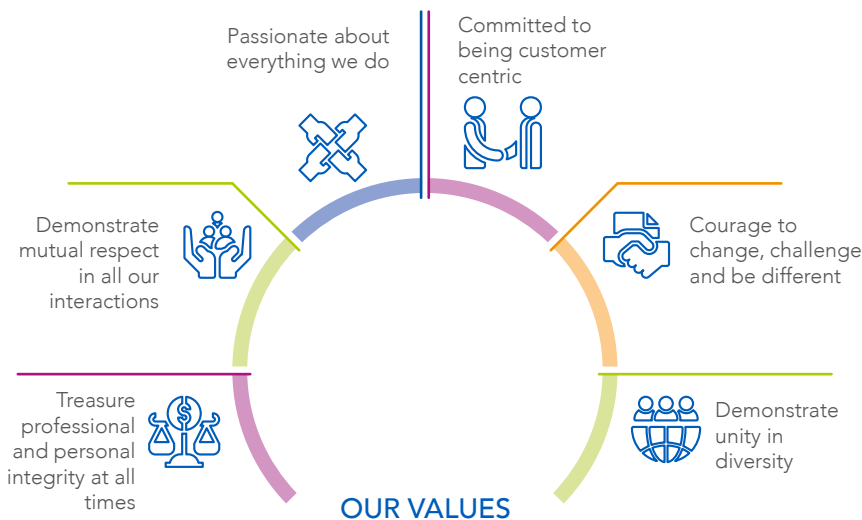
HNB conducts its business dealings in an ethical and sound manner, doing the right business in the right way. To this end, the Board assumes ultimate responsibility for a sound strategy and business offering that treats customers fairly, a commonly accepted and lived set of values and demonstrated ethical leadership.

### 1.3.1 Entrenching Ethics

The Board and Corporate Management set the tone from the top, ensuring their conduct is aligned to the Bank's values and Code of Conduct & Ethics and that these inform decision-making across the organisation. In executing their duties, Board members are transparent and act with integrity and fairness.

To ensure our employees understand our approach to ethics, we have in place a comprehensive portfolio of policies and frameworks including an Employee Handbook (as explained below) to be guided by.

Our Values and Code of Conduct guide the way we conduct our business and shapes organisational culture.



### HNB CONDUCT AND CULTURE POLICIES

- » Anti-Bribery and Corruption Policy
- » Anti-Harassment Policy
- » Employee Recognition and Rewards Policy
- » Employee Share Trading Policy
- » Equability and Diversity Policy
- » Grievance Handling Policy
- » Industrial Relations Policy
- » Management and Resolution of Complaints Policy
- » Whistleblowing Policy
- » Health & Safety Policy

Through frequent employee engagement around ethical behaviour, the Bank seeks to deter non-compliance and reduce exposure to unethical opportunities. All business units and corporate functions staff are required to 'declare' all gifts (received and given), as well as to declare any conflicts, or potential conflicts of interest, on a quarterly basis. The Compliance Officer tables reports on compliance to the Board Integrated Risk Management Committee (BIRMC) and the Board regularly and any non-compliance issues are highlighted for necessary action/advice.

Awareness and implementation are supported by mandatory training and by incorporating criteria into the annual performance review objectives, incentivising employees for living our values. Accordingly, the Bank's Remuneration Policy is aimed at ensuring that reward processes support and reinforce our required culture and encourage ethical behaviour.

### 1.3.2 Code of Conduct & Ethics

The Bank's Employee Handbook encompassing the Code of conduct & Ethics is a key element of the Bank's ethical framework. It provides employees with practical guidance on how to behave, outlines acceptable conduct and empowers them to make faster, more confident decisions within clearly defined parameters. Key topics covered are given alongside. The Handbook is being reviewed to refresh it with timely and relevant information to fit in to the present context, including updates on behaviour at work, work life balance, use of social media, information security, talent development, etc. HNB employees receive training on compliance with the Code as part of their induction process and regular refresher training.

The Handbook is communicated and adhered to by all employees. Directors also abide by a 'Standard of Conduct' embodied in the Board Charter.

The Board is not aware of any material violations of any of the provisions of the Code of Conduct and Ethics/Standard of Conduct by any Director or KMP of the Bank.

### 1.3.3 Whistleblowing

All employees are responsible for ensuring that their behaviour, and that of the Bank,

reflects HNB's values, principles and policies. If any internal or external stakeholder believes that the Bank has contravened these commitments, they are encouraged to make disclosures in good faith, without fear of victimisation or prejudice, under the provisions of our whistleblowing policy. All reports are confidential, and reporters are able to submit their disclosure(s) anonymously. Information on accessibility, anonymity, processes and the policy relating to the whistle blowing service is communicated to all employees.

Mr Devaka Cooray, Independent Non-Executive Director, was appointed by the Board to handle whistle blowing matters since October 2020. There were no significant incidents or compliance breaches in the period under review, with matters highlighted through whistleblowing receiving urgent executive attention and action. The whistle blower policy was revised during the year to incorporate minor amendments.

### 1.3.4 Anti-Corruption and Bribery

The Bank is firmly opposed to all forms of corruption. Our Bribery and Anti-Corruption Policy, explicitly

1. Requires all employees including officers and Directors, to fully comply with all applicable laws and regulations of the country including, anti-corruption laws.
2. Strictly prohibits all employees to offer, give or accept bribes, facilitation payments, kickbacks, unacceptable gifts, hospitality or expenses or political contributions of any kind, either directly or indirectly when carrying out Bank's transactions and business dealings. Gifts, hospitality or expenses deemed as "Acceptable" is provided for in the Policy.
3. Requires all employees to ensure that the books and records of the Bank are kept accurately and sufficiently clear, detailed and timely.

As disclosed above, the Bank's Code of Conduct and Ethics, also embodies provisions of the Anti-Corruption and Bribery policy. Employee awareness of the Policy and reinforcement of desired behaviour is enhanced through structured communication of the Code and training conducted at induction. The policy is further supported through internal control systems



## HNB CODE OF CONDUCT & ETHICS

- » Act ethically, responsibly, honestly and with integrity, in the best interests of the Bank
- » Safeguard the Bank from fraud, corruption, collusion and coercion
- » Compliance with laws, rules and regulations
- » Avoidance of conflict of interest
- » Discrimination and harassment
- » Bribery and corruption
- » Confidentiality
- » Fair dealing
- » Entertainment and gifts
- » Accurate accounting and record keeping
- » Fair and transparent procurement practices
- » Protection and proper use of Bank assets including information assets
- » Encourage whistleblowing
- » Corporate opportunities

# Corporate Governance Report

and procedures for the effective countering of corruption in areas where bribery and corruption risk may be present.

The Policy provides guidelines on how to identify and deal with issues related to bribery and corruption.

All concerns are reviewed, assessed, and where necessary, investigated, and if a breach of the Anti-Corruption and Bribery Policy is substantiated, appropriate disciplinary action is taken.

## 1.3.5 Balance of Power

 Principles A.5.7, A.5.9

Arrangements for delegation to Board Sub-Committees and a clear division of roles and responsibilities assist with the balance of power. Key roles of the Chairperson and MD/CEO are separate as disclosed on CG&RR page, strengthening the Board's effectiveness, and ensuring objective decision making in the discharge of duties.

Concurrent to the appointment of Mrs Aruni Goonetilleke, Non-Executive Director as Chairperson of the Bank on 29th September 2021, Mr Devaka Cooray Independent Non-Executive Director was appointed as Senior Independent Director in line with regulations 3.5 (ii) of the Banking Direction No.11 of 2007 on Corporate Governance.

In the absence of the Chairperson, the Senior Independent Director leads the Board. He acts

as intermediary between the Chairperson and other members of the Board if necessary, and chairs discussions and decision making by the Board on matters where the Chairperson has a conflict of interest.

The Chairman/ Chairperson meets the Non-Executive Directors without the Executive Directors being present, as necessary. The Chairman met the Non- Executive directors without the Executive Directors once during 2021.

## 1.3.6 Conflict of Interest

 Principle A.10

Directors are required to declare any personal financial interests that pose a conflict of interest through a formal disclosure process at appointment and quarterly thereafter. It is a standing agenda item at every Board meeting. Where conflicts of interest may exist, Directors are expected to excuse themselves from Meetings. The Directors' share dealing policy also requires a declaration of interests. This is strictly applied and maintained.

The Board is aware of the other commitments of its Directors and is satisfied that all Directors allocate sufficient time and attention to enable them to discharge their responsibilities at HNB effectively.

The Related Party Transactions Review Committee (RPTRC) reviews and provides oversight over Related Party Transactions to











ensure transactions are fair and in the best interests of HNB. The Committee is guided by the Bank's Related Party Transactions Policy and applicable regulations.

Key appointments of the Directors are included in their profiles on IR pages 70 to 75 and Related Party Transactions are disclosed in note 60 of the Financial Statements on IR pages 318 to 324. The total number of Board seats (excluding Directorship in HNB) held by each Director as of 31st December 2021 is given in the below table.

## 1.3.7 Promoting Diversity & Gender Equality

### Diversity and equal opportunity

HNB appreciates the positive impact to balance and perspective that diversity in leadership and functional teams lends, boosting effectiveness, resilience, and improving competitiveness. The Bank believes diversity is a significant driver of innovation while an inclusive workplace provides equal opportunity for all. The Board has in place policies that promote fair representation, equal opportunity and a safe workplace.

| Name of Director       | Directorship Status   | No. of Board Seats held in Listed Companies |                        | No. of Board seats held in Unlisted Companies |                        |
|------------------------|---|---|------------------------|---|------------------------|
|                        |   | Executive Capacity                          | Non-Executive Capacity | Executive Capacity                            | Non-Executive Capacity |
| Mrs Aruni Goonetilleke |  | -   | 2                      | -   | 2                      |
| Mr Jonathan Alles      |  | -   | -                      | -   | -                      |
| Mr Amal Cabraal        |  | -   | 4                      | -   | 13                     |
| Mr Damien Fernando     |  | -   | 1                      | -   | 3                      |
| Mr Madu Ratnayake      |  | -   | -                      | 1   | 3                      |
| Mr Dilshan Rodrigo     |  | -   | 2                      | -   | 3                      |
| Mr Devaka Cooray       |  | -   | 2                      | 1   | 8                      |
| Mr Osman Chandrawansa  |  | -   | -                      | -   | -                      |
| Mr Rimoe Saldin        |  | -   | 2                      | 3   | 10                     |
| Mr Nihal Jayawardene   |  | -   | -                      | -   | -                      |

 Independent Non-Executive Director |  Executive Director |  Non-Executive Director



### Gender Representation

HNB remains committed to improve gender representation across the Bank. The Bank's family-friendly workplace practices support employees, who are also caregivers, in creating a balance between their professional and family priorities.

Board representation improved during the year with the appointment of Mrs Aruni Goonetilleke as a Nonexecutive Director in April 2021. Her subsequent appointment as Chairperson of the Bank on the demise of Mr Nilanth De Silva, is noteworthy and reflective of the Bank's policy on gender parity. By year end, female employees accounted for 43% of the overall workforce (2020: 43%) and 21% of senior management positions (2020: 22%).

### Women's empowerment and Responsible branding

The Bank has been at the forefront of women's empowerment in Sri Lanka actively supporting women's advancement and forging gender parity. HNB's women-centric product schemes have sought to drive financial inclusion and economic independence of women. Initiatives such as "Gami Pubuduwa" provides access to personalized finance and microfinance products and enhanced financial literacy and management ability among women entrepreneurs. In marketing these products, the Bank has been conscious of portraying women with respectful and realistic reflections.

### 1.3.8 Fair & Responsible Remuneration

 Principles B.1, B.2

#### Remuneration Policy and Procedure

The Board strives to ensure that remuneration is fair, responsible and transparent. The HRRC has been mandated to make recommendations to the Board regarding remuneration of the Executive Directors and KMP.

### Remuneration Level and Makeup

Remuneration packages are designed to attract eminent professionals with the requisite skills and experience. Remuneration is structured taking into consideration performance and risk factors entailed in the job and is competitive in comparison with our peers. It encompasses a variable pay component tied to the achievement of the Bank's business objectives, which objectives are defined by key business metrics that are consistent with HNB's growth strategy and will deliver long-term shareholder value. MD/CEO participates at Meetings when deciding the remuneration of the Corporate Management team.

Remuneration of Executive Directors are compliant with the provisions of Schedule E of the Code of Best Practice on Corporate Governance issued by the Institute of Chartered Accountants of Sri Lanka in 2017.

No special early termination clauses are included in the contract of employment of Executive Directors that would entitle them to extra compensation. However, such compensation, if any, would be determined by the Board of Directors.

The Board as a whole determines the remuneration of the NED's who receive a fixed fee for being the Chairman/Chairperson or a Director of the Board and an additional fee for being a Member of a Committee.

#### Professional Advice

Independent professional advice is sought when required, by the Board/HRRC on matters within its purview.

#### Remuneration Disclosures

Refer IR page 215 for the total Directors' Remuneration.



### PROMOTING DIVERSITY

Our policies seek to harness the full potential of all our employees by providing equal opportunity and a safe environment, in the workplace.

- » Equality and Diversity Policy
- » Employee Recognition and Rewards Policy
- » Anti-Harassment Policy
- » Grievance Handling Policy
- » Management and Resolution of Complaints Policy
- » Health & Safety Policy
- » Code of Conduct & Ethics

### REMUNERATION POLICY

The Bank's remuneration philosophy and policies are designed to attract, retain and motivate employees to meet the Bank's strategic objectives, and to give them due recognition.

# Corporate Governance Report

## 1.4 Accountability



### 1.4.1 Reporting and Disclosure

### 1.4.2 Appraisal of the Board

As a trusted corporate leader committed to high standards of business integrity and ethics, being accountable and responsible, to all stakeholders is a priority. The Board ensures accountability through robust disclosure practices, striving for open, transparent and reliable communication with both internal and external stakeholders. The Annual Report and the AGM are key forums for external communication of the Bank's performance during the year. Meanwhile, the annual appraisal supports self-accountability, facilitating the Board to evaluate whether its objectives are being met.

Board Sub-Committee Chairman/ Chairperson are accountable for the effective functioning of their respective Committees. Reports of the Committees are provided on IR pages 96 to 110.

#### 1.4.1 Reporting and Disclosure

 Principles C.1, C.2, D.1, E,F

HNB is committed to fair and transparent reporting with emphasis on integrity, timeliness and relevance of information disclosed. Information is presented in such a manner as to avoid the creation of a false market. Such disclosure and reporting enable stakeholders to effectively assess performance and take informed decisions.

The Bank's Corporate Communication Policy provides guidelines to ensure all communications to key stakeholders are coherent and cohesive. Covering internal and external communication, the policy has been communicated to all staff members and sets out formal areas of responsibility. The Corporate Communication Policy was revised in 2021.

All reporting and disclosures are in compliance with applicable laws and regulations.

#### *Shareholder Engagement and the Annual General Meeting (AGM)*

Shareholders are engaged through multiple channels of communication, including the Annual General Meeting (AGM), annual report, interim financial statements, a dedicated investor relations page on the Bank's website, press releases in 3 languages in the main newspapers and notification of key events through announcements in the CSE.

The AGM provides an opportunity for the Board to interact with and be accountable to our shareholders and for our shareholders' views to be heard and fully considered. Notices of the Meetings are circulated to shareholders within the timeframes established by law and are also available on the Bank's investor relations webpage. The notice regarding the AGM includes the Annual Report and Accounts, resolutions to be considered at the meeting together with the corresponding information, a summary of the

procedures governing voting at the AGM and how shareholders can access the AGM.

At the AGM, the Board provides an update to shareholders on the Bank's performance. Shareholders are then offered an opportunity to ask questions. The Chairman, Board Members including the Chairman of the Sub-Committees such as Audit, Remuneration, Nomination & Related Party Transactions and External Auditors were present to answer any queries.

All Shareholders are encouraged to participate at the AGMs and exercise their voting rights. The Bank has a mechanism to record and count all proxy votes lodged for each resolution.

In response to the COVID 19 pandemic restrictions imposed on physical attendance of public gatherings by the Sri Lankan Government, and social distancing rules observed, the AGM 2021 was conducted for the second time as a hybrid meeting at a physical location as well as via an extended teleconference facility, in line with the prevailing health and safety standards examined by the Government authorities. The Board ensured that shareholders were given the opportunity to submit questions ahead of the AGM or in real time on the AGM platform, with all questions being carefully considered and answered individually by the Chairman, MD/CEO, Board members and KMP present. Voting was concluded on a show of hand by those physically present, while shareholders participating via electronic platform were able to vote by means of MS Teams - forms tool.

| Mode of Participation | No of Shareholders | No of Shares Presented | % of Shareholding |
|-----------------------|--------------------|------------------------|-------------------|
| In person             | 50                 | 397,128                | 0.10%             |
| By Proxy              | 64                 | 303,958,468            | 74.08%            |
| Total represented     |                    | 304,355,596            | 74.18%            |

### Annual report and interim financials

The Annual Report is the key medium through which the Board presents a fair and balanced review of the of the Bank's financial position, performance and prospects combining narrative and visual elements to facilitate readability and comprehension. External audit/ third-party assurance has been obtained where relevant, to enhance credibility. The Board of Directors review and approve the Annual Report, prior to publication while the Interim Financials are reviewed and recommended by the Board Audit Committee and approved by the Board of Directors, prior to publication. The high standard of reporting maintained by the Bank is evidenced by the awards received over an extended period.

### Investors Meetings

The Board and KMP continually meet with institutional investors and equity analysts on financial performance and strategic matters. As in 2020, this year too, investor roadshows were hosted virtually and primarily to promote the HNB Debenture Issue 2021. The Board believes that such communication leads to mutual respect, accountability and trust. It also enables the Board to exercise constructive influence, as and when appropriate, and to protect the interests of our minority shareholders. Directors ensure the protection of share price sensitive information at these Meetings.

### Shareholder access to corporate information

Shareholders may, at any time, direct questions, request for publicly available information and provide comments and suggestions to Directors or Management of the Bank. Such questions, requests and comments should be addressed to the Company Secretary. The Company Secretary maintains a record of all correspondence received and deliver as soon as practicable such correspondence to the Board or individual Director/s as applicable. The Board or individual Director/s, as applicable, will generate an appropriate response to all validly received shareholder correspondence, if it deemed appropriate, and will direct the Company Secretary to send the response to the particular shareholder.

### 1.4.2 Appraisal of the Board

 Principles A1.8, A.9

An appraisal of the Board is conducted annually to support continued improvement in performance and effectiveness. The evaluation outcomes are used as a base to build leadership capability, affirm best practices, identify where challenges lie, remove obstacles to better performance while reinforcing and supporting continuous improvement. Overseen by the Chairman/ Chairperson, Directors assess their collective performance against measures including the independence of Directors, in judgement

and character, boardroom dynamics, and the Bank's strategy.

The 2020 appraisal was held in April 2021. Results were collated by the Board Secretary and made available to the Nomination Committee. The outcome of the appraisal indicated that the performance of the Board met expectations. Areas identified for improvement were communicated to the Board, including training needs.

Similarly, a self-evaluation of each Board Sub-Committee is carried out annually by the respective Committee Chairman/Chairperson and circulated amongst the members of the Committee for necessary action. Summary of the results are submitted to the Board.

### Appraisal of the MD/CEO

 Principle A.11

The performance of the MD/CEO is assessed annually using criteria aligned to the short, medium and long-term objectives of the Bank which are agreed with the MD/CEO at the beginning of the year. The appraisal is discussed by the Chairman/Chairperson with the MD/CEO and responses documented prior to approval by Board as a whole. HRRC assists in the evaluation process, recommending a revised remuneration based on performance.

# Corporate Governance Report

## APPENDIX I: COMPLIANCE WITH BANKING DIRECTION NO.11 OF 2007 ON CORPORATE GOVERNANCE

| Section   | Principle, Compliance & Implementation   |
|-----------|--|
| 3 (1)     | <b>Responsibilities of the Board</b>   |
| 3 (1) (i) | <p><b>Strengthening the safety and soundness of the Bank</b></p> <p>The Board's responsibilities are set out in the Board Charter. The Board is accountable for the management of the affairs of the Bank and the safety and soundness of the Bank.</p> <hr/> <p><b>a. Setting Strategic Objectives and Corporate Values - Complied <input checked="" type="checkbox"/></b></p> <p>The Bank's strategic objectives derived from the Vision and Mission Statements and its corporate values, have been determined and approved by the Board of Directors and communicated to all levels of staff through multiple channels. The corporate values are included in the Code of Conduct &amp; Business Ethics which is provided in hard copy to all new employees is available on the intranet, explained at orientation programmes. It is made available on the intranet and reinforced at Meetings.</p> <hr/> <p><b>b. Approving Overall Business Strategy including Risk Policy and Management - Complied <input checked="" type="checkbox"/></b></p> <p>The business strategy (Corporate Strategic Plan) together with the projections covering 2021 - 2023 was approved by the Board in 2021. The strategy and execution thereof, is regularly reviewed by the Board. The Annual budget, derived from the business strategy is approved after discussing in detail with the corporate management and monitored periodically, by the Board.</p> <p>The Board also approved the overall risk strategy of the Bank, determining the Risk Appetite, Policies and Risk Management Framework &amp; Mechanisms. The Corporate Strategic Plan is aligned to the overall risk strategy of the Bank, where Risk Appetite is considered in areas such as capital allocation and in the adoption of risk matrix to measure the risk levels. Governance and Compliance which are embedded in the Risk Management Policy Framework have also been included in the strategic plan. Further, the risk management procedures and mechanisms with time bound implementation milestones were approved and monitored by the Board Integrated Risk Management Committee (BIRMC) on a regular basis.</p> <hr/> <p><b>c. Risk Management - Complied <input checked="" type="checkbox"/></b></p> <p>The Board takes overall responsibility for risk management of the Bank. The BIRMC, is tasked with assisting the Board in structuring the Bank's Risk Policy, defining the risk appetite, identifying principal risks, setting governance structures and implementing systems to measure, monitor and manage the principal risks.</p> <p>The following reports provide further insights in this regard:</p> <ul style="list-style-type: none"><li>» Risk &amp; Capital Review on CG&amp;RR pages 42 to 87.</li><li>» Board Integrated Risk Management Committee Report on IR pages 101 to 105.</li></ul> <hr/> <p><b>d. Communication with all Stakeholders - Complied <input checked="" type="checkbox"/></b></p> <p>The Board has approved a Corporate Communication Policy to ensure effective and timely communication with all stakeholders including depositors, creditors, shareholders and borrowers. The Corporate Communication Policy, which was reformulated in 2016 (revised in 2021), is guided by the principles of efficiency, transparency, proactivity, clarity and feedback. Investor forums, AGMs are used for communication with stakeholders in addition to responding to specific investor queries. Shareholder engagement is described on CG&amp;RR page 24.</p> <p>The Bank has substantially implemented the provisions of Banking Act Directions No 8 of 2011 "Customer Charter of Licensed Banks", which became effective in 2012. The Charter seeks to improve the quality and content in dispensing of customer service by enhancing customer protection and instilling trust and confidence in the Bank while incorporating a set of customer obligations generated in the interests of Bank stability.</p> <hr/> <p><b>e. Internal Control System and Management Information Systems - Complied <input checked="" type="checkbox"/></b></p> <p>The Board reviews the adequacy and the integrity of the Bank's Internal Control Systems and Management Information Systems and is satisfied with same. It is assisted in this regard by the Board Audit Committee (BAC). The BAC has reviewed reports from the Internal Audit Department in carrying out this function, together with the Management responses on the same. The findings have been reported to the Board.</p> |

| Section | Principle, Compliance & Implementation |
|---------|--|
|---------|--|

**f. Key Management Personnel (KMP) - Complied**

KMP are defined in the Sri Lanka Accounting Standard – LKAS 24 on “Related Party Disclosures”, as the persons who significantly influence policy, direct activities and exercise control over business activities, operations, and risk management. All appointments of designated KMP are recommended by the Nomination Committee and approved by the Board.

For financial reporting purposes, the Board of Directors of the Bank is considered as KMP of the Bank.

For Corporate governance reporting and monitoring purposes, Key Management Personnel comprise the Corporate Management (MD/ CEO, COO, DGMs and AGMs), Chief Technology & Digital Officer, Head of Custody & Trustee Services as per the guideline on “Key Management Personnel in Banking Act Direction for Corporate Governance” issued by the Banking Supervision Department of CBSL. All appointments of Key Management Personnel are recommended by the Nomination Committee and approved by the Board.

**g. Define areas of authority and key responsibilities for Directors and Key Management Personnel - Complied**

Areas of authority and key responsibilities for the Board of Directors are set out in the Board Charter. Areas of authority and key responsibilities for Key Management Personnel are stated in their Job Descriptions as recommended by the Nomination Committee and approved by the Board. The delegated authority limits for Key Management Personnel have been approved by the Board.

**h. Oversight of affairs of the Bank by Key Management Personnel - Complied**

The MD/CEO and other Key Management Personnel are accountable to the Board for the Bank’s operational and financial performance, in accordance with the policies set by the Board. The Board reviews the performance of the Bank against the strategic plan and receives reports from its Sub-Committees on matters delegated to them, through which the Board exercises oversight over the affairs of the Bank and the Key Management Personnel. Further, Key Management Personnel make regular presentations to the Board on matters under their purview and are also called in by the Board to explain matters relating to their areas.

**i. Assess effectiveness of own Governance Practices - Complied**

The effectiveness of the Board’s own governance practices, including the process for selection, nomination and election of Directors (which is explained in detail under Rule 3 (2) (ix)) and the process for management of conflict of interest (which is explained in detail under Rule 3 (1) (xii)) are reviewed by Board on a periodic basis. Implementation of changes required is discussed and determined by the Board at year-end following the submission of the summary of annual self-evaluations of the Board and Board sub committees.

**j. Succession plan for Key Management Personnel - Complied**

The Bank has an appropriate succession plan for Key Management Personnel aligned to the Bank’s strategic objectives and Talent Management Programme. The plan is guided by the policy on Succession Planning for Key Management Personnel and Directors, last reviewed in 2020. The Nomination Committee is responsible for the formulation, review and rollout of the plan.

**k. Regular Meetings with Key Management Personnel - Complied**

The Board maintains a sound relationship with the Corporate/Senior Management led by the MD/CEO, who in turn assists the Board to formulate policies, strategies, processes and practices that fit the Bank and its business needs in achieving corporate objectives. The Management is open and transparent with the Board, bringing all significant matters to its attention. Key Management Personnel are regularly invited to attend Board and Sub-Committee Meetings for discussion on matters concerning their areas of responsibility or make presentations on key agenda items.

**l. Regulatory environment and maintaining an effective relationship with regulator - Complied**

On appointment, Directors are provided with a folder containing all relevant governance information, including regulatory laws, directions and guidelines. Directors are briefed about regulatory developments at Board and Sub-Committee Meetings by Key Management Personnel including the Heads of Internal Audit, Risk and Compliance and by attending Director Forums arranged by the Central Bank of Sri Lanka (CBSL). Further, Board Members regularly meet with CBSL officials to discuss strategic matters specific to the Bank, maintaining an effective relationship with the regulator.

**m. Hiring and oversight of External Auditors - Complied**

The External Auditor is appointed following the procedures set out in Article 53 (iv) of the Articles of Association. The Board Audit Committee makes recommendations to the Board for the appointment, re-appointment or removal of the External Auditor in-line with professional & ethical standards and regulatory requirements. In addition the Board has adopted a policy of rotation of auditors, once in five years, in keeping with the principal of good corporate governance. A policy for Engagement of the External Auditor to provide Non-Audit Services is in place, as reviewed and recommended by the Board Audit Committee.

On the recommendation of the Board, the shareholders approved the reappointment of Messrs. KPMG as the External Auditor of the Bank, at the last AGM. In compliance with Section 163 (3) of the Companies Act No. 07 of 2007, the External Auditors submit a statement annually confirming their independence in relation to the External Audit.

# Corporate Governance Report

| Section      | Principle, Compliance & Implementation  |
|--------------|---|
| 3 (1) (ii)   | <p><b>Appointment of Chairman and CEO and defining and approving their functions and responsibilities - Complied <input checked="" type="checkbox"/></b></p> <p>The Board has appointed the Chairman and the MD/CEO. Their roles and responsibilities are separate and set out clearly in the Board Charter, ensuring a balance of power and authority and preventing unfettered power being vested with an individual. These functions and responsibilities are in line with Direction 3(5) of the said Direction.</p>   |
| 3 (1) (iii)  | <p><b>Regular Board Meetings - Complied <input checked="" type="checkbox"/></b></p> <p>Monthly Board Meetings are held regularly, and Special Meetings are scheduled based on need. Seventeen (17) Board Meetings were held in 2021 out of which Sixteen (16) Meetings were conducted with extended teleconferencing for participants unable to attend the Meetings in person due to the prevailing pandemic situation. Directors actively participate in the Meetings deliberating on matters set before the Board. Attendance at Board Meetings is given on CG&amp;RR page 10. Urgent Board Papers are approved via circular resolution only on an exceptional basis, where such resolutions are ratified by the Board at the next meeting. 14 Resolutions and 374 credit papers were approved in 2021, via circulation.</p>                                |
| 3 (1) (iv)   | <p><b>Arrangements for Directors to include proposals in the agenda - Complied <input checked="" type="checkbox"/></b></p> <p>The Board Calendar with tentative dates for Board and Sub-Committee Meetings for the following year is sent to all members approximately one month before the end of the current year. The Chairman sets the Board Agenda assisted by the Company Secretary. Directors submit proposals for inclusion in the agenda up on discussion with the Chairperson.</p>  |
| 3 (1) (v)    | <p><b>Notice of Meetings - Complied <input checked="" type="checkbox"/></b></p> <p>Notice of Meetings, Agenda and Board Papers for the Meetings are sent generally seven (7) days before the Meeting, giving Members sufficient time to attend the Meeting and study the documents. Urgent Board Papers are included on an exceptional basis, with the consent from the Chairman/Chairperson.</p>   |
| 3 (1) (vi)   | <p><b>Director's Attendance - Complied <input checked="" type="checkbox"/></b></p> <p>At appointment, all Directors are apprised of the regulations on attendance in accordance with the Banking Act Direction No.11 of 2007 (the Direction). Attendance at Board Meetings is given on CG&amp;RR page 10. All Directors have attended at least two thirds (2/3) of Board Meetings held during 2021, the lowest attendance being ten (10) Directors at a Meeting (including attendance of an Alternate Director). No Director has been absent from three (3) consecutive Meetings during 2021.</p>   |
| 3 (1) (vii)  | <p><b>Appointment and setting responsibilities of the Company Secretary - Complied <input checked="" type="checkbox"/></b></p> <p>The Board has appointed a Company Secretary, an Attorney at Law, who satisfies the provisions of Section 43 of the Banking Act No.30 of 1988. The Company Secretary guides the Board on discharging its duties and responsibilities, facilitates adherence to best practices in Corporate Governance and apprises the Board of relevant legislative and regulatory changes.</p>   |
| 3 (1) (viii) | <p><b>Directors access to advice and services of Company Secretary - Complied <input checked="" type="checkbox"/></b></p> <p>All Board Members have full access, to the advice and services of the Company Secretary to ensure that proper Board procedures are followed and all applicable rules and regulations are complied with.</p>  |
| 3 (1) (ix)   | <p><b>Maintenance of Board Minutes - Complied <input checked="" type="checkbox"/></b></p> <p>Company Secretary maintains the minutes of the Board Meetings. The Minutes are reviewed by the Chairman/Chairperson and are circulated to all Board Members and approved at the next Board Meeting upon incorporating any amendments proposed by other Directors. The minute book is maintained by the Company Secretary and open for inspection by any Director.</p>  |
| 3 (1) (x)    | <p><b>Minutes to be of sufficient detail and serve as a reference for regulators and supervisory authorities - Complied <input checked="" type="checkbox"/></b></p> <p>Minutes of Board Meetings are recorded in sufficient detail to reflect that the Board acted with due care and prudence in performing its duties and to serve as a reference for regulatory and supervisory authorities to assess the depth of deliberations at Board Meetings.</p>   |
| 3 (1) (xi)   | <p><b>Directors ability to seek independent professional advice - Complied <input checked="" type="checkbox"/></b></p> <p>Procedures are in place to allow Directors to seek independent professional advice, as and when necessary and at the Bank's expense, in discharging their duties and responsibilities. This facility is coordinated through the Company Secretary.</p>  |
| 3 (1) (xii)  | <p><b>Dealing with Conflicts of Interest - Complied <input checked="" type="checkbox"/></b></p> <p>Article 40 of Articles of Association addresses the provision with regard to this requirement. The Board is conscious of its obligations to ensure that Directors avoid conflicts of interest (both fact and apparent) between their duty to HNB and their other interests.</p> <p>The Board has taken steps to ensure that conflicts and potential conflicts of interest of Directors are disclosed to the Board. Any Director with a material personal interests in a matter being considered by the Board declares his/her interests and unless the Board resolves otherwise, he/she does not participate in discussions or vote on that specific matter. The Directors declare their interests at appointment and thereafter on a quarterly basis.</p> |
| 3 (1) (xiii) | <p><b>Formal schedule of matters for decision making - Complied <input checked="" type="checkbox"/></b></p> <p>The Board reserves for itself a formal schedule of matters on which it takes the ultimate decision.</p>  |

| Section      | Principle, Compliance & Implementation  |
|--------------|---|
| 3 (1) (xiv)  | <p><b>Inform Central Bank, if there are solvency issues - Complied <input checked="" type="checkbox"/></b></p> <p>The Bank is solvent and no situations have arisen to challenge its solvency.</p> <p>In the unlikely event, the Bank is about to become insolvent, a procedure is however in place to inform the Director of Banking Supervision of same, prior to taking any decision or action to suspend payments due to depositors and other creditors.</p>  |
| 3 (1) (xv)   | <p><b>Capital Adequacy - Complied <input checked="" type="checkbox"/></b></p> <p>The Board monitors capital adequacy and other prudential measures to manage risk and to ensure compliance with regulatory requirements. The Bank is in compliance with the minimum capital requirements of the Monetary Board.</p>   |
| 3 (1) (xvi)  | <p><b>Publish Corporate Governance Report in Annual Report - Complied <input checked="" type="checkbox"/></b></p> <p>This report forms part of the Corporate Governance Report of the Bank which is set out on CG&amp;RR pages 2 to 41.</p>   |
| 3 (1) (xvii) | <p><b>Self-Assessment of Directors - Complied <input checked="" type="checkbox"/></b></p> <p>Each Director undertakes annually, a self-assessment of the Board, to ensure responsibilities are satisfactorily discharged. The outcome of the appraisal for the financial year 2020 was tabled at the Board Meeting held in April 2021. The 2021 annual appraisal is currently in progress. Further, each Director carries out an assessment of "fitness and propriety" to serve as Director.</p>  |
| <b>3 (2)</b> | <b>The Board's Composition</b>  |
| 3 (2) (i)    | <p><b>Number of Directors - Complied <input checked="" type="checkbox"/></b></p> <p>The Board consists of ten (10) Directors, compliant with CBSL direction which requires the number of Directors to be not less than seven (7) and not more than thirteen (13).</p>   |
| 3 (2) (ii)   | <p><b>Period of service of a Director - Complied <input checked="" type="checkbox"/></b></p> <p>The total period of service of all Non-Executive Directors does not exceed nine (9) years as required by the CBSL Direction. Tenures of service of Directors are given on CG&amp;RR page 8.</p>   |
| 3 (2) (iii)  | <p><b>Director Appointment of an Employee as a Director - Complied <input checked="" type="checkbox"/></b></p> <p>There are two (2) Directors who serve in an Executive Capacity in the Board. The Board balance is compliant with the CBSL Direction which limits the number of Executive Directors to 1/3 of the Board.</p>   |
| 3 (2) (iv)   | <p><b>Independent Non-Executive Directors - Complied as at 31st December 2021 <input checked="" type="checkbox"/></b></p> <p>The Board of comprises five (5) Independent Non-Executive Directors, in compliance with regulatory requirement. The Directors satisfy the criteria for determining independence, which is reviewed annually by the Board based on self-declaration forms submitted by the Directors.</p> <p>However, the Bank remained non-compliant with this provision for a period of forty three (43) days, following the sudden demise of Mr Nilanth De Silva, Independent Non-Executive Director on 29th September 2021 and until 11th November 2021. The number of Independent Directors on the Board of HNB fell to three (3), being less than one third of the total number of Directors. Subsequent to appropriate action being taken by Mrs Aruni Goonetilleke and Mr Amal Cabraal, the Board deemed them "Independent" based on the criteria specified in the Banking Act Direction No.11 of 2007. Consequently, the nature of the Directorships of Mrs Aruni Goonetilleke and Mr Amal Cabraal were amended to Independent Non-Executive from Non-Executive with effect from 12th November 2021 and 16th November 2021, respectively. As at the balance sheet date, the Bank is complied with the direction.</p> |
| 3 (2) (v)    | <p><b>Alternate Independent Directors - Complied <input checked="" type="checkbox"/></b></p> <p>No Alternate Directors were appointed to represent Independent Non-Executive Directors. The Alternate Directors appointed to represent the Non-Executive Directors, are not executives of the Bank.</p>   |
| 3 (2) (vi)   | <p><b>Criteria for Non-Executive Directors - Complied <input checked="" type="checkbox"/></b></p> <p>All Non-Executive Directors are eminent professionals in their respective fields, with credible track records and necessary skills and experience. They contribute diverse perspective to matters set before the Board, bringing independent judgment to bear on issues of strategy, performance and resource.</p>   |
| 3 (2) (vii)  | <p><b>More than half the quorum to comprise Non-Executive Directors - Complied <input checked="" type="checkbox"/></b></p> <p>Majority of the Board comprise of Non-Executive Directors.</p>  |
| 3 (2) (viii) | <p><b>Identify Independent Non-Executive Directors in communications and disclose categories of Directors in Annual Report - Complied <input checked="" type="checkbox"/></b></p> <p>The Independent Non-Executive Directors are expressly identified in all corporate communications that disclose the names of Directors of the Bank. Composition and details of the Board are given on CG&amp;RR pages 4 to 5.</p>   |

# Corporate Governance Report

| Section      | Principle, Compliance & Implementation   |
|--------------|--|
| 3 (2) (ix)   | <p><b>Formal and transparent procedure for appointments to the Board - Complied <input checked="" type="checkbox"/></b></p> <p>The Board has a formal and transparent process in place for the succession and appointment of Directors. The Nominations Committee processes and short-lists candidates and makes recommendations to the Board for approval. The attributes and experience required from potential appointees are identified and agreed prior to the search process considering the combined knowledge, experience and diversity of the Board in relation to the Bank's strategic plans and any gaps thereof. The candidate's other directorships and commitments are also considered to ensure sufficient time to discharge their role at HNB, effectively. Upon completion of this process, names are referred to the Director of the Bank Supervision Department of the Central Bank of Sri Lanka for approval as a "fit and proper" person, prior to the appointment.</p> <p>Mrs Aruni Goonetilleke, Mr Osman Chandrawansa, Mr Rimoe Saldin and Mr Nihal Jayawardene were appointed to the Board in 2021.</p> |
| 3 (2) (x)    | <p><b>Re-election of Directors filling casual vacancies - Complied <input checked="" type="checkbox"/></b></p> <p>All Directors appointed to the Board are subjected to re-election by shareholders at the first Annual General Meeting after their appointment.</p> <p>Mrs Aruni Goonetilleke, Mr Osman Chandrawansa, Mr Rimoe Saldin and Mr Nihal Jayawardene were appointed to the Board in 2021 to fill casual vacancies. Further Mr Rasitha Gunawardana and Mr Kithsiri Gunawardana were appointed to the Board subsequent to the year end to fill casual vacancies. All six (6) Directors appointed to fill casual vacancies will offer themselves for re-election at the AGM to be held in March 2022.</p>  |
| 3 (2) (xi)   | <p><b>Communication of reasons for removal or resignation of Director - Complied <input checked="" type="checkbox"/></b></p> <p>Resignations of Directors and the reasons thereof are promptly informed to the regulatory authorities and shareholders in compliance with the CSE regulations together with a statement confirming whether or not there are any matters that need to be brought to the attention of shareholders.</p>  |
| 3 (2) (xii)  | <p><b>Prohibition of Directors or employees of an appointment of Bank becoming a Director at another Bank - Complied <input checked="" type="checkbox"/></b></p> <p>None of the Directors are Directors or employees at any other Bank. This is a requirement when seeking appointment of Directors.</p>   |
| <b>3 (3)</b> | <b>Criteria to assess fitness and propriety of Directors</b>   |
| 3 (3) (i)    | <p><b>Age of Director should not exceed 70 years - Complied <input checked="" type="checkbox"/></b></p> <p>There are no Directors who are over seventy (70) years of age.</p>  |
| 3 (3) (ii)   | <p><b>Directors should not be Directors of more than 20 companies and not more than 10 companies classified as Specified Business Entities - Complied <input checked="" type="checkbox"/></b></p> <p>The Directors do not hold Directorships of more than twenty (20) companies/entities/institutions inclusive of Subsidiaries or Associate Companies of the Bank.</p>  |
| 3 (3) (iii)  | <p><b>Cooling - off period when appointing Directors or CEO - Complied <input checked="" type="checkbox"/></b></p> <p>The Bank has complied with the directions when appointing Directors during the year.</p>   |
| <b>3 (4)</b> | <b>Management functions delegated by the Board</b>   |
| 3 (4) (i)    | <b>Understand and study delegation arrangements - Complied <input checked="" type="checkbox"/></b>   |
| 3 (4) (ii)   | <b>Extent of delegation should not hinder Board ability to discharge its functions - Complied <input checked="" type="checkbox"/></b>  |
| 3 (4) (iii)  | <p><b>Review delegation arrangements periodically to ensure relevance to operations of the Bank - Complied <input checked="" type="checkbox"/></b></p> <p>The Board has a clear understanding of the delegation arrangements, studying, reviewing and approving the extent of delegation annually to ensure it meets the business needs of the Bank whilst enabling the Board to effectively discharge their duties.</p>   |
| <b>3 (5)</b> | <b>The Chairman and Chief Executive Officer</b>  |
| 3 (5) (i)    | <p><b>Separation of roles - Complied <input checked="" type="checkbox"/></b></p> <p>There is a clear separation of roles of the Chairman/Chairperson and the CEO, ensuring a balance of power for decision-making.</p>   |
| 3 (5) (ii)   | <p><b>Non-Executive Chairman and appointment of a Senior Independent Directors - Complied <input checked="" type="checkbox"/></b></p> <p>The previous Chairmen, Mr Dinesh Weerakkody, (Chairman until 30th March 2021), Mr Harsha Cabral (Acting Chairman until 30th March 2021) and Mr Nilanth De Silva (Chairman until 29th September 2021) were Independent Non-Executive Directors.</p> <p>Mrs Aruni Goonetilleke (Non-Executive Director) was appointed as the Chairperson of the Bank on 29th September 2021 and Mr Devaka Cooray (Independent Non-Executive Director) was appointed as the "Senior Independent Director" on the same day. Mrs Aruni Goonetilleke was deemed "Independent" from 12th November 2021, Mr Devaka Cooray resigned from his role, as Senior Independent Director in December 2021.</p>  |



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| 3 (5) (iii)  | <p><b>Disclosure of identity of Chairman and CEO and any relationships with the Board Members - Complied <input checked="" type="checkbox"/></b></p> <p>The profiles of the Chairperson and CEO are disclosed on IR page 72.</p> <p>As declared by the Directors, no relationships including financial, business, family, or any other, prevailed between the Chairman/ Chairperson, MD/ CEO or among other Board Members.</p>  |
| 3 (5) (iv)   | <p><b>Chairman to provide leadership to the Board - Complied <input checked="" type="checkbox"/></b></p> <p>The Chairman/Chairperson led the Board ensuring that it works effectively, and acts in the best interests of the Bank in a timely basis. The effectiveness of the Chairperson in the discharge of the Board functions is assessed annually by Board and in her self-assessment.</p>   |
| 3 (5) (v)    | <p><b>Responsibility for agenda lies with Chairman but may be delegated to Company Secretary - Complied <input checked="" type="checkbox"/></b></p> <p>The Chairperson sets the Board agenda, assisted by the Company Secretary and MD/CEO.</p>   |
| 3 (5) (vi)   | <p><b>Ensure that Directors are properly briefed and provided adequate information - Complied <input checked="" type="checkbox"/></b></p> <p>The Chairman/Chairperson ensured that the Board is sufficiently briefed and informed regarding the matters arising at Board.</p> <p>Board papers are circulated generally seven (7) days prior to meeting, giving the Members adequate time to study the documents. Directors have access to KMP to clarify matters and to external specialists for independent advice, when required.</p>   |
| 3 (5) (vii)  | <p><b>Encourage active participation by all Directors and lead in acting in the interests of the Bank - Complied <input checked="" type="checkbox"/></b></p> <p>The Chairman/Chairperson has encouraged all Directors to actively contribute towards the best interests of the Bank and it is addressed in the list of functions and responsibilities of the Chairman/Chairperson was approved by the Board.</p>  |
| 3 (5) (viii) | <p><b>Encourage participation of Non-Executive Directors and relationships between Non-Executive and Executive Directors - Complied <input checked="" type="checkbox"/></b></p> <p>The Chairman/Chairperson has encouraged effective participation of all Directors and has encouraged constructive relations between the Executives and the Non-Executive Directors. This function is assessed annually by the Board and by the Chairman/Chairperson in the self-assessment. Additionally, Non-Executive Directors chair the Board Sub-Committees providing further opportunity for active participation.</p>  |
| 3 (5) (ix)   | <p><b>Refrain from direct supervision of Key Management Personnel and executive duties - Complied <input checked="" type="checkbox"/></b></p> <p>The Chairman/Chairperson was not get involved in the supervision of Key Management Personnel or any other executive duties.</p>  |
| 3 (5) (x)    | <p><b>Ensure effective communication with Shareholders - Complied <input checked="" type="checkbox"/></b></p> <p>The Annual General Meeting (AGM) is the main mechanism for shareholders' views to be heard and where the Board interacts with and clarifies matter for the shareholders. The Board has formulated a formal policy to handle shareholders' complaints. The shareholder engagement is given on CG&amp;RR page 24.</p>  |
| 3 (5) (xi)   | <p><b>CEO functions as the apex executive in charge of the day to day operations and business - Complied <input checked="" type="checkbox"/></b></p> <p>As set out in the Board Charter, the responsibility for the day to day operations and business of the Bank has been delegated to the MD/CEO in his capacity as the apex executive-in-charge of the Board.</p>   |
| <b>3 (6)</b> | <b>Board appointed Committees</b>   |
| 3 (6) (i)    | <p><b>Establishing Board Committees, their functions and reporting - Complied <input checked="" type="checkbox"/></b></p> <p>The Board has appointed ten (10) Sub-Committees to ensure its oversight and control over the affairs of the Bank.</p> <p>The details of Board Sub-Committees are disclosed on CG&amp;RR pages 14 to 15.</p> <p>Each Sub-Committee is governed by its own Terms of Reference and has a Secretary who arranges the Meetings and maintains minutes and records under the supervision of the Chairman/Chairperson of the Sub-Committee. The Sub-Committee Chairman/Chairperson are accountable for the effective functioning of the Committees and reports on a periodic basis to the Board on the activities of their respective Sub-Committees, highlighting matters for Board attention. Committee mandates are reviewed regularly.</p> |
| 3 (6) (ii)   | <p><b>Board Audit Committee</b></p> <p><b>a. Chairman to be an Independent Non-Executive Director with qualifications and experience in accountancy and/or audit - Complied <input checked="" type="checkbox"/></b></p> <p>The Chairman of BAC, Mr Devaka Cooray is an Independent Non-Executive Director, a fellow member of the Institute of Chartered Accountants of Sri Lanka and the Chartered Institute of Management Accountants United Kingdom. He has worked with Messrs. Ernst &amp; Young for over 40 years of which 30 years was as a Senior Assurance and Talent Partner. He functioned as the Deputy Managing Partner from 2016 until his retirement in 2019. Mr Devaka Cooray has spearheaded many initiatives during his tenure at Messrs. Ernst &amp; Young. Details are provided on IR page 73.</p>   |

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|         | <p><b>b. Committee to comprise solely of Non-Executive Directors - Complied <input checked="" type="checkbox"/></b></p> <p>All members are Non-Executive Directors of which two (02) are Independent Non-Executive Directors as at 31.12.2021.</p>   |
|         | <p><b>c. Board Audit Committee functions - Complied <input checked="" type="checkbox"/></b></p> <p>In terms of its mandate, the Board Audit Committee is responsible for the following key recommendations:</p> <ol style="list-style-type: none"><li>I. The appointment of the External Auditor for audit services in line with professional and ethical standards and in compliance with regulatory requirements. On the recommendation of the Board Audit Committee/Board, the shareholders have approved Messrs. KPMG as the External Auditor of the Bank for the year 2021,</li><li>II. The service period, audit fee and any resignation or dismissal of the auditor. The Board Audit Committee ensures that the service period of the engagement of the External Audit partner shall not exceed five (5) years, and that the particular audit partner is not re-engaged for the audit before the expiry of three (3) years from the date of the completion of the previous term,</li><li>III. The implementation of the Central Bank guidelines issued to auditors from time to time and</li><li>IV. Monitoring and review of the adequacy and effectiveness of accounting policies and the application of relevant accounting.</li></ol> |
|         | <p><b>d. Review and monitor External Auditor's independence and objectivity and the effectiveness of the audit processes - Complied <input checked="" type="checkbox"/></b></p> <p>The Board Audit Committee monitors and reviews the external Auditor's independence, objectivity and the effectiveness of the audit process taking into account relevant professional and regulatory requirements. In addition, the Bank has adopted the policy of rotation of audits once in every five years.</p>  |
|         | <p><b>e. Provision of Non-Audit services by External Auditor - Complied <input checked="" type="checkbox"/></b></p> <p>The BAC is guided by the Board approved policy for Engagement of the External Auditor to provide Non-Audit Services. The Policy was reviewed in 2021.</p> <p>In assignment of non-audit services to External Auditors by the Bank, the Board/Board Audit Committee ensures that the External Auditor has the necessary skills and experience for the assignment and ascertains that independence and/or objectivity of the External Auditor in carrying out his duties and responsibilities will not be impaired. Assigning such Non-Audit Services to External Auditors is discussed at BAC Meetings and prior Board approval obtained. Please refer Board Audit Committee Report on IR pages 106 to 108 for further details.</p>  |
|         | <p><b>f. Determines scope of Audit - Complied <input checked="" type="checkbox"/></b></p> <p>The External Auditor Messrs. KPMG attended eight (8) Meetings during the year. The External Auditor presented to the Committee the audit approach and procedures, including nature &amp; scope of the audit and auditor's independence.</p>   |
|         | <p><b>g. Review financial information of the Bank - Complied <input checked="" type="checkbox"/></b></p> <p>The Committee reviews the financial information of the Bank, which are reviewed and presented by the CFO in order to monitor the integrity of the Bank's Financial Statements, Annual Report, accounts and quarterly reports prepared for disclosure, and the significant financial reporting judgements contained therein. The review focuses particularly on the following:</p> <ol style="list-style-type: none"><li>I. Major judgemental areas,</li><li>II. Any changes in accounting policies and practices,</li><li>III. Significant adjustments arising from the audit,</li><li>IV. The going concern assumption,</li><li>V. Compliance with relevant accounting standards and other legal requirements.</li></ol>  |
|         | <p><b>h. Discussions with External Auditor on interim and final audits - Complied <input checked="" type="checkbox"/></b></p> <p>The Board Audit Committee discusses issues, problems and reservations arising from the interim and final audits with the External Auditor.</p>  |
|         | <p><b>i. Review of Management Letter and Bank's response - Complied <input checked="" type="checkbox"/></b></p> <p>The Board Audit Committee reviewed the External Auditor's management letter for 2020, Audit and the Management's response and follow up on addressing the same thereto during 2021.</p>   |

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**j. Review of Internal Audit Function - Complied**

During the year, the Board Audit Committee reviewed the independence, objectivity and performance of the Internal Audit Function, ensuring the function acts with impartiality, proficiency and due professional care.

BAC reviewed the adequacy of coverage of the internal audit plan and approved the same. The Committee also assessed the Internal Audit Department's resource requirements including succession planning and is satisfied that the Internal Audit Department has the necessary authority to carry out its work.

The Committee reviewed internal audit findings, management responses thereto and results of the follow up action taken on the recommendations of the Internal Audit Department.

The Internal Audit Department's evaluation of the Bank's internal controls were reviewed by the Board Audit Committee.

The Committee reviewed the performance appraisal of the Chief Internal Auditor and other senior staff members of the Internal Audit Department. The Committee is kept apprised of resignations of senior staff of the Internal Audit Department together with the reasons for resigning.

The Chief Internal Auditor directly reports to the Board Audit Committee, ensuring the independence of the Internal Audit Function.

**k. Internal Investigations - Complied**

Major findings of internal investigations and management's responses thereto are reviewed by the Board Audit Committee and implementation of the recommendations.

**l. Attendees at Board Audit Committee Meetings - Complied**

Chairman of BIRMC, MD/CEO, COO, Chief Risk Officer, Chief Financial Officer, Chief Internal Auditor, Head of Compliance, Chief Technology & Digital Officer, Head of Operations and a representative of the External Auditor are typically invited to attend Meetings. Other Board Members may also attend Meetings upon invitation. The Committee met the External Auditor on two (2) occasions in 2021, in the absence of the Executive Directors and KMP.

**m. Explicit authority, resources and access to information - Complied**

The Board Audit Committee is guided by the Committee Charter which sets out authority and responsibility of the said Committee. The Charter was last reviewed in 2019. The Board Audit Committee is authorised to obtain external professional advice and to invite outsiders with relevant experience to attend as and when necessary. The Committee also has full access to information in order to investigate into matters relating its Terms of Reference. Terms of Reference of the Committee is described in the Committee Report given on IR pages 106 to 108.

**n. Regular Meetings - Complied**

The Board Audit Committee met eight (8) times during the year. Conclusions in discharging its duties and responsibilities are recorded in the minutes of the Meetings maintained by the secretary to BAC.

**o. Disclosure in Annual Report - Complied**

Details of the activities of the BAC are included in the report of the Board Audit Committee given on IR pages 106 to 108.

The number of meetings held and attendance at Board Audit Committee meetings held in 2021 are set out on CG&RR page 10.

**p. Maintain Minutes of Meetings - Complied**

Minutes of Board Audit Committee Meetings are recorded and maintained by the Secretary to the Committee. The Chief Internal Auditor serves as the Secretary to the Committee.

**q. Whistle blowing policy and relationship with External Auditor - Complied**

A Board approved whistle blowing policy is in place. The whistle blowing policy and the mechanism had been communicated to all staff members.

The Board Audit Committee reviews issues relating to breach of ethics if any and the arrangements by which the staff of the Bank may in confidence raise concerns about possible improprieties. The Committee also ensured that the procedures for the independent investigations of such matters are appropriate and are in place. The Independent Non-Executive Director handling whistle blowing complaints provides regular updates on the investigation results to the BAC.

The Board Charter addresses the Board's responsibility to encourage any communication regarding non-compliances and unethical behaviour within the Bank.

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| 3 (6) (iii) | <p><b>Human Resources &amp; Remuneration Committee</b></p> <p><i>a. Remuneration Policy - Complied</i> <input checked="" type="checkbox"/></p> <p>The Committee reviews all significant human resource policies and initiatives, salary structures, promotions and terms and conditions relating to staff at Senior Management Level with information and recommendations from the MD/CEO and the Chief Human Resource Officer. Terms of Reference of the Committee is described in the Committee Report on IR pages 96 to 97.</p> <p>Separate Remuneration Policies for the Board of Directors, MD/CEO, ED/COO and all employees of the Bank including KMP are in place.</p> <p><i>b. Goals and Targets - Complied</i> <input checked="" type="checkbox"/></p> <p>The goals and targets of the Board of Directors have been clearly set out and evaluated at the end of the year. The goals and targets for the MD/CEO and the senior leadership team are documented under the Balance Score Card system. Further, the goals and targets for 2021 for the MD/CEO and the senior leadership team was approved at a Board Meeting.</p> <p><i>c. Performance Evaluation- Complied</i> <input checked="" type="checkbox"/></p> <p>The Directors are evaluated at the end of the year based on the goals and targets set out.</p> <p>The Committee deliberates upon and recommends to the Board of Directors the remuneration packages, annual increments and bonuses of the MD/CEO, COO, members of the Corporate Management and Senior Management staff, having evaluated their performance against the set goals and targets.</p> <p><i>d. Meetings - Complied</i> <input checked="" type="checkbox"/></p> <p>The HRRC Committee met four (4) times during the year.</p> <p>The MD/CEO attends Human Resources &amp; Remuneration Committee by invitation. The MD/CEO is not present at the time when matters relating to him are being discussed.</p> |
| 3 (6) (iv)  | <p><b>Nomination Committee</b></p> <p><i>a. Appointment of Directors, CEO and Key Management Personnel - Complied</i> <input checked="" type="checkbox"/></p> <p>A formal procedure is in place to appoint new Directors, MD/CEO and Key Management Personnel.</p> <p><i>b. Re-election of Directors - Complied</i> <input checked="" type="checkbox"/></p> <p>The Committee considers and recommends the re-election of the Directors to the Board. The Committee also set criteria of the succession of the MD/CEO.</p> <p><i>c. Eligibility criteria for appointments to key managerial positions including CEO - Complied</i> <input checked="" type="checkbox"/></p> <p>The Committee sets the eligibility criteria, including qualifications, experience and key attributes, for appointment or promotion to key managerial positions including the position of the MD/CEO.</p> <p>A Board approved procedure to appoint Directors, MD/CEO and KMP is in place.</p> <p><i>d. Fit &amp; proper persons - Complied</i> <input checked="" type="checkbox"/></p> <p>Each Director including the MD/CEO carries out an assessment of “fitness and propriety” to serve as a Director of the Bank. These declarations are reviewed by the Nomination Committee prior to submission to the Director Bank Supervision of the Central Bank of Sri Lanka.</p> <p><i>e. Succession plan and new expertise - Complied</i> <input checked="" type="checkbox"/></p> <p>A Succession Planning Policy is in place for KMP and Directors. Each year, the Nomination Committee reviews the additional/ new expertise requirements and succession arrangements for Directors and KMP of the Bank, in line with the Strategic Plan.</p>  |

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**f. Composition of Nomination Committee - Complied**

The following Non-Executive Directors served on the Nomination Committee during 2021.

**Chairmen**

Mr Dinesh Weerakkody - Independent Non-Executive Director (Until 30th March 2021)

Dr Harsha Cabral - Independent Non-Executive Director (Appointed w.e.f. 23rd April 2020 / Chairman w.e.f. 5th April 2021 and resigned w.e.f. 5th July 2021)

Mr Nilanth De Silva - Independent Non-Executive Director (Appointed w.e.f. 05th April 2020 / Chairman w.e.f. 30th July 2021 until demise on 29th September 2021)

Mr Devaka Cooray - Independent Non-Executive Director (Appointed w.e.f. 30th July 2021 / Chairman w.e.f. 4th October 2021)

**Other Committee Members**

Mr Madu Rathnayake - Independent Non-Executive Director (Appointed w.e.f. 4th October 2021)

Mrs Aruni Goonetilleke - Independent Non-Executive Director (Appointed w.e.f. 4th October 2021)

Terms of Reference of the Committee is described in the Committee Report on IR pages 98 to 100.

| 3 (6) (v) | Board Integrated Risk Management Committee |
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**a. Composition of Risk Management Committee - Complied**

The following personnel served on the Board Integrated Risk Management Committee during 2021.

**Chairmen/Chairperson**

Mr Duliksha Soosaipillai - Independent Non-Executive Director (Until 30th March 2021)

Mrs Aruni Goonetilleke - Independent Non-Executive Director (From 5th April 2021 to 4th October 2021)

Mr Rimoe Saldin - Non-Executive Director (Appointed w.e.f. 30th April 2021/ Chairman w.e.f. 05th October 2021)

**Other Committee Members**

Mr Damien Fernando - Non-Executive Director

Mr Jonathan Alles - Managing Director/CEO

Mr Madu Ratnayake - Independent Non-Executive Director (Until 31st May 2021 and re-appointed on 30th July 2021)

Mr Rusi Captain - Non-Executive Director (Retired w.e.f. 2nd April 2021)

The Chairman of BAC, ED/COO, Chief Financial Officer, Chief Technology & Digital Officer and Chief Internal Auditor attend Meetings on invitation. The Committee makes decisions on behalf of the Board within the framework of the authority and responsibility assigned.

Terms of Reference of the Committee is described in the Committee Report on IR pages 101 to 105.

**b. Risk Assessment - Complied**

Policies on Credit Risk Management, Market Risk Management and Operational Risk Management have been approved by the Committee, providing a framework for management and assessment of risks. In discharging its responsibilities further as per the mandate, periodic reports on pre-established risk indicators prepared by the Risk Department is submitted to the Committee for review.

The risk management process followed by the subsidiary companies has also been reviewed by the BIRMC during 2021.

**c. Review of management level committees on risk - Complied**

The Committee reviews the reports of the Management Committees including the Asset and Liability Committee (ALCO) and the Executive Risk Management & Credit Policy Committee to assess their adequacy and effectiveness in addressing specific risks and managing the same within the quantitative and qualitative risk limits set in the Risk Appetite Statement approved by the Board.

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|              | <p><b>d. Corrective action to mitigate risks exceeding prudential levels - Complied</b> <input checked="" type="checkbox"/></p> <p>The Risk Dashboards, prepared on a periodic basis, reflects the actual exposure levels under each risk category against the tolerance levels, decided by the Committee on the basis of the Bank's policies and regulatory and supervisory requirements. The Committee has taken prompt corrective actions to mitigate the effects of risk indicators which have gone beyond the tolerance levels.</p>   |
|              | <p><b>e. Frequency of meetings - Complied</b> <input checked="" type="checkbox"/></p> <p>The Committee has met ten (10) times during the year. The agenda covers matters assessing all aspects of risk management including the updated business continuity plans.</p>   |
|              | <p><b>f. Actions against officers responsible for failure to identify specific risks or implement corrective action - Complied</b> <input checked="" type="checkbox"/></p> <p>Such matters, if any, are referred to the Human Resources Division for necessary action.</p>   |
|              | <p><b>g. Risk assessment report to Board - Complied</b> <input checked="" type="checkbox"/></p> <p>Detailed reports of the BIRMC Meetings are submitted to the Board at the subsequent Board Meeting.</p>  |
|              | <p><b>h. Compliance Function - Complied</b> <input checked="" type="checkbox"/></p> <p>The Bank has established a compliance function to assess and ensure the Bank's compliance with laws, regulations, regulatory guidelines, internal controls and approved policies on all areas of business operations, headed by a dedicated Compliance Officer who reports to the BIRMC.</p>  |
| <b>3 (7)</b> | <b>Related Party Transactions</b>  |
| 3 (7) (i)    | <p><b>Avoid conflict of interest - Complied</b> <input checked="" type="checkbox"/></p> <p>A Board approved policy to enhance the transparency of Related Party Transactions is in place. The RPTRC oversees the process relating to the said subject and the Committee report is provided on IR pages 109 to 110.</p> <p>Steps have been taken by the Board to avoid any conflicts of interest, that may arise, in transacting with related parties as per the definition of this Direction. The Directors provide declarations to the Board of their outside business interests at appointment and quarterly thereafter. The Directors do not participate in, and excuse themselves from, the Meeting when the Board considers any matters in which lending to related entities are discussed and where a conflict in interest may arise.</p> <p>Transactions carried out with related parties as defined by LKAS 24 on 'Related Party Disclosures' in the normal course of business are disclosed in note 60 to the Financial Statements on 'Related Party Disclosures' on IR pages 318 to 324. Directors' interests in contracts which do not fall into the definition of Related Party Transactions as per LKAS 24 are reported separately in the Annual Report, outside the Financial Statements. The net accommodation granted to each category of related parties as a percentage of the Bank's regulatory capital is given under Rule 3 (8) (ii) (e).</p> |
| 3 (7) (ii)   | <p><b>Related Party Transactions covered by direction - Complied</b> <input checked="" type="checkbox"/></p> <p>The Related Party Transactions Policy approved by the Board covers the following transactions:</p> <ol style="list-style-type: none"><li>The grant of any type of accommodation, as defined in the Monetary Board's Directions on maximum amount of accommodation,</li><li>The creation of any liabilities of the Bank in the form of deposits, borrowings and investments,</li><li>The provision of any services of a financial or non-financial nature provided to the Bank or received from the Bank and</li><li>The creation or maintenance of reporting lines and information flows between the Bank and any related parties which may lead to the sharing of potentially proprietary, confidential or otherwise sensitive information that may give benefits to such related parties.</li></ol>  |

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| 3 (7) (iii)  | <p><b>Prohibited transactions - Complied <input checked="" type="checkbox"/></b></p> <p>The Bank's Related Party Transactions Policy prohibits transactions which would grant related parties more favourable treatment than that accorded to other customers. These include the following:</p> <ol style="list-style-type: none"> <li>I. Granting of "Total Net Accommodation" to related parties, exceeding a prudent percentage of the Bank's regulatory capital. Refer Rule 3 (8) (ii) (e) on CG&amp;RR page 38.</li> <li>II. Charging of a lower rate of interest than the Bank's best lending rate or paying more than the Bank's deposit rate for a comparable transaction with an unrelated comparable counterparty.</li> <li>III. Providing of preferential treatment, such as favourable terms, covering trade losses and/or waiving fees/commissions, that extend beyond the terms granted in the normal course of business undertaken with unrelated parties.</li> <li>IV. Providing services to or receiving services from a related-party without an evaluation procedure and</li> <li>V. Maintaining reporting lines and information flows that may lead to sharing potentially proprietary, confidential or otherwise sensitive information with related parties, except as required for the performance of legitimate duties and functions.</li> </ol>   |
| 3 (7) (iv)   | <p><b>Granting accommodation Director or close relation to a Director - Complied <input checked="" type="checkbox"/></b></p> <p>A formal procedure is in place for granting accommodation to Directors or to close relatives of Directors. Such accommodation must be sanctioned at Board Meetings, by not less than 2/3 of the number of Directors excluding Director concerned, voting in favour of such accommodation or through circulation of papers which requires approval by all. The terms and conditions of the facility include a provision that it will be secured by such security as may from time to time be determined by the Monetary Board.</p>   |
| 3 (7) (v)    | <p><b>Accommodations granted to persons, or concerns of persons, or close relations of persons, who subsequently are appointed as Directors of the Bank - Complied <input checked="" type="checkbox"/></b></p> <p>During the year, four (4) new Directors were appointed to the Board and accommodation extended to one Director was not secured by approved securities. However, it was within the exemption period of one year. As at the Balance sheet date no accommodation was outstanding in respect of the newly appointed Director.</p>   |
| 3 (7) (vi)   | <p><b>Favourable treatment or accommodation to Bank employees or their close relations - Complied <input checked="" type="checkbox"/></b></p> <p>No favourable treatment or accommodation is provided to Bank employees or their relatives, other than staff benefits.</p>  |
| 3 (7) (vii)  | <p><b>Remittance of accommodations subject to Monetary Board approval - Complied <input checked="" type="checkbox"/></b></p> <p>No such situation has arisen during the year.</p>   |
| <b>3 (8)</b> | <b>Disclosures</b>  |
| 3 (8) (i)    | <p><b>Publish annual and quarterly Financial Statements - Complied <input checked="" type="checkbox"/></b></p> <p>Annual Audited Financial Statements and Quarterly Financial Statements of the Bank were prepared in accordance with the formats prescribed by the Supervisory and Regulatory Authorities and applicable accounting standards and have been published in the newspapers in all three (3) languages.</p>  |
| 3 (8) (ii)   | <p><b>Disclosures in Annual Report</b></p> <p><i>a. A Statement to the effect that the Annual Audited Financial Statements have been prepared in line with applicable accounting standards and regulatory requirements, inclusive of specific disclosures - Complied <input checked="" type="checkbox"/></i></p> <p>Disclosures on the compliance with the applicable accounting standards and regulatory requirements in preparation of the Annual Audited Financial Statements have been made in the 'Statement of Directors' Responsibility for Financial Reporting' on IR page 128, 'Chief Executive Officer's and Chief Financial Officer's Statement of Responsibility' on IR page 127 and note 2.1.1 Statement of Compliance to the Financial Statements on IR page 147.</p> <p><i>b. Report by the Board on the Bank's internal control mechanism - Complied <input checked="" type="checkbox"/></i></p> <p>A confirmation by the Directors on the effectiveness of the internal control system over financial reporting is given under the Directors' Statement on Internal Control over Financial Reporting on IR page 111.</p> <p><i>c. External Auditor's certification on the effectiveness of the internal control mechanism - Complied <input checked="" type="checkbox"/></i></p> <p>The Assurance Report issued by the External Auditor on the Internal Control over Financial Reporting based on "SLSAE 3050 – Assurance Reports for Banks on Directors' Statement on Internal Controls" issued by the Institute of Chartered Accountants of Sri Lanka (CA Sri Lanka) is given on IR page 111. The recommendations made by the Auditors where relevant, will be dealt with in 2022.</p> |

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*d. Details of Directors, including names, fitness and propriety, transactions with the Bank and the total of fees/remuneration paid by the Bank - Complied*

Profiles of Directors are given on IR pages 70 to 75.

Directors' transactions with the Bank are disclosed in note 60 to the Financial Statements on IR pages 318 to 324.

Remuneration paid by the Bank to the Board of Directors (which includes the remuneration of the Executive Directors) is disclosed in note 18 to the Financial Statements on IR page 215.

*e. Total accommodations granted to each category of related parties and as a percentage of the Bank's regulatory capital - Complied*

The net accommodation granted to each category of related parties is given below as a percentage of the Bank's regulatory capital.

| Category of Related Party Transactions   | Rs Mn   | %     |
|--|---------|-------|
| Non-Executive Directors and their close family members   | 11.4    | 0.01  |
| Key Management Personnel* and their close family members   | 173.4   | 0.11  |
| Subsidiaries   | 2,052.2 | 1.34  |
| Joint Venture  | 4,486.3 | 2.92  |
| Entities which Directors and their close family members have a substantial interest                                      | 186.3   | 0.12  |
| Government of Sri Lanka/Entities Controlled, Jointly Controlled, Significantly Influenced by the Government of Sri Lanka | 56,011  | 36.49 |

\* includes the Executive Directors

*f. Aggregate values of remuneration to, and transactions with Key Management Personnel - Complied*

The aggregate amount of remuneration paid during 2021 to KMP and the transactions with KMP are given below;

| Remuneration and transactions with the Key Management Personnel | Rs. Mn |
|---|--------|
| Remuneration paid   | 393.2  |
| Loans and Advances  | 402.7  |
| Deposits  | 505.6  |
| Investments   | 37.7   |

*g. External Auditor's certification of compliance - Complied*

The External Auditors have performed procedures set out in Sri Lanka Standards on Related Service 4400 issued by the Institute of Chartered Accountants of Sri Lanka (SLSRS 4400), to meet the compliance requirement of the Corporate Governance Directive. Their findings presented in their report addressed to the Board are consistent with the matters disclosed above and did not identify any inconsistencies to those reported above by the Board. The recommendations made by the Auditors where relevant will be dealt with in 2022.

*h. Report confirming compliance with prudential requirements, regulations, laws and internal controls - Complied*

There were no material non-compliance to prudential requirements, regulations, laws and internal controls affecting the Bank.

*i. Non-compliance Report - Complied*

There were no supervisory concern lapses in the Bank's Risk Management Systems or non-compliance with the said Direction that have been pointed out by the Director of the Banks Supervision Department of the CBSL, which has been directed to be disclosed to the public. Hence, there are no disclosures in this regard.

| 3 (9) | Transitional and Other General Provisions |
|-------|---|
|-------|---|

*Transitional and other general provisions - Complied*

Transitional provisions have been complied with.



**APPENDIX II: COMPLIANCE WITH THE CODE OF BEST PRACTICE ON CORPORATE GOVERNANCE ISSUED BY THE INSTITUTE OF CHARTERED ACCOUNTANTS OF SRI LANKA IN 2017**

| Code Ref | Requirement   | Reference   | Complied                            | Page Ref                         |
|----------|---|---|-------------------------------------|----------------------------------|
| <b>A</b> | <b>Directors</b>  |   |                                     |                                  |
| A.1      | The Board   | The Board<br>Effective Board Oversight<br>Active Board Engagement   | <input checked="" type="checkbox"/> | CG&RR 4<br>CG&RR 7<br>CG&RR 10   |
| A.1.1    | Board Meetings  | Board Meetings<br>Informed Decision Making  | <input checked="" type="checkbox"/> | CG&RR 10<br>CG&RR 12             |
| A.1.2    | Roles & Responsibilities of the Board                                 | Effective Board Oversight- Board's Key Responsibilities   | <input checked="" type="checkbox"/> | CG&RR 8                          |
| A.1.3    | Compliance<br>Independent Professional Advice                         | Compliance Governance<br>Comprehensive Policy Framework<br>Informed Decision Making - Access to Information | <input checked="" type="checkbox"/> | CG&RR 19<br>CG&RR 16<br>CG&RR 12 |
| A.1.4    | Access to advice and services of Company Secretary<br>Insurance Cover | Company Secretary<br>Effective Board Oversight  | <input checked="" type="checkbox"/> | CG&RR 12<br>CG&RR 7              |
| A.1.5    | Independent Judgement   | Independent Judgement   | <input checked="" type="checkbox"/> | CG&RR 8                          |
| A.1.6    | Dedicate Adequate Time and Effort Board Pack                          | Agility, Delegation and Empowerment   | <input checked="" type="checkbox"/> | CG&RR 13                         |
| A.1.7    | Calls for Resolutions   | Governance of Meetings  | <input checked="" type="checkbox"/> | CG&RR 11                         |
| A.1.8    | Board Induction and Training Annual Assessment of Training Needs      | Informed Decision Making - Knowledge Development<br>Appraisal of the Board                                  | <input checked="" type="checkbox"/> | CG&RR 12<br>CG&RR 25             |
| A.2      | Chairman & Chief Executive Officer                                    | Segregation of Roles and Responsibilities   | <input checked="" type="checkbox"/> | CG&RR 17                         |
| A.3      | Chairman's Role in Preserving Good Corporate Governance               | Segregation of Roles and Responsibilities   | <input checked="" type="checkbox"/> | CG&RR 17                         |
| A.4      | Availability of Financial Acumen                                      | Board Diversity   | <input checked="" type="checkbox"/> | CG&RR 8                          |
| A.5      | Board Balance   | Board Diversity   | <input checked="" type="checkbox"/> | CG&RR 8                          |
| A.5.1    | Independent Non-Executive Directors                                   | Board Diversity   | <input checked="" type="checkbox"/> | CG&RR 8                          |
| A.5.2    |   |   |                                     |                                  |
| A.5.3    | Director's Independency   | Board Diversity – Independence  | <input checked="" type="checkbox"/> | CG&RR 10                         |
| A.5.4    | Annual Declaration  | Board Diversity – Independence  | <input checked="" type="checkbox"/> | CG&RR 10                         |
| A.5.5    | Evaluation of Independency  | Independent Judgement   | <input checked="" type="checkbox"/> | CG&RR 8                          |
| A.5.6    | Alternate Directors   | The Alternate Director appointed to represent the Non-Executive Director is not an executive of the Bank.   | <input checked="" type="checkbox"/> |                                  |
| A.5.7    | Senior Independent Director (SID)                                     | Balance of Power  | <input checked="" type="checkbox"/> | CG&RR 22                         |
| A.5.8    |   |   |                                     |                                  |
| A.5.9    | Meetings with Non-Executive Directors                                 | Balance of Power  | <input checked="" type="checkbox"/> | CG&RR 22                         |
| A.5.10   | Resolutions   | Governance of Meetings – Minutes  | <input checked="" type="checkbox"/> | CG&RR 11                         |
| A.6      | Provision of Appropriate and Timely Information                       | Informed Decision Making - Supply of Information<br>Governance of Meetings - Board Agenda, Minutes          | <input checked="" type="checkbox"/> | CG&RR 12<br>CG&RR 11             |
| A.7      | Appointments to the Board   | Active Board Engagement - Appointments<br>Nomination Committee Report                                       | <input checked="" type="checkbox"/> | CG&RR 9<br>IR 98                 |
| A.8      | Re-election of Directors  | Active Board Engagement – Re-election   | <input checked="" type="checkbox"/> | CG&RR 9                          |
| A.9      | Appraisal of Board & Sub-Committees<br>-Review at Re-Election         | Appraisals of the Board   | <input checked="" type="checkbox"/> | CG&RR 25                         |

# Corporate Governance Report

| Code Ref                              | Requirement   | Reference  | Complied                            | Page Ref  |
|---------------------------------------|---|--|-------------------------------------|---|
| A.10                                  | Annual Report to Disclose Specified Information Regarding Directors   | The Board<br>Conflict of Interest<br>Board Sub-Committees<br>Board Meetings  | <input checked="" type="checkbox"/> | CG&RR 4<br>CG&RR 22<br>CG&RR 14<br>CG&RR 10   |
| A.11                                  | Annual appraisal of the CEO   | Appraisal of the MD/CEO  | <input checked="" type="checkbox"/> | CG&RR 25  |
| <b>B. Directors' Remuneration</b>     |   |  |                                     |   |
| B.1                                   | Directors' & Executive Remuneration – HRRC  | Fair and Responsible Remuneration<br>Board Sub-Committees  | <input checked="" type="checkbox"/> | CG&RR 23<br>CG&RR 14  |
| B.2                                   | Level & Make up of Remuneration   | Fair and Responsible Remuneration<br>There were no Employee Share Option Plans (ESOP) available in 2021.   | <input checked="" type="checkbox"/> | CG&RR 23  |
| B.3                                   | Disclosures related to Remuneration in Annual Report  | Financial Statements<br>HRRC report  | <input checked="" type="checkbox"/> | IR 136-330<br>IR 96-97  |
| <b>C. Relations with Shareholders</b> |   |  |                                     |   |
| C.1                                   | Constructive use of the AGM & conduct of General Meetings   | Reporting & Disclosure - Shareholder Engagement and the Annual General Meeting (AGM)   | <input checked="" type="checkbox"/> | CG&RR 24  |
| C.2                                   | Communication with shareholders   | Reporting and Disclosure   | <input checked="" type="checkbox"/> | CG&RR 24  |
| C.3                                   | Disclosure of Major and Material Transactions   | There were no such major or material transactions during the year.   | <input checked="" type="checkbox"/> |   |
| <b>D. Accountability &amp; Audit</b>  |   |  |                                     |   |
| D.1                                   | Present a balanced and understandable assessment of the Company's financial position, performance and prospects                   | Key Board Responsibilities<br>Reporting & Disclosure - Annual Report and Interim Financials<br>Chief Executive Officer's and Chief Financial Officer's Responsibility Statement<br>Annual report of the Board of Directors on the affairs of the Bank<br>Directors Responsibility for Financial Reporting<br>Directors' Statement on Internal Control Over Financial Reporting<br>Management Discussion and Analysis<br>Statement of going concern of the Bank on note 2.1.5, to the Financial Statements<br>Related Party Transactions<br>(i) Note 60 in the Financial Statements<br>(ii) Report of the RPTRC<br>In the unlikely event of the net assets of the Bank falling below 50% of Shareholders Funds, the Board will summon an Extraordinary General Meeting (EGM) to notify the shareholders of the position and to explain the remedial action being taken. | <input checked="" type="checkbox"/> | CG&RR 8<br>CG&RR 24<br>IR 127<br>IR 84-95<br>IR 128<br>IR 111<br>IR 7<br>IR 148<br>IR 318-324<br>IR 109-110 |
| D.2                                   | Process of Risk Management and a sound system of internal control to safeguard shareholders' investments and the Company's assets | Risk Governance<br>Internal Controls<br>Risk & Capital Review<br>Directors' Statement on Internal Control over Financial Reporting   | <input checked="" type="checkbox"/> | CG&RR 18<br>CG&RR 18<br>CG&RR 42-87<br>IR 111   |

| Code Ref   | Requirement   | Reference  | Complied                            | Page Ref             |
|------------|---|--|-------------------------------------|----------------------|
| D.3        | Audit Committee   | Board Audit Committee Report   | <input checked="" type="checkbox"/> | IR 106-108           |
| D.4        | Related Party Transactions Review Committee                             | Board Related Party Transactions Review Committee report                 | <input checked="" type="checkbox"/> | IR 109-110           |
| D.5        | Code of Conduct and Ethics  | Ethical Leadership<br>Chairperson's Message                              | <input checked="" type="checkbox"/> | CG&RR 20<br>CG&RR 2  |
| D.6        | Corporate Governance Disclosures  | Corporate Governance Report  | <input checked="" type="checkbox"/> | CG&RR 4-41           |
| <b>E/F</b> | <b>Institutional and other Investors</b>                                |  |                                     |                      |
|            | Encourage voting at AGM – institutional and other investors             | Reporting & Disclosure   | <input checked="" type="checkbox"/> | CG&RR 24             |
| <b>G.</b>  | <b>Internet of Things &amp; Cyber security</b>                          |  |                                     |                      |
| G.1        | Identify connectivity and related cyber risks                           | Information & Cyber Security Governance<br>Digital Technology Governance | <input checked="" type="checkbox"/> | CG&RR 18<br>CG&RR 16 |
| G.2        | Appoint a CISO and allocate budget to implement a cyber security policy | Information & Cyber Security Governance                                  | <input checked="" type="checkbox"/> | CG&RR 18             |
| G.3        | Include cyber security on Board agenda                                  | Information & Cyber Security Governance                                  | <input checked="" type="checkbox"/> | CG&RR 18             |
| G.4        | Assurance   | Information & Cyber Security Governance                                  | <input checked="" type="checkbox"/> | CG&RR 18             |
| G.5        | Disclosures in Annual Report  | Information & Cyber Security Governance                                  | <input checked="" type="checkbox"/> | CG&RR 18             |
| <b>H.</b>  | <b>Environment, Society &amp; Governance</b>                            |  |                                     |                      |
| H.1        | ESG Reporting   | Integrated Strategy  | <input checked="" type="checkbox"/> | CG&RR 7              |

# Risk & Capital Reviews

The Bank's risk landscape continues to evolve rapidly in response to the prolonged impact of the COVID-19 pandemic. Ongoing business disruptions, the "new normal" and global headwinds continue to impact all aspects of our operation; contributing to greater uncertainty and elevated risk levels. Credit risk remained elevated as businesses continued to experience extreme cash flow constraints amidst sluggish economic conditions due to COVID-19. Market risk factors including currency volatility, trade imbalances and sovereign risks remained a concern. Health and safety concerns and work from home arrangements continued to impact operational risk while cyber risks continued to increase due to the higher dependency on digital networks and work from home arrangements. In the face of these challenges, the Bank continued to strengthen its Risk Management structures, policy frameworks, operational processes and work culture to effectively respond to the evolving risk factors. This report seeks to provide an overview of measures taken by the Bank to safeguard and support its business operations and all stakeholders.



## RISK MANAGEMENT ACHIEVEMENTS IN 2021

- » "Managing risks for sustainable growth and profitability"
- » Bank was not exposed to any Cyber breaches during the year
- » Bank recorded the Lowest Non-Performing Ratio among peers
- » Bank's Operational Losses were an all-time low due to strengthened Operational Risk practices
- » Bank's staff were supported on all health and safety matters thereby ensuring over 98% of the staff are fully vaccinated

## KEY RISKS 2021

The Bank's key risks are those factors that shape the risk profile of the financial industry and the Bank itself.

Many of these factors are inter-linked and inter-dependant, further increasing complexity and vulnerabilities of the risk landscape.

### A Global Pandemic

Recurring waves of the COVID-19 Pandemic throughout 2021 continued to strain health care systems and economies around the world, with emerging economies in particular continuing to face the economic repercussions of capital outflows, business lockdowns and disruption on key industries such as tourism.

### Societal Expectations

Banks and financial Institutions are expected to play a key role in facilitating the post COVID-19 economic recovery of the country by providing essential financial relief to their customers across industries and geographies. Meanwhile with the rapid growth in digital platforms for banking services, higher customer expectations on convenience, reliability, availability of services and security are inevitable.

### Health & Safety

Having in place the infrastructure and processes to implement health and safety protocols such as social distancing, tele-working arrangements etc are becoming a critical necessity as the country gradually opens up and adapts to the new normal post COVID-19.

### People & Behaviours

Behaviours of customers and staff continue to evolve in response to the unprecedented pressures brought about by the COVID-19 pandemic. Working from home, performance pressures, customer behaviours, pandemic related fears and financial stress have all combined to bring about increased and complex challenges for our customers and staff.

### Technology & Cybersecurity

Technology has paved the way for customers to transition to digital platforms as society sought to minimise contact. Cyber threats escalated due to increased volumes of digital transactions and remain a concern as financial stress increases globally. The expansion and enrichment of HNB's digital payment platforms have paved the way for contactless banking with high level of security. The Bank has also invested in increasing the rigor of safeguards against cyberattacks and hacking and also in upgrading the business continuity infrastructure to ensure readiness to any given eventuality

### Foreign currency Restrictions

The Central Bank of Sri Lanka with a view to easing pressure on the exchange rate, introduced several regulations for Banks including the restrictions on purchasing of Sri Lanka International Sovereign Bonds, restrictions on entering into forward contracts of foreign exchange, revoking of short term foreign currency borrowing limits and the imposition of maximum interest rates on foreign currency deposits. These capital controls together with import restrictions and additional exchange controls have had a significant impact on the Banks foreign currency operations.

### Geopolitical Stress

Developments in the Global front including the global economic fallout post COVID-19, rising trade tensions between China and the USA and Brexit implications remain concerns as they impact trade, exchange rates and oil prices.

### Policy Uncertainty

Policy uncertainty remains a key risk with the Government having to take extraordinary policy decisions to support systemic financial stability. Policies aimed at curtailing imports, inflation and interest rates have a direct impact on the banking sector with implications on profitability and liquidity.

### Government Moratorium Programs







The debt moratorium granted to the tourism sector under Circular No. 08 of 2020 dated 26 August 2020 was extended till 30 June 2022. Meanwhile concessions for COVID-19 affected businesses and individuals granted under Circular No. 05 of 2021 dated 25 May 2021 were also extended till December 2021 with provisions for the deferment or restructure of existing performing and non-performing credit facilities. HNB continues to support the Government in these programs and have provided Rs 86 Bn in moratoriums across all customer groups.

# Risk & Capital Reviews

## OUR MATERIAL RISKS

Our material risks are summarized below in Figure 1: Material Risks, and has been signposted to the respective sections for the purpose of providing greater information and analysis.

Figure 1: Material Risks

|                        |  <b>Credit Risk</b>   |  <b>Operational Risk</b>  |  <b>Information &amp; Cyber Risk</b>   |
|------------------------|--|--|---|
| <b>Definition</b>      | The risk of losses due to one or more counterparties failing to meet all or part of their contractual obligations towards the Bank in accordance with agreed terms.  | The risk of loss due to inadequate or failed internal processes, people, and systems or from external events. This definition includes legal risk but excludes strategic and reputational risk   | Risk of financial loss, disruption or damage to the reputation of the Bank from any sort of compromise of information to unintended parties and unauthorized access to our systems or data/information. It also arises from failure of the Bank's information technology systems. |
| <b>Drivers</b>         | Arises from concentration of portfolio by product, business sector, geography etc.; deterioration of economic conditions, rigour of credit evaluation and monitoring processes, Bank's credit risk appetite, internal risk goals and tolerance level, Expectation on government concessions to postpone repayment. | Arises from day-to-day operations and external events.   | Arises from the integration of information technology into all aspects of banking operations which facilitate convenience, scalability and capability but also makes the Bank vulnerable to unauthorized access to systems and information assets.                                |
| <b>Measured</b>        | Based on credit exposure, Probability of Default (PD), expected losses, Loss Given Default (LGD) and recovery rates. NPA ratios, stress testing on concentration, large borrower default, increase in provision etc. Additional capital under Pillar 2 risk is assessed by ICAAP as per Basel III                  | Measured using operational losses, loss events/near misses, key risk indicators, overall risk grid matrix, risk ranking and prioritizing, risk heat map. Capital is allocated under CAR as per Basel III.  | Reference to cyber risk loss limits and cyber risk matrix, hacking attempts for a month.  |
| <b>Monitored</b>       | By Credit Risk Vertical using the Credit Risk Dashboard which provides metrics on several parameters including analysis of arrears, collateral, concentration etc. submitted to BIRMC, BCC and executive committees.   | By Operational risk management vertical under the guidance of ORSC with input from business units through Risk and Control Self Assessments. Operational risk monthly Dashboards are submitted to ERMCP, BIRMC and Board.  | By Information and cyber security risk vertical through a cyber-risk dashboard presented to BIRMC and ERMCP monthly, Monitoring of Privileged User Activities on a periodic basis and report to BIRMC.  |
| <b>Managed</b>         | In accordance with Credit Risk management policy suite supported by dedicated resources for monitoring of arrears, strong documentation, and a proactive approach to resolving issues. Directions issued by CBSL for extending moratoria were used as the basis for rescheduling of facilities.                    | Managed through a sound Operational Risk Management Framework by the ORSC with the participation of all business/support units, availability of comprehensive Business Continuity Plan (BCP) covering all mission critical units and BCP drills conducted periodically | Through the Bank's action plan for digital resilience, awareness programs for staff, business continuity plans, use of physical controls, technical and logical access and administrative controls.   |
| <b>Key Information</b> | Assessment: High<br>Trend: <br>Page 57  | Assessment: High<br>Trend: <br>Page 63  | Assessment: High<br>Trend: <br>Page 67   |



### Liquidity Risk



The risk that the Bank is unable to meet its debt obligations associated due to lack of funds or having to meet these obligations at excessive cost.



### Market Risk



The risk that movements in market factors could reduce our income or value of portfolios.



### Strategic Risk



Refers to uncertainties and untapped opportunities embedded in our strategic intent and how well they are executed.



### Reputation Risk



The loss resulting from damages to a firm's reputation, in lost revenue; increased operating, capital or regulatory costs; or destruction of shareholder value,

Arises from mismatches in cash flow due to potential short-term cash demands placed upon the Bank, by depositors, borrowers, the Bank's own borrowing activity, trading activities and counterparty interactions.

Arises from movement in market factors such as foreign exchange rates, interest rates, credit spreads, equity prices and commodity prices.

Arises from external developments in technology, products, business models.

Arises from events that could adversely impact public perception of the Bank as a responsible corporate citizen.

Measured using a range of metrics including regulatory limits such as the LCR, internal models and balance sheet based measures and stress testing on interest rate sensitivity, probabilistic analysis and NII analysis.

Measured using Value at Risk, Sensitivity analysis and stress testing on open positions, mark to market on daily basis to identify the trading book position. Capital is allocated under CAR as per Basel III

Measured using a scorecard approach to quantify strategic risk under the Basel III Pillar 2 calculation.

Measured using a scorecard approach by assessing underlying risk drivers of reputational risk due to qualitative nature of the risk

Monitored by ALCO and Treasury Middle Office (TMO) using a matrix of regulatory and prudential limits and gaps using both stock and flow approaches, dashboards submitted to ALCO and BIRMC and Board.

Monitored by ALCO using Market Risk Dashboards supported by an independent Treasury Middle Office (TMO) which reports to CRO. Internal and regulatory limits and exceptions are immediately reported to ALCO

Monitored by the Integrated risk management unit through a scorecard and evaluated for any additional capital requirement through the ICAAP submission to Board annually.

Monitored by the Integrated risk management unit through a scorecard and evaluated for any additional capital requirement through the ICAAP submission to Board annually

Managed through a strong liquidity risk management Framework which includes contingency plans with both contracted and un-contracted liquidity positions with liquidity buffers and liquidity ladders.

Managed by Treasury within a robust market risk management framework, market risk limits, through diversification and hedging strategies.

Managed at corporate management and Board level with reference to market developments and potential disruptions to current business model Assessments.

Managed by setting the tone at the top and reinforcing its core values and purpose. A Reputation Risk Task Force was established as a sub-committee of ORSC to manage risk in case of trigger events.

Assessment: Moderate

Trend: →

Page 69

Assessment: Moderate

Trend: →

Page 69

Assessment: Moderate

Trend: →

Page 79

Assessment: Moderate

Trend: →

Page 79

# Risk & Capital Reviews

## ENTERPRISE RISK GOVERNANCE

The Bank's risk governance structure ensures that, roles and responsibilities for risk management are clearly defined and given due attention to key aspects of risk management, facilitating high levels of specialisation in these identified areas. The Board has the ultimate responsibility for managing risk and is assisted by the Board Integrated Risk Management Committee (BIRMC) who has oversight responsibility for risk management while the executive functions are responsible for the effective implementation of the risk management framework. Executive committees serve to draw on the collective experience and wisdom of corporate and senior management teams and play a key role in the delegation of authority as well.

The Bank's risk governance structure is based on the Three Lines of Defence model in line with best practice.

### Three Lines of Defence



The Bank continues to strengthen these lines of defence in response to the evolving risk landscape. The appointment of a separate Chief Information Security Officer in July 2020 strengthened the Information Security governance and the overall Information Security framework of the Bank. In 2021 the

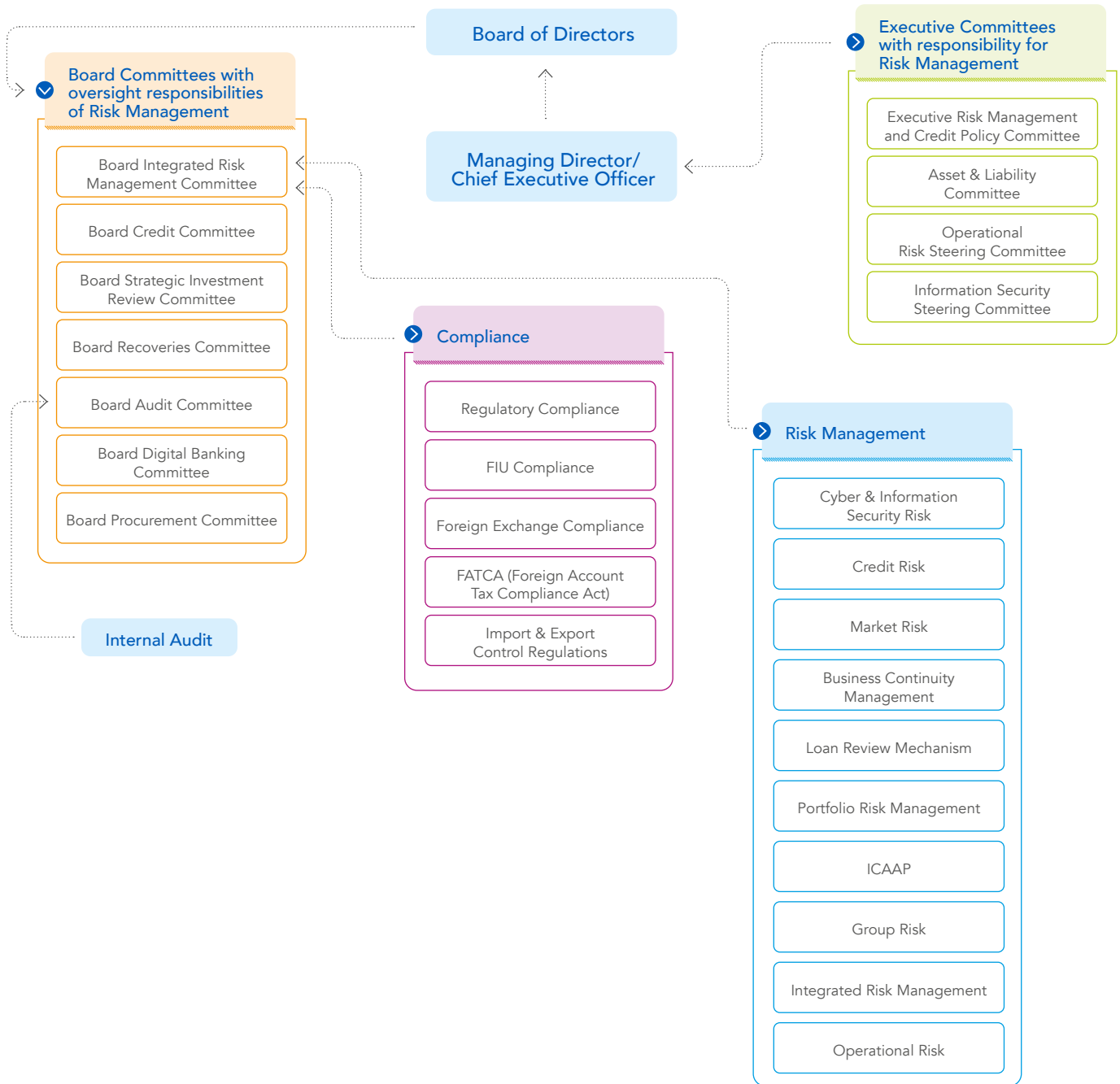
Risk Management Department functions were further streamlined to increase the focus on the monitoring and advisory functions.

The Branch Operating Model (BOM) initially implemented in 2019 was further reinforced, strengthening the first line of defence with

clear segregation of relationship management. Additionally, operational processing at branches was streamlined with higher levels of specialization throughout the Branch workflow processes.



Figure 2: Risk Governance Structure of the Bank



# Risk & Capital Reviews

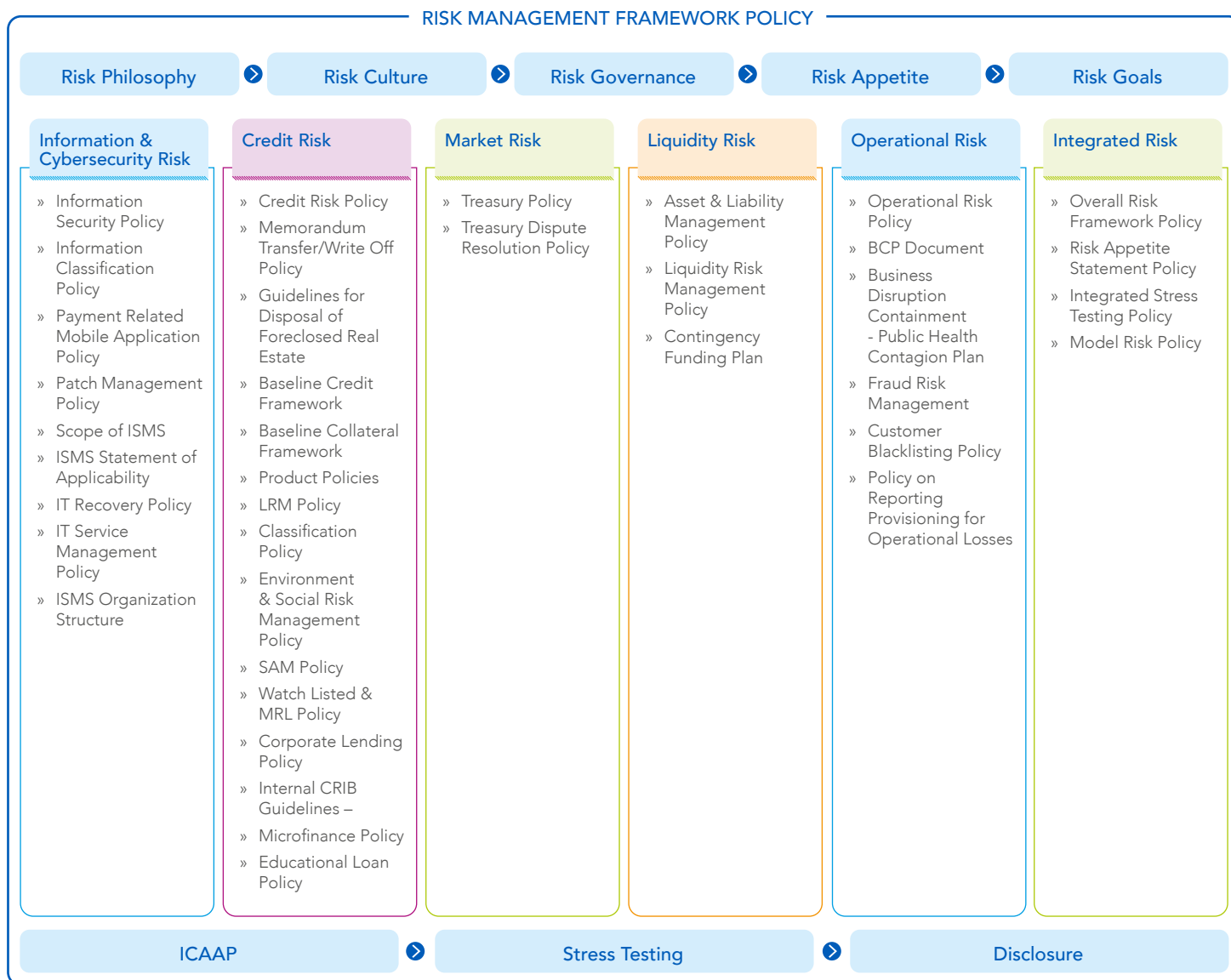
Figure 3: Roles & Responsibilities of Committees in Relation to Risk Management

| Board Committees  | Role of Committee in Relation to Risk Management   |
|---|--|
| Board Integrated Risk Management Committee (BIRMC)              | This Committee has the responsibility of oversight for Risk Management and makes recommendations to the Board on developing and implementing Risk Management Policies, setting the Bank's Risk Appetite and monitoring material risks of the Bank through risk dashboards. The Chief Risk Officer and Chief Compliance Officer have a direct technical reporting line to the BIRMC.  |
| Board Credit Committee (BCC)                                    | BCC has the responsibility of oversight for the management of Credit and approves credit granted above a specified exposure threshold. BCC reviews the Credit Risk dashboards and makes recommendations on areas including credit limits, sector-wise exposure, sector risks, or any other related areas concerning Credit Risk Management policies and processes.   |
| Board Recoveries Committee (BRC)                                | This Committee of the Board is set up to strengthen the delinquent loan recovery function of the Bank. BRC has oversight responsibility for recoveries of advances and provides strategic directions to ensure speedy recovery of defaulting and stressed facilities.  |
| Board Audit Committee (BAC)                                     | BAC has responsibility for financial reporting risk and the effective operation of internal controls. The Bank's Chief Internal Auditor has a direct technical reporting line to the BAC. This Committee plays a key role in the implementation of the Bank's risk management and compliance policy by the monitoring of key controls.   |
| Board Strategic Planning & Investment Committee (BSPIC)         | This Committee sets the overall business strategy of the Bank and ensures there is a congruence in the Bank's strategic direction, goals and KPIs and the Board's Risk Appetite.   |
| Board Digital Banking Committee (BDBC)                          | This Committee has the responsibility of oversight mainly in relation to the Bank's implementation of its proposed Digital Banking Platform and Products. The Committee reviews key technology risks and associated strategies including overall risk profile of the Bank's digital proposition and is responsible for identifying and monitoring of key risks arising from the Digital area and refers such risks to the Risk Department and Compliance Department for advice and action. |
| Board Procurement & Asset Disposal Committee                    | This Committee is primarily responsible for assessing proposals submitted by the management for procurement of assets or disposal of assets/ disposal properties of the Bank and ensures transparency in procurement/disposal processes and good practices.  |
| Executive Committees  | Role of Committee in Relation to Risk Management   |
| Executive Risk Management and Credit Policy Committee (ERMPCPC) | ERMPCPC is the apex executive committee for risk management and supports BIRMC and BCC in effective implementation of the policy framework in monitoring and managing risk. This key committee is chaired by MD/CEO and comprises heads of key business lines and operating units of the Bank.   |
| Asset & Liability Committee (ALCO)                              | ALCO plays a key role in managing liquidity risk and financial stability of the Bank. It reviews liquidity forecasts to manage gaps, adequacy of contingency funding plans and stress testing results in achieving its objectives. The Committee also determines the ideal structure of the Bank's balance sheet to provide the optimal profitability while minimizing potential risks.  |
| Operational Risk Steering Committee (ORSC)                      | The key activity of this Committee is to critically assess operational processes and internal controls with a view to ensuring operational losses are minimised and that a compliance and adherence culture is instilled amongst the Bank staff. This Committee is chaired by COO and comprises of DGM-Risk/CRO, Heads of Operations, Audit, Compliance, IT, HR and Network Management.  |
| Information Security Steering Committee (ISSC)                  | ISSC is responsible for assessing and making recommendations on Bank Wide Information Security and Cyber security initiative to manage relevant risk exposures. The Committee is chaired by MD/CEO and comprises of representatives from corporate business, IT, Audit, Compliance and Support Functions.  |

## RISK MANAGEMENT POLICY FRAMEWORK

The Bank's underlying premise for managing risks is to ensure sustainable growth in economic value for the Bank and all of its stakeholders including shareholders, customers, suppliers, employees, investors, the general public and the CBSL. As a "Systemically Important Bank" (SIB) in Sri Lanka, it is imperative that HNB carefully manages its risks to ensure that the Bank creates value to the economy and eco systems that it operates in. The Bank's risk management framework aims to establish a process to effectively identify, measure, manage, monitor and control risks faced by the Bank and to determine its Risk Appetite in line with the overall business strategy of the Bank. The Board approved risk management policies provide guidance to the management on implementing processes within the Bank.

Figure 4: Risk Management Policy Framework



# Risk & Capital Reviews

## RISK CULTURE

A strong risk culture ensures a bottom-up approach to risk management and is critical for effective risk management of the Bank. The Bank's risk culture which is shaped by a comprehensive risk management policy framework is supported by mandatory training and capacity building, a strong code of conduct applicable to all employees and a remuneration framework that rewards a balanced approach to risk. Collectively, these mechanisms emphasise the Bank's attitudes, norms, and behaviours in relation to risk awareness, acceptance and management which is the key to sustainable growth and profitability.

Figure 5: Key Determinants of Risk Culture

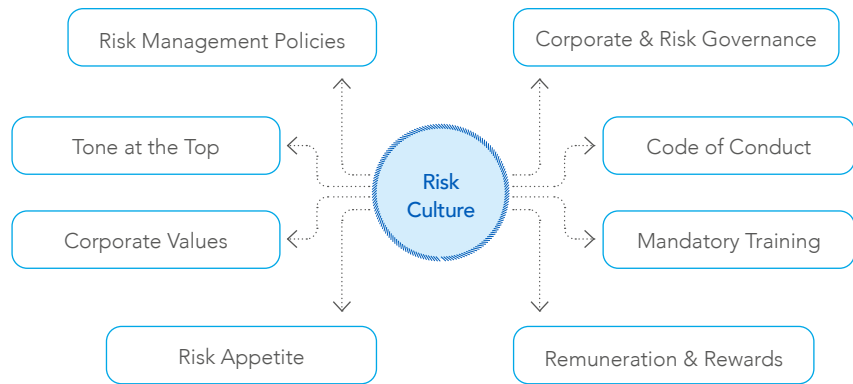
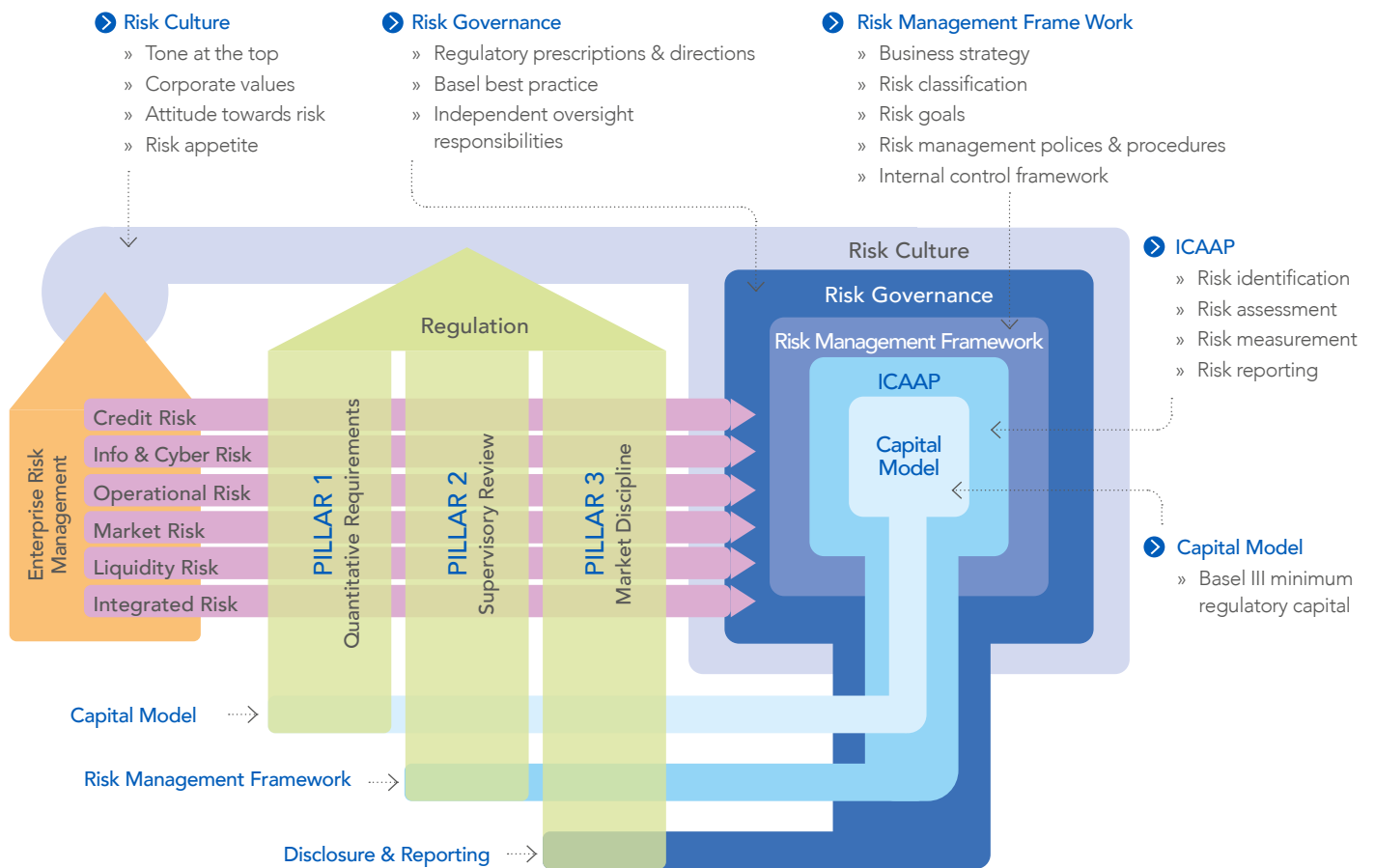


Figure 6: HNB Philosophy in Managing Risk



## RISK APPETITE

The Risk Appetite Statement sets targets for quantitative elements such as capital adequacy, profitability and efficiency, concentration limits, liquidity positioning and limits for other risk types. Limits are set considering economic & market conditions and familiarity of business.

The Risk Appetite Framework (RAF) of the Bank aims to achieve the following objectives:

- » Link the Bank's business strategy, products and processes with associated risk levels
- » Design Risk Appetite and thresholds in line with the Risk Management Framework of the Bank
- » Enable the Senior Management and the Board of Directors (BOD) to effectively monitor the material risks across various business units of the Bank, and take corrective actions, as and when required
- » Compliance to regulatory principles on Risk Appetite requirements

## STRESS TESTING

Stress Testing assesses the resilience of the Bank to movements in financial variables, which could impact the Bank's profitability, liquidity and capital adequacy. The Bank's Stress testing framework complies with the guidelines issued by CBSL and the Basel Committee, encompassing all significant and high impact risk areas of the Bank. Appropriate stress scenario development methodologies applicable to each risk area are clearly specified. The identification of key macroeconomic factors impacting the Bank, methodologies for assessing stress conditions and the feedback from key business drivers support this key process. Key principles driving the stress testing framework are as follows:

- » Stress testing framework is based on an effective governance structure, with clearly documented responsibilities across the first line, second line and third line of defence
- » The stress testing framework is a key risk management tool within the Bank employed to ensure readiness of the Bank to face adverse events and drive business strategies and decisions

- » The stress testing framework aims to capture material and relevant risks that apply across its business and apply stresses that are sufficiently severe
- » The models and methodologies to assess the impact of scenarios and sensitivities need to be fit for purpose, and are regularly reviewed to ensure their effectiveness and relevance
- » The stress test framework, models, and results are subject to challenge and regular review

The main object of stress testing is to assess the impact of adverse scenarios on the Bank's Capital Adequacy Ratio (CAR). Once all the Stress Tests for various risk factors are performed, the net impact on the Bank's CAR is assessed.

Results of stress testing are reviewed by BIRMC of the Bank within the defined risk appetite and these are also communicated to the Board. Certain trigger actions are predetermined at defined risk levels and action taken in this manner are also communicated to BIRMC and to the Board.

## GROUP RISK

The Bank has four direct subsidiaries and managing risks arising from the operations of these entities is necessary to ensure the resilience of the HNB Group. The Integrated Risk Management Division of the Risk Management function has overall responsibility for managing Group Risk and receives regular risk reports from the subsidiaries. Two direct subsidiaries are public listed companies and comply with the regulatory reporting requirements of the Colombo Stock Exchange. Additionally, HNB Assurance PLC and HNB General Insurance Ltd., are regulated by the Insurance Regulatory Commission of Sri Lanka and HNB Finance PLC is regulated by CBSL and comply with the requirements of their respective legal enactments and other regulatory directions and guidelines. The two insurance companies and HNB Finance PLC have their own dedicated risk management functions which liaise with the Bank's IRM division, providing relevant information to facilitate monitoring of risks stemming from the operation of these subsidiaries.

In addition to having senior officials of the Bank on the Board of the subsidiaries, IRM also receives the Regulatory Inspection Reports and Management Letters of the Group entities to ascertain potential areas of risk concern and follow up on agreed remedial action to strengthen the risk management environment.

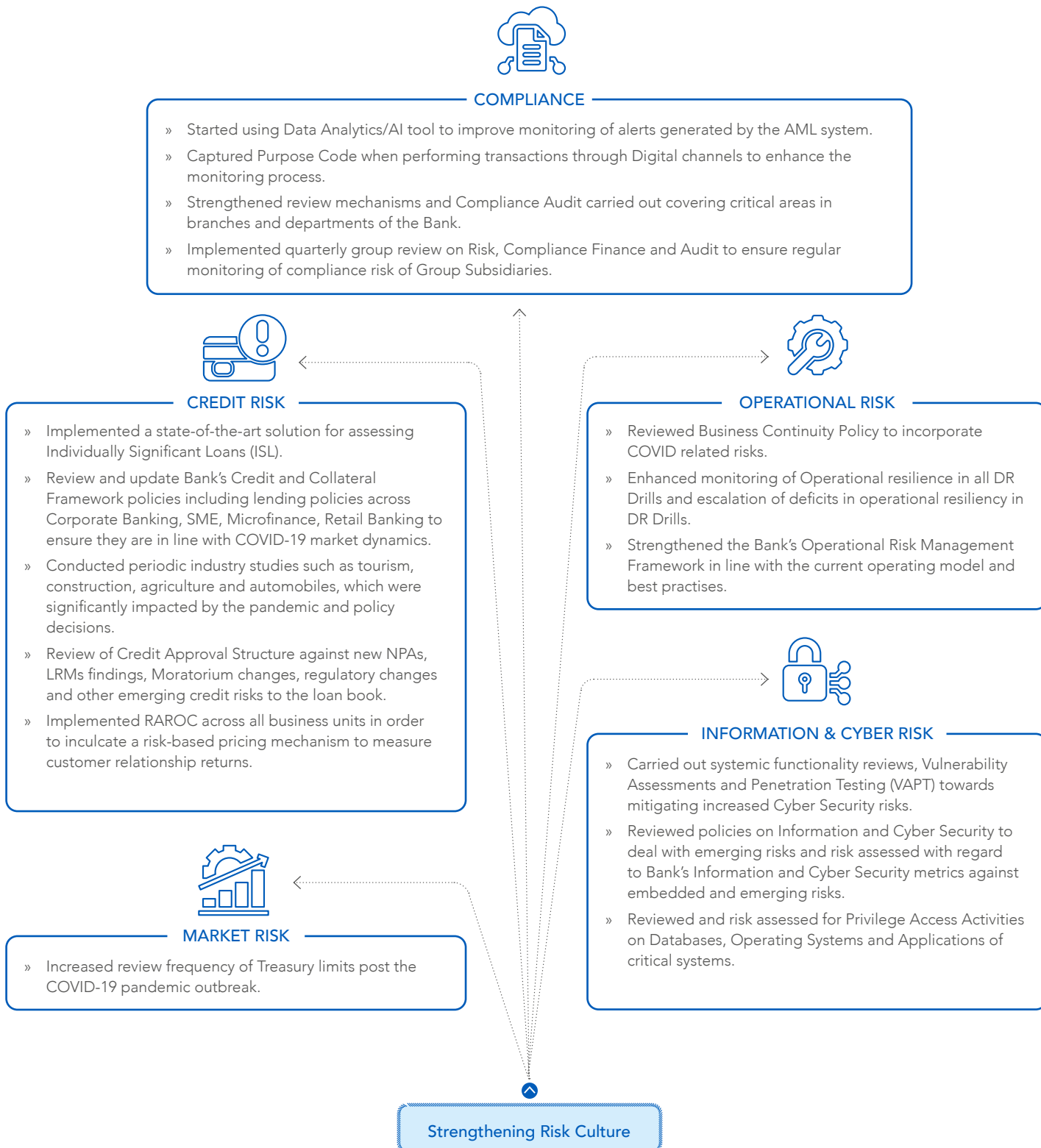
## STRENGTHENING RISK MANAGEMENT IN 2021

Risk management is a dynamic function that needs to constantly evolve in response to increasing systemic financial and operational risks. Recent advances in technology provide a multitude of tools and techniques that can significantly enhance risk management capabilities. As a transformational bank, HNB continues to adopt these developments in order to strengthen its risk management capabilities and overall resilience.

The Bank continued its timely submission of Statutory Reports such as the ICAAP report to Regulator despite challenges encountered with COVID 19, reflecting the resilience of this key function.

# Risk & Capital Reviews

Figure 7: Key Initiatives of the Bank to Strengthen Risk Management in 2021



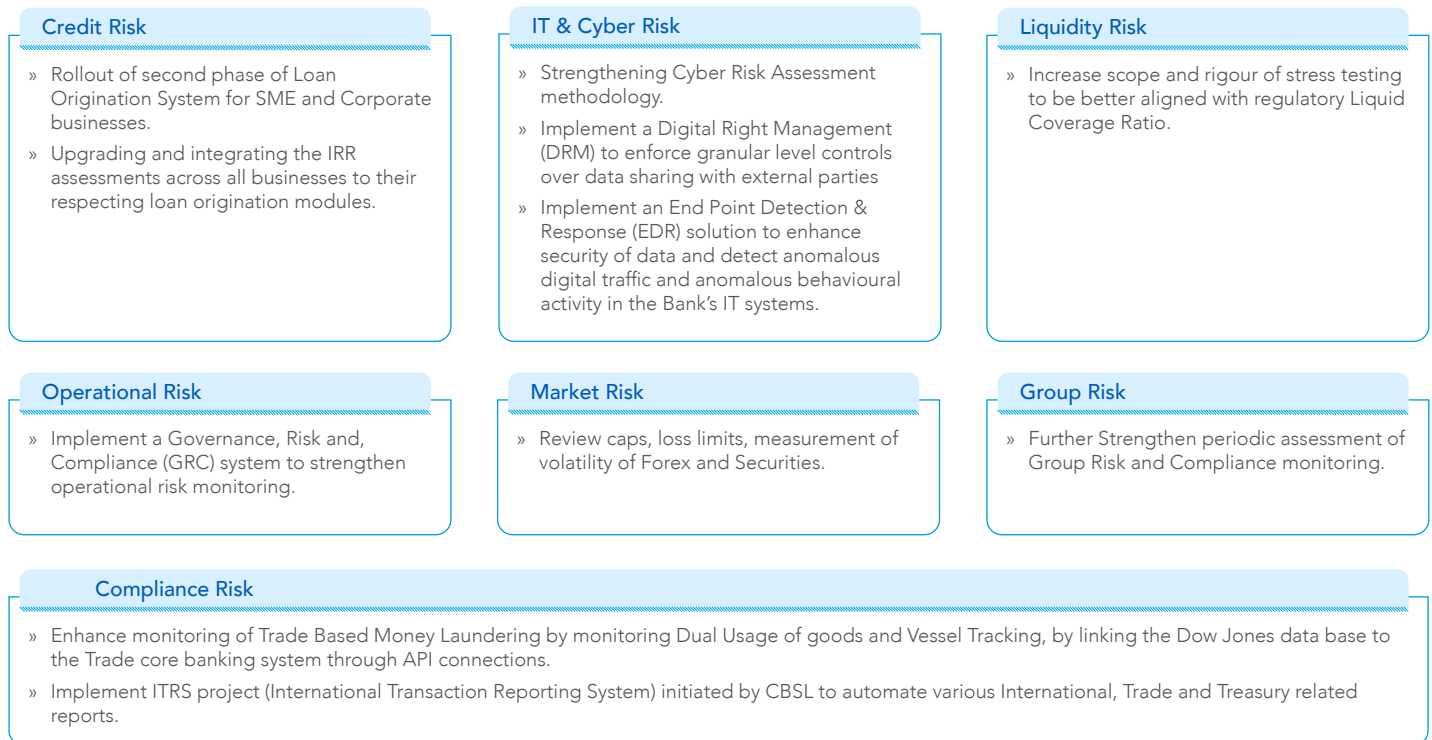
## PLANS FOR 2022

With the banking sector expected to continue to face risks in terms of pressures on foreign currency liquidity, prolonged moratoria to pandemic affected borrowers and increasing threats pertaining to IT and cyber-security;

it is imperative that we adopt a dynamic approach to risk management. Technology will be a key enabler going forward as we seek to enhance our capabilities and build resilience. Meanwhile we will accelerate several of

projects that we were compelled to defer due to the disruptions caused by the pandemic. Key projects planned for 2022 are listed below.

Figure 8: Planned Initiatives To Strengthen Risk Management In 2022



# Risk & Capital Reviews

## INTEGRATED RISK MANAGEMENT & CAPITAL MANAGEMENT

### Regulatory Capital

ICAAP is managed in compliance with the Banking Act Direction No. 1 of 2016 Capital Requirements Under Basel III for Licensed Commercial Banks and Licensed Specialised Banks which specifies the minimum capital ratios and buffers in respect of total risk weighted assets phased out between 1st July 2017 and 1st January 2019. CBSL issued three directions on reclassification of Domestic Systemically Important Banks and revision to the compliance requirement of Basel III direction

namely, No 10,11 and 12 of 2019. These amended the composition of Domestic Systemically Important Banks (D-SIB), revised the compliance requirement of Basel III directions in 2019 amending the composition of D-SIBs and revised the requirement of applicable Higher Loss Absorbency (HLA). Accordingly, HNB is required to maintain a CETI 1.0% of Risk-Weighted Assets as HLA as opposed to 1.5% as per Direction No 01 of 2016. Requirements relevant to HNB are given below:

Figure 9: Regulatory Capital Requirements

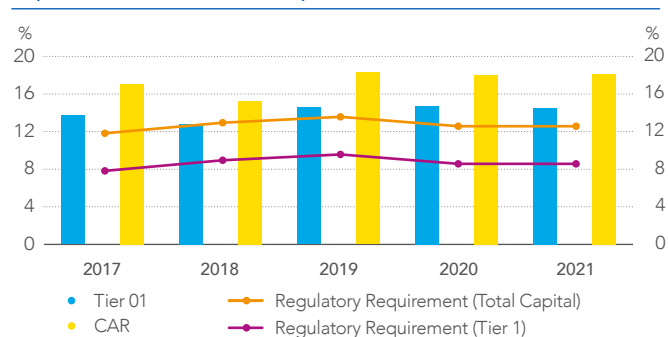
| Components of Capital                     | Regulatory Requirement as at |            |            | Bank's Position as at |            |            |
|---|------------------------------|------------|------------|-----------------------|------------|------------|
|   | 31.12.2019                   | 31.12.2020 | 31.12.2021 | 31.12.2019            | 31.12.2020 | 31.12.2021 |
| Common Equity Tier (CET) 1 <sup>(a)</sup> | 8.0%                         | 7%         | 7%         | 14.57%                | 14.73%     | 14.53%     |
| Total Tier 1 <sup>(a)</sup>               | 9.5%                         | 8.5%       | 8.5%       | 14.57%                | 14.73%     | 14.53%     |
| Total Capital <sup>(a)</sup>              | 13.5%                        | 12.5%      | 12.5%      | 18.28%                | 17.98%     | 18.16%     |

(a) Including Capital Conservation Buffer and Capital Surcharge on Domestic Systemically Important Banks

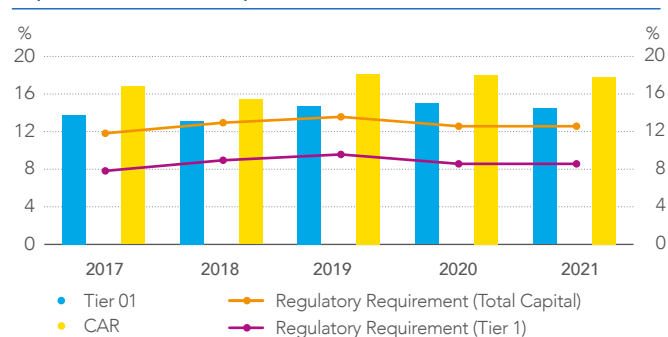
Extraordinary regulatory measures taken by CBSL to provide flexibility licensed banks to support businesses and individuals affected by the outbreak of COVID-19 included a deferment of the Rs.20 Bn requirement for Licensed Commercial Banks. However, as HNB had already complied with the requirement, this had no impact on the Bank.

Figure 9 depicts the components of the Bank's capital and compliance with regulatory requirements. Basel III Market Discipline, Minimum Disclosures Under Pillar 3 are given on Page 100 as required by CBSL Direction No 1 of 2016.

### Capital Adequacy - Banking Operations



### Capital Adequacy -Group



### Risk Weighted Assets

Capital requirements are measured as a percentage of Risk Weighted Assets which are calculated on the following basis as per CBSL direction No.1 of 2016:

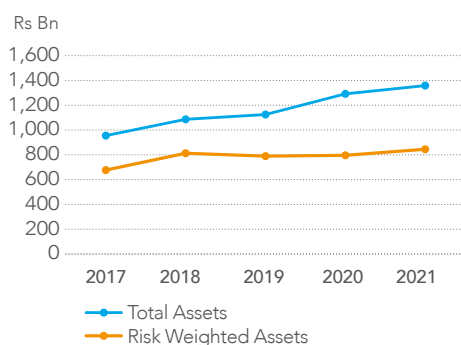
- » Credit Risk – The Standardised Approach
- » Market Risk – The Standardised Measurement Method
- » Operational Risk – Basic Indicator Approach



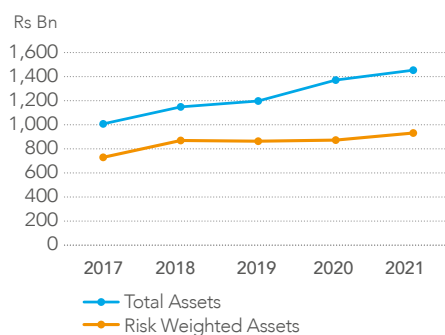
Figure 10: Risk Weighted Assets & Capital Charge

| Item<br>Rs.'000  | Risk Weighted Assets |                    | Capital Required  |                    |
|------------------|----------------------|--------------------|-------------------|--------------------|
|                  | 2020                 | 2021               | 2020              | 2021               |
| Credit Risk      | 724,293,579          | 770,527,810        | 90,536,697        | 96,315,976         |
| Market Risk      | 832,706              | 1,495,688          | 104,088           | 186,961            |
| Operational Risk | 70,963,945           | 73,034,096         | 8,870,493         | 9,129,262          |
| <b>Total</b>     | <b>796,090,230</b>   | <b>845,057,594</b> | <b>99,511,297</b> | <b>105,632,199</b> |

#### Total Assets Vs. Risk Weighted Assets Bank

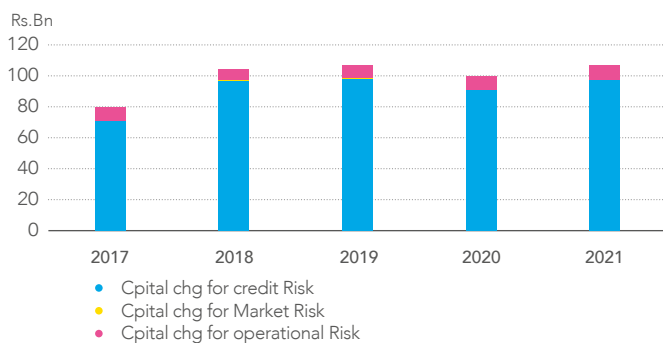


#### Total Assets Vs. Risk Weighted Assets Group

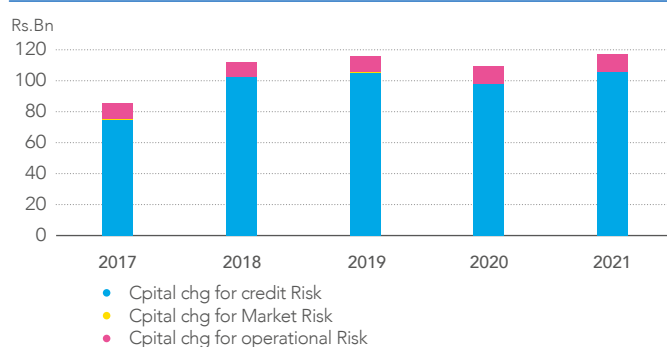


RWAs increased by Rs 49 Bn during the year to Rs 845 Bn. The difference between Total Assets and Risk Weighted assets increased during the year to Rs 513 Bn.

#### Capital Charge for Risk- Bank



#### Capital Charge for Risk - Group



## STRESS TESTING

Stress testing is a key component of Capital Planning as detailed on page 51. Extracts from the Bank's comprehensive stress tests on the Bank's CAR are given below for the highest risk indicator in each major risk category.

# Risk & Capital Reviews

Figure 11: Stress Testing Results On A Moderate Stress Scenario

|   |  | Impact on CAR as at 31.12.2020 |                 |               |
|---|--|--------------------------------|-----------------|---------------|
|   |  | High Impact                    | Moderate Impact | Severe Impact |
| NPL Stress  | Increase in NPL ratio for different portfolio and thereby increase in provision.   | ✓                              |                 |               |
| Credit Risk – Asset Downgrade                           | Increasing the direct non-performing facilities over the direct performing facilities balance for the entire portfolio.  | ✓                              |                 |               |
| Credit Concentration Risk – Large Borrowers Default     | Default of the higher borrowers by classifying the credit granted to them as non-performing.   | ✓                              |                 |               |
| Credit Concentration Risk – HHI                         | % increase in HHI under stress.  | ✓                              |                 |               |
| Interest Risk in Banking Book (IRRBB) EAR and EVE (LKR) | To assess the long-term impact of changes in interest rates on Bank's Economic Value of Equity (EVE) through changes in the economic value of its assets and liabilities and to assess the immediate impact of changes in interest rates on Bank's earnings through changes in interest rates on Bank's earnings through changes in its Net Interest Income (NII). | ✓                              |                 |               |
| Foreign Exchange Risk                                   | % shock in the LKR exchange rate against all other currencies.   | ✓                              |                 |               |
| Liquidity Risk  | Deposit runs and rollovers   | ✓                              |                 |               |
| Global Financial Crisis (Multiple Scenarios)            | 1. Adverse changes in Foreign Exchange Rates<br>2. Interest Rate Risk<br>3. Liquidity  | ✓                              |                 |               |
| Overall Credit Portfolio Deterioration                  | 1. NPL Stress<br>2. Asset Downgrade<br>3. Concentration Increase   | ✓                              |                 |               |

## ACTIVITIES IN 2021

### Integrated Risk Management

Key activities implemented to enhance the Bank's management of integrated risk are as follows:



## CREDIT RISK MANAGEMENT

Credit Risk which arises from the Bank's lending and investment activities, present the largest risk exposure for the Bank. As at 31 December 2021 Assets with exposure to credit risk accounted for Rs 1,317 Bn, equivalent to 97% of Total Assets. The Bank manages this key exposure in accordance with the Credit Risk Policy suite whilst continuing to strengthen its credit risk capabilities in response to elevated risk factors in the operating environment.

### Definition

The risk of financial loss to the Bank if a customer or a counterparty to a financial instrument fails to meet its contractual obligations

### Credit Risk Components

- » Default Risk
- » Counterparty Risk
- » Concentration Risk
- » Residual Risk
- » Recovery Risk

|  | 2021<br>Maximum<br>Exposure<br>Rs. 000's | 2020<br>Maximum<br>Exposure<br>Rs.000's | %        |
|--|--|---|----------|
| Maximum Credit Exposures   | 1,473,319,693                            | 1,415,525,837                           | 3.94%    |
| - Total Assets subject to Credit Risk                                | 1,317,640,574                            | 1,256,507,315                           | 4.70%    |
| - Off Balance Sheet Commitment subject to Credit Risk                | 155,679,119                              | 159,018,522                             | (2.10%)  |
| - Max Exposure to credit risk Gross Loans & Receivables to customers | 928,971,730                              | 814,543,457                             | 14.05%   |
| - Net exposure to credit risk of Loans & Receivables to Customers    | 380,445,266                              | 328,972,999                             | 15.55%   |
| Impaired Loans   | 63,635,083                               | 63,035,895                              | 1%       |
| Provisions for impairment  | 52,717,037                               | 41,962,735                              | 25.6%    |
| - Individual Impairment  | 25,005,778                               | 20,195,010                              | 23.82%   |
| - Collective Impairment  | 27,711,258                               | 21,767,725                              | 27.3%    |
| Impaired Loans as a % of gross Loans and Receivables                 | 6.85%                                    | 7.74%                                   | 13%      |
| NPA (Gross)  | 3.38%                                    | 4.31%                                   | (21.58%) |

## CREDIT RISK REVIEW

Maximum exposures to credit risk increased by 14% reflecting a growth in loan exposure due to a gradual pick up in private credit demand in 2021. Non-Performing Advances were curtailed at 3.38% of gross advances of the Bank and the lowest NPA among peers reflecting the effectiveness of strengthened credit processes. Importantly, the Bank was able to reduce the number and value of moratoriums during the year, working proactively with clients to consider the long term impact of moratoriums on their businesses.

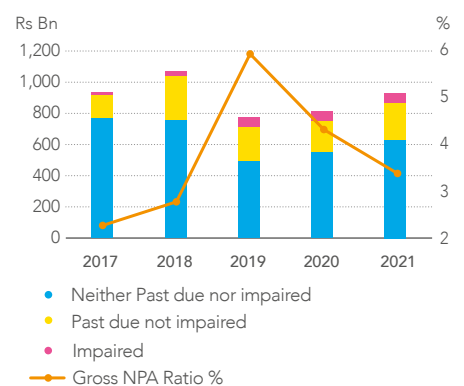
Provisions for impairments increased by 26% due to heightened threats of the

operating landscape. Allowance for individual impairments increased by 24% to Rs 25 Bn while allowance for collective impairments increased by 27% to Rs 27.7 Bn. Impairment allowance coverage is 51.73%.

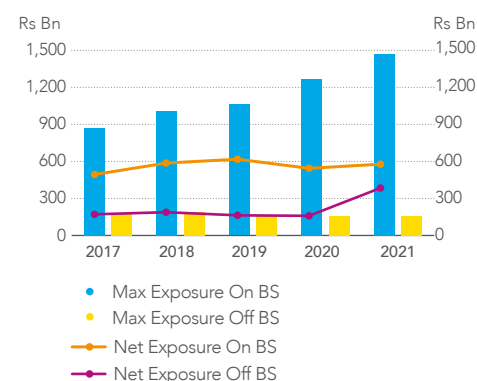
## REGULATORY CHANGES

The COVID pandemic has had a significant impact on Credit Risk with borrowers' repayment capacity being significantly challenged. Accordingly, the debt moratorium granted to the tourism sector under Circular No. 08 of 2020 dated 26 August 2020 and Circular No. 10 of 2021 dated 13 September 2021 was extended till 30 June 2022. Meanwhile concessions for COVID-19 affected businesses and individuals granted under

## Credit Quality



## Credit Exposure



Circular No. 05 of 2021 dated 25 May 2021 and Circular No. 08 of 2021 dated 1 September 2021 were also extended till December 2021 with provisions for the deferment or restructure of existing non-performing credit facilities.

CBSL also issued a direction for the classification, recognition and measurement of financial assets other than credit facilities with a view to strengthening and harmonizing the regulatory framework with SLFRS 9: Financial Instruments.

# Risk & Capital Reviews

## ACTIVITIES IN 2021

Key activities implemented to enhance the Bank's management of credit risk are as follows:

### Policy Framework and Reviews

- » Reviewed Credit Policies and Guidelines to ensure applicability to current market conditions.

### Strengthening Processes

- » Strengthened guidelines to capture customer behaviour analytics facilitating identification of early warning signs.
- » Introduced additional credit evaluation criteria across all product portfolios aligning to the challenging business environment.
- » Completed the implementation of the new fully integrated Retail Loan Originating System (LOS) module across all branches in the network.
- » Introduced an enhanced TOD management process to identify and report on exceptions to the TOD approval guidelines.
- » Provided valuable inputs to business units for decision making by making improvements to the monthly Portfolio Risk Dashboards that are circulated.
- » Strengthened controls over Margin Trading products in view of the volatility of underlying market variables.

### Monitoring

- » Introduced additional guidelines to strengthen identification of Watchlist and Management Review List (MRL) customers in order to take corrective action at the earliest instance.
- » Monitored and reviewed the portfolios under moratoriums in order to proactively take steps to restructure facilities including identifying those that require greater credit supervision.
- » Reviewed large group exposures of the Bank with emphasis on exposures related to moratoria and elevated credit risk on quarterly basis.
- » Reviewed COVID-19 impacted industries to assess implications to Bank's lending portfolio.
- » Carried out the annual review of the LRM Policy aligning with the Bank's focus on increasing credit underwriting standards and quality of the lending portfolio given the current challenging business environment.
- » Enhanced the scope of LRM reviews to capture the learnings from new additions to NPA, Watch Listed and Management Review List, accounts approved for Parate Auctions and highlighted areas for improvement in credit underwriting and monitoring.
- » LRM findings were circulated to Corporate Management for remedial action and also followed up on these corrective measures taken to ensure effective implementation. Additionally, the LRM unit also followed up on the implementation of Internal Audit Review recommendations with relevant business and operational units.
- » Introduced a new reporting process to effectively monitor and manage the temporary overdraft portfolio i.e. identifying and reporting exceptions to the new TOD approval guidelines.
- » Implemented state-of-the-art solution for Individually Significant Loan (ISL) assessments for measurement of expected credit loss.

### Internal Risk Rating Models

- » Existing IRR assessment process was streamlined till the introduction of fresh Models.

### Strengthening Risk Culture

- » Commenced circulation of credit bulletin to share organisation learnings on credit risk management to enhance credit underwriting and evaluation capabilities in the Bank

## CREDIT RISK GOVERNANCE

Extensive changes to the Credit Risk governance structure were implemented in 2019 which included the establishment of the Board Recoveries Committee, roll out of a new Branch Operating Model and the establishment of a separate Credit Management vertical which significantly strengthened the credit risk governance structure and remain in place. The Risk Management Department function meanwhile was further streamlined to focus on the monitoring and advisory functions, in order to enhance objectivity.

### Approved Regulatory Capital Approach

The Bank uses the Standardised Approach to measure the capital charge for Credit Risk as required by CBSL Direction No.1 of 2016. Accordingly, specific risk weights are applied to net counterparty exposures in defined categories after recognising a limited set of qualifying collateral. Template 9: Credit Risk under Standardised Approach: Exposures by Assets Classes and Risk Weights on page 96 provide details according to risk weights while

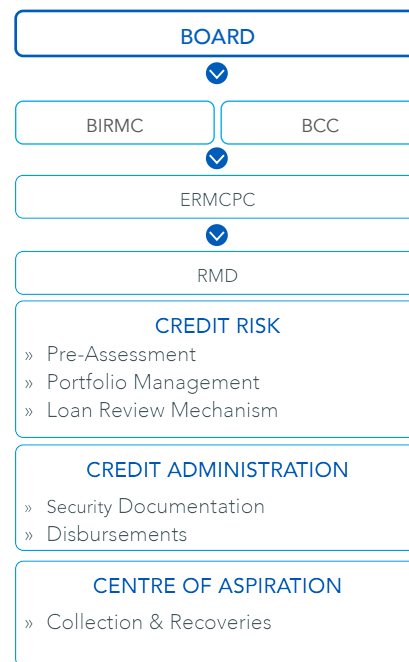
Template 8: Credit Risk under Standardised Approach on page 94 details the computation of Risk Weighted Assets for Credit Risk.

### Internal Risk Ratings

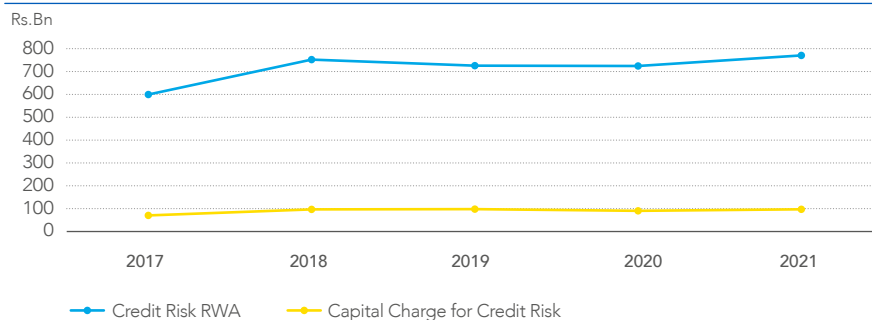
The Bank has developed its own Basel III compliant Internal Risk Rating to progress to the more advanced Internal Ratings based approach to computing the charge for Credit Risk. Further, the Internal Risk Ratings also serve to strengthen our capability to manage default risk.

Internal risk rating models for Large Corporate, Mid-Market, Financial Institutions and SME were validated and recalibrated in 2019. Discussions are currently underway to extend the rating models to the entire credit portfolio including retail and micro finance. Meanwhile plans are also underway to recalibrate existing IRR models to align with current market developments.

Figure 12: Credit Risk Governance



## RISK WEIGHTED ASSETS & CAPITAL CHARGE FOR CREDIT RISK



### Credit Risk Management Processes

The Bank has a comprehensive suite of Credit risk management tools, controls and processes ensuring that Credit Risk is managed throughout the lifecycle of the loan.

- » **Segregation of credit risk management tasks at branch level** – The new branch model has a clear segregation of duties between relationship management/ sales and the loan approval process for SME and retail segments facilitating high

levels of specialisation. Separation of recoveries from these functions enabled focused attention on this vital area with monitoring at management and Board levels. Consequently, the Credit Risk vertical is able to measure, monitor and make recommendations at portfolio level for managing credit risk in line with the Bank's risk appetite.

- » **Independent Risk Assessment** – Corporate, Emerging Corporates and SME facilities are independently reviewed by the Credit Risk

Management function. Retail facilities are reviewed by the Centre of Excellence (COE) enabling high levels of specialisation, and improved turnaround times.

- » **Delegation of Authority** - Approval of credit facilities above a specified threshold have been assigned to Credit Approval Committees. The Credit Risk management division provides its assessment on credit facilities prior to approval of facilities in order to support decision making of the relevant approving committee.

# Risk & Capital Reviews

» **Internal Risk Ratings** – Risk rating are assigned to borrowers above a certain threshold using the Internal Risk Rating framework, which has been approved/ accepted by the regulator. Since 2021, the Bank also computes the Risk adjusted return on capital (RAROC) for corporates and emerging corporates across the portfolio to assess the risk returns of customer relationships

» **Loan Origination System (LOS)** – The new Retail Loan Originating System (LOS) was rolled out across all branches during the year, automating existing manual credit evaluation/approval processes. This supports uniform under writing and evaluation of all retail credit product applications as per Bank’s credit principles of. The system is integrated with the core banking system, security documentation and other peripheral systems maximizing efficiencies, strengthening controls and the quality of management information for monitoring credit risk.

» **Collateral** – The Bank obtains collateral as a secondary recourse through mortgage bonds over movable and immovable property, guarantees, liens over financial assets and assignments of receivables. Regular valuations are carried out to ensure adequacy of collateral throughout the lifecycle of the loan.

» **Security Documentation and Disbursement** – The Centralised Security Repository centre checks completeness and authenticity of documentation including security documentation and compliance with pre-disbursement conditions. This function supports compliance and recovery processes with required documentation while the pre-disbursement function ensures that correct limits and rates are marked in the system facilitating accurate billing, monitoring and recovery processes.

» **Loan Review Mechanism** – The LRM function carries out post reviews of credit facilities covering all business lines to identify qualitative improvements in credit evaluation and administration processes and gain insights regarding the effective functioning of processes and controls in place. Reports from LRM are submitted

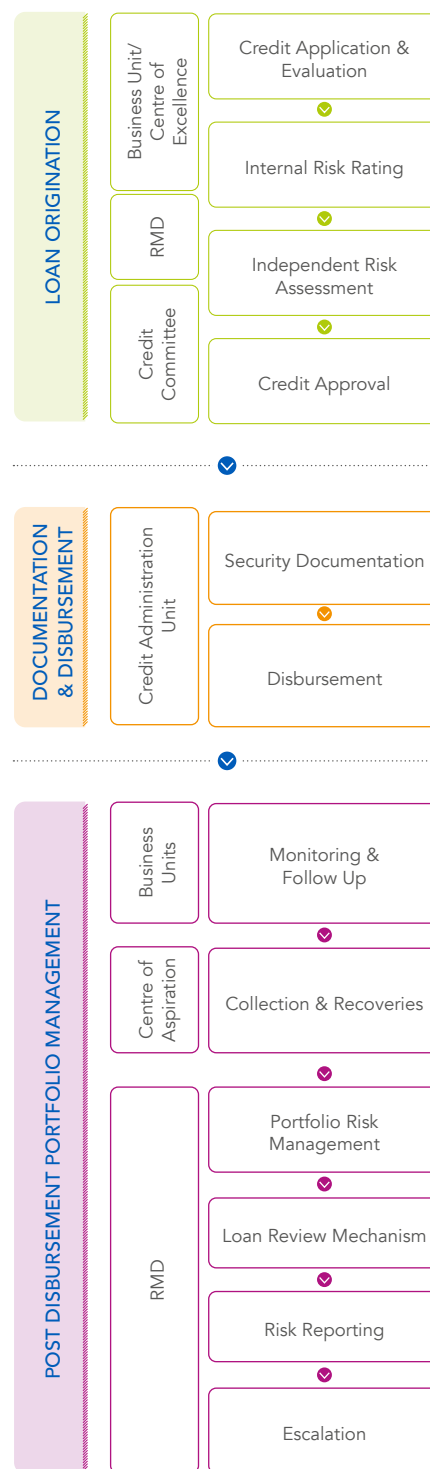
to BIRMC and Board and the feedback and learnings from LRM reports are incorporated when Credit Policies are reviewed. RMD commenced circulation of repeat lapses in the form of a news bulletin in 2021 to share organisation learnings and inculcate a greater risk awareness culture.

» **Management of Large Exposures** – Large borrower exposures of 20 largest exposures are maintained within internal risk limits and bank monitors material exposures and substantial exposures as a part of the Bank’s internal risk goals. Further, Industry risk limits are set to monitor concentration risk facilitating early action on industries with elevated risk.

» **Portfolio Risk Management** – The Portfolio Risk Management Unit and Collections and Recovery Divisions together with business units monitor accounts to identify early warning signs of asset quality deterioration. EWS, Watch Lists and Management Review Lists, Likely to fall in to NPA lists are used for alerting Business units, Risk Management department, Management Committees and the Board to support managing the credit quality of the lending portfolio. The Special Asset Management (SAM) Unit manages accounts with Early Warning Signals leveraging on the teams highly specialised skills to provide appropriate solutions to manage credit risk of distress accounts.

» **Environmental and Social Risk Management** – The Bank’s Environmental and Social Risk Management division provides the framework to establish internationally accepted best Environmental and Social Risk Management practices, ensuring that all our activities and operations are environmentally and socially responsible and compatible with the applicable regulatory environmental and social standards, country regulations as well as globally accepted best practices and standards such as IFC Performance standards and ADB Safeguards.

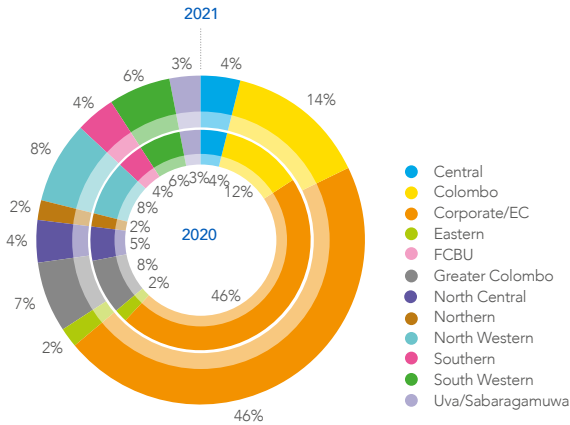
Figure 13: segregation of duties for credit risk management



## CONCENTRATION RISK

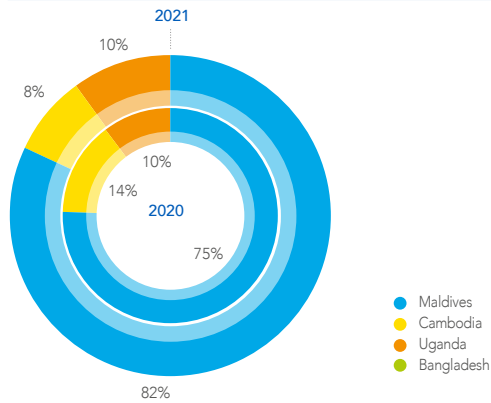
The Bank maintains a diversified portfolio, managing concentrations across products, industry sectors, counterparties, and geographies in line with its risk appetite. Credit concentration risk is quantified using HHI model to derive additional capital requirement under Pillar 2 during the ICAAP computation. Review of concentration risk is a key factor in managing credit risk and dashboards are reviewed at all levels of the risk governance structure to balance portfolio quality and earnings.

### Exposure By Geography

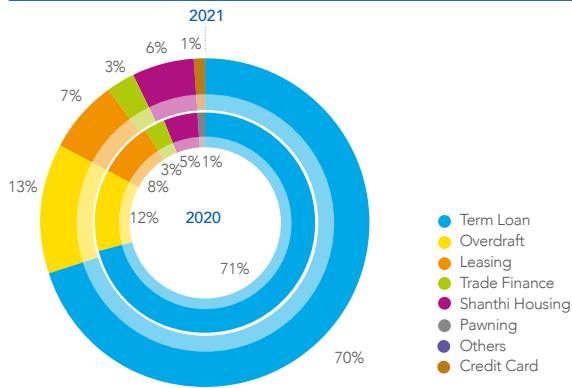


| Portfolio Growth by Region (Mn) | Dec'20 (Rs. Mn) | Dec'21 (Rs. Mn) |
|---------------------------------|-----------------|-----------------|
| Central                         | 35,635          | 39,519          |
| Colombo                         | 100,453         | 126,597         |
| Corporate/EC                    | 375,810         | 432,991         |
| Eastern                         | 15,140          | 16,612          |
| FCBU                            | 1,100           | 956             |
| Greater Colombo                 | 63,811          | 68,765          |
| North Central                   | 36,329          | 40,192          |
| Northern                        | 18,618          | 20,449          |
| North Western                   | 64,717          | 69,836          |
| Southern                        | 35,655          | 39,612          |
| South Western                   | 49,195          | 53,282          |
| Uva/Sabaragamuwa                | 24,275          | 25,896          |
| <b>Total</b>                    | <b>820,738</b>  | <b>934,708</b>  |

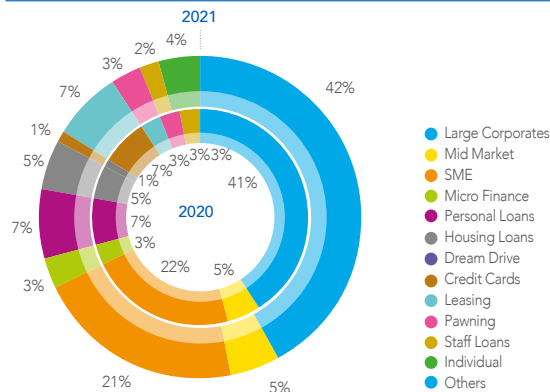
### Cross Border Exposures



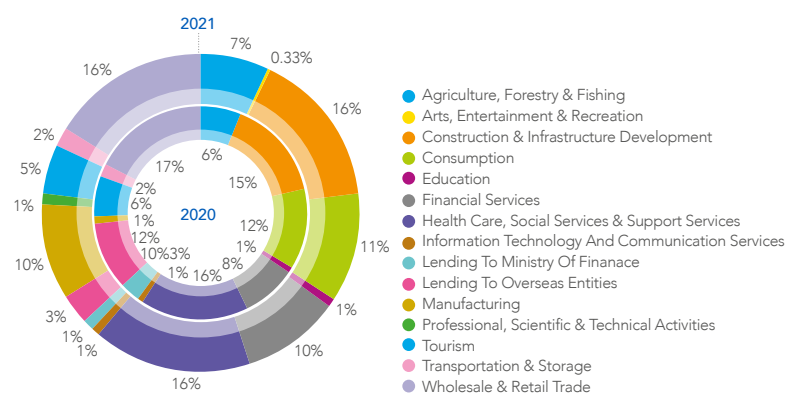
### Exposure By Product



### Exposure By Counter Party



### Exposure By Industry Sector

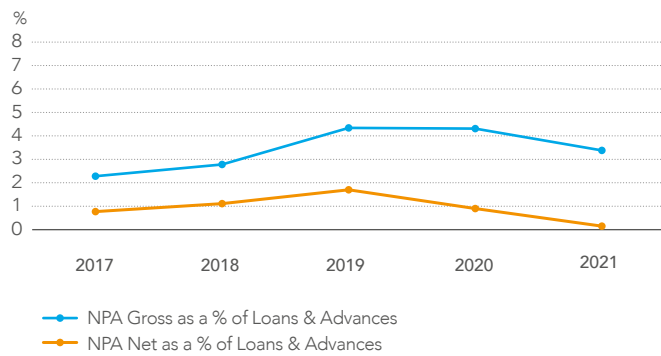


# Risk & Capital Reviews

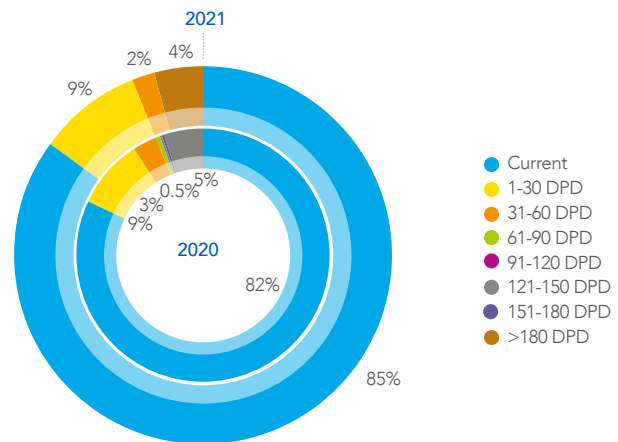
## DEFAULT RISK

Default risk indicators include non-performing ratios, ageing of exposures and classification of the portfolio using Internal Risk Rating models as given below. The COVID-19 pandemic and a recessionary economy continued to contribute to elevate default risk in 2021. Moratoria extended by the GOSL and Bank efforts to support businesses and individuals impacted by the COVID-19 pandemic eased the pressure on default risk to an extent, however a slower than anticipated economic recovery will continue to impact default risk. Increased vigilance and strengthened processes will however enable the Bank to identify and proactively address these risk factors.

### Non Performing Advances



### Ageing of Past Due Loans





## OPERATIONAL RISK

Operational Risk is a key risk for the Bank due to its pervasive presence across all banking activities and significant resources are allocated to managing this key risk. A key highlight is the completion of documentation for transition to the more advanced Alternative Standardised Approach for measurement of operational risk capital charge which is expected to optimise capital utilisation and ROI. Information & Cyber Risk is handled as a separate pillar due to its significance although it is defined within Operational Risk by the CBSL and Basle III Regulatory Management Framework for Banks

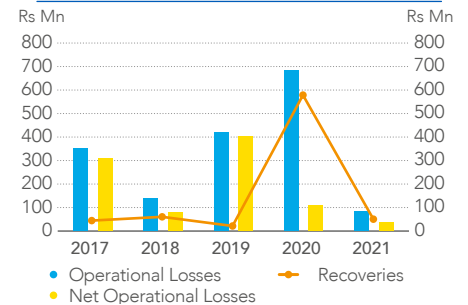
### Definition

The risk of loss resulting from inadequate or failed internal processes, people or systems, or from external events

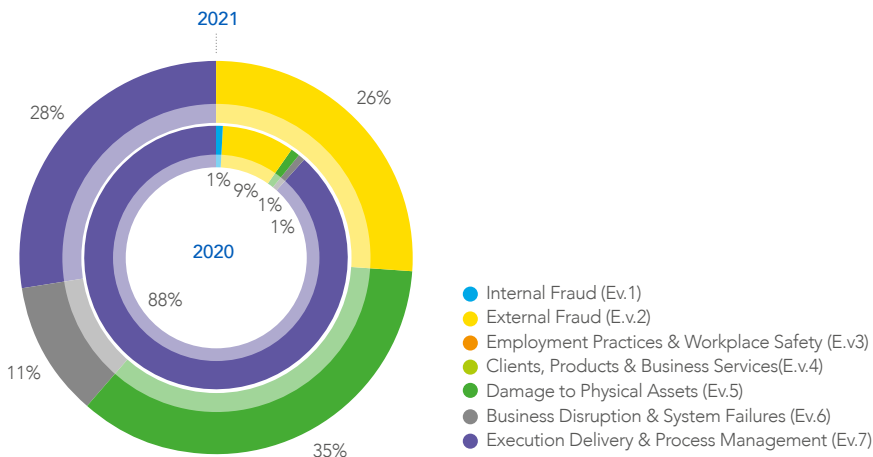
### Operational Risk Components

- » Compliance Risk
- » Legal Risk
- » Financial Crimes Risk
- » Technology Risk
- » Information & Cyber Risk
- » Business Continuity Management
- » Conduct Risk

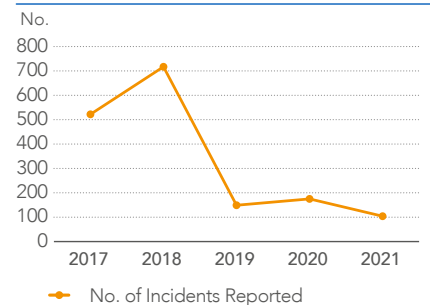
### Operational Losses & Recoveries



### Operational Losses by Event Type 2020 /2021



### No. of Incidents



### Operational Risk Review

Operational risk threat levels remained elevated during the year as the duration of the pandemic extended with new waves and variants. Ensuring the safety of our employees, outsourced workers and customers was a top priority as we needed to provide essential cash lifelines to customers despite the increased risk of infection and associated closures of branches. The extensive branch network and digital infrastructure of the Bank were key strengths that facilitated mitigation of

the risk of contagion to a large extent. The Bank's COVID-19 Committee continued to function throughout the year, leading a holistic response to the pandemic with representation from all key areas including HR, IT, Finance and Services. The Committee met weekly under the leadership of the COO and its activities included the following:

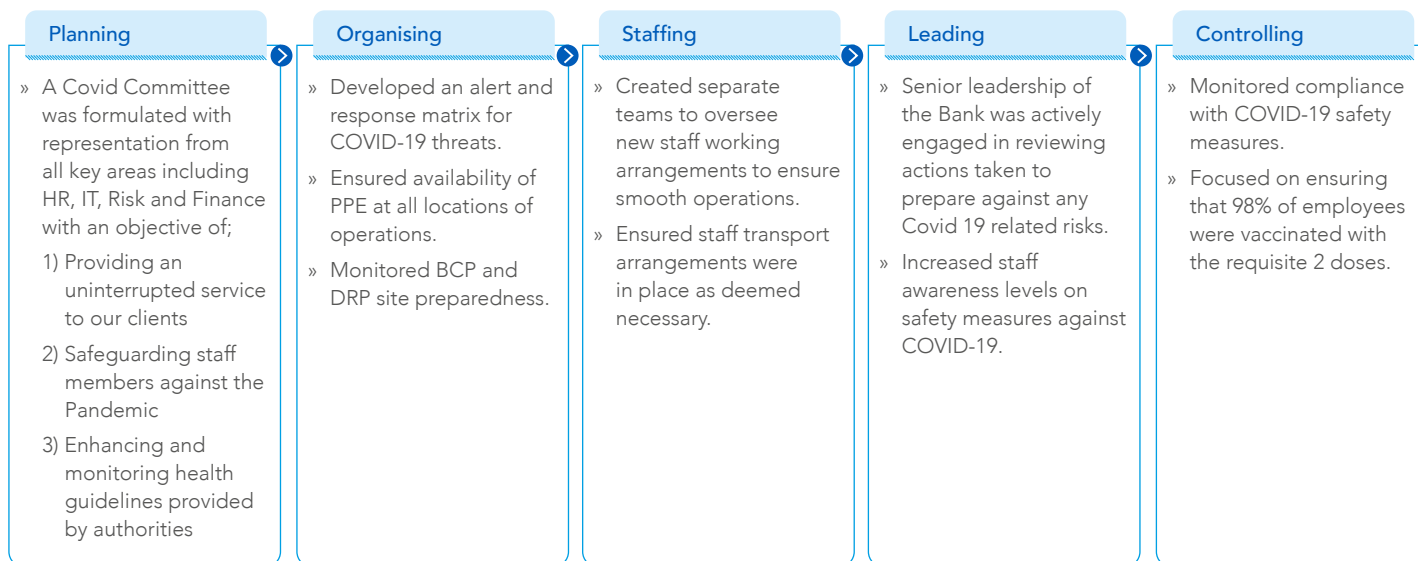
- » Monitoring and taking prompt action to meet any threats from the contagion.
- » Ensuring adequate service capacity and delivery of uninterrupted services including

oversight to minimise any potential operational risks.

- » Secure treatment for employees and their families in case of infection.

COVID-19 was managed by this Committee under the following pillars:

# Risk & Capital Reviews



Accommodation at care centers were provided by the Bank including critical care for all employees. It also spearheaded the Bank's initiative to ensure that all its employees were vaccinated which has enabled the Bank to have 98% of employees vaccinated with two doses by the end of 2021. During the year, we created hybrid models of working which varied in intensity with the external threats as we strived to maintain high levels of service excellence throughout our branch network for the convenience of our customers.

The Bank also made considerable progress in moving from the Basic Indicator Approach used to calculate the capital charge for operational risk to the more sophisticated Alternative Standardised Approach. The necessary documentation has been completed and submitted to the regulator for approval. Adoption of the Alternative Standardised Approach will enable the Bank to reduce the capital charge for operational risk through the use of more detailed calculations which in turn will enhance the Bank's ROI.

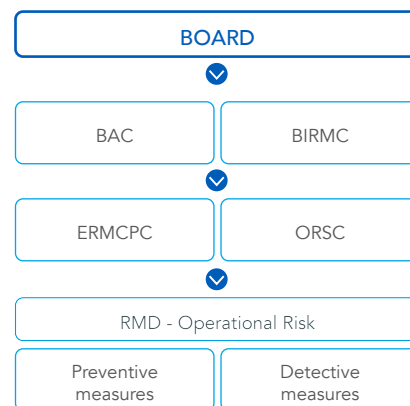
It is noteworthy that the intensity of initiatives and the volume of work increased during the year due to the prolonged impacts of the pandemic. A number of processes were reviewed for necessary changes while ensuring regulatory compliance and Operational Risk played a proactive role in monitoring risks and ensuring that the systems were aligned to heightened threat levels.

## Operational Risk Governance

Operational Risk is managed in line with the Bank's Operational Risk Policy which was reviewed and revised during the year. The Board plays a key role in approval of policy, setting the tone at the top, monitoring risk and shaping the risk culture of the Bank. BIRMC assists the Board in discharge of its duties and has oversight responsibility for management of Risk including operational risk. The Board Audit Committee (BAC) plays a key role through oversight of the implementation of sound internal controls and obtaining assurance on the effective operation of the same through internal and external audits.

Executive Risk Management & Credit Policy Committee (ERMPC) is one of the executive committees for risk management in addition to the Operational Risk Steering Committee (ORSC) which supports the BIRMC in identifying, measuring, monitoring and managing Operational Risk. The Operational Risk Unit focuses on Preventive and Detective measures and supports the Executive and Board level committees.

Figure 14: Operational Risk Governance



## KEY ACTIVITIES IN 2021

### Policy Framework and Reviews

- » Strengthened the Bank's Operational Risk Management Framework in line with the current operating model and best practices.
- » Public Health Policy was enhanced in response to prolonged duration of pandemic.
- » Reviewed the Business Continuity Policy to incorporate both embedded and emerging COVID related risks.

### Strengthening Processes

- » Redefined Near- Miss items to facilitate improved measurement, monitoring and management.
- » Identified risk vulnerabilities of outsourced business activities and formulated a more stringent / focused outsourced business policy model.

### Monitoring

- » Carried out Risk & Control Self-Assessment (RCSA) across the Branch Network and achieved 100% coverage of the entire Bank despite the business disruptions.
- » Enhanced Operational resilience by monitoring all Disaster Recovery Drills and strengthening perceived areas for improvement.

### Strengthening Risk Culture

- » Launched online training programs aligned to the Bank's competency matrix.

## APPROVED REGULATORY CAPITAL APPROACH

The Banking Act Direction 1 of 2016 allows the use of the Basic Indicator Approach, the Standardised Approach and the Advanced Measures Approach for calculation of regulatory capital for operational risk. The Standardised Approach and the Advanced Measures Approach are considered advanced approaches requiring regulatory approval. The Bank uses the Basic Indicator Approach for calculation of regulatory capital at present as set out in Template 11 on page 97. The Bank has completed the necessary documentation to move to the Alternative Standardised Approach and has submitted an application to the regulator for approval.

The capital charge for operational risk is the second highest, reflecting its significance in risk management. Moving to advanced approaches is expected to reduce the charge in the future.

## MANAGING OPERATIONAL RISK

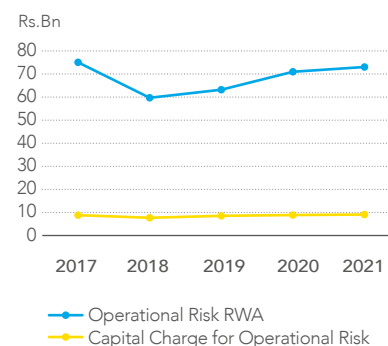
The ORM framework sets out the following specific tools for managing operational risk:

- » **Risk & Control Self-Assessment (RCSA)** - The RCSA process is forward looking and requires business units to assess their own processes and controls on a quarterly basis. These are reviewed, validated and consolidated by the Operational

Risk Unit to assess the operational risk profile of the entire Bank. This process facilitates prioritisation and resource allocation, supporting operational risk identification, measurement, monitoring and management. The frequency of the RCSA process was increased to quarterly assessments enhancing risk monitoring.

- » **Key Risk Indicators (KRI)** - Key risk indicators provide early warnings of escalations in risks identified by the Bank which are monitored continuously to initiate timely and effective action. Triggers and thresholds are reviewed and revised regularly to reflect regulatory requirements and changes to the Bank's risk appetite. Internal benchmarks which reflect trends observed externally and internally. The bank focuses primarily on lead indicators and secondarily on lagged indicators in determining the KRIs.
- » **Internal Loss Data Capturing & Reporting** - Operational Risk Dashboards provide information appropriately categorised according to Basel guidelines on internal losses including potential losses and "near misses" for material risks. These are reviewed by ORSC, ERMCPD and BIRMC to identify potential threats and determine appropriate action to manage the same. External loss events and incidents are captured on best effort basis and reviewed in relation to internal control environment.

## Risk Weighted Assets & Capital Charge for Operational Risk



- » **Root Cause Analysis** - Material loss events and incidents are reviewed to ascertain the root cause and these learnings are used to improve the control environment under the Operational Risk Management function.
- » **Risk Matrices** - The Bank uses risk matrices to consolidate and prioritize risks considering the potential impact and likelihood of occurrence.
- » **Risk Review of New Products & Processes** - Policy and procedures for introducing new products or amending or discontinuing existing products or delivery channel are clearly set out to minimise associated risks.

# Risk & Capital Reviews

## MITIGATING OPERATIONAL RISK

Operational risk is mitigated through operational risk event analysis. The following tools are key to mitigating operational risk:

- » **Risk Culture** – The risk culture is a key preventive tool and is nurtured through a fit for purpose policy framework, governance structure, regular training to increase risk awareness and effective internal controls.
- » **Insurance** – A comprehensive insurance cover is in place securing the Bank from low frequency- high severity and high frequency- low severity loss events. Adequacy and effectiveness of insurance covers were reviewed during the year with the assistance of external consultants. A new Cyber insurance cover was put in place in view of heightened threat levels.
- » **Scenario planning** - The operational risk unit uses scenario planning mainly in its BCM and related activities to demonstrate and make use of the development of appropriate responses to few potential loss events that can or likely to take place together such as fire, security breach etc. Scenario planning was further refined in 2021 to factor in changes in the country's risk profile and the extended duration of the pandemic.
- » **Assessment of Outsourcing Activities** – A comprehensive Outsourcing Policy and guideline sets out the activities, terms and conditions relating to outsourced activities and the Compliance Division monitors the same. Detailed KYC and due diligence tests are conducted before engagement or renewal of existing contracts to assess the AML/CFT risks that may arise regarding the outsourcing arrangements. The Operational Risk Unit carries out a risk-based review of critical outsourcing activities on a need basis. The Operational Risk Unit will also ensure that all critical outsourcing service providers have a satisfactory BCP and that they perform regular tests on its BCP to ensure disaster readiness and a return to normal operations as quickly as possible.

## Business Continuity Planning & Disaster Recovery

A comprehensive Business Continuity plan clearly defines roles and responsibilities and procedures, Crisis Management, Emergency

Response, Business Recovery and IT Disaster Recovery Planning facilitating continuity of operations in the event of emergency or disaster. This was augmented by a Business Continuity Management and Public Health Contagion Plan in response to the COVID-19 pandemic in 2020. Business Continuity policy documents and plans were updated to reflect the regulatory changes during the 2021 and was approved by the Board.

Business Continuity Steering Committee (BCSC) and a Disaster Management Team (DMT) oversee the BCP strategy and provide an effective structure to enable the Bank to respond to a crisis and stabilize until the situation returns to normalcy. Timely appointment of a COVID-19 Committee in early 2020 was critical to respond effectively to the multi-faceted challenges posed by the pandemic.

A comprehensive Business Impact Analysis (BIA) has identified mission critical units, critical processes and necessary resources, which have been clearly documented together with Recovery Time Objectives (RTO), Recovery Point Objectives (RPO) and Recovery Strategies in the BCP documents.

Regular BCP and Disaster Recovery tests are conducted to cover all critical systems and the Mission Critical Units (MCUs) of the Bank. BCP tests are reviewed by the Bank's Internal Audit department and recommendations for improvements are implemented. The Bank also conducts awareness sessions and publishes Newsletters amongst the staff to enhance the knowledge of Business Continuity Management process.

The Bank's Business Continuity Plans have been tested over the past two years with the Easter terror attacks in 2019 and the COVID-19 pandemic in 2020 /2021 and we have continued operations with minimal downtime. Clear communications with the public supported our efforts as we were able to communicate our emergency responses to situations that were of concern to local communities and customers. The operations have remained resilient, adapting successfully to a new norm including telecommuting and product innovation with solutions like SOLO and MOMO to support customers.

## INFORMATION & CYBER RISK

Unprecedented levels of migration to digital platforms, increased online activity and the growing sophistication of cyber-crimes, continue to make Information and Cyber Risk a critical concern for the Bank. The Bank therefore continues to invest in this vital area of risk, strengthening governance structures, policy frameworks, competence of teams and surveillance and monitoring tools.

### Definition

Risk of financial loss, operational disruption, or damage, from the failure of the digital technologies employed for informational and/or operational functions via electronic means from the unauthorized access, use, disclosure, disruption, modification, or destruction of systems, services or data.

### Components of Cyber Risk

- » Information Risk
- » Cyber Risk
- » Financial Crime Risk
- » Technology Risk

### Key trends impacting Bank's Cyber Risk in 2021

- » Increasingly sophisticated malware, ransomware and phishing attacks
- » Unprecedented levels of online activity have made systems more expose to attacks
- » New cyber threats in the form of supply chain attacks have dramatically changed the risk landscape

### Information & Cyber Risk Reviews

- » Information Security Policy & Procedure review
- » Privilege Access Management (PAM) review
- » Internet Security Review
- » Independent Firewall Reviews
- » Mobile Application Reviews
- » End User level security controls reviews
- » Cyber Risk reviews related to critical business functions

### Global Cybercrime damage costs 2021

- \$6 Trillion USD** a Year.
- \$500 Billion** a Month.
- \$115.4 Billion** a Week.
- \$16.4 Billion** a Day.
- \$684.9 Million** an Hour.
- \$11.4 Million** a Minute.
- \$190,000** a Second.

Source: Cybersecurity Ventures

### Cybersecurity Threat Statistics

**\$4.24 million**

Average cost of data breach

**287**

Average number of days to identify and contain a data breach

**350k**

Number of new malware programs found per day

**18 k**

Number of Solarwinds customers affected by supply chain breach

**\$1.85 million**

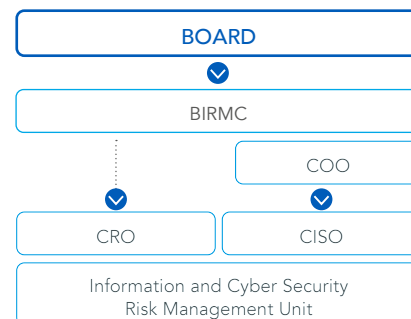
Average cost of remediating ransomware attack.

**74%**

U.S. companies experiencing successful phishing attack in 2020

Source: CompTIA, Inc.

Figure 15: Information and Cyber Risk Governance



## Information & Cyber Risk Governance

The Information and Cyber Security Risk Management Unit which operates within the Risk Management Department of the Bank, reports to the CRO who in turn reports independently to BIRMC. Given the growing importance of Information and cyber risk governance, the first line of defence was further strengthened with the appointment of a Chief Information Security Officer (CISO) who reports directly to the COO. Accordingly, policy formulation is under the purview of the CISO while implementation and compliance is overseen by the Information and Cyber Security Risk Management Team. The segregation of functions has brought about greater focus on the implementation and monitoring aspects of the cyber risk management function.

# Risk & Capital Reviews

## ACTIVITIES IN 2021

Key initiatives implemented to enhance the Bank's management of information and cyber risk are as follows:

### Strengthening Policy Framework

- » Policies on information and cyber security were reviewed to assess the Bank's Information and Cyber security metrics against embedded and emerging risks to ensure that they are in line with industry best practices.
- » Guidelines were developed to strengthen the detection and prevention of supply chain related Cyber Attacks.

### Strengthening Processes

- » Digital Rights Management (DRM) solution was implemented to enhance security of data transfers with third party entities.
- » Implemented a Mobile Application Management (MAM) to provide secure email access via mobile devices.
- » Implemented Data Loss Prevention controls over the cloud email platform.
- » Conducted phishing simulations to test resilience of Bank and Bank staff to potential threats and assess Bank's readiness against phishing attacks.
- » Implemented Security Operations Centre (SOC) in order to strengthen Bank's cyber security surveillance.

### Monitoring

- » Conducted an independent review of limits assigned to core banking users by external consultants and implemented recommendations.
- » Reviewed Privilege Access Management.
- » Conducted periodic reviews of the Bank's Internal IT/IS Management by Information & Cyber Security Risk Team in addition to independent reviews conducted by Internal audit and CISO.

## Information Security Management

The Information & Cyber Security Policy sets out the framework for management of its information assets, hardware and software which are vital strategic assets. The policy framework seeks to protect these assets from identified internal and external threats to ensure that all statutory and contractual obligations are met, and the brand is protected. It also provides guidance for systematic management of information assets throughout its lifecycle supporting the operational and strategic needs of the Bank in compliance with regulations and internal risk appetite.

Additional tools used to ensure continuous protection of its information assets from emerging threats include the following:

- » **Layered Defence Model** – The Bank has implemented a layered defence model to support management of Information Security.
- » **Third Party Vulnerability Assessments and Third Party Security & Compliance Reviews** – Carried out to manage risks arising from connectivity with third parties.

- » **Periodic reviews of the effectiveness of the Bank's Internal IT/IS Management by IT Security Team** - Internal Audit and CISO carry out separate reviews to assess the effectiveness of the Information and Cyber Risk Management processes and controls.
- » **Monitoring cyber Threat Intelligence** – Review up to date information on current and emerging cyber threats with a view to initiating necessary action in a timely manner.
- » **Data Classification Methodology** - This initiative supports safeguarding of information assets through clear categorization of access to documents and uses leading IT tools.
- » **Controls over Data in Transit, At Rest and in Use** - Email flow and USB/CD ROM restrictions implemented together with organization wide awareness campaigns enhance levels of information security.
- » **Security Information & Event Management (SIEM) Solution** - All critical systems and databases are integrated for log analysis enhancing capabilities of identifying IT & Cyber risks

- » **Surveillance & Upgrading** – Continuous upgrade of anti-virus/ Malware/ Ransomware protection.
- » **Cyber Risk Dashboard** – Communicates developments in Information & Cyber Risk to Executive and Board Committees on a monthly basis. This dashboard includes a tracker of Information and Cyber Risk related incidents, Top 10 cyber risks, Cybersecurity incidents reported during 6 months, IS audit findings, adherence level of security standards, Cybersecurity awareness activities, risk update on Key IT projects, update on BCP and DR drill, update on Endpoint exposed with risks, etc.
- » **IT disaster Recovery Plan** – A key component of the Bank's Business Continuity Plan, this is tested regularly and amended as appropriate.
- » **Privilege Access Management (PAM)** – Provide granular level visibility over activities carried out by privilege users in the banking systems.
- » **Security Operating Centre (SOC)** – Strengthens the Cybersecurity surveillance and incident response process.

## MARKET RISK

Profitability of the Bank is impacted by movements of market factors which are beyond the Bank's control. These factors impact valuations of portfolios of assets and liabilities as most transactions involve at least one element of market risk. Consequently, the Bank manages these exposures, carefully balancing profitability and stability within its predetermined risk appetite.

### Definition

Potential losses arising from factors that affect the overall performance of the financial markets which cannot be eliminated through diversification

### Components of Market Risk

- » Interest Rate Risk
- » Foreign Exchange Risk
- » Equity Price Risk
- » Commodity Price Risk

## Market Risk Review

The Bank's market risk exposures arise mainly from the Bank's Non-Trading Portfolio (Banking Book) which accounts for 27% of Total Assets and 30% of Total Liabilities. Interest Rate Risk (IRR) and Foreign Exchange (FX) Risk are the most significant components of market risk as the Bank has minimal exposure to commodity price risk and equity risk as these account for less than 5% of the total risk weighted exposure for market risk at the close of the year.

|  | 2021<br>(Rs 000) | 2020<br>(Rs 000) |
|--|------------------|------------------|
| <b>Assets Subject to Market Risk</b>                                       |                  |                  |
| Cash & Cash Equivalents  | 38,185           | 34,124           |
| Balances with Central Bank   | 25,820           | 7,212            |
| Placements with Banks  | -                | -                |
| Derivative Financial Assets  | 927              | 1,032            |
| Financial assets measured at fair value through profit or loss             | 103              | 84               |
| Financial assets measured at amortised cost - debt and other instruments   | 160,678          | 186,606          |
| Loans & Receivables to other customers                                     | 876,250          | 772,581          |
| Financial assets measured at fair value through other comprehensive income | 203,426          | 249,272          |
| <b>Liabilities subject to Market Risk</b>                                  |                  |                  |
| Due to Banks   | 17,076           | 89,747           |
| Derivative Financial Liabilities   | 353              | 337              |
| Due to Other Customers/Deposits from customers                             | 1,075,709        | 967,821          |
| Other Borrowings   | 24,748           | 30,526           |
| Subordinated Liabilities   | 23,552           | 28,298           |

## ACTIVITIES IN 2021

The Market Risk Management unit implemented the following during the year:

### Strengthening Policy Framework

- » Strengthened ALM Policy with improved risk metrics.
- » Reviewed Treasury Policy and supplementary policies related to Treasury such as Treasury Disputes Resolution Policy, Liquidity Policy and Contingency Funding Policy including changes to Treasury Limits in line with the current environment.

### Strengthening Processes

- » Reviewed Delta limits for investment in securities.
- » Strengthened controls over exposures to securities markets.
- » Strengthened stress testing by introducing additional scenarios and increasing the number of variables.

### Monitoring

- » Counterparty limits were recalibrated to capture the impact of the prolonged pandemic

Interest rates which declined sharply in 2020 with the accommodative policy stance adopted by the government due to the onset of the pandemic have now bottomed out and are on an upward trajectory to address the imbalances on the external sector of the economy while managing inflation and growth.

The sharp decline of the country's foreign reserves to US\$ 3.1Bn or 2 month's imports as at 31 December 2021 and sovereign rating downgrades during the year resulted in the rupee devaluing by 8% against the US Dollar in 2021. It recorded a sharper decline of 6.75% against the British Pound while the decline against the Yuan and Indian Rupee were 11% and 5.76% respectively.

The Financial Conduct Authority of UK ceased to issue the London Interbank Borrowing Rate (LIBOR) for all settings except the overnight and 2 year US Dollar rates as at 31 December 2021.

While the demand for gold loans increased during the year, exposure remains at Rs 27.2 Bn at the close of the year as the Bank adopted a prudent approach with prudent loan to value ratios. A similar approach was adopted to manage equity price risk despite the upward movement of the All Share Price Index of the Colombo Stock Exchange.

# Risk & Capital Reviews

## Market Risk Governance

The Board has overall responsibility for managing risk and are assisted by BIRMC who have oversight responsibility for this key topic. ERMCPCC makes proposals on policy to monitor risk, supporting BIRMC with their observations. ALCO manages market risk exposures and profitability, ensuring that risks taken are commensurate with the rewards and managed within the RAS.

Treasury plays an important role in managing both banking/trading book and the asset and liability position of the Bank. Accordingly, duties are segregated into Front Office, Middle Office and Back Office in line with best practice. Treasury Middle Office (TMO) ensures that Treasury Front Office deals within limits set out in the Bank's risk appetite and Treasury Back Office reconciles and escalates key issues promptly.

The Market Risk Management Unit of RMD independently measures, monitors and reports on market risk exposures using Market Risk Dashboards and assists in review of the Bank's market risk related policies and exposure limits, supporting ALCO, ERMCPCC, BIRMC and the Board with information required for decision making.

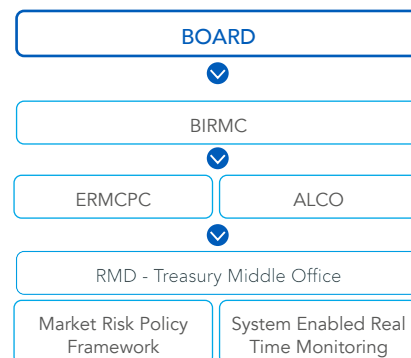
## Approved Regulatory Capital Approaches

The Bank uses the Standardised Measurement method as required by CBSL Direction No.1 of 2016 in line with Basel III requirements for computing regulatory capital for Market Risk. Accordingly, the calculation of regulatory capital is based on specified risk weightings applied to net exposures in defined categories as set out in Template 10: Market Risk Under Standardised Measurement Method. The Bank is moving towards the more advanced Internal Model Approach.

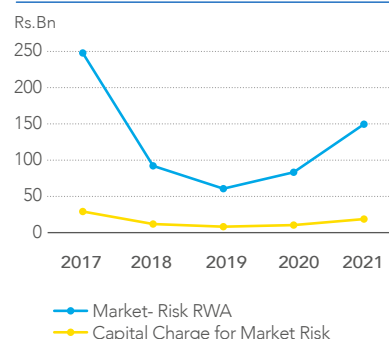
## Market Risk Management

Market Risk is managed in accordance with the Asset and Liability Management (ALM) and Treasury Policy which support management of Interest Rate Risk, Investment and the Foreign Exchange Risk. The trading portfolio is managed by Treasury while the Non-Trading portfolio is impacted by both the Bank's business lines and Treasury. The Balance Sheet and Income Statement implications of market risk are summarised below.

Figure 16: Market Risk Governance



## Risk Weighted Assets & Capital Charge For Market Risk



| Portfolio           | Banking Book<br>"Hold Until Maturity" and<br>"Available for Sale" | Trading Book<br>"Intend to Actively Trade"   |
|---------------------|---|--|
| Line Items          | » Deposits<br>» Loans<br>» Bonds (Investment Portfolio)           | » Bills & Bonds (Treasury Portfolio)<br>» Derivatives<br>(Forward, Swaps and Options,) |
| Balance Sheet Value | Historical Cost   | Mark to Market daily   |
| Income Statement    | Net Interest Margins  | Net Interest margins<br>+<br>Net Change in Value (Mark to Market)                      |
| Risk exposure       | » Repricing risk<br>» Basis risk<br>» Forex Risk                  | All components of market risk  |

Market risk management is a critical aspect in implementing Asset and Liability Management (ALM) framework of the Bank.

Key tools and processes used to manage market risk include the following:

- » Market Risk Limits – Limits contain trading activities within a specified range in line with the Bank's Risk Appetite Statement. These are reviewed and approved by the BIRMC as well as BOD and are regularly reviewed by ALCO and ERMCPCC.



Figure 17: Market Risk Limits

| Limit Type | Activity Limit  | Target Risk Area  |
|------------|---|---|
| Exposure   | Trading/Investment in foreign currency fixed income securities (excluding investment in Sri Lanka Government Treasury Bills & Bonds | Governs the trading/investment in long-term securities with reputed issuers, with minimum credit ratings of A or equivalent.          |
|            | Investment in Sri Lanka Government Treasury Bills & Bonds/CBSL Securities   | Governs trading & investments in Sri Lanka Government Treasury Bills & bonds that are denominated in Sri Lanka Rupees.                |
|            | Cap on total investment on Gov. Securities  | Will govern overall exposure to government securities in terms of balance sheet exposure.   |
|            | Standing Deposit Facility (SDF) With CBSL   | Governs Money Market Deals with CBSL  |
|            | Interbank Money Market/Trade borrowings in FCY both in Sri Lanka and Outside  | Limits the Bank's exposure to liquidity risk arising from funding mismatches and over reliance of FC borrowings to generate liquidity |
|            | Cap on inter-bank call borrowing / Call lending   | Limits the Bank's exposure to adverse fluctuations in inter-bank call money rates and liquidity risk arising due to market liquidity  |
| Tolerance  | Rate tolerances   | Governs minimum / maximum deviation from market rates on interest / exchange rates to ensure no undue risks are undertaken            |
|            | Amount Tolerances   | Govern maximum transaction size undertaken on a currency, instrument or by a dealer.  |
|            | Tenor Tolerances  | Protects the bank from both market and counterparty risk that could arise with time.  |

- » Value at Risk (VaR) - The VaR of a portfolio is the estimated loss that will arise on the portfolio over a specified period of time (holding period) from an adverse market movement with a specified probability (confidence level). The VaR model used by the Bank is based upon a 99% confidence level and assumes 1-day and a 10-day holding period. It is based mainly on historical simulation. The model generates a wide range of plausible future scenarios for market price movements considering market data and observed relationships between different markets and prices.
- » Stress Testing - The Bank conducts stress testing on key components of market risk including interest rate, foreign currency, equity and gold to understand the potential

- impacts. This information is used to provide direction in managing portfolios, optimizing profitability and liquidity.
- » Bank also periodically conducts simulation on severe liquidity crisis event can be triggered off by any one or more of the following events taking place:
  - Loss of reputation due to rumours of a large loss, fraud, management misdemeanour etc.
  - Severe rating downgrade (3-4 notches or to below investment grade)
  - News/speculation of an impending takeover/merger.
  - Large regulatory penalty/qualification of accounts by Auditors/other compliance related loss of reputation.

- » The following stress scenarios were applied to assess the impact of a liquidity squeeze on the Bank:
    - A run on the Bank by depositors
    - Loss of short term interbank LKR liquidity
    - A global banking crisis which could affect short term interbank FC liquidity
    - Worst case scenario comprising of the above stress situations (scenarios 1,2 and 3)
    - Loss of wholesale savings and deposits
- Results of the stress testing are tabled at ERMPCP/ ALCO/ BIRMC for their reference on ALM decisions.

## Risk & Capital Reviews

### Stress Testing On Projected NII

Results of stress tests carried out on Interest Rate Risk for its Loans and Advances portfolio and the Fixed Income Securities portfolio are given below.

|                      | 2021                           |                                  | 2020                           |                                  |
|----------------------|--------------------------------|----------------------------------|--------------------------------|----------------------------------|
|                      | 100 bp Parallel Up<br>Rs. '000 | 100 bp Parallel Down<br>Rs. '000 | 100 bp Parallel Up<br>Rs. '000 | 100 bp Parallel Down<br>Rs. '000 |
| As at December 31st  | 5,171,597                      | (5,478,992)                      | 3,673,172                      | (3,887,179)                      |
| Average for the Year | 5,246,966                      | (5,560,314)                      | 3,963,945                      | (4,168,178)                      |
| Maximum for the Year | 6,008,522                      | (4,432,035)                      | 6,762,722                      | (7,106,954)                      |
| Minimum for the Year | 4,160,462                      | (6,367,403)                      | 2,782,980                      | (2,950,572)                      |

| Minimum for the year           |              | 1%               | 2%     | 5%     |
|--------------------------------|--------------|------------------|--------|--------|
| Fixed Income Risk              | Original CAR | CAR after Change |        |        |
| Fixed Income Total Portfolio   | 18.16%       | 17.40%           | 17.31% | 17.02% |
| Fixed Income Trading Portfolio | 18.16%       | 17.50%           | 17.50% | 17.50% |

### Interest Rate Risk in Banking Book

IRRBB arises due to the differences in re-pricing of Rate Sensitive Assets (RSA) and Rate Sensitive Liabilities (RSL), which impact future interest income and expenses and its economic value. The Bank's interest rate sensitive assets and interest rate sensitive liabilities are analysed by different maturity buckets to determine suitable strategies to optimize earnings based on identified gaps and future interest rate forecasts. The modified duration gap approach is used for analysing changes in economic value of equity, which requires the mapping of assets and liabilities into different time buckets based on their residual maturity as set out below depicting an increased/decreased sensitivity.

|   | Up to 1 Month | 1-3 Months | 3-6 Months | 6-12 Months | 1-3 Years | 3-5 Years | Over 5 Years | Non-Sensitive | Total (Rs.Mn) |
|---|---------------|------------|------------|-------------|-----------|-----------|--------------|---------------|---------------|
| Assets and Off-Balance Sheet Exposures      | 503,292       | 225,207    | 80,165     | 107,243     | 191,631   | 94,405    | 67,936       | 109,476       | 1,379,356     |
| Liabilities and Off-Balance Sheet Exposures | 143,109       | 206,480    | 181,837    | 224,194     | 127,641   | 102,340   | 92,254       | 325,035       | 1,402,890     |
| Period Gap                                  | 360,183       | 18,728     | (101,672)  | (116,951)   | 63,990    | (7,935)   | (24,318)     |               |               |
| Cumulative Gap                              | 360,183       | 378,910    | 277,238    | 160,288     | 224,277   | 216,342   | 192,025      |               |               |
| RSA/RSL                                     | 3.52          | 1.09       | 0.44       | 0.48        | 1.50      | 0.92      | 0.74         |               |               |

## Foreign Exchange Risk

Foreign Exchange Risk is managed using currency swaps, exposure limits and VaR. Market risk exposure of the Bank's overnight foreign exchange positions is measured using 10 day VaR, at 99% confidence level. TMO monitors limits in real time and at specified frequencies in accordance with the Bank's comprehensive market risk management limit structure to ensure compliance with Bank's risk appetite. Trigger points are escalated to CRO, MD/ CEO or Board of Directors depending on the potential loss that may arise. The Bank's exposure to FX risk as at the end of the reporting period is given below and it is noteworthy that over 85% of the Bank's foreign currency exposure is in US dollars.

|  | Net Open Position (NOP) | Overall Exposure in Respective Foreign Currency | Overall Exposure in LKR |
|--|-------------------------|---|-------------------------|
| United States Dollar   | 6,627                   | 2,202,999                                       | 447,142,752             |
| Great Britain Pound  | 11                      | 85,595  | 23,455,503              |
| Euro   | 5                       | 147,139   | 33,849,348              |
| Japanese Yen   | -526                    | 618,304   | 1,088,215               |
| Singapore Dollar   | 0.3                     | 6,080   | 915,242                 |
| Other currencies in USD  | 226                     | 95,317.81                                       | 19,347,133              |
| Total Exposure   | 6,870                   | 2,590,457.90                                    | 525,798,193             |
| Total Capital Funds as at December 31, 2021                    | 153,483,612             |   |                         |
| Total exposure as a % of Capital Funds as at December 31, 2021 | 0.91%                   |   |                         |
| VaR (99%, 1 day) 31st December 2021                            | 1.03%                   |   |                         |
| VaR (99%, 1 day) 31st December 2020                            | 0.73%                   |   |                         |

Foreign exchange exposures are subject to stress testing by applying shocks between 5% to 15% to estimate the impact on profitability and capital adequacy of the Bank. Accordingly, a 5% change in exchange rate has a minimal impact on CAR as given in the table below.

| Magnitude of shock     |              | 5%               | 10%    | 15%    |
|------------------------|--------------|------------------|--------|--------|
| Foreign Currency Risk  | Original CAR | CAR after Change |        |        |
| All foreign currencies | 18.16%       | 18.16%           | 18.15% | 18.14% |
| USD/LKR                | 18.16%       | 18.16%           | 18.15% | 18.14% |

## Equity Price Risk

The Bank's equity portfolio amounts to a mere Rs 103.36 Mn and is managed taking a long term view. Stress testing conducted at 10% to 40% change in equity prices indicate no change in CAR. The bank conducts mark-to-market calculations on a daily basis for held-for-trading and available-for sale portfolios and VaR calculations on a 10 day basis. Year-end positions are summarized below.

|             | Dec 2021       |                   | Dec 2020       |                   |
|-------------|----------------|-------------------|----------------|-------------------|
|             | Exposure Rs.mn | VaR (99%, 10 day) | Exposure Rs.mn | VaR (99%, 10 day) |
| Equity (MV) | 103 Mn         | 11.94 Mn          | 84 Mn          | 8.53Mn            |

## Commodity Price Risk

Commodity price risk of the Bank is limited to the extent of the Pawning portfolio which is impacted by movements in the price of gold. The Bank's exposure amounts to less than 5% of Total Market Risk exposures due to the Bank's cautious approach to managing risks associated with the Pawning portfolio. The Bank also uses conservative loan to value ratios to manage its exposures to commodity price risk. It is noteworthy that the regulatory approach is to treat the exposure in line with Foreign Exchange Risk as described in the Approved Regulatory Capital Approach on Market Risk.

# Risk & Capital Reviews

## LIQUIDITY RISK

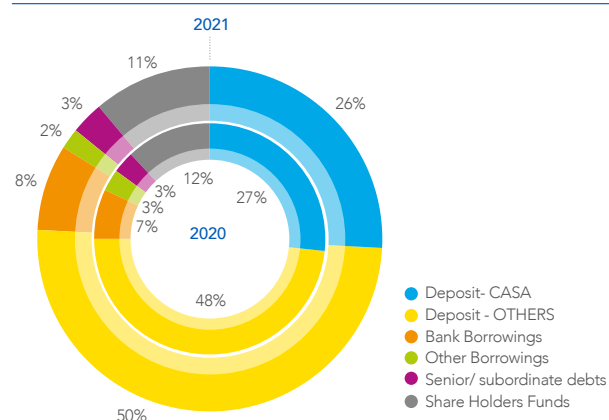
Liquidity risk management enables the Bank to have the appropriate amount, diversification and tenor of funding and liquidity to support its asset base and strategic goals at all times.

### Definition

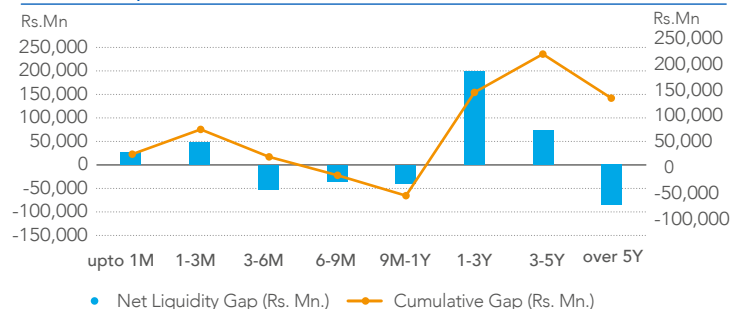
A bank's inability to meet its short term contractual obligations without sustaining unacceptable losses

| Liquidity Ratios                        | 2020    | 2021    |
|---|---------|---------|
| Statutory Liquid Asset Ratio (SLAR)     | 39.58%  | 28.02%  |
| - Domestic Banking Unit                 | 38.95%  | 27.51%  |
| - Offshore Banking Unit                 | 35.92%  | 24.95%  |
| Liquidity Coverage Ratio                | 290.29% | 207.60% |
| Net Advances to Deposit Ratio           | 60.23%  | 64.99%  |
| Loans to Customer Deposits              | 87.15%  | 89.04%  |
| Liquid Assets to Short Term Liabilities | 90.40%  | 78.25%  |
| Commitments to Liquid Assets            | 76.59%  | 68.11%  |
| Commitments to Total Loans              | 45.99%  | 32.51%  |

### Funding Diversification by Product



### Liquidity Gap Based on Behavioral Analysis



### Liquidity Risk Review

Liquidity ratios continued to strengthen during the year to meet potential contingencies stemming from the prolonged duration of the COVID-19 pandemic as the Bank adopted a conservative approach to capital management. While the regulatory policies were accommodative at the beginning of 2021, the second half of 2021 witnessed a tightening of monetary policy with increases in policy interest rates and the Statutory Reserve Ratio applicable on all rupee deposit liabilities of all licensed commercial banks. The Statutory Reserve Ratio increased from 2% to 4% which sharply reduced the liquidity in the market, exerting pressure on interest rates.

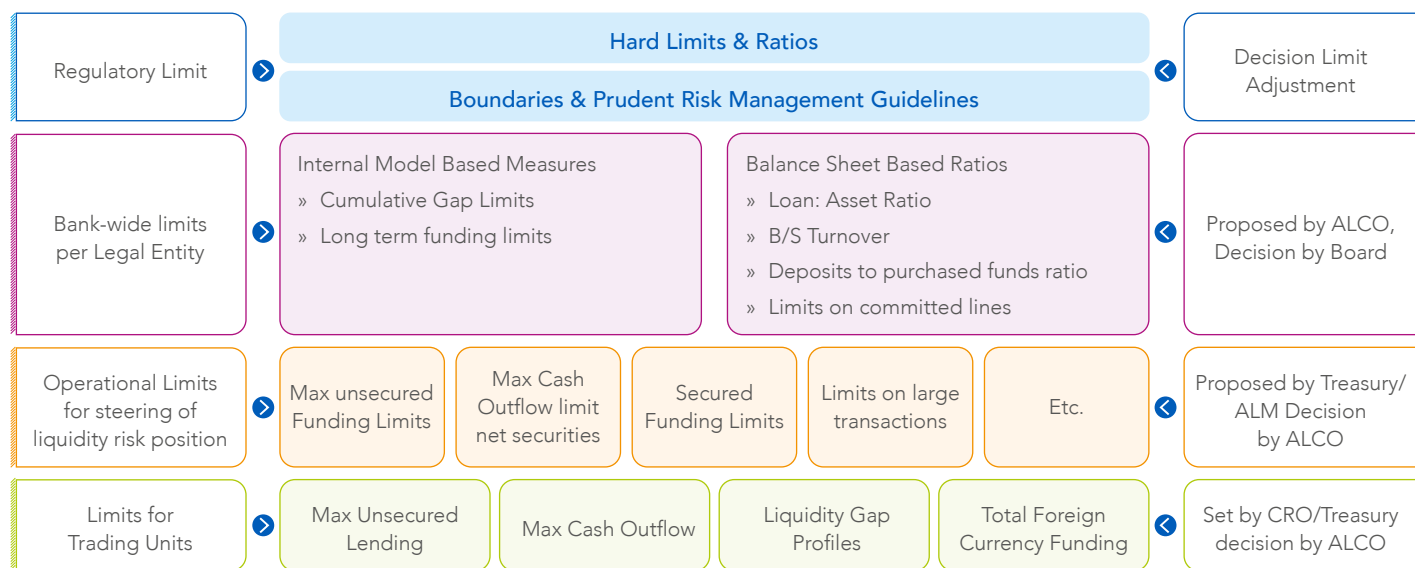
Foreign currency liquidity was straitened throughout the year due to the decline in the country's foreign currency reserves which gave rise to restrictions on imports, barring of forward sales and purchases of foreign exchange and setting maximum interest rates for foreign currency deposits by CBSL.

The issue of Basel III compliant, Tier 2 listed, rated, unsecured, subordinated, redeemable debentures amounting to Rs.7 Bn in August 2021 further strengthened the liquidity ratios. The Bank's Liquidity coverage ratio (all currencies) stands at 207.6%, comfortably above the regulatory requirement of 100%. Bank's liquid asset ratio (LAR) stands at 28.02% within the statutory minimum of 20%.

### Liquidity Risk Governance

A comprehensive liquidity risk management framework is in place which includes a contingency plan encompassing both contracted and un-contracted liquidity positions as summarized in Figure 18. The column on the extreme right reflects the governance structures identifying roles of those with responsibility for managing liquidity risk. The Board, BIRMC, ERMPC and ALCO regularly review reports on the Bank's liquidity indicators to ensure that they are managed within agreed parameters.

Figure 18: Liquidity Risk Management Framework



### Liquidity Risk Management

Liquidity risk is managed by monitoring key liquidity risk indicators which indicate changes in assets and liabilities and also by determining appropriate funding activities to maintain desired levels of liquidity in line with the Bank's risk appetite. Liquidity ladders, probabilistic analysis and stress tests are undertaken to evaluate liquidity requirements of the Bank using both stock and flow approaches. Internal limits in place are more stringent than the regulatory requirements in line with the Bank's overall approach to risk management. Liquidity gaps are monitored based on the behavioural analysis of the Bank's assets and liabilities, historical rollover patterns, drawdown of unutilized overdrafts and disbursement of approved but undisbursed loans.

Figure 19: Managing Liquidity Risk

| Funding Plan  | Managing Liquidity Risk                              | Managing intraday liquidity risk | Identify Contingent Funding Requirement | Managing Regulator                         |
|---|--|----------------------------------|---|--|
| Identify concentration risk in banking book                           | Establish liquidity policy and appetite              | Maintain liquidity buffers       | Early warning indicators                | Maintaining LCR                            |
| Pricing liquidity risk via transfer pricing mechanism within the bank | Monitor intraday limits and carry out stress testing | Daily clearing and settlement    | Conduct liquidity simulations           | Reporting on liquidity assets and reserves |

The Bank also measures its liquidity position in all major currencies at both individual and aggregate levels to maintain potential risks within specified limits. Potential liquidity commitments resulting from loan disbursements and undrawn overdrafts are also monitored to assess adequacy of funding sources. Liquidity risk is mitigated by maintaining an adequate margin in high quality liquid assets and diverse funding sources. Contingency funding agreements with peer banks are in place ensuring availability of sufficient liquidity buffers in accordance with the Bank's Contingency Funding Plan.

Competition among financial institutions and market interventions, challenge the mobilising of low cost LKR customer deposits. Moreover, with the dearth of lending opportunities in foreign currency and access to low cost foreign currency funding lines the bank has taken a strategic decision to generate low cost LKR funding through foreign currency swaps for short to medium term liquidity. Exposure limits in terms of regulatory and internal, regular management information to ALCO/BIRMC/BOD manages the liquidity risk that could arise from overreliance of borrowings and cross currency liquidity generation, are actively managed.

### Funding Diversification

Deposits from customers account for 80% of funds making this the primary source of funding for the Bank. Total Capital grew by 7% as the Bank increased equity to comply with regulatory capital requirements at the close of the year.

# Risk & Capital Reviews

## Credit Ratings

The credit ratings of the Bank at the close of the year are as follows;

| Rating Type                     | Long Term National Rating   |
|---------------------------------|---|
| Issuer                          | Fitch Ratings Lanka Ltd.  |
| Rating                          | AA- (lka)   |
| Outlook                         | Stable  |
| Date Issued                     | 03rd August 2021  |
| What can change rating up       | Limited upside potential due to sovereign rating and operating environment outlook  |
| What can change the rating down | » Deterioration in sovereign rating<br>» Deterioration in its credit profile, such as a sustained decline in its capital buffers while operating environment risks are high |

## COMPLIANCE RISK

Compliance continues to be a key area of focus for the HNB Group and Compliance Risk is managed by a dedicated Compliance Department. The Department is headed by the Compliance Officer who reports directly to the Board Integrated Risk Management Committee (BIRMC), ensuring the independence of this key function in line with the regulatory requirements. The Bank maintains a zero tolerance approach for non-compliance with regulatory requirements and ensures that systems and policy frameworks are updated with the regulatory changes to facilitate compliance.

### Definition

Compliance risk is defined as the risk of legal or regulatory sanctions, financial loss, or loss of reputation that a bank may suffer as a result of its failure to comply with all applicable laws, regulations, codes of conduct and standards of good practice.

### Key Activities of the Compliance Function

- » Foreign Exchange Regulations
- » Financial Crime
- » Anti Money Laundering & Know Your Client
- » FATCA
- » Group Compliance

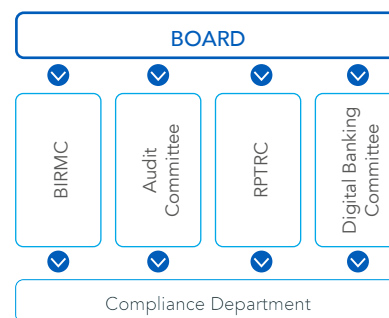
## Compliance Risk Governance

The main focus of the Compliance Department is to ensure that the Bank complies with all legal and regulatory requirements including CBSL, SEC, CSE, SLAASMB etc., in line with the wide-ranging policy framework of the Bank. Its scope encompasses both financial and operational compliance. While the function reports directly to BIRMC, it operates independently of the Risk Management Department. It is also invited to the Board Audit Committee, Board Related Party Review Committee and the Special Board Digital Banking Committee.

## Compliance Risk Review

The focus on the rigor of compliance was maintained throughout the year as the regulator issued a number of directions. Anti-Money Laundering (AML) compliance was strengthened during the year with the use of Data Analytics and an Artificial Intelligence tool. This improved the monitoring of alerts generated by the AML system and capturing of purpose codes for digital transactions. Compliance Risk was further strengthened by the review of more than 170 branches and departments by the newly set up Compliance Audit Team. The Bank complied fully with the CBSL guidelines on Anti Money Laundering (AML) with the introduction of GoAML (the CBSL system to monitor AML activities), facilitating online reporting of AML information.

Figure 20: Compliance Risk Governance



## ACTIVITIES IN 2021

The following projects were implemented to strengthen this key function:

### Strengthening AML Processes

- » Started using Data Analytics/AI tools to improve monitoring of alerts generated by the AML system.
- » Started capturing Purpose Code when performing transactions through Digital channels to enhance the monitoring process.
- » Strengthened review mechanisms and Compliance Audits carried out covering critical areas in branches and departments of the Bank.

### Strengthening Group Risk

- » Implemented a quarterly group reviews on Risk, Compliance Finance and Audit to ensure regular monitoring of compliance risk of Group Subsidiaries.

### Strengthened KYC/AML Processes

- » Started capturing of the images of customers at the time of on-boarding.
- » Started identifying risk profile of customers based on their transaction patterns.
- » Started capturing NIC/ phone number for all deposits through CDMs / CRMs.
- » Commenced data cleansing projects covering beneficial ownership data collection, KYC data collection and Power of Attorney data collection as an ongoing exercise.

# Risk & Capital Reviews

## Mitigation

The Compliance Division staffed with specialists, supports the Compliance Officer in implementing the Bank's compliance programme, thereby ensuring the business- and industry-specific standards are met.

The Bank's policy framework is updated regularly to incorporate changes in regulations, emerging threats, the Bank's processes and learnings from industry experiences and our own. All policy revisions are reviewed by the relevant board sub-committees and approved by the Board of Directors.

The Compliance Division plays a key role in enhancing awareness on statutory regulations, internal policies and best practices in the industry by integrating these into the training programmes of the Bank, strengthening the first line of defense. As regulation in the financial sector continues to increase, regular training is a vital component of the Bank's compliance function to ensure that employees do not overstep boundaries as a result of ignorance or uncertainty. New recruits and promoted employees receive a compliance training tailored to meet the demands of their new role and function. An e-learning

AML module further supports knowledge enhancement on Anti Money Laundering areas.

The following training activities implemented during the year to further strengthened mitigation of compliance risk.

- » Compliance Certification Programme was launched to certify Operation Managers in the network & to update them on compliance related areas of Financial crimes, Foreign Exchange Regulations, Trade Based Money Laundering, Data Security, FATCA, GDPR etc.
- » Staff members attached to Compliance Division have been nominated to attend Local & Foreign Training programmes, International Summits, Webinars, Online certification courses to update their knowledge with the latest Regulations.
- » E - Learning system has been updated with the latest Regulations, AML Courses, Forex courses, & FAQs, for knowledge sharing.
- » New systems & modules have been introduced to enhance the processes on Transaction monitoring, Trade Based Money Laundering & Sanction screening.

## Plans for 2022

### Anti-Money Laundering

- » Enhance monitoring of Trade Based Money Laundering by monitoring Dual Usage of goods and Vessel Tracking by linking the Dow Jones data base to the Trade core banking system through API connections.
- » Implementation ITRS project (International Transaction Reporting System) initiated by CBSL to automate various International, Trade and Treasury related reports.

### Other

- » Reviewing the of CCTV operation of the bank and to retain images for 06 months to support law enforcement investigations.



## REPUTATION RISK

Reputation risk refers to the potential adverse effects which can arise from the Bank's reputation being tarnished due to factors such as unethical practices, regulatory actions, customer dissatisfaction, negative/adverse publicity, inability to meet obligations, etc.

The Bank has carefully managed its reputation risk during a difficult year with timely communication with its stakeholders and cooperation with regulators to extend moratoria as well as, initiatives to facilitate customer access to cash and banking services. The state-of-the-art digital platforms of the Bank supported customers in fulfilling their banking needs with much ease and convenience. As an essential service, the Bank implemented safety measures to safeguard the health of its employees and customers while ensuring customer touchpoints functioned efficiently to serve the needs of the communities it operates in. Additionally, awards and accolades reflect the high esteem in which the Bank is held, including its response during the COVID-19 pandemic.

### Mitigation

The Leadership of the Bank set the tone at the top, nurturing the right behaviours and creating an environment of transparency and accountability across the Bank. Other mechanisms in place to safeguard the reputation of the Bank include:

- » COVID-19 Responses
  - Providing moratorium according to CBSL guidelines for customers whose cash flows have been adversely impacted as a result of the pandemic
  - Establishing Business Continuity Management and conducting of DR drills covering mission critical units
  - COVID-19 response team to identify potential areas of concerns and address them promptly
  - Extending outreach through mobile ATMs, implementation of IPG as well as SOLO, MOMO etc.
  - Product innovation to meet customer and community challenges stemming from pandemic

- » A Code of Ethics issued to all employees ensures that corporate values and expectations of conduct are clearly communicated throughout the Bank.
- » Comprehensive customer engagement mechanisms are in place including the contact centre, which is operative 24x7, enabling customers to contact the Bank for any assistance, report of a complaint and also enables the Bank to address any concerns promptly
- » Print and electronic media exposure is monitored for any adverse remarks or customer complaints on the Bank and its services
- » A comprehensive training and development plan facilitate employee learning on the subject and sharing of learnings while supporting competency development in this area
- » Response plans and identification of spokespersons in events of crisis supports organization readiness to handle reputation risk events, supporting initiation of timely and effective action to minimise potential impacts.

### Monitoring

The Bank uses a scorecard approach to assess Reputation Risk. The Reputational Risk Task Force (RRTF) which operates with the supervision of ORSC reviews reputational risk trigger events and manages attributes that impact the reputation of the Bank, reducing the capital requirement. These pre-emptive measures support scoring, reducing capital allocation under reputational risk.

## STRATEGIC RISK

Strategic risk is the risk that the Bank's future business plans and strategies may be inadequate to meet desired business goals and expectations including protecting and enhancing the Bank's competitive position and shareholder returns. The Leadership of the Bank is collectively responsible for providing strategic direction and undertake evaluation of alternative strategies which are deliberated in depth to chart its course.

During the year, strategic risk was assessed to accommodate the significantly altered outlook of the Bank's operating environment, which was impacted by Covid 19 Pandemic, and

strategies were recalibrated to align with the same.

### Mitigation

A dedicated strategic planning department oversees the strategic planning process. Inputs from RMD strengthen the process through testing of key assumptions and analysis to identify and assess potential areas of concern. Due care is exercised to facilitate compliance with all regulatory requirements including those anticipated for implementation within the forecast period. Key risk drivers and other material matters are monitored to identify potential areas of regulation, facilitating early understanding of related impacts and issues.

Optimizing risk and return with a thorough understanding of risks and opportunities is key to managing strategic risk. The Bank engages external resources to support its strategic planning processes, bringing in global expertise to support management of strategic risk, recognizing the systemic importance of the Bank to the country's economy. Additionally, regular communication with employees on progress of Project Everest through meetings, dedicated monthly newsletters and the intranet ensured that employees were engaged and clearly understood their role in the transformation.

### Monitoring

The bank carries out Strategic risk assessment in both quantitative and qualitative dimensions using a scorecard to compute capital allocation for strategic risk as a part of Pillar II risk assessment under ICAAP. Bank plans on operationalizing a strategic risk dashboard through which major strategic risks can be escalated to BSIRC through BIRMC which would support the BSIRC in reviewing macroeconomic strategic opportunities and risks available within and outside of Sri Lanka.

## CONDUCT RISK

Conduct risk in banking business is defined as any action of a bank or the banking industry that leads to customer dissatisfaction or negatively impacts market stability due to unacceptable or unexpected behaviour in meeting bank's obligations towards its stakeholders.

# Risk & Capital Reviews

Managing conduct risk has become increasingly critical in the banking industry as the number of risk events continues to rise. Underlying factors contributing to elevated conduct risk include failures in internal controls, noncompliance, negligence and failure to incentivize the right behaviours etc. The banking and financial sector have been penalized by regulators globally with penalties awarded in judgements or expensive settlements which continue to grab headlines.

The pandemic and the resultant global recession are widely expected to escalate this risk as personal stress factors add pressure on finances and mental health of employees. As these factors are expected to persist in the foreseeable future, managing conduct risk has gained importance in the Bank's risk management agenda.

## Mitigating

Understanding what has driven poor conduct in the past helps the Bank in estimating and preventing poor conduct in the future. Accordingly, the Bank has defined its key conduct risk drivers.

## Monitoring

Lines of defence in managing conduct risk:

- » Operational: Day to day monitoring and reviewing management of information. This line of defence remains with the respective business unit itself.
- » Compliance: Implementing policies and procedures as prescribed by regulator and industry best standards. The Operational Risk Management department is under the purview of RMD, and the Audit and Compliance department ensures the management of the risk control framework and ongoing compliance monitoring.
- » Board: Assessing conduct risks through review and analysis of periodic management information.

## LEGAL RISK

Legal risk is the current and prospective risk to earnings or capital arising from violations of, or non-conformance with laws, rules, regulations, prescribed practice, or ethical standards issued by the regulator from time to time. As per ISO 31000, Legal Risk can be of following types:

- » Litigation Risk
- » Contract Risk
- » Regulatory Risk
- » Structural Risk

## Mitigation

A legal risk scorecard was introduced as a part of improvements made to the ICAAP document of the Bank and same was considered as quantitative risk assessing parameters to be used in Pillar 2 risk assessment. The Bank looks at following risk drivers in assessing legal risk.

The Legal Department of the Bank carries out a comprehensive assessment prior to entering into an agreement with any 3rd party service providers. Additionally, the Bank retains reputed legal counsellors to safeguard the Bank's interest in dealing with litigation against the Bank.

## Monitoring

Legal risks are analysed using a scorecard to ascertain the additional capital requirement under Basel II, pillar 2 calculation. Factors considered for the assessment of legal risk include, Legal Risk governance and framework, Claims arising from / deprived due to defective documentation in contracts, Legislative / regulatory developments resulting in claims against / deprivation of making claims etc.

The Legal Department prepares a quarterly compliance assessment report based on a comprehensive checklist covering a broad spectrum of the Bank's litigation and related functionalities which is signed off by every member of the legal department. This is reviewed by the Compliance Division on a quarterly basis, strengthening Legal Risk monitoring.

## MODEL RISK

Model risk is the risk of loss that an institution may incur as a consequence of decisions that could be primarily based on the output of the internal models or as a result of the errors in the development, implementation or use/ maintenance of the models. As models are widely used to support decision making in the financial sector, it is a critical component of the Bank's risk management and is governed by the Model Risk Management Framework.

The Model risk management framework provides guidance on the structure of models and assumptions used for the Bank's business projections, financial analysis and risk management capabilities to ensure that they are sufficiently robust and effective to support its business strategies, risk assessment and measurement capabilities. Model risk can potentially lead to over/underestimating future profits or losses as it supports decision making. Regular back testing done on internal models drives continuous improvement in our models and in the assumptions used for the models, supporting effective management to mitigate model risk. Accordingly, the Bank

## LEGAL RISK GOVERNANCE AND FRAMEWORK

- » Claims arising from / deprived due to defective documentation in contracts
- » Mis - selling / mis - buying
- » Legislative / regulatory developments resulting in claims against / deprivation of making claims
- » Dispute Management
- » Claims arising from / deprived of due to non - contractual rights / obligations risks
- » Constraints faced due to technological advancements

engaged with external risk consultants in 2019 to establish a Model Risk policy and framework governing all material models used by the Bank and the policy was reviewed in 2021.

The governance principles for models' lifecycle are prescribed below:

- » Compliance to model development rules and risk estimation methodologies prescribed by Basel principles and leading model development practices across the globe;
- » Maintain data for models in line with the Risk Data Aggregation (and Reporting) Principles prescribed by the Basel Committee on Banking Supervision through the BCBS 239 principles;
- » Develop distinct models across different portfolios of the Bank such as Retail, Corporate, etc. for credit portfolios and loss data for market risk and operational risk;
- » Models are to be parsimonious, taking into account the appropriateness of variables, data length, ease of availability, with the aim to maximize performance with resources available;
- » Independent validation of models with the aim of ensuring accuracy of models.

Maintaining strong governance over development of models and their lifecycle is fundamentally important to their effectiveness and risk control. Given below is the overview of the Model Governance structure at the Bank.

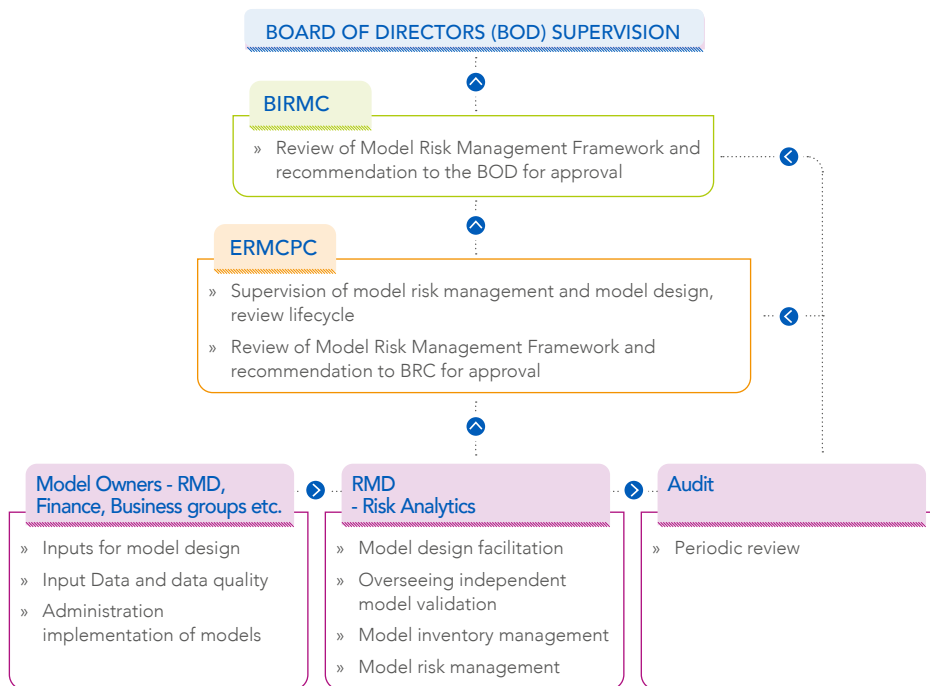
### Monitoring

The governance of Bank's model management framework is characterized by cross-departmental involvement in various stages of model development, implementation and review; with the oversight of the Board of Directors, through the Board Integrated Risk Management Committee (BIRMC).

The following areas are managed through specific models in the Bank.

- » Gauging the market risk parameters for the Bank, assessment and monitoring methodology
- » Statistical methodologies for business or risk estimations

Figure 21: Model Risk Governance Structure



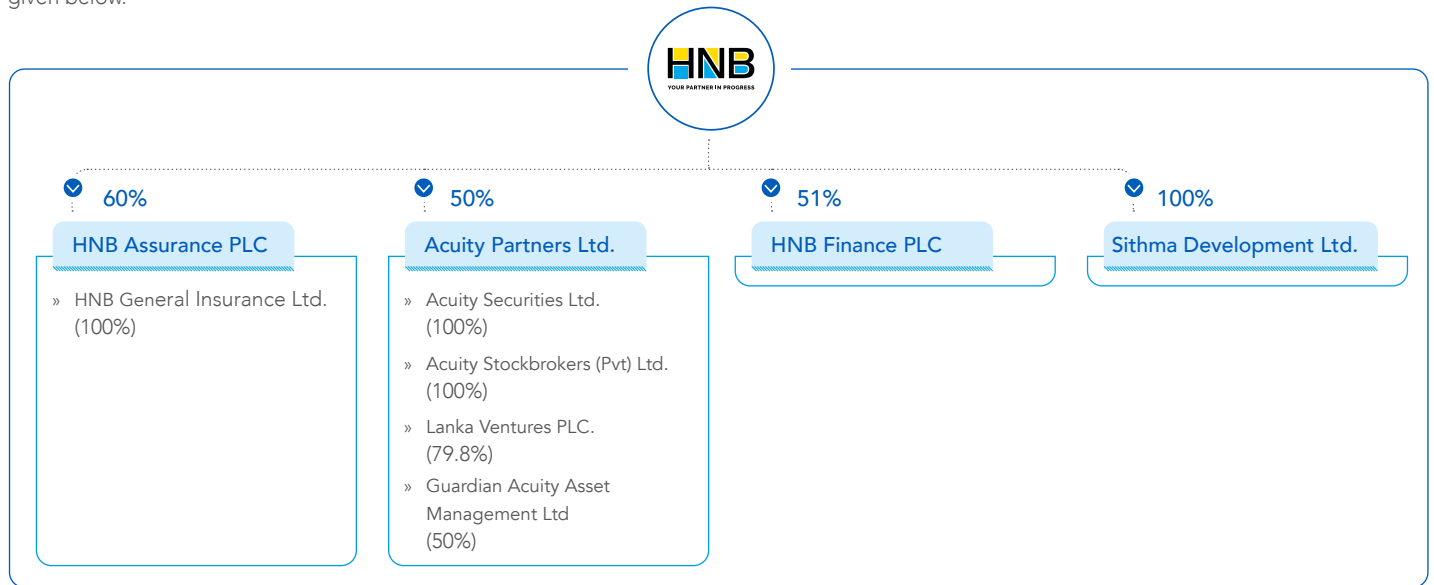
- » Non statistical models (such as Pillar 2 risk assessment models)
- » Models for assessment of obligors or facilities, to gauge the creditworthiness and risks involved with the same
- » Estimation of losses (market, credit or operational risk losses) for specific portfolios of the Bank
- » Bank's credit risk models, which aim to enable the Bank to predict the Probability of Defaults (PD), Loss Given Defaults (LGD) based on recoveries information, and Exposure at Default (EAD) based on customer and macroeconomic characteristics, facilitate calculation of impairment due to Expected Credit Loss(es) (ECL) as per the IFRS 9 stipulations of impairment and provision computation

Performance of models against actuals are reported via dashboards and other monthly reporting. Additionally, we also obtain Independent validation of data quality and model processes to strengthen model risk management.

# Risk & Capital Reviews

## MANAGING GROUP RISK

HNB Group has 4 subsidiaries, all of which are engaged in financial services except for Sithma Development Ltd., which is the real estate arm of the HNB Group. Acuity Partners is a joint venture providing the investment banking services which has four subsidiaries which make up a fully-fledged wealth management and investment banking cluster. HNB Assurance PLC and HNB Finance PLC are listed on the Colombo Stock Exchange. Additionally, these two subsidiaries are regulated by the Insurance Regulatory Commission of Sri Lanka and the Central Bank of Sri Lanka respectively. Activities of Acuity Partners are subject to regulations of the SEC as market intermediaries. The Group structure and the significance to the Group are given below.



## Mitigation & Monitoring

The performance of Group companies is closely monitored, facilitated by the presence of the Corporate Management on the Boards of the same. Additionally, Risk management divisions of the subsidiaries forward Risk Management Review Reports to the IRM function. These reports identify the key risks faced by each entity, measures taken to manage or mitigate the and the financial statements of the preceding month.

Risk aggregating poses some challenges due to the varying operating models of the group companies and the Bank continues to address this to facilitate assessment of the Bank's material risks as a Group. Accordingly, the Bank's risk management department has developed a Group risk dashboard to monitor subsidiary specific financial and non-financial risk parameters covering changes to group structure, general and specific financial highlights of each subsidiary, adherence to respective governing authorities, compliance breaches if and non-financial risks faced by respective subsidiaries on quarterly basis

Effectiveness of the Group risk management is supported by the following:

- » All Group Companies indicate healthy financial positions at the close of the year as reported from page 88 to 107 despite a challenging year
- » HNB's capital at risk is limited to amount invested in these companies in the form of equities at the time of companies were incorporated or acquired
- » Key Management Personnel/Director representation on boards of Group Companies support alignment to core values, business strategy and a sufficient information flow

| Group Co.                  | Board Representation | Chairman | Board Risk Committee Representation |
|----------------------------|----------------------|----------|-------------------------------------|
| HNB Assurance PLC          | ✓                    | -        | ✓                                   |
| Acuity Partners (Pvt) Ltd  | ✓                    | -        | -                                   |
| Sithma Development Pvt Ltd | ✓                    | ✓        | -                                   |
| HNB Finance PLC            | ✓                    | ✓        | ✓                                   |

- » Group companies engaged in Insurance, Finance Business and Investment Banking are subject to regulatory oversight and have structures in place to facilitate compliance.



### KEY INITIATIVES IMPLEMENTED IN 2021

- » Strengthened Credit Policy framework and Credit Risk Governance framework for HNB Finance
- » Strengthened credit risk management strategies and monitored effective implementation of the same through Group Risk Dashboard
- » Regular compliance briefings were conducted to facilitate compliance with regulatory requirements and internal policies
- » Monitored liquidity risk to strengthen resilience and ensure that robust contingency funding plans were in place
- » Ensured that regulatory liquidity/ capital adequacy ratios remained within the limits prescribed by the regulators
- » Tested Business Continuity Plans and Disaster Recovery simulations during the year and the results were reviewed by the BIRMC

# Risk & Capital Reviews

## HNB ASSURANCE PLC

HNB Assurance PLC (HNBA) and its fully owned subsidiary HNB General Insurance Limited (HNBGI) have well established compliance and risk management systems in place and comply with the regulations of the Insurance Regulatory Commission of Sri Lanka, the CSE and the SEC. The key risk indicators of these two subsidiaries are given below and a summary of their performance is given on page 42 in the IR.

### Capital Adequacy Ratio

HNBA      HNBGI  
**277%**    **260%**

### HNB Assurance PLC

HNB Assurance PLC National  
IFS Rating & National Long  
Term Rating

**A+(lka)**

Outlook: Stable

### HNB General Insurance

HNB General Insurance  
National IFS Rating &  
National Long Term Rating

**A+(lka)**

Outlook: Stable

### Key Risk Indicator

|  | 2021     | 2020     |
|--|----------|----------|
| <b>HNB Assurance PLC</b>                 |          |          |
| Gross Written Premium (Rs.)              | 7,091 Mn | 5,487 Mn |
| Profits After Tax (Rs.)                  | 1,000 Mn | 724 Mn   |
| Claims Ratio (without policy maturities) | 10%      | 10%      |
| Expense Ratio                            | 42%      | 45%      |
| Combined Ratio                           | 52%      | 55%      |
| Capital Adequacy Ratio                   | 277%     | 338%     |
| <b>HNB General Insurance Limited</b>     |          |          |
| Gross Written Premium (Rs.)              | 5,649 Mn | 4,998 Mn |
| Profits After Tax (Rs.)                  | 338 Mn   | 451 Mn   |
| Claims Ratio                             | 63%      | 54%      |
| Expense Ratio                            | 37%      | 39%      |
| Combined Ratio                           | 100%     | 93%      |
| Capital Adequacy Ratio                   | 258%     | 256%     |

HNBA has its own Risk Governance structure which includes a Board Level Risk Management Committee and the Board Audit Committee. The HNBA Group Risk management policy framework defines the risk management policies and processes and provides clear guidance for managing foreseeable risks. The policy framework is aligned to the HNB policies where relevant to achieve strategic alignment and minimise potential adverse impacts.

The Company reports the details of the risk management activities carried out by HNBA and HNBGI to the Board Integrated Risk Management Committee (BIRMC) of Hatton National Bank PLC on a quarterly basis. Further, in order to manage the compliance risk, confirmation on compliance is submitted to the compliance division of HNB on a quarterly basis. The following officials of the Bank are directors of HNBA facilitating alignment of values and culture:

| Name                      | Role in HNBA                  | Role at the Bank                                 |
|---------------------------|-------------------------------|--|
| Mr. Dilshan P.N. Rodrigo  | Non-Executive Director- HNBA  | COO/Executive Director HNB                       |
| Ms. L Chiranthi Cooray    | Non-Executive Director- HNBGI | Chief Transformation Officer HNB                 |
| Mr. Sanjay Wijemanne      | Non-Executive Director- HNBGI | Deputy General Manager<br>– Retail and SME       |
| Mr. Arjuna Abeygunasekara | Non-Executive Director- HNBGI | Deputy General Manager<br>– Treasury and Markets |



### KEY INITIATIVES IMPLEMENTED IN 2021

- » Introduced risk dashboards for key risks including the statutory CAR ratios.
- » Conducted stress testing of subsidiary and Group cashflows to ensure there is sufficient liquidity at entity level and Group level.
- » Presented Top risks and Mitigation strategies to the Board Risk Management Committee.
- » Increased emphasis on cybersecurity and IT risks.
- » Continuous monitoring by the Board Risk Management Committee on the HNBGI core system development project including the Core system for Life and Call Center systems.
- » Conducted work from home and cybersecurity awareness training for employees.
- » Increased emphasis on management of reinsurance arrangements and counter party risks.
- » Conducted BCP test and Disaster Recovery simulations during the year and the results were reviewed by the Board Risk Management Committee.
- » Daily meetings were conducted on COVID-19 response with EXCO and Disease Outbreak Response Team (DORT) to identify, monitor and manage impacts on employees and business partners.
- » Reported daily COVID-19 statistics to the parent company.
- » CRO of HNB PLC was a regular invitee to the HNBA Risk Management Committee.

## HNB FINANCE PLC

HNB is a fully fledged finance company and was listed on the CSE in 2020. Its risk profiles is shaped by a legacy of microfinance with more recent successful penetration into the SME market segment, extending the customer life cycle and broad basing the market segments. As a regulated finance company, HNB has a comprehensive Risk Management Framework aligned to the Bank's risk objectives and parameters. The key risk indicators of HNB are given below while a summary of its performance is given on page 43 in the IR.

### Capital Adequacy Ratio

**11.78%**

### HNB Finance PLC

**A(Ika)**

Outlook: Stable

### Key Risk Indicator

|                             | 2021   | 2020   |
|-----------------------------|--------|--------|
| Deposit Growth (%)          | 13.89  | 12.18  |
| Advances Growth (%)         | 26.02  | (3.66) |
| Profitability (Rs. Mn)      | 514    | (273)  |
| Total Assets (Rs.Mn)        | 44,386 | 37,414 |
| Shareholder Funds (Rs. Mn)  | 5,383  | 4,514  |
| Total Capital (Rs.Mn)       | 4,738  | 3,977  |
| CAR (%) Total Capital       | 11.78  | 14.28  |
| Impairment Charge (%)       | 16.11  | 13.11  |
| Impaired Portfolio (Rs. Mn) | 754    | 774    |
| NPA Ratio (%)               | 12.78  | 17.24  |

HNB recorded a profit of Rs. 514 Mn for the year 2021 NII which recorded an increase of 25%. Increased credit risk necessitated another year of high provisioning which dampened profitability. Interest rate caps of 35% for micro finance loans continued to impact profitability, skewing market equilibrium as elevated levels of risk were not reflected in pricing. Interest rate caps on deposits introduced by CBSL in 2020 remained in place easing competitive pressures. Liquidity risk remained at comfortable levels due to the strong domestic franchise of the HNB Group which enabled HNB to attract deposits and lending activities were at a low ebb.

The CRO of HNB is the BIRMC Chairman of HNB, and provides guidance on development of Risk Management policies, structures, processes and controls using the extensive experience of the Bank's risk management function.

| Name of the Director     | Role in HNB                       | Role at the Bank        |
|--------------------------|-----------------------------------|-------------------------|
| Mr. D. P. N. Rodrigo     | Chairman/ Non-Executive Director) | Executive Director/ COO |
| Mr. R.D Manatunga        | Non-Executive Director            | Chief Risk Officer      |
| Mr. A. G. R. Dissanayake | Non-Executive Director            | Chief Financial Officer |

RMD assessed the quality of the loan book, NPA ratio, portfolio quality indicators, risk coverage ratios etc., due to elevated risk levels stemming from the operating environment. Additionally, stress testing of cashflows at entity level and HNB Group level were also carried out including scenarios factoring COVID-19 impacts. Additionally, HNB complies fully with the regulatory requirements for Non-Bank Financial Institutions and CSE including publishing its financial statements quarterly.



## KEY INITIATIVES IMPLEMENTED IN 2021

### CREDIT RISK

- » Strengthened Credit Policy framework and Credit Risk Governance framework.
- » Enhanced credit risk management strategies and monitoring their effective implementation.
- » Improved Risk Performance Management Information systems across all business segments.
- » Increased focus on monitoring and managing risks related to gold loan operations.

### OPERATIONAL RISK

- » Formulated and implemented a BCP Policy.
- » Enhanced Operational Risk Reviews across the Branch Network and Head Office Departments.
- » Implemented Business Continuity Management (BCM) framework across the Company.
- » Segregated critical and non-critical roles supporting work from home when necessary.
- » Reviewed Operational Losses and near misses.
- » Developed a comprehensive KRI library.
- » Enhanced the RCSA processes through improved reporting.
- » Trained 1st line of defence to support risk identification in day to day operations.
- » Reviewed Privilege Access Management solution.

### COMPLIANCE RISK

- » Regular compliance briefings were conducted.
- » Reviewed periodic progress updates on CBSL supervisory concerns.
- » Reviewed the new AML / CFT System implementation and aligned with regulatory requirements.

### TECHNOLOGY AND SYSTEMS RISK

- » Reviewed and followed up on work from home solution implementation, Business Continuity Planning and Disaster Recovery preparedness of technology and systems that are identified as critical.
- » Reviewed the Assessments on Network Security Vulnerability and Ransomware Readiness and implementing necessary changes.

### MARKET & LIQUIDITY RISK

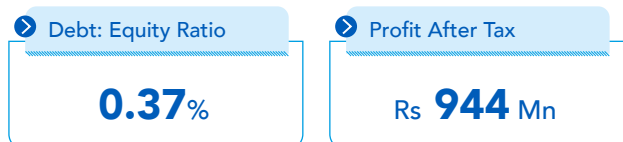
- » Monitored liquidity risk to strengthen resilience and ensure that robust contingency funding plans were in place.
- » Maintained a comfortable Liquid Assets Ratio in line with regulatory requirements.
- » Reviewed Stress Testing on liquidity position on a periodic basis.

# Risk & Capital Reviews

## ACUITY PARTNERS (PVT) LTD

APL Group Risk exposure is monitored and followed by the Groups' Audit Committee with oversight by HNB BIRMC. APL group submits a quarterly report on Risk management activities to the Board Integrated Risk Management Committee of the Bank. Acuity Stock Brokers operates under a license issued by the SEC and complies with its requirements while Acuity Securities Ltd., is regulated by CBSL.

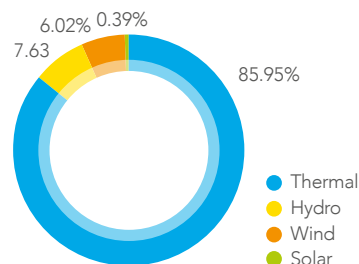
Material risks identified by the APL are market risk, compliance risk and liquidity risk. Those risks are assessed and mitigated through laid down procedures based on regulatory and internal procedures. Additionally, Lanka Ventures is impacted by Climate Risks as its portfolio comprises investments in renewable energy. However, climate risks are largely mitigated through diversification as the portfolio covers solar, wind and hydro power generation.



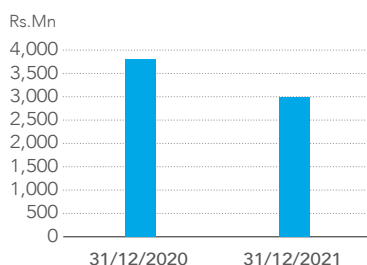
### Key Risk Indicator

|     | 2021  | 2020  |
|-----|-------|-------|
| ROE | 10.4% | 16.3% |
| ROI | 39%   | 53%   |

### Break up of Installed power generation capacity



### Funds Under management by Unit trust



APL Group has recorded a commendable performance despite the COVID-19 impacts as equity markets remained active throughout the year with the benchmark ASPI increasing by 86% during 2021 despite lack luster economic conditions. However, gradual increase in interest rates led to a slight decline in performance in the 4th quarter. Additionally, deal flows picked up during the year and bond yields increased exponentially. The diversified power sector portfolio of Lanka Equities also supported stable power generation and profitability.

The following officials of the Bank are directors of Acuity Partners facilitating oversight and alignment of values and culture:

| Name                  | Role in Acuity Partners   | Role at the Bank            |
|-----------------------|---|-----------------------------|
| Rajive Dissanayake    | Director-Acuity Partners(Pvt) Ltd & Member of Board integrated Audit Committee for ASB/APL                      | CFO                         |
| Damith Pallewatte     | Director -Acuity Partners (Pvt) Ltd, Director-Acuity Securities Ltd & member of board integrated Risk Committee | DGM-Wholesale Banking       |
| Sanjay Wijemanne      | Director -Acuity Partners (Pvt) Ltd & Director-Acuity Stockbrokers (Pvt) Ltd                                    | DGM -Retail & SME banking   |
| Arjuna Abeygunasekara | Director-Acuity Securities Ltd & member of board integrated Audit Committee                                     | DGM-Treasury & Markets      |
| Thushari Ranaweera    | Director-Acuity Stockbrokers (Pvt) Ltd  | DGM-Legal & Board Secretary |



## SITHMA DEVELOPMENT (PVT) LTD

Sithma Developers owns and manages the landmark building of the Bank's Head Office and manages the branch premises owned by the Bank. Risks related to Sithma are monitored by the Bank's Audit Committee and BIRMC in addition to the Board of the subsidiary and the Bank in its role as the parent company.

Typically, the main risks faced by the subsidiary are Market Risk and Compliance Risk. However, operational risk factors became the main risk in 2020 and 2021 as precautionary measures relating to COVID-19 needed to be implemented throughout 22 floors involving the cooperation of its tenants, their employees and customers and outsourced service providers. Additionally, Sithma was also able to retain their clients despite the steep drop in demand in the commercial real estate rental market. Sithma was able to handle these measures satisfactorily through regular communication with key stakeholders and increased investment in personal protective gear and rigorous reinforcement of agreed upon procedures.

The value of its assets and rental revenues are impacted by real estate market movements which stagnated during the period under review. However, these are expected to remain in line with 2021 rates due to its prime location and A grade facility. As the building houses over 2,500 people, compliance with best practice in health and safety standards including fire detection and prevention is a key aspect of risk that is monitored continuously.

| Value of Properties   | Rs. '000   |
|---|------------|
| <b>HNB Towers - No 479, TB Jayah Mawatha, Colombo 10.</b>       |            |
| Net Book Value  | 9,169,040  |
| Market Value  | 18,606,600 |
| <b>SMART Building - No 21, Janadhipathi Mawatha, Colombo 1.</b> |            |
| Net Book Value  | 57,798     |
| Market Value  | 468,900    |
| <b>Building at Kegalle</b>                                      |            |
| Net Book Value  | 100,297    |
| Market Value  | 390,000    |

|   | 2021<br>Rs. '000 | 2020<br>Rs. '000 |
|---|------------------|------------------|
| <b>Revenues from Rental</b>             |                  |                  |
| Rental Income                           | 1,017,160        | 1,018,953        |
| <b>Profitability</b>                    |                  |                  |
| Profit After Tax                        | 464,294          | 426,104          |
| <b>Equity &amp; Debt : Equity Ratio</b> |                  |                  |
| Equity & Reserves                       | 8,240,760        | 7,776,631        |
| Liabilities                             | 2,696,122        | 2,688,413        |
| Total Equity & Liabilities              | 10,936,882       | 10,465,044       |

### Compliance Risk

Complies with **British Standards** for Fire Detection & Prevention

### Sithma Development (Pvt) Ltd

**A Grade**

Outlook: Stable

# Market Discipline -Disclosure Requirements Under Pillar III

## TEMPLATE 1

### Key regulatory ratios - Capital and liquidity

| As at December 31,  | Bank        |             | Group       |             |
|---|-------------|-------------|-------------|-------------|
|   | 2021        | 2020        | 2021        | 2020        |
| <b>Regulatory Capital</b>   |             |             |             |             |
| Common Equity (Rs 000)  | 122,797,863 | 117,243,040 | 134,611,494 | 130,836,136 |
| Tier 1 Capital (Rs 000)   | 122,797,863 | 117,243,040 | 134,611,494 | 130,836,136 |
| Total Capital (Rs 000)  | 153,483,612 | 143,171,814 | 165,799,543 | 157,269,339 |
| <b>Regulatory Capital Ratios</b>  |             |             |             |             |
| Common Equity Tier 1 Capital Ratio (Minimum Requirement - 2021-7% ; 2020-7% )           | 14.53%      | 14.73%      | 14.45%      | 14.99%      |
| Tier 1 Capital Ratio (Minimum Requirement - 2021-8.5% ; 2020-8.5%)                      | 14.53%      | 14.73%      | 14.45%      | 14.99%      |
| Total Capital Ratio (Minimum Requirement - 2021-12.5% ; 2020-12.5%)                     | 18.16%      | 17.98%      | 17.80%      | 18.02%      |
| Leverage Ratio (Minimum Requirement - 3%)   | 7.97%       | 7.73%       | 8.22%       | 8.20%       |
| <b>Regulatory Liquidity</b>   |             |             |             |             |
| Statutory Liquid Assets (Rs 000)  | 326,079,579 | 436,153,114 |             |             |
| Statutory Liquid Assets Ratio (Minimum Requirement – 20%)                               |             |             |             |             |
| Domestic Banking Unit (%)   | 27.51%      | 38.95%      |             |             |
| Off-Shore Banking Unit (%)  | 24.95%      | 35.92%      |             |             |
| Liquidity Coverage Ratio (%) – Rupee (Minimum Requirement - 2021-90% ; 2020-90%)        | 191.38%     | 285.50%     |             |             |
| Liquidity Coverage Ratio (%) – All Currency (Minimum Requirement - 2021-90% ; 2020-90%) | 207.99%     | 290.29%     |             |             |

## TEMPLATE 2

### Basel III computation of capital ratios

| As at December 31,  | Bank        |             | Group       |             |
|---|-------------|-------------|-------------|-------------|
|   | 2021        | 2020        | 2021        | 2020        |
|   | Rs 000      | Rs 000      | Rs 000      | Rs 000      |
| Common equity Tier 1 (CET1) Capital after Adjustments   | 122,797,863 | 117,243,040 | 134,611,494 | 130,836,136 |
| Total common equity Tier 1 (CET1) Capital   | 132,774,260 | 121,925,658 | 144,168,933 | 135,425,972 |
| Equity Capital (Stated Capital)/Assigned Capital  | 38,679,005  | 37,364,244  | 38,679,005  | 37,364,244  |
| Reserve fund  | 8,560,000   | 7,660,000   | 8,560,000   | 7,660,000   |
| Published retained earnings/(Accumulated retained losses)   | 30,266,696  | 19,730,429  | 38,687,797  | 26,501,436  |
| Published accumulated other comprehensive income (OCI)  | (1,831,441) | (150,378)   | (4,838,668) | (179,654)   |
| General and other disclosed reserves  | 57,100,000  | 57,321,363  | 57,541,056  | 58,601,235  |
| Unpublished current year's profit/(losses) and gains reflected in OCI   | -           | -           | -           | -           |
| Ordinary shares issued by consolidated banking and financial subsidiaries of the Bank and held by third parties   | -           | -           | 5,539,743   | 5,478,711   |
| Total adjustments to CET1 Capital   | 9,976,396   | 4,682,618   | 9,557,439   | 4,589,836   |
| Goodwill (net)  | -           | -           | 181,396     | 119,457     |
| Intangible assets (net)   | 1,307,880   | 1,189,715   | 1,407,880   | 1,289,715   |
| Deferred tax assets (net)   | 4,461,561   | 806,539     | 4,941,106   | 1,728,958   |
| Defined benefit pension fund assets   | 1,248,708   | -           | 1,248,708   | -           |
| Revaluation losses of property, plant & equipment   | -           | -           | -           | -           |
| Investments in the capital of banking and financial institutions where the bank does not own more than 10 per cent of the issued ordinary share capital of the entity | 377,538     | 194,159     | 348,552     | 137,165     |
| Significant investments in the capital of financial institutions where the bank owns more than 10 per cent of the issued ordinary share capital of the entity         | 2,580,709   | 2,492,204   | 1,429,797   | 1,314,541   |
| Additional Tier 1 (AT1) capital after adjustments   | -           | -           | -           | -           |
| Additional Tier 1 (AT1) capital   | -           | -           | -           | -           |
| Qualifying additional Tier 1 capital instruments  | -           | -           | -           | -           |
| Instruments issued by Consolidated Banking and Financial Subsidiaries of the Bank and held by Third Parties   | -           | -           | -           | -           |
| Total adjustments to AT1 capital  | -           | -           | -           | -           |
| Investment in Own Shares  | -           | -           | -           | -           |
| Others (specify)  | -           | -           | -           | -           |
| Tier 2 capital after adjustments  | 30,685,749  | 25,928,773  | 31,188,049  | 26,433,203  |
| Total Tier 2 Capital  | 30,685,749  | 25,928,773  | 31,188,049  | 26,433,203  |
| Qualifying Tier 2 capital instruments   | 18,963,673  | 15,835,122  | 18,644,442  | 15,522,576  |
| Revaluation gains   | 2,090,479   | 2,090,479   | 2,090,479   | 2,090,479   |
| General provision/eligible impairment   | 9,631,598   | 8,003,173   | 10,453,129  | 8,820,148   |
| Instruments issued by Consolidated Banking and Financial Subsidiaries of the Bank and held by Third Parties   | -           | -           | -           | -           |
| Total adjustments to Tier 2 capital   | -           | -           | -           | -           |
| Investment in own shares  | -           | -           | -           | -           |
| Others (specify)  | -           | -           | -           | -           |

# Market Discipline

## -Disclosure Requirements Under Pillar III

### TEMPLATE 2 (Contd.)

#### Basel III computation of capital ratios

| As at December 31,  | Bank        |             | Group       |             |
|---|-------------|-------------|-------------|-------------|
|   | 2021        | 2020        | 2021        | 2020        |
|   | Rs 000      | Rs 000      | Rs 000      | Rs 000      |
| Investments in the capital of financial institutions and where the bank does not own more than 10 per cent of the issued capital carrying voting rights of the issuing entity | -           | -           | -           | -           |
| CET1 capital  | 122,797,863 | 117,243,040 | 134,611,494 | 130,836,136 |
| Total Tier 1 capital  | 122,797,863 | 117,243,040 | 134,611,494 | 130,836,136 |
| Total capital   | 153,483,612 | 143,171,814 | 165,799,543 | 157,269,339 |
| Total risk weighted amount (RWA)  | 845,057,594 | 796,090,230 | 931,653,271 | 872,777,199 |
| RWAs for Credit Risk  | 770,527,810 | 724,293,579 | 836,250,291 | 781,917,200 |
| RWAs for Market Risk  | 1,495,688   | 832,706     | 1,770,833   | 974,642     |
| RWAs for Operational Risk   | 73,034,096  | 70,963,945  | 93,632,147  | 89,885,357  |
| CET1 capital ratio (including capital conservation buffer, countercyclical capital buffer & surcharge on D-SIBs) (%)  | 14.53%      | 14.73%      | 14.45%      | 14.99%      |
| Of which: capital conservation buffer (%)   | 1.50%       | 1.50%       | 1.50%       | 1.50%       |
| Of which: countercyclical buffer (%)  |             |             |             |             |
| Of which: capital surcharge on D-SIBs (%)   | 1.00%       | 1.00%       | 1.00%       | 1.00%       |
| Total Tier 1 capital ratio (%)  | 14.53%      | 14.73%      | 14.45%      | 14.99%      |
| Total capital ratio (including capital conservation buffer, countercyclical capital buffer & surcharge on D-SIBs) (%)   | 18.16%      | 17.98%      | 17.80%      | 18.02%      |
| Of which: capital conservation buffer (%)   | 1.50%       | 1.50%       | 1.50%       | 1.50%       |
| Of which: countercyclical buffer (%)  |             |             |             |             |
| Of which: capital surcharge on D-SIBs (%)   | 1.00%       | 1.00%       | 1.00%       | 1.00%       |

### TEMPLATE 3

#### Leverage Ratio

| As at December 31,   | Bank          |               | Group         |               |
|--|---------------|---------------|---------------|---------------|
|  | 2021          | 2020          | 2021          | 2020          |
|  | Rs 000        | Rs 000        | Rs 000        | Rs 000        |
| Tier 1 capital   | 122,797,863   | 117,243,040   | 134,611,494   | 130,836,136   |
| Total exposures  | 1,541,401,389 | 1,516,923,701 | 1,637,315,685 | 1,595,042,163 |
| On-balance sheet items (excluding derivatives and securities financing transactions, but including collateral) | 1,327,980,535 | 1,282,948,314 | 1,417,648,555 | 1,358,239,726 |
| Derivative exposures   | 79,773,591    | 131,225,119   | 79,773,591    | 131,225,119   |
| Securities financing transaction exposures   | 52,976,429    | 13,549,670    | 59,222,705    | 16,376,720    |
| Other off-balance sheet exposures  | 80,670,834    | 89,200,598    | 80,670,834    | 89,200,598    |
| Basel III leverage ratio (Tier 1/Total Exposure) (minimum requirement 3%)                                      | 7.97%         | 7.73%         | 8.22%         | 8.20%         |

## TEMPLATE 4

### Liquidity coverage ratio (LCR) - All currency

| As at December 31,  | 2021             |                | 2020             |                |
|---|------------------|----------------|------------------|----------------|
|   | Total            | Total          | Total            | Total          |
|   | Unweighted Value | Weighted Value | Unweighted Value | Weighted Value |
|   | Rs 000           | Rs 000         | Rs 000           | Rs 000         |
| Total stock of High-Quality Liquid Assets (HQLA)  | 258,645,986      | 248,265,881    | 325,892,151      | 314,678,021    |
| Total adjusted level 1 assets   | 192,950,928      | 192,950,928    | 252,327,699      | 252,327,699    |
| Level 1 assets  | 189,584,236      | 189,584,236    | 251,239,138      | 251,239,138    |
| Total adjusted level 2A assets  | 69,002,201       | 58,651,871     | 74,606,790       | 63,415,772     |
| Level 2A assets   | 69,002,201       | 58,651,871     | 74,606,790       | 63,415,772     |
| Total adjusted level 2B assets  | -                | 29,774         | 46,223           | 23,111         |
| Level 2B assets   | 59,548           | 29,774         | 46,223           | 23,111         |
| Total cash outflows   | 1,188,655,343    | 187,419,777    | 1,084,589,473    | 166,094,800    |
| Deposits  | 853,805,013      | 85,380,501     | 762,154,997      | 76,215,500     |
| Unsecured wholesale funding   | 160,097,825      | 64,375,197     | 161,856,305      | 53,062,438     |
| Secured funding transactions  | 31,928,291       | -              | 10,004,543       | -              |
| Undrawn portion of committed (irrevocable) facilities and other contingent funding obligations                                  | 118,811,903      | 13,651,767     | 128,902,359      | 15,145,593     |
| Additional requirements   | 24,012,312       | 24,012,312     | 21,671,269       | 21,671,269     |
| Total cash inflows  | 128,226,432      | 68,057,930     | 116,452,064      | 57,693,065     |
| Maturing secured lending transactions backed by collateral  | -                | -              | -                | -              |
| Committed facilities  | 3,000,000        | -              | 3,000,000        | -              |
| Other inflows by counterparty which are maturing within 30 days   | 103,361,643      | 60,560,978     | 92,526,949       | 50,962,224     |
| Operational deposits  | 7,316,633        | -              | 7,752,924        | -              |
| Other cash inflows  | 14,548,155       | 7,496,952      | 13,172,191       | 6,730,841      |
| Liquidity coverage ratio (%) (Stock of High Quality Liquid Assets/Total Net Cash Outflows over the Next 30 Calendar Days) * 100 |                  | 207.99%        |                  | 290.29%        |

## TEMPLATE 5

### Net Stable Funding Ratio (NSFR)

| As at December 31,                                  | Bank          |             |
|---|---------------|-------------|
|   | 2021          | 2020        |
|   | Rs 000        | Rs 000      |
| Total available stable funding (ASF)                | 1,005,970,929 | 929,169,118 |
| Required stable funding – On balance sheet assets   | 839,667,564   | 810,951,321 |
| Required stable funding – Off balance sheet items   | 15,944,363    | 14,191,261  |
| Total required stable funding (RSF)                 | 855,611,928   | 825,142,582 |
| NSFR (minimum requirement - 2021 - 90%, 2020 - 90%) | 117.57%       | 112.61%     |

# Market Discipline

## -Disclosure Requirements Under Pillar III

### TEMPLATE 6

#### Main Features of Regulatory Capital Instruments

| Description of the capital instrument  | Stated Capital | Debentures - 2007 | Debentures - 2006 Type F | Debentures - 2016 |
|--|----------------|-------------------|--------------------------|-------------------|
| Issuer   | HNB PLC        | HNB PLC           | HNB PLC                  | HNB PLC           |
| Unique identifier  |                |                   |                          |                   |
| Governing law(s) of the instrument   | Sri Lanka      | Sri Lanka         | Sri Lanka                | Sri Lanka         |
| Original date of issuance  | Not Applicable | August 1, 2007    | April 1, 2006            | November 1, 2016  |
| Par value of instrument  |                | LKR 100/-         | LKR 100/-                | LKR 100/-         |
| Perpetual or dated   | Perpetual      | Dated             | Dated                    | Dated             |
| Original maturity date, if applicable  | Not Applicable | July 31, 2022     | March 31, 2024           | November 1, 2023  |
| Amount recognised in regulatory capital (in Rs 000 as at the reporting date) | 38,679,005     | 140,000           | 992,701                  | 1,600,000         |
| Accounting classification (equity/liability)                                 | Equity         | Liability         | Liability                | Liability         |
| Issuer call subject to prior supervisory approval                            |                |                   |                          |                   |
| Optional call date, contingent call dates and redemption amount (Rs 000)     | Not Applicable | Not Applicable    | Not Applicable           | Not Applicable    |
| Subsequent call Dates, if applicable   | Not Applicable | Not Applicable    | Not Applicable           | Not Applicable    |
| Coupons/Dividends  | Dividends      | Coupons           | Coupons                  | Coupons           |
| Fixed or floating dividend/coupon  | Not Applicable | Fixed             | Fixed                    | Fixed             |
| Coupon rate and any related index  |                | 16.75% p.a.       | 11.25% p.a.              | 13% p.a.          |
| Non-cumulative or cumulative   | Non-cumulative | Cumulative        | Cumulative               | Cumulative        |
| Convertible or Non-Convertible   | Not Applicable | Not Applicable    | Not Applicable           | Not Applicable    |
| If Convertible, Conversion Trigger (s)                                       |                |                   |                          |                   |
| If Convertible, fully or partially   | Not Applicable | Not Applicable    | Not Applicable           | Not Applicable    |
| If convertible, mandatory or optional  | Not Applicable | Not Applicable    | Not Applicable           | Not Applicable    |
| If convertible, conversion rate  | Not Applicable | Not Applicable    | Not Applicable           | Not Applicable    |

| Debentures - 2019<br>(Basel III compliant – Tier 2 listed rated unsecured subordinated redeemable debentures with a non-viability conversion)  | Debentures - 2019<br>(Basel III compliant – Tier 2 listed rated unsecured subordinated redeemable debentures with a non-viability conversion)  | Debentures - 2021 (Basel III compliant – Tier 2 listed rated unsecured subordinated redeemable debentures with a non-viability conversion)   |
|--|--|--|
| HNB PLC  | HNB PLC  | HNB PLC  |
| Sri Lanka  | Sri Lanka  | Sri Lanka  |
| September 23, 2019   | September 23, 2019   | July 28, 2021  |
| LKR 100/-  | LKR 100/-  | LKR 100/-  |
| Dated  | Dated  | Dated  |
| September 22, 2024   | September 22, 2026   | July 28, 2031  |
| 1,153,542  | 8,077,430  | 7,000,000  |
| Liability  | Liability  | Liability  |
| Not Applicable   | Not Applicable   | Not Applicable   |
| Not Applicable   | Not Applicable   | Not Applicable   |
| Coupons  | Coupons  | Coupons  |
| Fixed  | Fixed  | Fixed  |
| 12.3% p.a.   | 12.8% p.a.   | 9.50% p.a.   |
| Cumulative   | Cumulative   | Cumulative   |
| Convertible  | Convertible  | Convertible  |
| A "Trigger Event" is determined by and at the sole discretion of the Monetary Board of the Central Bank of Sri Lanka (i.e., conversion of the said Debentures upon occurrence of the Trigger Event will be affected by the Bank solely upon being instructed by the Monetary Board of the Central Bank of Sri Lanka), and is defined in the Banking Act Direction No. 1 of 2016 of Web-Based Return Code 20.2.3.1.1.1.(10) (iii) (a&b) as a point/event being the earlier of – | A "Trigger Event" is determined by and at the sole discretion of the Monetary Board of the Central Bank of Sri Lanka (i.e., conversion of the said Debentures upon occurrence of the Trigger Event will be affected by the Bank solely upon being instructed by the Monetary Board of the Central Bank of Sri Lanka), and is defined in the Banking Act Direction No. 1 of 2016 of Web-Based Return Code 20.2.3.1.1.1.(10) (iii) (a&b) as a point/event being the earlier of – | A "Trigger Event" is determined by and at the sole discretion of the Monetary Board of the Central Bank of Sri Lanka (i.e., conversion of the said Debentures upon occurrence of the Trigger Event will be affected by the Bank solely upon being instructed by the Monetary Board of the Central Bank of Sri Lanka), and is defined in the Banking Act Direction No. 1 of 2016 of Web-Based Return Code 20.2.3.1.1.1.(10) (iii) (a&b) as a point/event being the earlier of – |
| (a) A decision that a write-down, without which the Bank would become non-viable, is necessary, as determined by the Monetary Board, OR  | (a) A decision that a write-down, without which the Bank would become non-viable, is necessary, as determined by the Monetary Board, OR  | (a) A decision that a write-down, without which the Bank would become non-viable, is necessary, as determined by the Monetary Board, OR  |
| (b) The decision to make a public sector injection of capital, or equivalent support, without which the Bank would have become non-viable, as determined by the Monetary Board.  | (b) The decision to make a public sector injection of capital, or equivalent support, without which the Bank would have become non-viable, as determined by the Monetary Board.  | (b) The decision to make a public sector injection of capital, or equivalent support, without which the Bank would have become non-viable, as determined by the Monetary Board.  |
| Fully  | Fully  | Fully  |
| Optional. At the discretion of the monetary board of the Central Bank of Sri Lanka upon occurrence of trigger points as detailed above.  | Optional. At the discretion of the monetary board of the Central Bank of Sri Lanka upon occurrence of trigger points as detailed above.  | Optional. At the discretion of the monetary board of the Central Bank of Sri Lanka upon occurrence of trigger points as detailed above.  |
| The price based on the simple average of the daily volume of weighted average price (VWAP) of an ordinary voting share of the Bank during the three (03) months period, immediately preceding the date of the Trigger Event.   | The price based on the simple average of the daily volume of weighted average price (VWAP) of an ordinary voting share of the Bank during the three (03) months period, immediately preceding the date of the Trigger Event.   | The price based on the simple average of the daily volume of weighted average price (VWAP) of an ordinary voting share of the Bank during the three (03) months period, immediately preceding the date of the Trigger Event.   |

# Market Discipline

## -Disclosure Requirements Under Pillar III

### TEMPLATE 6 (Contd.)

#### Main Features of Regulatory Capital Instruments

##### Notes

1. A "Trigger Event" is determined by and at the sole discretion of the Monetary Board of the Central Bank of Sri Lanka (i.e., conversion of the said Debentures upon occurrence of the Trigger Event will be affected by the Bank solely upon being instructed by the Monetary Board of the Central Bank of Sri Lanka), and is defined in the Banking Act Direction No. 1 of 2016 of Web-Based Return Code 20.2.3.1.1.1.(10) (iii) (a&b) as a point/event being the earlier of –
  - (a) A decision that a write-down, without which the Bank would become non-viable, is necessary, as determined by the Monetary Board, OR
  - (b) The decision to make a public sector injection of capital, or equivalent support, without which the Bank would have become non-viable, as determined by the Monetary Board.
2. Optional. At the discretion of the monetary board of the Central Bank of Sri Lanka upon occurrence of trigger points as detailed above.
3. The price based on the simple average of the daily volume of weighted average price (VWAP) of an ordinary voting share of the Bank during the three (03) months period, immediately preceding the date of the Trigger Event.

### TEMPLATE 7

#### Summary discussion on adequacy/meeting current and future capital requirements

The starting point for the Bank's capital planning exercise is the strategic plan and the 3 year financial projections which are reviewed annually. Expected macro-economic conditions, strategies planned to drive business growth and the Bank's risk appetite, underpin the financial projections.

Based on the financial projections, future capital requirements are assessed. Subsequently, the assessment proceeds towards gauging how much of required capital will be generated internally and the extent of which, if any is to be sourced externally.

If requirement for external capital is identified, the Bank could consider options such as rights Issues being the raising of capital from existing shareholders, debenture issues, divestment of capital inefficient Investments to free up capital etc. The option determined by management to be the most appropriate would then be recommended to the Board of Directors and a Board Decision would be taken on raising the sufficient amount of capital through one or more of the options identified above.

However, the Bank is extremely well placed on Capital Adequacy with Tier I and Total CAR at 14.53% and 18.16% respectively being among the best in the industry. The financial projections for the next 3 years indicate that HNB will continue to be comfortable on Tier I and Total Capital Adequacy.

In the event that loan growth exceeds forecasts by a considerable margin and/or unforeseen events impede profitability and internal capital generation the Bank would still be well placed to raise capital from one or more of the external sources identified previously as in the past.



## TEMPLATE 8

### Credit risk under standardised approach

#### Credit risk exposures and credit risk mitigation (CRM) effects - Bank

| As at December 31, 2021   | Exposures before Credit Conversion Factor (CCF) and CRM |                              | Exposures post CCF and CRM  |                              | RWA and RWA Density (%) |                       |
|---|---|------------------------------|-----------------------------|------------------------------|-------------------------|-----------------------|
|   | On-balance sheet amount (a)                             | Off-Balance Sheet Amount (b) | On-balance sheet amount (c) | Off-Balance Sheet Amount (d) | RWA (e)                 | RWA Density {e/(c+d)} |
|   | Rs 000  | Rs 000                       | Rs 000                      | Rs 000                       | Rs 000                  | Rs 000                |
| Claims on Central Government and CBSL                                 | 442,063,525   | -                            | 406,217,573                 | -                            | 15,348,025              | 3.78%                 |
| Claims on foreign sovereigns and their central banks                  | -   | -                            | -                           | -                            | -                       | -                     |
| Claims on public sector entities (PSEs)                               | -   | -                            | -                           | -                            | -                       | -                     |
| Claims on Official Entities and Multilateral Development Banks (MDBs) | -   | -                            | -                           | -                            | -                       | -                     |
| Claims on banks exposures   | 12,193,647  | -                            | 12,193,647                  | -                            | 4,452,666               | 36.52%                |
| Claims on financial institutions                                      | 28,800,025  | 1,664,011                    | 28,800,025                  | 1,664,011                    | 18,092,323              | 59.39%                |
| Claims on corporates  | 361,574,102   | 285,619,384                  | 346,696,913                 | 66,781,327                   | 375,235,277             | 90.75%                |
| Retail claims   | 410,042,810   | 103,053,076                  | 364,549,776                 | 17,847,033                   | 270,082,333             | 70.63%                |
| Claims secured by residential property                                | 56,713,342  | -                            | 56,713,342                  | -                            | 30,207,114              | 53.26%                |
| Claims secured by commercial real estate                              | -   | -                            | -                           | -                            | -                       | -                     |
| Non-Performing Assets (NPAs)(i)                                       | 16,490,578  | -                            | 16,490,578                  | -                            | 17,336,208              | 105.13%               |
| Higher-risk categories  | 1,253,786   | -                            | 1,253,786                   | -                            | 3,134,464               | 250.00%               |
| Cash items and other assets   | 66,891,625  | -                            | 66,891,625                  | -                            | 36,639,400              | 54.77%                |
| Total   | 1,396,023,441   | 390,336,470                  | 1,299,807,265               | 86,292,371                   | 770,527,810             |                       |

### Credit risk under standardised approach

#### Credit risk exposures and credit risk mitigation (CRM) effects - Group

| As at December 31, 2021   | Exposures before Credit Conversion Factor (CCF) and CRM |                              | Exposures post CCF and CRM  |                              | RWA and RWA Density (%) |                       |
|---|---|------------------------------|-----------------------------|------------------------------|-------------------------|-----------------------|
|   | On-balance sheet amount (a)                             | Off-Balance Sheet Amount (b) | On-balance sheet amount (c) | Off-Balance Sheet Amount (d) | RWA (e)                 | RWA Density {e/(c+d)} |
|   | Rs 000  | Rs 000                       | Rs 000                      | Rs 000                       | Rs 000                  | Rs 000                |
| Claims on Central Government and CBSL                                 | 451,527,304   | -                            | 415,681,351                 | -                            | 15,348,025              | 3.69%                 |
| Claims on foreign sovereigns and their central banks                  | -   | -                            | -                           | -                            | -                       | -                     |
| Claims on public sector entities (PSEs)                               | -   | -                            | -                           | -                            | -                       | -                     |
| Claims on Official Entities and Multilateral Development Banks (MDBs) | -   | -                            | -                           | -                            | -                       | -                     |
| Claims on banks exposures   | 22,127,241  | -                            | 22,127,241                  | -                            | 8,119,213               | 36.69%                |
| Claims on financial institutions                                      | 32,975,784  | 1,664,011                    | 32,975,784                  | 1,664,011                    | 20,180,202              | 58.26%                |
| Claims on corporates  | 369,256,580   | 285,619,384                  | 354,379,391                 | 66,781,327                   | 382,610,805             | 90.85%                |
| Retail claims   | 444,790,256   | 103,053,076                  | 399,297,222                 | 17,847,033                   | 296,142,917             | 70.99%                |
| Claims secured by residential property                                | 56,713,342  | -                            | 56,713,342                  | -                            | 30,207,114              | 53.26%                |
| Claims secured by commercial real estate                              | -   | -                            | -                           | -                            | -                       | -                     |
| Non-Performing Assets (NPAs)(i)                                       | 16,490,578  | -                            | 16,490,578                  | -                            | 17,336,208              | 105.13%               |
| Higher-risk categories  | 1,360,413   | -                            | 1,360,413                   | -                            | 3,401,032               | 250.00%               |
| Cash items and other assets   | 95,975,005  | -                            | 95,975,005                  | -                            | 62,904,774              | 65.54%                |
| Total   | 1,491,216,502   | 390,336,470                  | 1,395,000,327               | 86,292,371                   | 836,250,291             |                       |

# Market Discipline

## -Disclosure Requirements Under Pillar III

### TEMPLATE 9

#### Credit risk under standardised approach - Exposures by asset classes and risk weights (Post CCF & CRM) - Bank

| As at December 31,2021   | 0%          | 10%         | 20%        | 35%        | 50%        | 60%        | 75%         | 100%        | 150%      | >150%     | Total Credit Exposures Amount |
|--|-------------|-------------|------------|------------|------------|------------|-------------|-------------|-----------|-----------|-------------------------------|
|  | Rs 000      | Rs 000      | Rs 000     | Rs 000     | Rs 000     | Rs 000     | Rs 000      | Rs 000      | Rs 000    | Rs 000    | Rs 000                        |
| Claims on central government and Central Bank of Sri Lanka     | 252,737,318 | 153,480,255 | -          | -          | -          | -          | -           | -           | -         | -         | 406,217,573                   |
| Claims on foreign sovereigns and their central banks           | -           | -           | -          | -          | -          | -          | -           | -           | -         | -         | -                             |
| Claims on public sector entities                               | -           | -           | -          | -          | -          | -          | -           | -           | -         | -         | -                             |
| Claims on official entities and multilateral development banks | -           | -           | -          | -          | -          | -          | -           | -           | -         | -         | -                             |
| Claims on banks exposures                                      | -           | -           | 6,656,270  | -          | 4,927,481  | -          | -           | 514,346     | 95,550    | -         | 12,193,647                    |
| Claims on financial institutions                               | -           | -           | -          | -          | 24,898,857 | -          | -           | 5,409,750   | 155,429   | -         | 30,464,037                    |
| Claims on corporates   | -           | -           | 27,957,665 | -          | 31,832,463 | -          | -           | 353,609,307 | 78,804    | -         | 413,478,239                   |
| Retail claims  | -           | -           | -          | -          | -          | 98,224,862 | 179,754,265 | 76,331,716  | -         | -         | 354,310,844                   |
| Claims secured by gold   | 28,085,966  | -           | -          | -          | -          | -          | -           | -           | -         | -         | 28,085,966                    |
| Claims secured by residential property                         | -           | -           | -          | 40,778,813 | -          | -          | -           | 15,934,529  | -         | -         | 56,713,342                    |
| Claims secured by commercial real estate                       | -           | -           | -          | -          | -          | -          | -           | -           | -         | -         | -                             |
| Non-Performing Assets (NPAs)                                   | -           | -           | -          | -          | 32,446     | -          | -           | 14,734,428  | 1,723,705 | -         | 16,490,578                    |
| Higher-risk categories   | -           | -           | -          | -          | -          | -          | -           | -           | -         | 1,253,786 | 1,253,786                     |
| Cash items and other assets                                    | 30,252,225  | -           | -          | -          | -          | -          | -           | 36,639,400  | -         | -         | 66,891,625                    |
| Total  | 311,075,509 | 153,480,255 | 34,613,935 | 40,778,813 | 61,691,246 | 98,224,862 | 179,754,265 | 503,173,477 | 2,053,488 | 1,253,786 | 1,386,099,636                 |

#### Credit risk under standardised approach - Exposures by asset classes and risk weights (Post CCF & CRM) - Group

| As at December 31,2021   | 0%          | 10%         | 20%        | 35%        | 50%        | 60%        | 75%         | 100%        | 150%      | >150%     | Total Credit Exposures Amount |
|--|-------------|-------------|------------|------------|------------|------------|-------------|-------------|-----------|-----------|-------------------------------|
|  | Rs 000      | Rs 000      | Rs 000     | Rs 000     | Rs 000     | Rs 000     | Rs 000      | Rs 000      | Rs 000    | Rs 000    | Rs 000                        |
| Claims on central government and Central Bank of Sri Lanka     | 262,201,096 | 153,480,255 | -          | -          | -          | -          | -           | -           | -         | -         | 415,681,351                   |
| Claims on foreign sovereigns and their central banks           | -           | -           | -          | -          | -          | -          | -           | -           | -         | -         | -                             |
| Claims on public sector entities                               | -           | -           | -          | -          | -          | -          | -           | -           | -         | -         | -                             |
| Claims on official entities and multilateral development banks | -           | -           | -          | -          | -          | -          | -           | -           | -         | -         | -                             |
| Claims on banks exposures                                      | -           | -           | 10,990,435 | -          | 10,526,910 | -          | -           | 514,346     | 95,550    | -         | 22,127,241                    |
| Claims on financial institutions                               | -           | -           | -          | -          | 29,074,616 | -          | -           | 5,409,750   | 155,429   | -         | 34,639,795                    |
| Claims on corporates   | -           | -           | 28,105,777 | -          | 32,209,384 | -          | -           | 360,766,752 | 78,804    | -         | 421,160,717                   |
| Retail claims  | -           | -           | -          | -          | -          | 98,224,862 | 214,501,711 | 76,331,716  | -         | -         | 389,058,290                   |
| Claims secured by gold   | 28,085,966  | -           | -          | -          | -          | -          | -           | -           | -         | -         | 28,085,966                    |
| Claims secured by residential property                         | -           | -           | -          | 40,778,813 | -          | -          | -           | 15,934,529  | -         | -         | 56,713,342                    |
| Claims secured by commercial real estate                       | -           | -           | -          | -          | -          | -          | -           | -           | -         | -         | -                             |
| Non-Performing Assets (NPAs)                                   | -           | -           | -          | -          | 32,446     | -          | -           | 14,734,428  | 1,723,705 | -         | 16,490,578                    |
| Higher-risk categories   | -           | -           | -          | -          | -          | -          | -           | -           | -         | 1,360,413 | 1,360,413                     |
| Cash items and other assets                                    | 33,070,231  | -           | -          | -          | -          | -          | -           | 62,904,774  | -         | -         | 95,975,005                    |
| Total  | 323,357,293 | 153,480,255 | 39,096,212 | 40,778,813 | 71,843,355 | 98,224,862 | 214,501,711 | 536,596,297 | 2,053,488 | 1,360,413 | 1,481,292,697                 |

## TEMPLATE 10

### Market risk under standardised measurement method

| As at December 31,                                     | Bank      |         | Group     |         |
|--|-----------|---------|-----------|---------|
|  | 2021      | 2020    | 2021      | 2020    |
|  | Rs 000    | Rs 000  | Rs 000    | Rs 000  |
| (a) Capital charge for interest rate risk              | -         | -       | -         | -       |
| General interest rate risk                             | -         | -       | -         | -       |
| (i) Net long or short position                         | -         | -       | -         | -       |
| (ii) Horizontal disallowance                           | -         | -       | -         | -       |
| (iii) Vertical disallowance                            | -         | -       | -         | -       |
| (iv) Options   | -         | -       | -         | -       |
| Specific interest rate risk                            | -         | -       | -         | -       |
| (b) Capital charge for equity                          | 12,251    | 8,439   | 46,644    | 26,181  |
| (i) General equity risk                                | 7,444     | 4,622   | 26,838    | 13,745  |
| (ii) Specific equity risk                              | 4,807     | 3,817   | 19,806    | 12,437  |
| (c) Capital charge for foreign exchange & gold         | 174,710   | 95,649  | 174,710   | 95,649  |
| Capital charge for market risk [(a) + (b) + (c)] * CAR | 1,495,688 | 832,706 | 1,770,833 | 974,642 |

# Market Discipline

## -Disclosure Requirements Under Pillar III

### TEMPLATE 11

#### Operational Risk under basic indicator approach - Bank

| As at December 31,                        | Capital Charge Factor | Fixed Factor | 2020       |            |            | 2021       |            |            |
|---|-----------------------|--------------|------------|------------|------------|------------|------------|------------|
|   |                       |              | 1st Year   | 2nd Year   | 3rd Year   | 1st Year   | 2nd Year   | 3rd Year   |
|   |                       |              | Rs 000     | Rs 000     | Rs 000     | Rs 000     | Rs 000     | Rs 000     |
| Gross Income                              | N/A                   | N/A          | 60,830,747 | 60,000,953 | 56,578,162 | 60,000,953 | 56,578,162 | 66,006,125 |
| Capital Charges                           | 15%                   | N/A          | 9,124,612  | 9,000,143  | 8,486,724  | 9,000,143  | 8,486,724  | 9,900,919  |
| Capital Charges for Operational Risk      |                       |              |            |            | 8,870,493  |            |            | 9,129,262  |
| The Basic Indicator Approach              |                       |              |            |            | 8,870,493  |            |            | 9,129,262  |
| Risk Weighted Amount for Operational Risk |                       |              |            |            | 70,963,945 |            |            | 73,034,096 |

#### Operational Risk under basic indicator approach - Group

| As at December 31,                        | Capital Charge Factor | Fixed Factor | 2020       |            |            | 2021       |            |            |
|---|-----------------------|--------------|------------|------------|------------|------------|------------|------------|
|   |                       |              | 1st Year   | 2nd Year   | 3rd Year   | 1st Year   | 2nd Year   | 3rd Year   |
|   |                       |              | Rs 000     | Rs 000     | Rs 000     | Rs 000     | Rs 000     | Rs 000     |
| Gross Income                              | N/A                   | N/A          | 75,398,127 | 76,867,302 | 72,447,964 | 76,867,302 | 72,447,965 | 84,765,100 |
| Capital Charges                           | 15%                   | N/A          | 11,309,719 | 11,530,095 | 10,867,195 | 11,530,095 | 10,867,195 | 12,714,765 |
| Capital Charges for Operational Risk      |                       |              |            |            | 11,235,670 |            |            | 11,704,018 |
| The Basic Indicator Approach              |                       |              |            |            | 11,235,670 |            |            | 11,704,018 |
| Risk Weighted Amount for Operational Risk |                       |              |            |            | 89,885,357 |            |            | 93,632,147 |

## TEMPLATE 12

### Differences between Accounting and Regulatory Scopes and Mapping of Financial Statement Categories with Regulatory Risk Categories – Bank only

| Amount as at December 31 ,2021  | a   | b   | c                                | d                                | e  |
|---|---|---|----------------------------------|----------------------------------|--|
|   | Carrying Values as Reported in Published Financial Statements | Carrying Values under Scope of Regulatory Reporting | Subject to Credit Risk Framework | Subject to Market Risk Framework | Not subject to Capital Requirements or Subject to Deduction from Capital |
|   | Rs 000  | Rs 000  | Rs 000                           | Rs 000                           | Rs 000   |
| Assets  | 1,358,336,621   | 1,387,203,618                                       | 1,280,019,542                    | 103,365                          | 102,959,711  |
| Cash and cash equivalents   | 38,185,254  | 38,194,133  | 38,194,133                       | -                                | -  |
| Placements with banks   | -   | -   | -                                | -                                | -  |
| Balances with Central Bank of Sri Lanka                                       | 25,820,489  | 25,820,489  | 30,225,639                       | -                                | -  |
| Reverse repurchase agreements   | -   | -   | -                                | -                                | -  |
| Derivative financial instruments  | 927,487   | -   | -                                | -                                | -  |
| Financial assets measured at fair value through profit or loss                | 103,365   | 103,365   | -                                | 103,365                          | -  |
| Financial assets at amortised cost - Loans and advances to banks              | -   | -   | -                                | -                                | -  |
| Financial assets measured at amortised cost - loans and advances to customers | 876,254,693   | 899,569,691   | 803,353,515                      | -                                | 96,216,176   |
| Financial assets measured at amortised cost - debt and other instruments      | 160,677,520   | 172,133,698   | 172,133,698                      | -                                | -  |
| Financial assets measured at fair value through other comprehensive income    | 203,426,433   | 200,666,754   | 197,030,383                      | -                                | 3,636,370  |
| Investment in joint venture   | 755,000   | 755,000   | -                                | -                                | 755,000  |
| Investments in subsidiaries   | 3,017,285   | 3,017,285   | 1,973,000                        | -                                | 1,044,285  |
| Investments in associates   | -   | -   | -                                | -                                | -  |
| Investment properties   | 469,774   | 469,774   | 469,774                          | -                                | -  |
| Property, plant and equipment   | 24,953,738  | 24,953,738  | 24,953,738                       | -                                | -  |
| Right-of-use assets   | 5,439,384   | 5,439,384   | -                                | -                                | -  |
| Intangible assets and goodwill  | 1,429,544   | 1,429,544   | -                                | -                                | 1,307,880  |
| Deferred tax assets   | 4,461,561   | -   | -                                | -                                | -  |
| Other assets  | 12,415,094  | 14,650,764  | 11,685,662                       | -                                | -  |
| Liabilities   | 1,206,295,267   | 1,214,858,973                                       | -                                | -                                | -  |
| Due to banks  | 17,075,502  | 17,075,502  | -                                | -                                | -  |
| Derivative financial instruments  | 353,356   | -   | -                                | -                                | -  |
| Securities sold under repurchase agreements                                   | 33,524,226  | 33,524,226  | -                                | -                                | -  |
| Financial liabilities measured at amortised cost - due to depositors          | 1,075,709,287   | 1,076,274,453                                       | -                                | -                                | -  |
| Dividends payable   | 989,212   | 989,212   | -                                | -                                | -  |
| Financial liabilities measured at amortised cost - other borrowings           | 24,747,869  | 24,879,626  | -                                | -                                | -  |
| Debt securities issued  | 1,962,749   | 1,962,749   | -                                | -                                | -  |
| Current tax liabilities   | 10,051,689  | 10,961,395  | -                                | -                                | -  |
| Deferred tax liabilities  | -   | 7,359,259   | -                                | -                                | -  |
| Other provisions  | 3,928,598   | 7,012,669   | -                                | -                                | -  |
| Other liabilities   | 14,400,456  | 11,267,559  | -                                | -                                | -  |

# Market Discipline

## -Disclosure Requirements Under Pillar III

### TEMPLATE 12 (Contd.)

#### Differences between Accounting and Regulatory Scopes and Mapping of Financial Statement Categories with Regulatory Risk Categories – Bank only

| Amount as at December 31 ,2021   | a   | b   | c                                | d                                | e  |
|--|---|---|----------------------------------|----------------------------------|--|
|  | Carrying Values as Reported in Published Financial Statements | Carrying Values under Scope of Regulatory Reporting | Subject to Credit Risk Framework | Subject to Market Risk Framework | Not subject to Capital Requirements or Subject to Deduction from Capital |
|  | Rs 000  | Rs 000  | Rs 000                           | Rs 000                           | Rs 000   |
| Due to subsidiaries  | -   | -   | -                                | -                                | -  |
| Subordinated liabilities   | -   | -   | -                                | -                                | -  |
| Subordinated term debts  | 23,552,323  | 23,552,323  | -                                | -                                | -  |
| Off-Balance Sheet Liabilities  | 676,242,350   | 676,242,350   | -                                | -                                | -  |
| Guarantees   | 56,870,256  | 56,870,256  | 56,870,256                       | -                                | -  |
| Performance Bonds  | 43,904,180  | 43,904,180  | 43,904,180                       | -                                | -  |
| Letters of Credit  | 32,567,799  | 32,567,799  | 32,567,799                       | -                                | -  |
| Other Contingent Items   | 103,763,239   | 103,763,239   | 103,763,239                      | -                                | -  |
| Undrawn Loan Commitments   | 439,136,875   | 439,136,875   | 439,136,875                      | -                                | -  |
| Other Commitments  | -   | -   | -                                | -                                | -  |
| Shareholders' Equity   | -   | -   | -                                | -                                | -  |
| Equity Capital (Stated Capital)/Assigned Capital of which Amount Eligible for CET1 | 37,364,244  | 37,028,291  | -                                | -                                | -  |
| Of which Amount Eligible for AT1   | -   | -   | -                                | -                                | -  |
| Retained Earnings  | 35,186,607  | 54,571,793  | -                                | -                                | -  |
| Accumulated Other Comprehensive Income   | (1,254,053)   | -   | -                                | -                                | -  |
| Other Reserves   | 80,744,556  | 80,744,562  | -                                | -                                | -  |
| Total Shareholders' Equity   | 152,041,354   | 172,344,645   | -                                | -                                | -  |

## TEMPLATE 12 (A)

### Explanation of Significant Differences between Accounting and Regulatory Exposure Amounts

#### (a) Derivative financial instruments

Derivatives are financial instruments which derive values in response to changes in interest rates, financial instrument prices, commodity prices, foreign exchange rates, credit risk and indices.

The fair value of these derivative financial instruments are determined using forward pricing models. The positive fair value changes of these financial instruments as at the balance sheet date are reported as assets while the negative fair value changes are reported as liabilities. The details of derivative financial instruments have been disclosed in Note 29 to the financial statements.

#### (b) Loans and receivables to other customers

The loans and receivables to customers considered in regulatory reporting differs with the published financial statements since CBSL time based provisions were netted off when arriving at loans and receivables for regulatory reporting purposes, while impairment allowances based on incurred losses have been netted off in loans and receivables for publication purposes. The impairment allowance has been computed using established processes with judgments being exercised when determining the presence of objective evidences of impairment. The process used in determining the impairment provision has been described in detail in Note 31 (c) to the financial statements.

#### (c) Financial assets measured at fair value through OCI

Financial assets at fair value through OCI have been measured at fair value in published financial statements while these investments have been measured at cost for regulatory reporting purpose. The details of financial investments - available for sale have been disclosed in Note 33 to the financial statements.

## TEMPLATE 13 : BANK RISK MANAGEMENT APPROACH

The Risk Report from pages 41 to 87 in CG&RR sets out the Bank's approach to risk management including governance structures, policies, processes, limits and the current risk profile of the Bank.

## TEMPLATE 14 : RISK MANAGEMENT RELATED TO KEY RISK EXPOSURES

| Risk   | Compliance  |
|--|---|
| Section I -Credit Risk                               | Refer Note 5 to the Financial Statements on pages 160 to 193 in IR  |
| Section II Market Risk                               | Refer Note 5 to the Financial Statements on pages 160 to 193 in IR  |
| Section II (a) IRR                                   | Refer Page 102 in CG&RR   |
| Section II (b) Equity Position Risk                  | Refer Page 102 in CG&RR   |
| Section II (c) Foreign Exchange                      | Refer Page 73 in CG&RR  |
| Section III Liquidity Risk                           |   |
| Section III (a)                                      | Refer Page 104 in CG&RR   |
| Section III (b)                                      | Refer Pages 105 to 106 in CG&RR   |
| Section III (c) & (d)                                | Refer Pages 74 to 75 in CG&RR   |
| Section IV Operational Risk                          | Refer Note 5 to the Financial Statements on pages 160 to 193 in IR<br>Major Financial Losses incurred by Bank on page 63 in CG&RR<br>Details of activities that have been outsourced together with parties and basis for payment for such services on page 65 in CG&RR.<br>Details of due diligence tests of third party service providers on page 65 in CG&RR. |
| Section V Interest Rate Risk in Banking Book (IRRBB) | Refer page 107 in CG&RR   |

# Market Discipline

## -Disclosure Requirements Under Pillar III

### TEMPLATE 14 - SECTION II MARKET RISK -(A) INTEREST RATE RISK

#### Interest Rate Sensitivity Gap Analysis as at 31-Dec-2021-LKR

(Values are in Millions LKR)

|                                  |  |  | 1M         | 3M         | 6M          | 1Y          | 3Y         | 5Y          | >5Y          |
|----------------------------------|--|--|------------|------------|-------------|-------------|------------|-------------|--------------|
| Account Type                     | Product                                  | Product Name Level18                                       |            |            |             |             |            |             |              |
| Rate Sensitive Assets            | Inflows                                  | Balances due from Head Office, Affiliates and Own Branches | 0.00       | 0.00       | 0.00        | 0.00        | 0.00       | 0.00        | 3,772.29     |
|                                  |  | Bills of Exchange  | 80.80      | 14.16      | 0.00        | 0.00        | 0.00       | 0.00        | 0.00         |
|                                  |  | Cash on hand   | 30,245.16  | 0.00       | 0.00        | 195.75      | 0.00       | 0.00        | 0.00         |
|                                  |  | Deposits with CBSL   | 1,291.02   | 1,291.02   | 1,291.02    | 2,582.05    | 6,455.12   | 6,455.12    | 6,455.12     |
|                                  |  | Investments (Net of provisions)                            | 53,191.34  | 119,938.53 | 984.79      | 592.37      | 17,825.64  | 8,356.39    | 8,900.88     |
|                                  |  | Loans and Advances   | 305,200.61 | 47,166.09  | 59,606.88   | 78,063.06   | 107,859.85 | 58,683.19   | 31,360.44    |
|                                  |  | NPLs   | 0.86       | 0.86       | 0.00        | 1,342.65    | 0.00       | 0.00        | 4,027.95     |
|                                  |  | Net Inter-Branch Transactions                              | 0.00       | 0.00       | 0.00        | 0.00        | 0.00       | 0.00        | 0.14         |
|                                  |  | Other Assets   | 1,050.29   | 1,697.40   | 60.06       | 7,139.33    | 0.00       | 0.00        | 10,297.00    |
|                                  |  | Overdraft  | 74,076.55  | 7,578.59   | 4,095.33    | 6,226.85    | 3,641.76   | 3,335.02    | 3,284.66     |
|                                  |  | Accrued Interest   | 2,190.08   | 467.04     | 534.11      | 736.40      | 119.05     | 0.41        | 0.67         |
|                                  |  | Balances due from Other Banks                              | 0.00       | 0.00       | 0.00        | 0.00        | 0.00       | 0.00        | 0.00         |
|                                  |  | Fixed Assets L1  | 0.00       | 0.00       | 0.00        | 0.00        | 0.00       | 0.00        | 26,849.31    |
|                                  |  |  | 467,326.72 | 178,153.69 | 66,572.19   | 96,878.45   | 135,901.41 | 76,830.13   | 94,948.46    |
| Rate Sensitive Liabilities       | Outflows                                 | Balances due to Other Banks                                | 0.00       | 0.00       | 0.00        | 0.00        | 0.00       | 0.00        | 629.90       |
|                                  |  | Bills Payable  | 1,589.31   | 0.00       | 0.00        | 0.00        | 0.00       | 0.00        | 0.00         |
|                                  |  | Demand Deposits  | 13,680.04  | 13,680.04  | 10,260.03   | 13,680.03   | 15.77      | 15.77       | 17,110.55    |
|                                  |  | Interest Payable   | 1,937.40   | 2,519.22   | 2,760.35    | 2,940.58    | 3,913.74   | 143.36      | 0.09         |
|                                  |  | Other Liabilities  | 172.21     | 0.00       | 210.72      | 6,280.11    | 20,245.70  | 3,034.45    | 9,054.41     |
|                                  |  | Savings Deposits   | 21,020.69  | 44,206.97  | 14,421.15   | 19,208.97   | 72,107.18  | 72,105.74   | 72,105.74    |
|                                  |  | Time Deposits  | 58,604.47  | 111,043.25 | 100,842.92  | 151,716.23  | 23,698.84  | 3,682.28    | 13.14        |
|                                  |  | Bonds Issued   | 0.00       | 0.00       | 0.00        | 700.00      | 8,903.66   | 8,077.43    | 7,000.00     |
|                                  |  | Borrowings   | 659.52     | 856.58     | 512.90      | 1,895.29    | 3,941.11   | 2,734.43    | 105.24       |
|                                  |  | Capital & Reserves   | 0.00       | 0.00       | 0.00        | 0.00        | 0.00       | 0.00        | 37,028.29    |
|                                  |  | Repo   | 31,928.29  | 1,343.62   | 198.62      | 16.95       | 0.00       | 0.00        | 0.00         |
|                                  |  | Reserves   | 0.00       | 0.00       | 0.00        | 0.00        | 0.00       | 0.00        | 154,555.39   |
|                                  |  |  |            |            | 129,591.93  | 173,649.68  | 129,206.68 | 196,438.15  | 132,826.00   |
| Net Gap                          |  |  | 337,734.78 | 4,504.01   | (62,634.49) | (99,559.71) | 3,075.41   | (12,963.33) | (202,654.29) |
| Cumulative Gap                   |  |  | 337,734.78 | 342,238.79 | 279,604.30  | 180,044.59  | 183,120.00 | 170,156.67  | (32,497.62)  |
| Rate Sensitive Assets total      | (Excl- Cash on hand, Deposits with CBSL) |  | 435,790.54 | 176,862.66 | 65,281.16   | 94,100.65   | 129,446.29 | 70,375.01   | 88,493.34    |
| Rate Sensitive Liabilities total | (Excl- Demand Deposits, Capital)         |  | 115,911.90 | 159,969.64 | 118,946.66  | 182,758.12  | 132,810.23 | 89,777.70   | 243,463.90   |
| Net Gap                          |  |  | 319,878.64 | 16,893.02  | (53,665.49) | (88,657.48) | (3,363.94) | (19,402.69) | (154,970.56) |
| Cumulative Gap                   |  |  | 319,878.64 | 336,771.66 | 283,106.16  | 194,448.69  | 191,084.74 | 171,682.06  | 16,711.50    |



## TEMPLATE 14 - SECTION II MARKET RISK -(A) INTEREST RATE RISK

### Interest Rate Sensitivity Gap Analysis as at 31-Dec-2021-USD

(Values are in Thousands USD)

|   |          |                                 | 1M         | 3M         | 6M          | 1Y          | 3Y         | 5Y         | >5Y        |
|---|----------|---------------------------------|------------|------------|-------------|-------------|------------|------------|------------|
| Account Type  | Product  | Product Name Level18            |            |            |             |             |            |            |            |
| Rate Sensitive Assets                                   | Inflows  | Bills of Exchange               | 2,827.55   | 1,828.54   | 55.91       | 0.00        | 0.00       | 0.00       | 0.00       |
|   |          | Cash on hand                    | 1,976.59   | 0.00       | 0.00        | 0.00        | 0.00       | 0.00       | 0.00       |
|   |          | Investments (Net of provisions) | 87,500.00  | 115,000.00 | 20,000.00   | 95,755.00   | 300,827.00 | 115,134.95 | 71,380.00  |
|   |          | Loans and Advances              | 242,537.47 | 130,181.20 | 55,635.09   | 1,836.74    | 5,074.44   | 2,506.00   | -18,577.37 |
|   |          | NPLs                            | 0.00       | 0.00       | 0.00        | 5,185.18    | 0.00       | 0.00       | 15,555.55  |
|   |          | Other Assets                    | 917.17     | 1,698.14   | 0.00        | 0.00        | 0.00       | 0.00       | 225.07     |
|   |          | Overdraft                       | 9,064.44   | 307.15     | 226.35      | 452.71      | 628.72     | 628.66     | 628.90     |
|   |          | Accrued Interest                | 506.71     | 169.82     | 459.05      | 214.91      | 110.14     | 0.00       | 0.00       |
|   |          | Balances due from Other Banks   | 0.00       | 0.00       | 0.00        | 0.00        | 0.00       | 0.00       | 32,857.46  |
|   |          |                                 | 345,329.92 | 249,184.86 | 76,376.41   | 103,444.54  | 306,640.30 | 118,269.61 | 102,069.62 |
| Rate Sensitive Liabilities                              | Outflows | Balances due to Other Banks     | 2,500.00   | 25,042.00  | 95,384.62   | 0.00        | 0.00       | 0.00       | 0.00       |
|   |          | Demand Deposits                 | 4,862.78   | 4,862.79   | 3,647.07    | 4,862.70    | 209.07     | 209.06     | 6,217.82   |
|   |          | Interest Payable                | 2,250.85   | 5,417.77   | 6,224.95    | 3,010.43    | 2,884.32   | 519.66     | 0.00       |
|   |          | Other Liabilities               | 332.34     | 417.51     | 359.37      | 3,038.68    | 1,245.79   | 1,245.76   | 16,661.91  |
|   |          | Savings Deposits                | 14,450.98  | 14,452.06  | 10,833.63   | 14,430.40   | 54,169.24  | 54,168.16  | 54,168.16  |
|   |          | Time Deposits                   | 114,022.06 | 183,970.57 | 193,643.39  | 198,824.30  | 28,799.84  | 13,346.87  | 0.00       |
|   |          |                                 | 138,419.02 | 234,162.70 | 310,093.03  | 224,166.51  | 87,308.26  | 69,489.51  | 77,047.89  |
| Net Gap   |          |                                 | 206,910.90 | 15,022.16  | -233,716.62 | -120,721.97 | 219,332.04 | 48,780.09  | 25,021.73  |
| Cumulative Gap  |          |                                 | 206,910.90 | 221,933.06 | -11,783.56  | -132,505.53 | 86,826.51  | 135,606.60 | 160,628.33 |
| Rate Sensitive Assets total (Excl - Cash on Hand)       |          |                                 | 343,353.34 | 249,184.86 | 76,376.41   | 103,444.54  | 306,640.30 | 118,269.61 | 102,069.62 |
| Rate Sensitive Liabilities total (Excl- Demand Deposit) |          |                                 | 133,556.24 | 229,299.91 | 306,445.96  | 219,303.81  | 87,099.19  | 69,280.45  | 70,830.06  |
| Net Gap   |          |                                 | 209,797.10 | 19,884.94  | -230,069.55 | -115,859.27 | 219,541.11 | 48,989.16  | 31,239.56  |
| Cumulative Gap  |          |                                 | 209,797.10 | 229,682.04 | -387.51     | -116,246.78 | 103,294.33 | 152,283.48 | 183,523.04 |

#### Notes

- 1) The above figures have been prepared including interest cash flows and may differ from SLFRS figures given in the Statement of Financial Position
- 2) Prepared as per the requirements given in the Banking Act Direction No 7 of 2011 on "Integrated Risk Management Framework".

## TEMPLATE 14 - SECTION II MARKET RISK -(B) EQUITY POSITION RISK

| Equity               | Carrying Value | Fair Value | Realized Gains/Losses | Unrealized Gains/Losses | Capital Adequacy Calculation |
|----------------------|----------------|------------|-----------------------|-------------------------|------------------------------|
| Investment Portfolio | 12,860         | 23,835     |                       |                         | 1,496                        |
| Trading Portfolio    | 129            | 103        |                       |                         | 187                          |

# Market Discipline

## -Disclosure Requirements Under Pillar III

### TEMPLATE 14 - SECTION II MARKET RISK -(C) FOREIGN EXCHANGE RISK

#### Report on Liquidity Gap Summary as at 31st Dec 2021 (Consolidated Foreign Currency)

(Amounts are in Thousands USD)

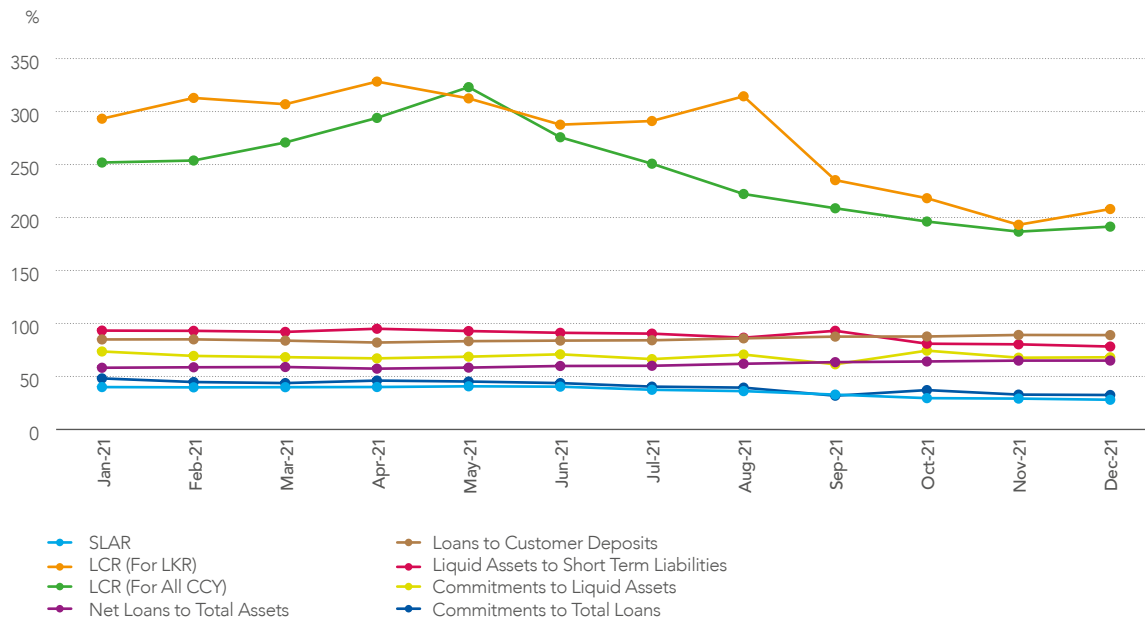
|                                |  | 1M         | 3M           | 6M           | 1Y           | 3Y          | 5Y         | >5Y        |
|--------------------------------|--|------------|--------------|--------------|--------------|-------------|------------|------------|
| Particulars                    | Product                                      |            |              |              |              |             |            |            |
| Total Inflows                  | Bills of Exchange                            | 0.00       | 0.00         | 0.00         | 0.00         | 0.00        | 0.00       | 0.00       |
|                                | Cash on hand                                 | 0.00       | 0.00         | 0.00         | 0.00         | 0.00        | 0.00       | 0.00       |
|                                | Investments (Net of provisions)              | 94,162.49  | 121,091.48   | 29,255.72    | 113,639.10   | 348,056.65  | 138,543.82 | 76,063.25  |
|                                | Loans and Advances                           | 29,399.11  | 59,473.11    | 94,604.65    | 47,759.55    | 116,807.65  | 62,558.37  | 72,767.08  |
|                                | NPLs   | 0.00       | 0.00         | 0.00         | 5,185.18     | 0.00        | 0.00       | 15,555.55  |
|                                | Other Assets                                 | 917.17     | 1,161.09     | 0.00         | 0.00         | 0.00        | 0.00       | 0.00       |
|                                | Other  | 0.00       | 0.00         | 3,605.48     | 7,212.05     | 0.00        | 0.00       | 0.00       |
|                                | Overdraft                                    | 946.95     | 1,021.31     | 1,074.40     | 2,102.19     | 3,395.47    | 3,028.73   | 2,670.37   |
|                                | Accrued Interest                             | 519.65     | 169.82       | 491.31       | 227.81       | 110.22      | 0.00       | 0.00       |
|                                | Balances due from Other Banks                | 0.00       | 0.00         | 0.00         | 0.00         | 0.00        | 0.00       | 30,947.25  |
|                                | Forward Contracts                            | 123,619.42 | 66,963.99    | 17,639.22    | 3,000.00     | 0.00        | 0.00       | 0.00       |
|                                |  | 249,564.79 | 249,880.80   | 146,670.78   | 179,125.88   | 468,369.98  | 204,130.92 | 198,003.50 |
| Total Outflows                 | Balances due to Other Banks                  | 2,512.15   | 16,143.90    | 32,643.11    | 5,297.62     | 24,548.91   | 40,259.24  | 11,087.71  |
|                                | Demand Deposits                              | 5,572.07   | 5,572.07     | 4,179.03     | 5,571.98     | 221.32      | 221.31     | 7,112.59   |
|                                | Interest Payable                             | 2,444.24   | 5,689.46     | 6,795.45     | 3,306.75     | 2,897.06    | 519.67     | 0.00       |
|                                | Letters of Credit/Guarantees/<br>Acceptances | 0.00       | 3,614.95     | 3,614.95     | 3,616.04     | 0.00        | 0.00       | 0.00       |
|                                | Other Liabilities                            | 355.85     | 0.00         | 392.40       | 3,143.81     | 1,333.89    | 1,333.87   | 3,952.53   |
|                                | Savings Deposits                             | 17,527.03  | 17,845.20    | 13,867.13    | 19,031.37    | 70,309.98   | 67,833.33  | 65,406.41  |
|                                | Time Deposits                                | 127,482.87 | 207,832.35   | 227,852.92   | 244,245.35   | 35,317.68   | 16,864.20  | 0.00       |
|                                | Forward Contracts Payable                    | 83,542.63  | 95,659.98    | 15,349.81    | 3,000.00     | 0.00        | 0.00       | 0.00       |
|                                |  | 239,436.83 | 352,357.91   | 304,694.80   | 287,212.92   | 134,628.84  | 127,031.62 | 87,559.24  |
| Net Liquidity Gap              |  | 10,127.96  | (102,477.11) | (158,024.03) | (108,087.04) | 333,741.14  | 77,099.30  | 110,444.26 |
| Net Gap as % of Total Outflows |  | 4.23       | (29.08)      | (51.86)      | (37.63)      | 247.90      | 60.69      | 126.14     |
| Cumulative Gap                 |  | 10,127.96  | (92,349.15)  | (250,373.18) | (358,460.22) | (24,719.07) | 52,380.22  | 162,824.48 |

#### Notes

- 1) The above figures have been prepared including interest cash flows and may differ from SLFRS figures given in the Statement of Financial Position
- 2) Prepared as per the requirements given in the Banking Act Direction No 7 of 2011 on "Integrated Risk Management Framework".

### TEMPLATE 14 - SECTION III LIQUIDITY RISK - KEY LIQUIDITY RATIOS

| Ratio                                   | Jan-21  | Feb-21  | Mar-21  | Apr-21  | May-21  | Jun-21  | Jul-21  | Aug-21  | Sep-21  | Oct-21  | Nov-21  | Dec-21  |
|---|---------|---------|---------|---------|---------|---------|---------|---------|---------|---------|---------|---------|
| SLAR                                    | 39.99%  | 39.72%  | 39.89%  | 40.05%  | 40.71%  | 40.38%  | 37.45%  | 36.17%  | 32.88%  | 29.54%  | 29.12%  | 28.02%  |
| LCR (For LKR)                           | 293.25% | 312.85% | 306.91% | 328.28% | 312.42% | 287.61% | 291.07% | 314.39% | 235.27% | 218.22% | 193.13% | 207.99% |
| LCR (For All CCY)                       | 251.88% | 253.79% | 270.82% | 293.99% | 323.04% | 275.75% | 250.78% | 222.20% | 208.72% | 196.21% | 186.66% | 191.38% |
| Net Loans to Total Assets               | 58.23%  | 58.67%  | 58.92%  | 57.35%  | 58.36%  | 59.89%  | 60.08%  | 61.99%  | 63.50%  | 64.15%  | 64.97%  | 64.99%  |
| Loans to Customer Deposits              | 84.94%  | 85.02%  | 83.83%  | 82.01%  | 83.31%  | 83.84%  | 84.16%  | 85.98%  | 87.61%  | 87.72%  | 89.17%  | 89.04%  |
| Liquid Assets to Short Term Liabilities | 93.29%  | 93.06%  | 92.05%  | 95.03%  | 92.87%  | 91.20%  | 90.42%  | 86.59%  | 93.10%  | 80.92%  | 80.33%  | 78.25%  |
| Commitments to Liquid Assets            | 73.58%  | 69.39%  | 68.23%  | 67.08%  | 68.66%  | 70.91%  | 66.39%  | 70.69%  | 61.48%  | 74.38%  | 67.71%  | 68.11%  |
| Commitments to Total Loans              | 48.17%  | 44.75%  | 43.77%  | 46.12%  | 45.23%  | 43.75%  | 40.41%  | 39.47%  | 31.84%  | 37.14%  | 32.89%  | 32.51%  |



# Market Discipline

## -Disclosure Requirements Under Pillar III

### TEMPLATE 14 - SECTION III (B) LIQUIDITY RISK - CURRENCY WISE

#### Report on Liquidity Gap Summary as at 31st Dec 2021 (LKR/ Behavioural)

(Amounts are in Millions LKR)

|   |  | 1M          | 3M          | 6M          | 1Y          | 3Y           | 5Y          | >5Y          |
|---|--|-------------|-------------|-------------|-------------|--------------|-------------|--------------|
| Particulars                             | Product  |             |             |             |             |              |             |              |
| Total Inflows                           | Balances due from Head Office, Affiliates and Own Branches | 0.00        | 0.00        | 0.00        | 0.00        | 0.00         | 0.00        | 3,772.29     |
|   | Bills of Exchange  | 80.80       | 14.16       | 0.00        | 0.00        | 0.00         | 0.00        | 0.00         |
|   | Cash on hand   | 30,245.16   | 0.00        | 0.00        | 195.75      | 0.00         | 0.00        | 0.00         |
|   | Deposits with CBSL   | 1,291.02    | 1,291.02    | 1,291.02    | 2,582.05    | 6,455.12     | 6,455.12    | 6,455.12     |
|   | Investments (Net of provisions)                            | 53,679.04   | 115,890.53  | 1,214.78    | 2,235.97    | 22,850.94    | 15,208.79   | 10,977.42    |
|   | Loans and Advances   | 68,056.99   | 95,196.46   | 105,415.56  | 125,244.25  | 230,982.23   | 118,048.23  | 121,520.04   |
|   | NPLs   | 0.86        | 0.86        | 0.00        | 1,342.65    | 0.00         | 0.00        | 4,027.95     |
|   | Net Inter-Branch Transactions                              | 0.00        | 0.00        | 0.00        | 0.00        | 0.00         | 0.00        | 0.14         |
|   | Other Assets   | 1,050.29    | 1,697.40    | 60.06       | 7,139.33    | 0.00         | 0.00        | 10,297.00    |
|   | Other  | 0.00        | 0.00        | 606.90      | 1,213.97    | 0.00         | 0.00        | 0.00         |
|   | Overdraft  | 8,113.80    | 9,327.42    | 10,058.36   | 19,676.78   | 34,128.85    | 28,980.80   | 23,933.03    |
|   | Accrued Interest   | 2,190.08    | 467.04      | 534.11      | 736.40      | 119.05       | 0.41        | 0.67         |
|   | Balances due from Other Banks                              | 0.00        | 0.00        | 0.00        | 0.00        | 0.00         | 0.00        | 0.00         |
|   | Fixed Assets L1  | 0.00        | 0.00        | 0.00        | 0.00        | 0.00         | 0.00        | 26,849.31    |
|   | Forward Contracts  | 2,429.40    | 6,844.86    | 366.80      | 610.44      | 0.00         | 0.00        | 0.00         |
|   | Reverse Repo   | 0.00        | 0.00        | 0.00        | 0.00        | 0.00         | 0.00        | 0.00         |
|   |  | 167,137.45  | 230,729.75  | 119,547.59  | 160,977.58  | 294,536.19   | 168,693.36  | 207,832.97   |
| Total Outflows                          | Balances due to Other Banks                                | 0.00        | 0.00        | 0.00        | 0.00        | 0.00         | 0.00        | 629.90       |
|   | Bills Payable  | 1,589.31    | 0.00        | 0.00        | 0.00        | 0.00         | 0.00        | 0.00         |
|   | Demand Deposits  | 13,680.04   | 13,680.04   | 10,260.03   | 13,680.03   | 15.77        | 15.77       | 17,110.55    |
|   | Interest Payable   | 1,937.40    | 2,519.22    | 2,760.35    | 2,940.58    | 3,913.74     | 143.36      | 0.09         |
|   | Letters of Credit/Guarantees/ Acceptances                  | 0.00        | 606.90      | 606.90      | 607.08      | 0.00         | 0.00        | 0.00         |
|   | Other Liabilities  | 172.21      | 0.00        | 210.72      | 6,280.11    | 20,245.70    | 3,034.45    | 9,054.41     |
|   | Savings Deposits   | 21,853.73   | 22,512.56   | 17,896.93   | 25,003.59   | 91,509.03    | 86,361.69   | 81,316.64    |
|   | Time Deposits  | 60,892.30   | 115,367.22  | 106,609.71  | 161,393.64  | 29,933.36    | 4,690.49    | 29.19        |
|   | Bonds Issued   | 0.00        | 0.00        | 120.72      | 1,520.51    | 12,983.02    | 13,232.86   | 12,970.46    |
|   | Borrowings   | 709.44      | 896.63      | 545.85      | 1,990.31    | 4,142.83     | 2,786.44    | 114.34       |
|   | Capital  | 0.00        | 0.00        | 0.00        | 0.00        | 0.00         | 0.00        | 37,028.29    |
|   | Forward Contracts Payable                                  | 10,443.76   | 5,521.00    | 1,315.43    | 602.94      | 0.00         | 0.00        | 0.00         |
|   | Repo   | 31,981.82   | 1,368.39    | 205.77      | 17.76       | 0.00         | 0.00        | 0.00         |
|   | Reserves   | 0.00        | 0.00        | 0.00        | 0.00        | 0.00         | 0.00        | 154,555.39   |
|   |  | 143,260.00  | 162,471.96  | 140,532.40  | 214,036.54  | 162,743.45   | 110,265.06  | 312,809.26   |
| Net Liquidity Gap                       |  | 23,877.45   | 68,257.80   | (20,984.81) | (53,058.95) | 131,792.74   | 58,428.29   | (104,976.29) |
| Net Gap as % of Total Outflows          |  | 16.67       | 42.01       | -14.93      | -24.79      | 80.98        | 52.99       | -33.56       |
| Cumulative Gap                          |  | 23,877.45   | 92,135.24   | 71,150.43   | 18,091.48   | 149,884.21   | 208,312.51  | 103,336.22   |
| Adjustments for Behavioural Maturities  | Time Deposits  | 50,336.72   | 93,030.79   | 73,010.68   | 103,008.48  | (140,847.09) | (87,832.85) | (90,706.74)  |
|   | Unutilised O/D   | (13,640.90) | (13,640.90) | (13,640.90) | (27,281.80) |              |             |              |
|   | Undisbursed Loans  | (2,601.54)  | (2,601.54)  | (2,601.54)  | (5,203.09)  | (4,335.90)   |             |              |
|   | Pawning Rollovers  | (369.46)    | (956.28)    | (1,370.95)  | (9,119.83)  | 11,816.51    |             |              |
| Total Adjustments                       |  | 33,724.82   | 75,832.07   | 55,397.28   | 61,403.77   | (133,366.48) | (87,832.85) | (90,706.74)  |
| Adjusted Net Liquidity Gap              |  | 57,602.27   | 144,089.87  | 34,412.47   | 8,344.82    | (1,573.74)   | (29,404.56) | (195,683.02) |
| Adjusted Net Gap as % of Total Outflows |  | 52.59       | 166.31      | 40.42       | 5.47        | (0.53)       | (14.84)     | (48.49)      |
| Adjusted Cumulative Gap                 |  | 57,602.27   | 201,692.13  | 236,104.60  | 244,449.42  | 242,875.68   | 213,471.12  | 17,788.10    |

#### Notes

- 1) The above figures have been prepared including interest cash flows and may differ from SLFRS figures given in the Statement of Financial Position
- 2) Prepared as per the requirements given in the Banking Act Direction No 7 of 2011 on "Integrated Risk Management Framework"

## TEMPLATE 14 - SECTION III (B) LIQUIDITY RISK - CURRENCY WISE

### Report on Liquidity Gap Summary as at 31st Dec 2021 (USD/ Behavioural)

(Amounts are in Thousands USD)

| Particulars                             | Product                                      | 1M         | 3M         | 6M         | 1Y         | 3Y           | 5Y           | >5Y          |
|---|--|------------|------------|------------|------------|--------------|--------------|--------------|
| Total Inflows                           | Bills of Exchange                            | 2,827.55   | 1,835.75   | 55.91      | 0.00       | 0.00         | 0.00         | 0.00         |
|   | Cash on hand                                 | 1,976.59   | 0.00       | 0.00       | 0.00       | 0.00         | 0.00         | 0.00         |
|   | Investments (Net of provisions)              | 94,162.49  | 121,091.48 | 29,255.72  | 113,639.10 | 348,056.64   | 138,543.81   | 75,706.23    |
|   | Loans and Advances                           | 28,593.99  | 58,555.21  | 92,545.94  | 45,835.09  | 113,673.40   | 61,728.46    | 72,399.69    |
|   | NPLs   | 0.00       | 0.00       | 0.00       | 5,185.18   | 0.00         | 0.00         | 15,555.55    |
|   | Other Assets                                 | 917.17     | 1,698.14   | 0.00       | 0.00       | 0.00         | 0.00         | 0.00         |
|   | Other  | 0.00       | 0.00       | 2,499.62   | 4,999.99   | 0.00         | 0.00         | 0.00         |
|   | Overdraft                                    | 946.94     | 1,021.31   | 1,074.39   | 2,102.19   | 3,395.45     | 3,028.72     | 2,670.36     |
|   | Accrued Interest                             | 506.71     | 169.82     | 459.05     | 214.91     | 110.14       | 0.00         | 0.00         |
|   | Balances due from Other Banks                | 0.00       | 0.00       | 0.00       | 0.00       | 0.00         | 0.00         | 32,857.46    |
| Forward Contracts                       | 49,059.79                                    | 26,121.86  | 7,692.10   | 3,000.00   | 0.00       | 0.00         | 0.00         |              |
|   |  | 178,991.22 | 210,493.57 | 133,582.73 | 174,976.45 | 465,235.63   | 203,301.00   | 199,189.29   |
| Total Outflows                          | Balances due to Other Banks                  | 2,512.15   | 16,143.90  | 32,643.11  | 5,297.62   | 24,548.91    | 40,259.24    | 14,191.04    |
|   | Demand Deposits                              | 4,862.78   | 4,862.79   | 3,647.07   | 4,862.70   | 209.07       | 209.06       | 6,217.82     |
|   | Interest Payable                             | 2,250.85   | 5,417.77   | 6,224.95   | 3,010.43   | 2,884.32     | 519.66       | 0.00         |
|   | Letters of Credit/Guarantees/<br>Acceptances | 0.00       | 2,508.75   | 2,508.75   | 2,509.50   | 0.00         | 0.00         | 0.00         |
|   | Other Liabilities                            | 332.34     | 418.07     | 363.22     | 3,050.71   | 1,245.79     | 1,245.76     | 16,436.84    |
|   | Savings Deposits                             | 14,822.11  | 15,116.01  | 11,784.05  | 16,214.16  | 59,820.51    | 57,532.06    | 55,289.46    |
|   | Time Deposits                                | 116,536.22 | 192,074.91 | 204,356.95 | 209,432.37 | 34,711.13    | 16,854.71    | 0.00         |
|   | Forward Contracts Payable                    | 86,323.25  | 68,855.05  | 12,153.10  | 3,000.00   | 0.00         | 0.00         | 0.00         |
|   |  | 227,639.72 | 305,397.25 | 273,681.20 | 247,377.50 | 123,419.72   | 116,620.50   | 92,135.16    |
| Net Liquidity Gap                       |  | (48,648)   | (94,904)   | (140,098)  | (72,401)   | 341,816      | 86,680       | 107,054      |
| Net Gap as % of Total Outflows          |  | (21.37)    | (31.08)    | (51.19)    | (29.27)    | 276.95       | 74.33        | 116.19       |
| Cumulative Gap                          |  | (48,648)   | (143,552)  | (283,651)  | (356,052)  | (14,236)     | 72,445       | 179,499      |
| Adjustments for Behavioral Maturities   | Time Deposits                                | 99,477.57  | 155,977.47 | 150,058.22 | 115,077.31 | (241,283.70) | (132,670.39) | (146,636.49) |
|   | Unutilised O/D                               | (930.75)   | (930.75)   | (930.75)   | (1,861.49) |              |              |              |
|   | Undisbursed Loans                            | (609.28)   | (609.28)   | (609.28)   | (1,218.56) | (1,015.47)   |              |              |
| Total Adjustments                       |  | 97,937.55  | 154,437.45 | 148,518.20 | 111,997.26 | (242,299.16) | (132,670.39) | (146,636.49) |
| Adjusted Net Liquidity Gap              |  | 49,289.05  | 59,533.77  | 8,419.73   | 39,596.21  | 99,516.75    | (45,989.89)  | (39,582.36)  |
| Adjusted Net Gap as % of Total Outflows |  | 38.00      | 39.44      | 6.73       | 29.25      | 27.21        | (18.45)      | (16.58)      |
| Adjusted Cumulative Gap                 |  | 49,289.05  | 108,822.82 | 117,242.55 | 156,838.75 | 256,355.50   | 210,365.61   | 170,783.24   |

#### Notes

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- 2) Prepared as per the requirements given in the Banking Act Direction No 7 of 2011 on "Integrated Risk Management Framework"

# Market Discipline

## -Disclosure Requirements Under Pillar III

### TEMPLATE 14 - SECTION (V) INTEREST RATE RISK IN THE BANKING BOOK (IRBB)

#### Present Market Value of RSA/RSL on Movement of Market Interest Rates - LKR

(Amounts are in Millions LKR)

|   | 1M         | 3M         | 6M          | 1Y          | 3Y         | 5Y          | >5Y          |
|---|------------|------------|-------------|-------------|------------|-------------|--------------|
| Rate Sensitive Assets total                                 | 435,790.54 | 176,862.66 | 65,281.16   | 94,100.65   | 129,446.29 | 70,375.01   | 88,493.34    |
| Rate Sensitive Liabilities total                            | 115,911.90 | 159,969.64 | 118,946.66  | 182,758.12  | 132,810.23 | 89,777.70   | 243,463.90   |
| Net Gap   | 319,878.64 | 16,893.02  | (53,665.49) | (88,657.48) | (3,363.94) | (19,402.69) | (154,970.56) |
| Cumulative Gap  | 319,878.64 | 336,771.66 | 283,106.16  | 194,448.69  | 191,084.74 | 171,682.06  | 16,711.50    |
| Duration weight   | 0.08       | 0.25       | 0.50        | 1.00        | 3.00       | 5.00        | 30.00        |
| Market Rates  | 7.08       | 9.07       | 9.26        | 9.16        | 10.61      | 11.84       | 13.06        |
| Present Value at market rates                               | 318,060    | 16,530     | 51,342      | 81,221      | 2,486      | 11,086      | 3,904        |
| Present Value at market rates + 50 basis pt                 | 317,936    | 16,512     | 51,225      | 80,851      | 2,452      | 10,842      | 3,420        |
| Change in Market value for 50 basis point interest movement | (123)      | (19)       | (117)       | (370)       | (33)       | (245)       | (484)        |

#### Present Market Value of RSA/RSL on Movement of Market Interest Rates - USD

(Amounts are in Thousands USD)

|   | 1M         | 3M         | 6M          | 1Y          | 3Y         | 5Y         | >5Y        |
|---|------------|------------|-------------|-------------|------------|------------|------------|
| Rate Sensitive Assets total                                 | 343,353.34 | 249,184.86 | 76,376.41   | 103,444.54  | 306,640.30 | 118,269.61 | 102,069.62 |
| Rate Sensitive Liabilities total                            | 133,556.24 | 229,299.91 | 306,445.96  | 219,303.81  | 87,099.19  | 69,280.45  | 70,830.06  |
| Net Gap   | 209,797.10 | 19,884.94  | -230,069.55 | -115,859.27 | 219,541.11 | 48,989.16  | 31,239.56  |
| Cumulative Gap  | 209,797.10 | 229,682.04 | -387.51     | -116,246.78 | 103,294.33 | 152,283.48 | 183,523.04 |
| Duration weight   | 0.08       | 0.25       | 0.5         | 1           | 3          | 5          | 10         |
| Market Rates  | 0.10425    | 0.22375    | 0.35438     | 0.586       | 1.183      | 1.379      | 1.613      |
| Present Value at market rates                               | 209,779    | 19,874     | 229,663     | 115,184     | 211,930    | 45,747     | 26,620     |
| Present Value at market rates + 10 basis pt                 | 209,761    | 19,869     | 229,549     | 115,070     | 211,303    | 45,522     | 26,360     |
| Change in Market value for 10 basis point interest movement | (17)       | (5)        | (114)       | (114)       | (627)      | (225)      | (261)      |

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