Driven by a new vision and guided by a new mission, we set out to achieve certain corporate goals. We are happy to report that we have not merely succeeded in achieving our objectives, but we have surpassed every parameter we had set out to fulfill during our growth process. Receiving the prestigious Bracken Award for the “Sri Lankan Bank of the Year 2006” by globally acclaimed “The Banker” publication is considered a landmark achievement, reflecting the commitment and passion of our team to settle for nothing less than the best.

We look back upon the year with positive satisfaction, knowing that we worked tirelessly as a team to drive our Bank to the topmost echelons in the industry. Our achievements, we dedicate to the outstanding HNB team, who will continue to power the Bank’s progress into the future.
HNB, today, stands as Sri Lanka’s premier private sector Bank. An acknowledged leader as the Bank of the Year 2006, we reflect the quintessence of being ‘truly Sri Lankan’. Our ethos espouses unity in diversity and we revel in our ability to formulate and fortify relationships across communities using the strengths of a gamut of financial products and service solutions that encompass the entire nation and beyond. The strong branding depicted via the three robust letters of ‘HNB’ captures the spirit behind every smile in Sri Lanka and the portfolio of offerings that HNB has to offer to every single Sri Lankan or global customer who singles out HNB as their partner in progress.

The Hatna Team has for long been an integral link in the continuous chain of relationships. Through the relationships they have nurtured with our customers, they have built a strong foundation of trust, loyalty and long standing commitment that forms an umbrella of brands and services to touch, cherish and foster interaction.

HNB’s strategic intent is emblazoned through its vision. We intend our growth path to be etched with pioneering endeavours and leadership initiatives that increase stakeholder value. Our growth will be sustainable, innovative and focused. We will seek opportunities to grow, organically or through collaboration, but all the while strengthening our presence, creating financial landscapes and working towards our vision of being the acknowledged leader and chosen partner in providing financial solutions through inspired people.
FINANCIAL HIGHLIGHTS

<table>
<thead>
<tr>
<th>Results for the year</th>
<th>2006</th>
<th>2005</th>
<th>Change</th>
</tr>
</thead>
<tbody>
<tr>
<td>Income</td>
<td>21,513,173</td>
<td>16,915,314</td>
<td>+ 27.18</td>
</tr>
<tr>
<td>Net profit before income tax</td>
<td>3,019,450</td>
<td>1,849,962</td>
<td>+ 63.22</td>
</tr>
<tr>
<td>Income on profits</td>
<td>738,961</td>
<td>195,400</td>
<td>+ 308.88</td>
</tr>
<tr>
<td>Net profit after taxation</td>
<td>2,220,489</td>
<td>1,654,562</td>
<td>+ 34.20</td>
</tr>
<tr>
<td>Gross dividends</td>
<td>588,824</td>
<td>471,058</td>
<td>+ 25.00</td>
</tr>
<tr>
<td>Profit available after appropriation</td>
<td>1,631,665</td>
<td>1,183,504</td>
<td>+ 37.87</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>At the year end</th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Shareholders’ funds</td>
<td>12,929,808</td>
<td>11,239,260</td>
<td>+ 15.04</td>
</tr>
<tr>
<td>(Capital and Reserves)</td>
<td>147,882,025</td>
<td>128,283,681</td>
<td>+ 15.28</td>
</tr>
<tr>
<td>Deposits from customers</td>
<td>128,171,701</td>
<td>107,133,793</td>
<td>+ 19.64</td>
</tr>
<tr>
<td>Advances to customers including Leasing and Bills of Exchange</td>
<td>196,429,028</td>
<td>166,012,410</td>
<td>+ 18.32</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Information per ordinary share</th>
<th>2006</th>
<th>2005</th>
<th>Change</th>
</tr>
</thead>
<tbody>
<tr>
<td>Earnings(Rs.)</td>
<td>18.86</td>
<td>15.09</td>
<td>+ 24.98</td>
</tr>
<tr>
<td>Dividends(Rs.)</td>
<td>5.00</td>
<td>4.00</td>
<td>+ 25.00</td>
</tr>
<tr>
<td>Dividend Yield (%)</td>
<td>3.21</td>
<td>3.56</td>
<td>- 9.83</td>
</tr>
<tr>
<td>Net Asset Value (Rs.)</td>
<td>169.79</td>
<td>95.44</td>
<td>+ 15.04</td>
</tr>
<tr>
<td>Market Value (Rs.) - Voting</td>
<td>155.75</td>
<td>112.50</td>
<td>+ 38.44</td>
</tr>
<tr>
<td>Market Value (Rs.) - Non Voting</td>
<td>70.00</td>
<td>41.50</td>
<td>+ 68.67</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Ratios</th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Return on average shareholders’ funds (%)</td>
<td>18.37</td>
<td>16.31</td>
<td>+ 12.63</td>
</tr>
<tr>
<td>Price earning (Times)</td>
<td>8.26</td>
<td>7.46</td>
<td>+ 10.72</td>
</tr>
<tr>
<td>Dividend cover (Times)</td>
<td>3.77</td>
<td>3.51</td>
<td>+ 7.40</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Capital Adequacy ratios</th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Tier 1 (%)</td>
<td>10.23</td>
<td>10.87</td>
<td>- 5.89</td>
</tr>
<tr>
<td>Tier 1 &amp; 2 (%)</td>
<td>11.32</td>
<td>11.55</td>
<td>- 1.99</td>
</tr>
</tbody>
</table>

GROWTH IN ADVANCES

GROWTH IN DEPOSITS

GROWTH IN PROFITS
OPERATING HIGHLIGHTS

- Growth of Deposits by 15%
- Growth of Advances by 20%
- ROA improved by 18%
- Pre Tax Profit with 63% increase over 2005
- Post Tax Profit with 34% increase over 2005
- NPA ratio with 16% improvement over 2005
- Provision Cover 74%
- Market Capitalisation with 38% increase over 2005

FINANCIAL GOALS / PERFORMANCE

For the year ended 31st December 2006

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Return on average assets (%)</td>
<td>over 1.5 %</td>
<td>1.2%</td>
<td>1.0%</td>
<td>0.7%</td>
<td>0.8%</td>
<td>0.6%</td>
</tr>
<tr>
<td>Return on average shareholders' funds</td>
<td>over 20 %</td>
<td>18.4%</td>
<td>16.3%</td>
<td>12.2%</td>
<td>15.2%</td>
<td>9.8%</td>
</tr>
<tr>
<td>Cost/Net income ratio (1)</td>
<td>65%</td>
<td>66.1%</td>
<td>62.3%</td>
<td>70.4%</td>
<td>63.2%</td>
<td>72.8%</td>
</tr>
<tr>
<td>Dividend rate</td>
<td>30%</td>
<td>50%</td>
<td>40%</td>
<td>35%</td>
<td>40%</td>
<td>30%</td>
</tr>
<tr>
<td>Capital Adequacy</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Tier 1 Capital ratio</td>
<td>9.00%</td>
<td>10.23%</td>
<td>10.87%</td>
<td>9.83%</td>
<td>8.06%</td>
<td>9.98%</td>
</tr>
<tr>
<td>Total Capital ratio</td>
<td>12.50%</td>
<td>11.32%</td>
<td>11.55%</td>
<td>11.26%</td>
<td>11.47%</td>
<td>12.40%</td>
</tr>
</tbody>
</table>

(1) Operating expenses as a percentage of net income.

Operating expenses consist of staff costs, premises costs, financial VAT and establishment expenses and other overhead expenses.

Net income consist of net interest income, foreign exchange income, commission income, dividend income and other income.
Dear Shareholder,

It is my pleasure to welcome you to the thirty eighth Annual General Meeting of Hatton National Bank and present the Annual Report which gives a comprehensive review of the year 2006.

The year 2006 saw the Bank performing exceptionally well with all the financial indicators displaying healthy growth and exceeding the targets. HNB has from its inception recognised the importance of serving all segments of the population and placed emphasis on providing financial services to the rural sectors in addition to their core business of commercial banking. With the present Government’s declared policy of promoting the rural economy, in particular areas outside the Western Province, the Bank was able to make good use of its well spread branch network to complete the year with excellent results. In tandem, we also carried out several exercises to meet community needs under our well-focused policy of fulfilling corporate social responsibility.

In view of the encouraging results amidst difficult conditions, the Board recommends a final dividend of Rs 2.50 per ordinary share, making the total dividend for the financial year Rs 5.00 per ordinary share. Total dividend payout for 2006 will be Rs 589 million, reflecting a growth of 25% over 2005. Furthermore, the Board also recommends a scrip issue on the basis of one ordinary share for every ordinary share on the existing share capital, for your approval. More information on the performance indicators are detailed in the MD/CEO’s Assessment of the Year, Management Discussion & Analysis and in the Statement of Accounts found later on, in this Annual Report.

The global economy and its influence

Despite oil prices topping US $75 a barrel during the year, world GDP growth is estimated to have strengthened in 2006, coming in at 3.9 percent, compared with 3.5 percent in 2005. This strong global performance reflects the very rapid expansion in developing economies, which grew by 7.0 percent. Overall, 38 percent of the increase in global output originated in developing countries, far exceeding their 22 percent share in world GDP. Developing countries are expected to continue this faster growth trend in the next two decades which will eventually see their share of world output rise to about 31 percent by 2030. China contributed immensely to world GDP, growing at a rapid 10.4 percent and contributing 0.5 percent to global growth, while world industrial production also grew at an average of 6.7 percent.

However, there are some inflationary trends that have emerged over the last year with high oil prices and the rapid pace of global growth contributing to a gradual increase in median inflation among developing countries, while contrastingly, inflation in high income countries saw a decline post October 2006 due to reducing oil prices. In many developing countries, inflation first picked up in response to higher oil prices, but has since declined, reflecting both solid productivity growth and the impact of more credible monetary policies that have helped anchor inflation expectations.

Several years of loose monetary policy, an ample supply of global savings, business-sector consolidation in the United States and Asia and high savings rates in the fastest-growing sectors of the world economy have combined to buoy global liquidity which has translated into financial conditions for developing countries remaining favourable, despite high short term interest rates. It is estimated that high-income liquidity exceeds historical norms by between 15 and 17 percent and although interest rates are projected to increase, liquidity is estimated to remain relatively abundant and be a crucial factor behind strong developing-country growth. The Chinese and Indian economies seem to be getting more strident each year, showing signs of becoming certain economic giants and surpassing the US, which has for long held the position of being the benchmark of the world economy. The West, meanwhile continues to struggle with the protracted Iraq war, especially the US which has seen its economic indicators slide. With vast amounts of resources being channeled towards the Iraq war by the US, it can be perceived that the US's
unwarranted interference in the Middle East has taken a heavy
toll on its economy.

GDP in the South Asian region has expanded at rapid pace settling
in at 8.2 percent and attributed to progress in promoting private
sector led growth, improved macro management and greater
integration. Astute fiscal policies and strong remittance inflows also played
a role in boosting domestic demand, while the re-imposition of restrictions on
Chinese exports of textiles and clothing, combined with strong external demand
kept export growth strong. But inflation within the region continued to rise due to an
excess of demand over supply which resulted in net exports actually contributing to a reduction of 1.7 percent in
GDP growth. Strong remittance inflows have supported the growth trend in the region especially in post tsunami
Sri Lanka. The largest economy in the region, India, expanded 8.7 percent with non-agricultural growth exceeding
10 percent. An improved business climate and increased savings have augmented higher investment rates to help
sustain stronger growth.

Economic outlook
It has been a year that has seen Sri Lanka and the world undergo numerous challenges, where political and
economic instability has had definite impact on nations, people and development. The US involvement in Iraq has
seen the world change and become even more polarized. The cascading effect of the Iraqi war had heavy impact
on aid allocations by donor agencies to developing countries like ours as was reflected in the tsunami donor funds,
which though pledged initially were dismally lacking in realization. The world’s priorities changed and Sri Lanka
and other developing countries were left to manage the best we could. Another concern is that a large percentage
of the resources that should be allocated for emerging and developing economies are used quite generously towards
administrative and other expenditure of the very donor agencies that are supposedly distributing these resources to
the developing nations. This, in event, leaves very little of the allocated funds to be distributed for donor purposes.
There is justification therefore, in the argument that NGOs are wasteful and I do believe that even organizations
like the UN do have to re-look at the true objective of their existence and rework their agendas accordingly.

At the same time, in Sri Lanka, our priorities too kept changing. The tsunami reconstruction was carried out but
less emphasis was made on achieving timelines and in garnering and pushing for the promised funding. Instead, a
battle on two fronts has been witnessed – the escalation of fighting in the North and East and fighting economic
battles which are both taking priority. With the Chinese and Indian economies getting stronger, Sri Lanka has had
to cope with the strident impact both these countries have had on our exports and trade. The positive factors
however, are that Sri Lanka continues to be held in favour by both the US and Europe, our biggest trading partners
and in fact, US Ambassador Robert Blake and British High Commissioner Dominick Chilcott have both spoken very
favourably for Sri Lanka at various forums and have vowed to assist in the fight against terrorism, which augurs well
in our global standing. The Sri Lankan government however, must use these signals to its advantage and garner the
support necessary to return to the negotiating table and in tandem, grow the country’s economy using a long term
focus and not one that’s based on political gain.

The deteriorating law and order situation and the sheer indifference to continuous media reports about endless
corruption, particularly in public organizations, is a major cause for concern to all citizens of this country. Those of
us who manage organizations are struggling to cut costs, make transactions more efficient and improve productivity
and it is a very sad scenario to see the imposition of extremely heavy taxes on the very people who continue to drive
the engines of growth and such revenue of the Government drained out on waste and mismanagement, inefficiency and corruption.

For almost three decades, the private sector has performed exceptionally under very trying conditions, contributing to the country's economy in every possible manner despite heavy obstacles mainly due to the ethnic/security problem.

One can well imagine what more benefits could have been accrued to the country, for our industry and our organizations if we were able to work in a more peaceful environment. Therefore, it is of utmost importance for every one of us, as well as the political leadership, to ensure that future managers are given an opportunity to manage their organizations in a more peaceful environment.

Sri Lanka’s GDP stands at 7.5 percent at end of the third quarter of 2006, despite the several major challenges that the country faced during the year with spiraling oil prices and the escalation of violence being two primary factors that the country had to deal with. Excluding tea, all other agricultural sectors continued to expand, while the industry sector also increased growth benefiting from the rapid global economic growth and domestic demand. Telecommunications, ports, domestic and international trade and financial services also posed as healthy contributors to the services sector growth. But inflation remains at a high of 19 percent during each of the last two months of the year and core inflation which is directly caused by demand pressures, rising to 15 percent in November 2006.

Savings and investment, both recording upward trends, saw domestic private savings standing at 19.4 percent of GDP, while national savings, which result from increased savings by expatriate Sri Lankans and private sector investment, has also increased considerably. The latter accounts for 87 percent of total investment - an increase of 31.4 percent. More emphasis on infrastructure development, community development and tsunami related construction is believed to have triggered 7.5 percent growth in public sector investment as well.

During the year, the Central Bank of Sri Lanka implemented a number of supervisory and regulatory measures into the banking and financial sector operations in a bid to improve risk management, further efficiency of the financial sector and enhance access to finance. Banks are required to include market risk in the computation of capital adequacy to ensure adequate capitalization designed to meet any adverse fluctuations in market prices and able to weather unanticipated shocks. The Central Bank also drafted and declared a public policy regarding the regulatory framework.

However, while the regulatory framework for banks and financial institutions continues to be stringent, it can be clearly seen that Sri Lanka’s economic black market continues to thrive, which in effect impacts the country’s balance of payment and inflows. This is one important area that the government needs to look at urgently as the taxation net at this point of time, excludes the thriving black economy which can, if brought into the tax net, contribute considerably towards the country’s balance of payment equation.

I also find that commercial banks have to compete on an uneven playing field with the state banks enjoying privileges and political patronage extensively. We do require firm apolitical financial leadership to ensure that the financial services sector is able to achieve full potential, which unfortunately has not materialized thus far. It is imperative that the Central Bank, which is the custodian of the country’s economy must and has to remain unbiased and impartial, taking decisive actions that would aid the growth of this sector rather than work towards stifling the goose that lays the golden eggs. The past year has seen numerous diktats aimed at banks that have not been
conducive to growth but rather been short sighted and repressive. It is imperative that financial leadership must have a more holistic approach to development and growth and not work on a short term agenda that will eventually have repercussions on the entire economy of the country.

**In conclusion**

At Hatton National Bank, we draw from a rich heritage and legacy that has today evolved into an innovative forward thinking institution. Your Bank, whilst perusing exciting growth opportunities and through prudent policies and developing modern soft skills, particularly in marketing, customer segmentation and performance management, continues to drive HNB towards newer and broader horizons.

**Appreciation**

I would like to take this opportunity to thank my fellow Directors who have given me their unstinted co-operation and support. The Management and staff worked tirelessly to post encouraging results despite unsettled conditions in the country.

I take this opportunity to thank all members of the Management and staff for a job well done.

None of this would be possible if we did not have a loyal clientele who continued to be with us despite strong pressure from our competitors.

I take this opportunity to thank His Excellency the President and Minister of Finance Mahinda Rajapakse and officials at his Ministry and the Governor of the Central Bank of Sri Lanka, Ajith Nivard Cabraal and his officials for their guidance and continued support during 2006. Finally, I would like to thank all shareholders for the trust and confidence they place in our Bank.

On behalf of the Board of Directors, I wish to pledge that we will continue to add to shareholder wealth through prudent and carefully planned business strategies.

Rienzie T Wijetilleke

*February 15th, 2007*

*Colombo, Sri Lanka*
A new vision, mission and values signaled a renaissance for the Bank this year. Having implemented strategies to meet the challenges we had faced in the last few years, our genesis into newly defined dimensions to meet the opportunities that will characteristically arise, now that we have re-established ourselves into a premier position within the industry, has clearly seen results even in this short span of one year. The vision, mission and values have redefined our journey and set ambitious albeit achievable goals. The foundation we have laid is certain to etch the lines of growth even further into the coming years, as we strongly believe that HNB is now poised on the threshold of exciting but sustainable growth for the coming years.

Financial overview
The year posted several challenges in the domestic environment with escalation of violence in the North and East of the country, impact of increasing oil prices, spiraling inflation and rising interest rates. Despite this, the Bank has demonstrated its resilience by outperforming several of the internal targets we set ourselves. Hatton National Bank, its subsidiaries and associate companies recorded a Pre tax profit this year of Rs 3,095 million compared to Rs 2,008 million last year, which is a significant growth of 54% in 2006. The Bank alone recorded a Pre tax profit of Rs 3,019 million which is a 63% growth over the previous year.

Working on a paradigm of consistent sustainable growth, net interest income has continued to be the major contributor to the bottom line accounting for 74% of the net income (before operational expenses).

The Sri Lankan Rupee depreciated against the US Dollar by 5.5% during the year to Rs 107.65. This helped HNB in posting an exchange profit of Rs 792 million despite being wary of trading in derivatives and bullion based on a clearly defined strategy established last year.

Commission, dividend and other income reached Rs 2,269 million up by 6.1% compared to the previous year. While the non-funded aspects saw mixed reactions this year, especially in tourism in Sri Lanka, we have been compensated by other sectors including construction. Trading in Fixed Income securities remained at a low due to the volatility in interest rates while the equity trading portfolio contributed Rs 91 million.

We continued the trend shown last year by meeting our entire operating expense bill of Rs 7,733 million from Net interest income, another facet that examples the sustainable growth pattern we are espousing despite signs of unpredictability seen in the local economy. Total operating expenses, including the loan losses and provisions, increased from the previous year’s Rs 7,784 million to Rs 8,677 million which was an increase of 11.5%.

Provision for corporate tax for 2006 was Rs 798.9 million resulting in the after-tax profit recording Rs 2,220 million, an increase of 34% which is pleasing as we think it shows a healthy sustainable outlook for the next few years.

The Group’s assets increased by 18% during the year to Rs 206.9 billion as at 31st December 2006. While the Bank’s asset base of Rs 196.4 billion is one of the largest among private sector commercial banks in Sri Lanka, our emphasis is to retain and grow profitability. Return on Assets (ROA) as at 31st December 2006 was 1.23% which is in line with our medium term goal of exceeding 1.5% and has heralded our qualification for development oriented refinance schemes such as the JBIC (Japan Bank for International Cooperation) funded SMILE III scheme in the SME segment.

Capital adequacy, an issue we addressed two years ago today, stands at a commendable 11.32%. Our goal however is to exceed 12% despite the payout challenges, which looking at our progress we are confident is achievable, giving us the impetus to grow our business. We continue to explore numerous innovative means of raising capital, aptly exampled last year by our ability to raise Rs 1.12 billion in debentures with tenures ranging up to 18 years successfully, a unique proposition in Sri Lanka.
Infusing cost efficiencies

‘Spending wisely and for good value’ remained the axiom upon which we focused our cost consolidation measures. We imbued aggressive cost efficiencies into our operational portfolio in a bid to expeditiously manage our cost/net income ratio which in past years has been one of the highest in the banking industry. Even though expenses have shown an increase of 29% over last year, the aggressive approach we deployed in cost cutting has seen a manageable cost milieu evolve. An important driver has been our focus in controlling our non-performing advances ratio which has decreased by almost 16%. Sound inventory management, waste minimization and building sustainable partnerships with our valued business partners in ensuring level negotiations for long term benefits have seen the aggression in implementing and executing our cost efficiencies which infused the desired positives. Collate these ingredients under the common umbrella of a 4,000 strong team working towards one vision and one focus has seen operating costs (including provisions for bad and doubtful debts) increase by only 11.5%, despite 19% inflation.

Excellent teamwork

Having been somewhat challenged in the past due to lack of astute infrastructure to pursue a bigger market share in retaining our market leadership position, this year the team worked on the single minded focus of identifying and righting weaknesses, recognizing and building on strengths and ascertaining opportunities from a top down and bottom up approach. The commendable growth in bottom line profits of 127% in the last two years, despite a flat head count, showcases the incisive deployment and utilization of resources we have instigated in our restructuring efforts. I am exceptionally proud of Team HNB which has put their shoulder to the wheel in ensuring that the Bank remains aligned to its vision and mission, instilling the ingrained values into our culture so that we can be acknowledged as the leader in our industry.

We infuse best practices in line with world class practices permeated via specifically designed training and development programmes that will meet our goal to be the best. The MaFoi Employee Engagement survey we conducted this year among our Team for the first time has opened communication lines, shown us the paths we should take to bond better and above all, tangibly displayed that the Team shares equal ownership in the future of the Bank. It is also significant that nearly 85% of the team undertook the survey online, which displays the increasing utilization of IT being used as a tool by the Team.

Winning the Bracken Award this year was certainly the single highest honour HNB has been bestowed within the recent past, giving credence to the fact that we have achieved a tenet of our vision in being ‘acknowledged’ by our peers internationally as a leader in the Sri Lankan financial industry. We also passed the Rs 2 billion mark in After-tax profit, for the first time in our history. All this signals the sharp and perceptive workings of a Top Team!

Implementing tools effectively

The commendable recovery seen in our non-performing loan portfolio is a result of an aggressive focused formula which hedged on using good negotiating tools for key recovery efforts that would instigate a win-win milieu for all. The new portfolio in tandem then, is being built on a qualitative platform where strong infrastructure compliments timely forewarning signals that have blended well this year. The risk management unit established just two years ago has now matured to work independently, utilizing the right tools and know how, wherein risk is minimized through an alert cautionary framework in place.
We do expect to use these tools more emphatically in the next year to pursue the SME sector which we believe is a vital cog in the wheel of the nation’s economy but has not received the due recognition or emphasis it should in being a crucial contributor to growth. Given the current national agenda in focusing more on this key area of development, we remain totally committed to grow this segment of the economy in order to make it a sustainable and viable facet in our operations. We have already set in motion plans that will professionalize our delivery methodologies especially in the rural areas, establishing the apt risk management tools and the appropriate human resources and training implements together with the IFC, to build capacity that would showcase the desired deliverables in the SME segment within the next two years. Garnered from the pioneering 15 years experience we have in micro finance, we aim to similarly, vigorously concentrate on micro finance which we perceive has immense potential, professionalizing delivery in order to instigate smart portfolio diversification while delivering an appropriately priced product that ensures bottom line contribution as well.

**Beyond customer expectations**

Customers continue to be the quintessence to our existence, the pivot upon which our success is built upon. We have continued to innovate, create, develop and present customer conveniences that bring banking to the home of the customer, whose profile spans the entire economic and social strata of the country. Acknowledged as the most powerful brand in the financial services sector in Sri Lanka in a survey conducted in LMD by Sting Consultants, our brand remains at top of the mind recall among the people of this country which underscores the strong bonding we continue to maintain with our customers and valued business partners. We also conducted a customer engagement survey through AC Nielson and continuously conduct sub surveys on a regular basis to be atop customer expectations. The findings stress the need for continued improvement and allow us to set our goals beyond industry benchmarks.

A technology revolution has also taken place at HNB where customer convenience deliveries have undergone a facelift. SMS banking with Mobitel and Lanka Bell coupled with a host of account related conveniences was launched with more rollouts expected through other telecommunication service providers in the next year and a Virtual Branch has been introduced enabling transactions 24/7 all year around, anytime, anyplace, anywhere in the world. These are two of the most significant achievements this year in implementing our IT convenience platform for our personal banking portfolio.

Remittances also showed immense progress this year, a significant contributor to the foreign exchange coffers of the economy. Positioning ourselves with a mix of international channel partners in strategic countries mainly in the Middle East and signing up with Italy and the UK this year, complimented by HNB Team members also placed in four locations for noteworthy value addition into our operations, we have significantly captured 35% of the remittance business. This global focus will be strengthened to other markets that house a considerable Sri Lankan diaspora spreading into other countries in the Middle East and Canada and Australia as well.

**To exceed in compliance**

Going beyond compliance remains a priority when in governance and the structure that enfolds it. As we have progressed according to guidelines laid down by the Institute of Chartered Accountants of Sri Lanka, the Central Bank of Sri Lanka and ACCA UK as well as other statutory bodies both in Sri Lanka and internationally, I do believe that the HNB internal governance structure has improved tremendously in the last few years. This is due to the strong foundation built on the philosophy that success at business must not be at the expense of governance, but rather be achieved by retaining integrity, values, ethics and exceeding compliance at all times. The multi-skilled composition of the Board of Directors has ensured that the independent structure of the Board is maintained, while the clearly defined roles of the Chairman and the Managing Director/CEO assist in preserving and maintaining policy, strategy and operational features autonomously.

**Macro industry perspectives**

The 2007 Budget proposed two new pieces of legislation which will have a depressing impact on the banking industry. Firstly, banks which do not meet the ‘deemed dividend payout’ of 25% of distributable profits will have to pay an additional 15% on the difference between deemed dividend payout and the actual dividend paid. This obviously has not considered the regulatory obligation on licensed commercial banks to maintain a minimum level of capital to support its growth and normal business which is invariably financed by retained profits after-tax. Secondly, banks will have to limit the deduction of Specific Loan Loss Provision from Taxable Profits to a mere 1%
of the total loan portfolio. This proposal appears to be counter-productive, since such restriction would discourage prudent banks from making provisions in excess of the minimum regulatory requirements. We have made representations to the Secretary of Treasury through the Sri Lanka Banks Association, to reconsider the proposals with some amendments reflecting the above concerns. The recent direction by the Central Bank of Sri Lanka requiring commercial banks to "build up" a General Provision of a further 1% of performing and overdue portfolios over a period of ten quarters, certainly runs counter to Sri Lanka’s journey towards adopting the set of International Financial Reporting Standards (IFRS) which fundamentally frowns upon the creation of General Reserves.

The taxation thresholds in Sri Lanka remain high, especially for the banking industry. We firmly believe that by almost unfairly imposing a very stringent taxation regime for the very engine of growth that is one of Sri Lanka’s best performing sectors from an investor’s view point, the immense potential the industry has in enticing investment will continue to dim. What we see unfortunately, is a compromise of long term benefits for short term gains, which should be re-strategized if the country hopes to leverage on the investment potential that the financial industry possesses.

We also firmly believe that consolidation and convergence must and has to be deployed and encouraged in enhancing HNB’s presence as a regional and a global player. There has to be clear articulation between restricting ownership in a business sense and managing fears in terms of ownership concentration, through the infusion of good governance structures and monitoring. The right to buy and sell should be market driven in order to develop the much maligned capital market. Sri Lanka does not yet sport large banks akin to those in India or Pakistan to be a significant player regionally. Strong banks are important and we must be given the opportunity of being robust and dynamic, being able to introduce ourselves into the big league.

**The future in perspective**

Our new vision, mission and values will undoubtedly take us vibrantly into the next two to three years pointing Team HNB in the direction we must take to regain and consolidate our leadership position, which I must stress, has to be acknowledged by others. Winning the Bracken Award where we excelled in key drivers from among several local and foreign banks operating in Sri Lanka was our first step in getting closer to our vision.

The initiatives taken in extending our reach by increasing our network of branches, constantly improving our delivery and distribution channels, especially with the use of IT, enhancing our products to suit changing mindset, customer profiles and categories and in strengthening Team HNB to exceed stakeholder expectations, continues to remain a priority for us. India will continue to remain an attraction while also a challenge to the local banking industry but we are currently pursuing a number of options in our quest to enter the Indian market.

The focus on compliance with BASEL II will see us investing more in technology to comply with that roadmap and with the Anti-Money Laundering diktat. The Core Banking system, which we feel has reached its full potential but will not from this point onwards add further value to our future direction, will also be revamped with the rollout expected in the first half of 2007.

I would like to extend my appreciation to the Governor of the Central Bank and his staff for their support throughout the year. My deep gratitude to the Chairman and Board of Directors of the Bank for their encouragement and guidance and for giving me the impetus to lead Team HNB to deliver good results. Team HNB continues to be my motivation and I do thank them very sincerely for their unstinted support and co-operation in having the confidence to undertake this journey, driving the momentum for when HNB will once again be acknowledged as the leader in the financial services industry.

Rajendra Theagarajah

February 15th, 2007

Colombo, Sri Lanka
Our Visionaries

CHAIRMAN
MR RIENZIE T WIJETILLEKE
Chairman since March 2004. He was Managing Director & Chief Executive Officer from July 1988 to December 2004 and counts over 46 years in Banking including overseas assignments. He is Chairman of HNB Assurance Limited, HNB Stockbrokers (Pvt) Limited, HNB Securities Limited, Sithma Development (Pvt) Limited, Sunshine Holdings Limited. He is a Director of Colombo Stock Exchange, Nawaloka Hospitals Limited, Ceylon Biscuits Limited.

DEPUTY CHAIRMAN
DR. V P VITTACHI
B.Com. (London), Ph.D.
Director since 1988. He was the past Head of Sri Lanka Customs, past Chairman of several public corporations and past Governing Council Member of the Peradeniya and Moratuwa universities. He is Chairman of Distilleries Company of Sri Lanka Ltd., Lanka Milk Foods (CWE) Ltd., Stassen Group of Companies and Browns Beach Hotels Ltd.

MANAGING DIRECTOR/CHIEF EXECUTIVE OFFICER
MR RAJENDRA THEAGARAJAH
He was appointed Director/General Manager/Chief Executive Officer in December 2004. He was appointed Managing Director/Chief Executive Officer in December 2005. He was a Member of the Corporate Management of HNB since 1997. He counts over 22 years in Banking including overseas assignments. He is a Director of HNB Assurance Ltd., HNB Securities Ltd., HNB Stockbrokers (Pvt) Ltd, Sithma Development (Pvt) Ltd., Lanka Clear (Pvt) Ltd and Lanka Financial Services Bureau Ltd. He is a Board Member of the Asian Banks Association and Sri Lanka Bankers Association. He is also the President of the Association of Professional Bankers in Sri Lanka.

DIRECTOR
MR D H S JAYAWARDENA
Director since 1988. He is Chairman of Sri Lankan Airlines Ltd., the national carrier, Aitken Spence & Co. Ltd., Sri Lanka Insurance Corporation Ltd., Lanka Bell (Pvt) Ltd. and Periceyl (Pvt) Ltd. He is the Managing Director and Chief Executive Officer of Distilleries Company of Sri Lanka Ltd., Lanka Milk Foods (CWE) Ltd., Stassen Group of Companies and the Managing Director of Balangoda Plantations Ltd. and Madulsima Plantations Ltd. He is a Director of Browns Beach Hotels Ltd. and Apollo Hospital (Pvt) Ltd. He is also Consul General for Denmark in Sri Lanka.

DIRECTOR
MR M V THEAGARAJAH
Associated with the Bank since its inception and a Director since 1979, M V Theagarajah retired as Chairman of the Browns Group of Companies on 30th June 2006. He has over 40 years experience in commerce, finance, industry and management.
DIRECTOR
MR R K OBEYESKERE
Director since 1998. He is the Deputy Chairman of Sri Lanka Insurance Corporation Ltd. He is a Director of Stassen Group of Companies, Lanka Milk Foods (CWE) Ltd., Distilleries Company of Sri Lanka Ltd., Madulsima Plantations Ltd., Balangoda Plantations Ltd. and Lanka Dairies (Pvt) Ltd.

DIRECTOR
MRS PAMELA C COORAY LL.B.
Appointed Director in April 2004. She was a past Director of Board of Investment of Sri Lanka and Associated Battery Manufacturers (Ceylon) Ltd.

DIRECTOR
MR RATNA SIVARATNAM (Absent)
Appointed Director in December 2004. He is a Director of Aitken Spence & Co. Ltd., Acme Printing & Packaging Ltd and Lanka Aluminium Industries Ltd. He was past Chairman and Managing Director of Aitken Spence Group of Companies, past Chairman - Employers Federation of Ceylon, Steering Committee of the Airports & Port Development and past Executive Chairman – Sri Lanka Export Development Board. He was past President – Association of Group Tour Agencies, past Vice President – Ceylon Tourist Hotels Association and Travel Agents Association of Sri Lanka. He is the Consul General for Finland in Sri Lanka and an Executive Committee Member – Ceylon Chamber of Commerce.

DIRECTOR
MR RASHID GHAZALLI (Absent)
B.Sc (Econ ) (Banking & Finance) – University of Wales/Institute of Science & Technology, Wales
Appointed Director in September 2005. He is the Chief Executive Officer of MAA Corporate Advisory Sdn Bhd, Malaysia, the investment advisory division of the Melewar Group, Malaysia a conglomerate with core interests in financial and industrial services sector. He has wide experience in financial services industry in Malaysia and overseas. He is a Director of Eversendai Group, Malaysia, a steel engineering group. He held Executive Directorships previously in the Maju Group, Malaysia – a conglomerate with core interests in property development, toll highways, manufacturing steel and trading in building materials.

DIRECTOR ALTERNATE (TO MR R GHAZALLI)
MR YEO TOOK KEAT (Absent)
F.C.C.A
Director – HNB Assurance Ltd. He is Group Chief Operating Officer – MAA Holdings Berhad (MAAH), Malaysia. He is a Director of MAAH from February 2005 and holds several Directorships in the MAAH Group of Companies. He has vast experience in accounting and finance, having served in various capacities in insurance companies and audit firms upon completion of studies in 1980. He is an Executive Committee Member – Federation of Public Listed Companies Berhad and has contributed to the Working Groups on accounting standards led by the Malaysian Accounting Standards Board.

BOARD SECRETARY
MS INDRANI GOONESEKERA
ATTORNEY-AT-LAW & NOTARY PUBLIC
Management Discussion and Analysis
PRODUCTS & SERVICES
Term finance including syndicate loans, Overdraft facilities, Import & Export Finance by way of Letters of Credit, Import/Export loans, Guarantee facilities, Money Market Loans, Commercial Paper, Bonds and other financial instruments.

THE YEAR IN FOCUS
The Bank continued to perform above the forecasted figures due to a number of internal initiatives implemented in order to optimise the synergies within the Bank more strategically. Given that corporate banking is a critical business segment, infusing the principles of being upwardly mobile and working on strategies that would challenge and beat competition, one of the most significant among the change initiatives implemented was the centralization and consolidation of the Treasury, Project Finance and Corporate Banking divisions. In addition, from September 2006, corporate banking functions which were earlier spread out over the branch network, were centralized at the Head Office to ensure a speedier more efficient response time, while the branches operate as distribution units. This has led to strengthening existing relationships and forging potential relationships built on pragmatic tenets being put into place, as maintaining a healthy portfolio that would result in the desired growth within a competitive environment remained critical throughout the year. The significant results were also aided by the upward trend in the economy and the opportunities resultant from it. Agriculture, telecommunication, construction, leisure, health, apparel, manufacturing, finance and offshore banking were the thrust areas that brought in the desired results during the year. The Project Finance Division’s diversified portfolio comprises 35% in FCBBU loans for local BOI projects and overseas investments, with the leisure sector contributing 27%, power and energy 20% and real estate 15% to the portfolio with a total value of Rs 6.65 billion, a growth of 14% from Rs 5.8 billion displayed at 31st December 2005. Loans approved during the year totaled Rs. 1.93 billion with 60% approved for leisure projects in both Sri Lanka and the Maldives, 16% for the real estate sector and 4% for power and energy projects. While 2005 saw more emphasis on mini-hydropower projects due to the availability of refinancing under the World Bank’s RERED Credit Line this year, the sector aggressively pursued the high potential area of offshore leisure projects, approving FCBBU facilities totaling US $ 15.6 million for offshore projects.
Catering to an extensive but qualitative portfolio of corporate and medium to large domestic commercial clientele, the corporate banking sector comprises 41% of the Bank’s total loans and advances.

Having signed the agreement for the EIB credit lines to be extended for tsunami related projects in September this year, we already have about Rs 1.5 billion projects which commenced work this year and need to be worked through to the next.

IN 2007, UPWARD MOBILITY WILL CONTINUE BY...
• Being more aggressive in the thrust industries of off shore leisure, infrastructure, telecommunications, construction and real estate,
• Implementing the projects already earmarked for the e-Friends loans and expanding the EIB credit lines,
• Venturing into Islamic banking,
• Taking advantage of economic growth patterns and investments coming into the country and lobbying for investor friendly policies,
• Continuing to build on the principle of a quality portfolio and being more risk conscious, disciplined and astute in our investment decisions improving asset quality and aggressively reducing our NPAs.
PRODUCTS & SERVICES
Savings Accounts: Pathum Vimana/Pathum Udananaya/Singithi Surakum/Singithi Pathum Minors Savings Scheme/Saubhagya Planned Savings Scheme/Divi Shakthi/Senior Citizen Scheme; Current Accounts: Lifeline/Shareline for HNB Shareholders; Time Deposits: Certificates of Deposit/Term Deposit Accounts; Loan Schemes: Shanthi Housing Loans/Group Consumer Loans/HNB Personal Loans/Dream Drive Vehicle Loans/HNB Graduateship Educational and Career Development Loan scheme. Special Educational loans for CIMA/Danuma Educational loans exclusively for ETF members; Credit Cards: HNB Master card and HNB Visa card. Hot Shot Credit Card for teenagers; Leasing: Lease Master/Finance Leasing/Wasi Leasing/Finance Leasing; Other: Virtual Banking/Teleline Banking/Hatna SMS/Cashline ATM facilities/Safe deposit lockers/HNB Home Care accounts for utility bill payments/money transfer services/insurance/share broking/sale of gold; Pawning Services

THE YEAR IN FOCUS
The year notched good growth with all sectors recording significant upward trends including the Card Centre, home loans, leasing and pawning contributing commendably to the bottom line. Competition has been intense and the challenges immense, which led us to realign our stance and be more astute in our focus, working towards a more qualitative portfolio rather than a volume oriented one.

Promotions for our key products, namely Pathum Vimana, Singithi Pathum, Divi Shakthi, housing loans, leasing, pawning, credit cards and personal loans were stepped up with internal target achievement via a well balanced distribution mix including the island wide branch network. The Pathum Vimana Savings Scheme, home loans, leasing, pawning, credit cards and personal loan segments of our products were revamped during the year to provide more strategic focus to the business in line with the competitive external milieu.

Our most significant innovation this year has been the establishment of the ‘Virtual Branch’. Using the IT platforms that are now available within the global banking industry, as a spin off to the HNB web page, a Virtual Branch was conceptualized, with the aim of taking the comfort of personal banking to the customer’s home. All functions performed within a branch will be infused into the Virtual Branch, showcasing the momentum that HNB has employed in being upwardly mobile this year and unleashing untapped potential in the coming years.

HNB’s continued focus has been to augment and intensify the emphasis on the upward growth curve. Realising that banking in the current context continues to remain a retail oriented one, we have ensured that our products continue to achieve good results, despite very stiff competition within the industry, employing creativity and
innovation to maintain market leadership in most product areas. Our products embrace the concept of a partnership from cradle to twilight years, starting from Singithi which has seen HNB even tie up with the main hospitals in order to instill the savings culture permeating from the parents to a new born, right up to the Senior Citizens Scheme.

Our flagship product, Pathum Vimana, which has mobilized a savings base of Rs 50.7 billion, a growth of 7% compared to Rs 47.4 billion last year, has seen over 8,000 customers rewarded with numerous prizes, including luxury vehicles. Conceptualized to inculcate the savings habit among people, HNB also has 152 school banking units located island wide, mobilized by students themselves, which infuses the positives of a savings culture among students and young people, while at the same time inculcating the rudiments of banking among them. Our minor savings portfolio grew by Rs 400 million this year. A major attraction to the ‘young’ savers has been the gift of the trademark unique elephant till of which HNB has already distributed over 500,000 numbers country wide.

The HNB Five year Fixed Deposit scheme recorded a base of Rs 1.2 billion, a growth of 23% over last year, while the Senior Citizens scheme showed an increase of 154%.

**Branch Network**

HNB continued to increase its presence around the country and beyond, boosting the branch network to 151 customer centers. During the year, five customer centers in Akurana, Peradeniya, Kahawatte, Seeduwa and Hatton were relocated with a view to provide more spacious and convenient banking facilities. Strengthening the distribution channel, this year HNB introduced “Saturday Banking” through 30 customer centres, which saw a significant increase in business and positive customer testimony to the conveniences extended by the Bank.

**Leasing**

The leasing market too has remained extremely competitive. Achieving targets remained a challenge with the market reacting negatively to the volatility and high interest rates regime experienced during the year. Despite this however, leasing achieved an impressive gain, showcasing Rs 6.8 billion in disbursements, an increase of 21% from Rs 5.6 billion last year, while the leasing portfolio showed growth of 30.6% over 2005. Having foreseen the challenges leasing would be up against this year, HNB worked on customized promotions to ensure a positive growth pattern for this segment. The innovative promotions included those conducted with major vehicle agents for the leading brands of Proton, TATA, Eicher, Maruti, Toyota, Kelisa and Mahendra complimented by location based ‘Town Storming’ campaigns.

**Pawning**

Our advantages within the pawning industry lies with the extensive HNB branch network, wherein almost every branch has a dedicated fully equipped Pawning Unit/lobby manned by a professional officer to cater to a broad based clientele segment. Our portfolio was enhanced by about Rs 1 billion despite aggressive competition. We have also seen a marked increase in business in the North and East. Strategic initiatives during the year to reduce the NPA ratio from 5% to about 2% proved to be very successful.

**Shanthi Housing Loans**

One of the high growth areas over the past few years has been the housing loans segment. On average, HNB disbursed 300 loans monthly through the Shanthi Housing Loan scheme, which marked its tenth anniversary this year. Total outstanding advances also grew by 25% over last year. Perceiving the competition however, and in the stance of being upwardly mobile, HNB imbued a number of value additions into the existing scheme including the Second Home Loan and Home Loan Wipe off. The Second Home Loan is available to those customers who have already repaid a substantial portion of their loan and are pursuing the purchase or construction of a second home for residential or rental options.

**HNB Personal Loan Scheme**

The Bank’s Subasiri Personal Loan Scheme, encompassing almost the entire gamut of personal requirements was re-launched towards the latter part of this year with expectations of better results next year. Due to streamlining processes being introduced prior to the re-launch, loans disbursed have not shown any increase during the year.
Credit Card Business
HNB continues to remain a significant player in the Credit Card market, issuing both Mastercard and Visa. The business segment grew impressively by 55% to Rs 265.5 million compared to 26% last year with the total advances portfolio growing by 23%. The majority income is derived from interest and other income recording 33% growth and merchant commission seeing 25% growth.

However, with competition within the industry continuing unabated, HNB constantly infuses value additions to make HNB credit cards more attractive to customers. The value additions this year included the annual discount brochure with offers from over 50 merchant outlets, the 0% instalment scheme for purchase of consumer durables and the introduction of the IDD calling card. The Avurudu Usage Promotion and the 31 days of Christmas promotion were significant contributory factors to the growth of the Bank’s Credit Card advances portfolio. The Bank’s Maldives Acquiring Business also recorded a growth of 54% in profit.

SMS alerts, which aid credit card users immediately on any transactions effected have also gained popularity with a 28% growth in messages sent.

SMS Banking
In August this year, SMS banking using ‘Over the Air’ menu driven solutions, the first of its kind in Sri Lanka, in partnership with Mobitel and Lanka Bell was launched. This allows HNB credit card customers to view balances and settle monthly bills via SMS. The Bank has also tied up with various other service providers to enhance the product scope.

IN 2007, UPWARD MOBILITY WILL CONTINUE BY...
• Relaunching of Pathum Vimana and Pathum Udananaya Savings Schemes with extensive value additions,
• Augmenting the key growth areas of housing, leasing, pawning, development banking and credit card business through value additions and innovations and employing the extensive branch network to deliver speedy solutions efficiently,
• Enhancing virtual banking with four strategically placed kiosks,
• Adding customer centres,
• Introducing extended banking hours and withdrawals via cards,
• Setting ourselves a target to achieve an increase of Rs 1.5 billion in the pawning business augmented by increased promotions and strategic marketing initiatives, while using the upward trend in gold prices to our advantage,
• Pursuing mortgage financing for high value real estate developments through the tri-partite agreement initiated by the Bank,
• Further ingratiating our presence in the housing loan market by adding a home improvement loan scheme,
• Promoting the HNB Personal Loan Scheme extensively vis a vis target mass media communication campaigns,
• Conceptualizing value additions for existing products and innovating newer products including a new savings product, to reach outwards regionally and meet increasing competition in the retail banking sector,
• Improving the existing IT platform used in pawning to deliver enhanced customer service, product diversification and centralized control for accelerated growth; use the advantages prevalent in the high value customer segment of the market for larger pawning facilities to be used for alternate working capital or investment finance,
• Being the most sought after finance lessor in the market.
PRODUCTS & SERVICES
Rural Credit: Tea Development Project (TDP), Second Perennial Crop Development Project Credit Revolving Fund (SPCDPC), New Comprehensive Rural Credit Scheme (NCRC), Coconut Development Project Scheme (Kapruka Avojana), Southern Province Rural Economic Advancement Project (SPREAP), Poverty Alleviation Micro Finance Project (PAMP), Aquatic Resources & Quality Improvement Development Project (ARQIDP); Microfinance: Gami Pubuduwa, German Savings Banks Funded Credit Scheme; SME: SMILE I Revolving, SMILE III, e-Friends II

THE YEAR IN FOCUS
Growth has been seen in all sectors with more emphasis nationwide being made on entrepreneurial ventures and the re-emergence of micro, small and medium sectors as potential contributors to the economy. The financing of rural agricultural activities saw a growth of 28% to Rs 2.65 billion with a loan disbursement portfolio of Rs 1.0 billion. Nearly 40% of the total portfolio is contributed by medium and long term agricultural projects for tea, coconut and perennial crop development.

Gami Pubuduwa, HNB’s successful micro finance programme continued its upward curve, growing by 37%, to disburse Rs 900 million, over 5,000 micro enterprises benefiting about 15,000 families. Conducted on the platform of sustainable development to develop the rural economy of the country, the collective portfolio comprises 15,000 loans amounting to Rs 1.8 billion, with 51% of the portfolio covered by refinance funds and a creditable collection ratio of over 95%. Rs 1.0 billion has also been mobilized as rural deposits through Gami Pubuduwa. With 17 years experience in this segment of the market, HNB uses its strengths to ensure that financed projects are sustainable, aided by 120 trained field officers, some of whom are specialist agricultural executives working throughout the country, including the North and East.

The Bank also became an active participant in the German Savings Bank Funded Credit Scheme (GSBFCS) to facilitate funding to micro enterprises within the tsunami affected areas. Earmarked for disbursement over a period of two years, HNB’s efficient and speedy processes saw the target met within one year. With this success, the Bank signed the Second Agreement for a loan component of Euro 3 million (Rs 390 million approximately) and has already disbursed Rs 220 million to date.

An innovative micro insurance product was launched in partnership with HNB Assurance designed to cover both life and the liability of borrowers in the micro finance sector. This is a pioneering product within the insurance industry in Sri Lanka.
HNB remains emphatic on developing the SME sector seeing the potential of its contribution to the economy. Aiding the funding process, the Bank is currently participating in the e-Friends II Credit Line and SMILE I Revolving Credit Line. As a result of the success seen from SMILE I Revolving Credit Line, which eventually evolved into the SMILE II and III Credit Lines, the SME portfolio has increased by 20%. To be more efficient and speedier in implementing initiatives, we also employed the novel approach of categorizing and sub-segmenting the SME sector in order to be more focused in our mission, whilst also re-energizing the Head Office SME Unit by bringing it under the umbrella of the Development Banking Division.

**IN 2007, UPWARD MOBILITY WILL CONTINUE BY...**
- Speedily and efficiently disbursing the balance loan disbursement of Rs 170 million under GSBFCS ahead of time,
- Increasing our e-Friends II, SMILE III and SMILE I Revolving Loan Disbursement Portfolio by 50%, 10% and 40% respectively,
- Creating more innovative products to add value to our philosophy of sustainable development,
- Continuing to be emphatic about creating an entrepreneurial culture, especially among the rural economy by deploying the necessary resources to achieve growth.
PRODUCTS & SERVICES
The scope of International Operations encompasses Correspondent Banking, Inward Remittances, Issue and Encashment of Travellers Cheques, Foreign Currency Drafts and Currency Notes, Issue of Guarantees on behalf of our Correspondents, International Trade pertaining to imports & exports, Formulation and Reviewing Anti Money Laundering Policy and Know Your Customer Policy, Treasury Back & Middle Office operations and handling of communications between correspondents via SWIFT.

THE YEAR IN FOCUS
During the year 2006, evaluation and analysis of correspondent relationships received priority status with a view to rationalize relationships to build on efficient and cost effective relationships resulting in a saving of around 40% of costs. This is an ongoing exercise and is expected to produce a cost saving, in this sphere of operation, of around 30% in 2007.

Establishment of relationships for inward remittances from Saudi Arabia and Italy are significant breakthroughs considering the fact that the Sri Lankan expatriate community had limited avenues of remitting their earnings back home from these countries. The placement of additional representatives in the Middle East region and also in Italy has contributed towards harnessing a large volume of inward remittances. A total volume of Rs 115 billion was achieved as inward remittances during the year 2006. This is an increase of around 13% over the previous year.

Infrastructural projects in Sri Lanka supported by European donor funding mainly provided us with opportunities to participate in the issue of bid bonds, performance bonds, advance payment guarantees and Letters of Guarantee on behalf of our correspondents. An increase in volume of around 15% was achieved during 2006 in comparison to 2005.

International Trade Services offers customers products such as issue of import LCs, processing of import bills under LCs, import collections, issue of shipping guarantees, endorsement of advance documents/airway bills, granting import loans, avalisation of import collections, advising of export LCs, adding confirmation to export LCs, transfer of export LCs, export collections, processing bills under export LCs, negotiation of LCs, discounting of export bills and pre-shipment export loans.

HNB’s Trade Services, being ISO 9001:2000 and a centralized operation, has continued to have a positive impact in maintaining our upwardly mobile positioning in a highly competitive environment.
Our Representative Offices in Chennai and Karachi have been supporting the trade operations by facilitating trade contacts for our customers especially in relation to the products that qualify for concessions under the respective Free Trade Agreements.

We also pursued a strategy to reach out to the non urban areas using our branch network with the objective of converting these indirect exporters and local traders to direct exporters and importers respectively.

Income from trade services exceeded the performance levels of the previous year by 25%.

HNB played a lead role in the incorporation of Lanka Financial Services Bureau Ltd., which brings 21 banks/financial institutions under its umbrella and will facilitate the operation of a SWIFT Service Bureau in the country. This move will result in tremendous cost savings for inward and outward SWIFT message traffic by exploiting synergies.

Having comprehensively trained our staff in Anti Money Laundering and Know Your Customer compliance it should be noted that our forte has been recognized within the industry with HNB being requested to train other banks as well. We have already trained those in the Bank of Maldives and aim to conduct a few more training programmes offshore. This emphasizes the best practices already employed at HNB with regard to compliance and also extends a sense of confidence to our clientele as it is understood with these examples that HNB remains above par on the issues of quality, governance and compliance.

**IN 2007, UPWARD MOBILITY WILL CONTINUE BY...**

- Taking the import/export service to the rural sector, thereby strengthening the relationships and also enhancing volumes,
- Conducting workshops and seminars targeted for customers in and around Colombo and also for others in the rural areas emphasizing the advantages of the Free Trade Agreements with India and Pakistan,
- Developing an IT platform in the field of trade business to meet customer expectations,
- Penetrating European markets where there is a high concentration of Sri Lankan community to attract remittances through recognized banking channels from these regions,
- Playing an active role in the SWIFT Service Bureau Sri Lanka which goes live in March 2007,
- Ensuring quality and productive Correspondent Banking Arrangements throughout the globe,
- Ensuring all relationships are compliant with best practices of AML and KYC and comply with local and international laws.
PRODUCTS & SERVICES
Spot & Forward FX, FX Swaps, Derivatives, Repos, Bonds

THE YEAR IN FOCUS
The thrust of the Treasury was focused on the areas of improving overall fund management and increasing market share through strengthened relationships and value additions and maintaining the Bank’s premier position in the forex and money markets. However, lack of depth and lower trading volumes coupled with a volatile external environment resulting from the Central Bank’s stringent monetary policies, saw bond trading come to a virtual standstill. While policy rates increased by 1.25% during the year, real interest rates continued to be negative, giving rise to anticipation of further interest rate hikes. The inability to short-sell bonds continues to act as a further constraint to the development of the bond market.

But the Bank’s drive to continue its upward journey saw the sector differentiating itself from competition by forging closer ties with corporate clients and infusing value added services including stronger communications, consultation and advice to strengthen relationships. This has led to a significant portion of the income pertaining to Treasury coming from corporate clientele.

In aligning ourselves to being upwardly mobile, stringent cash management, yield enhancement techniques and active participation in the forex and money markets were undertaken. Trading in foreign bank notes also gained momentum.

IN 2007, UPWARD MOBILITY WILL CONTINUE BY...
• Differentiating our strengths of service, quality and value additions,
• Building deeper, stronger and more meaningful relationships with our clients,
• Continuing to efficiently manage our funds,
• Launching a 3 year High Yield Fixed Deposit denominated in USD,
• Facilitating trade related options for processed oil on behalf of a processed oil importer.
PRODUCTS & SERVICES
Corporate Finance & Advisory, Equities, Fixed Income, Loan Syndications & Structured Finance, Derivatives & Treasury Products

THE YEAR IN FOCUS
HNB offers a full range of investment banking products and services including corporate finance & advisory, equities and loan syndications & structured finance. Corporate finance & advisory capabilities include the handling of transactions relating to mergers & acquisitions and capital raising advisory services. Our equity capabilities include the origination, structuring and transaction management of IPO’s, follow on issues, convertible issues, private placements, underwriting, listing services and proprietary trading. HNB’s loan syndications & structured finance product offering includes the structuring and arranging of syndicated lending, management of loan syndications, acquisition & leveraged finance, and the origination and placement of a wide range of securitised instruments.

HNB’s full service investment banking capability was further strengthened with measures taken to amalgamate the equities brokerage and fixed income dealing activities under the newly formed HNB Investment Banking Group. Completion of the amalgamation process would result in all investment banking activities being vested with HNB Investment Banking Group enabling the realisation of significant synergies and cost efficiencies while further leveraging our capabilities as a full-service investment banking services provider. We firmly believe that the strategic amalgamation is timely and will further strengthen capabilities and improve our competitiveness in a difficult and fragmented market.

Corporate Finance
Corporate Finance activities remained subdued during the year under review in a volatile and sentiment driven market. Equity markets performed below expectations on account of the volatile political situation. Large equity market transactions consisted mainly of block sales involving selected blue chip and value driven stocks. There was a lack of quality IPO’s coming to the market as prospective issuers adopted a wait and see policy. However, proprietary equity trading activities undertaken on behalf of HNB achieved a significant degree of success and positive results are expected to continue in the coming year. Some of the key transactions successfully completed during the year were as follows:
Loan Syndications
- HNB was the Lead Bank and Co-Arranger for a LKR 4,700 million syndicated credit facility for Celltel Lanka (Private) Limited.
- HNB was the Lead Bank and Lead Arranger for a USD 17.5 million syndicated credit facility for Yacht Tours Maldives (Private) Limited for the development of a resort project.
- HNB was the Lead Bank and Lead Arranger for a LKR 1,600 million syndicated credit facility for a mixed real estate development project promoted by the Ceylon Theatres Group.

Equities and Listing Services
- HNB was the Lead Manager for the acquisition of 20% equity stake in Colombo Dockyards Limited by Horizon Energy LLC.
- HNB is currently mandated for two IPO’s and two introductory listings. We are also mandated as the Advisor and Manager for a block sale of equity by a leading listed company.

Structured Finance
- HNB was the Manager and Arranger for asset backed financing of LKR 500 million through securitisation of lease receivables for Commercial Leasing Company Limited.

Transaction & Advisory Services
- HNB was the Manager to the mandatory offer by Sri Lanka Insurance Corporation Limited, for acquisition of the controlling interest of the Lanka Hospitals Corporation Limited. The mandatory offer was successfully concluded.
- HNB was the Manager to the mandatory offer by Sri Lanka Insurance Corporation Limited, for acquisition of the controlling interest of Asiri Surgical Hospitals Limited.

Primary Dealership
Having seen a year where the market remained inactive, HNB Securities hopes that the security and economic situation within the country will be more conducive to a sentiment change resulting in better business prospects. However, predictions are difficult at this point of time with Government policy and direction yet to be seen for the coming year in order to affect our strategic initiatives.

IN 2007, UPWARD MOBILITY WILL CONTINUE BY...
- Wider consolidation of Group synergies realised through the full amalgamation of all investment banking activities including HNB Securities, HNB Stockbrokers and Corporate Finance within the Investment Banking Group,
- Leveraging on the strengths of the activities within the Group to build a sustainable and strong portfolio whilst rolling out new product lines,
- Using the extensive specialised Human Resources resultant of the amalgamation as a strategic selling point in building the business.
THE YEAR IN FOCUS
The Bank implemented the much anticipated cheque imaging and truncation system on a nationwide initiative of the Central Bank of Sri Lanka, which has benefited a large number of our clients through the one day clearing umbrella. The one day clearing initiative will be extended to all parts of the island during 2007.

Constantly looking towards value addition, Internet Banking was replaced with the innovative Virtual Banking Suite providing a varied gamut of convenient features which includes third party fund transfer to any account within HNB and added flexibility in managing funds.

Augmenting our IT platform into the sphere of telecommunications, HNB signed up with both Mobitel and Lanka Bell to present customers with a unique menu driven option for banking transactions. This pioneering effort by HNB is a result of substantial background work in the past that has now taken SMS Banking to CDMA telephone units as well.

Fully automated self service kiosks were added to the Internet services offered by the Bank in December this year, with the added feature of bill payment receipts being issued.

IN 2007, UPWARD MOBILITY WILL CONTINUE BY...
• Replacing the Bank’s existing core banking platform with a new banking solution to support current and future growth,
• Strengthening our IT platform to give more value additions via our products to our customer base including HNB Money2Home facility,
• Implementing an efficient 24/7 funds transfer facility for exchange houses,
• Expanding the HNB Easy Pay payment portal.
HNB affirmed the foundation already created that we are a bank that has truly become one with the people. In communicating this message, we emphasized that our products and services encompass the essence of the Sri Lankan citizen, from an infant to a senior citizen giving them the stability and security they have always wanted. We have also worked on the aspect that the citizens of this country should have equal opportunity wherever they are, to have the basic rights of having banking services offered to them devoid of hassles.

THE YEAR IN FOCUS

Our marketing approach has been consolidated to reflect top-of-the-mind recall for Brand HNB. We have striven to give our stakeholders the philosophy that HNB is accessible to all with an extensive product portfolio that would encompass every single person who aspires to build a relationship with HNB. This anthology of products comes under the overarching branding of HNB to ensure that stakeholders are aware that Sri Lanka’s premier private sector bank will live up to its promises and brand values. Innovation and thinking out-of-the-box have remained key elements in retaining our product leadership positions in most areas. HNB has been a pioneer in innovating product development especially in the retail banking areas of housing, children’s savings and rewards programmes.

While we did use the traditional media channels of TV, radio and print to communicate our message, one of our innovative communication strategies this year was to have universal HNB branding for all our branches. Facades and interiors were streamlined to reflect a common branding strategy with easily identifiable signage across the country. In addition, our Wattala branch launched the initiative of making every HNB branch more accessible to customers requesting assistance with mobility, a strategy which will gather momentum during the next four years. Other product delivery mechanisms including the school units, micro finance centres and mobile units were strengthened. Envelope messaging via our credit card and account statements innovatively communicated new products or services being launched to customers, while road shows, tie-ups with local radio stations for promotions and town storming activities augmented our communication methodologies.

In addition to a number of social community projects conducted by HNB which are detailed in the Sustainability Report, some of the highlights of our marketing activities pursuant to products and brands this year are given below:
• With HNB winning the Bank of the Year 2006 award, a concerted corporate media campaign was spread across the print media.

• Pathum Vimana 2006 was re-launched under the theme, ‘Better, Bigger and Back Again’ with a value addition of a mid year premium for an Audi A4 car and the grand year end draw for a Mercedes Benz E-Class. The Pathum Vimana 2006 concept was also given a value extension with the introduction of a TV game show with all participants winning cash prizes.

• The HNB Shanthi Housing Loan scheme celebrated ten years with a promotion that presented a grand prize of wiping off a housing loan of up to Rs 2 million among a host of other prizes.

• The minor savings scheme, Singithi Pathum, was launched with a special promotion of gifts presented to our young customers who deposited stipulated amounts during the promotional period, over and above the usual prizes won at the raffle.

• HNB Leasing strengthened its image and brand this year with a number of strategic tie-up and promotions with vehicle dealers. Around 25 localised promotions were carried out in tandem with aggressive town storming events in locations with a HNB branch presence.

• HNB credit cards launched two usage promotions during the Sinhala New Year and Christmas, the latter themed ‘The 31 days of Christmas’ supported by print, radio and point-of-sale material.

• HNB Fixed Deposits offered attractive interest rates periodically communicated through print and radio.

• Driven mainly via print and radio, HNB Subasiri personal loans were re-branded as HNB Personal Loans.

• HNB Pawning was aggressively promoted throughout the year with the introduction of special promotions including the presentation of gifts to customers, driven through print, radio and TV advertising as well as localized promotions in selected areas with strong HNB branch presence.

• Giving customers secure online access to current, savings and credit card accounts, HNB launched its ‘Virtual Branch’, styled on internet banking services. Customers can also use the Virtual Branch for bill payment facilities for utility services including the CEB, Dialog, Mobitel, Celltel, HNB Assurance and Lanka Bell. E-banking kiosks were also introduced as a service value addition for remote internet banking as a part of HNB’s e-banking strategy for 2006.

• In partnership with Mobitel, HNB introduced the first ever OTA (Over the Air) menu driven SMS banking service in Sri Lanka, allowing customers to avail themselves of information on accounts, fund transfers, credit card inquiries and bill payment as well as online settlement of mobile phone bills and top ups.

• SMS Banking was further expanded in partnership with Lanka Bell when HNB pioneered the usage of CDMA technology allowing customers to use the fixed line telephone systems for their inquiries.

**IN 2007, UPWARD MOBILITY WILL CONTINUE BY...**

• Strengthening our product delivery channels for accessibility, especially to remote areas so that HNB will be at top-of-the-mind recall,

• Re-furbishing the mobile units with stronger branding and a face lift,

• Pursuing non-traditional methods of communication to spread our message,

• Continuing to make our Customer Centres accessible to those requiring assistance with mobility.
The year for HNB Stockbrokers has been a challenging one despite market gains and the ASPI growing by 41.6% and the Stock Exchange recording some significant trading benchmarks. Despite a slow start to the year, market picked up towards latter part of 2006, surpassing the 27.6% ASPI growth witnessed in year 2005. However, the market turnover declined by 8.29% to stand at Rs. 210 billion when compared to last year’s figure of Rs. 229 billion.

However, HNB Stockbrokers continues to reflect the upwardly mobile attitude permeated by the Bank, by being ranked among the top four stock brokering companies in the country on the basis of the number of transactions effected at the Colombo Stock Exchange. The average market share registered was 7% (or the highest market share registered was in the month of July at 19%). A turnover of Rs. 14.5 billion is recorded for 2006 with a pre tax profit of Rs. 35 million reflected from a brokerage income of Rs. 100 million. Net assets stand at Rs. 120.8 million this year a significant 433% increase from 2001 when HNB Stockbrokers became a fully owned subsidiary of Hatton National Bank.

HNB Stockbrokers participated in numerous road shows conducted by the Colombo Stock Exchange interacting with a number of investors who were interested in Sri Lanka. The most evident facet from the feedback received was that while investors remain positive about Sri Lanka’s investment potential, peace and stability remain a priority for attracting investors and until a stable solution is achieved, full potential of the investment will not be experienced by the country.

**THE YEAR IN FOCUS**

- **Jayathura Lottery**: The first brokerage house in the industry to launch a rewards scheme for HNB and HNB stock broking clients in 2005, we extended the reach of the Jayathura Lottery. Having begun with just one sponsor, Etihad Airways, in 2006 we aligned the scheme to Singhagiri Limited, the sole agents for Samsung and Galway Hotels was also added.

- **HNB Stock Web and Retail Market Booster**: In a bid to infuse state-of-the-art technology into daily operations, the Company launched www.hnbstock.com in March 2006, a comprehensive website together with the ‘Retail Market Booster – Internet Trading System’, which won the Gold Award in the financial services sector and a silver award in the overall category at the National Best Quality Software Awards. The system was developed by Messrs Affno (Pvt) Ltd. This facilitates online trading in a speedier and more efficient environment, giving the company an edge in technological advancement over competition. Better time management and a more effective usage of technology which spreads to clients in any part of the world is also a result of this development.
• **Awareness programmes on the Stock Market:** Distribution of literature on the stock market, its workings and requirements were effected to existing and potential clients through direct mailers, the HNB Card Centre and HNB branches.

• **Stock Exchange Investment Advisor Programme:** A total of 27 who underwent training at the Stock Market Training Centre were nominated to follow the Stock Exchange Investment Advisor Programme as a preamble to the promotion of share trading through HNB branches.

• **Road Shows:** HNB Stockbrokers were active participants at the road shows conducted by Colombo Stock Exchange in Australia, New Zealand, and Singapore. Road shows were also held to coincide with the World Bank and Commonwealth Finance Ministers’ meetings held in Singapore where the top four listed companies were showcased to promote Sri Lanka as an investment destination. Our GM/CEO along with a group of CEO’s of member firms visited the Nasdaq, New York Stock Exchange, Boston Stock Exchange, International Derivatives Exchange of New York in USA and the Canada Stock Exchange as a part of a familiarization program.

• **Research Publications:** An active component of the Company, the Research Department publishes regular Industry and Company Research, Strategy and Economic Reports, Weekly Reports, Daily Reports and daily valuations continue to be published. This year, the Research Department published a comprehensive report on a number of conglomerates in Sri Lanka, a report on the Banking sector and an analysis on Budget 2007 and its impact on the stock market, the economy and major industry.

**IN 2007, UPWARD MOBILITY WILL CONTINUE BY...**

• Aggressively promoting internet trading for high net worth clients as well as offshore clients,

• Taking initiatives to implement internet payment and receipt methodologies for stock market transactions,

• Introducing internet trading to ten HNB branches, equipping them with a special trading area manned by a banking assistant /a stockbroker, complimented by regular awareness campaigns,

• Commencing SMS market alerts,

• Enhancing communication via mass media especially overseas for publication of research reports and other required information,


---

**SUBSIDIARY OPERATIONS**

**HNB Securities (Pvt) Limited**

HNB Securities Ltd., weathered a number of shocks during the year 2006, stemming from the continued uncertainty over the peace process and the resultant volatility in the political and economic arena.

Rising interest rates and adverse inflationary trends had a negative impact on the bottom-line of the Company in the form of losses on government securities. The Company ended the year with a net loss after tax of 18.2 million compared to a net profit after tax of Rs. 87.4 million during the previous year.

Although, the domestic government securities market remained subdued during most parts of the year, the Company maintained a strong presence in the retail sector.
The aggressive but astute stance pursued by HNB Assurance Ltd, saw the Company achieve the milestone of reaching a combined annual turnover of Rs 1 billion this year, crossing the mark within just five years since inception, the fastest within the industry to achieve this milestone. The commendable figures were further augmented when at the end of the year, the Company posted a combined turnover of Rs 1,122 million, amounting to a growth of 36% over the turnover registered last year. The Company does utilize the significant advantage of being a subsidiary of one of the premier banks in the country but has continued to hold its own individual stance as well. At the Annual Report Awards 2006 conducted by the Institute of Chartered Accountants of Sri Lanka, HNB Assurance was placed third and awarded a merit certificate in the Insurance Sector, a significant achievement for a relatively young company in a highly competitive industry.

The Company’s General Insurance premium grew by 32% to reach Rs. 619 million while its Life Insurance premium grew by 42% to reach Rs. 503 million. The profitability of the Company improved further registering a net profit after tax of Rs. 91.3 million, recording a growth of 51.5% over the last year. General Insurance business contributed Rs. 62.7 million to the profit before tax of Rs. 92.7 million while the contribution of the Life Insurance business stood at Rs. 30.0 million.

In a bid to expand the product portfolio aiming towards above industry growth, during the latter part of the year the Company launched Travel Assist which supplements the existing range of travel insurance products that include Travel Pal, Travel Max and 70+. Pitched as a travel assistance product rather than the conventional travel insurance to give customers a more rounded package of services, the product was launched to bridge a gap within the travel insurance market which has hitherto remained untapped. The Company also launched a new Medical Insurance Plan targeting the top end of the retail market.

Together with parent HNB, the company also launched a unique micro insurance product aimed specifically for micro entrepreneurs wherein the entrepreneur’s entire risk is borne by HNB Assurance. The product, worked on an affordable premium, gives multiple cover for all eventualities. This initiative has seen immense success in areas as diverse as Akkaraiapattu, Chilaw, Nocchhiyagama and Galle with over 500 policies issued and a monthly growth rate of 20%.

The increasing popularity of our motor insurance product ‘Motorguard’ assisted in achieving a growth of 36% in the premium income from motor insurance. We also launched a cashless hospitalization facility for corporate health insurance plans facilitated through a tie-up with Medilink, a specialist third party administrator of claims. The Company also introduced a web-based facility through which marine open cover certificates could be printed online by customers.

The total number of branches opened this year stands at six with new branches opened in Embilipitiya, Ja-ela, Ambalangoda, Bandarawela, Ambalantota and Gampola to further strengthen the distribution network. New Insurance Desks were also established at Polonnaruwa, Kalmunai and Batticaloa within HNB branch premises.

The total number of branches opened this year stands at six with new branches opened in Embilipitiya, Ja-ela, Ambalangoda, Bandarawela, Ambalantota and Gampola to further strengthen the distribution network. New Insurance Desks were also established at Polonnaruwa, Kalmunai and Batticaloa within HNB branch premises.
PRODUCTS & SERVICES
Manage HNB Towers/Develop other potential real estate sites

Our main source of income is generated through our tenants, HNB, our parent company who occupies 80% of HNB Towers and other Organizations. With prudent management of operational and maintenance costs, we have curtailed our loss this year to Rs. 22.5 million, which is 55% lower than the previous year. Our strength lies in a committed small in-house team of technical personnel who has mastered the efficient utilisation of the advanced energy saving systems installed for the first time in Sri Lanka at HNB Towers.

We have, this year ventured into a real estate development project at Havelock Road, Colombo 5. "Spathodea Residencies", 48 luxury apartments situated in a prime residential area, due for completion in 2008. We believe the completion of this project will augment our income and will look forward to tapping the resources of more real estate opportunities that may arise.
Reflecting the vicissitudes inherent in our business, we faced a challenging year, largely due to the decline in investment income by 14% over last year, recording an income of Rs 73 million compared to last year’s Rs 85 million. We exited from two venture capital investments and partially exited from another during the year, but the realized capital gains were much less than gains realized previously. However, taking advantage of the buoyant stock market conditions that prevailed during some part of the financial year, we exited from several stock market investments at a substantial profit.

Past records show that we have realized substantial capital gains when exiting investments through the stock market and would welcome the opportunity to maximize exits through this route. However, promoters of many companies, specifically medium sized enterprises that do have good listing potential as an avenue to raise capital, prefer to remain unlisted on the belief that through the exposure of a public listing, they will face innumerable challenges including the fear of losing management control, stringent disclosures and complex listing requirements. Hence, in the immediate past, majority of our exits was achieved through redemptions or sale of investment back to the promoters.

Being aware of our responsibilities to our shareholders, we are pursuing avenues of sustainable and stable income in the future. Furthermore, being a listed company, we cannot afford to function within a milieu of uncertainty. We have identified power and energy and healthcare sectors as those with potential for growth and will be seeking opportunities in these sectors for investment. LVL Energy Fund was incorporated this year to aggressively pursue this growth strategy with future investments in the power and energy sector being channeled through this subsidiary. We were also the pioneers in assisting the setting up of the leading dedicated private heart-care centre in the country and given the response to these niche healthcare segments, we will be pursuing further opportunities akin to this in the coming year.
Global Presence

**Americas**
- Argentina
- Bahamas
- Bermuda
- Brazil
- Canada
- Chile
- Colombia
- Hawaii
- Mexico
- Peru
- Uruguay
  - United States of America

**Europe**
- Austria
- Belgium
- Cyprus
- Czech Republic
- Denmark
- Finland
- France
- Germany
- Gibraltar
- Greece
- Hungary
- Ireland
- Italy
- Netherlands
- Norway
- Poland
- Portugal
- Romania
- Russian Federation
- Serbia & Montenegro
  - Spain
  - Sweden
  - Switzerland
  - Turkey
  - United Kingdom

**Middle East & Africa**
- Bahrain
- Botswana
  - Egypt
  - Ethiopia
  - Ghana
  - Iran
  - Israel
  - Jordan
  - Kenya
  - Kuwait
  - Lebanon
  - Libya
  - Mauritius
  - Oman
  - Qatar
  - Saudi Arabia
  - Sierra Leone
  - Somalia
  - South Africa
  - Sudan
  - Swaziland
  - United Arab Emirates
  - Yemen
  - Zambia
  - Zimbabwe

**Asia & Pacific**
- Australia
- Bangladesh
  - China
  - Fiji Islands
  - Hong Kong
  - India
  - Indonesia
  - Japan
  - Korea
  - Maldives Islands
  - Malaysia
  - Nepal
  - New Zealand
  - Pakistan
  - Philippines
  - Singapore
  - Taiwan
  - Thailand
  - Uzbekistan
  - Vietnam
Customer Centre Network

HNB Customer Centres to be opened during the 1st quarter of the year 2007
• Nikaweratiya • Wellawatte - 2nd Office • Wariyapola • Hettipola • Alawwa

HNB Student Banking Centres - 152
HNB Gami Pubuduwa Banking Centres - 109
Village Based - 23  Branch Based - 86

HNB Mobile Banking Centres - 2
Hotel Culture Club and Kandalama Hotel - Dambulla

Overseas Representative Offices
Chennai - India and Karachi - Pakistan

Western Province

Airport Office
Aluthgama
Aluthkade
Apollo Hospitals
Asha Central Hospital
Athurugiriya
Avissawella
Bambalapitiya
Biyagama
Boralesgamuwa
Borella
Cinnamon Gardens
City Office
Dehiwela
Delgoda
Dematagoda
Emirates
Gampaha
Grandpass
Gunasinghepura
Hanwella
Head Office Branch
Homagama
Horana
Hulftsdorp

IWMI - Pelawatta
Ja-Ela
Jampettah Street
Kadawatha
Kaduwela
Kalutara
Kandana
Katunayake
Kiribathgoda
Kirindiwela
Kirullapone
Kollupitiya
Kollupitiya Extension Office
Kotahena
Kottawa
Kotte
Maharagama
Main Branch
Malabe
Maligawatte
Maradana
Marandagahamulla
Minuwangoda
Mirigama
Mirihana
Moratumulla
Moratuwa
Mt. Lavinia
Mutwal
Narahenpita
Nawaloka Hospital
Nawam Mawatha
Negombo
Negombo Extension Office

Nittambuwa
Nugegoda
Overseas School of Colombo
Padukka
Panadura
Panchikawatte
Pettah
Pettah - 3rd Office
Piliyandala
Ports Authority
Ragama
Ratmalana
Sea Street
Seeduwa
Sri Jayewardenepura Hospital
Sri Lankan Airlines
Administrative Complex
Talangama
Thalawathugoda
Thimbirigasyaya
Wattala
Wellawatte
Wijerama
HNB’s astute initiatives implemented in the last two years saw fruition to post positive results in most areas despite 2006 having been a challenging year for the financial services industry in Sri Lanka. In terms of our core business, we have been able to achieve the set targets commendably mainly due to the singular focus we had in achieving our objectives. We do believe that this trend will be sustainable in the medium term future. The results we have seen in our multi dimensional objectives and targets do indicate that the upward trend has been built on a sound sustainable financial platform that will continue into the future.

The sound management practices at HNB combined with this focused journey have allowed us to manage the external financial policies and stringent taxation regime that posed the majority of the challenges over the year. Yet, the Bank posted a significant growth in Profit Before Tax of 63% displaying Rs 3,019 million compared to last year’s Rs 1,850 million. For the first time, the Bank’s Profit After Tax figure crossed the Rs 2 billion threshold which is an extremely noteworthy achievement for us and showcased an increase of 34.2% over the Rs 1,654 million shown in 2005.

The Bank’s income tax expense significantly increased by 308% to Rs 798.9 million during the year. The main reasons for the increase in income tax were the upward revision in tax rate by 5% and the growth in pre tax profits.

5% increase in income and financial services value added tax rates are indications that this source of revenue to the Government may increase in the future. Hence, the taxation regime in place at present does not signal a pro-growth environment for the Bank.

Total assets recorded at Rs 196 billion, a modest growth of 18% over last year’s Rs 166 billion. Cash and short term funds as well as Advances (post provisioning) displayed at Rs 55 billion and Rs 128 billion respectively, propped the figures significantly. Loans under FCBU net of provisioning also had an increase of Rs 2.6 billion. Housing and pawning, our main retail products of the asset categories reported 16% growth and the growth in the corporate segment was posted at 20%. The interest earning assets of the Bank as a percentage of total assets now lies at 86.6% and this ratio was 86.4% in 2005.

The Bank’s deposit base showed a growth of 15% to Rs 148 billion, certainly a witness to the concentrated drive the Bank employed this year to increase its deposit base. Savings deposits saw a growth of 7% over the year, while both Demand Deposits and Minor Savings Deposits grew at 1% and 14.9% respectively. However, despite some concerted marketing efforts including the popular Pathum Vimana scheme, Fixed Deposits still hold more attraction due to the higher interest rate which, this year, averaged at 12% as opposed to 9% during the last year. Fixed and Call Deposits also posted final figures of
Rs 52 billion compared to Rs 37 billion last year which is an increase of 40%, while NRFC/RFC/EFC deposits posted a growth of 4% to stand at Rs 32 billion at end of 2006. Interest expenditure also rose by 35% during the year. Matured deposits getting reinvested at higher rates and regular savings accounts shifting to Fixed Deposits due to the higher rate were significant causes of interest expenditure increase. However, over this year, HNB was emphatic on managing the interest rate margin and curtailing growth in operational costs, transforming its nationwide penetrative capabilities and humane approach to take the banking concept closer to all strata of society, results of which will be seen in the next few years. This will ensure judicious management of operational expenditure, while not compromising on growth opportunities.

The total revenue of the Bank increased by 27.2% over the year. Interest income showed a growth of 30.5%, Net interest income by 26%, Commissions & Fee income by 7.9% and Exchange income by 22.5%. The noteworthy increase in interest income is mainly due to the Bank’s collection ratio being above industry average of 2005 and this year showing a ratio of 90.65%. The Bank further concentrated on acquiring a high quality portfolio by working through a weaning process, which would, in the long run, add value to the bottom line with the growth in advances. However, interest income increased more than the growth in advances, which could be attributed largely to good loan recoveries during the year and the rise in interest rates. Exchange income which encompasses a significant component of non interest income recorded a growth of 22.5% this year, posting Rs 792 million, depreciation of the Sri Lankan Rupee by 5.5% through the year and an increase in volumes have contributed to the good figures displayed in Exchange income. Increase in the Fee & Commission income was a modest 7.9% and capital gains earned from fixed income securities reduced significantly due to the escalation of domestic interest rates. Further, a conscious decision taken to reduce the scale of activities in derivatives and bullion trading due to their associated high volatility and risks, also reduced an avenue of other income.

Other Income is displayed at Rs 396 million compared to the 2005 figure of Rs 410 million.

We took a cautious approach with our equity trading portfolio and made investments with a two-year horizon in mind. The exposure which was at Rs 345 million at the end of the 2005 was increased to Rs 400 million after the Geneva Rounds of Peace Negotiations commenced. Commencement of hostilities between the Government forces and LTTE subsequent to the blocking of Marvilaaaru anicut reduced our exposure and the realization of part of the capital gains from the portfolio. Thus, the contribution to the other income from the equity portfolio has decreased. However, the Rs 77 million provision made in 2005 for diminution in value is fully recovered as the current portfolio has performed well above its cost.
Our operating expenses however, increased by 29% to Rs 7,732 million over last years' Rs 6,001 million, with the main contributory factors being staff emoluments, financial value added tax, advertising, fuel, rent and rates. We continue to manage our expenses with the staff head count remaining the same but have employed effective strategies in utilizing our human resources more astutely to ensure enhanced productivity which in effect will continue to contribute positively.

The advances to deposits ratio which reflects the efficiency at which the deposits are utilized to grant advances was maintained around 80% during the year.

The liquid asset ratio which reflects the liquidity position of the Bank was also maintained above 22% which is well above the stipulated minimum by CBSL.

With the Rs 2.22 billion after tax profit, we realized this year, total shareholders' funds grew to Rs 12.93 billion. Conscious curtailment in growth of non interest bearing assets has increased the free capital from Rs 3.7 billion in 2005 to Rs 6.4 billion in 2006, which now stands at 49% of the shareholders' funds.

The Bank’s Core Capital as at end 2006 stands at Rs 12,691 million while Total Capital is displayed at Rs 14,049 million. The Bank’s Tier 1 ratio recorded a marginal decrease of 0.6% to reach 10.23%. The Bank’s Total Capital Adequacy Ratio stands at 11.32% down from 11.55%.

The main reason for the decrease in the Tier 1 capital is, as directed by the Central Bank of Sri Lanka, the risk weighting for loans secured by primary mortgage over residential property increased from 50% to 55% and risk weighting for other loans increased from 100% to 110%. These changes have resulted in an increase in the risk weighted asset base by approximately Rs 8.4 billion. Bank raised Rs 1.12 billion at the beginning of the year through a series of debentures with maturities running up to 18 years. Such long tenure instruments not only compliments the capital but smoothens the depreciation process stipulated by the regulator and reduces the maturity mismatch of long end assets and liabilities.

Return on average assets has settled on a comfortable 1.23%, compared to last year’s 1%, which essentially reflects the firm stand taken by the Bank over the last two years that balance sheet growth must concentrate largely on the productivity of the asset, while maintaining the profitability equilibrium. We have trusted upon ourselves to improve the ROA to 1.5% within the next three years and this will be achieved by consciously monitoring the need of acquiring non interest bearing assets in the future, managing the margins realized from each asset class, managing on time collections and facilitating a steady growth in asset portfolio.

With the strategic initiatives that have been implemented in the last two years and augmented this year, the Bank looks forward to a post-tax profit growth of above 20% in 2007.
SUSTAINABILITY REPORTING
PREAMBLE

As an organisation whose core existence and sustainability is totally dependent on our relationship with each stakeholder segment, at each level of our interaction, we remain acutely aware that sustainability is now a business fundamental, an aspect that HNB must and has to be completely and holistically committed to. Sustainability is defined as ‘meeting the needs of the present generation without compromising the ability of future generations to meet their own needs’, which to us is the axiom upon which our value truss is built upon.

HNB is a bank whose history spans 118 years. We have seen and been a part of history making epochs, not only in an economic and business sense but also in the attitudinal change and dynamic demand trends of customers, valued business partners, investors, the community and the general public. We have seen the basic fundamental facets of our business convert from creating wealth for our shareholders to encompassing the complete landscape of sustainability, where the focus has transformed to the socio-economic aspects of environmental and social change within the macro picture of sustainable development. Thus sustainability now co-relates to the entire gamut of transparency, accountability and sincerity of action on our part with each stakeholder segment demanding responsible business actions, minimising negative impacts economically, socially and environmentally. It is this thought flow that has spurred HNB to spearhead a more systematic approach towards sustainability where a committed team focuses on predetermined platforms to ensure that the Bank remains aligned to its vision, mission and values within the larger picture of sustainability.
“SUSTAINABILITY – AN ETHOS, NOT JUST RHETORIC.”

“We have often asked ourselves the question, ‘Where do we want to be in the next three to five years?’ And the response has unwaveringly been “As the Leader”. But leadership is not an aspect that comes overnight and it is not for us to call ourselves leaders but for others to recognise us in that unquestionable position and emulate our example. We want to be the most preferred bank in the country where HNB would be the partner in progress of our stakeholders. And we don’t want to be simply perceived as a Bank but rather as an entity that strongly believes in, contributes and partners development that will create a sustainable economic and social milieu for all stakeholders to grow and thrive in the long term.

We have now taken our sustainability philosophy to the next level – reporting on our sustainability initiatives. A Sustainability Report is an important tool which encapsulates the true meaning of the entity, not just on corporate social responsibility but by providing a sustainable business platform to survive and to engage in the environment around it. In that process, we have looked at the facets of a customer, valued business partner, shareholder, team member and citizen and have demonstrated the initiatives we have established and implemented in creating a sustainable model for HNB. Having the Report independently validated too became important and for the first time last year, we engaged the services of KPMG Ford Rhodes Thornton & Co as an independent assurance provider to validate our Report. From a shareholders’ perspective it is imperative to note that HNB is no longer a locally owned bank but rather one that encompasses international investors. The moment we open ourselves to the world, we also bare ourselves to international scrutiny and are bound to maintain international best practices and standards. A Sustainability Report also becomes a risk management tool and is currently being used constructively to better the standards, trouble shoot and create a sustainable economic platform which anticipates and manages risks better.

We have always espoused the true ethos of sustainability, not merely talking about making a difference to each of our stakeholder segments, but in a true sense, conceptualizing and driving initiatives that will make a difference in their economic and social fabric. We have analyzed the impacts our decisions will make on stakeholders and have consciously tried to maintain a platform of equality, fairness, sincerity of action, accountability and transparency in everything we have set out to do. Our relationships thus have grown and strengthened and we have seen the image of HNB become one with the people, becoming a part of their lifestyles and their future decisions. This we feel is the all important thread that should run through in sustainability, where a strong partnership has been created between our stakeholders and ourselves, built on a long term vision of growth, development and sustenance.

Sustainability to us is creating an entrepreneurial culture; thinking out of the box and being innovative to sustain a leadership stance; living in harmony with the environment to ensure that future generations will continue to enjoy a similar or better quality of life than us; being philanthropic in lending a helping hand as the first step towards empowerment and espousing the true tenets of an ethical and responsible corporate citizen who sets an example for others to follow.

We hope this Report in which we have explained to you our actions, will assist you in gauging our performance against your expectations of the HNB Group as one of Sri Lanka’s premier financial service providers. We value your comments with a view to further enhance our service levels and product portfolios and to augment the sustainability of your Bank. An Investor Feedback Form is appended for your ease of use. Your feedback is important to us”.

Rajendra Theagarajah
MD/ CEO
PURPOSE OF THIS REPORT
Sustainability Reporting, as we understand in HNB, is the practice of measuring, disclosing and being accountable to internal and external stakeholders for HNB’s performance towards the goal of sustainable development. We have developed this Report with the view to provide a balanced and reasonable representation of the sustainability performance of HNB, including both positive and negative contributions.

The Global Reporting Initiative (GRI) which is an official Collaborating Centre of the United Nations Environment Programme located in Amsterdam, is a long term, multi-stakeholder organization whose mission is to develop and disseminate globally applicable Sustainability Reporting Guidelines (Guidelines). These Guidelines are intended to serve as a generally accepted framework for reporting on an organisation’s economic, environmental and social performance. We have endeavoured to compile this Report based on the GRI Guidelines and have disclosed outcomes and results that occurred within the reporting period in the context of HNB’s commitments, strategy and management approach.

REPORTING PRINCIPLES
SCOPE
The Sustainability Report covers HNB’s activities and performance in the field of sustainability. It includes qualitative and quantitative data about the year ended 31 December 2006.

SELECTION OF TOPICS
Most topics in this Report are based upon our continuous interactions with our stakeholders on what they feel is of importance to form opinion on our sustainability behaviour. We have used the GRI Guidelines to ensure that we cover relevant topics identified by a broad range of stakeholders, which are generic to sustainability reporting. This Report has been compiled based on GRI’s Guidelines (G3 version) and its supplement for the financial services sector. The guidelines comprise of several sections of which the two most important ones are the Reporting Principles and Standard & Guidance Disclosures.

REPORTING PROCESS
We have no overall information system in place for sustainability comparable to the systems used for obtaining financial information for the Annual Report. Nevertheless, whenever possible we use corporate information systems for gathering data. Only for those indicators that we considered to be relevant, but that were not covered in an existing system, did we use local information systems and questionnaires to aggregate the information. We verified such information via one-to-one conversations with the Heads of the respective Business Units and in meetings of the sustainability committee. Although we are confident of the overall reliability of the data reported, we recognized that some of this information was subject to a degree of uncertainty because of limitations associated with measuring, calculating or estimating it.

ASSURANCE REPORT
We have asked KPMG Ford Rhodes Thornton & Co (KPMG) to review HNB’s Sustainability Report 2006 to provide the readers with a reasonable level of assurance on selected financial data and limited level of assurance on Key Performance Indicators (KPI) and the other information in the Report. The Report, including the identification of material issues is our responsibility. Based on the defined scope, KPMG decided to perform the activities described in the assurance report on page 78.

We realize that building sustainability into our business process is an ongoing process and that the quality of data collection and analysis, and internal controls at product/service division and corporate level, need our continuous attention. We are in the process of improving this and we anticipate that in the coming years we will have the reliability of information for a selection of material subjects to be reviewed by KPMG. Accordingly, we will be reassessing the scope of the assurance assignment, in order to further optimize the added value of the assurance process for our stakeholders and its contribution to internal improvements.
SUSTAINABILITY COMMITTEE

DUTIES OF THE SUSTAINABILITY COMMITTEE

• Act as the think tank in developing the Sustainability Agenda for the Bank
• Oversee progress in economic, business, employee, community and environmental projects
• Set standards for policies and procedures in meeting Sustainability Principles
• Ensure business and operational initiatives conform to all Sustainability Principles.
• Proactively evaluate all decisions that would have an impact on the reputation, ethics and values of the Bank
• Identify and manage areas of non-compliance within the Sustainability Principles

SUSTAINABILITY STEWARDSHIP

A dedicated Sustainability Committee headed by the MD/CEO which demonstrates the Bank’s complete commitment to ensuring that sustainability is integrated into our business processes, sets out the goals, direction, framework and sustainability platform focus, while three sub committees set out the project focus, investment and approvals in the areas of Customer/Investor, Employee Liaison and Environment/Community areas.
SUSTAINABILITY STRUCTURE AT HNB

With the Sustainability Committee driving direction and giving leadership, the sustainability reporting focus is now under the focused platforms of:

INVESTOR RELATIONS creating wealth for shareholders, managing risk prudently and professionally contributing to the larger economic picture whilst setting benchmarks for the industry.

EMPLOYEE RELATIONS creating two-way relationships that inculcate team spirit within the Hatna Family concept and pursuing excellence.

SUPPLIER RELATIONS focussing on long lasting partnerships on qualitative platforms.

CUSTOMER RELATIONS ensuring that service excellence remains a fundamental in the delivery of superlative products and services and building our business on the foundation of trust and confidentiality.

COMMUNITY RELATIONS creating sustainable communities through enhanced education opportunities, entrepreneurial assistance and improved health conditions.

ENVIRONMENTAL RELATIONS ensuring a sustainable planet through conservation and preservation of the environment by introducing best practices.

TOTAL INVESTMENT DISBURSED ON SUSTAINABILITY PROJECTS THAT ENCOMPASS COMMUNITY AND ENVIRONMENTAL RELATIONS THIS YEAR IS RS 16 MILLION.
CONTRIBUTING TO THE SRI LANKAN ECONOMY

Dating back to 1888, HNB’s history has evolved from being a bank that was formed to cater to the emerging needs of the European planters, to merging with the Sri Lankan operation of National and Grindlays Bank to become Hatton National Bank Limited, to today being recognised and honoured by local and global compatriots as a bank that espouses industry leadership, entrepreneurial spirit, community empathy and people power. The exponential growth the Bank has showcased over the centuries has seen the Bank’s contribution to the national economy continuing to grow, a contribution that has been utilised for national development and the upliftment of the people of Sri Lanka.

BANKS’ CONTRIBUTION TO THE ECONOMY IN 2006

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Banks’ expenditure</td>
<td>Rs. 17.64 billion</td>
</tr>
<tr>
<td>Of which, amount spent on wages / salaries, etc</td>
<td>Rs. 3.165 billion</td>
</tr>
<tr>
<td>Banks’ tax contribution (PAYE, VAT, Income Tax and other taxes)</td>
<td>Rs. 1.872 billion</td>
</tr>
</tbody>
</table>

- There are 16,839 shareholders (Resident-16,654, Non Resident-185) the Bank pays in dividends each year.
- HNB Market capitalization Rs. 14,672 million.
- More than 4200 employees work for Hatton National Bank Ltd.

**GOVERNMENT TAX**

- Income Tax (42%)
- Provision for VAT (52%)
- Debit Tax (1%)
- Payee Tax & Stamp Duty (5%)

**Tax Figures**

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Income Tax</td>
<td>799 Mn *</td>
<td>42%</td>
</tr>
<tr>
<td>Provision for VAT</td>
<td>973 Mn *</td>
<td>52%</td>
</tr>
<tr>
<td>Debit Tax</td>
<td>9 Mn</td>
<td>1%</td>
</tr>
<tr>
<td>Payee Tax &amp; stamp duty</td>
<td>91 Mn *</td>
<td>5%</td>
</tr>
</tbody>
</table>

* Provisional figures
Our customers remain the catalyst to our service ethos and we have strived throughout the years to introduce and initiate products and services that satisfy their financial needs and wants and foster long term partnerships spanning their whole life, from birth to the twilight years. Whilst most of our product and service enhancements and introductions are covered elsewhere in this Report, we detail below some of the other important aspects of our enduring service commitment.

**LISTENING AND RESPONDING**

Two Customer Satisfaction Surveys that gave the Bank a comprehensive and scientific feedback and analysis of customer satisfaction were conducted this year.

**INTERNAL CUSTOMER SATISFACTION SURVEY**

Conducted twice a year through the Regional Offices, the survey is randomly conducted among 50 customers of each branch to gauge service and delivery levels. The findings are the basis for the annual competition conducted by the Bank for the region-wise Inter-Branch Customer Service Award.

Responses received: (2006) 1,865

<table>
<thead>
<tr>
<th>Aspects of Service rated as Excellent/V. Good</th>
<th>Aspects of Service where need for improvement is indicated (at some branches)</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Overall Staff Competence</td>
<td>• Parking and other similar facilities</td>
</tr>
<tr>
<td>• Courtesy of Branch Staff and Willingness to Help</td>
<td>• Counter Service</td>
</tr>
<tr>
<td>• Accessibility to Senior Branch Officers</td>
<td>• ATM Service</td>
</tr>
<tr>
<td></td>
<td>• Despatch of Current Account Statements &amp; Debit/Credit Advices</td>
</tr>
</tbody>
</table>
EXTERNAL CUSTOMER SATISFACTION SURVEY 2006

TNS Lanka (Pvt) Ltd., the local subsidiary of a global market research agency, conducted this survey among 1,200 customers in the Personal Banking and Small & Medium Business segments drawn from Outstation Branches.

Results of the External Customer Satisfaction Survey

Overall Customer Satisfaction Index/Score (Out of a maximum of 120) 89
Customer Satisfaction Index/Score for Personal Banking Customers 81
Customer Satisfaction Index/Score for Small & Medium Business Customers 97

Other key findings of the Survey

<table>
<thead>
<tr>
<th>Personal Banking Segment</th>
<th>Small &amp; Medium Business Segment</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Strengths</strong></td>
<td><strong>Strengths</strong></td>
</tr>
<tr>
<td>• Staff Courtesy and Quality of Customer-Staff Interaction</td>
<td>• Staff Courtesy and Quality of Customer-Staff Interaction</td>
</tr>
<tr>
<td>• ATM Services</td>
<td>• Security for Advances (Too Stringent &amp; Complex) and Delivery Delays</td>
</tr>
<tr>
<td>• General Image of the Bank as a Modern and Trustworthy Partner</td>
<td>• Professionalism of Branch Staff/Officers - Not up to Customer Expectations</td>
</tr>
<tr>
<td><strong>Weaknesses</strong></td>
<td><strong>Weaknesses</strong></td>
</tr>
<tr>
<td>• Delay in Credit Delivery Processes</td>
<td>• Unattractive Lending Rates</td>
</tr>
<tr>
<td>• Response/Delivery Times(Other Products) - Not up to Expectations</td>
<td>• Security for Advances (Too Stringent &amp; Complex) and Delivery Delays</td>
</tr>
<tr>
<td>- Issue of Cheque Books</td>
<td>• Professionalism of Branch Staff/Officers - Not up to Customer Expectations</td>
</tr>
<tr>
<td>- Issue of Cashline Cards</td>
<td>• Inadequacies in the Technology Driven Delivery/Distribution Processes including ATMs</td>
</tr>
<tr>
<td>- Despatch of Current Account Statements</td>
<td>• Business Hours (Need to be Extended)</td>
</tr>
<tr>
<td>• Unattractive Interest Rates for Savings</td>
<td></td>
</tr>
<tr>
<td>• Inadequate Customer Information (Regarding Products and Services)</td>
<td></td>
</tr>
</tbody>
</table>

Action taken to address weaknesses in Service Delivery

• A major upgrade of the ATM operations is under way with network expansion and service enhancement.
• Continuous staff training is being given top priority to enhance professional standards. About 15 training programs were conducted during the year on various aspects of credit for different categories of staff.
• Weekend banking has commenced at about 30 branches (including Colombo branches) to provide extended time for customer transactions.
• Action is being taken to improve parking facilities and other service logistics at branches.
  - Parking facility has been improved at three Customer Service Centres as a result of re-locations done during the year,
  - Two of the three new Customer Service Centres opened during the year have been provided with adequate parking facility,
  - Most of the new Customer Service Centres to be opened during 2007 will have adequate parking facility. This aspect is an important consideration now in identifying buildings/sites for new branches.
USING THE TECHNOLOGY ADVANTAGE IN A QUEST TO EXPAND PRESENCE

HNB has continued to use the advantages of our IT platforms to deliver superior services to our customers, which essentially reach out to all parts of the country.

The entire ATM network is being technologically enhanced and the implementation of this project is to be fast-tracked next year. 30 ATMs have already been upgraded. The daily cash withdrawal limit has been increased from Rs. 20,000 to Rs. 40,000 and third party fund transfers have also been introduced. We also expanded our ATM delivery network with two additional ATMs which takes our total ATM strength to 145 machines under the umbrella of the ‘Anywhere Banking Facility’ which we proudly espouse.

INTERNET BANKING

<table>
<thead>
<tr>
<th></th>
<th>Total number of customers - end of 2006</th>
<th>Total number of customers - end of 2005</th>
<th>Growth over last year</th>
<th>New services this year</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total number of customers - end of 2006</td>
<td>5,191</td>
<td></td>
<td></td>
<td>Bill payments for HNB Assurance, Mobitel, Dialog, Lanka Bell, CEB and Celltel</td>
</tr>
<tr>
<td>Total number of customers - end of 2005</td>
<td>2,447</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Growth over last year</td>
<td></td>
<td></td>
<td>112%</td>
<td></td>
</tr>
</tbody>
</table>

VALUED ADDED SERVICES – SMS BANKING

This is a partnership that was implemented with Mobitel for value added services including bill payments, pre-paid payments, credit card payments and fund transfers. Similar arrangements are being negotiated with Dialog Telekom for implementation in 2007.

EXPANDING PRESENCE

Accessibility to our products and services is a priority in our service delivery channels and expanding our presence remain at the top of the agenda. Our presence in all nine provinces enables us to reach out to even the most difficult parts of the country ensuring that our services are available equally to all strata of society. Three new Customer Service Centres were opened this year bringing the total number to 151. Our total ATMs now stand at 145 with the two new installations this year. 2007 will see approximately 15 new Customer Service Centres established and about 80 new ATMs installed either at new locations or as replacements to further augment our network expansion.

Awareness continues to be created through our network of 151 Customer Service Centres. A dedicated team of field staff of 109 Agri Officers and Gami Pubuduwa Upadeshakas assist with our activities in the rural areas especially in micro finance and micro savings.

Mobile campaigns were also carried out regularly this year through the Mobile Units via the nine Regional Offices. The new HNB Internet Portal, the Virtual Branch, SMS Banking for alerts on products, interest and exchange rates, direct mailers, leaflets, posters, brochures, banners, customized envelopes and extensive advertising in the mass media and promotional campaigns have also enabled customer information and awareness to be extensively and effectively cascaded. The ATMs too are being utilized for product information to be displayed with posters at the locations and some of the newly installed ATMs themselves providing customer information and advertising options.
Four e-Banking kiosks were installed during the year at specially selected locations to enable customers to perform their internet banking functions and access information on products and services at their convenience.

A successful initiative begun last year, Weekend Banking was extended to 15 more branches in Colombo and the outstations with a total of 30 branches now open for weekend banking.

**OUR OVERSEAS PRESENCE**

We continue to augment our presence overseas in order to ensure that the essential Sri Lankan spirit is permeated to those living overseas. Having already established Representative Offices in both Chennai and Karachi to facilitate regional trading activities and having HNB team members positioned in Abu Dhabi, Dubai, Bahrain and Kuwait in order to assist Sri Lankan expatriates working in those countries, this year we initiated the following to continue extending our services overseas:

- Launched Tele Money, a web-based remittance product of the Arab National Bank of Saudi Arabia and Fast Cash, also a web-based remittance product of the Currency Exchange Corporation, UK to promote remittances from UK and Australia.
- Signed Remittance Agreements with a leading banking Group with 1,172 branches to facilitate remittances from Italy to Sri Lanka.
- Also signed four other Remittance Agreements with Exchange Houses and Banks in the Middle East to facilitate easy remittances from the Middle East to Sri Lanka.

**GIVING MORE**

Our team remains constantly aware of the necessity to stay ahead in a challenging environment and is in constant pursuit of innovativeness in conceptualising, creating and imparting service excellence. To aid this single minded philosophy of being a leader, our training and development processes incorporate programmes that emphasize customer service as an essential ingredient to the Bank’s sustainable success. As an example, this emphasis led to an unprecedented 66 special training programmes being conducted specifically on customer service and its rudiments, with other training programmes also incorporating some modules that detail the concept of service excellence.

**DEVELOPING STUDENT BANKERS**

One of our most significant achievements has been the inculcation of the savings culture among students through Singithi Accounts which gives them an overarching knowledge of rudiments of banking as they are also encouraged to manage their own accounts, create awareness among other students and participate in banking activities. This spearheaded the formation of a Student Bankers’ Association in 2001 comprising Student Managers from 32 Colombo and suburban schools. Under the aegis of HNB, the Student Bankers have earmarked community projects over the years while also fostering the spirit of teamwork through sports and extra curricular activities. This year, the Association organised a six-a-side Cricket Tournament to foster fellowship among its members with eight schools participating and the unique feature of a women’s cricket match added to the lustre and appeal of the event. Members of the Sri Lanka Cricket Team were present at the tournament to make presentations to the winning teams and sign autographs.
**HNB PATHUM VIMANA**
Conducted continuously for 14 years is yet another example of successful customer relations. HNB Pathum Vimana is a unique rewards programme that has seen customers win houses, luxury cars, and a whole range of durables and cash. This year, HNB Pathum Vimana broke new ground with its launch as a TV Game Show, with 22 Pathum Vimana Account Holders picked at random monthly and invited to compete in the Show, where each winner is presented with a cash prize ranging from Rs 10,000 to Rs 200,000.

**EQUAL ACCESS FOR ALL**
We also remain conscious of granting equal access to anyone who visits the Bank and are in the process of making our branches accessible to all and empathically welcoming those customers requiring some assistance with mobility to conduct their banking transactions with the minimum hassle. This year, we reconstructed ten more branches to meet with this ideal and aim to extend this concept to 34 more branches next year.

**CUSTOMER EDUCATION**
Developing/improving customer knowledge, awareness and skills were further encouraged this year with the organization of:

- A special presentation on treasury products to about 50 corporate customers by the Treasury Division.
- An international trade seminar styled as 'International Trade – The Future' for about 125 corporate clients.
- A Customer Awareness Programme/Workshop by the Development Banking Division for about 60 small entrepreneurs in Kalutara, aimed at enhancing the technical knowledge of these entrepreneurs.
- Student Banking Convention 2006 - With a view to enhance the information technology skills of school students who are exposed to and familiar with the banking function, the HNB Student Bankers’ Association organized a seminar for three hundred students. Chosen as they indicated an interest in the Banking industry and functioned as Student Managers attached to Singithi Savings Units in schools in and around Colombo and its suburbs, the focus of the seminar was to create further interest in the sector. The seminar consisted of four sessions conducted by IT specialists who spoke on the importance of IT in the modern world. Recognizing a possible dearth in banking expertise in the future, the Student Bankers’ Association proactively organizes similar events to enhance the attractiveness of the industry to future career seekers. The Association has been functioning for over five years and has been instrumental in identifying and formulating a series of training and development programs for the benefit of the student population of Sri Lanka.
COMPLAINTS HANDLING
A systematic and vibrant complaints handling process is implemented under the Financial Ombudsman Scheme and it is handled by the specially dedicated Complaints Handling Unit established at Head Office. The Unit has resolved 134 complaints this year, while 8 complaints referred to the Independent Financial Ombudsman have also been resolved satisfactorily. Most of the complaints received from customers related to the following:

• Loans related issues - delays and refusals
• Cheque returns and other issues arising from the newly introduced Cheque Imaging and Truncation System
• ATM related issues/problems
• Customer handling and counter service

CUSTOMER SAFETY & SECURITY
HNB follows stringent guidelines on safety requirements at all our Customer Service Centres based island wide.

Branches which are specially designed with safety being a priority are equipped with appropriate fire fighting devices and other safety equipment. Fire drills form a part of the Training & Development calendar with all employees thoroughly conversant to cope in case of emergencies.

Specially trained armed security guards are also in attendance during business hours at 107 of the 151 Customer Service Centres and all Customer Service Centres have 24 hour security provided by professional security firms. All on-site ATMs are covered by CCTV cameras.

SMS Alerts give customers the unique added benefit of instant information on credit card transactions. This is a free service already enjoyed by about 7,500 of our card holders. Firewalls, passwords, PIN numbers and internal information access controls are also in place to ensure exceptional IT security.

Funds lying to the credit of dormant or deceased accounts are especially protected with the segregation of such accounts and appropriate restrictions placed on the reactivation process. The account mandates of these accounts are secured in the vaults of the Bank under the custody of the Branch Manager.

IGNITING THE ENTREPRENEURIAL SPARK OF ECONOMICALLY CHALLENGED CUSTOMERS
HNB’s flagship micro finance programme, Gami Pubuduwa continues to be the lifeline in reawakening villages towards development and sustainability. Using both social and commercial dimensions in this unique programme, Gami Pubuduwa empowers poor rural communities to embark on entrepreneurial ventures, funding and advising these entrepreneurs to ensure sustainability of the ventures. Corporate Management undertook a field tour to obtain first hand experience of the rural entrepreneurs under the Gami Pubuduwa scheme in the Dambulla and Sigiriya areas.
MICRO INSURANCE WITH HNB ASSURANCE
A unique micro insurance product was launched this year in partnership with our subsidiary HNB Assurance, the first of its kind in Sri Lanka that covers both life and the loan liability of the borrower. All micro entrepreneurs under the Gami Pubuduwa umbrella are eligible. One of the most notable features of the insurance scheme is that the Bank bears 50% of the single premium and in the event of death or total disability, HNB Assurance will settle the outstanding liability on the loan to the Bank, while also paying the sum assured to the next of kin of the customer.

More information on sustainable Gami Pubuduwa programmes is detailed under Community Relations.

Mr. Upali Jayalal Fernando, a customer of HNB Moratumulla Branch, lost his entire family, except his 8-year-old daughter to the train catastrophe during the tsunami. HNB, which has always instilled the caring partner in progress tenet to its stakeholders, wrote off all outstanding loans which would otherwise have been a financial burden on the customer’s family, while also giving protection to the orphaned daughter by reverting the title of the mortgaged property in her name.
Our people continue to be the nucleus to our existence and sustainable success, ensuring that continuous improvement, upward mobility, creativity and innovation become the formative trusses for the umbrella of customer service excellence which is inbuilt at the very core of our operations. The upwardly mobile facet is augmented by:

- Creating a culture and an understanding that emphasizes individual and organizational growth which includes continuous professional development, acquisition of skills and capabilities and managing attitudinal and transformational change.
- Implementing a measurement based performance driven culture with rewards and career progress linked to performance.
- Creating a sense of ownership to inspire individual career aspirations towards alignment with organizational vision with a participatory bottom-up management framework aiding the process. The SEARCH suggestion scheme, Quality Circles, In-house publications and Cross Functional committees representing the team at all hierarchical levels give impetus to this.
- Continuous training and development on and off the job is assisted by comprehensive skills inventory and regular performance appraisals which identifies strengths, weaknesses and avenues to bridge gaps.
- Harnessing a cordial relationship through harmonious industrial relations and assisting team members during crisis.
- Identifying the Best Branch, region wise, to support the concepts of leadership, teamwork and high productivity.
Believing strongly that an united and harmonious working environment will always herald better productivity and higher performance, we have striven to inculcate the ‘Hatna Family’ concept among our team members. The Share Option Scheme complements the ownership principle and ensures a sense of belonging.

**KEY INDICATORS THAT ILLUSTRATE MEETING OF HR GOALS**

- A competent, committed and contented workforce demonstrated by the Employee Satisfaction Survey carried out in partnership with Ma Foi this year.
- A professional target-driven team equipped with the required competencies, skills and knowledge to optimize their performance.
- HNB is considered one of the preferred employers in the financial services industry in Sri Lanka.
- Fast career progression exemplified by a relatively young managerial team.
- Employee turnover at senior management and corporate management level remaining at a low 1.67%, indicative of the Bank’s ability to retain these specialist jobs and meet career goals and aspirations.
- No industrial disputes for the last six years due to timely signing of Collective Agreements and remuneration and rewards remaining above market rates.
- Remaining mindful of all ILO conventions and maintaining internationally accepted labour standards.
- Emphasis on creating an enabling culture for the differently abled.
- An equal opportunity employer that works on stringent meritocracy rules.

**EMPLOYEE SATISFACTION SURVEY**

![Employee Satisfaction Survey Graphs](image-url)
RECRUITMENT PROCESS
Bestowed with the label of being a preferred employer in the financial services industry, HNB always espouses the credo of being an equal opportunity employer whose recruitment, promotion, rewards and remuneration features remain transparent and built on meritocracy. At executive level, we strive to build an internal succession concept identifying promising personnel from our branch network.
TRAINING & DEVELOPMENT

Creating a learning culture on the foundations of knowledge, skills and competence, enhances our ability to create a motivated team which we firmly believe is necessary for us to meet our determined goals. Training and Development therefore, remain an integral factor to personal, professional and corporate growth. The in-house training plan, formulated by the HNB Training Centre is designed in accordance with the Training Needs Analysis which is compiled based on information, data and recommendations received through performance appraisals and questionnaires filled in by heads of department and regional managers.

The overarching factors integrated into the HR training plan include:

- The need to train and develop a team aligned to the vision and mission of the Bank,
- Strategic focus given to business growth, cost management, HR, productivity, control and compliance, portfolio quality and customer care,
- The need to develop managerial competence among executives and supervisory staff,
- Continuous training on service quality and achieving customer service excellence levels,
- Create a marketing and selling culture,
- Understand the importance of self management in realizing individual and organizational objectives,
- Pursue multi-skilling to support succession planning and job rotation.

More trainers were also mobilized during the year to implement and achieve the far reaching goals of the Training Plan, which included a total of 172 internal and external training workshops, retreats and programmes covering a total of 3789 team members over 2432 training hours which was supported by a comprehensive e-learning system. The main T&D programmes conducted by HR this year were focused around the subject areas of Management/Leadership, Operations, Credit, International, Skills Development, Information Technology, Self Development and Customer Care. Stepping up the emphasis on customer care, we conducted an unprecedented 22 programmes within the branch network on customer service this year and in complementing the holistic features of our training, also held a series of programmes on Personal Grooming and Image Building in 15 branches.

<table>
<thead>
<tr>
<th>Category</th>
<th>No of staff trained</th>
</tr>
</thead>
<tbody>
<tr>
<td>Corporate Management</td>
<td>22</td>
</tr>
<tr>
<td>Senior Management</td>
<td>110</td>
</tr>
<tr>
<td>Management</td>
<td>68</td>
</tr>
<tr>
<td>Executives</td>
<td>452</td>
</tr>
<tr>
<td>Junior Executives</td>
<td>1084</td>
</tr>
<tr>
<td>Banking Assistants</td>
<td>1226</td>
</tr>
<tr>
<td>GPUs</td>
<td>188</td>
</tr>
<tr>
<td>Stenos, Typists</td>
<td>199</td>
</tr>
<tr>
<td>Confidential Secretaries</td>
<td>30</td>
</tr>
<tr>
<td>Trainees</td>
<td>247</td>
</tr>
<tr>
<td>Support Staff</td>
<td>163</td>
</tr>
</tbody>
</table>

One of the most significant features in the programmes conducted by our Training Centre this year was the first ever international training programme in Male for 40 staff of the Bank of Maldives, a definite testimony that our training methodologies and processes are being recognized beyond the shores of Sri Lanka.
INCORPORATING IT INTO THE HR PROCESS
To further facilitate our HR goals, we launched a number of initiatives including an in-house developed Training Management System to aid training for self development and increase productivity within the Training Centre.

A new interface will be introduced into our e-learning modules next year linking all 150 branches online. The interface aids faster access and a host of new features to enable location based training with interactive modules. Comprehensive details of all courses, chat rooms, Q&A sessions and mock examinations for preparation are currently included in the feature and in the future, online examinations and virtual classrooms will also be facilitated. We already have 2,700 team members registered online for e-learning facilities with daily usage a commendable 200 hits which is an indicator of the success in using IT as a platform to enhance knowledge development.

This year, we enabled all executive staff to have online facilities to aid performance management, in order to give them first hand insight into the training required for their job profile, their current skill
status, requirements for the future and training programmes currently in place. These details are also available to HR in the process of streamlining training needs efficiently and speedily.

Performance evaluation is also being performed online from this year. This brings transparency into the evaluation process. All Executives are rated on merit based on individual Balanced Scorecards and core competencies. A performance accountable system ensures that qualitative results and target based evaluations are linked and balanced. Target achievements focus on financial rewards and promotions while the evaluation of core competencies forms the basis for personal development reviews leading to skill and knowledge development and the competencies available for particular job roles, job rotation, job changes etc.

BRINGING THE HATNA FAMILY TOGETHER
On the firm belief that contented people make a happy and productive workplace, the Bank continues to have annual and periodic events that bring the entire team and their families together. Hence, while the Bank strives to become a knowledge centre for its Team to improve and develop professionally, we also encourage participation in extracurricular activities to ensure a holistic people development aspect into the workplace.

A healthy workforce remains a priority and the Bank has now opened the facilities of its Gymnasium within the Head Office building and also conducts regular health awareness programmes.

SCHOLARSHIP SCHEME FOR HNB EMPLOYEES’ CHILDREN
This year the Bank finalized the introduction of a scholarship scheme for children of employees who have excelled at district level at the GCE A/level examination. The Bank has provided an investment of Rs 25 million initially for this purpose, with up to 15 scholarships to be disbursed annually under this scheme, to enable University education.

FELICITATING BEST RESULTS
For the first time, an employee’s child Master B M K Fernando, obtained an all island ranking with the second highest marks at the GCE O/level examination 2005. A modest ceremony was held at the MD/CEO’s office in June 2006 to felicitate the student with a gift of Rs 50,000 credited to his Singithi Account.

EMPLOYEE AND FAMILY EVENTS
- Sports fiesta covering the regions
- Bhakthi Gee
- Christmas Carols and Christmas Party
- 25 year service awards

STAFF STRENGTH
- Male (65%)
- Female (35%)
WORK / LIFE BALANCE - OUR ACHIEVEMENTS THIS YEAR

CRICKET
• Triple Champions in Mercantile Cricket.
• HNB A Team toured Singapore and won the trophy against Lanka Lions SC.
• Organised Inter-bank six-a-side Cricket tournament in July.

SOCCER
• Triple Champions in Mercantile soccer winning the Mercantile Knockout A Division, Mercantile Seven-a-side Championship and Mercantile League A Division Championship.

NETBALL
• National Champions in Netball for the 11th consecutive year, we also won several Championships in Netball in 2006.
  • Champions in the Open Club Netball Tournament.
  • Winners in the Deluxe Ronuk Trophy A Division.
  • Winners of the Mercantile Netball Challenge Trophy.

ATHLETICS
• Champions in the Novices category, First Runner Up at the Overall Veterans Event and Second Runner Up Overall at the Athletics Meet 2006.
• Sponsored Dhammika Menike whose Sri Lankan records in the 800m and 1500m set in 1992 remain unbroken, for the Thailand Open Master Athletic Championship in March 2006. She won a gold medal in the 800m and a silver in the 1,500 m 35 to 40 age group. She also set a new record in the 400m at the National Master Athletic Championships in the same age group.
• Sponsored Dulal Dalpathado to the Asian Master Athletics Championships 2006 held in Bangalore in November. He won a Gold Medal for the High Jump event in the 50 to 55 age group.

BADMINTON
• 10th South Asian Games – Two team members won Bronze Medals in the individual event and a Silver medal in Ladies Doubles with one also having participated in the Indian Satellite Championship.

BASKETBALL
• Champions in the Mercantile five-a-side tournament.

HOCKEY
• League Tournament champions in Mercantile Hockey Association Tournament.
• Seven a side tournament champions in Mercantile Hockey Association Tournament.
• Bronze medals won by team members at the South Asian Games 2006.

TOASTMASTERS’ SPECIAL
Two of our team members now hold key positions in the main body of the Toastmasters’ Club with HNB having begun a Toastmasters’ Club three years ago, a testimony to the success of this initiative of setting up the club.
FUTURE PLANS
We aim to leverage on the human development initiatives we have already implemented to ensure the continued development of individuals within a performance oriented culture. Knowledge, competency building and empowerment will be key thrust areas that human resources will link to business. We remain acutely conscious of the need to extract the best from our team and impress upon them the role they have to play in sustaining the business. This can only be achieved through a thorough understanding of the organization they work in.
The year has seen HNB create new history! The Bank has been judged on its adherence to global standards, prevalent industry standards and conformance to stringent governance diktats. The Bank has displayed its resilience in a volatile economic environment through astute decision making and sustainable leadership, which translates into long term partnerships with our investors who are confident of the stability of the organisation and the transparency and accountability that form the firm foundation of the Bank.

**BRACKEN AWARD – SRI LANKAN BANK OF THE YEAR 2006**

Adjudged by the prestigious publication, 'The Banker’, at a glittering ceremony held in London in November this year, HNB accepted the coveted Bracken Award as the Bank of the Year 2006 for Sri Lanka. Assessed on stringent criteria from among the leading banks operating in Sri Lanka and overseas including incorporating performance indicators, qualitative achievements and strategic business initiatives, HNB has also proven to have broken new grounds in efficiencies, effectiveness and profitability.

**ANNUAL REPORT AWARDS 2006**

HNB was placed 2nd Runner Up in the Banking Institutions Sector category at the Annual Report Awards 2006 organised by the Institute of Chartered Accountants of Sri Lanka.
HNB went up two positions in the LMD 50 Leaderboard 2005/6 Ranking in the results published in the LMD December 2006 issue, akin to Sri Lanka’s version of THE FORTUNE 500. HNB also had the distinction of leading the banking sector, retaining its leading listed bank tag for the second consecutive year.

In addition, in the December 2005 issue of LMD, in a survey conducted by Sting Consultants and Brand Finance, HNB was ranked as the No 1 Brand in the financial sector and the third leading brand in the country with top of the mind recall.

HNB was also ranked amongst Top 10 of the most reputed entities in Sri Lanka for 2006 by LMD.

A proven track record of tangible and sustainable growth has seen investors enjoy consistency, stability and a certain sense of innovative and incisive thinking for the future which has held HNB in good stead to seek opportunities to enhance growth. Focused on building and strengthening investor relations to ensure that HNB would continuously add value to investment while also minimizing risk and adhering to stringent governance principles, HNB strives to create a relationship of mutual trust, strong ethics and values and consistent growth.

Thus being acknowledged by the industry and others with accolades including being named among the Top Ten Leaderboard of the LMD 50, being acknowledged internationally by The Banker as the Bank of the Year 2006 in Sri Lanka and the HNB Brand being ranked first in the financial sector and third as the leading brand in the country according to Brand Finance UK and LMD Sri Lanka have certainly been added imperatives that would encourage investors to perceive HNB as a bank with a robust investment potential. With profitability rising significantly, improved capital formation supported by better asset quality and increased ROA of 18% year on year, Fitch Ratings upgraded HNB’s national long term rating to A+ (LKA) this year.

HNB’s path of progress imbibed with its good governance principles, values and ethics were further acknowledged this year when the CEO was invited to Chair the Technical Session of Financial Sector Reforms at the Asian Banks’ Association (ABA) Convention in Taipei. The ABA includes a membership of 120 leading banks from the Asia Pacific Region, with this year’s convention having the participation of over 200 senior bankers from South, South East and East Asia and presentations from eminent regulators and industry practitioners.
ICICI “INDIA UNLIMITED” ANNUAL CONFERENCE
HNB was invited for two successive years to profile the Bank at ICICI’s annual profiling of top corporates from India and other South Asian countries. At the annual conference, some of the leading fund managers from the region attend to get an insight view on the corporate. The event is attended by such prominent personalities as Marc Faber, Central Bank Governors, Finance Ministers and CEOs of top corporates in India. HNB is the only Sri Lankan bank to be profiled at the conference. This stems from the special relationship HNB and ICICI Securities fostered three years ago.

SHARING THE EXPERIENCE OF MICROFINANCING IN GERMANY
HNB strengthened its ties with Germany in 2006. At the invitation of the Savings Banks Foundation for International Cooperation (SBFIC), the HNB management team took part in a ten day visit to Germany to share the experience of micro financing in Sri Lanka. The co-operation between the two institutions was increased beyond tsunami reconstruction work. The visit enabled HNB to develop links to further strengthen the micro finance sector, develop a partnership for remittance from EU member countries, learn the latest trends in the IT industry and share resource persons on specific training programs.

HNB first entered into a partnership with SBFIC in August 2005. The initial goal was to assist micro and small entrepreneurs by providing financial assistance to help reconstruct their businesses and uplift economic/employment activities in areas affected by the tsunami.

To date, the Bank has provided financial assistance to 1,907 entrepreneurs amounting to Rs 469 million. As a result of this initiative, approximately 5,000 new employment opportunities were created and 7,000 families (directly and indirectly) affected by the tsunami benefited from the partnership micro finance program.

HNB SHARELINE CARD – AN ADDITIONAL BENEFIT TO SHAREHOLDERS
HNB’s unique Shareline Card to all shareholders enables numerous benefits that would complement the returns our shareholders gain from the Bank. HNB Shareline exempts cardholders from annual and registration fees for local and Gold Mastercards and half yearly fees on current accounts. The card also ensures VIP treatment at all HNB branches and easy access to front office services. In addition, commission is not charged for the issue of travelers cheques, drafts and standing orders and no internal documentation fees will be levied for facilities above Rs 1 million.
INDICATORS THAT DEPICT THE SUSTAINED GROWTH OF HNB

<table>
<thead>
<tr>
<th></th>
<th>2002</th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
</tr>
</thead>
<tbody>
<tr>
<td>EPS</td>
<td>8.00</td>
<td>13.69</td>
<td>12.51</td>
<td>15.09</td>
<td>18.86</td>
</tr>
<tr>
<td>Dividend yield (%) - Voting</td>
<td>3.80</td>
<td>5.80</td>
<td>6.14</td>
<td>3.56</td>
<td>3.21</td>
</tr>
<tr>
<td>Dividend yield (%) - Non Voting</td>
<td>6.38</td>
<td>10.88</td>
<td>10.69</td>
<td>9.64</td>
<td>7.14</td>
</tr>
<tr>
<td>Asset Growth (year on year %)</td>
<td>16.45</td>
<td>15.50</td>
<td>14.59</td>
<td>8.66</td>
<td>18.32</td>
</tr>
<tr>
<td>Holding Period Return - Voting (%)**</td>
<td>73.46</td>
<td>(7.59)</td>
<td>(10.29)</td>
<td>104.39</td>
<td>42.89</td>
</tr>
<tr>
<td>Holding Period Return - Non Voting (%)**</td>
<td>52.78</td>
<td>(13.30)</td>
<td>-</td>
<td>38.93</td>
<td>80.72</td>
</tr>
<tr>
<td>Operating Cost - Efficiency Ratio (%)</td>
<td>72.80</td>
<td>63.20</td>
<td>70.35</td>
<td>62.29</td>
<td>66.11</td>
</tr>
<tr>
<td>Share Price - Voting</td>
<td>79.00</td>
<td>69.00</td>
<td>57.00</td>
<td>112.50</td>
<td>155.75</td>
</tr>
<tr>
<td>Share Price - Non Voting</td>
<td>47.00</td>
<td>36.75</td>
<td>32.75</td>
<td>41.50</td>
<td>70.00</td>
</tr>
<tr>
<td>Dividends</td>
<td>30%</td>
<td>40%</td>
<td>35%</td>
<td>40%</td>
<td>50%*</td>
</tr>
</tbody>
</table>

* Inclusive of final dividends of 25% for year 2006 (To be approved at the AGM & payable on 10th April 2007).
** No. of shares in year 2000 is assumed to be 1000

<table>
<thead>
<tr>
<th>2004</th>
<th>2005</th>
<th>2006</th>
</tr>
</thead>
<tbody>
<tr>
<td>Market Value Addition (Rs. Bn.)***</td>
<td>(4.1)</td>
<td>0.2</td>
</tr>
<tr>
<td>Economic Value Addition (Rs. Bn.)</td>
<td>(0.7)</td>
<td>(0.6)</td>
</tr>
</tbody>
</table>

*** For market value addition the share price of GDR is considered as equivalent to the local market price of shares.

[Graphs of Dividend, Share Price, Earnings Per Share, and Share Price & Market Capitalization]
HNB has always emphasized on long lasting partnerships among all stakeholders and valued business partners too come under this umbrella. We believe that our platform should be driven on a qualitative relationship that espouses values, ethics, integrity, transparency in processes, value for money and cohesive but open dialogue. We have striven to instill the tenets of quality products and services being imparted from our suppliers through constant interaction and relationship building. We firmly believe that being a leader in the banking industry in Sri Lanka, examples and benchmarks must be set by us for others to emulate and have emphasized the need for our suppliers too to work together with us on this strategy.

All suppliers are required to register with the Bank, encouraging micro, small and medium organizations also to apply.

The entire selection process remains absolutely transparent with each step documented and available for inspection at any time.

The selection process for procurements above Rs. 100,000/- is by tender and entails the following:
- Tenders are called for on a cyclical basis to enable a fair and just chance for all suppliers to tender,
- Procurement procedures are conducted according to a streamlined framework which remains transparent right throughout the process,
- The primary criteria for awarding the tender is tabulated on the quality of the product and the price quoted.
Prior to supply of goods stringent verification procedures including supplier audits are implemented at the time of registration. On delivery, the following is done:

- Physical verification of items delivered,
- Sample testing of the products,
- Quality of paper based supplies tested with a GSM machine,
- Inspection of large suppliers’ factory or source.

These procedures have ensured that the quality of products supplied to HNB remains superior and that in the event of the products not meeting the stringent quality standards that HNB promotes, suppliers are required to rethink their quality strategies and processes, which have resulted in the subsequent improvement of the end product.
Community relations are an integral aspect of taking the concept of sustainability to a higher realm. Our team is aware of the importance of building relationships among the communities we operate in, the impact our decisions will have on the community and hence hedge our community projects towards the betterment and sustainability of those communities, rather than on a philanthropic course of action. The primary platform that HNB builds its community relations is on sustainability of the community.

**MICRO FINANCE AS A SUSTAINABLE TOOL**

**SAVINGS BANKS’ FOUNDATION FOR INTERNATIONAL CO-OPERATION (SBFIC)**

HNB, through its partnership with SBFIC, which is the advisory body to one of the largest financial groups worldwide housing an umbrella of 489 Savings Bank Groups and joint institutions, assists micro and small entrepreneurs directly or indirectly affected by the tsunami to reposition their livelihoods and reconstruct their businesses. Joint awareness programmes were conducted by HNB and SBFIC aimed at giving more impetus for micro entrepreneurs to re-establish themselves in a sustainable vocation. Corporate management and a group of journalists too visited the sites to gain first hand information.

- Initial refinance funding fully utilised within one year: Euro 2 million
- Second partnership agreement in progress: Euro 3 million
- Directly financed: 1,907 projects
- Existing portfolio: Rs. 451 million
- New employment opportunities created: 5,000
- Families benefited: 7,000 approx.
The Distribution of micro finance projects funded through SBFIC are given below:

<table>
<thead>
<tr>
<th>Category</th>
<th>No of Loans</th>
<th>Amount (Rs Mn)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Agricultural</td>
<td>345</td>
<td>62.4</td>
</tr>
<tr>
<td>Fisheries</td>
<td>178</td>
<td>40.6</td>
</tr>
<tr>
<td>Animal products</td>
<td>113</td>
<td>10.4</td>
</tr>
<tr>
<td>Civil engineering</td>
<td>24</td>
<td>8.6</td>
</tr>
<tr>
<td>Food processing</td>
<td>142</td>
<td>29.9</td>
</tr>
<tr>
<td>Hotel &amp; Catering</td>
<td>47</td>
<td>22.3</td>
</tr>
<tr>
<td>Light engineering</td>
<td>43</td>
<td>11.6</td>
</tr>
<tr>
<td>Manufacturing</td>
<td>252</td>
<td>65.5</td>
</tr>
<tr>
<td>Medical service</td>
<td>12</td>
<td>5.9</td>
</tr>
<tr>
<td>Miscellaneous</td>
<td>272</td>
<td>83.7</td>
</tr>
<tr>
<td>Textile</td>
<td>94</td>
<td>25.0</td>
</tr>
<tr>
<td>Trading</td>
<td>248</td>
<td>68.2</td>
</tr>
<tr>
<td>Transport</td>
<td>137</td>
<td>35.1</td>
</tr>
</tbody>
</table>

GAMI PUBUDUWA

As mentioned earlier, the unique Gami Pubuduwa Micro Finance Scheme, which completes 17 years in 2006, emphasizes the fundamentals of sustainability, harnessing the entrepreneurial spirit of poverty stricken villagers and empowering them towards their own development and thereby their own communities. Gami Pubuduwa comes under HNB’s Micro Finance Banking Scheme which essentially began in 1973 as a rural village upliftment programme and migrated to the flagship programme of Gami Pubuduwa in 1989.

Total Number of Projects financed - cumulative 65,000
Total Exposure Rs 3.5 billion
Existing Portfolio Rs. 1.84 billion
Existing portfolio caters to 14,812 projects
NPA Rate 4.9%

The objectives of Gami Pubuduwa include sustainable development of the rural community via funding, skills and community development, building sustainable relationships between HNB and the community, positively contributing towards micro sector sustainability through total financial solutions, technical advice and assistance and seeing contribution from the micro finance sector contributing to bottom line growth. The critical success factors in micro financing have been customer focus, innovation, teamwork, sustainability, outreach, cost effectiveness and risk management.
EMPOWERING WOMEN IN MUKKUTHODUWAWA – INVESTMENT RS 2.1 MILLION
On a unique initiative, the spouses of the fisherfolk in a poverty stricken village whose source of income decreases during the fishing off season, were granted micro loans through the Women’s Society. In a bid to supplement the meager fishing income affected drastically due to the vagaries of the weather, 39 women have been initially granted loans totalling Rs 2.1 million accommodated under the German Savings Bank Foundation for International Co-operation Credit Line. This is the fifth time that loans have been granted via this society to the women of this village.

CONSTRUCTION OF CAUSEWAY BRIDGE – INVESTMENT RS 200,000
Signifying the essence of teamwork, a group of Gami Pubuduwa Field Officers in association with the Avissawella branch volunteered cash, time and energy to construct a small causeway bridge for the benefit of the villagers in Hingurana, 20 kms to the interior of Deraniyagala town. With the village being essentially dependent on agriculture, a motorable road was a dire need to transport produce and the timely action by the team has been lauded by the villagers. The bridge was declared open in February 2006.

VALUE ADDITIONS TO INCREASE OUTREACH
Innovativeness being one of the key factors in the longevity and sustainability of the micro finance programme, HNB continues to conceive, craft and design products and services that will continuously add value to the existing product.

- Partnership with post offices in remote areas for credit delivery, repayment and savings mobilisation.
- Mobile ATMs in rural areas.
- Convenient migrant remittance channels through the Internet Money to Home system.
- Online loan approval system.

MADURU OYA REAWAKENED – INVESTMENT RS 6.1 MILLION
The poverty stricken fishing village of Maduru Oya in Padiyathalawa was completely ‘reawakened’ to celebrate the Shanthi Housing tenth anniversary. Having observed the abject poverty prevalent in the village due to the Bank’s involvement in the project ‘Help Protect Maduru Oya Inland Fishery Project’, the team was spurred into action to construct 28 homes and equip the fishermen with 70 fishing nets through micro finance support, construction of a library for the village school and a trading centre for the Maduru Oya fishing village. The reason for the dwindling income among the fishermen was due to the use of inappropriate fishing nets being used for fishing in the tank, which disrupted the breeding cycle and thus destroyed the inland fishery population. The Bank continues to monitor and impart technical advice to the fishermen to ensure that correct methodologies are used in their vocation for a sustainable balance of economy and environment. The library constructed for the village school is now a new building under the HNB Nena Pubuduwa 100 library project.

Utilising the funds usually allocated by HNB for the Wesak greeting advertisements in print media, a home was constructed for Y A Kusumalatha in Kirindiwela who has to look after her very ill mother, while living in abject poverty with no permanent income.
EMERGENCY RELIEF FOR REFUGEES – INVESTMENT RS 1 MILLION
HNB was the first bank to initiate a relief programme for refugees in the Mutur and Kinniya areas, left stranded and bereft due to resumed fighting in the North and East during August 2006. Essential items including dry rations, clothes, medicines and recreational items were transported to the refugee camps in Trincomalee and Kantale facilitated under the Bank’s Emergency Relief Operations operated by the HNB Customer Centres in the areas affected. This was a team effort that brought together the Hatna Family under the unifying umbrella of caring for fellow human beings, irrespective of caste, creed or religious beliefs.

RECONSTRUCTION OF THE TANK AND DEVELOPING THE VILLAGE – INVESTMENT RS 2 MILLION
The 431 underprivileged families in a farming community located in the small village of Mankadawela had to make ends meet with a neglected 300-year-old water tank. The tank is the lifeline for 250 acres of paddy. With the participation of team members closest to the area, the Anuradhapura Irrigation Engineer and the Department of Irrigation, HNB has now identified the need for the reconstruction and rehabilitation of the entire infrastructure of the tank which will also include four canals and three bathing areas. This will give a new lease of life to the deprived village and will direct them towards sustained livelihoods and better sanitation.

‘NANA PUBUDUWA’ – 100 SCHOOL LIBRARY PROJECT – INVESTMENT RS 8.1 MILLION
A laudable corporate social responsibility exercise being implemented on the platform of education, HNB’s 100 school library project initiated last year saw 94 libraries completed by December 2006. Schools, especially those in impoverished villages around the country, were identified and given this impetus of knowledge gaining ground. However, what must be noted is that the Bank has plans of exceeding the 100 libraries mark and continues identifying more schools in dire need, while investing in the existing libraries to ensure that a sustainable knowledge base remains vibrant and continuously updated with more books and other facilities and equipment being installed.
The sustainability of the planet depends on mankind’s actions – both positive and negative.Benchmarked as an industry leader, we firmly believe that we must set an example in creating the necessary awareness and in actioning initiatives that would spearhead the conservation and preservation of the environment.

**CLEARING INVASIVE SPECIES AT BUNDALA – INVESTMENT RS 560,000**

One of our most significant projects during the year has been a project that brought together the HNB Team and the Wildlife and Nature Protection Society of Sri Lanka. HNB funded the clearing of the five hectares of jungle which had been attacked by two invasive species in Bundala. The Bundala wetlands is known as one of the best wetlands in the world, comprising lagoons, a reservoir and shrub jungle which is home to numerous migrant birds, some of them from as far as Siberia and is also a nesting ground for very rare sea turtles. The Bundala wetlands is identified as a RAMSAR site of Southern Sri Lanka, an important waterfowl habitat and economic zone. The invasive species has brought with it habitat problems for the birds, animals, insects, amphibians and other beings within the Park. On completion of this project, HNB will undertake to continue the preservation of the environment within and surrounding the Bundala National Park, instigating a programme that would make the park a sanctuary for the abundant bird and insect life based within. The HNB Team intend to get personally involved in clearing the site in the future.
MADURU OYA FISHING VILLAGE PROJECT – INVESTMENT
RS 6.1 MILLION

It was brought to the attention of HNB that the fish population within the Maduru Oya tank at Padiyatalawa was fast dwindling as the fishing nets and equipment used by the less educated fishermen was completely destroying the breeding cycle and systematically eliminating the small fish. A two pronged approach by HNB to address the vocational problems of the fishermen and to sustainably develop the village were quickly put into action. While the village upliftment is detailed in the Community Relations section of this Report, HNB assisted the fishermen under the micro finance scheme with more appropriate fishing nets and gear to ensure that the fishery life inside the Maduru Oya tank will remain unharmed and continue to breed, while the fishermen will continue with their known livelihood uninterrupted.

ENERGY SAVING

HNB Head Office is considered the most energy efficient building in Colombo as it used revolutionary technology at the time of construction to ensure that environmentally friendly best practices are infused into everyday operations as much as possible. The energy saving features within the HNB Tower includes variable air volume units which control the supply of air temperature and the rate of airflow based on actual demand, fans connected to the air volume units are of variable speed type and a demand controlled ventilation system comprises an energy saving feature that controls the amount of outdoor air supplied based on carbon dioxide levels within the air conditioned space. The system is also designed to eliminate ‘Sick Building Syndrome’ risks by reducing odors, air pollutants, colds and virus causing germs. In addition, the air conditioning system is controlled and monitored by the EBI Excel 5000 Building Management System from Honeywell Singapore. General lighting too has energy efficient fluorescent fixtures and an intelligent microprocessor which senses the daylight component to provide only the necessary levels of illumination. The exterior of the building uses energy efficient high pressure sodium vapor, metal halide and compact fluorescent lamps.

In addition, energy saving measures have been introduced into the branches with team members urged to switch off unnecessary lights and energy saving computers being pursued as a future procurement imperative. We encourage our team members also to use the intranet and email facilities as often as possible to minimise the usage of paper in printing.
KEY PERFORMANCE INDICATORS

CUSTOMER RELATIONS

Customer Satisfaction Survey
The results of the Customer Satisfaction Survey conducted by both internal and external resources are given on pages 48 and 49.

Customer Care
Ten branches were reconstructed during the year to better facilitate the needs of those customers requiring some assistance with mobility.

Customer Education
Details of the number of customer awareness programs conducted during the year are given on page 53.

EMPLOYER RELATIONS

Employment - Gender Analysis of Staff

<table>
<thead>
<tr>
<th></th>
<th>Female</th>
<th>Male</th>
<th>Total</th>
<th>Female % of total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Corporate Management</td>
<td>5</td>
<td>15</td>
<td>20</td>
<td>25</td>
</tr>
<tr>
<td>Executives</td>
<td>143</td>
<td>410</td>
<td>553</td>
<td>26</td>
</tr>
<tr>
<td>Junior Executives</td>
<td>332</td>
<td>652</td>
<td>984</td>
<td>34</td>
</tr>
<tr>
<td>Banking Assistants</td>
<td>392</td>
<td>1042</td>
<td>1434</td>
<td>27</td>
</tr>
<tr>
<td>Trainees</td>
<td>200</td>
<td>230</td>
<td>430</td>
<td>46</td>
</tr>
<tr>
<td>Allied Grades</td>
<td>402</td>
<td>13</td>
<td>415</td>
<td>97</td>
</tr>
<tr>
<td>Support Staff</td>
<td>-</td>
<td>406</td>
<td>406</td>
<td>-</td>
</tr>
<tr>
<td>Contract Staff</td>
<td>11</td>
<td>34</td>
<td>45</td>
<td>24</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>1485</strong></td>
<td><strong>2802</strong></td>
<td><strong>4287</strong></td>
<td></td>
</tr>
</tbody>
</table>

Training and Education
Categorywise training details are given on pages 59 and 60.

SCHOLARSHIP SCHEME FOR CHILDREN OF HNB EMPLOYEES
Investment by HNB - Rs 25mn
Number of scholarships to be disbursed annually - 15

EMPLOYEE SATISFACTION SURVEY
Details are given on page 57.

EMPLOYEE TURNOVER
Employee turnover at Senior/Corporate Management levels - 1.67%.

INVESTOR RELATIONS
Indicators that depict the sustained growth of HNB are given on page 67.

BRAND STRENGTH
Bracken Award – Sri Lankan Bank of the year 2006
LMB 50 Leaderboard 2005/6 ranking - 4th
Fitch Rating - A+ (LKA)
SUPPLIER RELATIONS
Selection Process for Procurement

The selection of suppliers is by tender for procurements above the sum of Rs 100,000.

COMMUNITY RELATIONS
Assistance to Micro and Small Entrepreneurs:

Details of the assistance to micro and small entrepreneurs affected by the Tsunami are given on page 70.

Micro Financing Scheme – Gami Pubuduwa
The details are given on page 71.

School Library Project
Number of libraries completed by December 2006 - 94

Village Development
Developing a village - Mankadawela
Reconstruction of a water tank and village development - Rs 2 Mn

ENVIRONMENTAL RELATIONS
Preservation of the Environment

During the year the Bank had invested Rs 6.6 Mn on two projects:

- Clearing invasive species at Bundala - Rs 560,000
- Investment on the Maduru Oya Fishing Project - Rs 6.1Mn

Environment Risk Assessment for Project Financing

The Bank performs a high-level assessment of environmental risks when it lends to corporate and institutional customers for Special Projects based on the nature and locality.
ASSURANCE REPORT TO THE READERS OF THE SUSTAINABILITY REPORT 2006

INTRODUCTION
We have been engaged by Hatton National Bank Limited (HNB) to review the Sustainability Report 2006 (further referred to as The Report). The Report, including the identification of material issues, is the responsibility of HNB’s management. Our responsibility is to issue an assurance report on The Report.

CONTEXT AND SCOPE
In The Report HNB describes its efforts and progress in relation to Sustainability. Our engagement was designed to provide the readers of The Report with:

• reasonable assurance on whether:
  - the data on financial performance, as specified on page 67 of The Report are properly derived from financial statements of HNB for the year ended 31 December 2006;
  - limited assurance on whether:
    - the data on Key Performance Indicators for 2006 specified on pages 76 and 77 are fairly stated;
    - the other information in The Report is fairly stated.

‘Fairly stated’ means that the reported information properly reflects the information contained in the underlying sources such that it is consistent with the source information. Reasonable assurance is a higher level of assurance than limited assurance, which is reflected in the nature and depth of the work performed.

STANDARDS AND CRITERIA
We conducted our engagement in accordance with the Sri Lanka Auditing Practice Statement (SLAPS 3) applicable to review engagements, and the International Standard on Assurance Engagements (ISAE 3000): Assurance Engagements other than Audits or Reviews of Historical Financial Information, issued by the International Auditing and Assurance Standards Board. Amongst others, these standards require that:

• the assurance team members possess the specific knowledge, skills and professional competencies needed to understand and review the information in The Report;
• when providing limited assurance, which is a lower level than reasonable assurance, a negative form of conclusion is used.

There are no generally accepted standards for reporting sustainability performance. HNB applies its own internal sustainability reporting criteria, derived from Sustainability Reporting Guidelines of the Global Reporting Initiative and its stakeholder engagement process as detailed on page 44 of The Report.

CONSIDERATIONS AND LIMITATIONS
Environmental and social performance data are subject to inherent limitations given their nature and the methods used for determining, calculating and estimating such data.

To obtain a thorough understanding of the financial results and financial position of HNB, the reader should consult HNB’s audited financial statements for the year ended 31 December 2006, included in the Annual Report from page 106 to 172.

WORK UNDERTAKEN AND CONCLUSIONS
We reviewed the reliability of the data on Key Performance Indicators for 2006 based on:

• visits to selected project sites and branches to review systems and data;
• reviews of:
  - the systems used to generate, aggregate and report these data.
  - the data reported by the relevant business units to corporate level;
  - the data validation processes at corporate and business level;
  - the data trends in discussions with management.

Based on the above, the data for Key Performance Indicators for 2006, specified on pages 76 and 77 do not appear to be unreliable.

FINANCIAL DATA
We have reconciled the data on financial performance reported on page 67 of The Report with the audited financial statements of HNB for the year ended 31st December 2006.

Based on the above, we conclude that the data on financial performance reported on page 67 are properly derived from the financial statements of HNB for the year ended 31 December 2006 for which the independent auditors issued an unqualified audit opinion dated 15 February, 2007 on page 105 of the Annual Report.

OTHER INFORMATION
We reviewed the other information in The Report, based on:

• an analysis of the systems and processes used to generate this information;
• review of internal documentation and sources;
• interviews with staff for the information;
• our knowledge and understanding of the sector and HNB’s business.

Based on the above, the other information in The Report does not appear to be unfairly stated.

KPMG KAPLAN THOMAS EXELBY & CO

CHARTERED ACCOUNTANTS

15 February 2007
Colombo, Sri Lanka
ANCHORING FOR THE FUTURE

We have always remained optimistic even in the face of dire challenges believing strongly that our astute decisions, unfailing leadership and constant care imparted to the community around us will be the panacea in fashioning a strong and dynamic triple bottom line. Our new vision of being the acknowledged leader and chosen partner in providing financial solutions and mission in combining entrepreneurial spirit with empowered people and leading-edge technology to constantly exceed shareholder expectations encapsulates our ethos in looking forward to a sustainable future where all stakeholders will play a vital part in our forward journey.

THE FIVE KEY INITIATIVES that are embedded into our very existence to continue as a leader in the financial industry are:

1. Increased focus on small and medium sized enterprises through careful segmentation for growth thereby creating a culture composed of entrepreneurs who will build a sustainable economy for future generations.

2. Single mindingly drive towards improved asset quality which will focus on investing and creating a healthy risk management philosophy with optimal risk/return balance in order to create a sustainable wealth portfolio for our shareholders.

3. Drive for productivity and economies of scale through greater efficiencies, enhanced competencies and creating a knowledge centric framework built on customer focus for our team, who will be passionately empowered to use world class best practices to achieve our vision.

4. Using IT as a fundamental driver to reap the full potential of competitive advantage.

5. Helping to create a sustainable base where environmentally friendly practices and preservation and conservation of the environment around us become integral to our culture.
Corporate Management

R Theagarajah
Managing Director/Chief Executive Officer

J M J Perera
F.C.I.B. (London)
Senior Deputy General Manager - Business Development & International

J D N Kekulawala
Chief Financial Officer

U A C Obeysekere
F.I.P.M. (Sri Lanka)
Deputy General Manager - Human Resources & Administration

C P Abeywickrema
B.Com. (Special) Sri Lanka
Deputy General Manager - Personal Banking & Network Management

Ms I Goonesekera
Attorney-at-Law & Notary Public
Deputy General Manager - Legal / Board Secretary

Ms S N Wickramasinghe
Attorney-at-Law & Notary Public, F.C.M.I. (UK)
Deputy General Manager - Senior Relationships

N Hapuarachchy
M.B.A. (Sri J.), Dip. in Bank Mgmt.
Deputy General Manager - Credit Supervision & Recoveries

A S Ibrahim
B.Sc. (Hons) Colombo, F.C.I.B. (London)
Deputy General Manager - Corporate Banking & Treasury
Ms D C Cooke
F.C.A. (Sri Lanka)
Deputy General Manager - Operations & Systems

Ms I R D Thenabadu
F.C.I.B. (London), F.C.M.A.
Deputy General Manager - Corporate Banking

Ms L L C C Thambiah
Assistant General Manager - Zone II

P D Hennayake
M.B.A. (A.I.T.) Thailand, P.G Dip. (Eng.),
B.Sc. Eng. (Hons) Moratuwa,
C.Eng., M.I.E. (Sri Lanka)
Assistant General Manager - Services

J R P M Paiva
B.A. (Hons) Ceylon
Assistant General Manager - Human Resources & Administration

P Sridharan
Assistant General Manager - Personal Financial Services & Business Development

G Ramanan
C.F.A., A.C.M.A.
Assistant General Manager - Investment Banking / Chief Executive Officer - HNB Securities Ltd.

D Rodrigo
M.B.A. (Cranfield), F.C.M.A., F.C.C.A.
Assistant General Manager - Risk & Compliance

R H Abayasekara
Assistant General Manager - International

A Ratnasabapathy
F.P.M.A.
Assistant General Manager - Zone I

H N J Chandrasekera
Assistant General Manager - Zone III
Senior Management

B J Sinniah
Chief Manager - Risk & Compliance

Ms R P P Wickremasinghe
B.Dev.Studies (Hons) Colombo,
Dip. in Personnel Management (N.I.B.M.),
Dip. in Counselling (S.L.F.I.)
Chief Manager - Employee Relations

A P L Fernando
F.I.B. (SL), Dip. in Bank Mgmt.
Chief Manager - Credit Supervision & Recoveries

V G P Vidyaratne
P.G.Dip.(Ind.Eng.), B.Sc. (Eng.)Cey., C.Eng., M.I.E. (SL)
Chief Manager - Premises & Engineering

R M P Ratnayake
Chief Manager - International Operations

V K A F Rajasekara
MPMA (UK)
Chief Manager - South Western Region

A N J De Silva
Chief Manager - Business Development - Subsidiaries

M K Nambiyarooran
Chief Manager - Treasury

K L Wijesooriya
LL.B
Chief Manager - Remittances

D St E Fernando
Chief Manager - Operations

V Vijayakumar
Chief Manager – Information Technology

T Govinthadas
M.B.A. (Colombo), B.Sc. (Hons) P.E.T. Cey., A.C.I.B. (Lond.)
Chief Manager- Network Banking

I H A Wickramasinghe
M.B.A. (Sri J.), A.M.I.E. (SL), M.C.I.M. (UK), M.S.L.I.M.
Chief Manager - Project Finance

B K Wijeratne
B.Sc. (Physical Science) Colombo
Chief Manager - Leasing

N U Jumat
A.I.B. (SL)
Chief Manager - Trade Services

P G Wilson
B.Sc. (Kelaniya), Dip. in I.T. (N.I.B.M.)
Chief Manager - IT Research & Development

J U N Chandrasena
M.A. (Econ) Colombo, A.C.M.A.
Chief Manager - Planning

R J Thambirajah
Chief Manager - Colombo Region

I A Baduge
Dip.in Bank Mgmt., A.I.C.M.
Chief Manager - Corporate Banking

R M P Dayawansa
M.B.A. (Sri J.), F.I.B. (SL), M.C.I.M. (UK), M.S.L.I.M.
Chief Manager - Greater Colombo Region
S L Wijayasinghe  
**Chief Manager - Finance**

S Sivalingam  
A.C.I.B. (London)  
**Chief Manager - Procurement & Logistics**

T M A Mutaliph  
A.I.B. (SL), Dip. in Bank Mgmt.  
**Senior Manager - Operational Risk**

N Premakumar  
**Senior Manager - Admin & Trade Services (City)**

J J Namasivayam  
**Senior Manager - Currency Division**

A Goonesekere  
M.B.A. (Sri J.), A.C.A. (Sri Lanka), A.S.C.M.A.  
**Senior Accountant**

U N I Elapata  
B.A. (Hons) - Univ. of Texas (Austin)  
**Senior Manager - Head Office Branch**

Ms N M C P Wettasinha  
**Attorney-at-Law & Notary Public**

E C Alles  
B. Sc. (Bangalore)  
**Senior Manager - Cinnamon Gardens**

R B Warnakulasuriya  
B.Com. (Special) Kelaniya, M.A.A.T., A.I.C.M.  
**Senior Manager - North Western Region**

V Ratnasabapathy  
A.C.I.B. (London)  
**Senior Manager - Credit Risk 2**

D L V Chandrasekera  
**Senior Manager - Leasing**

S Udayakumar  
M.C.M.I. (Lond), A.M.S.L.I.M, Dip. in Busi.Mgmt & Admin (UK), Dip. in Sales Mgmt & Marketing (UK)  
**Senior Manager - Operational Risk [Zone II]**

J T M Weeresinghe  
**Senior Manager - Credit Risk**

N Premarajah  
Higher Dip. in Int. Busi. Mgmt. - Chennai  
**Senior Manager - Consumer Banking & Housing Finance**

Mrs M K Rambukwella  
**Senior Manager - Training & Development**

Mrs R Prabhakaran  
A.I.B. (SL)  
**Senior Manager - Treasury Operations**

W D A G Wickrama  
**Senior Manager - Pettah**

B K Achan  
M.Sc. (Bombay), B.Sc. (Hons) (Calcutta),C.A.I.I.B.(India)  
**Chief Representative Officer - Chennai**

A B Shahid  
M.B.A, B.Sc. (Univ. of Karachi), F.I.B. (Pakistan)  
**Chief Representative Officer - Karachi**
Effective management of risk is crucial for success in financial services and is fundamental to HNB’s strategy. Risk management aspires to be a culture inherent in all our associates which comprehends the downside and effectively manages risk based on pre-set parameters while leveraging on areas where upside potential exists. The focus across HNB is to manage risk effectively to generate sustainable profits.

HNB set up a dedicated risk management unit two years ago to drive better understanding of risk management across the network and to set the platform for compliance required by BASEL II. The Bank formulated a Risk Charter at the beginning of the year against which progress and achievements are reviewed. A robust IT platform too is being established to enforce this single minded focus which is extremely crucial at this juncture.

The Risk Management Committee chaired by the Chief Executive Officer, serves as the principal Risk Strategy and Risk Policy decision making body within the Bank and provides the Board the assurance on the performance of the overall Risk Management Framework.

**RISK FACTORS**
The following are the key risk factors that may impact HNB’s future results:

<table>
<thead>
<tr>
<th>Risk Factor</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>Credit Risk</td>
<td>Credit risk arises from potential that a borrower or counter-party to a transaction will fail to perform on an obligation.</td>
</tr>
<tr>
<td>Market Risk</td>
<td>Market risk is the risk to a financial institution’s condition resulting from adverse movement in market rates or prices including interest rates, foreign exchange rates and equity prices.</td>
</tr>
<tr>
<td>Operational Risk</td>
<td>Operational risk arises from the potential that inadequate information systems, operational problems, breaches in internal controls, fraud or unforeseen catastrophes will result in unexpected losses.</td>
</tr>
<tr>
<td>Liquidity Risk</td>
<td>Liquidity risk works on the probability that a bank will be unable to meet its obligations as they become due, owing to the inability to liquidate assets or obtain adequate funding (referred to as ‘funding liquidity risk’) or that it cannot easily unwind or offset specific exposures without significantly lowering market prices due to inadequate market depth or market disruptions (market liquidity risk).</td>
</tr>
<tr>
<td>Legal / Compliance Risk</td>
<td>Legal risk arises from the potential that unenforceable contracts, lawsuits, or adverse judgments can disrupt or otherwise negate operations or the condition of the organization.</td>
</tr>
<tr>
<td>Reputation / Strategic Risk</td>
<td>Reputation risk is the likelihood that negative publicity regarding an institution’s business practices, whether true or not, will cause a decline in the customer base, costly litigation, or revenue streams. This arises from bad and poor management decisions, strategic planning, and dissatisfied stakeholders.</td>
</tr>
</tbody>
</table>
HNB’s Risk Management platform encompasses the following:

**People**
- Skilled staff with extensive experience
- Active Board and Senior Management oversight

**Policies**
- Defined Risk Appetite
- Structured Risk Acceptance Criteria

**Systems**
- Comprehensive Internal Controls
- Regular measurement, analysis and actioning cycle for key risk areas

Given that finance and banking remain in the frontline of a number of risks in any environment, HNB continuously monitors and anticipates its risk environment, essentially but not limited to:
- Regular feedback from the extensive branch network
- Staying abreast of local and international events
- Regular scenario analysis
- Changes in the Regulatory Framework

Credit Risk has been identified as a major risk factor that HNB is exposed to. The following initiatives were introduced during the year to strengthen the process:
- Dedicated Relationship Managers for Key Accounts
- An improved credit monitoring and actioning culture
- A watchlisting process

### Compliance Initiatives

<table>
<thead>
<tr>
<th>Initiative</th>
<th>Monitored by</th>
<th>Execution</th>
</tr>
</thead>
<tbody>
<tr>
<td>Single Borrower Limit</td>
<td>Compliance</td>
<td>Credit</td>
</tr>
<tr>
<td>Related Party Transactions</td>
<td>Compliance</td>
<td>Credit</td>
</tr>
<tr>
<td>Capital Adequacy Ratio</td>
<td>Finance</td>
<td>Treasury / ALCO</td>
</tr>
<tr>
<td>Liquidity Ratio</td>
<td>Finance</td>
<td>ALCO (Asset &amp; Liability Committee)</td>
</tr>
<tr>
<td>Other Monthly and Quarterly Returns</td>
<td>Compliance</td>
<td>Relevant Departments</td>
</tr>
</tbody>
</table>

### PROGRESS ACHIEVED AGAINST RISK CHARTER IN 2006

#### Risk Mitigation Strategies

1. CREDIT RISK

1.1 Portfolio Issues

   a) Review the effectiveness of credit risk strategies and monitor their ongoing review.

   b) Review the adequacy of portfolio monitoring

   c) Review Large and High Risk Accounts that could potentially have a material impact on future Asset Quality.

   Periodic Review of Existing Product Portfolios and Risk Review of New Products

   New KPI Format introduced for reporting of Network performance

   Introduced Performance Dashboards for Credit Meetings

   Industry Reports for Poultry, Plantations – Tea, Rubber, Coconut, Construction, Apparel and Sugar sectors were reviewed and implications on HNB’s portfolio observed.

   Branch Reviews – Eight Large Branches comprising 260 Middle Market Clients were reviewed

   Miscellaneous reports on topical issues affecting industries & country trading partners.

   Top 10 Local and Foreign Currency Loan Reviews (Quarterly)

   High Risk Accounts (Internally Risk Rated CCC and below) Customer Reviews (Quarterly)

   Review of Watchlisted accounts (Quarterly)
1.2 Policy Issues

d) Review the effectiveness of credit risk policies and monitor their ongoing review.

e) Review delegated commitment authorities.

f) Mandate Head of Credit to decide on watchlisted and high risk credits and refer findings for Committee review.

Adequacy and Effectiveness of Credit Policies were evaluated in Monthly Meetings
Simplifying and Standardising Credit Documentation to enhance effectiveness
Amended Credit Approval Guidelines enhancing the level of autonomy
Framework developed for identification and reporting of Watchlisted Exposures
Independent Review of Watchlisted Exposures for actioning

2 REGULATORY / COMPLIANCE RISK

a) Review the adequacy and effectiveness of HNB’s compliance management framework.

b) Review of compliance monitoring plans and results.

c) Oversee compliance by HNB with applicable laws, regulations and regulatory requirements that may impact HNB’s risk management.

Successfully migrated to submit returns electronically to CBSL.
All returns submitted on time.
* Report on adherence submitted to Audit Committee, Quarterly
* Business Continuity Planning documented across the network

Audit Management Letter and CBSL Inspection Reports recommendations followed through and actioned.

New Regulations proposed / introduced during the year (e.g. CB Anti Money Laundering and FTR Regulations, Parate Ruling) impact assessed and followed through in terms of changes to internal policy, systems and guidelines

3 MARKET RISK

a) Review HNB’s market risk control framework and assess whether it is appropriately independent from the line of business and comprehensive.

b) Review appropriateness of Limit/Exposure position in light of prevailing market conditions

c) Evaluate models to be used to measure risks and decide on risk appetite

Structure ensures independence in reporting between Front Office and Back Office. Approved Limits are monitored by Middle Office
Focus is on covering Corporate Banking Positions with minimal trading on own account under the guidance of ALCO and Treasury Committee.
Revisiting existing models and review of its appropriateness is being carried out with a view to introducing a new Treasury Trading System.

4 OPERATIONAL RISK

a) Review the operational risk profile and operational risk strategy/appetite of HNB and monitor HNB’s overall risk control framework.

b) Review the IT Risk Profile and Strategy based on the Risk Appetite of HNB

c) Review Plan to make major modifications / enhancements to the system

Operational Risk Management Structure in place to carry out Risk Assessments across the network
Operational loss reporting across the network reviewed and learnings shared across the network on an ongoing basis
Monitored through internal control systems / reviews and independent IT Audits conducted by our External Auditors.
HNB is in the process of migrating to a new Core Banking System, the process of selection, implementation planning and review is managed through a separate committee that meets on a regular basis
5 LEGAL RISK
   a) Review litigation and any trends arising from litigation against HNB from a risk management perspective
   b) Review HNB’s Legal policies and practices from a risk management perspective

   Ongoing follow up.

   Ongoing review of legal documentation and Service Standards.

6 LIQUIDITY
   a) Review the effectiveness of the risk management systems and policies adopted by the ALCO to manage structural interest rate risk.
   b) Review new Balance Sheet Management policies

   Ongoing Review through post implementation follow up of major decisions taken

   Capital Management Committee reviews Capital Structure, Structure and Composition of the Balance Sheet in the context of Capital Adequacy Regulations and liquidity. Its recommendations are presented to the ALCO Committee and actioned.

7 REPUTATION / STRATEGIC RISK
   a) Review strategic risks identified by the CFO.
   b) Decide on risk appetite and /or those requiring escalation to the Board of Directors
   c) Review CSR / Sustainability Reporting policies and compliance with Bank’s Risk Management Framework

   Reviewed as an integral part of the Strategic Planning and Budgeting process. Specific action plans developed for key risks (competitor strategies, regulatory changes etc.) identified.

   System in place to escalate all quantified risks above a threshold level to the Board Audit Committee on a regular basis

   Sustainability Committee meets to discuss and implement approved CSR Projects

The focus this year has been on enforcing a strong risk culture, implementing robust system support and setting the platform for BASEL II IRB initiatives that will take precedence into next year as well. We strongly believe that our reporting and control mechanisms remain above par to the industry and in line with global norms. Our ethos of portraying stability, sustainability, compliance and good governance continue to remain an integral facet within our workings. The features which we feel have contributed immensely to our emphasis of being true to our ethos are:

- Board composition and independence
- Integrity and oversight of management – Risk Charter and Risk Management Committee
- Effective use of internal and external audit functions
- Higher level of disclosure and transparency
- Greater engagement with investors – listed in Luxemborg Stock Exchange and CSE.
BEYOND 2007

Looking beyond 2007, key priorities over the Medium Term would be to gear ourselves for a BASEL II IRB Platform.

Enforcing a Strong Risk Culture
- Developing Meeting Dashboards
- Data clean up exercise across the network
- Improving Performance KPI’s across all units
- Credit Skills Training of our staff

Implementing Robust System Support
- Enhancement of Compliance Risk Mitigation through the introduction of new Core Banking System
- Introduction of AML Monitoring Tools with appropriate software support
- Developing an MIS to be able to better support growth in SME and Micro-Finance Segments

Setting the platform for BASEL II IRB Approach
- Revisiting existing Risk Management Structure in line with global best practices
- Ensuring more effective use of Internal Risk Ratings for booking Quality Credits and effectively managing the Credit Portfolio
- Developing Internal Credit Rating Score Sheets for SME and Retail Segments
INCIDENTS OF OPERATIONAL LOSSES REPORTED IN 2006
- Business Disruption & System Failures (6%)
- Execution, Delivery, & Process Management (60%)
- External Fraud (14%)
- Internal Fraud (19%)

EXPOSURE BY COUNTERPARTIES
- Corporates >1Bn (5%)
- Corporates 100mn - 1Bn (27%)
- Corporates 35mn - 100mn (8%)
- SME 35mn - 100mn (4%)
- Micro-finance (4%)
- Housing (10%)
- Personal Loans (27%)
- Leasing (11%)

EXPOSURE BY COUNTERPARTIES
- Overdrafts (24%)
- Trust Receipts (6%)
- Packing Credit (1%)
- Term Loans (60%)
- Leasing Facilities (10%)

INDUSTRYWISE EXPOSURE
- Agriculture & Fishing (44%)
- Manufacturing (16.44%)
- Tourism (12.15%)
- Transport (1.16%)

PORTFOLIO QUALITY
- AAA (3%)
- BB (20%)
- CCC (3%)
- CC (2%)
- C (1%)

NON PERFORMING ADVANCES (NPA)
- NPA Gross as a % of Loans and Advances
- NPA Net as a % of Loans and Advances

Annual Report 2006
Corporate Governance

Being continuously committed to reviewing and improving our conformance and compliance initiatives and practices, the Board of Directors institute transformational change wherever necessary to ensure best practices are maintained and enhanced according to the principles of Corporate Governance. The Board of Directors remain the catalyst in governance, recognizing that both corporate governance and business governance are integral to maintaining a sustainable enterprise which displays continued growth performance and value creation for our stakeholders.

At HNB, the Board of Directors, lead by the Chairman, is responsible for the governance of the Bank, and establishes effective governance practices to meet challenges, both in the short and long term and ensure value creation to the stakeholders. The Board of Directors emphasizes the role of the executive management team in monitoring compliance with the established governance framework of the Bank to ensure that all business activities are conducted in accordance with the legal and regulatory framework applicable to the industry.

In a broader perspective, our shared responsibility towards good governance includes:

• Protecting our franchise by placing long term shareholder value ahead of short term gains,
• Providing our customers with superior products and services and good advice, while not compromising on the highest standards of integrity,
• Practicing the principles of good corporate citizenship, playing an active role in the communities around us,
• Instilling a culture of excellence amongst our team by proffering upwardly mobile opportunities to high achievers, promoting mutual respect, tolerance and unity within an inspiring work environment,
• Continuously reviewing and strengthening our conformance and performance strategies including the control environment and risk management strategies.

HNB incorporates in its governance code the guidelines prescribed in the Code of Best Practices on Corporate Governance issued by the Institute of Chartered Accountants of Sri Lanka, the Code of Corporate Governance for Banks and Financial Institutions issued by the Central Bank of Sri Lanka and the Exposure Draft on Rules on Corporate Governance for Listed Companies issued jointly by the Institute of Chartered Accountants of Sri Lanka and the Securities and Exchange Commission of Sri Lanka.

The extent of compliance by HNB for the year ended 31st December 2006 with the said principles and best practices are disclosed in the table on Pages 91 to 97 of the Annual Report.
## DIRECTORS

### The Board of Directors

#### Composition

The Board comprises nine Directors, all of whom are non-executive with the exception of the CEO. All Directors possess a wide range of skills and experience complimented with a high sense of integrity, independent judgment and considerable knowledge to add value to their roles and the ultimate performance of the Bank. The profiles of the Directors are on pages 12 and 13 of the Annual Report.

#### Meetings

Monthly meetings of the Board are held to review the Bank’s performance and to determine whether its strategies and business practices are aligned with stakeholders’ expectations. Additional meetings are convened whenever necessary. The number of meetings of the Board, Board appointed sub-committees and individual attendance by members are given on page 97 of the Annual Report.

#### Availability of a formal schedule of matters for Board discussion

Roles and responsibilities are formalized via a Board Charter, which also defines matters reserved for the Board and its Committees and those delegated to management. In summary the Board is accountable to the stakeholders for the Bank’s overall performance and its responsibilities include:

- **Strategy** - Providing strategic direction and formulating corporate strategic initiatives.
- **Board Performance and Composition** - Evaluating the performance of non-executive Directors, determining the size and composition of the Board and making recommendations to shareholders on the appointment and removal of Directors.
- **Leadership Selection & Succession Planning** - Appointing, evaluating and providing direction to the CEO and CFO and developing plans for Board and executive management.
- **Remuneration** - Determining the remuneration of the CEO and non-executive Directors.
- **Financial Reporting** - Reviewing and monitoring the process, controls and procedures which are in place to maintain the integrity of the Bank’s accounting and financial records and statements. Considering and approving quarterly and annual financial statements.
- **Risk Management** - Approving and monitoring the effectiveness of the Bank’s risk management strategy.
- **Relationship with Stock Exchanges, Regulators and Continuous Disclosure** - Maintaining a direct and ongoing dialogue with the SEC and other stock exchanges where our securities are listed, ensuring that the market and our stakeholders are kept informed of material developments.
- **Social Responsibility** - Considering the social, ethical and environmental impacts of our activities, setting standards and monitoring compliance with our social responsibility policies and practices.
- **Audit** - Recommending to shareholders the appointment of the External Auditor based on the review process conducted by the Audit Committee, and the direct ongoing dialogue with the External Auditor.

The following responsibilities have been delegated by the Board to the Corporate management:

- **Strategy** - Developing and implementing corporate strategies and making recommendations to the Board on significant strategic initiatives.
- **Senior Management Selection** - Recommending senior management selection and appointments, terms of appointment, performance evaluation and succession planning.
- **Financial Performance** - Developing the annual budget and managing day to day operations in line with budgetary forecasts.
- **Continuous Disclosure** - Keeping the Board and market fully informed of material developments.
- **Social Responsibility** - Maintaining standards of social, ethical and environmental practices established by the Board.

### Corporate Governance Level of Compliance

<table>
<thead>
<tr>
<th>Principle</th>
<th>Level of Compliance</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Composition</strong></td>
<td>The Board comprises nine Directors, all of whom are non-executive with the exception of the CEO. All Directors possess a wide range of skills and experience complimented with a high sense of integrity, independent judgment and considerable knowledge to add value to their roles and the ultimate performance of the Bank. The profiles of the Directors are on pages 12 and 13 of the Annual Report.</td>
</tr>
<tr>
<td><strong>Meetings</strong></td>
<td>Monthly meetings of the Board are held to review the Bank’s performance and to determine whether its strategies and business practices are aligned with stakeholders’ expectations. Additional meetings are convened whenever necessary. The number of meetings of the Board, Board appointed sub-committees and individual attendance by members are given on page 97 of the Annual Report.</td>
</tr>
<tr>
<td><strong>Availability of a formal schedule of matters for Board discussion</strong></td>
<td>Roles and responsibilities are formalized via a Board Charter, which also defines matters reserved for the Board and its Committees and those delegated to management. In summary the Board is accountable to the stakeholders for the Bank’s overall performance and its responsibilities include:</td>
</tr>
<tr>
<td><strong>Strategy</strong></td>
<td>Providing strategic direction and formulating corporate strategic initiatives.</td>
</tr>
<tr>
<td><strong>Board Performance and Composition</strong></td>
<td>Evaluating the performance of non-executive Directors, determining the size and composition of the Board and making recommendations to shareholders on the appointment and removal of Directors.</td>
</tr>
<tr>
<td><strong>Leadership Selection &amp; Succession Planning</strong></td>
<td>Appointing, evaluating and providing direction to the CEO and CFO and developing plans for Board and executive management.</td>
</tr>
<tr>
<td><strong>Remuneration</strong></td>
<td>Determining the remuneration of the CEO and non-executive Directors.</td>
</tr>
<tr>
<td><strong>Financial Reporting</strong></td>
<td>Reviewing and monitoring the process, controls and procedures which are in place to maintain the integrity of the Bank’s accounting and financial records and statements. Considering and approving quarterly and annual financial statements.</td>
</tr>
<tr>
<td><strong>Risk Management</strong></td>
<td>Approving and monitoring the effectiveness of the Bank’s risk management strategy.</td>
</tr>
<tr>
<td><strong>Relationship with Stock Exchanges, Regulators and Continuous Disclosure</strong></td>
<td>Maintaining a direct and ongoing dialogue with the SEC and other stock exchanges where our securities are listed, ensuring that the market and our stakeholders are kept informed of material developments.</td>
</tr>
<tr>
<td><strong>Social Responsibility</strong></td>
<td>Considering the social, ethical and environmental impacts of our activities, setting standards and monitoring compliance with our social responsibility policies and practices.</td>
</tr>
<tr>
<td><strong>Audit</strong></td>
<td>Recommending to shareholders the appointment of the External Auditor based on the review process conducted by the Audit Committee, and the direct ongoing dialogue with the External Auditor.</td>
</tr>
</tbody>
</table>

The following responsibilities have been delegated by the Board to the Corporate management:

- **Strategy** - Developing and implementing corporate strategies and making recommendations to the Board on significant strategic initiatives.
- **Senior Management Selection** - Recommending senior management selection and appointments, terms of appointment, performance evaluation and succession planning.
- **Financial Performance** - Developing the annual budget and managing day to day operations in line with budgetary forecasts.
- **Continuous Disclosure** - Keeping the Board and market fully informed of material developments.
- **Social Responsibility** - Maintaining standards of social, ethical and environmental practices established by the Board.
<table>
<thead>
<tr>
<th>Corporate Governance Principle</th>
<th>Level of Compliance</th>
</tr>
</thead>
<tbody>
<tr>
<td>Obtaining independent professional advice</td>
<td>The procedures for Directors, in the furtherance of their duties, to seek advice at the Bank’s expense is co-ordinated through the Company Secretary.</td>
</tr>
<tr>
<td>Company Secretary</td>
<td>All Directors have access to the Company Secretary who is an Attorney-at-Law by profession. She is responsible for supporting and advising the Chairman and the Board on all corporate governance matters, Board procedures and compliance with applicable rules and regulations.</td>
</tr>
<tr>
<td>Independent judgment</td>
<td>All Directors exercise their independent and objective judgment on issues of strategy, policy, resources and standards of conduct. The Board is conscious of its obligations to ensure that Directors avoid conflicts of interest (both real and apparent) between their duty to HNB and their other interests. The Board has adopted a procedure to ensure that conflicts and potential conflicts of interest of Directors are disclosed to the Board. Any Director with a material personal interest in a matter being considered by the Board must declare their interest and unless the Board resolves otherwise, they do not participate in boardroom discussions or vote on matters in which they face a conflict. All related party transactions and Director’s interest in contracts are disclosed on pages 155 to 169 of the Annual Report.</td>
</tr>
<tr>
<td>Dedication of adequate time and effort for the matters of the Board and the Company</td>
<td>The Chairman &amp; members of the Board dedicate adequate time for the fulfillment of their duties as Directors of the Bank. In addition to attending Board meetings, they attend sub-committee meetings and make decisions via circular resolution. The Board sub-committees include; - Nomination Committee - Audit Committee - Credit Committee - Procurement Committee - Human Resources/Remuneration Committee - Asset Disposal Committee</td>
</tr>
<tr>
<td>Training for new Directors</td>
<td>Directors undertake such professional development as they consider necessary in assisting them to carry out their duties as Directors. Presentations are made to the Board by the senior management of the Bank from time to time on industry related matters.</td>
</tr>
<tr>
<td>Chairman &amp; CEO Division of responsibilities of the Chairman &amp; MD/CEO</td>
<td>The functions of the Chairman and MD/CEO are clearly separated in order to ensure a balance of power and authority, such that no individual has unfettered powers of decision.</td>
</tr>
<tr>
<td>Presence of a strong non-executive element on the Board</td>
<td>All nine Directors are non-executive with the exception of the MD/CEO.</td>
</tr>
<tr>
<td>Chairman’s Role Role of the Chairman</td>
<td>The Chairman of the Bank is an independent non-executive Director, elected by the Board. The Chairman’s role encompasses: - Ensuring that Board members undertake appropriate induction covering terms of appointment, duties and responsibilities. - Providing effective leadership in formulating Board strategy. - Representing the views of the Board to the public. - Ensuring regular meetings, the minutes of which are accurately recorded and where appropriate included the individual and collective views of the Directors. - Encouraging effective participation of all Directors in the decision making process to optimize contribution. - Developing the agenda together with the Company Secretary and conducting Board meetings.</td>
</tr>
<tr>
<td>Corporate Governance Principle</td>
<td>Level of Compliance</td>
</tr>
<tr>
<td>--------------------------------</td>
<td>---------------------</td>
</tr>
<tr>
<td><strong>Financial Acumen</strong>&lt;br&gt; Availability of sufficient financial acumen and knowledge</td>
<td>The MD/CEO is a fellow member of the Institute of Chartered Accountants of Sri Lanka and a fellow member of the Chartered Institute of Management Accountants – UK. In addition, the Board includes a fellow member of the Chartered Institute of Management Accountants – UK. These members of the Board have the ability to offer guidance on matters of finance to the Board.</td>
</tr>
<tr>
<td><strong>Board Balance</strong>&lt;br&gt; Balance of the Board</td>
<td>The Board consists of eight non-executive Directors and only one Executive Director, who is also the MD/CEO. Each of them brings to the Board, wide experience and an independent and objective viewpoint, and carries significant weight in the Board’s decisions. In exercising independent judgment, the Board has established a procedure which is discussed above under “Independent Judgment”.</td>
</tr>
<tr>
<td><strong>Supply of Information</strong>&lt;br&gt; Timely and accurate management information</td>
<td>All Directors receive accurate, timely and clear information on all relevant matters. Any requests for further information are co-ordinated by the Board Secretary.</td>
</tr>
<tr>
<td><strong>Appointments to the Board</strong>&lt;br&gt; Availability of a formal and transparent procedure for new appointments</td>
<td>The Nomination Committee of the Bank is comprised of five Directors including the CEO. The composition of the Board is subject to continuous review by the Nomination Committee, and one of the responsibilities of the Board is identifying, evaluating and selecting candidates for suitable positions to ensure succession planning within the Bank. All new appointments as well as continuing directorships are reviewed by the Nomination Committee. Directors are required to report any substantial change in their professional responsibilities, occupation or business associations to the Nomination Committee, which will examine the facts and circumstances and make recommendations to the Board.</td>
</tr>
<tr>
<td>Disclosure of details of new Directors to shareholders</td>
<td>Details of new Directors are disclosed to the shareholders on their appointment. Prior notice on appointment of new Directors is given to the Director of Bank Supervision.</td>
</tr>
<tr>
<td><strong>Re - election</strong>&lt;br&gt; Re - election of Directors</td>
<td>According to the Articles of Association of the Bank, each Director other than the Managing Director/CEO and any nominee Director, retires by rotation once every three years and is required to stand for re-election by the shareholders at the Annual General Meeting. The Nomination Committee will consider their independence at that time and the proposed re-election of Directors is subject to prior review by the full Board.</td>
</tr>
<tr>
<td><strong>Appraisal of Board Performance</strong>&lt;br&gt; Appraisal of Board performance</td>
<td>The performance of the Board and its committees is evaluated by the Chairman to ensure that the Board functions effectively and efficiently, although such evaluation is not formally documented.</td>
</tr>
<tr>
<td><strong>Appraisal of the CEO</strong>&lt;br&gt; Appraisal of the MD/CEO</td>
<td>The performance of the MD/CEO is reviewed every year by the full Board against financial and non financial targets which are in line with the short, medium and long term objectives of the Bank.</td>
</tr>
<tr>
<td><strong>DIRECTORS’ REMUNERATION</strong>&lt;br&gt; Remuneration Procedure</td>
<td>The Remuneration Committee comprises of three non-executive Directors. The CEO attends meetings on invitation. The Remuneration Committee is responsible for assisting the Board with regard to remuneration policy for non-executive Directors and for making all relevant disclosures. The Remuneration Committee determines and agrees with the Board, the broad policy framework for the remuneration of the CEO. The MD/CEO does not participate in such meetings.</td>
</tr>
</tbody>
</table>
## Corporate Governance

<table>
<thead>
<tr>
<th>Principle</th>
<th>Level of Compliance</th>
</tr>
</thead>
<tbody>
<tr>
<td>The level and make up of remuneration</td>
<td>The remuneration package of the MD/CEO is structured to link rewards to corporate and individual performance. Non-executive Directors receive a nominal fee as disclosed in this Annual Report.</td>
</tr>
<tr>
<td>Disclosure of remuneration.</td>
<td>The details of the total remuneration of the Directors are disclosed on page 125 of the Annual Report.</td>
</tr>
</tbody>
</table>

### RELATIONS WITH SHAREHOLDERS

Constructive use of the Annual General Meeting: The Board remains mindful of being accountable to the shareholders and the need for transparency at all levels, striving to maintain this value framework in all shareholder dealings and communications. The primary modes of communication between the Bank and the shareholders are the Annual Report and the Annual General Meeting. Information is received by the shareholders prior to the AGM to give them an opportunity to exercise the prerogative to raise any issues relating to their shareholdings and the business, either verbally or in writing prior to the AGM. The Board which includes the Chairmen of the Audit, Remuneration and Nominations Committees are present to answer any questions.

Circularization of notice of the AGM: The Annual Report, financial statements and the notice of the meeting are sent to shareholders at least 21 calendar days prior to the date of the AGM. The Bank proposes a separate resolution for each item of business, giving shareholders the opportunity to vote on each substantially different issue.

Major transactions: During 2006 there were no major transactions which materially affected the Bank’s net asset base. Transactions, if any, which materially affect the net assets of the Bank will be disclosed in the annual/quarterly financial statements.

### ACCOUNTABILITY AND AUDIT

**Financial Reporting**

The Bank has presented a balanced and understandable assessment of Company’s position and prospects for the year ended 31st December and at the end of each quarter.

In the preparation of quarterly and annual financial statements, the Bank had strictly complied with the requirements of the Companies Act No.17 of 1982, the Banking Act No. 30 of 1988 and amendments thereto, and are prepared and presented in conformity with Sri Lanka Accounting Standards. The Bank has complied with the reporting requirements prescribed by the regulatory authorities such as the Central Bank and CSE. As the Bank’s Global Depository Receipts (GDRs) are listed in the Luxemburg Stock Exchange, the Bank has also complied with all the reporting requirements of the Luxemburg Stock Exchange.

Directors’ report in the Annual Report: The Directors’ report is given on pages 100 to 102 of the Annual Report.

Statement of Directors’ responsibility on the preparation and presentation of financial statements: The statement of Directors’ responsibility for financial reporting is given on page 103 of the Annual Report.

Statement of the External Auditors’ on their responsibilities: The Auditor’s Report given on page 105 of the Annual Report includes the scope of their responsibilities and their opinion on the financial statements.

Management report in the Annual Report: The Management Discussion and Analysis is given on pages 14 to 40 of the Annual Report.

Declaration by the Board that the business is a going concern: This is given in the Directors’ report on page 100 of the Annual Report.

Summoning an EGM to notify shareholders if net assets fall below one half of the shareholders’ funds: Likelihood of such occurrence is remote. However, should the situation arise, an EGM will be called for and shareholders will be notified.
**Corporate Governance**

<table>
<thead>
<tr>
<th>Principle</th>
<th>Level of Compliance</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Internal Control</strong>&lt;br&gt;Maintaining a sound system of internal control and risk management</td>
<td>The Board is ultimately responsible for the Bank’s systems of internal control and for reviewing their effectiveness. These systems manage the risk of the Bank’s business and ensure that the financial information on which business decisions are made and which is published is reliable, and also ensures that the Bank’s assets are safeguarded. The systems of internal control are designed to manage rather than eliminate the risk of failure to achieve business objectives. In pursuing these objectives, internal controls are aimed at providing reasonable and not absolute assurance against material misstatement or loss. The Board of Directors is satisfied with the effectiveness of the system of internal control. A detailed Risk Management Report is given on pages 84 to 89 of the Annual Report.</td>
</tr>
<tr>
<td>Reviewing the effectiveness of the internal control system</td>
<td>The Internal Audit Division of the Bank carries out regular reviews on the internal control system. A control self assessment is also being used by the Bank over the past three years as a means to enhancing process discipline and internal control. The Audit Committee monitors and reviews the effectiveness of the Bank’s internal audit function and the internal control system.</td>
</tr>
<tr>
<td><strong>Audit Committee and Auditors</strong>&lt;br&gt;Availability of an Audit Committee with a written terms of reference comprising of at least three non-executive Directors</td>
<td>The Audit Committee of the Bank is comprised of three non-executive Directors, majority of whom are independent, and meets regularly throughout the year. The Committee has also co-opted an external consultant, who is a fellow member of the Institute of Chartered Accountants of Sri Lanka and the Institute of Chartered Accountants, England &amp; Wales, to attend every meeting and provide the necessary financial expertise. The Company Secretary functions as the Secretary to the Audit Committee. The CEO attends meetings on invitation. The role and responsibilities of the Audit Committee is set out in the Audit Committee Charter. The Committee reviews the Bank’s internal control and risk management systems with particular reference to internal controls over financial reporting. The Committee monitors the integrity of the Bank’s financial statements and formal announcements relating to the Bank’s financial performance by reviewing the presentation of such reports and significant financial judgments/estimates contained in them. The Audit Committee also reviews issues relating to breach of ethics, such matters as fraud, accounting issues, employee wrong-doing and regulatory violations and the arrangements by which the staff of the Bank may in confidence raise concerns about possible irregularities. The Committee also ensures that the procedures for the independent investigations of such matters are appropriate. A continuous review of the performance of the Audit Committee has been set up by retaining an independent consultant who is considered a financial expert, and has wide experience in audit and governance best practices. The consultant participates at all meetings of the Committee and provides feedback. He also meets separately with the Corporate Management and makes recommendations to the Committee in order to improve the effectiveness of the financial reporting process and control environment. The Audit Committee Charter specifies a set of terms of reference defining its scope of authority, which includes review of internal and external audit process, the adequacy of internal controls, accounting policies and compliance with accounting standards. The report of the Audit Committee of the Bank for the year 2006 is given on page 104 of the Annual Report.</td>
</tr>
<tr>
<td>Review of the audit function and relationship with External Auditor</td>
<td>The Audit Committee monitors and reviews the effectiveness of the Bank’s Internal Audit function, the External Auditor’s independence, objectivity, and the effectiveness of the audit process taking into account relevant professional and regulatory requirements. The Committee also sets out the policy for the engagement of the External Auditor to provide non-audit services, taking into account relevant ethical guidance with regard to the provision of non-audit services by the External Auditor. The Audit Committee has the primary responsibility for making a recommendation on the appointment, re-appointment or removal of the External Auditor in-line with professional standards and regulatory requirements.</td>
</tr>
</tbody>
</table>
## Corporate Governance

### Disclosure on the adherence to the principles and best practices of Corporate Governance.

The Board of Directors is of the view that it has put in place the resources and the process to ensure that the Bank is substantially compliant with the Code of Best Practices on Corporate Governance issued by Institute of Chartered Accountants of Sri Lanka, throughout the year ended 31st December 2006.

### COMPLIANCE

#### Regulatory Compliance

An independent risk & compliance function is in place to ensure that the Bank complies with applicable laws and regulations.

The Compliance Reports signed by the MD/CEO and CFO are reviewed by the Audit Committee prior to publishing interim financial statements. The CFO is required to submit a report on whether the Bank is up to date in the settlement of statutory payments.

### CONTROLLED ENTITIES

#### Monitoring of Controlled Entities

The activities of every company in the Group are overseen by their own Board of Directors.

Directors of each of the controlled entities are provided with corporate governance guidelines, which have been approved by the main Board of the Bank. The corporate governance guidelines set out the specific roles, duties and responsibilities of the Directors of controlled entities. Such guidelines set out the key expectations that the Board would have, from the Boards of controlled entities. The guidelines have been specifically tailored to the different entities, depending on the nature of its business and activities.

Confidence is maintained in the activities of a controlled entity Board through high quality of the Boards of the controlled entities and their commitment to Group objectives.

### OTHER CORPORATE GOVERNANCE INITIATIVES

#### Corporate Governance Culture

With a view to embedding in our culture, the highest standards of integrity and professionalism, and to instill in our employees an appreciation of our core values, our shared responsibilities and provide them with opportunities and tools required to accomplish their goals, continuing education is provided at different levels.

Orientation is provided to all new managers as well as to new employees. Manager training is provided to all existing managers. We strive to develop our talent and help our managers reach their potential through executive development programs and regular assessment and feedback.

#### Corporate Social Responsibility

In keeping with our core value of serving the community in which we live and work, the Bank has embarked on several ventures details of which are discussed on pages 41 to 79 in the Sustainability Report which was compiled based on the Global Reporting Initiative (GRI) guidelines. The Bank has set up a Sustainability Committee, which has three sub-committees addressing the social responsibility issues relating to our key stakeholders, namely:
- Customer Service and Investor Group
- Employee Liaison Group
- Environmental and Community Advisory Group
MEETINGS

The number of meetings of the Board, Board appointed sub-committees and individual attendance by members is shown below:

<table>
<thead>
<tr>
<th>Name</th>
<th>Total No. of meetings in 2006</th>
<th>Board Meetings</th>
<th>Audit Committee</th>
<th>Nomination Committee</th>
<th>Remuneration Committee</th>
</tr>
</thead>
<tbody>
<tr>
<td>Mr Rienzie T Wijetilleke</td>
<td>14</td>
<td>14</td>
<td>****</td>
<td>1</td>
<td>3</td>
</tr>
<tr>
<td>Dr V P Vittachi</td>
<td>13</td>
<td>13</td>
<td>****</td>
<td>****</td>
<td>****</td>
</tr>
<tr>
<td>Mr R Theagarajah</td>
<td>14</td>
<td>14</td>
<td>1</td>
<td>3</td>
<td></td>
</tr>
<tr>
<td>Mr D H S Jayawardena</td>
<td>14</td>
<td>13</td>
<td>4(Note b)</td>
<td>1</td>
<td>3(Note b)</td>
</tr>
<tr>
<td>Mr M V Theagarajah</td>
<td>13</td>
<td>13</td>
<td>****</td>
<td>1</td>
<td>****</td>
</tr>
<tr>
<td>Mr R K Obeyesekere</td>
<td>11</td>
<td>11</td>
<td>****</td>
<td>1</td>
<td>3</td>
</tr>
<tr>
<td>Mrs P C Cooray</td>
<td>14</td>
<td>14</td>
<td>4</td>
<td>****</td>
<td>3</td>
</tr>
<tr>
<td>Mr R Sivarattnam</td>
<td>8</td>
<td>8</td>
<td>1</td>
<td>****</td>
<td>****</td>
</tr>
<tr>
<td>Mr D R Ghazalli</td>
<td>3</td>
<td>3</td>
<td>****</td>
<td>****</td>
<td>****</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Credit Asset Procurement Committee</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total No. of papers approved in 2006</td>
</tr>
<tr>
<td>Mr Rienzie T Wijetilleke</td>
</tr>
<tr>
<td>Dr V P Vittachi</td>
</tr>
<tr>
<td>Mr R Theagarajah</td>
</tr>
<tr>
<td>Mr D H S Jayawardena</td>
</tr>
<tr>
<td>Mr M V Theagarajah</td>
</tr>
<tr>
<td>Mr R K Obeyesekere</td>
</tr>
<tr>
<td>Mrs P C Cooray</td>
</tr>
<tr>
<td>Mr R Sivarattnam</td>
</tr>
<tr>
<td>Mr D R Ghazalli</td>
</tr>
</tbody>
</table>

Note a - In addition, 17 papers were reviewed and approved by circulation during 2006
Note b - Mr. R Theagarajah attended all meetings by invitation.
Note c - Includes 59 papers approved by Messrs J M J Perera & J D N Kekulawela as alternates to Mr. R Theagarajah
Note d - While Mrs. P C Cooray is not a regular member of this committee, she has been co-opted in lieu of a regular committee member when not available.
**** - Not a committee member.
### INCOME STATEMENT NOTES

1. Income ___________________________ 124
2. Interest Income _____________________ 124
3. Interest Expenses ____________________ 124
4. Dividend Income _____________________ 124
5. Other Income ________________________ 125
6. Operating Expenses ___________________ 125
   (a) Directors' Emoluments ________ 125
   (b) Current Tax Expense ___________ 126
   (c) Deferred Tax Expense __________ 126
7. Provision for Loan Losses ____________ 125
8. Income Tax Expense _________________ 126
   (a) Current Tax Expense ___________ 126
   (b) Deferred Tax Expense __________ 126
9. Basic Earnings per Share _____________ 127

### ASSET NOTES

10. Cash and Cash Equivalents ___________ 127
11. Statutory Deposit with Central Bank of Sri Lanka ____________ 127
12. Dealings Securities ___________________ 127-129
   (a) Quoted shares – Bank __________ 127-128
   (b) Quoted shares – Subsidiaries ______ 129
   (c) Bonds – Bank _________________ 129
   (d) Bonds – Subsidiaries ___________ 129
13. Investment Securities _________________ 130-132
   (a) Quoted shares _________________ 130
   (b) Unquoted shares _______________ 130
   (c) Bonds and Debentures __________ 131-132
      i Bank – Long Term Investments 131
      ii Bank – Government of Sri Lanka Treasury Bonds 131
      iii Bank – Foreign Currency Bonds 131
      iv Subsidiaries – Quoted Debentures 132
      v Subsidiaries – Government of Sri Lanka Treasury Bonds 132
14. Bills of Exchange _____________________ 132
   (a) Movement in Provision for Bills of Exchange 132
15. Loans and Advances _________________ 133-138
   (a) Movement in Provision for Loan Losses 133
   (b) Total Provision for Loan Losses 134
      i Specific Provision ___________ 134
      ii General Provision __________ 134
   (c) Asset Quality – Bank __________ 134
   (d) Credit Risk – Bank ___________ 134-136
      i Collateral wise Analysis of Gross Non-Performing Lending Portfolio 134
      ii Sector/Product wise Analysis of Gross Lending Portfolio 135-136
   (e) Movement in Interest in Suspense – Bank 137
   (f) Movement in Foreclosed Properties 137
   (g) Movement in Provision for Foreclosed Properties 137
   (h) Provisions for Discount of Securities 137
   (i) Provision for Kabooka Lanka (Pvt) Ltd 138
16. Lease Rentals Receivable ______________ 138
   (a) Lease Rentals Receivable within one year 138
   (b) Lease Rentals Receivable after one year 138
   (c) Movement in Provision for Lease Rentals Receivable 138
17. Non Current Assets held for Sale ______ 139
   (a) Freehold Land _________________ 139
18. Investment in Associate Companies ___________ 139-140
   (a) Bank ________________ 139
   (b) Group – Quoted Investments ______ 140
      i Group – Negative Goodwill on Acquisition 140

### SHAREHOLDERS' FUNDS NOTES

32. Share Capital – Bank & Group ___________ 153

### COMMITMENT NOTES

33. Commitments and Contingencies – Bank & Group ___________ 153-154
   (a) Capital Commitments ___________ 153
   (b) Future monthly Commitments on Operating Leases – Bank 154
   (c) Irrevocable Commitments – Bank 154
   (d) Contingent Liabilities __________ 154
   (e) Litigation against the Bank ___________ 154
   (f) Tax Assessments against the Bank ___________ 154

### OTHER NOTES

34. Directors' Interest in Contracts with the Bank ___________ 155-156
   (a) Trading Transactions ___________ 155
   (b) Credit Card Facilities to Directors ___________ 155
   (c) Accommodation granted to Directors 156
35. Related Party Transactions ___________ 156-159
   (a) Transactions with/between Subsidiaries ___________ 156-158
      i Sithma Development [Pvt] Limited [Sithma] 156-158
      ii HNB Securities Limited ["Securities"] 157
      iii HNB Assurance Limited ["Assurance"] 157
      iv HNB Stockbrokers [Pvt] Limited ["Stockbrokers"] 158
   (b) Transactions with Associates 158
   (c) Transactions with Key Management Personnel of the Bank ___________ 158
   (d) Compensation of Key Management Personnel ___________ 158
   (e) Transactions with Other Related Parties ___________ 159-166
      i Sithma Development [Pvt] Ltd ___________ 157
      ii HNB Securities Ltd ___________ 157
      iii HNB Stockbrokers [Pvt] Ltd ___________ 157
      iv HNB Assurance Ltd ___________ 157
36. Maturity Analysis – Bank ___________ 170
37. Segment Reporting ___________ 171
38. Events Occurring After the Balance Sheet Date ___________ 171
   (a) Proposed dividends 171
   (b) Issue of Bonus Shares 171
39. Comparative Information ___________ 172
40. Directors' Responsibility Statement ___________ 172
2006
1st Quarter Results 2006 released on 23rd May, 2006
2nd Quarter Results 2006 released on 28th July, 2006
3rd Quarter Results 2006 released on 15th November, 2006
25% Interim Dividend for 2006 paid on 11th December, 2006
38th Annual General Meeting 29th March, 2007
25% Final Dividend for 2006 payable on 10th April, 2007

(*)subject to confirmation by Directors)

2007
1st Quarter Results 2007 April, 2007
2nd Quarter Results 2007 July, 2007
3rd Quarter Results 2007 October, 2007
*......% Interim Dividend for 2007 December, 2007
39th Annual General Meeting March, 2008
*......% Final Dividend for 2007 April, 2008

(*subject to confirmation by Directors)
Report of the Directors

The Directors take pleasure in presenting to members their report and the audited accounts of the Company for the year ended 31st December 2006. This was approved by the Directors at a meeting held on 19th February, 2007.

Principal Activities
The principal activities of the Bank and the Group during the year were general banking, development banking, mortgage financing, lease financing, corporate financing, dealing in government securities and quoted equities, pawn broking, stock broking, providing insurance services, property development, credit card facilities and other financial services. There have been no significant changes in the nature of the principal activities of the Bank and the Group during the financial year under review.

Review of Operations
A review of the operations of the Bank during the financial year and results of those operations are contained in the Chairman’s Statement and in the Managing Director’s Assessment of the year on Pages 4 to 11 of this Annual Report. These reports form an integral part of the Directors’ Report.

New Product Development
During the year 2006 the Bank introduced “HNB Virtual Branch” which is the Internet Banking Solution for customers.

For the first time in Sri Lanka the Bank introduced “HNB SMS Banking” using an Over the Air menu driven service, in collaboration with Mobitel (Pvt) Ltd.

The Bank also introduced “A Life & Liability” Insurance Cover to our Micro Finance Customers (Gami Pubuduwa) through HNB Assurance where HNB bears 50% of the insurance premium.

In addition to the above the Bank introduced “0% Interest Installment Scheme” through HNB Credit Cards.

Branch Expansion
During the year the Bank opened/relocated the following Customer Centres:

Customer Centres opened -
1) Jampettah Street 2) Pettah 3rd Customer Centre
3) Kochchikade

Customer Centres Relocated -
1) Peradeniya 2) Akurana 3) Hatton
4) Kahawatte 5) Seeduwa

Risk & Internal Control
The Board considers that strong internal controls are integral to the sound management of the Bank, and it is committed to maintaining strict financial, operational and risk management controls over all its activities.

The Directors are ultimately responsible for the Bank’s system of internal control and for reviewing its effectiveness. Such a system is designed to manage, rather than eliminate, the risk of failure to achieve business objectives and can provide only reasonable and not absolute assurance against material misstatement or loss. There is an ongoing process for identifying, evaluating and managing the risks that are faced by the Bank, and the Directors have reviewed this process, through the Audit Committee.

The Board of Directors is satisfied with the effectiveness of the system of internal control for the year under review and up to the date of approval of the Financial Statements and Annual Report.

Corporate Governance
The Board is committed to maintaining high standards of corporate governance, the process by which the Bank is directed and managed, risks are identified and controlled and effective accountability assured. The Board of Directors is of the view that it has put in place the resources & the process to ensure that the Bank is substantially compliant with the Code of Best Practices on Corporate Governance issued by Institute of Chartered Accountants of Sri Lanka, throughout the year ended 31st December 2006. The Corporate Governance Report is given on pages 90 to 97 of the Annual Report.

Audit Committee
The Audit Committee comprises entirely of Non-executive directors all of whom served throughout the year. The members of the Committee are:
Mr R Sivaratnam (Chairman)
Mr D H S Jayawardena
Mrs P C Cooray
Mr Ranjan Seevaratnam (Consultant)

The Report of the Audit Committee is given on page 104 of the Annual Report.

Going Concern
The Board is satisfied that the Bank has adequate resources to continue its operations in the foreseeable future. Therefore, we continue to adopt the going-concern basis in preparing the Financial Statements.

Code of Corporate Conduct
The Management has in clear terms emphasized amongst staff the need to uphold and maintain the highest standards of Corporate Conduct. At the point of entry, every staff member is issued with a letter of appointment and a separate document setting out the code of conduct expected of them which demand strict adherence. Their acceptance and understanding of the expectations of the Management in respect of corporate conduct is obtained by requiring them to subscribe to these documents. The Bank has in place, apart from its Vision & Mission Statements, a Value Statement enshrining the following:-

- Treasure professional & personal integrity at all times
- Demonstrate mutual respect in all interactions
- Passionate about everything we do
- Committed to being customer centric
- Courage to change, challenge and be different
- Demonstrate Unity in Diversity

The need for compliance and upholding of these values is re-emphasized by the CEO in his New Year message to the entire staff annually.

Ensuring secrecy, which is considered to be paramount, is protected by way of the Information Security Policy which prevents staff from disclosing information to unauthorized parties. The acceptance of any improper gratification for personal gain is strictly prohibited and the projected image of the Bank in the public eye is given significance in all interactions and transactions. Non compliance or the slightest deviation of the norms, rules and regulations set by the Management in respect of discipline are not condoned with and offenders are dealt with severely after just and equitable inquiry. The stern and uncompromising stand taken by the Management towards the enforcement of discipline has
proven to be a deterrent to indiscipline and reinforcement for good conduct and behaviour among staff.

**Turnover/Gross Income**
The Turnover/Gross Income of the Group for 2006 was Rs. 23,233,201,000/- (2005 – Rs. 18,216,729,000/-). An analysis of the Income is given in Note No. 1 to the Financial Statements.

### Profit

<table>
<thead>
<tr>
<th></th>
<th>2006</th>
<th>2005</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Rs.000</td>
<td>Rs.000</td>
</tr>
<tr>
<td>The Group Profit for the year ended 31st December 2006</td>
<td></td>
<td></td>
</tr>
<tr>
<td>less: income tax expense</td>
<td>3,095,211</td>
<td>2,008,350</td>
</tr>
<tr>
<td>group profit for the period</td>
<td>2,757,636</td>
<td>1,794,337</td>
</tr>
<tr>
<td>less: minority interest</td>
<td>36,530</td>
<td>24,116</td>
</tr>
<tr>
<td>unappropriated profit brought forward from previous year</td>
<td>1,141,653</td>
<td>642,660</td>
</tr>
<tr>
<td>transfer from capital reserve (revaluation surplus on property disposed)</td>
<td>-</td>
<td>19,251</td>
</tr>
<tr>
<td>unappropriated profit</td>
<td>46,377</td>
<td>-</td>
</tr>
<tr>
<td>balance available for appropriation</td>
<td>3,447,136</td>
<td>2,432,332</td>
</tr>
</tbody>
</table>

### Appropriations

<table>
<thead>
<tr>
<th></th>
<th>2006</th>
<th>2005</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Rs.000</td>
<td>Rs.000</td>
</tr>
<tr>
<td>transfer to general reserve</td>
<td>1,150,000</td>
<td>850,000</td>
</tr>
<tr>
<td>transfer to reserve fund</td>
<td>45,000</td>
<td>55,000</td>
</tr>
<tr>
<td>25% interim dividend paid (20% - 2005)</td>
<td>294,412</td>
<td>235,529</td>
</tr>
<tr>
<td>final dividend 2005/2004.</td>
<td>235,529</td>
<td>150,150</td>
</tr>
<tr>
<td>balance carried forward as at 31.12.2006</td>
<td>1,722,195</td>
<td>1,141,653</td>
</tr>
</tbody>
</table>

### Taxation

It is the Bank’s policy to provide for deferred taxation on all known timing differences on the liability method.

### Income tax rate applicable on the Bank’s domestic operations and FCBU on-shore Banking Operations is 35%. The off-shore operations of the FCBU is taxed at 20%.

### Statutory Payments

The Directors, to the best of their knowledge and belief are satisfied that all statutory payments in relation to the government and the employees have been made up to date.

### Dividends

The Directors recommend a 25% (2005 – 20%) Final Dividend to be paid on 10th April 2007 to holders of Issued and paid up Ordinary shares of the Company as at the close of business on 29th March 2007 subject to tax from the balance carried forward as at 31.12.2006 (Note 29). This Dividend together with the Interim Dividend of 25% (2005 - 20%) paid on 11th December 2006 amounts to a total dividend of 50% (2005 - 40%) for the year 2006.

A part of the interim dividend paid for the year represents a redistribution of the exempt dividends received by the company and will therefore be free of income tax in the hands of the shareholders. On this basis 94.25% of the 25% Interim dividend paid for 2006 is subject to taxation.

### Corporate Donations

During the year the Bank made donations amounting to Rs. 33,477,000/- (2005 – Rs. 19,641,891/-) in terms of the resolution passed at the last Annual General Meeting. No donations have been made to Government approved charities during the year (2005 – Rs. 540,860/-).

### Customers

One of the Bank’s primary objectives is to provide a caring customer service. To achieve this the Bank carries out regular customer service campaigns amongst its entire staff on the provision of a Courteous, Friendly and Caring Service to its customers. In addition the Bank also carries out customer awareness programmes at Branch level on new products and services offered by the Bank. The Bank offers financial services to both corporate and retail customers.

### Suppliers

It is the Bank’s policy to call for competitive quotations for the supply of goods and services. Suppliers of goods and services are paid promptly.

### Employment Policies

The Bank endeavours to employ, train, develop and retain the best talent available. The needs of the organization propel the employment policies of the Bank which are accordingly tuned from time to time.

A manpower plan is prepared at the beginning of each year on the basis of which recruitment levels are defined. Aspects including Information Technology, Profitability, Projected Growth, Overhead to Net Income Ratio, Optimum Utilization of Resources, Productivity, Work Volumes and Multi Skills come into play when deciding on staff in-take.

Being an equal opportunity employment company, males and females from varying racial, religious and social backgrounds are recruited. Moreover, the island-wide branch network of the Bank provides ample opportunities to youth from the various districts and remote areas to secure employment, provided they satisfy the necessary eligibility criteria.

The Bank fills vacancies through external and internal sources in accordance with the schemes of recruitment which are applicable to different categories of jobs. Due process is followed and every endeavour taken to recruit staff who would fit different jobs. Induction and placement are key aspects in the process of recruitment and selection while strategies are employed to develop and retain staff on a continuous basis.

### Capital Expenditure

The total capital expenditure on acquisition of Property, Plant & Equipment, Intangible Assets and Investment Property amounted to Rs. 586,184,000/- (2005 - 545,681,000/-) details of which are given in Notes 20,21 and 22 to the Financial Statements. Capital Expenditure approved and contracted for after the year end is given in Note 33 to the Financial Statements.

### Property, Plant & Equipment

The details of the property, plant, and equipment of the company are shown in Note 21 on page 142.

### Market Value of Freehold Properties

The value of freehold properties owned by the Bank as at 31st December 2006 is included in the accounts at Rs. 1,407,735,000/- (2005 – Rs. 1,579,147,000/-). A panel of Chartered
Valuers/Licensed Surveyors carried out a re-valuation of the Bank’s freehold properties in December 1993. The details of freehold properties owned by the Bank are shown in Note 21(b) on pages 144 to 147.

Reserves
The Group Reserves consist of:

<table>
<thead>
<tr>
<th>Reserve Type</th>
<th>2006</th>
<th>2005</th>
</tr>
</thead>
<tbody>
<tr>
<td>Share Premium</td>
<td>2,704,096</td>
<td>2,764,096</td>
</tr>
<tr>
<td>Capital Reserve</td>
<td>240,262</td>
<td>356,639</td>
</tr>
<tr>
<td>Reserve Fund</td>
<td>669,707</td>
<td>624,707</td>
</tr>
<tr>
<td>Repairs &amp; Renovation Reserve</td>
<td>6,700</td>
<td>6,700</td>
</tr>
<tr>
<td>Revenue Reserve</td>
<td>8,117,195</td>
<td>6,386,653</td>
</tr>
<tr>
<td>Total</td>
<td>11,737,760</td>
<td>10,028,795</td>
</tr>
</tbody>
</table>

The movement in these reserves is shown in the Statement of Changes in Equity on page 108.

Share Capital
The total issued and fully paid up capital as at 31st December 2006 was Rs. 1,177,647,000/- consisting of 94,664,700 ordinary shares of Rs. 10/- each voting and 23,100,000 ordinary shares of Rs. 10/- each non-voting.

Shareholding
As at 31st December 2006 there were 14,655 Registered shareholders. The distribution is indicated on pages 187 and 191.

Share Information
Information relating to earnings, dividend, net assets and market price per share is given in Financial Highlights on page 2 of the Annual Report. Information on share trading is given in Note 3 on page 188 of the Annual Report.

Major Shareholders
The twenty largest voting shareholders of the Bank as at 31st December 2006 are given on page 191 together with an analysis of the shareholding.

Future Developments
Information relating to the future developments in the operations of the Bank which will not, in the opinion of the Directors, be prejudicial to the Bank’s interest, is contained in the Chairman’s Statement and Managing Director’s Review of operations.

The Bank whilst implementing and reviewing strategies specified under its business plan, would closely monitor the possible challenges imposed by the fiscal and monetary policy framework. The Bank would continue the initiatives taken in extending the reach by aggressively increasing the branch network island wide and constantly improving the delivery and distribution channels specifically with the use of IT. The Bank also intends to draw synergies from its subsidiaries to harness greater business opportunities for the Group and consolidate the relationships developed so far for better profitability.

Directors
The Board of Directors of Hatton National Bank Limited consists of nine Directors with wide financial and commercial knowledge and experience.

The Directors of the Company and their experience as at the date of the report are shown on pages 12 and 13.

In accordance with the provisions of Article 87 of the Articles of Association, Mr R T Wijetilleke and Mr D H S Jayawardena retire by rotation and both being eligible offer themselves for re-election with the unanimous support of the Board.

In accordance with the provisions of Article 93 of the Articles of Association, Mr M V Theagarajah offers himself for re-election with the unanimous support of the Board. Special Notice have been given pursuant to Sections 138 and 192 of the Companies’ Act No. 17 of 1982 of the intention to propose a Special Resolution for such re-election, notwithstanding the age limit of 70 years stipulated by section 181 of the Companies Act.

Directors’ Interests
Directors’ interests in contracts with the Company, both direct and indirect are referred to in Note 34 to the Accounts. These interests have been declared at the Directors’ Meeting held on 25th January, 2007. The Directors have no direct or indirect interest in any other contract or proposed contract with the company.

Directors’ Interest in Shares and Debentures
Shareholdings of Directors together with their spouses and dependent children are as follows:

<table>
<thead>
<tr>
<th>Director</th>
<th>As at 31/12/06</th>
<th>As at 31/12/05</th>
</tr>
</thead>
<tbody>
<tr>
<td>Mr R T Wijetilleke</td>
<td>3,913</td>
<td>3,913</td>
</tr>
<tr>
<td>Dr V P Vittachi</td>
<td>5,005</td>
<td>5,005</td>
</tr>
<tr>
<td>Mr R Theagarajah</td>
<td>9,322</td>
<td>9,322</td>
</tr>
<tr>
<td>Mr D H S Jayawardena</td>
<td>5,005</td>
<td>5,005</td>
</tr>
<tr>
<td>Mr M V Theagarajah</td>
<td>133,374</td>
<td>120,974</td>
</tr>
<tr>
<td>Mr R K Obeyesekere</td>
<td>5,005</td>
<td>5,005</td>
</tr>
<tr>
<td>Mrs P C Cooray</td>
<td>12,505</td>
<td>12,505</td>
</tr>
<tr>
<td>Mr R Sivarathnam</td>
<td>5,040</td>
<td>5,040</td>
</tr>
<tr>
<td>Mr D R Ghazalli</td>
<td>500</td>
<td>-</td>
</tr>
</tbody>
</table>

No Director directly holds debentures of the Bank

There has been no change in their interests between 31st December 2006 and 15th February 2007 being the date of Notice of the Annual General Meeting.

Events occurring after the Balance Sheet date
No circumstances have arisen, since the balance sheet date which would require adjustments to or disclosure in the Financial Statements, except those disclosed in the Note 38 to the Financial Statements.

Annual General Meeting
The 38th Annual General Meeting of the Bank is convened on Thursday the 29th day of March 2007 at 10.00 in the forenoon at the Auditorium on Level 22 of “HNB Towers” (Registered Office) at No: 479, T.B. Jayah Mawatha, Colombo 10. The Notice of the 38th Annual General Meeting is on page 197 of this Report.

The Auditors
The retiring Auditors KPMG Ford, Rhodes, Thornton & Company have expressed their willingness to continue in office. In accordance with the Companies Act No: 17 of 1982, a resolution relating to their re-appointment and authorising the Directors to fix their remuneration will be proposed at the forthcoming Annual General Meeting.

By Order of the Board

Indrani Goonesekera  
Deputy General Manager (Legal) Board Secretary  
15th February, 2007  
Colombo, Sri Lanka
The Bank’s Financial Statements for the year ended 31st December 2006 prepared and presented in this report are in conformity with the requirements of Sri Lanka Accounting Standards, the Banking Act No: 30 of 1988, the amendments thereto and Companies Act No. 17 of 1982. The Financial Statements reflect a true and fair view of the state of affairs of the Group as at the date. Financial information presented in this report is consistent with that in the Financial Statements.

The Board of Directors has instituted effective and comprehensive systems of Internal Control. This comprises Internal Check, Internal Audit and the whole system of financial and other controls required to carry on the business of banking in an orderly manner, safeguard its assets and secure as far as practicable the accuracy and reliability of the records.

The Bank’s Auditors, KPMG Ford Rhodes, Thornton & Co. carry out reviews and test checks on effective internal control as they consider appropriate and necessary for providing their opinion on the Financial Statements.

The Board of Directors oversee the management’s responsibilities for financial reporting through their regular meeting reviews and the Audit Committee. The Audit Committee comprises three non-executive directors who are responsible for reviewing and approving financial information contained in the Annual Report and overseeing the management’s responsibilities for the preparation and presentation of Financial Statements and the effectiveness of the internal control system in the Bank. Mr R. Seevaratnam former partner, KPMG Ford Rhodes Thornton & Co functions as a Consultant to the Committee. The Board of Directors also reviews interim Financial Statements prior to their release. The Chief Financial Officer is required to submit a report explaining the fundamental accounting principles adopted and material variances in order that the Board of Directors may examine and obtain, all information and explanation required to ensure the reliability of the financial information presented therein.

KPMG Ford Rhodes Thornton & Co are the auditors appointed by the shareholders on the recommendation of the Audit Committee. They have examined the Financial Statements made available by the Board of Directors together with all financial records, related data, minutes of shareholders and Directors meetings and express their opinion which appears as reported by the Auditors on page 105 of the annual report.

By Order of the Board

Indrani Goonesekeara
Deputy General Manager
(Legal) Board Secretary
15th February, 2007
Colombo, Sri Lanka
Composition
The Audit Committee comprises three Non-Executive Directors a majority of whom are independent. Mr Ranjan Seevaratnam who is a fellow member of the Institute of Chartered Accountants of Sri Lanka and the Institute of Chartered Accountants, England & Wales and considered a financial expert with wide experience in audit and governance best practices, serves on the audit committee in the capacity of a consultant.

The Directors serving on the Audit Committee are:
Mr R Sivaratnam (Chairman)
Mr D H S Jayawardena
Mrs P C Cooray

The Company Secretary functions as the Secretary to the Audit Committee.

Meetings
The Audit Committee met four times during the year. Attendance by the committee members at each of these meetings is given in the table on page 97. The MD/CEO, CFO and the Internal Auditor also attended these meetings by invitation.

The consultant was in communication with the Internal Audit team and other key management personnel several times during the year.

Financial Reporting
The Committee, as part of its responsibility to oversee the Bank’s financial reporting process on behalf of the Board of Directors, has reviewed and discussed with the Management the annual and the quarterly financial statements prior to their release, including the extent of compliance with the Sri Lanka Accounting Standards and disclosure requirements. Matters of special interest in the current environment and the processes that support certifications of the financial statements by the Bank’s MD/CEO and CFO were also brought up for discussion.

The Committee also confirmed with the Chief Financial Officer that financial reporting requirements relating to the GDR listing have been complied with.

Risks and Controls
During the year, the Committee reviewed the effectiveness of the framework of the Bank’s systems of internal control and has received quarterly reports on all unexpected losses resulting from frauds or operational failures.

The Committee has reviewed the processes for identification, evaluation and management of all significant risks throughout the Bank. The Committee received reports on all significant matters discussed by the Risk Committee.

External Audit
The Audit Committee undertook the annual evaluation of the independence and objectivity of the External Auditor and the effectiveness of the audit process.

The Committee met with the External Auditor during the year to discuss the internal control report and their audit approach and procedures, including matters relating to the scope and auditor independence. The lead audit partner is rotated every five years.

The Committee reviewed the internal control report issued by the external auditor together with the management responses thereto.

The Audit Committee reviewed the non-audit services provided by the external auditor and was of the view that such services were not within the category of services identified as restricted under:

(i) The guideline issued by the Central Bank of Sri Lanka, for external auditors, relating to their statutory duties in terms of section 39 of Banking Act No.30 of 1988 and as amended by Banking Act No.33 of 1995.

(ii) The guidelines for Listed Companies on Audit and Audit Committees issued by the Securities and Exchange Commission of Sri Lanka.

The Letter of Representation issued to the External Auditors was tabled at an Audit Committee meeting.

The Audit Committee has recommended to the Board the remuneration and the re-appointment of KPMG Ford, Rhodes, Thornton & Co. for approval by the shareholders at the Annual General Meeting.

Internal Audit
During the year, the Audit Committee reviewed the performance of the internal audit function, the findings of the audits completed, the Department’s resource requirements including succession planning and also approved the internal audit plan.

During the year under review, a vacancy arose for the position of Head of Internal Audit. The Committee is in the process of evaluating a suitable candidate for the post.

Regulatory Compliance
The Committee reviewed the procedures established by management for compliance with the requirements of regulatory bodies. Assistant General Manager Risk & Compliance submitted to the Audit Committee on a quarterly basis, a report on the extent to which the Bank was in compliance with mandatory banking and statutory requirements.

Committee Evaluation
A self evaluation on the effectiveness of the Committee was carried out during the year.

Others
The Audit Committee reviewed issues relating to breach of ethics 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.

R Sivaratnam
Chairman
15th February, 2007
Colombo, Sri Lanka.
REPORT OF THE AUDITORS

TO THE MEMBERS OF
HATTON NATIONAL BANK LIMITED

We have audited the balance sheet of Hatton National Bank Ltd as at 31 December 2006, the consolidated balance sheet of the Company and its subsidiaries as at that date, and the related statements of income, changes in equity and cash flows for the year then ended, together with the accounting policies and notes exhibited on pages 106 to 172 of the Annual Report.

Respective Responsibilities of Directors and Auditors

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

Basis of Opinion

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

Opinion

In our opinion, so far as appears from our examination, the Company maintained proper books of account for the year ended 31 December 2006, and to the best of our information and according to the explanations given to us, the said balance sheet and related statements of income, changes in equity and cash flows and the accounting policies and notes thereto, which are in agreement with the said books and have been prepared and presented in accordance with the Sri Lanka Accounting Standards, provide the information required by the Companies Act No 17 of 1982 and the Banking Act No.30 of 1988 and give a true and fair view of the Company’s state of affairs as at 31 December 2006 and of its profit and cash flow for the year then ended.

In our opinion, the consolidated balance sheet and related statements of income, changes in equity and cash flows and the accounting policies and notes thereto have been properly prepared and presented in accordance with the Companies Act No 17 of 1982, the Banking Act No.30 of 1988 and the Sri Lanka Accounting Standards, and give a true and fair view of the state of affairs as at 31 December 2006, and of its profit and cash flow for the year then ended of the Company and its subsidiaries dealt with thereby, so far as concerns the members of the Company.

Directors’ Interests in Contracts with the Company

According to the information made available to us, the directors of the Company were not directly or indirectly interested in contracts with the Company during the year ended 31 December 2006, except as stated in Note 34 to these financial statements.

CHARTERED ACCOUNTANTS

15th February, 2007
Colombo, Sri Lanka.
## Income Statement

For the year ended 31st December

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Rs.000</td>
<td>Rs.000</td>
<td>Rs.000</td>
<td>Rs.000</td>
</tr>
<tr>
<td><strong>INCOME</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>1</td>
<td>21,513,173</td>
<td>16,915,314</td>
<td>23,233,201</td>
<td>18,216,726</td>
</tr>
<tr>
<td>Interest income</td>
<td>2</td>
<td>18,451,961</td>
<td>14,129,874</td>
<td>19,321,247</td>
</tr>
<tr>
<td>Less: Interest expenses</td>
<td>3</td>
<td>9,816,927</td>
<td>7,280,851</td>
<td>10,807,794</td>
</tr>
<tr>
<td>Net interest income</td>
<td></td>
<td>8,635,034</td>
<td>6,849,023</td>
<td>8,513,453</td>
</tr>
<tr>
<td>Foreign exchange profit</td>
<td></td>
<td>792,303</td>
<td>666,460</td>
<td>792,699</td>
</tr>
<tr>
<td>Fee and commission income</td>
<td></td>
<td>1,795,340</td>
<td>1,663,545</td>
<td>1,860,960</td>
</tr>
<tr>
<td>Dividend income</td>
<td>4</td>
<td>76,983</td>
<td>65,050</td>
<td>56,842</td>
</tr>
<tr>
<td>Other income</td>
<td>5</td>
<td>396,586</td>
<td>410,385</td>
<td>1,201,453</td>
</tr>
<tr>
<td><strong>OPERATING INCOME</strong></td>
<td></td>
<td>11,696,246</td>
<td>9,634,463</td>
<td>12,425,407</td>
</tr>
<tr>
<td>Less: OPERATING EXPENSES</td>
<td>6</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Personnel costs</td>
<td></td>
<td>2,765,728</td>
<td>2,415,295</td>
<td>2,894,711</td>
</tr>
<tr>
<td>Premises, equipment and establishment expenses</td>
<td></td>
<td>1,905,132</td>
<td>1,732,762</td>
<td>1,751,975</td>
</tr>
<tr>
<td>Fee and commission expenses</td>
<td></td>
<td>102,036</td>
<td>116,611</td>
<td>124,051</td>
</tr>
<tr>
<td>Provision for staff retirement benefits</td>
<td></td>
<td>399,189</td>
<td>326,361</td>
<td>400,602</td>
</tr>
<tr>
<td>Bad debts written off</td>
<td></td>
<td>404,036</td>
<td>23,477</td>
<td>10,796</td>
</tr>
<tr>
<td>Provision for loan losses</td>
<td>7</td>
<td>931,828</td>
<td>1,759,444</td>
<td>931,828</td>
</tr>
<tr>
<td>Provision for fall in value of investments</td>
<td></td>
<td>-</td>
<td>-</td>
<td>9,482</td>
</tr>
<tr>
<td>Amortization of goodwill/(negative goodwill)</td>
<td></td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Other expenses</td>
<td></td>
<td>2,560,678</td>
<td>1,410,551</td>
<td>3,220,368</td>
</tr>
<tr>
<td><strong>PROFIT FROM OPERATIONS</strong></td>
<td></td>
<td>8,676,796</td>
<td>7,794,801</td>
<td>9,343,813</td>
</tr>
<tr>
<td>Share of Associate Companies’ profit before taxation</td>
<td></td>
<td>3,019,450</td>
<td>1,869,962</td>
<td>3,081,594</td>
</tr>
<tr>
<td><strong>PROFIT BEFORE TAXATION</strong></td>
<td></td>
<td>3,019,450</td>
<td>1,869,962</td>
<td>3,095,211</td>
</tr>
<tr>
<td>Less: Income tax expense</td>
<td>8</td>
<td>798,961</td>
<td>195,400</td>
<td>819,575</td>
</tr>
<tr>
<td><strong>PROFIT FOR THE PERIOD</strong></td>
<td></td>
<td>2,220,489</td>
<td>1,674,562</td>
<td>2,275,636</td>
</tr>
<tr>
<td>Attributable to:</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Equity Holders of the Bank</td>
<td></td>
<td>2,220,489</td>
<td>1,654,562</td>
<td>2,239,106</td>
</tr>
<tr>
<td>Minority Interest</td>
<td></td>
<td>-</td>
<td>-</td>
<td>36,530</td>
</tr>
<tr>
<td><strong>PROFIT FOR THE PERIOD</strong></td>
<td></td>
<td>2,220,489</td>
<td>1,654,562</td>
<td>2,275,636</td>
</tr>
<tr>
<td><strong>BASIC EARNINGS PER SHARE (Rs.)</strong></td>
<td></td>
<td>18.86</td>
<td>15.09</td>
<td>19.01</td>
</tr>
<tr>
<td><strong>DIVIDEND PER SHARE (Rs.)</strong></td>
<td></td>
<td><em>5.00</em></td>
<td>4.00</td>
<td><em>5.00</em></td>
</tr>
</tbody>
</table>

The Significant Accounting Policies and the Notes from pages 110 to 172 form an integral part of these financial statements.

*Calculated on Interim Dividend paid and Final Dividend proposed, which is to be approved at the Annual General Meeting.*
## Bank Group

### Balance Sheet

As at 31st December

<table>
<thead>
<tr>
<th>Note</th>
<th>Bank 2006 Rs.000</th>
<th>Bank 2005 Rs.000</th>
<th>Group 2006 Rs.000</th>
<th>Group 2005 Rs.000</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>ASSETS</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Cash and cash equivalents</td>
<td>10 23,308,095</td>
<td>21,200,074</td>
<td>23,343,809</td>
<td>21,193,935</td>
</tr>
<tr>
<td>Statutory deposit with Central Bank of Sri Lanka</td>
<td>11 12,016,532</td>
<td>8,565,629</td>
<td>12,016,532</td>
<td>8,565,629</td>
</tr>
<tr>
<td>Government Treasury Bills</td>
<td>- 139,340</td>
<td>2,451,695</td>
<td>2,001,340</td>
<td>-</td>
</tr>
<tr>
<td>Commercial papers</td>
<td>290,667</td>
<td>434,073</td>
<td>290,667</td>
<td>434,073</td>
</tr>
<tr>
<td>Securities purchased under re-sale agreements</td>
<td>-</td>
<td>-</td>
<td>4,393,281</td>
<td>3,881,251</td>
</tr>
<tr>
<td>Dealing securities</td>
<td>12 738,719</td>
<td>313,113</td>
<td>975,153</td>
<td>319,707</td>
</tr>
<tr>
<td>Investment securities</td>
<td>13 21,006,789</td>
<td>17,284,945</td>
<td>22,659,639</td>
<td>18,816,494</td>
</tr>
<tr>
<td>Bills of Exchange</td>
<td>14 1,910,852</td>
<td>2,026,977</td>
<td>1,910,852</td>
<td>2,026,977</td>
</tr>
<tr>
<td>Loans and advances</td>
<td>15 114,708,374</td>
<td>96,242,465</td>
<td>114,708,374</td>
<td>96,242,465</td>
</tr>
<tr>
<td>Lease rentals receivable within one year</td>
<td>16 3,796,067</td>
<td>3,112,469</td>
<td>3,796,067</td>
<td>3,112,469</td>
</tr>
<tr>
<td>Lease rentals receivable after one year</td>
<td>16 7,756,408</td>
<td>5,751,882</td>
<td>7,756,408</td>
<td>5,751,882</td>
</tr>
<tr>
<td>Non-current assets held for sale</td>
<td>17 6,556</td>
<td>-</td>
<td>6,556</td>
<td>-</td>
</tr>
<tr>
<td>Investments in Associate Companies</td>
<td>18 132,326</td>
<td>132,326</td>
<td>164,869</td>
<td>170,592</td>
</tr>
<tr>
<td>Investments in Subsidiary Companies</td>
<td>19 2,293,663</td>
<td>2,293,663</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Investment properties</td>
<td>20 189,855</td>
<td>-</td>
<td>189,855</td>
<td>-</td>
</tr>
<tr>
<td>Property, Plant and Equipment</td>
<td>21 2,907,789</td>
<td>3,059,478</td>
<td>2,026,977</td>
<td>3,059,478</td>
</tr>
<tr>
<td>Total Assets</td>
<td>196,429,028</td>
<td>166,012,410</td>
<td>206,978,564</td>
<td>174,987,105</td>
</tr>
<tr>
<td><strong>LIABILITIES</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Deposits from customers</td>
<td>24 147,882,025</td>
<td>128,283,681</td>
<td>147,787,806</td>
<td>128,130,801</td>
</tr>
<tr>
<td>Dividends payable</td>
<td>25 38,103</td>
<td>50,291</td>
<td>38,103</td>
<td>50,291</td>
</tr>
<tr>
<td>Borrowings</td>
<td>26 11,031,501</td>
<td>3,940,111</td>
<td>11,031,501</td>
<td>3,940,111</td>
</tr>
<tr>
<td>Securities sold under re-purchase agreements</td>
<td>6,736,714</td>
<td>6,113,644</td>
<td>12,103,873</td>
<td>12,103,873</td>
</tr>
<tr>
<td>Bills payable</td>
<td>1,190,056</td>
<td>2,226,745</td>
<td>1,190,056</td>
<td>2,226,745</td>
</tr>
<tr>
<td>Long-term insurance fund</td>
<td>27 -</td>
<td>-</td>
<td>507,721</td>
<td>300,818</td>
</tr>
<tr>
<td>Non-life insurance reserves</td>
<td>28 -</td>
<td>-</td>
<td>319,538</td>
<td>267,020</td>
</tr>
<tr>
<td>Subordinated debentures</td>
<td>29 5,120,000</td>
<td>4,000,000</td>
<td>5,796,791</td>
<td>5,796,791</td>
</tr>
<tr>
<td>Current tax liability</td>
<td>20 761,729</td>
<td>5,992</td>
<td>774,035</td>
<td>36,826</td>
</tr>
<tr>
<td>Deferred tax liability</td>
<td>30 313,756</td>
<td>313,756</td>
<td>317,675</td>
<td>316,317</td>
</tr>
<tr>
<td>Other liabilities</td>
<td>31 10,425,336</td>
<td>9,838,930</td>
<td>10,940,075</td>
<td>10,282,275</td>
</tr>
<tr>
<td>Total Liabilities</td>
<td>183,499,220</td>
<td>156,773,150</td>
<td>193,882,631</td>
<td>163,631,868</td>
</tr>
<tr>
<td><strong>EQUITY</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Share capital - Voting</td>
<td>32 946,647</td>
<td>946,647</td>
<td>946,647</td>
<td>946,647</td>
</tr>
<tr>
<td>Share capital - Non-Voting</td>
<td>32 231,000</td>
<td>231,000</td>
<td>231,000</td>
<td>231,000</td>
</tr>
<tr>
<td>Statutory Reserve Fund</td>
<td>669,707</td>
<td>669,707</td>
<td>669,707</td>
<td>669,707</td>
</tr>
<tr>
<td>Retained Earnings</td>
<td>1,736,396</td>
<td>1,736,396</td>
<td>1,736,396</td>
<td>1,736,396</td>
</tr>
<tr>
<td>Other reserves</td>
<td>9,346,058</td>
<td>8,262,435</td>
<td>9,346,058</td>
<td>8,262,435</td>
</tr>
<tr>
<td>Total Equity attributable to Equity Holders of the Bank</td>
<td>12,929,808</td>
<td>11,239,260</td>
<td>12,915,607</td>
<td>11,206,442</td>
</tr>
<tr>
<td>Minority Interest</td>
<td>-</td>
<td>-</td>
<td>180,326</td>
<td>148,795</td>
</tr>
<tr>
<td>Total Equity</td>
<td>12,929,808</td>
<td>11,239,260</td>
<td>13,095,933</td>
<td>11,355,237</td>
</tr>
<tr>
<td><strong>Total Liabilities and Equity</strong></td>
<td>196,429,028</td>
<td>165,958,520</td>
<td>206,978,564</td>
<td>174,987,105</td>
</tr>
<tr>
<td><strong>Commitments and Contingencies</strong></td>
<td>33</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>44,784,964</td>
<td>44,784,964</td>
<td>44,784,964</td>
<td>44,784,964</td>
</tr>
</tbody>
</table>

The Significant Accounting Policies and the Notes from pages 110 to 172 form an integral part of these financial statements.

For and on behalf of the Board

Rienzie T Wijetilleke
Chairman

Dr V P Vittachi
Deputy Chairman

Rajendra Theagarajah
Managing Director /
Chief Executive Officer

Indrani Goonesekera
Deputy General Manager /
Legal/Board Secretary

Thursday 15th, February 2007
Colombo, Sri Lanka

Annual Report 2006

107
## Statement of Changes in Equity

For the year ended 31st December 2006

<table>
<thead>
<tr>
<th>Share Capital</th>
<th>Statutory Reserve Fund</th>
<th>Other Reserves</th>
<th>Retained Earnings</th>
<th>Minority Interest</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bank</td>
<td>Voting Shares</td>
<td>Non-Voting Shares</td>
<td>Rs.000</td>
<td>Rs.000</td>
<td>Rs.000</td>
</tr>
<tr>
<td>Balance as at 31.12.2004</td>
<td>770,000</td>
<td>231,000</td>
<td>569,707</td>
<td>1,962,246</td>
<td>325,890</td>
</tr>
<tr>
<td>Transfer of revaluation surplus on property disposed</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>(19,251)</td>
<td>-</td>
</tr>
<tr>
<td>Share issue as underlying for Global Depository Receipts</td>
<td>176,647</td>
<td>-</td>
<td>-</td>
<td>741,850</td>
<td>-</td>
</tr>
<tr>
<td>Net profit for the year 2005</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Final dividend for 2004</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Interim dividend for 2005</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Transfers during the year 2005</td>
<td>-</td>
<td>-</td>
<td>55,000</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Balance as at 31.12.2005</td>
<td>946,647</td>
<td>231,000</td>
<td>624,707</td>
<td>2,704,096</td>
<td>386,639</td>
</tr>
<tr>
<td>Net profit for the year 2006</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Final dividend for 2005</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Interim dividend for 2005</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Transfers during the year 2005</td>
<td>-</td>
<td>-</td>
<td>45,000</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Balance as at 31.12.2006</td>
<td>946,647</td>
<td>231,000</td>
<td>669,707</td>
<td>2,704,096</td>
<td>386,639</td>
</tr>
</tbody>
</table>

Statutory Reserve Fund represents the statutory requirement in terms of section 20 (1) and (2) of the Banking Act No. 30 of 1988.

Share Premium account is generally used for writing-off of share issue expenses. There are no restrictions on the distribution of balance to shareholders.

Capital Reserve relates to revaluation of Freehold Land & Buildings carried out in 1989 and 1993 and includes the surplus on revaluation of those assets.

General Reserve comprises the amounts appropriated by the Board of Directors as a general banking reserve.

Repairs and Renovation Reserve includes the amounts allocated for repairs and renovation.

The Significant Accounting Policies and the Notes from pages 110 to 172 form an integral part of these financial statements.
## Cash Flow Statement

For the year ended 31st December

<table>
<thead>
<tr>
<th></th>
<th>Bank</th>
<th>Group</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>2006</td>
<td>2005</td>
</tr>
<tr>
<td></td>
<td>Rs.000</td>
<td>Rs.000</td>
</tr>
<tr>
<td><strong>Cash flows from operating activities</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Interest and commission receipts</td>
<td>20,247,301</td>
<td>15,793,419</td>
</tr>
<tr>
<td>Interest payments</td>
<td>(9,816,927)</td>
<td>(7,280,851)</td>
</tr>
<tr>
<td>Receipts from other operating activities</td>
<td>1,017,922</td>
<td>860,276</td>
</tr>
<tr>
<td>Cash payments to employees</td>
<td>(3,164,917)</td>
<td>(2,741,656)</td>
</tr>
<tr>
<td>Cash payments to suppliers</td>
<td>(1,373,520)</td>
<td>(1,238,441)</td>
</tr>
<tr>
<td>Payments for other operating activities</td>
<td>(2,801,356)</td>
<td>(1,529,384)</td>
</tr>
<tr>
<td>Operating profit before changes in operating assets and liabilities [Note (a)]</td>
<td>4,108,503</td>
<td>3,863,363</td>
</tr>
<tr>
<td><strong>Increase/(Decrease) in operating assets:</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Treasury bills/commercial papers</td>
<td>282,746</td>
<td>108,702</td>
</tr>
<tr>
<td>Deposits held for regulatory or monetary control purposes</td>
<td>(3,450,903)</td>
<td>554,762</td>
</tr>
<tr>
<td>Loans and advances</td>
<td>(21,939,672)</td>
<td>(16,898,628)</td>
</tr>
<tr>
<td>Other short term assets</td>
<td>123,722</td>
<td>525,399</td>
</tr>
<tr>
<td><strong>Increase/(Decrease) in operating liabilities:</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Deposits from customers</td>
<td>19,884,021</td>
<td>10,573,449</td>
</tr>
<tr>
<td>Negotiable certificates of deposit</td>
<td>(285,677)</td>
<td>(813,702)</td>
</tr>
<tr>
<td>Other liabilities</td>
<td>(1,036,689)</td>
<td>558,371</td>
</tr>
<tr>
<td>Net cash from operating activities before income tax</td>
<td>(2,313,949)</td>
<td>471,816</td>
</tr>
<tr>
<td>Income taxes paid</td>
<td>-</td>
<td>(21,210)</td>
</tr>
<tr>
<td><strong>Net cash generated from/(used in) operating activities</strong></td>
<td>(2,313,949)</td>
<td>471,816</td>
</tr>
<tr>
<td><strong>Cash flows from investing activities</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Dividend income</td>
<td>76,983</td>
<td>65,050</td>
</tr>
<tr>
<td>Income from investment securities</td>
<td>188,141</td>
<td>122,433</td>
</tr>
<tr>
<td>Net proceeds from sale of securities</td>
<td>(2,966,402)</td>
<td>284,526</td>
</tr>
<tr>
<td>Net proceeds from sale of investment securities</td>
<td>(3,932,135)</td>
<td>(312,520)</td>
</tr>
<tr>
<td>Purchase of Property, Plant &amp; Equipment</td>
<td>(483,396)</td>
<td>(312,520)</td>
</tr>
<tr>
<td>Purchase of Intangible assets</td>
<td>(21,200)</td>
<td>184,091</td>
</tr>
<tr>
<td>Improvements to Investment properties</td>
<td>(25)</td>
<td>-</td>
</tr>
<tr>
<td>Net cash used in investing activities</td>
<td>(4,456,766)</td>
<td>(516,951)</td>
</tr>
<tr>
<td><strong>Cash flows from financing activities</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Increase in Debentures</td>
<td>1,120,000</td>
<td>-</td>
</tr>
<tr>
<td>Increase of borrowings</td>
<td>7,714,460</td>
<td>284,526</td>
</tr>
<tr>
<td>Net increase in other liabilities</td>
<td>586,405</td>
<td>(639,590)</td>
</tr>
<tr>
<td>Dividends paid</td>
<td>(542,129)</td>
<td>(443,687)</td>
</tr>
<tr>
<td>Proceeds from issue of shares</td>
<td>-</td>
<td>918,497</td>
</tr>
<tr>
<td><strong>Net cash generated from financing activities</strong></td>
<td>8,878,736</td>
<td>1,134,527</td>
</tr>
<tr>
<td>Net increase in cash and cash equivalents</td>
<td>2,108,021</td>
<td>1,092,289</td>
</tr>
<tr>
<td>Cash and cash equivalents at beginning of the year</td>
<td>21,200,074</td>
<td>20,107,789</td>
</tr>
<tr>
<td>Cash and cash equivalents at end of the year [Note (10)]</td>
<td>23,308,095</td>
<td>21,200,074</td>
</tr>
</tbody>
</table>

### Note (a) Reconciliation of operating profit

<table>
<thead>
<tr>
<th></th>
<th>Profit before taxation</th>
<th>(188,141)</th>
<th>(152,389)</th>
<th>(188,141)</th>
<th>(151,573)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Goodwill/(Negative goodwill) amortization</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td><strong>Net cash generated from operating activities</strong></td>
<td>4,108,503</td>
<td>3,863,363</td>
<td>4,307,003</td>
<td>4,121,136</td>
<td></td>
</tr>
</tbody>
</table>
REPORTING ENTITY

The consolidated financial statements of the Bank for the year ended 31st December 2006 cover the Bank and its Subsidiaries, HNB Securities Limited, HNB Stockbrokers (Pvt) Limited, HNB Assurance Limited and Sithma Development (Pvt) Limited (together referred to as the "Group") and the Group’s interest in its Associate companies M/s Lanka Ventures Limited and Browns Engineering (Pvt) Limited.

There were no significant changes in the nature of the principal activities of the Bank and the Group during the financial year under review.

The principal activities of the Bank continued to be banking and related activities such as accepting deposits, corporate and retail credit, personal financial services, off shore banking, foreign currency operations, trade services, investment banking, development banking, rural finance, project finance, dealing in government securities, etc.

The principal activities of HNB Securities Limited, HNB Stockbrokers (Pvt) Limited, HNB Assurance Limited and Sithma Development (Pvt) Limited are dealing in government securities as primary dealer, stock brokering, insurance services and property development respectively.

The principal activities of Lanka Ventures Limited and Browns Engineering (Pvt) Limited are providing venture capital services, construction and engineering.

1. APPROVAL OF FINANCIAL STATEMENTS BY DIRECTORS
The financial statements were authorised for issue by the Board of Directors on Thursday, 15th February 2007.

2. STATEMENT OF COMPLIANCE
The Balance Sheet, Income Statement, Statement of Changes in Equity and Cash Flow Statement have been prepared in accordance with the Sri Lanka Accounting Standards laid down by the Institute of Chartered Accountants of Sri Lanka.

3. BASIS OF PREPARATION
The financial statements are prepared under historical cost convention and applied consistently with no adjustments being made for inflationary factors affecting the financial statements, except for the following:

- Land and buildings are measured at cost at the time of acquisition and subsequently at revalued amounts, which are the fair values at the date of revaluation less any accumulated depreciation and impairment losses, if any. Land and buildings are revalued on a rolling basis with the view of completing the revaluation of this class of asset within a short period.
- Dealing securities are measured at market value.
- Foreclosed properties are measured at market value on an individual property basis.

Where appropriate, the policies are explained in the accompanying notes.

The accounting policies of the Bank have been consistently applied by Group entities where applicable and any deviations have been disclosed accordingly.

4. FUNCTIONAL AND PRESENTATION CURRENCY
The financial statements are presented in Sri Lanka Rupees, which is the Group’s functional currency. Except as indicated, financial information presented in Sri Lankan Rupees has been rounded to the nearest thousand.

5. USE OF ESTIMATES AND JUDGEMENTS
The preparation of financial statements requires management to make judgments, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.
Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised and in any future periods affected.

6. MATERIALITY AND AGGREGATION
Each material item is presented separately in the financial statements. Other amounts are aggregated with amounts of similar nature or function.

7. BASIS OF CONSOLIDATION
All entities which are controlled by the Bank are consolidated in the financial statements. The consolidated financial statements are prepared on the historical cost basis except that certain assets are stated at their fair value. Such assets are dealing securities, certain land and buildings and foreclosed properties.

7.1 Subsidiaries
Subsidiaries are entities that are controlled by the Bank. Control exists when the Bank has the power, directly or indirectly, to govern the financial and operating policies of an entity so as to obtain benefits from its activities. In assessing control, potential voting rights, that presently are exercisable are taken into account. The financial statements of Subsidiaries are included in the consolidated financial statements from the date that control effectively commences until the date that control effectively ceases.

The Minority Interest are presented in the consolidated Balance Sheet within Equity, separately from the equity attributable to the Equity Holders of the Bank. Minority Interest in the profit or loss of the Group are disclosed separately in the consolidated Income Statement.

The consolidated accounts are prepared to a common financial year end of 31st December. A list of Subsidiaries within the Group is provided in Note No. 19.

7.2 Associates
Associates are entities in which the Group has significant influence, but not control over the financial and operating policies. The consolidated financial statements include the Group’s share of the total recognised gains and losses of Associates under the equity method, from the date that significant influence effectively commences until the date that significant influence effectively ceases. A list of Associates within the Group is provided in Note No. 18.

7.3 Transactions Eliminated on Consolidation
Intra-group balances and transactions and any unrealised gains arising from intra-group transactions, are eliminated in preparing the consolidated financial statements. Unrealised gains arising from transactions with Associates are eliminated to the extent of the Group’s interest in the Associate against the investments in the Associate. Unrealised losses are eliminated in the same way as unrealised gains except that they are only eliminated to the extent that there is no evidence of impairment.

8. FOREIGN CURRENCY TRANSLATION
8.1 Transactions in foreign currencies are translated to Sri Lanka Rupees at the middle rate of exchange ruling at the date of the transaction.

Monetary assets and liabilities denominated in foreign currencies are stated at historical cost at the Balance Sheet date and are translated at the middle rate of exchange ruling at that date.

Foreign exchange differences arising on the settlement or reporting of the Bank’s monetary items at rates different from those which were initially recorded are dealt with in the Income Statement.

Non-monetary assets and liabilities denominated in foreign currency that are stated at historical cost at the Balance Sheet date are translated to Sri Lanka Rupees at the foreign exchange rates ruling at that date.

8.2 Forward Exchange Contracts are valued at the forward market rates ruling on the date of the Balance Sheet. Resulting net unrealised gains and losses are dealt with through the Income Statement.
9. ASSETS AND BASES OF THEIR VALUATION

9.1 Cash and Cash equivalents
Cash and cash equivalents include cash in hand, balances with banks, placements with banks, money at call and short notice and money market funds. They are brought to account at the face value or the gross value where appropriate.

9.2 Statutory Deposit with Central Bank of Sri Lanka
The Monetary Law Act requires that all commercial banks operating in Sri Lanka maintain reserves against all deposit liabilities denominated in Sri Lanka Rupees. The reserve is an amount equal to 10% of the total of such rupee deposit liabilities.

9.3 Securities Purchased Under Re-sale Agreements
Securities purchased under re-sale agreements are recorded separately in the financial statements at cost. The difference between the purchase and sale price represents interest income and is recognized in the Income Statement over the period of the resale agreement.

9.4 Investments
9.4.1 Dealing Securities
These are marketable securities acquired and held with the intention of resale over a short period of time. Such securities are recorded at market value. Adjustment for changes in market value is accounted for in the Income Statement.

The quoted ordinary shares classified as dealing securities were recorded at the lower of cost or market value on an aggregate portfolio basis in the previous years. The requirement to mark to market was stipulated by the direction issued by the Central Bank of Sri Lanka on ”Prudential norms for classification, valuation and operation of the Bank’s investment portfolio” dated 1st March 2006.

9.4.2 Investment Securities
These are acquired and held for yield or capital growth in the medium/long term with the positive intent and ability to hold until maturity. Such securities are recorded at cost. Interest and dividend income are accrued. Changes in market values of these securities are not taken into account, unless there is considered to be a diminution in value which is other than temporary.

9.4.2(a) Amortization of Premium/Discount on Foreign Bonds
The Bank holds foreign treasury bonds as long term investments. The premium/discount on the bonds is amortized on a straight line basis over the period to maturity.

9.4.3 Investments in Subsidiaries
Investments in Subsidiaries are stated at cost in the Bank’s financial statements.

9.4.4 Investments in Associates
Investments in Associates are accounted for at cost in the Bank’s financial statements and under Equity method in the consolidated financial statements.

Under the Equity method, the investments in Associates are initially accounted for at cost, and the carrying amount is adjusted for post acquisition changes in the Group’s share of net assets of the Associates, less any impairment in the Group’s net investments in Associates.

9.5 Non-Current Assets held for Sale
Non-current assets are classified as ”Non-current assets held for sale” once identified that the carrying amount will be recovered principally through a sale transaction rather than through continuing use. These are assets which are available for immediate sale in its present condition, subject only to terms that are usual and customary for sale of such assets and its sale is highly probable.

”Non-current assets held for sale” are presented separately on the face of the balance sheet at the lower of its carrying amount and fair value less costs to sell.

Assets classified as ”Non-current assets held for sale” are neither amortized nor depreciated.
9.6 **Loans and Advances to Customers**

Loans and advances to customers are stated in the Balance Sheet at the recoverable amount represented by the gross value of the outstanding balance adjusted for provision for loan losses and interest in suspense (interest which is not accrued to revenue).

9.6.1 **Non-performing Loans**

Loans, advances and finance leases which are 90 days or more in arrears of due capital and/or interest are classified as non-performing. Provision for possible loan losses are made on the basis of a continuous review of all advances to customers, in accordance with the Sri Lanka Accounting Standard 23, “Revenue Recognition” and the directions issued by the Central Bank of Sri Lanka and disclosed in the financial statements of the Bank.

9.6.2 **Foreclosed Properties**

Foreclosed properties represent properties acquired in full or partial settlement of loans and advances and are yet to be disposed. These are accounted for at the lower of cost or market value on an individual property basis. The shortfall between the prevailing market value of the foreclosed property and the related loan outstanding is recognised as a provision for loan losses in the Income Statement during the year of acquiring the foreclosed property in satisfaction of the debt. Any shortfall between the carrying amount of the foreclosed properties and their respective market values identified subsequently is charged as a provision for loan losses in the Income Statement. Subsequent gains and losses on the disposal of the foreclosed properties are treated as provisions written back or charged to the Income Statement respectively. Foreclosed properties are recorded under loans and advances until they are disposed.

9.6.3 **Provision for Loan Losses**

Specific provisions for loan losses are made as follows:

<table>
<thead>
<tr>
<th>Period outstanding</th>
<th>Classification</th>
<th>Provision made net of realisable value of security</th>
</tr>
</thead>
<tbody>
<tr>
<td>6-12 months</td>
<td>Sub-standard</td>
<td>20%</td>
</tr>
<tr>
<td>12-18 months</td>
<td>Doubtful</td>
<td>50%</td>
</tr>
<tr>
<td>18 months and over</td>
<td>Loss</td>
<td>100%</td>
</tr>
</tbody>
</table>

The provision made relates to all categories of advances including pawning and leasing identified as sub-standard, doubtful and loss.

Where necessary, specific provisions have been made over and above the minimum percentages stipulated above, on a case by case basis.

9.6.4 **Revenue Recognition on Non-performing Loans**

When an advance is classified as non-performing as set out in Accounting Policy No. 9.6.1, interest income ceases to be recognized and is taken to income only on a cash basis.

9.6.5 **General Provision**

A general provision of 0.1% of the total portfolio of pawning facilities, 2% of the lease receivables (net of specific provision) and 0.2% of the total portfolio of Shanthi Housing Loans is made in conformity with industry practice. The direction issued by the Monetary Board of the Central Bank of Sri Lanka on 5th December 2006, in terms of Section 46 of the Banking Act No 30 of 1988, as amended on “Requirements to maintain a general provision for Advances”, requires all licensed commercial banks to maintain a general provision of 1% of the total performing loans and advances and overdue loans and advances, net of Interest in Suspense and loans and advances secured by cash deposits, gold or Government securities. The general provision is to commence with a 0.1% provision as at 31st December 2006 and thereafter, incremental provisions of 0.1% every quarter till 31st March 2009, with the view of meeting the
total provision requirement of 1% not later than 31st March 2009.

9.7 **Finance Leases**

Assets leased to customers which transfer substantially all the risks and rewards associated with ownership other than legal title, are classified as finance leases. Amounts receivable under finance leases are included under ‘Lease Rentals Receivable’. Leasing balances are stated in the Balance Sheet after deduction of initial rentals received, unearned lease income and the provisions for rentals doubtful of recovery.

**9.7.1 Provision for Lease Receivables**

Specific provision has been made in relation to identified bad and doubtful leases as stated above in Accounting Policy No 9.6.3. In addition, a general provision has been made as stated above in Accounting Policy No 9.6.5.

9.8 **Intangible Assets**

**9.8.1 Basis of Recognition**

An intangible asset is recognized if it is probable that the future economic benefits that are attributable to the asset will flow to the entity and the cost of the assets can be measured reliably.

**9.8.1 (a) Goodwill**

Goodwill arising on the acquisition represents the excess of the cost of acquisition over the Group’s interest in the net fair value of the acquiree’s identifiable assets, liabilities and contingent liabilities at the date of acquisition. Upon transition to revised Sri Lanka Accounting Standard 25 “Business Combinations”, goodwill will no longer be amortized. Instead, goodwill will be tested for impairment annually and assessed for any indication of impairment at each reporting date to ensure that its carrying amount does not exceed its recoverable amount. If an impairment loss is identified, it will be recognized immediately in the Income Statement.

**9.8.1 (b) Software**

All computer software costs incurred, licensed for use by the Bank, which are not integrally related to associated hardware, which can be clearly identified, reliably measured and its probable that they will lead to future economic benefits, are included in the Balance Sheet under the category intangible assets and carried at cost less cumulative amortization and any accumulated impairment losses.

**9.8.2 Subsequent Expenditure**

Expenditure incurred on intangible assets is capitalized only when it increases the future economic benefits embodied in the specific asset to which it relates. All other expenditure is expensed as incurred.

**9.8.3 Amortization**

Intangible assets, except for goodwill are amortized on a straight line basis in the Income Statement from the date when the asset is available for use, over the best estimate of its useful economic life. The estimated useful life of intangible assets is six years.

9.9 **Investment Properties**

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

**9.9.1 Basis of Recognition**

The Bank applies the cost model for investment properties in accordance with Sri Lanka Accounting Standard 40 - “Investment Property” (revised 2005). Accordingly, land classified as investment properties are stated at cost and buildings classified as investment properties are stated at cost less any accumulated depreciation and any accumulated impairment losses.

**9.9.2 Depreciation**

Depreciation is provided on a straight line basis over the estimated life of the class of asset.

- Hatton National Bank
  - Freehold buildings: 2.5% per annum
- Sithma Development (Pvt) Ltd
  - Freehold buildings (Smart building): 2.5% per annum
- Plant, machinery & equipment
  - integral to freehold buildings: 20% per annum

Depreciation is provided from the date of purchase up to the date of disposal.
9.9.3 Derecognition
Investment properties are derecognised when disposed of, or permanently withdrawn from use because no future economic benefits are expected. Transfers are made to and from investment property only when there is a change in use.

9.10 Property, Plant and Equipment
9.10.1 Recognition and Measurement
Property, Plant and Equipment are recorded at cost of purchase or construction or valuation together with any incidental expenses thereon less accumulated depreciation and any accumulated impairment losses.

Cost includes expenditure that is directly attributable to the acquisition of the asset. The cost of self constructed assets includes the cost of materials and direct labour, any other costs directly attributable to bringing the asset to a working condition for its intended use and the costs of dismantling and removing the items and restoring the site on which they are located. Purchased software that is integral to the functionality of the related equipment is capitalized as part of computer equipment.

The Bank applies the revaluation model for the entire class of freehold land and buildings. Such properties are carried at a revalued amount, being its fair value at the date of revaluation less any subsequent accumulated depreciation and subsequent accumulated impairment losses. Freehold land & buildings of the Bank are revalued every seven years to ensure that the carrying amounts do not differ materially from the fair values at the balance sheet date. Freehold land and buildings are revalued on a rolling basis, so as to complete the revaluation within a short period.

On revaluation of an asset, any increase in the carrying amount is credited directly to equity, under capital reserve or used to reverse a previous revaluation decrease relating to the same asset, which was debited to the Income Statement. In this circumstance, the increase is recognized as income to the extent of the previous write down. Any decrease in the carrying amount is recognized as an expense in the Income Statement or debited directly to equity under revaluation reserve to the extent of any credit balance existing in the capital reserve in respect of that asset.

The Bank applies the cost model for all the other Property, Plant and Equipment and they are carried at cost less any accumulated depreciation and any accumulated impairment losses.

9.10.2 Subsequent Costs
The cost of replacing part of an item of Property, Plant and Equipment is recognized in the carrying amount of the item if it is probable that the future economic benefits embodied within the part will flow to the Bank and its cost can be measured reliably.

The costs of day to day servicing of Property, Plant and Equipment are charged to the Income Statement as incurred.

When replacement costs are recognized in the carrying amount of an item of Property, Plant and Equipment, the remaining carrying amount of the replaced part is derecognized. Major inspection costs are capitalized. At each such capitalization, the remaining carrying amount of the previous cost of inspections is derecognised.

9.10.3 Depreciation
The Bank and its Subsidiary companies provide depreciation from the date the assets are available for use up to the date of disposal, at the following rates on a straight line basis over the periods appropriate to the estimated useful lives of the different types of assets, except for which are disclosed separately.

HNB and Subsidiary companies [except for Sithma Development (Pvt) Ltd.]

<table>
<thead>
<tr>
<th>Asset Type</th>
<th>% per annum</th>
</tr>
</thead>
<tbody>
<tr>
<td>Freehold buildings</td>
<td>2.5</td>
</tr>
<tr>
<td>Motor vehicles</td>
<td>25</td>
</tr>
<tr>
<td>Computer equipment</td>
<td></td>
</tr>
<tr>
<td>- Additions before 1.7.2000</td>
<td>25</td>
</tr>
<tr>
<td>- Additions after 1.7.2000</td>
<td>16.7</td>
</tr>
<tr>
<td>- Additions before 1.1.2005 [HNB Assurance]</td>
<td>25</td>
</tr>
<tr>
<td>Office equipment</td>
<td>20</td>
</tr>
<tr>
<td>Furniture and fittings</td>
<td>10</td>
</tr>
<tr>
<td>Fixtures</td>
<td>10</td>
</tr>
</tbody>
</table>
Depreciation is not provided for freehold land. Improvements made to leasehold buildings are amortized over the lease period except for HNB Stockbrokers (Pvt) Ltd who amortizes at 20% per annum.

Sithma Development (Pvt) Ltd.

<table>
<thead>
<tr>
<th>Freehold buildings</th>
<th>% per annum</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sithma building</td>
<td>1</td>
</tr>
<tr>
<td>Smart building</td>
<td>2.5</td>
</tr>
</tbody>
</table>

Generators, generator panels and associated power cables 2

Chillers, cooling towers and associated equipment 4

Lifts and escalator 4

Building management systems 4

Plant and machinery 20

Equipment 20

Motor vehicle 25

9.10.4 Capital Work-in-Progress

Capital work-in-progress is stated at cost. These are expenses of a capital nature directly incurred in the construction of buildings, major plant and machinery and system development, awaiting capitalization.

9.10.4.(i) Sithma Development (Pvt) Ltd.

Sithma Development (Pvt) Ltd. commenced a project to develop a residential apartment complex. The expenses that are of a capital nature will be accounted as capital work-in-progress until the completion of the project.

9.10.5 Borrowing Costs

Borrowing costs that are directly attributable to the acquisition, construction or production of a qualifying asset have been capitalised as part of the cost of the asset in accordance with Sri Lanka Accounting Standard 20, “Borrowing Costs”. Capitalisation of borrowing costs cease when substantially all the activities necessary to prepare the qualifying asset for its intended use are completed.

10. IMPAIRMENT

10.1 Financial Assets

The Bank assesses at each Balance Sheet date whether there is objective evidence that a financial asset or a portfolio of financial assets is impaired. A financial asset or portfolio of financial assets is impaired and impairment losses are incurred if and only if, there is objective evidence of impairment as a result of one or more loss events that occurred after the initial recognition of the asset and prior to the balance sheet date (“a loss event”), and that loss event or events have had an impact on the estimated future cash flows of the financial asset (or the portfolio), that can be reliably estimated.

The Bank first assesses whether objective evidence of impairment exists individually for financial assets that are individually significant and collectively for financial assets that are not individually significant (except for loans and advance, which is explained below). Assets that are individually assessed for impairment and for which an impairment loss is or continues to be recognised are not included in a collective assessment of impairment.

For loans and advances, impairment loss is measured individually and collectively as explained in Accounting Policy No. 9.6. When a loan is uncollectible, it is written off against the related provision. Such loans are written off after all the necessary procedures have been completed and the amount of the loss has been determined. Subsequent recoveries of the amounts previously written off is included under “Other Income” in the Income statement.

If in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised, the previously recognised impairment loss is reversed by adjusting the impairment provision account. The amount of the reversal is recognised in the Income Statement.

10.2 Non Financial Assets

Tangible and intangible assets (excluding deferred tax assets which is explained in Accounting Policy No. 15.3.2) are written down to recoverable amount where their carrying value exceeds recoverable amounts.
The carrying values of Property, Plant and Equipment are reviewed for impairment annually or when events or changes in circumstances indicate that the carrying value may not be recoverable. If such indications exist and where the carrying values exceed the estimated recoverable amount, the assets are written down to their recoverable amount. Impairment losses are recognised in the Income Statement unless it reverses a previous revaluation surplus for the same asset.

Assets with an indefinite useful life, including goodwill, are not subject to amortization and are tested on an annual basis for impairment and additionally whenever an indication of impairment exists. Assets that are subject to amortization are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable.

The recoverable amount of an asset is the higher of its fair value less costs to sell or its value in use. Any decrease in the carrying value is recognised as an expense in the Income Statement in the reporting period in which the impairment loss occurs.

For assets that do not generate largely independent cash inflows, the recoverable amount is determined for the cash generating unit to which that asset belongs. Management judgement is applied to establish cash generating units. Each of these cash generating units is represented by an individual primary reporting segment, or a subdivision of a primary segment.

An impairment loss in respect of goodwill is not reversed. In respect of other assets impairment losses recognised in prior periods, are assessed at each balance sheet date for any indications that the loss has decreased or no longer exists. An impairment loss is reversed if there has been a change in estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent that the assets carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortization, if no impairment loss had been recognised.

11. LIABILITIES AND PROVISIONS

11.1 Deposits from Customers
Deposits include non interest bearing deposits, savings deposits, term deposits, deposits redeemable at call and certificate of deposits. They are brought to account at the gross value of the outstanding balance. Interest paid is charged to the Income Statement.

11.2 Dividends Payable
Provision for dividends is recognised at the time the dividend recommended and declared by the Board of Directors is approved by the shareholders.

11.3 Borrowings
Borrowings include refinance borrowings, call and time deposits, vostro balances and borrowings from financial institutions. They are brought to account at the gross value of the outstanding balance.

11.4 Securities Sold under Re-purchase Agreement
Securities sold under agreements to re-purchase are recorded separately in the financial statements. The difference between the sale and the purchase price represents interest expense, which is recognized in the Income Statement over the period of the re-purchase agreement.

11.5 Bills Payable and Other Liabilities
Bills payable and other liabilities include all financial liabilities, interest, fees, expenses payable and securities purchased but not delivered. These liabilities are recorded at the cash value to be realized when settled.

11.6 Employee Benefits
11.6.1 Pensions and Retirement Benefits
The Bank operates an approved Pension Fund to facilitate the following payments for permanent staff of the Bank:

a) Pensions to retiring staff
b) Benefits to staff who opted for the Optional Scheme for Pension introduced in 2005 

Monthly provision is made by the Bank to the Pension Fund, based on a percentage of the gross salary of employees. The percentage of contributions will be determined by an independent actuary and retirement benefits are provided to all permanent staff. The Bank carries out an actuarial valuation of the Pension Fund in December each year to ascertain the full liability of the Fund.

An actuarial valuation of the pension fund was carried out as at 31st December 2006 by M/s Actuarial and Management Consultants (Pvt) Ltd., a firm of professional actuaries. The valuation method used by the actuaries to value the Fund is the “Projected Unit Credit Method”, the benchmark method recommended by the Sri Lanka Accounting Standard No. 16 “Retirement Benefit Cost” [SLAS 16].

The principal financial assumptions used in the valuation are as follows:

- Long term rate of interest (Gross) 12% p.a.
- Salary increases (long term) 10% p.a.
- Increase in Cost of Living Allowance (long term) 10% p.a.

The demographic assumptions underlying the valuation are retirement age (55 yrs.), early withdrawals from service and retirement on medical grounds, death before and after retirement etc.

The results of the actuarial valuation indicate that the actuarial present value of the promised retirement benefit is Rs. 4,071 Mn. and that the fair value of the fund assets is Rs. 3,229 Mn. resulting in a past service deficit of Rs. 842 Mn. (2005 - 1,885.9 Mn.) in the Pension Fund due to the changes in actuarial assumptions that took place since the previous actuarial valuation as at 31st December 2005.

The actuary recommended the amortization of the past service deficit by regular contributions over the full working lifetime of the current employees by incorporating it into the ongoing contribution rate.

Accordingly, the Bank contributes on the following basis for the employees to the Pension Fund:

- Pensionable Employees - 24.34%
- Employees who opted for the Optional Scheme – 23%

The amount recognized as an expense for the current year is Rs. 399.2 Mn. (2005 – 326.3 Mn.). The assets of the fund, which are independently administered by the Trustees as per the provision of the Trust Deed held separately from those of the Bank.

No additional provision has been made in the accounts of the Bank for gratuities to employees who complete five or more years of service, payable under the Payment of Gratuity Act No. 12 of 1983, as the Bank contributes for all permanent employees to its own non-contributory pension scheme which is in force.

11.6.2 Widows, Widowers and Orphans Pension Fund

The Bank operates a separate Widows, Widowers and Orphans Pension Scheme (WW & OP) which was established with effect from 1st September 1995.

The actuarial valuation of Widows, Widowers and Orphans Pension Scheme is carried out by the same actuary, who carried out the actuarial valuation of the Pension Fund using the same method and same assumptions detailed in Note 11.6.1 above.

The results of the actuarial valuation of the Widows, Widowers and Orphans Pension Scheme indicates that the actuarial present value of the promised benefit is Rs.307 Mn. and that the fair value of the fund assets is Rs. 229 Mn. resulting in a past service deficit of Rs. 78 Mn. (2005 – 216.8 Mn.) in the Widows, Widowers and Orphans Pension Scheme as at 31st December 2006.

The actuary has confirmed that the ongoing rate of contribution which is 3% of the Gross Salary contributed by the members of the fund...
is sufficient to cover the total liability of the fund, including the past service deficit.

The amount contributed by the members for the current year is 21.4 Mn. (2005 - Rs. 24.6 Mn.).

11.6.3 Defined Contribution Plans
Contributions to defined contribution pension plans are recognised as an expense in the Income Statement as and when incurred.

Provident Fund
The Bank and employees contribute to the approved private Provident Fund. The total amount recognised as an expense for the current year is Rs.208.1 Mn. (2005 - Rs.180 Mn.).

Trust Fund
The Bank contributes to the Employees’ Trust Fund. The total amount recognised as an expense for the current year is Rs.52 Mn. (2005 - Rs. 45 Mn.).

11.6.4 Employee Share Option Plan
The Bank continued the Employee Share Option Plan to executive and higher rank officers which was introduced in 2005. The amount released to the employees who left the service in 2006 is Rs. 9 Mn. No new shares were offered to the employees during 2006 under the plan.

11.6.5 HNB Securities Limited
Defined Benefit Plan
Provision has been made for retirement gratuities from the first year of service for all employees in conformity with SLAS - 16. However, under the Payment of Gratuity Act No. 12 of 1983, the liability to an employee arises only on completion of five years of continual service. The gratuity liability is not externally funded.

Defined Contribution Plan
Obligations for contributions to Provident and Trust Funds covering all employees are recognised as an expense in the Income Statement.

11.6.7 HNB Assurance Limited
Defined Benefit Plan
Retiring gratuity is provided for in the financial statements. An actuarial valuation of the retirement benefit is performed by a qualified actuary as at the Balance Sheet date using the “Projected Unit Credit Method”. The liability is not externally funded.

Defined Contribution Plan
Obligations for contributions to Provident and Trust Funds covering all employees are recognised as an expense in the Income Statement.

11.6.8 Sithma Development (Pvt) Limited
Defined Benefit Plan
Provision is not made for retirement gratuities as all the employees of the company are either on contract basis or seconded by the Bank and are not entitled for gratuity from the company under the Payment of Gratuity Act No. 12 of 1983.

Defined Contribution Plan
Obligations for contributions to Employee’s Provident and Trust Fund are recognized as an expense in the Income Statement.

12. PROVISIONS
Provisions are recognised when a legal or constructive obligation exists as a result of a past event and it is probable that an outflow of benefits will be required to settle the obligation and it can be reliably estimated. Provisions for non-performing loans and advances are made as set out in Accounting Policy No 9.6.3.

12.1 Operational Risk Events
Provisions for operational risk events are recognised for losses incurred by the Bank, which do not relate directly to amounts of principal outstanding for loans and advances.
The amount recognised as a provision is the best estimate of the expenditure required to settle the present obligation as at the Balance Sheet date, taking into account the risks and uncertainties that surround the events and circumstances that affect the provision.

13. COMMITMENTS AND CONTINGENCIES
All discernible risks are accounted for in determining the amount of all known liabilities. The Bank’s share of any contingencies and capital commitments of a Subsidiary or an Associate for which the Bank is also liable severally or otherwise is also included with appropriate disclosures.

Contingent liabilities are possible obligations whose existence will be confirmed only by uncertain future events or present obligations where the transfer of economic benefit is not probable or cannot be reliably measured. Contingent liabilities are not recognised in the Balance Sheet but are disclosed unless they are remote.

14. EVENTS OCCURRING AFTER THE BALANCE SHEET DATE
All material and important events which occur after the Balance Sheet date have been considered and disclosed in Note No 38.

15. INCOME STATEMENT
15.1 Revenue Recognition
15.1.1 Interest Income
Interest receivable is recognised on an accrual basis. Interest from loans and advances ceases to be accrued when the recovery of interest or principal is in arrears for ninety days. Interest on non-performing loans and advances is accounted for on a cash basis. Interest on non-performing loans and advances is credited to the ‘Interest in suspense account’ which is netted in the Balance Sheet against the relevant loans and advances.

Interest income from investments is recognized on an accrual basis.

15.1.2 Dividend Income
Dividend income is recognised in the Income Statement on an accrual basis when the Bank’s right to receive the dividend is established.

15.1.3 Lease Income
The excess of aggregate lease rentals receivable over the cost of the leased assets constitutes the total unearned lease income at the commencement of a lease. The unearned lease income is taken into income over the term of the lease commencing with the month in which the lease is executed in proportion to the declining receivable balance.

Gross earnings under finance leases in respect of lease rentals due, cease to be taken to revenue when they are in arrears for three (3) months. Thereafter, such income is recognised on a cash basis.

15.1.4 Discount on Bills of Exchange
Income on discounting Bills of Exchange is recognised proportionately over the period of the instrument.

15.1.5 Trading Income
Gains or losses arising from the sale of investment securities, dealing securities, shares and units are accounted for on the date of transaction in the Income Statement.

15.1.6 Fee and Commission Income
Fee and commission income relating to specific transactions or events are recognised in the Income Statement in the period in which they are earned. However, when they relate to services provided over a period, they are recognised in the Income Statement on an accrual basis.

15.1.7 Profit/loss from Sale of Property, Plant and Equipment
Profit/loss from sale of Property, Plant and Equipment is recognised in the period in which the sale occurs and is classified as other income.

15.1.8 Profit/loss from Sale of Investment Properties
Any gains or losses on retirement or disposal of investment properties are recognised in the month of retirement or disposal.

15.1.9 Rental Income
Rental income is recognised on an accrual basis.
15.2 Interest and Other Expenses

15.2.1 Interest Expenses and Other Expenses
Interest payable and other expenses are recognised on an accrual basis.

15.2.2 Operating Leases
Payments made under operating leases are recognised in the Income Statement on a straight-line basis over the term of the lease. The future monthly commitments on operating leases are shown in Note 33(b).

15.2.3 Fee and Commission Expenses
Fee and commission expenses are recognised on an accrual basis.

15.3 Taxation

15.3.1 Income Tax
Provision for taxation is based on the profit for the year adjusted for taxation purposes in accordance with the provisions of the Inland Revenue Act No. 10 of 2006 at the rates specified in Note No. 8 of the financial statement.

15.3.2 Deferred Tax
Deferred taxation is provided using the balance sheet liability method, providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. The amount of deferred tax provided is based on the expected manner of realisation or settlement of the carrying amount of assets and liabilities, using tax rates enacted or substantively enacted by the reporting date. Deferred tax liabilities are not recognised for the following temporary differences: the initial recognition of goodwill, the initial recognition of assets and liabilities in a transaction that is not a business combination and that affects neither accounting nor taxable profit and differences relating to investments in subsidiaries to the extent that they probably will not reverse in the foreseeable future.

Deferred tax assets, including those related to temporary tax effects of income tax losses and credits available to be carried forward are recognised only to the extent that it is probable that future taxable profits will be available against which the asset can be utilised. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

15.3.3 Withholding Tax on Dividends Distributed by Subsidiaries and Associate Company
Dividend distributed out of taxable profit of the Subsidiaries and Associate company attracts a 10% deduction at source and is not available for set off against the tax liability of the Bank. Thus, the withholding tax deducted at source is added to the tax expense of the Subsidiary companies and Associate companies in the Group financial statements as a consolidation adjustment.

15.3.4 Value Added Tax on Financial Services
The base for the computation of Value Added Tax on Financial Services is the accounting profit before income tax adjusted for the economic depreciation, computed on prescribed rates and emoluments of employees.

16 INSURANCE BUSINESS

16.1 Non-life (General) Insurance Business

16.1.1 Premium
Upon inception of the policy, premiums are recorded as written and are earned primarily on a pro-rata basis over the term of the related policy coverage. However, for those contracts for which the period of risk differs significantly from the contract period, premiums are earned over the period of risk in proportion to the amount of insurance protection provided.

16.1.2 Outward Reinsurance
Premiums ceded to reinsurers are recognised as an expense in accordance with the pattern of reinsurance services received. Accordingly, a portion of outward reinsurance premium is treated at the Balance Sheet date as a prepayment.

16.1.3 Unearned Premium
The unearned premium reserve represents the portion of the premiums and outward reinsurance premiums written in the current year in respect of risks related to
subsequent periods. Unearned premiums are calculated on the 24th basis in accordance with the Regulation of Insurance Industry Act No. 43 of 2000.

16.1.4 Unexpired Risk
Provision is made where appropriate for the estimated amount required over and above unearned premiums to meet future claims and related expenses on the business in force as at end of the year.

16.1.5 Deferred Acquisition Expenses
Deferred acquisition expenses represent net commissions relating to unearned premiums.

16.1.6 Receivables
All premiums and other debtors are recognised at the amounts receivable, as they are due for settlement no more than 60 days from the date of recognition. Collectibility of premiums and other debtors is reviewed on an ongoing basis. Debts, which are known to be uncollectible, are written off. A provision for doubtful debts is provided on the following basis:

<table>
<thead>
<tr>
<th>Debt outstanding</th>
<th>Provision</th>
</tr>
</thead>
<tbody>
<tr>
<td>180 - 270 days</td>
<td>25%</td>
</tr>
<tr>
<td>271 - 365 days</td>
<td>50%</td>
</tr>
<tr>
<td>Over 365 days</td>
<td>100%</td>
</tr>
</tbody>
</table>

Reinsurance assets include the balances due from both insurance and reinsurance companies for paid and unpaid losses and loss adjustment expenses. Amounts recoverable from reinsurers are estimated in a manner consistent with the claim liability associated with the reinsured policy. Reinsurance is recorded gross in the Balance Sheet unless a right to offset exists.

16.1.7 Claims
Claims incurred include provisions for the estimated cost of claims and related handling expenses in respect of incidents up to 31st December, including those which had not been notified, net of salvage, anticipated reinsurance and other recoveries. The provision in respect of claims Insured But Not Reported (IBNR) is actuarially valued to ensure a more realistic estimation of the future liability based on the past experience and trends. Actual valuations are performed on an annual basis.

Whilst the Directors consider that the provision for claims are fairly stated on the basis of information currently available, the ultimate liability will vary as a result of subsequent information and events. This may result in adjustments to the amounts provided. Such amounts are reflected in the financial statements for that period. The methods used and the estimates made are reviewed regularly.

16.2 Life (Long Term) Insurance Business
16.2.1 Premiums (Revenue)
Premiums are accounted for as and when received and in the same period as the policy liabilities are created.

16.2.2 Reinsurance
Reinsurance premium expense is accrued on active policies on a monthly basis.

16.2.3 Benefits, Losses and Expenses
Expenses on the life insurance revenue account relate to the acquisition and maintenance of life insurance business and include investment expenses not treated as part of the capital cost of investment.

Claims by death and maturity are charged against revenue on notification of death or on expiry of the term.

The interim payments and surrenders are accounted for only at the time of settlement.

The actuarial valuation takes into account all liabilities and is based on assumptions recommended by the Consultant Actuary.

17. SEGMENT REPORTING
A business segment is a group of assets and operations engaged in providing products or services that are subject to risks and returns different from those of other business segments. For the purposes of segment reporting disclosures, the information is presented in respect of the Group’s business segments, which is based on the Group’s management and internal reporting.
structure. The Group comprises the following major business segments which are banking, leasing, dealing, property and insurance.

Measurement of segment assets, liabilities, segment revenue and results is based on the accounting policies set out above. Segment revenue results, assets and liabilities include items directly attributable to segments as well as those that can be allocated on a reasonable basis.

Unallocated items include depreciation and amortization costs.

18. CASH FLOW STATEMENT
The Cash Flow Statement has been prepared using the “Direct Method” of preparing of Cash Flows in accordance with the Sri Lanka Accounting Standard 9, “Cash Flow Statements”. Cash and cash equivalents comprise short term, highly liquid investments that are readily convertible to known amounts of cash and are subject to an insignificant risk of changes in value. The cash and cash equivalent include cash in-hand, balances with banks, placements with banks, money at call and short notice and money market funds.
Notes to the Financial Statements

For the year ended 31st December

<table>
<thead>
<tr>
<th></th>
<th>Bank</th>
<th>Group</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>2006</td>
<td>2005</td>
</tr>
<tr>
<td></td>
<td>Rs.000</td>
<td>Rs.000</td>
</tr>
<tr>
<td>1. INCOME</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Interest income (Note 2)</td>
<td>18,451,961</td>
<td>14,129,874</td>
</tr>
<tr>
<td>Foreign exchange profit</td>
<td>792,303</td>
<td>646,660</td>
</tr>
<tr>
<td>Fee &amp; commission income</td>
<td>1,795,340</td>
<td>1,663,545</td>
</tr>
<tr>
<td>Dividend income (Note 4)</td>
<td>76,983</td>
<td>65,050</td>
</tr>
<tr>
<td>Other income (Note 5)</td>
<td>396,586</td>
<td>410,385</td>
</tr>
<tr>
<td></td>
<td>21,513,173</td>
<td>16,915,314</td>
</tr>
<tr>
<td>2. INTEREST INCOME</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Government securities</td>
<td>1,295,466</td>
<td>952,475</td>
</tr>
<tr>
<td>Placements with Banks</td>
<td>525,053</td>
<td>418,585</td>
</tr>
<tr>
<td>Customer advances</td>
<td>16,188,917</td>
<td>12,670,259</td>
</tr>
<tr>
<td>Other interest income</td>
<td>442,525</td>
<td>88,555</td>
</tr>
<tr>
<td></td>
<td>18,451,961</td>
<td>14,129,874</td>
</tr>
</tbody>
</table>

Notional Credit for Withholding Tax on Government Securities on Secondary Market Transactions

Section 123 A of the Inland Revenue (Amendment) Act, No. 19 of 2003 provides that a company which derives interest income from the secondary market transactions in Government securities (on/after 1st April 2002) would be entitled to a notional credit (being one ninth of the net interest income) provided such interest income forms part of the statutory income of the company for that year of assessment.

Accordingly, the net income earned from secondary market transactions in Government securities for the year has been grossed up in the financial statements and the resulting notional tax credit amounts to Rs. 5.58 Mn. (2005 - Rs. 1.14 Mn.) for the Bank and Rs. 12.05 Mn. (2005 - Rs. 7.91 Mn.) for the Group.

3. INTEREST EXPENSES

<table>
<thead>
<tr>
<th></th>
<th>Bank</th>
<th>Group</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>2006</td>
<td>2005</td>
</tr>
<tr>
<td></td>
<td>Rs.000</td>
<td>Rs.000</td>
</tr>
<tr>
<td>Short term borrowings</td>
<td>1,162,752</td>
<td>900,399</td>
</tr>
<tr>
<td>Refinance borrowings</td>
<td>138,265</td>
<td>109,798</td>
</tr>
<tr>
<td>Customer deposits</td>
<td>7,624,051</td>
<td>5,533,455</td>
</tr>
<tr>
<td>Interest paid on debentures</td>
<td>637,964</td>
<td>472,405</td>
</tr>
<tr>
<td>Other interest expenses</td>
<td>253,895</td>
<td>264,794</td>
</tr>
<tr>
<td></td>
<td>9,816,927</td>
<td>7,280,851</td>
</tr>
</tbody>
</table>

4. DIVIDEND INCOME

<table>
<thead>
<tr>
<th></th>
<th>Bank</th>
<th>Group</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>2006</td>
<td>2005</td>
</tr>
<tr>
<td></td>
<td>Rs.000</td>
<td>Rs.000</td>
</tr>
<tr>
<td>Dealing securities</td>
<td>12,054</td>
<td>6,173</td>
</tr>
<tr>
<td>Investment securities - quoted</td>
<td>64,692</td>
<td>58,645</td>
</tr>
<tr>
<td>Investment securities - unquoted</td>
<td>237</td>
<td>232</td>
</tr>
<tr>
<td></td>
<td>76,983</td>
<td>65,050</td>
</tr>
</tbody>
</table>
### 5. OTHER INCOME

<table>
<thead>
<tr>
<th>Description</th>
<th>2006</th>
<th>2005</th>
<th>2006</th>
<th>2005</th>
</tr>
</thead>
<tbody>
<tr>
<td>Profit/(loss) from sale of dealing securities</td>
<td>(39,402)</td>
<td>141,839</td>
<td>(36,033)</td>
<td>143,803</td>
</tr>
<tr>
<td>Income from investment securities</td>
<td>188,141</td>
<td>122,433</td>
<td>188,141</td>
<td>122,433</td>
</tr>
<tr>
<td>Loss on marked to market valuation of dealing securities</td>
<td>(45,319)</td>
<td>(81,465)</td>
<td>(45,319)</td>
<td>(81,465)</td>
</tr>
<tr>
<td>Rent received</td>
<td>84,168</td>
<td>70,982</td>
<td>89,272</td>
<td>70,982</td>
</tr>
<tr>
<td>Rent received from Investment properties</td>
<td>16,134</td>
<td>-</td>
<td>29,981</td>
<td>-</td>
</tr>
<tr>
<td>Bad debts recovered [Note 15(a) and 16(c)]</td>
<td>209,120</td>
<td>142,095</td>
<td>209,120</td>
<td>142,095</td>
</tr>
<tr>
<td>Profit/(loss) from sale of Property, Plant and Equipment</td>
<td>4,064</td>
<td>(7,749)</td>
<td>4,064</td>
<td>(7,749)</td>
</tr>
<tr>
<td>Profit from sale of Foreclosed properties</td>
<td>21,783</td>
<td>21,483</td>
<td>21,783</td>
<td>21,483</td>
</tr>
<tr>
<td>Gain on sale of Government securities</td>
<td>1,789</td>
<td>4,179</td>
<td>1,789</td>
<td>19,433</td>
</tr>
<tr>
<td>Profit on gold/silver trading</td>
<td>11,617</td>
<td>19,026</td>
<td>11,617</td>
<td>19,026</td>
</tr>
<tr>
<td>Loss on FCBU revaluation</td>
<td>(58,603)</td>
<td>(29,956)</td>
<td>(58,603)</td>
<td>(29,956)</td>
</tr>
<tr>
<td>Others</td>
<td>3,094</td>
<td>7,518</td>
<td>785,641</td>
<td>704,531</td>
</tr>
<tr>
<td></td>
<td><strong>396,586</strong></td>
<td><strong>410,385</strong></td>
<td><strong>1,201,453</strong></td>
<td><strong>1,124,616</strong></td>
</tr>
</tbody>
</table>

### 6. OPERATING EXPENSES

Operating expenses, amongst others include the following:

<table>
<thead>
<tr>
<th>Description</th>
<th>2006</th>
<th>2005</th>
<th>2006</th>
<th>2005</th>
</tr>
</thead>
<tbody>
<tr>
<td>Legal expenses</td>
<td>38,202</td>
<td>14,430</td>
<td>38,439</td>
<td>14,430</td>
</tr>
<tr>
<td>Depreciation of Property, Plant and Equipment</td>
<td>430,211</td>
<td>457,229</td>
<td>523,343</td>
<td>551,942</td>
</tr>
<tr>
<td>Amortization of Intangible assets</td>
<td>100,116</td>
<td>37,092</td>
<td>106,379</td>
<td>42,116</td>
</tr>
<tr>
<td>Depreciation of Investment property</td>
<td>1,284</td>
<td>-</td>
<td>4,487</td>
<td>-</td>
</tr>
<tr>
<td>Directors’ emoluments [Note 6(a)]</td>
<td>24,505</td>
<td>11,911</td>
<td>31,015</td>
<td>12,351</td>
</tr>
<tr>
<td>Auditors’ remuneration - Audit fees</td>
<td>2,900</td>
<td>2,600</td>
<td>3,763</td>
<td>3,560</td>
</tr>
<tr>
<td>- Non audit fees</td>
<td>360</td>
<td>300</td>
<td>360</td>
<td>300</td>
</tr>
<tr>
<td>Donations</td>
<td>33,477</td>
<td>19,642</td>
<td>33,677</td>
<td>19,642</td>
</tr>
<tr>
<td></td>
<td><strong>24,505</strong></td>
<td><strong>11,911</strong></td>
<td><strong>31,015</strong></td>
<td><strong>12,351</strong></td>
</tr>
</tbody>
</table>

#### 6 (a) Directors’ emoluments

<table>
<thead>
<tr>
<th>Description</th>
<th>2006</th>
<th>2005</th>
</tr>
</thead>
<tbody>
<tr>
<td>Emoluments of Chairman</td>
<td>3,168</td>
<td>3,168</td>
</tr>
<tr>
<td>Emoluments of Executive Director/s</td>
<td>20,317</td>
<td>7,723</td>
</tr>
<tr>
<td>Emoluments of other Directors [fee only]</td>
<td>1,020</td>
<td>1,020</td>
</tr>
<tr>
<td></td>
<td><strong>24,505</strong></td>
<td><strong>11,911</strong></td>
</tr>
</tbody>
</table>

### 7. PROVISION FOR LOAN LOSSES

<table>
<thead>
<tr>
<th>Description</th>
<th>2006</th>
<th>2005</th>
<th>2006</th>
<th>2005</th>
</tr>
</thead>
<tbody>
<tr>
<td>Specific provision for loans and advances</td>
<td>435,997</td>
<td>1,396,837</td>
<td>435,997</td>
<td>1,396,837</td>
</tr>
<tr>
<td>Specific provision for Foreclosed properties</td>
<td>99,379</td>
<td>233,349</td>
<td>99,379</td>
<td>233,349</td>
</tr>
<tr>
<td>General provision for pawning advances</td>
<td>-</td>
<td>8,250</td>
<td>-</td>
<td>8,250</td>
</tr>
<tr>
<td>General provision for housing advances</td>
<td>6,275</td>
<td>4,300</td>
<td>6,275</td>
<td>4,300</td>
</tr>
<tr>
<td>Statutory general provision for performing and overdue loans and advances</td>
<td>294,363</td>
<td>-</td>
<td>294,363</td>
<td>-</td>
</tr>
<tr>
<td>Provision for loans and advances [Note 15(a)]</td>
<td>836,014</td>
<td>1,642,736</td>
<td>836,014</td>
<td>1,642,736</td>
</tr>
<tr>
<td>Specific provision for Bills of Exchange [Note 14(a)]</td>
<td>-</td>
<td>772</td>
<td>-</td>
<td>772</td>
</tr>
<tr>
<td>General provision for leases [Note 16(c)]</td>
<td>53,084</td>
<td>42,826</td>
<td>53,084</td>
<td>42,826</td>
</tr>
<tr>
<td>Specific provision for leases [Note 16(c)]</td>
<td>42,730</td>
<td>73,110</td>
<td>42,730</td>
<td>73,110</td>
</tr>
<tr>
<td><strong>Total provision made during the year</strong></td>
<td><strong>931,828</strong></td>
<td><strong>1,799,444</strong></td>
<td><strong>931,828</strong></td>
<td><strong>1,799,444</strong></td>
</tr>
</tbody>
</table>
8. **INCOME TAX EXPENSE**

<table>
<thead>
<tr>
<th></th>
<th>Bank</th>
<th>Group</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td><strong>2006</strong></td>
<td><strong>2005</strong></td>
</tr>
<tr>
<td></td>
<td><strong>Rs.000</strong></td>
<td><strong>Rs.000</strong></td>
</tr>
<tr>
<td>a) Current tax expense</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Income tax on profits for the year</td>
<td>795,454</td>
<td>232,000</td>
</tr>
<tr>
<td>Under provision during prior years</td>
<td>3,507</td>
<td>-</td>
</tr>
<tr>
<td>Income tax on profits on Associate companies</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td></td>
<td>798,961</td>
<td>232,000</td>
</tr>
<tr>
<td>b) Deferred tax expense</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Adjustments to opening deferred tax liability resulting from increase in tax rate</td>
<td>89,482</td>
<td>-</td>
</tr>
<tr>
<td>Net opening balance adjustment (Note 30(c))</td>
<td>(81,933)</td>
<td>(81,933)</td>
</tr>
<tr>
<td>Reversal from deferred taxation</td>
<td>(7,549)</td>
<td>(36,600)</td>
</tr>
<tr>
<td></td>
<td>-</td>
<td>(36,600)</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total income tax expense</td>
<td>798,961</td>
<td>195,400</td>
</tr>
<tr>
<td>c) Income tax on profits of Subsidiary companies</td>
<td></td>
<td></td>
</tr>
<tr>
<td>HNB Assurance Limited</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>HNB Stockbrokers (Pvt) Ltd.</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>HNB Securities Limited</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>d) Income tax on profits of Associate companies</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Lanka Ventures Limited</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>19,880</td>
<td>36,947</td>
</tr>
<tr>
<td>e) Reconciliation of Accounting Profit and Taxable Income</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Profit before taxation</td>
<td>3,019,450</td>
<td>1,849,962</td>
</tr>
<tr>
<td>Disallowable expenses</td>
<td>7,517,312</td>
<td>5,037,696</td>
</tr>
<tr>
<td>Allowable expenses</td>
<td>(3,794,009)</td>
<td>(3,143,378)</td>
</tr>
<tr>
<td>Tax exempt income</td>
<td>(3,036,505)</td>
<td>(2,492,958)</td>
</tr>
<tr>
<td>Tax losses brought forward and not utilised</td>
<td>(3,673,795)</td>
<td>(4,111,916)</td>
</tr>
<tr>
<td>Tax losses not utilised and carried forward</td>
<td>2,376,608</td>
<td>3,673,795</td>
</tr>
<tr>
<td>Taxable Income</td>
<td>2,409,061</td>
<td>813,653</td>
</tr>
<tr>
<td>Income tax provision for the year is made up of the following:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Income taxable at 35%</td>
<td>713,455</td>
<td>-</td>
</tr>
<tr>
<td>Income taxable at 32.5%</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Income taxable at 33 1/3%</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Income taxable at 30%</td>
<td>-</td>
<td>179,537</td>
</tr>
<tr>
<td>Income taxable at 20%</td>
<td>74,124</td>
<td>52,463</td>
</tr>
<tr>
<td></td>
<td>787,579</td>
<td>232,000</td>
</tr>
<tr>
<td>Social Responsibility levy at 1%</td>
<td>7,875</td>
<td>-</td>
</tr>
<tr>
<td>Income tax on profits for the year</td>
<td>795,454</td>
<td>232,000</td>
</tr>
<tr>
<td>Effective tax rate</td>
<td>26.34%</td>
<td>12.54%</td>
</tr>
</tbody>
</table>

f) The Bank’s Domestic Banking Unit (DBU) is liable for taxation on its income from banking operations at the rate of 35% (2005 - 30%) for the year. The taxable income of On Shore Operations of Foreign Currency Banking Unit (FCBU) is liable for taxation at the rate 35% for the year (2005 - 30%). The taxable income from Off Shore Operations of FCBU is liable for taxation at the rate of 20% (2005 - 20%).

The Bank has recorded a taxable income of Rs. 2,409 Mn. during the year 2006. The cumulative tax losses, which are available for setting off against future taxable income amounted to Rs. 2,376.6 Mn. as at 31st December 2006 (31st December 2005 - Rs. 3,673.7 Mn.). The amounts reflected above are provisional.

Sithma Development (Pvt) Ltd. enjoys a tax holiday as per the agreement signed with the Board of Investment of Sri Lanka. As such, no provision for income taxation has been made in the Financial Statements of the Company.

HNB Stockbrokers (Pvt) Ltd., is liable for income taxation at the rate of 35% (2005 - 32.5%) on its taxable income. Provision has been made in the financial statements accordingly.

HNB Assurance Ltd., is liable for income taxation at the rate of 33 1/3% (2005 - 30%) on its taxable income. Provision has been made in the financial statements accordingly.

HNB Securities Ltd., is liable for income taxation at the rate of 35% (2005 - 32.5%) on its taxable income. Provision has been made in the financial statements accordingly.
9. BASIC EARNINGS PER SHARE

Basic Earnings per Share (EPS) has been calculated by dividing the Profit for the period attributable to Equity Holders of the Bank, by the number of ordinary shares on issue [both Voting and Non-Voting] during the year ended 31st December 2006, calculated as per the requirements of the Sri Lanka Accounting Standard 34 - "Earnings per Share".

<table>
<thead>
<tr>
<th></th>
<th>Bank</th>
<th>Group</th>
</tr>
</thead>
<tbody>
<tr>
<td>For the year ended 31st December</td>
<td>2006</td>
<td>2005</td>
</tr>
<tr>
<td>Profit attributable to Equity Holders of the Bank, (Rs.000)</td>
<td>2,220,489</td>
<td>1,654,562</td>
</tr>
<tr>
<td>Number of ordinary shares used as the denominator [000]</td>
<td>117,764</td>
<td>109,682</td>
</tr>
<tr>
<td>Basic Earnings per Share (Rs.) [Note 38(b)]</td>
<td>18.86</td>
<td>15.09</td>
</tr>
<tr>
<td>As at 31st December</td>
<td>2006</td>
<td>2005</td>
</tr>
<tr>
<td>Rs.000</td>
<td>Rs.000</td>
<td>Rs.000</td>
</tr>
</tbody>
</table>

10. CASH AND CASH EQUIVALENTS

<table>
<thead>
<tr>
<th></th>
<th>2006</th>
<th>2005</th>
<th>2006</th>
<th>2005</th>
</tr>
</thead>
<tbody>
<tr>
<td>Local currency in hand</td>
<td>1,866,835</td>
<td>1,946,367</td>
<td>1,869,645</td>
<td>1,940,228</td>
</tr>
<tr>
<td>Foreign currency in hand</td>
<td>164,731</td>
<td>138,042</td>
<td>164,731</td>
<td>138,042</td>
</tr>
<tr>
<td>Balances with local banks</td>
<td>204</td>
<td>15,107</td>
<td>33,108</td>
<td>15,107</td>
</tr>
<tr>
<td>Balances with foreign banks</td>
<td>8,695,017</td>
<td>9,930,384</td>
<td>8,695,017</td>
<td>9,930,384</td>
</tr>
<tr>
<td>Money at call and short notice</td>
<td>5,500,000</td>
<td>1,150,000</td>
<td>5,500,000</td>
<td>1,150,000</td>
</tr>
<tr>
<td>Money market funds</td>
<td>5,194,968</td>
<td>5,366,187</td>
<td>5,194,968</td>
<td>5,366,187</td>
</tr>
<tr>
<td>Placements with banks by FCBU</td>
<td>1,886,340</td>
<td>2,653,987</td>
<td>1,886,340</td>
<td>2,653,987</td>
</tr>
</tbody>
</table>

|                           | 23,308,095 | 21,200,074 | 23,343,809 | 21,193,935 |

11. STATUTORY DEPOSIT WITH CENTRAL BANK OF SRI LANKA

<table>
<thead>
<tr>
<th></th>
<th>2006</th>
<th>2005</th>
<th>2006</th>
<th>2005</th>
</tr>
</thead>
<tbody>
<tr>
<td>Statutory deposit with Central Bank of Sri Lanka</td>
<td>12,016,532</td>
<td>8,565,629</td>
<td>12,016,532</td>
<td>8,565,629</td>
</tr>
</tbody>
</table>

As required by the provisions of Section 93 of Monetary Law Act, a cash balance is maintained with the Central Bank of Sri Lanka. As at 31st December 2006, the minimum cash reserve requirement is 10% of the rupee deposit liabilities. There are no reserve requirement for deposit liabilities of the Foreign Currency Banking Unit and foreign currency deposits liabilities in the Domestic Banking Unit.

12. DEALING SECURITIES

12 (a) Quoted shares - Bank

<table>
<thead>
<tr>
<th></th>
<th>2006</th>
<th>2005</th>
</tr>
</thead>
<tbody>
<tr>
<td>No of Shares of Rs.000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Cost of Ordinary Investment</td>
<td></td>
<td></td>
</tr>
<tr>
<td>% of Market Total Value</td>
<td></td>
<td></td>
</tr>
<tr>
<td>No of Shares of Rs.000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Cost of Ordinary Investment</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Market Value</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Rs.10/- each</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Banks, Finance and Insurance

<table>
<thead>
<tr>
<th></th>
<th>2006</th>
<th>2005</th>
</tr>
</thead>
<tbody>
<tr>
<td>Housing Development Finance</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Corporation Bank of Sri Lanka</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Seylan Bank Ltd.</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Seylan Bank Ltd, Non-Voting</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Union Assurance Ltd.</td>
<td>332,300</td>
<td>23,895</td>
</tr>
<tr>
<td></td>
<td>34,061</td>
<td>34,061</td>
</tr>
<tr>
<td>Banks, Finance and Insurance</td>
<td>23,895</td>
<td>8.42</td>
</tr>
<tr>
<td></td>
<td>34,061</td>
<td>34,061</td>
</tr>
<tr>
<td>Beverage Food and Tobacco</td>
<td>561,900</td>
<td>51,149</td>
</tr>
<tr>
<td>Distilleries Company of Sri Lanka Ltd.</td>
<td>50,852</td>
<td>18.01</td>
</tr>
<tr>
<td>Construction and Engineering</td>
<td>721,955</td>
<td>25,990</td>
</tr>
<tr>
<td>Colombo Dockyard Ltd.</td>
<td>100,000</td>
<td>3,543</td>
</tr>
<tr>
<td></td>
<td>2,225</td>
<td>2,225</td>
</tr>
</tbody>
</table>
### 12. DEALING SECURITIES (Contd.)

#### 12 (a) Quoted shares - Bank (Contd.)

<table>
<thead>
<tr>
<th>Shares of Ordinary Investment</th>
<th>No of Shares</th>
<th>Cost of Rs.000</th>
<th>% of Market</th>
<th>Cost of Rs.000</th>
<th>Market Value</th>
</tr>
</thead>
<tbody>
<tr>
<td>Hayleys Ltd.</td>
<td>258,600</td>
<td>26,416</td>
<td>9.30</td>
<td>33,489</td>
<td></td>
</tr>
<tr>
<td>Hemas Holdings Ltd.</td>
<td>150,200</td>
<td>17,401</td>
<td>6.13</td>
<td>17,536</td>
<td></td>
</tr>
<tr>
<td>John Keells Holdings Ltd.</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Diversified Holdings</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Hapo Reliance Holdings Ltd.</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>John Keells Holdings Ltd.</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>交织和旅游</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Aitken Spence Hotel Holdings Ltd.</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Asian Hotels &amp; Properties Ltd.</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Connaissance Holdings Ltd.</td>
<td>307,520</td>
<td>11,371</td>
<td>4.00</td>
<td>11,378</td>
<td></td>
</tr>
<tr>
<td>Galle Hotel Lanka Ltd.</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>John Keells Hotels Ltd.</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Riverina Hotels Ltd.</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>美国制造</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>ACL Cables Ltd.</td>
<td>200,000</td>
<td>24,865</td>
<td>8.76</td>
<td>42,550</td>
<td></td>
</tr>
<tr>
<td>Caltex Lanka Lubricants Ltd.</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Dankotuwa Porcelain Ltd.</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Kelani Tyres Ltd.</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Richard Pieris and Co Ltd.</td>
<td>401,900</td>
<td>36,940</td>
<td>13.01</td>
<td>31,348</td>
<td></td>
</tr>
<tr>
<td>Sierra Cables Limited (Rs.1 per share)</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Tokyo Cement (Lanka) Ltd.</td>
<td>74,000</td>
<td>14,042</td>
<td>4.95</td>
<td>14,412</td>
<td></td>
</tr>
<tr>
<td>Tokyo Cement (Lanka) Ltd.</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Non-Voting</td>
<td>1,000,000</td>
<td>14,305</td>
<td>5.04</td>
<td>17,000</td>
<td></td>
</tr>
<tr>
<td>电力和能源</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Lanka IOC Ltd.</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>作物</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Horana Plantations Ltd.</td>
<td>162,500</td>
<td>3,926</td>
<td>1.38</td>
<td>2,966</td>
<td></td>
</tr>
<tr>
<td>电信通讯</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Dialog Telekom (Rs. 1 per share)</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Sri Lanka Telecom Ltd.</td>
<td>1,565,400</td>
<td>36,497</td>
<td>12.85</td>
<td>43,440</td>
<td></td>
</tr>
<tr>
<td>现货交易</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Odd lots &amp; delisted shares</td>
<td>-</td>
<td>139</td>
<td>0.05</td>
<td>135</td>
<td></td>
</tr>
<tr>
<td>2006</td>
<td>283,946</td>
<td>100.00</td>
<td>325,027</td>
<td>345,884</td>
<td>268,543</td>
</tr>
<tr>
<td>2005</td>
<td>345,884</td>
<td>100.00</td>
<td>325,027</td>
<td>268,543</td>
<td></td>
</tr>
</tbody>
</table>

*Marked to market valuation gain/(loss):* 41,081 (77,341)
### 12. DEALING SECURITIES (Contd.)

#### 12 (b) Quoted shares - Subsidiaries

<table>
<thead>
<tr>
<th>Shares of Ordinary Investment</th>
<th>No of Shares of Rs.10/- each</th>
<th>Cost of Rs.000</th>
<th>% of Market</th>
<th>No of Shares of Rs.10/- each</th>
<th>Cost of Rs.000</th>
<th>% of Market</th>
</tr>
</thead>
<tbody>
<tr>
<td>Lanka IOC Ltd.</td>
<td>--</td>
<td>--</td>
<td>--</td>
<td>--</td>
<td>--</td>
<td>--</td>
</tr>
<tr>
<td>Sri Lanka Telecom Ltd.</td>
<td>--</td>
<td>--</td>
<td>--</td>
<td>350,000</td>
<td>9,211</td>
<td>5,775</td>
</tr>
</tbody>
</table>

Provision for diminution in market value: 

- 10,476 Rs.000

**Total Quoted Shares - Subsidiaries:**

- 6,594 Rs.000

As at 31st December

<table>
<thead>
<tr>
<th>Shares of Ordinary Investment</th>
<th>Cost of Investment Rs.000</th>
<th>Market Value Rs.000</th>
</tr>
</thead>
</table>

#### 12 (c) Bonds - Bank

**Government of Sri Lanka Treasury Bonds**

<table>
<thead>
<tr>
<th>Face Value</th>
<th>Year of Maturity</th>
<th>Discounted Value (Rs. 000)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Rs. 50 Mn.</td>
<td>2009</td>
<td>48,694</td>
</tr>
</tbody>
</table>

Marked to market valuation loss: 

- (5,315) Rs.000

**Foreign Currency Bonds**

<table>
<thead>
<tr>
<th>Face Value</th>
<th>Year of Maturity</th>
<th>Discounted Value (Rs. 000)</th>
</tr>
</thead>
<tbody>
<tr>
<td>US$ 5 Mn.</td>
<td>2010</td>
<td>532,863</td>
</tr>
</tbody>
</table>

Marked to market valuation loss: 

- (162,550) Rs.000

**Total Bonds - Bank:**

- 413,692 Rs.000

**Total Dealing Securities - Bank [Note 12 (a) & (c)]:**

- 738,719 Rs.000

#### 12 (d) Bonds - Subsidiaries

**Government of Sri Lanka Treasury Bonds**

<table>
<thead>
<tr>
<th>Face Value</th>
<th>Year of Maturity</th>
<th>Discounted Value (Rs. 000)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Rs. 15 Mn.</td>
<td>2007</td>
<td>14,811</td>
</tr>
<tr>
<td>Rs. 142 Mn.</td>
<td>2008</td>
<td>142,008</td>
</tr>
<tr>
<td>Rs. 93 Mn.</td>
<td>2009</td>
<td>245,762</td>
</tr>
</tbody>
</table>

Marked to market valuation loss: 

- (6,431) Rs.000

**Total Bonds - Subsidiaries:**

- 239,331 Rs.000

**Inter company adjustment:**

- [2,897] Rs.000

**Total Dealing Securities - Group:**

- 319,707 Rs.000
### 13. INVESTMENT SECURITIES

#### 13 (a) Quoted shares

<table>
<thead>
<tr>
<th>Bank</th>
<th>No. of Shares</th>
<th>Cost of Shares</th>
<th>Market Value of Shares</th>
</tr>
</thead>
<tbody>
<tr>
<td>Asha Central Hospital Ltd</td>
<td>120,000</td>
<td>1,578</td>
<td>4,890</td>
</tr>
<tr>
<td>Browns Beach Hotels Ltd</td>
<td>75,000</td>
<td>1,622</td>
<td>2,100</td>
</tr>
<tr>
<td>Commercial Bank of Ceylon Ltd</td>
<td>825,332</td>
<td>61,645</td>
<td>156,813</td>
</tr>
<tr>
<td>DFCC Bank</td>
<td>10,581,037</td>
<td>519,711</td>
<td>1,899,296</td>
</tr>
</tbody>
</table>

**Distilleries Company of Sri Lanka Ltd**

<table>
<thead>
<tr>
<th>No. of Shares</th>
<th>Cost of Shares</th>
<th>Market Value of Shares</th>
</tr>
</thead>
<tbody>
<tr>
<td>1,481,500</td>
<td>11,158</td>
<td>134,076</td>
</tr>
</tbody>
</table>

**Lanka Hospital Corporation Ltd**

<table>
<thead>
<tr>
<th>No. of Shares</th>
<th>Cost of Shares</th>
<th>Market Value of Shares</th>
</tr>
</thead>
<tbody>
<tr>
<td>1,455,000</td>
<td>22,055</td>
<td>37,830</td>
</tr>
</tbody>
</table>

**Magpek Exports Ltd**

<table>
<thead>
<tr>
<th>No. of Shares</th>
<th>Cost of Shares</th>
<th>Market Value of Shares</th>
</tr>
</thead>
<tbody>
<tr>
<td>359,000</td>
<td>14,360</td>
<td>*</td>
</tr>
</tbody>
</table>

**Metal Recyclers Colombo Ltd**

<table>
<thead>
<tr>
<th>No. of Shares</th>
<th>Cost of Shares</th>
<th>Market Value of Shares</th>
</tr>
</thead>
<tbody>
<tr>
<td>69</td>
<td>3</td>
<td>*</td>
</tr>
</tbody>
</table>

**Provision for diminution in market value b/f**

<table>
<thead>
<tr>
<th></th>
<th>2006</th>
<th>2005</th>
</tr>
</thead>
<tbody>
<tr>
<td>(14,363)</td>
<td>632,132</td>
<td>1,747,064</td>
</tr>
</tbody>
</table>

**Total Quoted Shares - Bank**

<table>
<thead>
<tr>
<th></th>
<th>2006</th>
<th>2005</th>
</tr>
</thead>
<tbody>
<tr>
<td>617,769</td>
<td>2,235,005</td>
<td>617,769</td>
</tr>
</tbody>
</table>

* Shares delisted – Market value shown as nil.

#### Subsidiaries

**Commercial Bank of Ceylon Ltd. cumulative redeemable preference shares**

<table>
<thead>
<tr>
<th>No. of Shares</th>
<th>Cost of Shares</th>
<th>Market Value of Shares</th>
</tr>
</thead>
<tbody>
<tr>
<td>725,000</td>
<td>7,250</td>
<td>6,706</td>
</tr>
</tbody>
</table>

**Hemas Holdings Ltd.**

<table>
<thead>
<tr>
<th>No. of Shares</th>
<th>Cost of Shares</th>
<th>Market Value of Shares</th>
</tr>
</thead>
<tbody>
<tr>
<td>4,200</td>
<td>447</td>
<td>490</td>
</tr>
</tbody>
</table>

**John Keells Holdings Ltd.**

<table>
<thead>
<tr>
<th>No. of Shares</th>
<th>Cost of Shares</th>
<th>Market Value of Shares</th>
</tr>
</thead>
<tbody>
<tr>
<td>20,000</td>
<td>2,672</td>
<td>3,900</td>
</tr>
</tbody>
</table>

**Dialog Telecom Ltd.**

<table>
<thead>
<tr>
<th>No. of Shares</th>
<th>Cost of Shares</th>
<th>Market Value of Shares</th>
</tr>
</thead>
<tbody>
<tr>
<td>100,000</td>
<td>2,075</td>
<td>2,650</td>
</tr>
</tbody>
</table>

**Sri Lanka Telecom Ltd.**

<table>
<thead>
<tr>
<th>No. of Shares</th>
<th>Cost of Shares</th>
<th>Market Value of Shares</th>
</tr>
</thead>
<tbody>
<tr>
<td>100,000</td>
<td>2,075</td>
<td>2,650</td>
</tr>
</tbody>
</table>

**Provision for diminution in value of investment**

<table>
<thead>
<tr>
<th></th>
<th>2006</th>
<th>2005</th>
</tr>
</thead>
<tbody>
<tr>
<td>(545)</td>
<td>14,545</td>
<td>16,521</td>
</tr>
</tbody>
</table>

**Total Quoted Shares - Subsidiaries**

<table>
<thead>
<tr>
<th></th>
<th>2006</th>
<th>2005</th>
</tr>
</thead>
<tbody>
<tr>
<td>14,000</td>
<td>16,521</td>
<td>7,069</td>
</tr>
</tbody>
</table>

**Total Quoted Shares - Group**

<table>
<thead>
<tr>
<th></th>
<th>2006</th>
<th>2005</th>
</tr>
</thead>
<tbody>
<tr>
<td>631,769</td>
<td>2,251,526</td>
<td>624,838</td>
</tr>
</tbody>
</table>

#### 13 (b) Unquoted shares

<table>
<thead>
<tr>
<th>Bank</th>
<th>No. of Shares</th>
<th>Cost of Shares</th>
<th>Directors’ Valuation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Browns Group Motels Ltd</td>
<td>50,000</td>
<td>500</td>
<td>500</td>
</tr>
<tr>
<td>Credit Information Bureau of Sri Lanka (Shares of Rs.100/- each)</td>
<td>5,300</td>
<td>530</td>
<td>530</td>
</tr>
<tr>
<td>Fitch Rating Lanka Ltd</td>
<td>62,500</td>
<td>625</td>
<td>625</td>
</tr>
<tr>
<td>Lanka Clear (Pvt) Ltd</td>
<td>2,200,000</td>
<td>22,000</td>
<td>22,000</td>
</tr>
<tr>
<td>S.W.I.F.T.</td>
<td>21</td>
<td>2,051</td>
<td>2,051</td>
</tr>
</tbody>
</table>

**Total Unquoted Shares - Bank**

<table>
<thead>
<tr>
<th></th>
<th>2006</th>
<th>2005</th>
</tr>
</thead>
<tbody>
<tr>
<td>25,706</td>
<td>25,706</td>
<td>25,706</td>
</tr>
</tbody>
</table>
### 13. INVESTMENT SECURITIES (Contd.)

#### 13 (c) Bonds and debentures

**As at 31st December**

<table>
<thead>
<tr>
<th>Bond Type</th>
<th>Cost Directors’ Valuation</th>
<th>Directors’ Valuation</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Rs.000</td>
<td>Rs.000</td>
</tr>
<tr>
<td><strong>Bank</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Long Term Investments</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Non-negotiable Bonds maturing on 14.11.2016</td>
<td>489,000</td>
<td>489,000</td>
</tr>
<tr>
<td>Mercantile Leasing Ltd - Debentures</td>
<td>60,000</td>
<td>60,000</td>
</tr>
<tr>
<td>People’s Leasing Co. Ltd. - Securitised Notes Trust 04</td>
<td>5,341</td>
<td>5,341</td>
</tr>
<tr>
<td>People’s Leasing Co. Ltd. - Securitised Notes Trust 10</td>
<td>83,333</td>
<td>83,333</td>
</tr>
<tr>
<td>People’s Leasing Co. Ltd. - Securitised Notes Trust 14</td>
<td>125,000</td>
<td>125,000</td>
</tr>
<tr>
<td>People’s Leasing Co. Ltd. - Securitised Notes Trust 20</td>
<td>72,917</td>
<td>72,917</td>
</tr>
<tr>
<td>People’s Leasing Co. Ltd. - Securitised Notes Trust 29</td>
<td>177,978</td>
<td>177,978</td>
</tr>
<tr>
<td>Sri Lanka Development Bonds matured in 2006</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Sri Lanka Development Bonds maturing in 2008</td>
<td>4,202,859</td>
<td>4,202,859</td>
</tr>
<tr>
<td>Sri Lanka Development Bonds maturing in 2009</td>
<td>2,794,740</td>
<td>2,794,740</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>8,011,168</td>
<td>8,011,168</td>
</tr>
</tbody>
</table>

**As at 31st December**

<table>
<thead>
<tr>
<th>Bond Type</th>
<th>Cost of Investment Directors’ Valuation</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Rs.000</td>
</tr>
<tr>
<td><strong>Government of Sri Lanka Treasury Bonds</strong></td>
<td></td>
</tr>
<tr>
<td>Face value</td>
<td>Year of Maturity</td>
</tr>
<tr>
<td>Rs.2,717.80 Mn</td>
<td>2007</td>
</tr>
<tr>
<td>Rs. 3,699.10 Mn</td>
<td>2008</td>
</tr>
<tr>
<td>Rs. 2,740.00 Mn</td>
<td>2009</td>
</tr>
<tr>
<td>Rs. 251.00 Mn</td>
<td>2013</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td></td>
</tr>
</tbody>
</table>

* Government of Sri Lanka Treasury Bonds with a face value of Rs. 9.408 Bn. were purchased for Rs. 10.116 Bn., incurring a premium of Rs. 0.708 Bn. Rs. 0.445 Bn. of the premium has been amortized to date and the amortized amount is included in other liabilities (Note 31).

The net value of the investment as at 31.12.2006 is therefore Rs. 9.671 Bn.

**Foreign Currency Bonds**

<table>
<thead>
<tr>
<th>Bond Type</th>
<th>Face value</th>
<th>Year of Maturity</th>
<th>Value US$</th>
<th>Equivalent Value in SLR (Rs.000)</th>
</tr>
</thead>
<tbody>
<tr>
<td>US$ 10 Mn.</td>
<td>2009</td>
<td>9,872,726</td>
<td>1,060,824</td>
<td></td>
</tr>
<tr>
<td>Foreign Investments</td>
<td>10,934,088</td>
<td>1,174,868</td>
<td>2,235,692</td>
<td></td>
</tr>
<tr>
<td><strong>Total Bonds and Debentures - Bank</strong></td>
<td>20,363,314</td>
<td>19,225,091</td>
<td>16,641,470</td>
<td></td>
</tr>
<tr>
<td><strong>Total Investment Securities - Bank</strong></td>
<td>21,006,789</td>
<td>17,284,945</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
13. INVESTMENT SECURITIES (Contd.)

Bonds and debentures
As at 31st December

<table>
<thead>
<tr>
<th>Subsidiaries</th>
<th>2006</th>
<th>2005</th>
</tr>
</thead>
<tbody>
<tr>
<td>No. of Debentures</td>
<td>Cost of Investment</td>
<td>No. of Debentures</td>
</tr>
<tr>
<td>-----------------------------------</td>
<td>-------------------</td>
<td>-------------------</td>
</tr>
<tr>
<td>Commercial Bank of Ceylon Ltd-</td>
<td>7,250 7,250</td>
<td>7,250 7,250</td>
</tr>
<tr>
<td>Debentures (Rs. 100/- each)</td>
<td>10,000 10,000</td>
<td></td>
</tr>
<tr>
<td>DFCC Bank (Rs. 100/- each)</td>
<td>150,000 15,000</td>
<td></td>
</tr>
<tr>
<td>Seylan Bank Ltd. (Rs. 100/- each)</td>
<td>50,000 5,000</td>
<td></td>
</tr>
<tr>
<td>Singer (Sri Lanka) Ltd. (Rs. 100/- each)</td>
<td>37,250 7,250</td>
<td></td>
</tr>
<tr>
<td>Total Quoted Debentures - Subsidiaries</td>
<td>37,250 7,250</td>
<td></td>
</tr>
</tbody>
</table>

As at 31st December

<table>
<thead>
<tr>
<th>Market Value</th>
<th>Cost of Directors' Valuation Investment</th>
</tr>
</thead>
<tbody>
<tr>
<td>Rs.000</td>
<td>Rs.000</td>
</tr>
<tr>
<td>--------------</td>
<td>----------------------------------------</td>
</tr>
<tr>
<td>13(c)iv</td>
<td>Government of Sri Lanka Treasury Bonds</td>
</tr>
<tr>
<td>Face value</td>
<td>Year of Maturity Discounted Value (Rs.000)</td>
</tr>
<tr>
<td>Rs. 1,139 Mn.</td>
<td>2007 1,154,901</td>
</tr>
<tr>
<td>Rs. 90 Mn.</td>
<td>2008 90,458</td>
</tr>
<tr>
<td>Rs. 296 Mn.</td>
<td>2009 290,611</td>
</tr>
<tr>
<td>Rs. 67 Mn.</td>
<td>2010 65,630</td>
</tr>
<tr>
<td>Total Bonds and Debentures - Subsidiaries</td>
<td>1,576,904 1,638,850</td>
</tr>
<tr>
<td>Total Bonds and Debentures - Group</td>
<td>21,940,218 18,092,086</td>
</tr>
<tr>
<td>Total Investments Securities - Group</td>
<td>22,659,639 18,816,694</td>
</tr>
</tbody>
</table>

14. BILLS OF EXCHANGE

<table>
<thead>
<tr>
<th>Inland bills</th>
<th>372,205 335,258</th>
</tr>
</thead>
<tbody>
<tr>
<td>Import bills</td>
<td>458,655 222,831</td>
</tr>
<tr>
<td>Export bills</td>
<td>954,300 1,060,293</td>
</tr>
<tr>
<td>Foreign Currency Banking Unit bills</td>
<td>416,863 696,639</td>
</tr>
<tr>
<td>Less: Specific provision [Note 14(a)]</td>
<td>2,202,023 2,315,021</td>
</tr>
<tr>
<td>1,910,852 2,026,977</td>
<td></td>
</tr>
</tbody>
</table>

14 (a) Movement in provision for Bills of Exchange

<p>| Balance brought forward | 288,044 288,763 |
| Exchange rate variance on foreign currency provision | 3,127 (1,491) |
| Specific provision made during the year (Note 7) | - 772 |
| 291,171 288,044 |</p>
<table>
<thead>
<tr>
<th></th>
<th>Bank</th>
<th>Group</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Rs.000</td>
<td>Rs.000</td>
</tr>
<tr>
<td>As at 31st December</td>
<td>2006</td>
<td>2005</td>
</tr>
</tbody>
</table>

### 15. LOANS AND ADVANCES

#### Sri Lanka Rupee loans and advances

<table>
<thead>
<tr>
<th>Description</th>
<th>2006</th>
<th>2005</th>
</tr>
</thead>
<tbody>
<tr>
<td>Overdrafts</td>
<td>27,455,224</td>
<td>22,952,834</td>
</tr>
<tr>
<td>Trust receipts</td>
<td>6,876,898</td>
<td>5,193,080</td>
</tr>
<tr>
<td>Packing credit loans</td>
<td>618,787</td>
<td>523,517</td>
</tr>
<tr>
<td>Staff loans</td>
<td>4,818,325</td>
<td>4,104,142</td>
</tr>
<tr>
<td>Term loans</td>
<td>37,130,160</td>
<td>31,667,736</td>
</tr>
<tr>
<td>Housing loans</td>
<td>12,987,528</td>
<td>10,224,844</td>
</tr>
<tr>
<td>Pawning advances</td>
<td>13,446,308</td>
<td>13,446,308</td>
</tr>
<tr>
<td>Foreclosed properties [Note 15(f)]</td>
<td>69,420</td>
<td>69,420</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>103,402,650</td>
<td>87,327,043</td>
</tr>
</tbody>
</table>

#### Foreign currency loans and advances

<table>
<thead>
<tr>
<th>Description</th>
<th>2006</th>
<th>2005</th>
</tr>
</thead>
<tbody>
<tr>
<td>Overdrafts</td>
<td>1,588,638</td>
<td>1,668,881</td>
</tr>
<tr>
<td>Trust receipts</td>
<td>1,647,432</td>
<td>1,647,432</td>
</tr>
<tr>
<td>Packing credit loans</td>
<td>3,460,009</td>
<td>3,460,009</td>
</tr>
<tr>
<td>Term loans</td>
<td>10,892,995</td>
<td>10,737,166</td>
</tr>
<tr>
<td>Housing loans</td>
<td>399,933</td>
<td>399,933</td>
</tr>
<tr>
<td>Pawning advances</td>
<td>423,250</td>
<td>423,250</td>
</tr>
<tr>
<td>Foreclosed properties [Note 15(f)]</td>
<td>423,250</td>
<td>423,250</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>18,412,257</td>
<td>15,381,438</td>
</tr>
</tbody>
</table>

#### Sri Lanka Rupee and Foreign currency loans and advances

<table>
<thead>
<tr>
<th>Description</th>
<th>2006</th>
<th>2005</th>
</tr>
</thead>
<tbody>
<tr>
<td>Less:</td>
<td>121,814,907</td>
<td>121,383,403</td>
</tr>
<tr>
<td>Specific provision for loans and advances</td>
<td>5,449,958</td>
<td>5,449,958</td>
</tr>
<tr>
<td>Specific provision for Foreclosed properties [Note 15(f)]</td>
<td>468,218</td>
<td>468,218</td>
</tr>
<tr>
<td>General provision for pawning advances</td>
<td>16,473</td>
<td>16,473</td>
</tr>
<tr>
<td>General provision for housing loans</td>
<td>294,363</td>
<td>294,363</td>
</tr>
<tr>
<td>Statutory general provision for performing and overdue loans and advances</td>
<td>5,722,241</td>
<td>5,722,241</td>
</tr>
<tr>
<td><strong>Total provision for loan losses [Note 15(a)]</strong></td>
<td>6,255,787</td>
<td>5,556,990</td>
</tr>
<tr>
<td>Loans and advances after provision</td>
<td>115,559,120</td>
<td>115,127,616</td>
</tr>
<tr>
<td>Less: Interest in suspense [Note 15(e)]</td>
<td>850,746</td>
<td>850,746</td>
</tr>
<tr>
<td><strong>Net loans and advances</strong></td>
<td>114,708,374</td>
<td>114,276,870</td>
</tr>
</tbody>
</table>

### 15 (a) Movement in provision for loan losses

<table>
<thead>
<tr>
<th>Description</th>
<th>2006</th>
<th>2005</th>
</tr>
</thead>
<tbody>
<tr>
<td>Balance brought forward</td>
<td>5,556,990</td>
<td>5,556,990</td>
</tr>
<tr>
<td>Exchange rate variance on foreign currency provision</td>
<td>165,251</td>
<td>165,251</td>
</tr>
<tr>
<td>Provision made during the year [Note 7]</td>
<td>836,014</td>
<td>836,014</td>
</tr>
<tr>
<td>Fully provided debts written off</td>
<td>(101,900)</td>
<td>(101,900)</td>
</tr>
<tr>
<td>Recoveries made during the year</td>
<td>(200,568)</td>
<td>(200,568)</td>
</tr>
<tr>
<td>Reversals made from General provision</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>6,255,787</td>
<td>5,556,990</td>
</tr>
</tbody>
</table>
15. LOANS AND ADVANCES (Contd.)

15(b) Total provision for loan losses

<table>
<thead>
<tr>
<th>As at 31st December</th>
<th>2006</th>
<th>2005</th>
</tr>
</thead>
<tbody>
<tr>
<td>Rs.000</td>
<td>Rs.000</td>
<td>Rs.000</td>
</tr>
</tbody>
</table>

15(b)i Specific provision

<table>
<thead>
<tr>
<th>Bills of Exchange</th>
<th>Rs.000</th>
<th>Rs.000</th>
</tr>
</thead>
<tbody>
<tr>
<td>291,171</td>
<td>288,044</td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Loans and advances</th>
<th>Rs.000</th>
<th>Rs.000</th>
</tr>
</thead>
<tbody>
<tr>
<td>5,918,176</td>
<td>5,520,017</td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Lease rentals receivable within one year</th>
<th>Rs.000</th>
<th>Rs.000</th>
</tr>
</thead>
<tbody>
<tr>
<td>248,227</td>
<td>6,457,574</td>
<td></td>
</tr>
</tbody>
</table>

15(b)ii General provision

<table>
<thead>
<tr>
<th>Loans and advances</th>
<th>Rs.000</th>
<th>Rs.000</th>
</tr>
</thead>
<tbody>
<tr>
<td>43,248</td>
<td>36,973</td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Lease rentals receivable within one year</th>
<th>Rs.000</th>
<th>Rs.000</th>
</tr>
</thead>
<tbody>
<tr>
<td>80,801</td>
<td>66,938</td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Lease rentals receivable after one year</th>
<th>Rs.000</th>
<th>Rs.000</th>
</tr>
</thead>
<tbody>
<tr>
<td>154,964</td>
<td>115,727</td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Statutory general provision for performing and overdue loans and advances</th>
<th>Rs.000</th>
<th>Rs.000</th>
</tr>
</thead>
<tbody>
<tr>
<td>294,363</td>
<td>573,376</td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Total provision [Note 14(a), 15(a) and 16(c)]</th>
<th>Rs.000</th>
<th>Rs.000</th>
</tr>
</thead>
<tbody>
<tr>
<td>7,030,950</td>
<td>6,242,183</td>
<td></td>
</tr>
</tbody>
</table>

As explained in Significant Accounting Policy no 9.6.5, the Bank has made additional general provision to meet the regulatory requirement. The total general provision of Rs 294.4 Mn. is 0.56% of the total performing and overdue loans and advances, net of interest in suspense as at the Balance Sheet date and is above the regulatory requirement of 0.1% as at 31st December 2006.

As at 31st December | 2006 | 2005 |
<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Rs.000</td>
<td>Rs.000</td>
<td></td>
</tr>
</tbody>
</table>

15(c) Asset quality - Bank

<table>
<thead>
<tr>
<th>Non-performing lending portfolio</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bills of Exchange</td>
</tr>
<tr>
<td>Loans and advances</td>
</tr>
<tr>
<td>Foreclosed properties</td>
</tr>
<tr>
<td>Lease rental receivable</td>
</tr>
<tr>
<td>Total</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Less: Specific provisions</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bills of Exchange</td>
</tr>
<tr>
<td>Loans and advances</td>
</tr>
<tr>
<td>Foreclosed properties</td>
</tr>
<tr>
<td>Lease rental receivable</td>
</tr>
<tr>
<td>Total</td>
</tr>
</tbody>
</table>

| Less: Interest in suspense | Rs.000 | 850,746 |
| Total net non-performing lending portfolio | Rs.000 | 3,073,004 |

15(d) Credit risk - Bank

15(d)i Collateral wise analysis of gross non-performing lending portfolio

The Bank holds collateral against its lending portfolio in the form of mortgage interest over property, other registered securities and assets. Estimation of fair value / realisable value are based on the value of collateral assessed at the time of lending and generally are not updated except when a loan is individually assessed as non-performing.

<table>
<thead>
<tr>
<th>As at 31st December</th>
<th>2006</th>
<th>%</th>
<th>2005</th>
<th>%</th>
</tr>
</thead>
<tbody>
<tr>
<td>Rs.000</td>
<td>Rs.000</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

| Secured by immovable assets | Rs.000 | 54 | 4,960,486 | 48 |
| Secured by movable assets | Rs.000 | 13 | 2,290,430 | 22 |
| Secured by cash/shares | Rs.000 | 4 | 1,119,938 | 11 |
| Other securities | Rs.000 | 14 | 1,522,389 | 15 |
| Clean | Rs.000 | 15 | 509,577 | 4 |
| Total | Rs.000 | 100 | 10,402,820 | 100 |
15. LOANS AND ADVANCES (Contd.)

15(d) Credit risk - Bank (Contd.)

15(d)ii Sector/Productwise analysis of gross lending portfolio

The Bank monitors concentration of credit risk by sectors. An analysis of concentration of credit risk as at the Balance Sheet date is shown below:

<table>
<thead>
<tr>
<th>Sector/Type of Loan</th>
<th>Short Term</th>
<th>Medium Term</th>
<th>Long Term</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Loans Rs.000</td>
<td>Loans Rs.000</td>
<td>Loans Rs.000</td>
<td></td>
</tr>
<tr>
<td>Bank - 2006</td>
<td>1,447,401</td>
<td>1,188,518</td>
<td>971,986</td>
<td></td>
</tr>
<tr>
<td>Food, beverages and tobacco</td>
<td>827,071</td>
<td>827,071</td>
<td>827,071</td>
<td></td>
</tr>
<tr>
<td>Agriculture, agro business and fisheries</td>
<td>1,599,581</td>
<td>1,599,581</td>
<td>1,599,581</td>
<td></td>
</tr>
<tr>
<td>Textiles and wearing apparel</td>
<td>1,598,649</td>
<td>1,598,649</td>
<td>1,598,649</td>
<td></td>
</tr>
<tr>
<td>Wood and paper products</td>
<td>351,341</td>
<td>351,341</td>
<td>351,341</td>
<td></td>
</tr>
<tr>
<td>Rubber and leather products</td>
<td>206,214</td>
<td>206,214</td>
<td>206,214</td>
<td></td>
</tr>
<tr>
<td>Metals, chemicals and engineering</td>
<td>1,860,076</td>
<td>1,860,076</td>
<td>1,860,076</td>
<td></td>
</tr>
<tr>
<td>Hotels</td>
<td>51,733</td>
<td>51,733</td>
<td>51,733</td>
<td></td>
</tr>
<tr>
<td>Services</td>
<td>1,311,776</td>
<td>1,311,776</td>
<td>1,311,776</td>
<td></td>
</tr>
<tr>
<td>Foreclosed properties</td>
<td>1,902,238</td>
<td>1,902,238</td>
<td>1,902,238</td>
<td></td>
</tr>
<tr>
<td>Others</td>
<td>17,999,786</td>
<td>17,999,786</td>
<td>17,999,786</td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>27,435,225</td>
<td>24,339,130</td>
<td>34,688,064</td>
<td>136,828,771</td>
</tr>
</tbody>
</table>

Gross Loans and Advances (Note 15) 121,814,907 90.03
Lease Rentals Receivable (Note 16) 15,013,864 10.97
136,828,771 100.00

The "others" category comprises the following advances:

<table>
<thead>
<tr>
<th>Category</th>
<th>Rs.000</th>
<th>Rs.000</th>
<th>Rs.000</th>
<th>Rs.000</th>
<th>Rs.000</th>
<th>Rs.000</th>
<th>Rs.000</th>
</tr>
</thead>
<tbody>
<tr>
<td>Exports</td>
<td>235,096</td>
<td>360,250</td>
<td>594,255</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Imports</td>
<td>2,749,100</td>
<td>4,823,747</td>
<td>4,823,747</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Trading</td>
<td>1,311,776</td>
<td>1,058,182</td>
<td>1,058,182</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Financial</td>
<td>1,599,581</td>
<td>1,599,581</td>
<td>1,599,581</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Housing</td>
<td>116,834</td>
<td>116,834</td>
<td>116,834</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Consumption</td>
<td>7,945,133</td>
<td>7,945,133</td>
<td>7,945,133</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Miscellaneous</td>
<td>17,999,786</td>
<td>17,999,786</td>
<td>17,999,786</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>24,421,715</td>
<td>23,784,623</td>
<td>31,962,844</td>
<td>12,521,666</td>
<td>116,844,449</td>
<td>100.00</td>
<td></td>
</tr>
</tbody>
</table>

Gross Loans and Advances (Note 15) 102,708,481 90.06
Lease Rentals Receivable (Note 16) 11,037,648 9.94
113,746,129 100.00

The "others" category comprises the following advances:

<table>
<thead>
<tr>
<th>Category</th>
<th>Rs.000</th>
<th>Rs.000</th>
<th>Rs.000</th>
<th>Rs.000</th>
<th>Rs.000</th>
<th>Rs.000</th>
<th>Rs.000</th>
</tr>
</thead>
<tbody>
<tr>
<td>Exports</td>
<td>46,594</td>
<td>114,124</td>
<td>160,718</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Imports</td>
<td>2,698,100</td>
<td>4,633,368</td>
<td>4,633,368</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Trading</td>
<td>1,058,182</td>
<td>1,058,182</td>
<td>1,058,182</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Financial</td>
<td>1,311,776</td>
<td>1,311,776</td>
<td>1,311,776</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Housing</td>
<td>66,944</td>
<td>66,944</td>
<td>66,944</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Consumption</td>
<td>8,719,742</td>
<td>8,719,742</td>
<td>8,719,742</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Miscellaneous</td>
<td>17,999,786</td>
<td>17,999,786</td>
<td>17,999,786</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>26,529,378</td>
<td>25,518,388</td>
<td>34,562,088</td>
<td>12,521,666</td>
<td>33,000,000</td>
<td>43.55</td>
<td>100.00</td>
</tr>
</tbody>
</table>
### 15. LOANS AND ADVANCES (Contd.)

#### 15(d) Credit risk - Bank (Contd.)

#### 15(d)ii Sector/Productwise analysis of gross lending portfolio (Contd.)

<table>
<thead>
<tr>
<th>Sector/Type of Loan</th>
<th>Overdrafts</th>
<th>Short Term Loans</th>
<th>Medium Term Loans</th>
<th>Long Term Loans</th>
<th>Pawning</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Rs.000</td>
<td>Rs.000</td>
<td>Rs.000</td>
<td>Rs.000</td>
<td>Rs.000</td>
<td></td>
</tr>
<tr>
<td><strong>Group - 2006</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Food, beverages and tobacco</td>
<td>827,071</td>
<td>1,447,401</td>
<td>1,188,518</td>
<td>971,986</td>
<td>-</td>
<td>4,434,976</td>
</tr>
<tr>
<td>Agriculture, agro business and fisheries</td>
<td>1,164,392</td>
<td>1,591,911</td>
<td>1,188,518</td>
<td>971,986</td>
<td>-</td>
<td>5,704,053</td>
</tr>
<tr>
<td>Textile and wearing apparel</td>
<td>1,514,654</td>
<td>1,599,581</td>
<td>1,862,494</td>
<td>1,707,970</td>
<td>-</td>
<td>6,684,519</td>
</tr>
<tr>
<td>Wood and paper products</td>
<td>205,257</td>
<td>320,054</td>
<td>351,341</td>
<td>216,364</td>
<td>-</td>
<td>1,093,016</td>
</tr>
<tr>
<td>Rubber and leather products</td>
<td>439,024</td>
<td>858,714</td>
<td>206,215</td>
<td>288,767</td>
<td>-</td>
<td>1,792,720</td>
</tr>
<tr>
<td>Metals, chemicals and engineering</td>
<td>2,094,038</td>
<td>1,577,494</td>
<td>1,860,075</td>
<td>3,467,820</td>
<td>-</td>
<td>8,999,420</td>
</tr>
<tr>
<td>Hotels</td>
<td>507,700</td>
<td>51,733</td>
<td>702,354</td>
<td>822,350</td>
<td>-</td>
<td>2,084,137</td>
</tr>
<tr>
<td>Services</td>
<td>2,385,341</td>
<td>1,795,575</td>
<td>3,663,720</td>
<td>3,295,731</td>
<td>-</td>
<td>11,140,367</td>
</tr>
<tr>
<td>Foreclosed properties</td>
<td>-</td>
<td>-</td>
<td>3,295,731</td>
<td>3,295,731</td>
<td>-</td>
<td>6,591,462</td>
</tr>
<tr>
<td>Others</td>
<td>17,886,137</td>
<td>15,096,772</td>
<td>22,970,719</td>
<td>24,571,446</td>
<td>13,446,308</td>
<td>93,971,382</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>27,023,614</td>
<td>24,339,235</td>
<td>34,688,064</td>
<td>36,900,046</td>
<td>13,446,308</td>
<td>136,397,267</td>
</tr>
</tbody>
</table>

**Loans and Advances (Note 15)**: 121,383,403, 90.01%

**Lease Rentals Receivable (Note 16)**: 15,013,864, 9.99%

The "others" category comprises the following advances:

- **Exports**: 525,509, 998,262, 340,776, 360,249, - 2,224,796, 2.37%
- **Imports**: 1,358,493, 3,544,561, 503,801, 616,636, - 6,023,491, 6.41%
- **Trading**: 3,978,768, 1,113,713, 1,987,816, 779,297, - 7,859,594, 8.36%
- **Financial**: 1,597,645, 419,677, 1,851,222, 1,709,185, - 5,577,729, 5.94%
- **Housing**: - 99,202, 1,902,238, 11,386,021, - 13,387,461, 14.25%
- **Consumption**: 5,064,224, 4,403,939, 7,543,128, 5,176,784, - 22,188,075, 23.60%
- **Miscellaneous**: 5,361,498, 4,517,418, 8,841,738, 4,543,274, 13,446,308, 36,710,236, 39.07%

**Group - 2005**

<table>
<thead>
<tr>
<th>Sector/Type of Loan</th>
<th>Overdrafts</th>
<th>Short Term Loans</th>
<th>Medium Term Loans</th>
<th>Long Term Loans</th>
<th>Pawning</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Rs.000</td>
<td>Rs.000</td>
<td>Rs.000</td>
<td>Rs.000</td>
<td>Rs.000</td>
<td></td>
</tr>
<tr>
<td><strong>Food, beverages and tobacco</strong></td>
<td>772,303</td>
<td>1,210,154</td>
<td>1,034,262</td>
<td>482,100</td>
<td>-</td>
<td>3,498,199</td>
</tr>
<tr>
<td><strong>Agriculture, agro business and fisheries</strong></td>
<td>1,043,720</td>
<td>1,373,757</td>
<td>1,545,722</td>
<td>842,540</td>
<td>-</td>
<td>5,825,747</td>
</tr>
<tr>
<td><strong>Textiles and wearing apparel</strong></td>
<td>1,363,807</td>
<td>1,311,776</td>
<td>1,569,483</td>
<td>1,535,139</td>
<td>-</td>
<td>5,780,205</td>
</tr>
<tr>
<td><strong>Wood and paper products</strong></td>
<td>177,822</td>
<td>216,582</td>
<td>285,091</td>
<td>150,130</td>
<td>-</td>
<td>829,685</td>
</tr>
<tr>
<td><strong>Rubber and leather products</strong></td>
<td>353,902</td>
<td>795,298</td>
<td>118,226</td>
<td>247,894</td>
<td>-</td>
<td>1,515,320</td>
</tr>
<tr>
<td><strong>Metals, chemicals and engineering</strong></td>
<td>1,894,705</td>
<td>1,222,324</td>
<td>1,685,961</td>
<td>3,383,443</td>
<td>-</td>
<td>8,185,833</td>
</tr>
<tr>
<td><strong>Hotels</strong></td>
<td>444,224</td>
<td>28,032</td>
<td>660,918</td>
<td>808,623</td>
<td>-</td>
<td>1,921,802</td>
</tr>
<tr>
<td><strong>Services</strong></td>
<td>2,022,454</td>
<td>1,311,845</td>
<td>3,094,082</td>
<td>3,100,230</td>
<td>-</td>
<td>9,538,611</td>
</tr>
<tr>
<td><strong>Foreclosed properties</strong></td>
<td>-</td>
<td>-</td>
<td>557,540</td>
<td>557,540</td>
<td>-</td>
<td>557,540</td>
</tr>
<tr>
<td><strong>Others</strong></td>
<td>15,962,239</td>
<td>10,094,655</td>
<td>17,999,786</td>
<td>20,247,262</td>
<td>12,521,666</td>
<td>76,826,208</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>24,054,976</td>
<td>17,564,623</td>
<td>27,973,531</td>
<td>31,364,914</td>
<td>12,521,666</td>
<td>113,479,710</td>
</tr>
</tbody>
</table>

**Gross Loans and Advances (Note 15)**: 102,141,742, 90.01%

**Lease Rentals Receivable (Note 16)**: 11,337,968, 9.99%

The "others" category comprises the following advances:

- **Exports**: 207,751, 235,096, 87,909, 335,869, - 866,625, 1.13%
- **Imports**: 1,115,525 | 2,749,100 | 303,541 | 485,202 | - | 6,453,368 | 6.06%
- **Trading**: 3,299,476 | 127,768 | 578,999 | 698,638 | - | 4,705,081 | 6.12%
- **Financial**: 1,117,581 | 268,263 | 1,536,820 | 1,747,281 | - | 4,661,945 | 6.07%
- **Housing** | - | 66,944 | 723,083 | 8,269,358 | - | 9,059,385 | 11.79%
- **Consumption**: 4,687,381 | 3,222,888 | 6,940,532 | 4,715,741 | - | 19,746,542 | 25.70%
- **Miscellaneous**: 5,554,725 | 3,432,796 | 7,828,902 | 3,995,173 | 12,521,666 | 33,133,262 | 43.13%
| **Total** | 15,762,239 | 15,094,835 | 17,999,786 | 20,247,262 | 12,521,666 | 76,826,208 | 100.00 |
15. LOANS AND ADVANCES (Contd.)

|  | As at 31st December |
|---|---|---|---|
|  | 2006 | 2005 |
| Rs.000 | Rs.000 |

15(e) **Movement in Interest in Suspense - Bank**

<table>
<thead>
<tr>
<th>Description</th>
<th>2006</th>
<th>2005</th>
</tr>
</thead>
<tbody>
<tr>
<td>Balance brought forward</td>
<td>909,026</td>
<td>1,028,502</td>
</tr>
<tr>
<td>Interest suspended</td>
<td>280,784</td>
<td>352,025</td>
</tr>
<tr>
<td>Amounts recovered</td>
<td>(315,850)</td>
<td>(375,520)</td>
</tr>
<tr>
<td>Interest written off</td>
<td>(23,214)</td>
<td>(95,981)</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>850,746</td>
<td>909,026</td>
</tr>
</tbody>
</table>

As a policy, the Bank seals off interest on non-performing loans and advances after one year of classification (after 18 months). However, at the time of recovery, further interest on such advances is calculated from the date on which interest was sealed off.

15(f) **Movement in Foreclosed properties**

<table>
<thead>
<tr>
<th>Description</th>
<th>2006</th>
<th>2005</th>
</tr>
</thead>
<tbody>
<tr>
<td>Balance brought forward</td>
<td>137,089</td>
<td>506,473</td>
</tr>
<tr>
<td>Disposals during the year</td>
<td>69,804</td>
<td>(170,175)</td>
</tr>
<tr>
<td>Exchange translation</td>
<td>11,085</td>
<td>(1)</td>
</tr>
<tr>
<td>Reclassified to provision for loan losses</td>
<td>43,410</td>
<td>-</td>
</tr>
<tr>
<td>Provision for the year</td>
<td>99,379</td>
<td>(233,349)</td>
</tr>
<tr>
<td>Provision recoveries during the year</td>
<td>24,221</td>
<td>34,141</td>
</tr>
<tr>
<td><strong>Balance as at 31st December</strong></td>
<td>24,452</td>
<td>137,087</td>
</tr>
</tbody>
</table>

The total of Foreclosed properties and related provisions have been classified under loans and advances.

15(g) **Movement in provision for Foreclosed properties**

<table>
<thead>
<tr>
<th>Description</th>
<th>2006</th>
<th>2005</th>
</tr>
</thead>
<tbody>
<tr>
<td>Balance brought forward</td>
<td>420,451</td>
<td>235,102</td>
</tr>
<tr>
<td>Reclassified to provision for loan losses</td>
<td>43,410</td>
<td>-</td>
</tr>
<tr>
<td>Exchange rate variance in foreign currency provision</td>
<td>16,019</td>
<td>(2,348)</td>
</tr>
<tr>
<td>Specific provisions made during the year</td>
<td>99,379</td>
<td>233,349</td>
</tr>
<tr>
<td>Recoveries made during the year</td>
<td>24,221</td>
<td>(34,610)</td>
</tr>
<tr>
<td>Fully provided debts written off</td>
<td>-</td>
<td>(11,042)</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>468,218</td>
<td>420,451</td>
</tr>
</tbody>
</table>

15(h) **Provisions for discount of securities**

As per an amendment to the directions issued by the Central Bank of Sri Lanka on 15th August 2003 (effective from 1st January 2004) under section 46 (A) of the Banking Act No. 30 of 1988, as amended by Banking (Amendment) Act No. 33 of 1995, the initial and progressive discounts that need to be applied to the forced sale value of immovable properties held as collateral are as follows:

At the time of first provisioning for a loan, only 75% of the forced sale value (FSV) of the property based on a current professional valuation report is considered as the value of collateral (i.e. an initial haircut of 25% will be applied);

When an advance is transferred to the ‘Loss’ category, the following progressive discounts apply to the forced sale value of immovable property held as collateral, based on a current professional valuation report, depending on the time period for which it remains in the ‘Loss’ category:

<table>
<thead>
<tr>
<th>No. of years in loss category</th>
<th>% of FSV of immovable property that can be considered as the value of collateral</th>
</tr>
</thead>
<tbody>
<tr>
<td>1 - 2 years</td>
<td>60%</td>
</tr>
<tr>
<td>2 - 3 years</td>
<td>50%</td>
</tr>
<tr>
<td>3 - 4 years</td>
<td>40%</td>
</tr>
</tbody>
</table>

All immovable property held as collateral, relating to loans in the ‘Loss’ category for more than four years are reviewed on a regular basis and discounted further at the discretion of management.
15. LOANS AND ADVANCES (Contd.)

15(i) Provision for Kabool Lanka (Pvt) Ltd.

The Bank continued to increase the provisions against the exposure to Kabool Lanka (Pvt) Ltd. of approximately Rs. 2.8 Bn. as a measure of prudence, despite the fact that land and building has a value adequate to cover the un-provided exposure.

The assets jointly owned by Hatton National Bank Ltd. and Bank of Ceylon, acquired through the legal process was subsequently acquired by the Government under the Provisions of the Land Acquisition Act and the Banks have lodged their claim for compensation.

Total provision made by the Bank up to 31st December 2006 is Rs. 2.6 Bn.

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Rs.000</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

16. TOTAL LEASE RENTALS RECEIVABLE

<table>
<thead>
<tr>
<th></th>
<th>2006</th>
<th>2005</th>
<th>2006</th>
<th>2005</th>
</tr>
</thead>
<tbody>
<tr>
<td>Rs.000</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

16(a) Lease rentals receivable within one year

<table>
<thead>
<tr>
<th></th>
<th>2006</th>
<th>2005</th>
<th>2006</th>
<th>2005</th>
</tr>
</thead>
<tbody>
<tr>
<td>Gross lease rentals receivable</td>
<td>24,521,330</td>
<td>18,953,416</td>
<td>24,521,330</td>
<td>18,953,416</td>
</tr>
<tr>
<td>Initial rentals received</td>
<td>(127,769)</td>
<td>(137,873)</td>
<td>(127,769)</td>
<td>(137,873)</td>
</tr>
<tr>
<td>Lease rentals received</td>
<td>(9,379,697)</td>
<td>(7,477,575)</td>
<td>(9,379,697)</td>
<td>(7,477,575)</td>
</tr>
<tr>
<td>Total Lease rentals receivable</td>
<td>15,013,864</td>
<td>11,337,968</td>
<td>15,013,864</td>
<td>11,337,968</td>
</tr>
</tbody>
</table>

16(b) Lease rentals receivable after one year

<table>
<thead>
<tr>
<th></th>
<th>2006</th>
<th>2005</th>
<th>2006</th>
<th>2005</th>
</tr>
</thead>
<tbody>
<tr>
<td>Gross lease rentals receivable</td>
<td>9,374,276</td>
<td>6,817,535</td>
<td>9,374,276</td>
<td>6,817,535</td>
</tr>
<tr>
<td>Unearned lease income</td>
<td>(1,662,904)</td>
<td>(949,926)</td>
<td>(1,662,904)</td>
<td>(949,926)</td>
</tr>
<tr>
<td>Provision for lease receivable</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>- General [16(c)]</td>
<td>(154,964)</td>
<td>(115,727)</td>
<td>(154,964)</td>
<td>(115,727)</td>
</tr>
<tr>
<td>Total Lease rentals receivable</td>
<td>7,756,408</td>
<td>5,751,882</td>
<td>7,756,408</td>
<td>5,751,882</td>
</tr>
</tbody>
</table>

16(c) Movement in provision for lease rentals receivable

<table>
<thead>
<tr>
<th></th>
<th>2006</th>
<th>2006</th>
<th>2005</th>
<th>2005</th>
</tr>
</thead>
<tbody>
<tr>
<td>Rs.000</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Specific General Specific General</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
</tbody>
</table>

Bank

<table>
<thead>
<tr>
<th></th>
<th>2006</th>
<th>2005</th>
<th>2006</th>
<th>2005</th>
</tr>
</thead>
<tbody>
<tr>
<td>Rs.000</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Specific General Specific General</td>
<td>214,484</td>
<td>182,665</td>
<td>150,384</td>
<td>140,617</td>
</tr>
<tr>
<td>Exchange rate variance on foreign currency provision</td>
<td>-</td>
<td>16</td>
<td>-</td>
<td>(27)</td>
</tr>
<tr>
<td>Additional provision made (Note 7)</td>
<td>214,484</td>
<td>182,681</td>
<td>150,384</td>
<td>140,590</td>
</tr>
<tr>
<td>Recoveries made during the year</td>
<td>(8,552)</td>
<td>-</td>
<td>(9,010)</td>
<td>(751)</td>
</tr>
<tr>
<td>Fully provided debts written off</td>
<td>(435)</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Total</td>
<td>248,227</td>
<td>235,765</td>
<td>214,484</td>
<td>182,685</td>
</tr>
</tbody>
</table>

Group

<table>
<thead>
<tr>
<th></th>
<th>2006</th>
<th>2005</th>
<th>2006</th>
<th>2005</th>
</tr>
</thead>
<tbody>
<tr>
<td>Rs.000</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Specific General Specific General</td>
<td>214,484</td>
<td>182,665</td>
<td>150,384</td>
<td>140,617</td>
</tr>
<tr>
<td>Exchange rate variance on foreign currency provision</td>
<td>-</td>
<td>16</td>
<td>-</td>
<td>(27)</td>
</tr>
<tr>
<td>Additional provision made (Note 7)</td>
<td>214,484</td>
<td>182,681</td>
<td>150,384</td>
<td>140,590</td>
</tr>
<tr>
<td>Recoveries made during the year</td>
<td>(8,552)</td>
<td>-</td>
<td>(9,010)</td>
<td>(751)</td>
</tr>
<tr>
<td>Fully provided debts written off</td>
<td>(435)</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Total</td>
<td>248,227</td>
<td>235,765</td>
<td>214,484</td>
<td>182,685</td>
</tr>
</tbody>
</table>

There were no lease rentals receivable beyond five years.

Financial Reports
17. **NON CURRENT ASSETS HELD FOR SALE**

As at 31st December 2006

<table>
<thead>
<tr>
<th>Description</th>
<th>Bank Carrying amount</th>
<th>Group Carrying amount</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Rs.000</td>
<td>Rs.000</td>
</tr>
<tr>
<td>Reclassified from Property, Plant and Equipment (Note 21)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Freehold land (Note 17(a))</td>
<td>5,614</td>
<td>5,614</td>
</tr>
<tr>
<td>Computer equipment</td>
<td>378</td>
<td>378</td>
</tr>
<tr>
<td>Equipment, furniture and fixtures</td>
<td>564</td>
<td>564</td>
</tr>
<tr>
<td></td>
<td>6,556</td>
<td>6,556</td>
</tr>
</tbody>
</table>

**17(a) Freehold land**

<table>
<thead>
<tr>
<th>Extent (perches)</th>
<th>Cost of land Rs.000</th>
</tr>
</thead>
<tbody>
<tr>
<td>Land at No. 118A, Negombo Road, Narammala</td>
<td>40</td>
</tr>
<tr>
<td>Land at No. 67/11, Kumaradola Road, Monaragala</td>
<td>20</td>
</tr>
<tr>
<td></td>
<td>5,614</td>
</tr>
</tbody>
</table>

As required by Sri Lanka Accounting Standard 38 (revised 2006) - "Non-Current Assets Held for Sale and Discontinued Operations" (SLAS 38), assets previously classified under Property, Plant & Equipment which met the definition of Non-Current Assets Held for Sale, have been reclassified during the year. The effective date of SLAS 38 is 1st April 2006, as such comparatives have not been reclassified.

18. **INVESTMENTS IN ASSOCIATE COMPANIES**

As at 31st December

<table>
<thead>
<tr>
<th>Principal Activity</th>
<th>Market Value 2006</th>
<th>Market Value 2005</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Holding %</td>
<td>Balance Rs.000</td>
</tr>
<tr>
<td><strong>18(a) Bank</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td><em>(Quoted)</em></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Lanka Ventures</td>
<td>20.07</td>
<td>132,326</td>
</tr>
<tr>
<td>Ltd</td>
<td></td>
<td>132,980</td>
</tr>
<tr>
<td><em>(Unquoted)</em></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Browns Engineering</td>
<td>32.63</td>
<td>20,560</td>
</tr>
<tr>
<td>(Pvt) Ltd</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Provision for diminution in value</td>
<td>(20,560)</td>
<td>(20,560)</td>
</tr>
<tr>
<td><strong>Total for the Bank</strong></td>
<td></td>
<td>132,326</td>
</tr>
</tbody>
</table>

Browns Engineering (Pvt) Limited is under liquidation and the Bank’s investment has been fully provided for.
### 18. INVESTMENTS IN ASSOCIATE COMPANIES (Contd.)

As at 31st December

<table>
<thead>
<tr>
<th>Principal Activity</th>
<th>2006</th>
<th>%</th>
<th>Balance Rs.000</th>
<th>Market Value Rs.000</th>
<th>%</th>
<th>Balance Rs.000</th>
<th>Market Value Rs.000</th>
</tr>
</thead>
<tbody>
<tr>
<td>18(b) Group Quoted Investments</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Investment in Associate companies (at cost)</td>
<td>132,326</td>
<td></td>
<td>132,326</td>
<td>132,326</td>
<td></td>
<td>132,326</td>
<td></td>
</tr>
<tr>
<td>Negative goodwill on acquisition</td>
<td>5,830</td>
<td></td>
<td>5,830</td>
<td>5,830</td>
<td></td>
<td>5,830</td>
<td></td>
</tr>
<tr>
<td>Group share of Associate company retained profits</td>
<td>-</td>
<td></td>
<td>-</td>
<td>-</td>
<td></td>
<td>-</td>
<td></td>
</tr>
<tr>
<td>Balance as at 1st January</td>
<td>32,436</td>
<td></td>
<td>31,598</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Current year’s share of profits after tax</td>
<td>8,244</td>
<td></td>
<td>15,734</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Dividends received during the year</td>
<td>(13,967)</td>
<td></td>
<td>(14,896)</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Group share of Associate company net assets</td>
<td>164,869</td>
<td></td>
<td>170,592</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Unamortized negative goodwill carried forward [Note 18(b)i]</td>
<td>-</td>
<td></td>
<td>-</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Group investment in Associate companies (equity basis)</td>
<td>164,869</td>
<td></td>
<td>170,592</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

#### 18(b)i Negative goodwill on acquisition

| | | |
| Unamortized negative goodwill brought forward | - | 1,166 |
| Amortized during the year | - | (1,166) |
| Balance as at 31st December | - | - |

### 19. INVESTMENTS IN SUBSIDIARY COMPANIES

#### Bank

**19(a) Quoted**

- HNB Assurance Ltd. (14,996,500 shares of Rs. 10/- each)
  - Insurance 60 149,965 374,912 60 149,965 191,205

**19(b) Unquoted**

<table>
<thead>
<tr>
<th>Principal Activity</th>
<th>Directors' Valuation Rs.000</th>
</tr>
</thead>
<tbody>
<tr>
<td>Property Development</td>
<td>100 1,973,000 1,973,000</td>
</tr>
<tr>
<td>HNB Securities Ltd (15,000,000 ordinary shares of Rs.10/- each)</td>
<td>100 150,000 150,000</td>
</tr>
<tr>
<td>HNB Stockbrokers (Pvt) Ltd (3,600,000 ordinary shares of Rs.10/- each)</td>
<td>100 20,698 20,698</td>
</tr>
<tr>
<td>Total for Bank</td>
<td>2,293,663</td>
</tr>
</tbody>
</table>

[Note 18(b)i]
## 20. INVESTMENT PROPERTIES

<table>
<thead>
<tr>
<th>Cost as at 1st January 2006</th>
<th>Bank</th>
<th>Group</th>
</tr>
</thead>
<tbody>
<tr>
<td>Reclassified from Property, Plant and Equipment</td>
<td>195,480</td>
<td>242,474</td>
</tr>
<tr>
<td>Improvements</td>
<td>25</td>
<td>25</td>
</tr>
<tr>
<td><strong>Cost as at 31st December 2006</strong></td>
<td><strong>Bank</strong></td>
<td><strong>Group</strong></td>
</tr>
<tr>
<td>Reclassified from Property, Plant and Equipment</td>
<td>195,505</td>
<td>242,499</td>
</tr>
<tr>
<td>Charge for the year</td>
<td>1,284</td>
<td>4,487</td>
</tr>
<tr>
<td><strong>Accumulated depreciation as at 31st December 2006</strong></td>
<td><strong>Bank</strong></td>
<td><strong>Group</strong></td>
</tr>
<tr>
<td></td>
<td>5,650</td>
<td>57,474</td>
</tr>
</tbody>
</table>

As required by Sri Lanka Accounting Standard 40 (revised 2005) - “Investment Property” (SLAS 40), assets previously classified under Property, Plant & Equipment which met the definition of Investment property, have been reclassified during the year. The effective date of SLAS 40 is 1st January 2006, as such comparatives have not been reclassified.

Land situated at No.479, T B Jayah Mw., Colombo 10 on which HNB Towers is built, is leased to Sithma Development [Pvt] Ltd and the Bank receives ground rent. Accordingly, this land was classified as Investment property in the Balance Sheet of the Bank. However, according to SLAS 40, the said land is treated as Property, Plant & Equipment in the Group Balance Sheet, since the land is leased to a Group entity.

### 20(a) Investment Properties

#### 20(a)i Bank

<table>
<thead>
<tr>
<th>Building Extent Land</th>
<th>Cost/Carrying amount</th>
<th>Fair Value</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Land</td>
<td>Building</td>
</tr>
<tr>
<td></td>
<td>Rs.000</td>
<td>Rs.000</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>As at 31st December 2006</td>
<td></td>
<td></td>
</tr>
<tr>
<td>23 &amp; 23 1/1 Independence Avenue Colombo 7</td>
<td>9,975</td>
<td>60.40</td>
</tr>
<tr>
<td>479 T B Jayah Mawatha Colombo 10</td>
<td>Land</td>
<td>100.00</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>195,505</strong></td>
<td><strong>1,063,250</strong></td>
</tr>
</tbody>
</table>

#### 20(a)ii Group

<table>
<thead>
<tr>
<th>Building Extent Land</th>
<th>Cost/Carrying amount</th>
<th>Fair Value</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Land</td>
<td>Building</td>
</tr>
<tr>
<td></td>
<td>Rs.000</td>
<td>Rs.000</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>As at 31st December 2006</td>
<td></td>
<td></td>
</tr>
<tr>
<td>23 &amp; 23 1/1 Independence Avenue Colombo 7</td>
<td>9,975</td>
<td>60.40</td>
</tr>
<tr>
<td>Smart building 21, 21A, 23 &amp; 25 Janadhipathi Mawatha Colombo 1</td>
<td>Land</td>
<td>42,765</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>242,499</strong></td>
<td><strong>712,050</strong></td>
</tr>
</tbody>
</table>

The fair value of the Investment properties as at 31.12.2006 was based on market valuations carried out as at Balance Sheet date by Messrs J M J Fernando, F. I. V., D.I.V. (Sri Lanka), K C B Condegama, A.I.V. (Sri Lanka) members of the Institute of Valuers of Sri Lanka, who are independent valuers not connected with the Bank.
### 21. PROPERTY PLANT AND EQUIPMENT

#### Bank

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Note 21(c) Note 21(b) Note 21(a) Note 21(a)</td>
<td>Rs.000</td>
<td>Rs.000</td>
<td>Rs.000</td>
<td>Rs.000</td>
<td>Rs.000</td>
<td>Rs.000</td>
<td>Rs.000</td>
<td>Rs.000</td>
</tr>
<tr>
<td>Cost/Valuation as at 31/12/2005</td>
<td>623,256</td>
<td>1,714,564</td>
<td>1,943,480</td>
<td>1,746,043</td>
<td>87,594</td>
<td>87,826</td>
<td>6,202,763</td>
<td>5,790,083</td>
</tr>
<tr>
<td>Transfers to Intangible assets</td>
<td>-</td>
<td>-</td>
<td>(611,422)</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>(611,422)</td>
<td>(627,331)</td>
</tr>
<tr>
<td>Adjusted Cost/Valuation as at 31/12/2005</td>
<td>623,256</td>
<td>1,714,564</td>
<td>1,332,058</td>
<td>1,746,043</td>
<td>87,594</td>
<td>87,826</td>
<td>5,591,341</td>
<td>5,362,752</td>
</tr>
<tr>
<td>Transfers to Investment property</td>
<td>-</td>
<td>(195,480)</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>(195,480)</td>
<td>-</td>
</tr>
<tr>
<td>Transfers to Non-current assets held for sale</td>
<td>-</td>
<td>(5,614)</td>
<td>(6,559)</td>
<td>(48,183)</td>
<td>-</td>
<td>-</td>
<td>(60,356)</td>
<td>-</td>
</tr>
<tr>
<td>Sub category transfers</td>
<td>6,801</td>
<td>(2,390)</td>
<td>(181,619)</td>
<td>177,208</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Additions and improvements</td>
<td>31,525</td>
<td>26,213</td>
<td>64,767</td>
<td>117,875</td>
<td>31,834</td>
<td>211,632</td>
<td>483,396</td>
<td>312,520</td>
</tr>
<tr>
<td>Disposals during the year</td>
<td>(2,621)</td>
<td>(1,193)</td>
<td>(7,004)</td>
<td>(31,603)</td>
<td>-</td>
<td>-</td>
<td>(42,421)</td>
<td>(83,931)</td>
</tr>
<tr>
<td>Transfers from capital work-in-progress</td>
<td>2,957</td>
<td>24,420</td>
<td>38,811</td>
<td>5,043</td>
<td>-</td>
<td>(71,231)</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Cost/Valuation as at 31/12/2006</td>
<td>661,918</td>
<td>1,560,520</td>
<td>1,240,454</td>
<td>1,966,383</td>
<td>118,978</td>
<td>228,227</td>
<td>5,776,480</td>
<td>5,591,341</td>
</tr>
<tr>
<td>Accumulated depreciation as at 31/12/2005</td>
<td>286,389</td>
<td>135,417</td>
<td>1,289,690</td>
<td>1,046,470</td>
<td>74,428</td>
<td>-</td>
<td>2,832,394</td>
<td>2,403,545</td>
</tr>
<tr>
<td>Transfers to Intangible assets</td>
<td>-</td>
<td>-</td>
<td>(300,531)</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>(300,531)</td>
<td>(263,439)</td>
</tr>
<tr>
<td>Adjusted accumulated depreciation as at 31/12/2005</td>
<td>286,389</td>
<td>135,417</td>
<td>989,159</td>
<td>1,046,470</td>
<td>74,428</td>
<td>-</td>
<td>2,531,863</td>
<td>2,140,106</td>
</tr>
<tr>
<td>Transfers to Investment property</td>
<td>-</td>
<td>(4,366)</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>(4,366)</td>
<td>-</td>
</tr>
<tr>
<td>Transfers to Non-current assets held for sale</td>
<td>-</td>
<td>-</td>
<td>(4,181)</td>
<td>(47,619)</td>
<td>-</td>
<td>-</td>
<td>(53,800)</td>
<td>-</td>
</tr>
<tr>
<td>Sub category transfers</td>
<td>734</td>
<td>(507)</td>
<td>(151,295)</td>
<td>151,068</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Charge for the year</td>
<td>68,634</td>
<td>22,247</td>
<td>93,448</td>
<td>235,979</td>
<td>9,883</td>
<td>-</td>
<td>430,211</td>
<td>457,229</td>
</tr>
<tr>
<td>Disposals during the year</td>
<td>(1,294)</td>
<td>(6)</td>
<td>(6,348)</td>
<td>(27,569)</td>
<td>-</td>
<td>-</td>
<td>(35,217)</td>
<td>(65,472)</td>
</tr>
<tr>
<td>Accumulated depreciation as at 31/12/2006</td>
<td>354,463</td>
<td>152,785</td>
<td>918,803</td>
<td>1,358,329</td>
<td>84,311</td>
<td>-</td>
<td>2,868,691</td>
<td>2,531,843</td>
</tr>
<tr>
<td>Net book value as at 31/12/2006</td>
<td>307,455</td>
<td>1,407,735</td>
<td>321,651</td>
<td>608,054</td>
<td>34,667</td>
<td>228,227</td>
<td>2,907,789</td>
<td></td>
</tr>
<tr>
<td>Net book value as at 31/12/2005</td>
<td>336,867</td>
<td>1,579,347</td>
<td>342,899</td>
<td>699,573</td>
<td>13,166</td>
<td>87,826</td>
<td>3,059,478</td>
<td></td>
</tr>
</tbody>
</table>

As set out in Significant Accounting Policy No.9.10.1, the Bank is in the process of revaluing its freehold land & building on a rolling basis. Based on the revaluations completed as at Balance Sheet date, the surplus on revaluation amounted to Rs. 704 Mn. The Bank has not recognised this surplus in the Statement of Changes in Equity and will credit the total surplus to Capital Reserve on completion of the revaluation process in 2007.
## 21. PROPERTY PLANT AND EQUIPMENT (Contd.)

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Note 21(c)</td>
<td>Rs.000</td>
<td>Rs.000</td>
<td>Rs.000</td>
<td>Rs.000</td>
<td>Rs.000</td>
<td>Rs.000</td>
<td>Rs.000</td>
<td>Rs.000</td>
</tr>
<tr>
<td><strong>Cost/Valuation</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>as at 31/12/2005</td>
<td>623,256</td>
<td>4,311,255</td>
<td>2,031,371</td>
<td>3,882,016</td>
<td>98,872</td>
<td>87,826</td>
<td>11,034,596</td>
<td>10,573,268</td>
</tr>
<tr>
<td>Transfers to</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Intangible assets</td>
<td>-</td>
<td>-</td>
<td>(650,935)</td>
<td>-</td>
<td>-</td>
<td></td>
<td>(650,935)</td>
<td>(655,839)</td>
</tr>
<tr>
<td><strong>Adjusted Cost/Valuation</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>as at 31/12/2005</td>
<td>623,256</td>
<td>4,311,255</td>
<td>1,380,436</td>
<td>3,882,016</td>
<td>98,872</td>
<td>87,826</td>
<td>10,383,661</td>
<td>10,117,429</td>
</tr>
<tr>
<td>Transfers to</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Investment property</td>
<td>-</td>
<td>(212,925)</td>
<td>-</td>
<td>(29,549)</td>
<td>-</td>
<td>-</td>
<td>(242,474)</td>
<td>-</td>
</tr>
<tr>
<td>Transfers to Non-current</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>assets held for sale</td>
<td>-</td>
<td>(5,614)</td>
<td>[6,559]</td>
<td>[48,183]</td>
<td>-</td>
<td>(60,356)</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Sub category transfers</td>
<td>6,801</td>
<td>(2,390)</td>
<td>(181,619)</td>
<td>177,208</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Additions and improvements</td>
<td>31,525</td>
<td>26,213</td>
<td>77,318</td>
<td>132,099</td>
<td>31,384</td>
<td>260,904</td>
<td>559,443</td>
<td>350,560</td>
</tr>
<tr>
<td>Disposals</td>
<td>(2,621)</td>
<td>(1,193)</td>
<td>(7,004)</td>
<td>(31,916)</td>
<td>-</td>
<td>-</td>
<td>(42,734)</td>
<td>(84,328)</td>
</tr>
<tr>
<td>Transfers from capital</td>
<td>-</td>
<td>-</td>
<td>(242,925)</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>work-in-progress</td>
<td>2,957</td>
<td>24,420</td>
<td>38,811</td>
<td>5,043</td>
<td>-</td>
<td>[71,231]</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td><strong>Cost/Valuation</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>as at 31/12/2006</td>
<td>661,918</td>
<td>4,139,766</td>
<td>1,301,383</td>
<td>4,086,718</td>
<td>130,256</td>
<td>277,499</td>
<td>10,597,540</td>
<td>10,383,661</td>
</tr>
<tr>
<td>Accumulated Depreciation</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>as at 31/12/2005</td>
<td>286,389</td>
<td>227,876</td>
<td>1,318,504</td>
<td>1,226,196</td>
<td>83,477</td>
<td>-</td>
<td>3,142,442</td>
<td>2,614,228</td>
</tr>
<tr>
<td>Transfers to</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Intangible assets</td>
<td>-</td>
<td>-</td>
<td>[311,532]</td>
<td>-</td>
<td>-</td>
<td></td>
<td>[311,532]</td>
<td>[269,415]</td>
</tr>
<tr>
<td><strong>Adjusted accumulated</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>depreciation as at 31/12/2005</td>
<td>286,389</td>
<td>227,876</td>
<td>1,006,972</td>
<td>1,226,196</td>
<td>83,477</td>
<td>-</td>
<td>2,830,910</td>
<td>2,344,813</td>
</tr>
<tr>
<td>Transfers to</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Investment property</td>
<td>-</td>
<td>(23,438)</td>
<td>-</td>
<td>(29,549)</td>
<td>-</td>
<td>(52,987)</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Transfers to non-current</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>assets held for sale</td>
<td>-</td>
<td>-</td>
<td>(6,181)</td>
<td>[47,619]</td>
<td>-</td>
<td>(53,800)</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Sub category transfers</td>
<td>734</td>
<td>(507)</td>
<td>(151,295)</td>
<td>151,068</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Charge for the year</td>
<td>68,634</td>
<td>50,701</td>
<td>101,026</td>
<td>291,621</td>
<td>11,361</td>
<td>-</td>
<td>523,343</td>
<td>551,942</td>
</tr>
<tr>
<td>Disposals during the year</td>
<td>(1,294)</td>
<td>(6)</td>
<td>(6,348)</td>
<td>(27,851)</td>
<td>-</td>
<td>(35,499)</td>
<td>(65,845)</td>
<td>-</td>
</tr>
<tr>
<td><strong>Accumulated Depreciation</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>as at 31/12/2006</td>
<td>354,463</td>
<td>254,626</td>
<td>944,174</td>
<td>1,563,866</td>
<td>94,838</td>
<td>-</td>
<td>3,211,967</td>
<td>2,830,910</td>
</tr>
<tr>
<td>Net book value</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>as at 31/12/2006</td>
<td>307,455</td>
<td>3,885,140</td>
<td>357,209</td>
<td>2,522,852</td>
<td>35,418</td>
<td>277,499</td>
<td>7,385,573</td>
<td>7,552,751</td>
</tr>
</tbody>
</table>
### 21(a) Computer Equipment - Bank

<table>
<thead>
<tr>
<th>Prior to 1.7.2000</th>
<th>Additions</th>
<th>After 1.7.2000</th>
<th>Total</th>
<th>Rate of depreciation</th>
<th>Cost/valuation as at 01.01.2006</th>
<th>Additions and improvements</th>
<th>Transfers from capital work-in-progress</th>
<th>Sub category transfers</th>
<th>Transfers to Non-current assets held for sale</th>
<th>Transfers to Intangible assets</th>
<th>Disposals during the year</th>
<th>Cost/valuation as at 31.12.2006</th>
</tr>
</thead>
<tbody>
<tr>
<td>Rs.000</td>
<td>Rs.000</td>
<td>Rs.000</td>
<td>Rs.000</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>1,72000</td>
<td>1,72000</td>
<td>3,440000</td>
<td>1,332,058</td>
<td>25%</td>
<td>646,047</td>
<td>-</td>
<td>64,767</td>
<td>-</td>
<td>(4,097)</td>
<td>-</td>
<td>(4,109)</td>
<td>576,822</td>
</tr>
<tr>
<td>1,787,119</td>
<td>1,787,119</td>
<td>1,787,119</td>
<td>1,787,119</td>
<td>16.67%</td>
<td>686,011</td>
<td>64,767</td>
<td>38,811</td>
<td>38,811</td>
<td>(2,462)</td>
<td>-</td>
<td>(2,895)</td>
<td>663,632</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>1,240,454</td>
<td></td>
<td>1,332,058</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>1,240,454</td>
</tr>
</tbody>
</table>

### 21(b) Freehold Land and Buildings - Bank

<table>
<thead>
<tr>
<th>Buildings</th>
<th>Extent (Sq.ft. or perches)</th>
<th>Cost of Land (Rs.000)</th>
<th>Cost of Buildings (Rs.000)</th>
<th>Total Value (Rs.000)</th>
<th>Accumulated Depreciation (Rs.000)</th>
<th>Net Book Value (Rs.000)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Within Colombo City Limits</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Borella Branch</td>
<td>7,530</td>
<td>28.00</td>
<td>21,702</td>
<td>37,232</td>
<td>58,934</td>
<td>2,789</td>
</tr>
<tr>
<td>53/1 D S Senanayake Mawatha, Borella</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Gunasinghepura Pay Office &amp; Stores</td>
<td>4,835</td>
<td>37.53</td>
<td>28,411</td>
<td>8,025</td>
<td>36,436</td>
<td>1,508</td>
</tr>
<tr>
<td>11 Mohandiram’s Road, Colombo 12</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Bambalapitiya Branch</td>
<td>12,786</td>
<td>20.00</td>
<td>10,000</td>
<td>28,044</td>
<td>38,044</td>
<td>6,411</td>
</tr>
<tr>
<td>285 Galle Road, Colombo 4</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>City Office</td>
<td>28,900</td>
<td>84.00</td>
<td>100,800</td>
<td>84,110</td>
<td>184,910</td>
<td>23,725</td>
</tr>
<tr>
<td>16 Janadhipathi Mawatha, Colombo 1 &amp; 25 Chatham Street, Colombo 1</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Centralized Operations Bldg. 92,008</td>
<td>90 Vinayalankara Mawatha, Colombo 10</td>
<td>249.00</td>
<td>145,599</td>
<td>32,046</td>
<td>177,645</td>
<td>1,493</td>
</tr>
<tr>
<td>Main Branch</td>
<td>36,379</td>
<td>40.00</td>
<td>32,000</td>
<td>81,516</td>
<td>113,516</td>
<td>21,776</td>
</tr>
<tr>
<td>10 R A De Mel Mawatha, Colombo 03</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Pettah Extension Office</td>
<td>3,708</td>
<td>7.60</td>
<td>9,099</td>
<td>892</td>
<td>9,991</td>
<td>12</td>
</tr>
<tr>
<td>149-151 Main Street, Colombo 11</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
## 21. PROPERTY PLANT AND EQUIPMENT (Contd.)

### 21(b) Freehold Land and Buildings - Bank (Contd.)

<table>
<thead>
<tr>
<th>Buildings Extent</th>
<th>Cost of Land</th>
<th>Cost of Buildings</th>
<th>Total Value</th>
<th>Accumulated Depreciation</th>
<th>Net Book Value</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Within Colombo City Limits (Contd.)</strong></td>
<td>Sq.ft. (perches)</td>
<td>Rs.000</td>
<td>Rs.000</td>
<td>Rs.000</td>
<td>Rs.000</td>
</tr>
<tr>
<td>Sea Street Branch</td>
<td>3,652</td>
<td>6.93</td>
<td>8,200</td>
<td>53,635</td>
<td>61,835</td>
</tr>
<tr>
<td>60 Sea Street Colombo 11</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Wellawatte Branch</td>
<td>18,040</td>
<td>36.05</td>
<td>29,854</td>
<td>62,658</td>
<td>92,512</td>
</tr>
<tr>
<td>102 Galle Road Wellawatte</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Grandpass Branch</td>
<td>9,325</td>
<td>24.00</td>
<td>9,359</td>
<td>22,337</td>
<td>31,696</td>
</tr>
<tr>
<td>182 St. Joseph Street Colombo 14</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Pettah Branch</td>
<td>9,732</td>
<td>7.56</td>
<td>33,919</td>
<td>93,484</td>
<td>127,403</td>
</tr>
<tr>
<td>88 Main Street Colombo 11</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Total freehold land and buildings within Colombo City Limits</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Outside Colombo City Limits</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Akkaraipattu Branch</td>
<td>7,700</td>
<td>19.32</td>
<td>3,351</td>
<td>20,811</td>
<td>24,162</td>
</tr>
<tr>
<td>1 Main street Akkaraipattu</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Ambalangoda Branch</td>
<td>4,950</td>
<td>29.90</td>
<td>3,102</td>
<td>9,022</td>
<td>12,124</td>
</tr>
<tr>
<td>94/1 New Road Ambalangoda</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Badulla Branch</td>
<td>3,584</td>
<td>28.44</td>
<td>2,418</td>
<td>11,390</td>
<td>13,808</td>
</tr>
<tr>
<td>15 151/1 Udayaraja Mawatha Badulla.</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Boralessgamuwa Branch</td>
<td>3,500</td>
<td>30.34</td>
<td>5,048</td>
<td>15,442</td>
<td>20,490</td>
</tr>
<tr>
<td>24 Maharagama Road Boralessgamuwa</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Dambulla Branch</td>
<td>6,600</td>
<td>100.00</td>
<td>14,565</td>
<td>18,456</td>
<td>33,021</td>
</tr>
<tr>
<td>622 Anuradhapura Road Dambulla</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Galle Branch</td>
<td>4,988</td>
<td>13.80</td>
<td>11,000</td>
<td>18,949</td>
<td>29,949</td>
</tr>
<tr>
<td>3 Wakwella Road Galle</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Gampola Branch</td>
<td>5,604</td>
<td>11.88</td>
<td>8,319</td>
<td>3,221</td>
<td>11,540</td>
</tr>
<tr>
<td>12 Kandy Road Gampola</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Hatton Branch</td>
<td>5,500</td>
<td>70.02</td>
<td>10,456</td>
<td>7,301</td>
<td>17,757</td>
</tr>
<tr>
<td>78 Dambulla Road Hatton</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
### 21. PROPERTY PLANT AND EQUIPMENT (Contd.)

#### 21(b) Freehold Land and Buildings - Bank (Contd.)

<table>
<thead>
<tr>
<th>Buildings</th>
<th>Extent (perches)</th>
<th>Cost of Land Rs.000</th>
<th>Cost of Buildings Rs.000</th>
<th>Total Value Rs.000</th>
<th>Accumulated Depreciation Rs.000</th>
<th>Net Book Value Rs.000</th>
</tr>
</thead>
<tbody>
<tr>
<td>Outside Colombo City Limits (Contd.)</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>“Mount Bungalow”</td>
<td>4,200</td>
<td>160.00</td>
<td>3,620</td>
<td>4,958</td>
<td>8,578</td>
<td>224</td>
</tr>
<tr>
<td>7 Mount Road Hatton</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Jaffna Property</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>18/1/5C Ponnambalam Road Jaffna</td>
<td>Under Development</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Kandy Branch</td>
<td>10,600</td>
<td>78.90</td>
<td>38,627</td>
<td>16,298</td>
<td>54,925</td>
<td>3,913</td>
</tr>
<tr>
<td>Kurunegala Branch</td>
<td>9,600</td>
<td>16.25</td>
<td>3,250</td>
<td>8,553</td>
<td>11,803</td>
<td>1,879</td>
</tr>
<tr>
<td>6 St. Anne’s Street Kurunegala</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Nawalapitiya Branch</td>
<td>2,324</td>
<td>46.00</td>
<td>875</td>
<td>8,049</td>
<td>8,924</td>
<td>1,413</td>
</tr>
<tr>
<td>92 Gampola Road Nawalapitiya</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Negombo Branch</td>
<td>3,504</td>
<td>8.88</td>
<td>1,776</td>
<td>14,930</td>
<td>16,706</td>
<td>3,731</td>
</tr>
<tr>
<td>18 Rajapakse Broadway Negombo</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Nittambuwa Branch</td>
<td>4,000</td>
<td>14.50</td>
<td>687</td>
<td>10,291</td>
<td>10,978</td>
<td>2,267</td>
</tr>
<tr>
<td>22 Kandy Road Nittambuwa</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Nochchiyagama Branch</td>
<td>1,800</td>
<td>40.00</td>
<td>320</td>
<td>11,140</td>
<td>11,460</td>
<td>1,988</td>
</tr>
<tr>
<td>10 Puttalam Road Nochchiyagama</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Wattala Branch</td>
<td>6,400</td>
<td>53.00</td>
<td>10,399</td>
<td>22,510</td>
<td>32,909</td>
<td>3,356</td>
</tr>
<tr>
<td>270, 270/1 Negombo Road Wattala</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Kuliyaapitiya Additional Bare Land Property</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>225 Madampe Road Kuliyaapitiya</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Kurunegala New Bare Land Property</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>34/16 St. Anne’s Road Kurunegala</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Nuwara Eliya Branch 181 High Level Road Nuwara Eliya</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>/Bungalow</td>
<td>11,639</td>
<td>19.50</td>
<td>7,550</td>
<td>28,678</td>
<td>36,228</td>
<td>6,807</td>
</tr>
<tr>
<td>42 Queen Elizabeth Drive Nuwara Eliya</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
21. PROPERTY PLANT AND EQUIPMENT (Contd.)

21(b) Freehold Land and Buildings - Bank (Contd.)

<table>
<thead>
<tr>
<th>Buildings Extent</th>
<th>Cost of Land</th>
<th>Cost of Buildings</th>
<th>Total Value</th>
<th>Accumulated Depreciation</th>
<th>Net Book Value</th>
</tr>
</thead>
<tbody>
<tr>
<td>Outside Colombo City Limits (Contd.)</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Trincomalee Branch</td>
<td>6,802</td>
<td>20.51</td>
<td>1,451</td>
<td>16,236</td>
<td>17,687</td>
</tr>
<tr>
<td>59 Ahambaram Road Trincomalee</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Anuradhapura Branch</td>
<td>2,000</td>
<td>25.59</td>
<td>5,337</td>
<td>13,247</td>
<td>18,584</td>
</tr>
<tr>
<td>30 Maitriplata Senanayake Mawatha Anuradhapura</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Maskeliya Branch</td>
<td>1,900</td>
<td>20.32</td>
<td>1,948</td>
<td>2,619</td>
<td>4,567</td>
</tr>
<tr>
<td>9 New Town Maskeliya</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Mannar Branch</td>
<td>4,200</td>
<td>23.00</td>
<td>619</td>
<td>5,271</td>
<td>5,890</td>
</tr>
<tr>
<td>68 Main Street Mannar</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Ratnapura Branch</td>
<td>3,048</td>
<td>21.01</td>
<td>12,479</td>
<td>11,062</td>
<td>23,541</td>
</tr>
<tr>
<td>21 &amp; 23 Senanayake Mawatha Ratnapura</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Ja - Ela Branch</td>
<td>4,300</td>
<td>19.00</td>
<td>2,729</td>
<td>10,016</td>
<td>12,745</td>
</tr>
<tr>
<td>73 Old Negombo Road Ja - Ela</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Matale Branch</td>
<td>7,615</td>
<td>22.08</td>
<td>3,459</td>
<td>11,814</td>
<td>15,273</td>
</tr>
<tr>
<td>660 Trincomalee Road Matale</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Kuliapitiya Branch</td>
<td>4,273</td>
<td>24.00</td>
<td>3,483</td>
<td>4,725</td>
<td>8,208</td>
</tr>
<tr>
<td>225 Main Street Kuliapitiya</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Mount Lavinia Branch</td>
<td>12,674</td>
<td>28.46</td>
<td>10,294</td>
<td>26,800</td>
<td>37,094</td>
</tr>
<tr>
<td>100 Galle Road Mount Lavinia</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Marawila Branch</td>
<td>4,640</td>
<td>23.30</td>
<td>3,916</td>
<td></td>
<td></td>
</tr>
<tr>
<td>534 Chilaw Road Marawila</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Marawila Staff Quarters</td>
<td>1,733</td>
<td>23.30</td>
<td>2,427</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Matara Branch</td>
<td>6,988</td>
<td>26.00</td>
<td>5,136</td>
<td>21,361</td>
<td>26,497</td>
</tr>
<tr>
<td>29 Anagarika Dharmapala Mw Matara</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Kegalle Property</td>
<td>Bare Land</td>
<td>48.70</td>
<td>15,600</td>
<td>-</td>
<td>15,600</td>
</tr>
<tr>
<td>Main Street Kegalle</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Kahawatte Branch</td>
<td>14,652</td>
<td>16.14</td>
<td>2,265</td>
<td>24,420</td>
<td>26,685</td>
</tr>
<tr>
<td>772A Main Street Kahawatta</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total freehold land and buildings outside Colombo City Limits</td>
<td>217,646</td>
<td>409,952</td>
<td>627,598</td>
<td>66,018</td>
<td>561,580</td>
</tr>
<tr>
<td>Total freehold land and buildings as at 31st December 2006</td>
<td>646,589</td>
<td>913,931</td>
<td>1,560,520</td>
<td>152,785</td>
<td>1,407,735</td>
</tr>
</tbody>
</table>
21. PROPERTY PLANT AND EQUIPMENT (Contd.)

### 21(c) Leasehold Buildings

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Cost of Accumulated Net Book</td>
<td>Cost of Accumulated Net Book</td>
<td>Cost of Accumulated Net Book</td>
<td>Cost of Accumulated Net Book</td>
</tr>
<tr>
<td></td>
<td>Buildings Depreciation Value</td>
<td>Buildings Depreciation Value</td>
<td>Buildings Depreciation Value</td>
<td>Buildings Depreciation Value</td>
</tr>
<tr>
<td></td>
<td>Rs.000</td>
<td>Rs.000</td>
<td>Rs.000</td>
<td>Rs.000</td>
</tr>
<tr>
<td>Up to 1 year</td>
<td>18,504</td>
<td>4,649</td>
<td>18,504</td>
<td>4,649</td>
</tr>
<tr>
<td>01 - 05 years</td>
<td>112,390</td>
<td>143,795</td>
<td>101,739</td>
<td>143,795</td>
</tr>
<tr>
<td>05 - 10 years</td>
<td>149,634</td>
<td>19,492</td>
<td>149,634</td>
<td>19,492</td>
</tr>
<tr>
<td>10 - 15 years</td>
<td>2,759</td>
<td>950</td>
<td>2,759</td>
<td>950</td>
</tr>
<tr>
<td>15 - 20 years</td>
<td>334,836</td>
<td>113,739</td>
<td>334,836</td>
<td>113,739</td>
</tr>
<tr>
<td>Above 20 years</td>
<td>661,918</td>
<td>354,463</td>
<td>661,918</td>
<td>354,463</td>
</tr>
</tbody>
</table>

### 21(d) Freehold Land and Buildings - Subsidiaries

<table>
<thead>
<tr>
<th>Buildings</th>
<th>Cost of</th>
<th>Total</th>
<th>Accumulated</th>
<th>Net Book</th>
<th>Net Book</th>
<th>Net Book</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Sq.ft.</td>
<td>Buildings Value</td>
<td>Depreciation Value</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Rs.000</td>
<td>Rs.000</td>
<td>Rs.000</td>
<td>Rs.000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Smart Building</td>
<td>42,765</td>
<td>128,115</td>
<td>22,275</td>
<td>105,840</td>
<td>109,043</td>
<td></td>
</tr>
<tr>
<td>Janadhipathi Mawatha</td>
<td>499,554</td>
<td>2,468,576</td>
<td>101,841</td>
<td>2,366,735</td>
<td>2,395,189</td>
<td></td>
</tr>
<tr>
<td>Sithma Building</td>
<td>125,765</td>
<td>2,468,576</td>
<td>101,841</td>
<td>2,366,735</td>
<td>2,395,189</td>
<td></td>
</tr>
<tr>
<td>Colombo 10</td>
<td>499,554</td>
<td>2,468,576</td>
<td>101,841</td>
<td>2,366,735</td>
<td>2,395,189</td>
<td></td>
</tr>
</tbody>
</table>

### 21(e) Fully depreciated property

The initial cost of fully depreciated Plant, Machinery and Equipment as at 31st December 2006, which are still in use as at Balance Sheet date.

<table>
<thead>
<tr>
<th>Buildings</th>
<th>Cost of Buildings</th>
<th>Total Accumulated Depreciation</th>
<th>Net Book</th>
<th>Net Book</th>
<th>Net Book</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Rs.000</td>
<td>Rs.000</td>
<td>Rs.000</td>
<td>Rs.000</td>
<td></td>
</tr>
<tr>
<td>Motor vehicles</td>
<td>73,482</td>
<td>73,482</td>
<td>22,275</td>
<td>51,207</td>
<td></td>
</tr>
<tr>
<td>Computer equipment</td>
<td>807,228</td>
<td>807,228</td>
<td>101,841</td>
<td>705,387</td>
<td></td>
</tr>
<tr>
<td>Equipment, furniture and fixtures</td>
<td>312,418</td>
<td>312,418</td>
<td>101,841</td>
<td>210,577</td>
<td></td>
</tr>
</tbody>
</table>

22. INTANGIBLE ASSETS

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Rs.000</td>
<td>Rs.000</td>
<td>Rs.000</td>
<td>Rs.000</td>
</tr>
<tr>
<td>Cost as at 1st January</td>
<td>611,422</td>
<td>611,422</td>
<td>650,935</td>
<td></td>
</tr>
<tr>
<td>Reclassified from Property, Plant and Equipment</td>
<td>-</td>
<td>427,331</td>
<td>-</td>
<td>455,838</td>
</tr>
<tr>
<td>Additions and improvements during the year</td>
<td>21,200</td>
<td>181,091</td>
<td>26,716</td>
<td>195,096</td>
</tr>
<tr>
<td>Cost as at 31st December</td>
<td>632,622</td>
<td>659,522</td>
<td>677,651</td>
<td>675,934</td>
</tr>
<tr>
<td>Accumulated amortization as at 1st January</td>
<td>300,531</td>
<td>300,531</td>
<td>311,532</td>
<td></td>
</tr>
<tr>
<td>Reclassified from Property, Plant and Equipment</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Amortization for the year</td>
<td>100,116</td>
<td>100,116</td>
<td>30,702</td>
<td>30,702</td>
</tr>
<tr>
<td>Accumulated amortization as at 31st December</td>
<td>400,647</td>
<td>400,647</td>
<td>341,932</td>
<td></td>
</tr>
<tr>
<td>Net book value as at 31st December</td>
<td>231,975</td>
<td>231,975</td>
<td>259,740</td>
<td>259,740</td>
</tr>
</tbody>
</table>

As stated in Significant Accounting Policy No.9.8.1(b), all computer software costs incurred by the Bank which are not integrally related to associated hardware have been classified as Intangible assets. The comparatives have been adjusted to reflect this reclassification.
23. OTHER ASSETS

<table>
<thead>
<tr>
<th></th>
<th>Bank</th>
<th>Group</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>2006</td>
<td>2005</td>
</tr>
<tr>
<td></td>
<td>Rs.000</td>
<td>Rs.000</td>
</tr>
<tr>
<td>Deposits and prepayments</td>
<td>2,642,806</td>
<td>2,191,046</td>
</tr>
<tr>
<td>Items in transit</td>
<td>361,617</td>
<td>1,583,030</td>
</tr>
<tr>
<td>Claims receivable</td>
<td>393,607</td>
<td>170,476</td>
</tr>
<tr>
<td>Other debtors</td>
<td>1,736,331</td>
<td>1,200,533</td>
</tr>
<tr>
<td></td>
<td>5,134,361</td>
<td>5,145,085</td>
</tr>
</tbody>
</table>

24. DEPOSITS FROM CUSTOMERS

<p>| | | |</p>
<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Bank</td>
<td>Group</td>
</tr>
<tr>
<td></td>
<td>2006</td>
<td>2005</td>
</tr>
<tr>
<td></td>
<td>Rs.000</td>
<td>Rs.000</td>
</tr>
<tr>
<td>Local Currency Deposits</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Current account deposits</td>
<td>12,635,473</td>
<td>12,511,256</td>
</tr>
<tr>
<td>Savings deposits</td>
<td>50,697,086</td>
<td>47,380,753</td>
</tr>
<tr>
<td>Time deposits</td>
<td>48,869,303</td>
<td>33,587,699</td>
</tr>
<tr>
<td>Certificates of deposit</td>
<td>3,348,716</td>
<td>3,348,716</td>
</tr>
<tr>
<td></td>
<td>115,550,578</td>
<td>97,114,101</td>
</tr>
</tbody>
</table>

<p>| | | |</p>
<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Bank</td>
<td>Group</td>
</tr>
<tr>
<td></td>
<td>2006</td>
<td>2005</td>
</tr>
<tr>
<td></td>
<td>Rs.000</td>
<td>Rs.000</td>
</tr>
<tr>
<td>Foreign Currency Deposits</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Current account deposits</td>
<td>1,188,634</td>
<td>1,013,589</td>
</tr>
<tr>
<td>Savings deposits</td>
<td>13,600,463</td>
<td>14,166,198</td>
</tr>
<tr>
<td>Time deposits</td>
<td>17,542,350</td>
<td>15,989,793</td>
</tr>
<tr>
<td></td>
<td>32,331,447</td>
<td>31,169,580</td>
</tr>
</tbody>
</table>

24 (a) Analysis of Deposits

<p>| | | |</p>
<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Bank</td>
<td>Group</td>
</tr>
<tr>
<td></td>
<td>2006</td>
<td>2005</td>
</tr>
<tr>
<td></td>
<td>Rs.000</td>
<td>Rs.000</td>
</tr>
<tr>
<td>Deposits from Non-Bank Customers</td>
<td>147,463,803</td>
<td>127,577,487</td>
</tr>
<tr>
<td>Deposits from Banks</td>
<td>24,354</td>
<td>462,778</td>
</tr>
<tr>
<td>Deposits from Finance Companies</td>
<td>393,868</td>
<td>393,868</td>
</tr>
<tr>
<td></td>
<td>147,882,025</td>
<td>128,283,681</td>
</tr>
</tbody>
</table>

25. DIVIDENDS PAYABLE

<p>| | | |</p>
<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Bank</td>
<td>Group</td>
</tr>
<tr>
<td></td>
<td>2006</td>
<td>2005</td>
</tr>
<tr>
<td></td>
<td>Rs.000</td>
<td>Rs.000</td>
</tr>
<tr>
<td>Balance as at 1st January</td>
<td>50,291</td>
<td>108,299</td>
</tr>
<tr>
<td>Dividends declared during the year</td>
<td>529,941</td>
<td>385,679</td>
</tr>
<tr>
<td>Dividends paid</td>
<td>(542,129)</td>
<td>(443,687)</td>
</tr>
<tr>
<td></td>
<td>38,103</td>
<td>50,291</td>
</tr>
</tbody>
</table>

The 25% interim dividend paid on 11th December 2006 included a re-distribution of tax exempt dividends of Rs. 16,926,771/- (2005 - Rs. 23,120,368/-) received by the Bank. Under the Inland Revenue Amendment Act No.10 of 2002, a withholding tax of 10% has been imposed on dividends declared from 1st April 2004.

Proposed final dividend

Board of Directors have recommended the payment of a final dividend of 25% for the year ended 31st December 2006 (2005 - 20%), which is to be approved at the Annual General Meeting to be held on 29th March 2007. In accordance with Sri Lanka Accounting Standard No. 12-[Revised], “Events After the Balance Sheet Date”, this proposed final dividend has not been recognised as a liability as at 31st December 2006.
26. BORROWINGS

<table>
<thead>
<tr>
<th>As at 31st December</th>
<th>Bank</th>
<th>Group</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>2006</td>
<td>2005</td>
</tr>
<tr>
<td></td>
<td>2006</td>
<td>2005</td>
</tr>
<tr>
<td>Rs.000</td>
<td>Rs.000</td>
<td>Rs.000</td>
</tr>
<tr>
<td>Call and time deposits from banks</td>
<td>4,584,620</td>
<td>510,517</td>
</tr>
<tr>
<td>Refinance borrowings</td>
<td>3,582,587</td>
<td>2,711,810</td>
</tr>
<tr>
<td>Borrowings from foreign banks</td>
<td>864,294</td>
<td>717,784</td>
</tr>
<tr>
<td>Borrowings from local banks</td>
<td>2,000,000</td>
<td>-</td>
</tr>
<tr>
<td>11,031,501</td>
<td>3,940,111</td>
<td>11,031,501</td>
</tr>
</tbody>
</table>

27. LONG TERM INSURANCE FUND

Long Term Insurance Fund balance represents the Life Fund of the Subsidiary HNB Assurance Ltd., which is carrying out life and non-life insurance business. This balance represents the amounts attributable to life policy holders included in the Group’s net assets.

The valuation of the Long Term Insurance Fund as at 31st December 2006 was made by Mr M Poopalanathan, AIA, of M/s Acturial and Management Consultants (Pvt) Ltd. for and on behalf of HNB Assurance Ltd. The life fund stands at Rs. 507.72 Mn. as at 31st December 2006 (2005 - Rs 300.82 Mn.) and in the opinion of the Actuary this amount is adequate to cover the liabilities pertaining to the long term insurance business of HNB Assurance Ltd., as per the Actuary’s Report dated 2nd February 2007.

28. NON-LIFE INSURANCE RESERVES

Non Life Insurance Reserves represents the following which are included in the financial statements of HNB Assurance Ltd., subsidiary of the Bank, as required by the Statement of Recommended Practice of Institute of Chartered Accountants of Sri Lanka (ICASL) and in accordance with the regulation of Insurance Industry Act No. 43 of 2000:

<table>
<thead>
<tr>
<th>Group</th>
<th>As at 31st December</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>2006</td>
</tr>
<tr>
<td></td>
<td>Rs.000</td>
</tr>
<tr>
<td>Unearned premium - Gross</td>
<td>327,174</td>
</tr>
<tr>
<td>- Reinsurance</td>
<td>(101,057)</td>
</tr>
<tr>
<td>- Net</td>
<td>226,117</td>
</tr>
<tr>
<td>Deferred acquisition expenses</td>
<td>(393)</td>
</tr>
<tr>
<td>Unexpired Risk Reserve</td>
<td>4,489</td>
</tr>
<tr>
<td>Total</td>
<td>230,213</td>
</tr>
<tr>
<td>Claims outstanding - Gross</td>
<td>82,207</td>
</tr>
<tr>
<td>Claims incurred but not reported - Gross</td>
<td>7,118</td>
</tr>
<tr>
<td>Claims reserve - Gross</td>
<td>93,305</td>
</tr>
<tr>
<td>Total</td>
<td>319,538</td>
</tr>
</tbody>
</table>
29. SUBORDINATED DEBENTURES

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Rs.000</td>
<td>Rs.000</td>
<td>Rs.000</td>
<td>Rs.000</td>
</tr>
<tr>
<td>Balance as at 1st January</td>
<td>4,000,000</td>
<td>4,000,000</td>
<td>5,976,791</td>
<td>5,983,450</td>
</tr>
<tr>
<td>Debentures issued</td>
<td>1,120,000</td>
<td>-</td>
<td>1,120,000</td>
<td>-</td>
</tr>
<tr>
<td>Debentures held by Group Companies</td>
<td>-</td>
<td>-</td>
<td>(13,341)</td>
<td>(6,659)</td>
</tr>
<tr>
<td>Balance as at 31st December</td>
<td>5,120,000</td>
<td>4,000,000</td>
<td>7,083,450</td>
<td>5,976,791</td>
</tr>
</tbody>
</table>

i Consists of twenty million unsecured, subordinated, redeemable debentures of Rs.100/- each. The six types of debentures have fixed or floating interest rate options as follows:

Redemption Period

<table>
<thead>
<tr>
<th></th>
<th>5 year</th>
<th>7 year</th>
<th>10 year</th>
</tr>
</thead>
<tbody>
<tr>
<td>Fixed</td>
<td>13.75%</td>
<td>14.00%</td>
<td>14.20%</td>
</tr>
<tr>
<td>Effective annual yield</td>
<td>14.22%</td>
<td>14.49%</td>
<td>14.70%</td>
</tr>
<tr>
<td>Floating</td>
<td>TB + 1%</td>
<td>TB + 1.1%</td>
<td>TB + 1.25%</td>
</tr>
</tbody>
</table>

The floating rate is based on the six month treasury bill rate with a cap of 17% p.a. and a floor of 12% p.a. Based on the duration, the debentures are redeemable on September 11th 2007, September 11th 2009 and September 11th 2012. These debentures are listed on the Colombo Stock Exchange.

ii Consists of twenty million unsecured, subordinated, redeemable debentures of Rs. 100/- each. The two types of debentures have fixed or floating interest rate options as follows:

Redemption Period

<table>
<thead>
<tr>
<th></th>
<th>5 Year</th>
</tr>
</thead>
<tbody>
<tr>
<td>Fixed</td>
<td>10.00%</td>
</tr>
<tr>
<td>Effective annual yield</td>
<td>10.25%</td>
</tr>
<tr>
<td>Floating</td>
<td>TB + 2.00%</td>
</tr>
</tbody>
</table>

The debentures are redeemable on July 23rd 2008 and are listed on the Colombo Stock Exchange.

iii Consists of eleven million two hundred thousand unsecured, subordinated, redeemable debentures of Rs.100/- each. The five types of debentures have fixed or floating interest rate options as follows:

Redemption Period

<table>
<thead>
<tr>
<th></th>
<th>6 Year</th>
<th>7 Year</th>
<th>8 Year</th>
<th>15 Year</th>
<th>18 Year</th>
</tr>
</thead>
<tbody>
<tr>
<td>Fixed</td>
<td></td>
<td>11%</td>
<td>11%</td>
<td>11.25%</td>
<td>11.25%</td>
</tr>
<tr>
<td>Effective annual yield</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Floating</td>
<td>TB + 2.25%</td>
<td>TB + 2.25%</td>
<td>TB + 2.25%</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

The floating rate is based on the six month treasury bill rate with a cap of 16% p.a. and a floor of 8 % p.a. Based on the duration, the debentures are redeemable on 31st March 2012, 31st March 2013, 31st March 2014, 31st March 2021 and 31st March 2024. These debentures are not listed on the Colombo Stock Exchange as at 31.12.2006.
### 30. DEFERRED TAX LIABILITY

#### As at 31st December

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Deferred tax liability [Note 30(a)]</td>
<td>618,828</td>
<td>313,756</td>
<td>622,747</td>
<td>316,317</td>
</tr>
<tr>
<td>Deferred tax asset [Note 30(b)]</td>
<td>(305,072)</td>
<td>-</td>
<td>(305,072)</td>
<td>-</td>
</tr>
<tr>
<td></td>
<td>313,756</td>
<td>313,756</td>
<td>317,675</td>
<td>316,317</td>
</tr>
</tbody>
</table>

#### 30(a) Deferred Tax liability

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Temporary Tax Difference</td>
<td>Rs.000</td>
<td>1,045,853</td>
<td>313,756</td>
<td>1,167,854</td>
<td>313,756</td>
<td></td>
</tr>
<tr>
<td>Tax Effect</td>
<td>Rs.000</td>
<td>1,167,854</td>
<td>350,356</td>
<td>1,054,390</td>
<td>316,317</td>
<td></td>
</tr>
<tr>
<td>Temporary Tax Difference</td>
<td>Rs.000</td>
<td>1,054,390</td>
<td>316,317</td>
<td>1,175,097</td>
<td>352,529</td>
<td></td>
</tr>
<tr>
<td>Tax Effect</td>
<td>Rs.000</td>
<td>316,317</td>
<td>316,317</td>
<td>352,529</td>
<td>352,529</td>
<td></td>
</tr>
<tr>
<td>Originating/(Reversal) during the year</td>
<td>(21,569)</td>
<td>(7,549)</td>
<td>(122,000)</td>
<td>(36,600)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Impact on rate increase</td>
<td>255,663</td>
<td>89,482</td>
<td>255,663</td>
<td>89,482</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Opening balance adjustment as per transitional provision</td>
<td>637,540</td>
<td>223,139</td>
<td>637,540</td>
<td>223,139</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>618,828</td>
<td>313,756</td>
<td>622,747</td>
<td>316,317</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

#### 30(b) Deferred Tax asset

<table>
<thead>
<tr>
<th></th>
<th>Bank</th>
<th>2006</th>
<th>Group</th>
<th>2006</th>
</tr>
</thead>
<tbody>
<tr>
<td>Temporary Tax Difference</td>
<td>Rs.000</td>
<td>871,634</td>
<td>305,072</td>
<td>871,634</td>
</tr>
<tr>
<td>Tax Effect</td>
<td>Rs.000</td>
<td>305,072</td>
<td>305,072</td>
<td></td>
</tr>
<tr>
<td>Opening balance adjustment as per transitional provision</td>
<td>871,634</td>
<td>305,072</td>
<td>871,634</td>
<td></td>
</tr>
<tr>
<td></td>
<td>871,634</td>
<td>305,072</td>
<td>871,634</td>
<td></td>
</tr>
</tbody>
</table>

#### 30 (c) Application of transitional provision

As per the transitional provision in Sri Lanka Accounting Standard 14 - "Income Taxes", (SLAS 14) the Bank has made an irrevocable choice to recognise the opening balance increase on a straight line basis over two years from 1st January 2006, the date of adoption of this standard.

i) The amount recognised in the current year

<table>
<thead>
<tr>
<th></th>
<th>Bank</th>
<th>2006</th>
<th>Group</th>
<th>2006</th>
</tr>
</thead>
<tbody>
<tr>
<td>Deferred tax asset</td>
<td>305,072</td>
<td>305,072</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Deferred tax liability</td>
<td>(223,139)</td>
<td>(223,139)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Income tax expense [Note 8(b)]</td>
<td>81,933</td>
<td>81,933</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

ii) The net amount of increase to be recognised next year

<table>
<thead>
<tr>
<th></th>
<th>Bank</th>
<th>2006</th>
<th>Group</th>
<th>2006</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>81,933</td>
<td>81,933</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

#### 30 (d) Unrecognised Deferred Tax asset

A deferred tax asset of Rs.527 Mn. arising from the balance carry forward unutilised tax losses of Rs. 1,505 Mn. has not been recognized as at 31st December 2006.

Recognition of the total unutilised tax losses would result in an additional credit of Rs. 527 Mn., to the Income Statement, which will cause wide fluctuation in the Income Statement this year being the year of adoption of SLAS 14 as these tax losses will be fully utilised in the immediate future.
31. OTHER LIABILITIES

<table>
<thead>
<tr>
<th></th>
<th>Bank</th>
<th>Group</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>2006</td>
<td>2005</td>
</tr>
<tr>
<td></td>
<td>Rs.000</td>
<td>Rs.000</td>
</tr>
<tr>
<td>Cheques sent on clearing</td>
<td>1,216,711</td>
<td>2,395,504</td>
</tr>
<tr>
<td>Accrued expenditure and interest</td>
<td>5,059,193</td>
<td>3,389,960</td>
</tr>
<tr>
<td>Claims payable</td>
<td>175,939</td>
<td>175,939</td>
</tr>
<tr>
<td>Margins</td>
<td>1,463,057</td>
<td>1,463,057</td>
</tr>
<tr>
<td>Pension fund</td>
<td>1,235,693</td>
<td>1,235,873</td>
</tr>
<tr>
<td>Widows’/widowers’ &amp; orphans’ pension fund</td>
<td>228,862</td>
<td>228,862</td>
</tr>
<tr>
<td>Employees provident fund</td>
<td>106,904</td>
<td>106,904</td>
</tr>
<tr>
<td>Other creditors</td>
<td>938,977</td>
<td>1,453,536</td>
</tr>
<tr>
<td></td>
<td>10,425,336</td>
<td>10,940,075</td>
</tr>
</tbody>
</table>

32. SHARE CAPITAL - BANK AND GROUP

<table>
<thead>
<tr>
<th></th>
<th>Bank</th>
<th>Group</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>2006</td>
<td>2005</td>
</tr>
<tr>
<td></td>
<td>Rs.000</td>
<td>Rs.000</td>
</tr>
<tr>
<td>AUTHoruISED</td>
<td>1 Billion ordinary shares of Rs.10/- each</td>
<td>10,000,000</td>
</tr>
</tbody>
</table>

33. COMMITMENTS AND CONTINGENCIES - BANK AND GROUP

In the normal course of business, the Bank makes various commitments and incurs certain contingent liabilities with legal recourse to its customers and would be party to litigation due to its operations. No material losses are anticipated as a result of these transactions.

33(a) Capital commitments

Capital expenditure approved by the Board of Directors for which provision has not been made in the accounts amount to approximately Rs. 225.5 Mn.

<table>
<thead>
<tr>
<th></th>
<th>Bank</th>
<th>Group</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>2006</td>
<td>2005</td>
</tr>
<tr>
<td></td>
<td>Rs.000</td>
<td>Rs.000</td>
</tr>
<tr>
<td>Approved and contracted for</td>
<td>225,527</td>
<td>19,957</td>
</tr>
<tr>
<td></td>
<td>225,527</td>
<td>19,957</td>
</tr>
</tbody>
</table>
33. COMMITMENTS AND CONTINGENCIES - GROUP AND BANK (Contd.)

33(b) Future monthly commitments on operating leases - Bank

<table>
<thead>
<tr>
<th></th>
<th>2006</th>
<th>2005</th>
</tr>
</thead>
<tbody>
<tr>
<td>As at 31st December</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Rs.000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>1 - 5 years</td>
<td>6,971</td>
<td>3,294</td>
</tr>
<tr>
<td>6 - 10 years</td>
<td>1,578</td>
<td>3,510</td>
</tr>
<tr>
<td>11 - 15 years</td>
<td>859</td>
<td>705</td>
</tr>
<tr>
<td>16 - 20 years</td>
<td>-</td>
<td>200</td>
</tr>
<tr>
<td></td>
<td>9,408</td>
<td>7,709</td>
</tr>
</tbody>
</table>

33(c) Irrevocable commitments - Bank

Commitments as at Balance Sheet date that cannot be revoked at the discretion of the Bank without the risk of incurring significant penalty or expense amounted to Rs. 23,894 Mn. (2005 - Rs. 21,016 Mn)

33(d) Contingent liabilities

<table>
<thead>
<tr>
<th></th>
<th>2006</th>
<th>2005</th>
</tr>
</thead>
<tbody>
<tr>
<td>Acceptances</td>
<td>3,626,830</td>
<td>3,983,731</td>
</tr>
<tr>
<td>Documentary credits</td>
<td>7,408,853</td>
<td>6,306,610</td>
</tr>
<tr>
<td>Guarantees</td>
<td>16,485,243</td>
<td>16,710,250</td>
</tr>
<tr>
<td>Bills for collection</td>
<td>7,198,400</td>
<td>6,147,266</td>
</tr>
<tr>
<td>Interest rate swap</td>
<td>499</td>
<td>1,761</td>
</tr>
<tr>
<td>Forward Exchange Contracts</td>
<td>10,065,139</td>
<td>13,613,590</td>
</tr>
<tr>
<td>Total Contingencies Group and Bank</td>
<td>44,784,964</td>
<td>44,763,208</td>
</tr>
</tbody>
</table>

33(e) Litigation against the Bank

(i) Three claims for damages made by customers in Cases Nos. 9030/M, 9272/M and 1773/M in the DCs in respect of cheques dishonoured.

(ii) HC (Civil) Case No. 132/2001 [i] a depositor’s claim for damages against Habib Bank AG Zurich Sri Lanka Branch (HBZ) for setting-off a customer liability with a deposit - the Bank substituted with acquisition of HBZ business.


Based on the available information and current status of the above cases, the Bank is not in a position to quantify the potential financial impact if any, as at the Balance Sheet date. Further, the Bank confirms that there is no case which is not disclosed above which would have a material impact on the financial position of the Bank.

33(f) Tax assessments against the Bank

(i) VAT on financial services for 2003 and 2004, amounting to Rs. 247 Mn. on Assessment Nos. VATFS/06/0312/06, VATFS/U6/0401/01, VATFS/J6/0402/02, VATFS/U6/0403/03, VATFS/U6/0404/04 and VATFS/U6/0405/05 against which, the Bank has appealed to the Board of Review.

(ii) VAT for the year 2003, taxes amounting to Rs. 323.8 Mn. on Assessment Nos. 8290566, 8290567, 8290568, 8290569, 8290570, 8290571, 8290572, 8290573, 8290574, 8290575, 8290576 and 8290577 against which, the Bank has duly appealed.

(iii) VAT for the year 2004, taxes amounting to Rs. 74.4 Mn. on Assessment Nos. 8325523, 8325524, 8325525, 8325526, 8325527, 8325528, 8325533 and 8325534 have been received on 02.02.07.

The Bank is of the view that the above assessments will not have any material impact on the financial statements.
### 34. DIRECTORS’ INTEREST IN CONTRACTS WITH THE BANK

#### 34(a) Trading transactions

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Brown &amp; Co. Ltd.</td>
<td>Mr M V Theagarajah [Chairman till 30.06.2006]</td>
<td>30.585</td>
<td>13.795</td>
<td>Payment for purchase of plant, equipment, repairs to assets and service agreements.</td>
</tr>
<tr>
<td></td>
<td></td>
<td>8.000</td>
<td>26.250</td>
<td>Payment for purchase of generators and generator service agreements.</td>
</tr>
<tr>
<td></td>
<td></td>
<td>0.018</td>
<td>0.042</td>
<td>Two premises were vacated in June 2005 and the last one was vacated in November 2006.</td>
</tr>
<tr>
<td>Madulsima Plantations Ltd.</td>
<td>Dr V P Vittachi [Chairman] Mr D H S Jayawardena [Managing Director] Mr R K Obeyesekere [Director]</td>
<td>0.900</td>
<td>0.720</td>
<td>Payment for lease of holiday bungalow at Bogawantalawa.</td>
</tr>
<tr>
<td>Lanka Bell (Pvt) Ltd. [from June 2005]</td>
<td>Mr D H S Jayawardena [Chairman]</td>
<td>10.000</td>
<td>1.360</td>
<td>Payment for voice communication charges.</td>
</tr>
<tr>
<td></td>
<td></td>
<td>5.000</td>
<td>1.811</td>
<td>Payment for data communication charges.</td>
</tr>
<tr>
<td></td>
<td></td>
<td>7.893</td>
<td>1.163</td>
<td>Telephone charges paid.</td>
</tr>
<tr>
<td>Sri Lanka Insurance Corporation Ltd.</td>
<td>Mr D H S Jayawardena [Chairman] Mr R K Obeyesekere [Deputy Chairman]</td>
<td>56.004</td>
<td>49.052</td>
<td>Insurance premiums paid, inclusive of taxes.</td>
</tr>
<tr>
<td>Stassen Exports Ltd.</td>
<td>Dr V P Vittachi [Chairman] Mr D H S Jayawardena [Managing Director] Mr R K Obeyesekere [Director]</td>
<td>-</td>
<td>0.906</td>
<td>Payment for purchase of promotional material.</td>
</tr>
<tr>
<td>Aitken Spence Printing [Pvt] Ltd.</td>
<td>Subsidiary of Aitken Spence Co. Ltd.</td>
<td>15.986</td>
<td>2.714</td>
<td>Printing charges</td>
</tr>
</tbody>
</table>

The details of the lending transactions with companies in which there is an interest by Directors of the Bank are disclosed in Note No. 35 “Related Party Transactions”.

---

Annual Report 2006
34. DIRECTORS’ INTEREST IN CONTRACTS WITH THE BANK (Contd.)

34(b) Credit Card facilities to Directors

<table>
<thead>
<tr>
<th>Name of Director</th>
<th>Limit as at 31.12.06</th>
<th>Outstanding as at 31.12.06</th>
</tr>
</thead>
<tbody>
<tr>
<td>Mr R T Wijetilleke (Chairman)</td>
<td>0.500</td>
<td>0.330</td>
</tr>
<tr>
<td>Dr V P Vittachi (Deputy Chairman)</td>
<td>0.500</td>
<td>0.040</td>
</tr>
<tr>
<td>Mr D H S Jayawardeniya*</td>
<td>12.500</td>
<td>2.310</td>
</tr>
<tr>
<td>Mr M V Theagarajah</td>
<td>0.500</td>
<td>0.007</td>
</tr>
<tr>
<td>Mr R K Obeyesekere</td>
<td>0.500</td>
<td>0.050</td>
</tr>
<tr>
<td>Mrs P Cooray</td>
<td>0.500</td>
<td>0.002</td>
</tr>
<tr>
<td>Mr R Sivaratnam*</td>
<td>1.240</td>
<td>0.180</td>
</tr>
<tr>
<td>Mr R Theagarajah</td>
<td>0.400</td>
<td>0.002</td>
</tr>
</tbody>
</table>

* Rs. 0.5 Mn clean and the balance is secured by cash deposits.

34(c) Accommodation granted to Directors

<table>
<thead>
<tr>
<th>Name of Director</th>
<th>Aggregate amount of accommodation</th>
<th>Security</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Limit as at 31.12.06</td>
<td>Outstanding as at 31.12.06</td>
</tr>
<tr>
<td>------------------</td>
<td>----------------------</td>
<td>-----------------------------</td>
</tr>
<tr>
<td>Mr R T Wijetilleke</td>
<td>0.72</td>
<td>0.67</td>
</tr>
<tr>
<td>Mr M V Theagarajah</td>
<td>4.60</td>
<td>-</td>
</tr>
<tr>
<td>Mr R Sivaratnam</td>
<td>1.50</td>
<td>0.24</td>
</tr>
<tr>
<td>Mr R Theagarajah</td>
<td>*5.00</td>
<td>0.80</td>
</tr>
</tbody>
</table>

* Original amount of loan granted at staff rate.
All facilities outstanding in the names of the Directors are performing.

35. RELATED PARTY TRANSACTIONS

The Bank carries out transactions in the ordinary course of its business with parties who are defined as related parties in Sri Lanka Accounting Standard 30 “Related Party Disclosures (revised 2005)”, the details of which are reported below. The pricing applicable to such transactions is based on the assessment of risk and the pricing model of the Bank and is comparable with what is applied to transactions between the Bank and its unrelated customers.

35 (a) Transactions with/between Subsidiaries

35(a) Sithma Development (Pvt) Ltd.

Sithma Development (Pvt) Ltd. ("Sithma"), is a wholly owned subsidiary of Hatton National Bank Ltd. [HNBL].

The details of the overdraft facility with HNB are as follows:

<table>
<thead>
<tr>
<th>Type of Facility</th>
<th>Rate of Interest</th>
<th>Limit Rs. Mn.</th>
<th>Outstanding as at 31/12/06 Rs.000</th>
<th>Security</th>
<th>Review</th>
</tr>
</thead>
<tbody>
<tr>
<td>Overdraft</td>
<td>2% above the one year *WATB. to be reviewed every 6 months.</td>
<td>800</td>
<td>414,787</td>
<td>Registered primary floating mortgage for Rs. 1,800 Mn. over land and building at No. 479, T B Jayah Mw., Colombo 10.</td>
<td>May-07</td>
</tr>
</tbody>
</table>

*WATB - Weighted Average Treasury Bill Rate
35. RELATED PARTY TRANSACTIONS (Contd.)

35(a) Transactions with/between Subsidiaries (Contd.)

35(ai) Sithma Development (Pvt) Ltd. (Contd.)

A summary of transactions of Sithma with HNB and other group companies are given below:

<table>
<thead>
<tr>
<th></th>
<th>HNB SECURITIES</th>
<th>HNB STOCKBROKERS</th>
<th>HNB ASSURANCE</th>
<th>HNB</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Rs.000</td>
<td>Rs.000</td>
<td>Rs.000</td>
<td>Rs.000</td>
</tr>
<tr>
<td>Rent income received</td>
<td>5,898</td>
<td>6,622</td>
<td>-</td>
<td>428,062</td>
</tr>
<tr>
<td>Rent advance received</td>
<td>1,498</td>
<td>1,778</td>
<td>-</td>
<td>108,952</td>
</tr>
<tr>
<td>Refundable deposit</td>
<td>3,000</td>
<td>3,000</td>
<td>-</td>
<td>500,000</td>
</tr>
<tr>
<td>Insurance premium paid</td>
<td>-</td>
<td>-</td>
<td>3,720</td>
<td>-</td>
</tr>
<tr>
<td>Interest paid</td>
<td>-</td>
<td>-</td>
<td>57,360</td>
<td>-</td>
</tr>
<tr>
<td>Ground rent paid</td>
<td>-</td>
<td>-</td>
<td>3,752</td>
<td>-</td>
</tr>
</tbody>
</table>

35(aii) HNB Securities Ltd.

HNB Securities Ltd. (“Securities”), is a fully owned subsidiary of Hatton National Bank Ltd.

Securities maintains a current account with HNB and the balance as at 31.12.2006 amounts to Rs. 4.6 Mn. (2005 - Rs. 23.02 Mn.).

A summary of transactions of Securities with HNB and other group companies are given below:

<table>
<thead>
<tr>
<th></th>
<th>SITHMA</th>
<th>HNB STOCKBROKERS</th>
<th>HNB ASSURANCE</th>
<th>HNB</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Rs.000</td>
<td>Rs.000</td>
<td>Rs.000</td>
<td>Rs.000</td>
</tr>
<tr>
<td>Interest received</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>14,342</td>
</tr>
<tr>
<td>Insurance premium paid</td>
<td>-</td>
<td>-</td>
<td>103</td>
<td>-</td>
</tr>
<tr>
<td>Interest paid</td>
<td>-</td>
<td>-</td>
<td>17,400</td>
<td>19,947</td>
</tr>
<tr>
<td>Rent paid</td>
<td>5,898</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Rent advance paid</td>
<td>1,498</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Refundable deposit</td>
<td>3,000</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
</tbody>
</table>

35(aiii) HNB Assurance Ltd.

HNB Assurance Ltd. (“Assurance”), is a subsidiary of Hatton National Bank Ltd.

Assurance held deposits with the Bank amounting to Rs. 63 Mn. (2005 - Rs. 43.7 Mn.) as at 31.12.2006. Further company held debentures of the Bank amounting to Rs. 36.6 Mn. (2005 - Rs.16.6 Mn.)

A summary of transactions of Assurance with HNB and other group companies are given below:

<table>
<thead>
<tr>
<th></th>
<th>SITHMA</th>
<th>HNB STOCKBROKERS</th>
<th>HNB SECURITIES</th>
<th>HNB</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Rs.000</td>
<td>Rs.000</td>
<td>Rs.000</td>
<td>Rs.000</td>
</tr>
<tr>
<td>Premium received</td>
<td>3,720</td>
<td>364</td>
<td>103</td>
<td>14,572</td>
</tr>
<tr>
<td>Interest received</td>
<td>-</td>
<td>-</td>
<td>17,400</td>
<td>5,194</td>
</tr>
<tr>
<td>Rent paid</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>13,415</td>
</tr>
<tr>
<td>Commission paid</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>37,462</td>
</tr>
<tr>
<td>Dividend paid</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>7,500</td>
</tr>
</tbody>
</table>
35. RELATED PARTY TRANSACTIONS (Contd.)

35 (a) Transactions with/between Subsidiaries (Contd.)

35(a)iv HNB Stockbrokers (Pvt) Ltd.

HNB Stockbrokers (Pvt) Ltd. ("Stockbrokers"), is a wholly owned subsidiary of Hatton National Bank Ltd.

Stockbrokers held deposits with the Bank and the balance as at 31.12.2006 amounts to Rs. 18.7 Mn. (2005 - Rs 78.9 Mn.)

A summary of transactions of Stockbrokers with HNB and other group of companies are given below:

<table>
<thead>
<tr>
<th>SITHMA</th>
<th>HNB</th>
<th>HNB</th>
<th>HNB</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Assuranc</td>
<td>Securities</td>
<td></td>
</tr>
<tr>
<td>Rs. 000</td>
<td>Rs. 000</td>
<td>Rs. 000</td>
<td>Rs. 000</td>
</tr>
<tr>
<td>Interest received</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Insurance premium paid</td>
<td>-</td>
<td>364</td>
<td>-</td>
</tr>
<tr>
<td>Interest paid</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Rent paid</td>
<td>6,622</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Rent advance paid (as at 31.12.2006)</td>
<td>1,778</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Refundable deposit paid</td>
<td>3,000</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Commission paid</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
</tbody>
</table>

Mr R T Wijetilleke, who is the Chairman of the Bank is also the Chairman of the above four subsidiary companies.

Mr R Theagarajah, a Director of the Bank, is also a Director of the four subsidiary companies mentioned above.

Mr Yeo Took Keat alternate to Mr D R Ghazalli, Director of the Bank is also a Director of HNB Assurance Ltd.

35(b) Transactions with Associates

Lanka Ventures Ltd.

Lanka Ventures Ltd. has invested Rs. 23.5 Mn. in quoted debentures of HNB and has term deposits of Rs. 60 Mn. placed with the Bank as at 31st December 2006, in respect of which interest amounting to Rs. 6.813 Mn. has been paid by the Bank for the financial year 2006.

35(c) Transactions with Key Management Personnel of the Bank

Key Management Personnel (Board of Directors) and their close family members’ transactions with the Bank/Group during the year are disclosed under Note No. 34(b) and 34(c).

35(d) Compensation of Key Management Personnel

Compensation paid to Key Management personnel of the Bank/Group is disclosed in under Note No 6(a).
### 35. RELATED PARTY TRANSACTIONS (Contd.)

#### 35 (e) Transactions with other related parties

<table>
<thead>
<tr>
<th>Name of Related Party</th>
<th>Name of Director (Relationship)</th>
<th>Nature of Transaction</th>
<th>Aggregate Amount of Security Limit (Rs. Mn.) Outstanding as at 31.12.06 (Rs. Mn.)</th>
<th>Security</th>
</tr>
</thead>
<tbody>
<tr>
<td>Stassen Exports Ltd.</td>
<td>Dr V P Vittachi</td>
<td>Overdraft I</td>
<td>753.00</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Chairman</td>
<td>Overdraft II</td>
<td>60.00 1,142.06</td>
<td>Cash Deposits</td>
</tr>
<tr>
<td></td>
<td>Mr D H S Jayawardena</td>
<td>Temporary Overdraft</td>
<td>400.00</td>
<td>Quoted Co. Shares</td>
</tr>
<tr>
<td></td>
<td>Managing Director</td>
<td>Letters of Guarantee</td>
<td>60.00 - 58.44</td>
<td>Inventories</td>
</tr>
<tr>
<td></td>
<td>Mr R K Obeyesekere</td>
<td>Letters of Credit</td>
<td>15.00 - 10.13</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Director</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>1,288.00 1,142.06 68.57</td>
<td></td>
</tr>
<tr>
<td>Stassen International Ltd</td>
<td>Dr V P Vittachi</td>
<td>Letters of Credit</td>
<td>70.00 - 51.90</td>
<td></td>
</tr>
<tr>
<td>Ltd</td>
<td>Chairman</td>
<td>Overdraft</td>
<td>20.00 5.19</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Mr D H S Jayawardena</td>
<td>Temp. Letters of Credit</td>
<td>- - 3.23</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Managing Director</td>
<td>Letters of Guarantee</td>
<td>125.00 - 101.89</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Mr R K Obeyesekere</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Director</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>215.00 5.19 153.79</td>
<td></td>
</tr>
<tr>
<td>Milford Exports (Cey) Ltd</td>
<td>Dr V P Vittachi</td>
<td>Letters of Credit</td>
<td>2.00 - 0.21</td>
<td></td>
</tr>
<tr>
<td>Ltd</td>
<td>Chairman</td>
<td>Overdraft</td>
<td>0.50 - -</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Mr D H S Jayawardena</td>
<td>Letters of Guarantee</td>
<td>30.00 - 31.20</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Managing Director</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Mr R K Obeyesekere</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Director</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>32.50 - 31.41</td>
<td></td>
</tr>
<tr>
<td>Madulsima Plantations Ltd</td>
<td>Dr V P Vittachi</td>
<td>Overdraft</td>
<td>175.20 134.63 -</td>
<td></td>
</tr>
<tr>
<td>Ltd</td>
<td>Chairman</td>
<td>Loan</td>
<td>4.76 4.76</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Mr D H S Jayawardena</td>
<td>Letters of Guarantee</td>
<td>1.00 - 0.15</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Managing Director</td>
<td>Temp. Letters of Credit</td>
<td>- - 3.23</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Mr R K Obeyesekere</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Director</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>180.96 139.39 3.38</td>
<td></td>
</tr>
<tr>
<td>Stassen Natural Food (Pvt) Ltd</td>
<td>Dr V P Vittachi</td>
<td>Letters of Guarantee</td>
<td>15.00 - 15.00</td>
<td></td>
</tr>
<tr>
<td>Ltd</td>
<td>Chairman</td>
<td>Letters of Credit</td>
<td>6.00 - 1.94</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Mr D H S Jayawardena</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Managing Director</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Mr R K Obeyesekere</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Director</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>21.00 - 16.94</td>
<td></td>
</tr>
<tr>
<td>CBD Exports Ltd</td>
<td>Dr V P Vittachi</td>
<td>Letters of Guarantee</td>
<td>10.00 - -</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Chairman</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Mr R K Obeyesekere</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Managing Director</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>10.00 - -</td>
<td></td>
</tr>
<tr>
<td>Browns Beach Hotels Ltd</td>
<td>Dr V P Vittachi</td>
<td>Temp. Letters of Credit</td>
<td>- - 2.39</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Chairman</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Mr D H S Jayawardena</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Director</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>- - 2.39</td>
<td></td>
</tr>
</tbody>
</table>
### 35. RELATED PARTY TRANSACTIONS (Contd.)

#### 35 (e) Transactions with other related parties (Contd.)

<table>
<thead>
<tr>
<th>Name of Related Party</th>
<th>Name of Director [Relationship]</th>
<th>Nature of Transaction</th>
<th>Aggregate Amount of Security</th>
<th>Outstanding as at 31.12.06 (Rs. Mn.)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>Direct (Rs. Mn.)</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>Indirect (Rs. Mn.)</td>
</tr>
<tr>
<td>Sri Lanka Insurance Corporation</td>
<td>Mr D H S Jayawardena Chairman</td>
<td>Letters of Guarantee</td>
<td>0.77</td>
<td>-</td>
</tr>
<tr>
<td></td>
<td>Mr R K Obeyesekere Deputy Chairman</td>
<td>Letters of Credit</td>
<td>4.00</td>
<td>-</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>-</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>4.77</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>-</td>
</tr>
<tr>
<td>Lanka Milk Foods (CWE) Ltd</td>
<td>Dr V P Vittachi Chairman</td>
<td>Letters of Credit</td>
<td>400.00</td>
<td>-</td>
</tr>
<tr>
<td></td>
<td>Mr D H S Jayawardena Managing Director</td>
<td>Letters of Guarantee</td>
<td>20.00</td>
<td>-</td>
</tr>
<tr>
<td></td>
<td>Mr R K Obeyesekere Director</td>
<td>Overdraft</td>
<td>200.00</td>
<td>173.78</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>-</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>620.00</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>173.78</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>261.44</td>
</tr>
<tr>
<td>Lanka Dairies (Pvt) Ltd</td>
<td>Dr V P Vittachi Chairman</td>
<td>Overdraft</td>
<td>30.00</td>
<td>21.31</td>
</tr>
<tr>
<td></td>
<td>Mr D H S Jayawardena Managing Director</td>
<td>Letters of Credit</td>
<td>10.00</td>
<td>-</td>
</tr>
<tr>
<td></td>
<td>Mr R K Obeyesekere Director</td>
<td></td>
<td></td>
<td>-</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>-</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>40.00</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>21.31</td>
</tr>
<tr>
<td>Ambewela Products (Pvt) Ltd</td>
<td>Mr D H S Jayawardena Managing Director</td>
<td>Overdraft</td>
<td>10.00</td>
<td>10.04</td>
</tr>
<tr>
<td></td>
<td>Mr R K Obeyesekere Director</td>
<td>Letters of Credit</td>
<td>50.00</td>
<td>-</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>-</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>60.00</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>10.04</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>14.49</td>
</tr>
<tr>
<td>Ambewela Livestock Co. Ltd</td>
<td>Dr V P Vittachi Chairman</td>
<td>Overdraft</td>
<td>50.00</td>
<td>42.75</td>
</tr>
<tr>
<td></td>
<td>Mr D H S Jayawardena Managing Director</td>
<td>Letters of Credit</td>
<td>10.00</td>
<td>-</td>
</tr>
<tr>
<td></td>
<td>Mr R K Obeyesekere Director</td>
<td></td>
<td></td>
<td>-</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>60.00</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>42.75</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>2.59</td>
</tr>
<tr>
<td>Pattipola Livestock Co. Ltd</td>
<td>Dr V P Vittachi Chairman</td>
<td>Overdraft</td>
<td>50.00</td>
<td>33.87</td>
</tr>
<tr>
<td></td>
<td>Mr D H S Jayawardena Managing Director</td>
<td>Letters of Credit</td>
<td>10.00</td>
<td>-</td>
</tr>
<tr>
<td></td>
<td>Mr R K Obeyesekere Director</td>
<td></td>
<td></td>
<td>-</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>60.00</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>33.87</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>-</td>
</tr>
<tr>
<td>Distilleries Company of Sri Lanka Ltd</td>
<td>Dr V P Vittachi Chairman</td>
<td>Letters of Credit</td>
<td>6.31</td>
<td>-</td>
</tr>
<tr>
<td></td>
<td>Mr D H S Jayawardena Managing Director</td>
<td>Letters of Guarantee</td>
<td>2.87</td>
<td>-</td>
</tr>
<tr>
<td></td>
<td>Mr R K Obeyesekere Director</td>
<td></td>
<td></td>
<td>-</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>9.18</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>-</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>98.88</td>
</tr>
</tbody>
</table>
### 35. RELATED PARTY TRANSACTIONS (Contd.)

#### 35 (e) Transactions with other related parties (Contd.)

<table>
<thead>
<tr>
<th>Name of Related Party</th>
<th>Name of Director (Relationship)</th>
<th>Nature of Transaction</th>
<th>Aggregate Amount of Accommodation Limit [Rs. Mn.]</th>
<th>Outstanding as at 31.12.06 [Rs. Mn.]</th>
<th>Security</th>
</tr>
</thead>
<tbody>
<tr>
<td>Periceyl (Pvt) Ltd</td>
<td>Mr D H S Jayawardena Chairman</td>
<td>Letter of Guarantee</td>
<td>1.00</td>
<td>-</td>
<td>1.00</td>
</tr>
<tr>
<td></td>
<td>Mr R K Obeyesekere Director</td>
<td></td>
<td></td>
<td></td>
<td>Cash Deposits</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>1.00</td>
<td>-</td>
<td>1.00</td>
</tr>
<tr>
<td>Lanka Hospitals Ltd</td>
<td>Mr D H S Jayawardena Director</td>
<td>Letter of Credit</td>
<td>80.00</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Import Loan (80.00)</td>
<td>80.00</td>
<td></td>
<td>Mortgage over movable assets</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Overdraft</td>
<td>220.00</td>
<td>178.37</td>
<td>-</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Syndicate Loan</td>
<td>200.00</td>
<td>138.54</td>
<td>-</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>500.00</td>
<td>396.91</td>
<td>-</td>
</tr>
<tr>
<td>Balangoda Plantations Ltd</td>
<td>Dr V P Vittachi Chairman</td>
<td>Letters of Guarantee</td>
<td>0.03</td>
<td>-</td>
<td>0.03</td>
</tr>
<tr>
<td></td>
<td>Mr D H S Jayawardena Managing Director</td>
<td>Overdraft</td>
<td>45.00</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td></td>
<td>Mr R K Obeyesekere Director</td>
<td>Development Loan</td>
<td>13.06</td>
<td>13.06</td>
<td>Cash Deposits</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>58.09</td>
<td>13.06</td>
<td>0.02</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Texprow Industries Ltd</td>
<td>Mr D H S Jayawardena Chairman</td>
<td>Letters of Credit</td>
<td>1.60</td>
<td>-</td>
<td>0.90</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Export Loans (1.60)</td>
<td>0.24</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Term Loan</td>
<td>0.50</td>
<td>0.50</td>
<td>-</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Term Loan</td>
<td>0.36</td>
<td>0.36</td>
<td>Property / Machinery</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Term Loan</td>
<td>0.11</td>
<td>0.11</td>
<td>-</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Term Loan</td>
<td>0.15</td>
<td>0.15</td>
<td>Cash deposits</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Overdraft</td>
<td>0.05</td>
<td>0.05</td>
<td>Inventories</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Overdraft (Rs. Mn)</td>
<td>7.20 (Rs. Mn) 6.69</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Letters of Guarantee</td>
<td>-</td>
<td>-</td>
<td>[Rs. Mn] 0.22</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>(US$. Mn) 2.77</td>
<td>1.41</td>
<td>0.90</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>(Rs. Mn) 7.20</td>
<td>6.69</td>
<td>0.22</td>
</tr>
</tbody>
</table>
### 35. RELATED PARTY TRANSACTIONS (Contd.)

#### 35 (e) Transactions with other related parties (Contd.)

<table>
<thead>
<tr>
<th>Name of Related Party</th>
<th>Name of Director (Relationship)</th>
<th>Nature of Transaction</th>
<th>Aggregate Amount of Security</th>
</tr>
</thead>
<tbody>
<tr>
<td>Falcon Commodities (Pvt) Ltd</td>
<td>Mr D H S Jayawardena</td>
<td>Overdraft/Import Bills</td>
<td>Limit</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Outstanding as at 31.12.06</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>(Rs. Mn.)</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Direct</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Indirect</td>
</tr>
<tr>
<td></td>
<td>Through the shareholding of</td>
<td>Overdraft Import</td>
<td>84.85</td>
</tr>
<tr>
<td></td>
<td>Stassen Exports Ltd, in Falcon</td>
<td>Cancelled</td>
<td>228.36</td>
</tr>
<tr>
<td></td>
<td>Commodities (Pvt) Ltd (Since</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>disposed)</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Cash Deposits</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Inventories</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Accommodation</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>granted to Falcon</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Commodities (Pvt) Ltd continues to be classified as non-performing.</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>The outstanding of Rs. 326.0 Mn as at 31.12.2006 is fully covered by the capital provisioning of Rs. 276.0 Mn made during the previous years.</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>(Habib Bank AG Zurich Ltd)</td>
<td>Overdraft</td>
<td>13.20</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Nil</td>
<td></td>
<td>98.05</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>228.36</td>
</tr>
</tbody>
</table>

#### Exposure to Aitken Spence Group

<table>
<thead>
<tr>
<th>Name of Related Party</th>
<th>Name of Director (Subsidiary of Aitken Spence Plantation Management Ltd)</th>
<th>Nature of Transaction</th>
<th>Aggregate Amount of Security</th>
</tr>
</thead>
<tbody>
<tr>
<td>Elpitiya Plantations Ltd</td>
<td></td>
<td>Overdraft</td>
<td>Limit</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Outstanding as at 31.12.06</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>(Rs. Mn.)</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Direct</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Indirect</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Overdraft</td>
<td>25.00</td>
</tr>
<tr>
<td></td>
<td></td>
<td>*84.51</td>
<td>-</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Overdraft</td>
<td>50.00</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Commercial Paper/</td>
<td>100.00</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Money Mkt Loan/</td>
<td>100.00</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Standby Overdraft</td>
<td>(100.00)</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Term Loan</td>
<td>6.28</td>
</tr>
<tr>
<td></td>
<td></td>
<td>6.28</td>
<td>-</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Term Loan</td>
<td>8.44</td>
</tr>
<tr>
<td></td>
<td></td>
<td>8.44</td>
<td>-</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Revolving Loan</td>
<td>5.00</td>
</tr>
<tr>
<td></td>
<td></td>
<td>5.00</td>
<td>-</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Short Term Loan</td>
<td>12.00</td>
</tr>
<tr>
<td></td>
<td></td>
<td>12.00</td>
<td>-</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Leases</td>
<td>13.34</td>
</tr>
<tr>
<td></td>
<td></td>
<td>13.34</td>
<td>-</td>
</tr>
</tbody>
</table>

* Excess is temporary. Since regularised.

<table>
<thead>
<tr>
<th>Name of Related Party</th>
<th>Name of Director (Subsidiary of Aitken Spence Hotels Ltd)</th>
<th>Nature of Transaction</th>
<th>Aggregate Amount of Security</th>
</tr>
</thead>
<tbody>
<tr>
<td>Kandalama Hotels Ltd</td>
<td></td>
<td>Letter of Guarantee</td>
<td>Limit</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Outstanding as at 31.12.06</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>(Rs. Mn.)</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Direct</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Indemnity</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Letter of Guarantee</td>
<td>0.36</td>
</tr>
<tr>
<td></td>
<td></td>
<td>-</td>
<td>0.36</td>
</tr>
<tr>
<td></td>
<td></td>
<td>0.36</td>
<td>-</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Name of Related Party</th>
<th>Name of Director (Subsidiary of Aitken Spence &amp; Co. Ltd)</th>
<th>Nature of Transaction</th>
<th>Aggregate Amount of Security</th>
</tr>
</thead>
<tbody>
<tr>
<td>Aitken Spence Travels Ltd</td>
<td></td>
<td>Foreign Drafts &amp;</td>
<td>Limit</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Travellers Cheque</td>
<td>Outstanding as at 31.12.06</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Purchase</td>
<td>(Rs. Mn.)</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Direct</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Indirect</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Foreign Drafts &amp;</td>
<td>3.00</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Travellers Cheque</td>
<td>0.78</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Purchase</td>
<td>-</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Cash Deposits</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>3.00</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>0.78</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>-</td>
</tr>
</tbody>
</table>
### 35. RELATED PARTY TRANSACTIONS (Contd.)

#### 35 (e) Transactions with other related parties (Contd.)

**Exposure to Aitken Spence Group (Contd.)**

<table>
<thead>
<tr>
<th>Name of Related Party</th>
<th>Name of Director</th>
<th>Nature of Transaction</th>
<th>Aggregate Amount of Security</th>
<th>Limit (Rs. Mn.)</th>
<th>Outstanding as at 31.12.06 (Rs. Mn.)</th>
<th>Direct</th>
<th>Indirect</th>
</tr>
</thead>
<tbody>
<tr>
<td>A E N Palm Oil Processing [Pvt] Ltd</td>
<td>[Subsidiary of Aitken Spence &amp; Co. Ltd]</td>
<td>Term Loan</td>
<td>58.46 -</td>
<td>58.46 -</td>
<td>Immovable property (leasehold)</td>
<td>58.46</td>
<td>58.46</td>
</tr>
<tr>
<td>Ace Containers [Pvt] Ltd</td>
<td>[Subsidiary of Aitken Spence &amp; Co. Ltd]</td>
<td>Overdraft</td>
<td>28.00 -</td>
<td>26.82 -</td>
<td>Corporate Guarantee</td>
<td>28.00</td>
<td>26.82</td>
</tr>
<tr>
<td>Ace Distriparks [Pvt] Ltd</td>
<td>[Subsidiary of Aitken Spence &amp; Co. Ltd]</td>
<td>Overdraft</td>
<td>10.00 -</td>
<td>1.09 -</td>
<td>Corporate Guarantee</td>
<td>10.00</td>
<td>1.09</td>
</tr>
<tr>
<td>Ace Freight Management [Pvt] Ltd</td>
<td>[Subsidiary of Aitken Spence &amp; Co. Ltd]</td>
<td>Overdraft</td>
<td>2.00 -</td>
<td>- -</td>
<td>Corporate Guarantee</td>
<td>2.00</td>
<td>-</td>
</tr>
<tr>
<td>Aitken Spence Garments Ltd</td>
<td>[Subsidiary of Aitken Spence &amp; Co. Ltd]</td>
<td>Letters of Credit</td>
<td>1.50 -</td>
<td>0.22</td>
<td></td>
<td>1.50</td>
<td>0.50</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Export Loan</td>
<td>0.25 -</td>
<td>0.02</td>
<td></td>
<td>0.25</td>
<td>0.02</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Overdraft</td>
<td>0.25 -</td>
<td>0.02</td>
<td></td>
<td>0.25</td>
<td>0.02</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Letter of Guarantee</td>
<td>150.00 -</td>
<td>150.08</td>
<td></td>
<td>150.00</td>
<td>150.08</td>
</tr>
<tr>
<td>Cowrie Investments</td>
<td>[Subsidiary of Aitken Spence Hotel Holdings Ltd]</td>
<td>Term Loans</td>
<td>4.71 -</td>
<td>4.71 -</td>
<td></td>
<td>4.71</td>
<td>4.71</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Overdraft</td>
<td>2.00 -</td>
<td>1.86 -</td>
<td></td>
<td>2.00</td>
<td>1.86</td>
</tr>
<tr>
<td>Ace Power Generation</td>
<td>Mr D H S Jayawardena Director</td>
<td>Letters of Credit</td>
<td>0.39 -</td>
<td>0.39</td>
<td></td>
<td>0.39</td>
<td>0.39</td>
</tr>
<tr>
<td>Horana [Pvt] Ltd</td>
<td></td>
<td>Term Loan</td>
<td>0.43 -</td>
<td>0.43</td>
<td></td>
<td>0.43</td>
<td>0.43</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Term Loan</td>
<td>1.18 -</td>
<td>1.18</td>
<td></td>
<td>1.18</td>
<td>1.18</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Overdraft</td>
<td>1.20 -</td>
<td>0.10</td>
<td></td>
<td>1.20</td>
<td>0.10</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Standby Letters of Credit</td>
<td>- -</td>
<td>- -</td>
<td></td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Letter of Guarantee</td>
<td>150.00 -</td>
<td>150.08</td>
<td></td>
<td>150.00</td>
<td>150.08</td>
</tr>
</tbody>
</table>

Annual Report 2006 163
### 35. RELATED PARTY TRANSACTIONS (Contd.)

**35 (e) Transactions with other related parties (Contd.)**

**Exposure to Aitken Spence Group (Contd.)**

<table>
<thead>
<tr>
<th>Name of Related Party</th>
<th>Name of Director [Relationship]</th>
<th>Nature of Transaction</th>
<th>Aggregate Amount of Security</th>
<th>Limit (US$. Mn.)</th>
<th>Outstanding as at 31.12.06 (US$. Mn.)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>Direct</td>
<td>Indirect</td>
</tr>
<tr>
<td><strong>Ace Power Generation</strong>&lt;br&gt;Matara (Pvt) Ltd</td>
<td>Mr D H S Jayawardena&lt;br&gt;Director</td>
<td>Term Loan</td>
<td>0.29</td>
<td>0.29</td>
<td>-</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Term Loan</td>
<td>0.97</td>
<td>0.97</td>
<td>-</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Letters of Credit</td>
<td>0.43</td>
<td>-</td>
<td>0.43</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Overdraft</td>
<td>1.20</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Letters of Credit (Rs. Mn)</td>
<td>150.00</td>
<td>-</td>
<td>(Rs. Mn)150.00</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Letter of Guarantee</td>
<td>(Rs. Mn) 0.13</td>
<td>-</td>
<td>(Rs. Mn)0.13</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Overdraft (Rs. Mn)</td>
<td>120.00</td>
<td>3.10</td>
<td>150.13</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>(US$. Mn) 2.89</td>
<td>1.26</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>(Rs. Mn) 150.13</td>
<td>3.10</td>
</tr>
<tr>
<td><strong>Ace Power Generation</strong>&lt;br&gt;Embilipitiya (Pvt) Ltd</td>
<td>(Subsidiary of Aitken Spence &amp; Co. Ltd)</td>
<td>Term Loan</td>
<td>0.37</td>
<td>0.37</td>
<td>-</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Term Loan</td>
<td>1.58</td>
<td>1.58</td>
<td>-</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Overdraft</td>
<td>0.62</td>
<td>0.98</td>
<td>-</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Letter of Credit</td>
<td>0.13</td>
<td>0.13</td>
<td>-</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Letter of Guarantee</td>
<td>(Rs. Mn) 44.67</td>
<td>-</td>
<td>(Rs. Mn)44.67</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Overdraft (Rs. Mn)</td>
<td>200.00</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>(US$. Mn) 5.33</td>
<td>2.93</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>(Rs. Mn) 244.67</td>
<td>-</td>
</tr>
<tr>
<td><strong>Elpitiya Lifestyle Solutions (Pvt) Ltd</strong> (50% owned by Elpitiya Plantations Ltd)</td>
<td>Term Loan</td>
<td>0.22</td>
<td>0.22</td>
<td>-</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>(US$. Mn) 0.22</td>
<td>-</td>
</tr>
<tr>
<td><strong>Cey Capital (Pvt) Ltd</strong> (50% owned by Aitken Spence &amp; Co. Ltd)</td>
<td>Term Loan</td>
<td>3.24</td>
<td>3.24</td>
<td>-</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>(US$. Mn) 3.24</td>
<td>-</td>
</tr>
</tbody>
</table>

**Exposure to Browns Group**

<table>
<thead>
<tr>
<th>Name of Related Party</th>
<th>Name of Director [Relationship]</th>
<th>Nature of Transaction</th>
<th>Aggregate Amount of Security</th>
<th>Limit (Rs. Mn.)</th>
<th>Outstanding as at 31.12.06 (Rs. Mn.)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>Direct</td>
<td>Indirect</td>
</tr>
<tr>
<td><strong>Brown &amp; Co. Ltd</strong>&lt;br&gt;(till 30.06.2006)</td>
<td>Mr M V Theagarajah&lt;br&gt;Chairman</td>
<td>Letter of Credit</td>
<td>-</td>
<td>-</td>
<td>6.90</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Letter of Credit</td>
<td>-</td>
<td>-</td>
<td>31.03</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Import Loan</td>
<td>-</td>
<td>172.11</td>
<td>-</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Letters of Guarantee</td>
<td>315.00</td>
<td>-</td>
<td>23.85</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Overdraft (US$. Mn)</td>
<td>(79.00)</td>
<td>72.38</td>
<td>-</td>
</tr>
<tr>
<td></td>
<td></td>
<td>One off Import Loans</td>
<td>175.00</td>
<td>175.00</td>
<td>-</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Term Loan</td>
<td>339.26</td>
<td>339.26</td>
<td>-</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Term Loan</td>
<td>134.00</td>
<td>134.00</td>
<td>-</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Lease</td>
<td>6.96</td>
<td>6.96</td>
<td>-</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>969.32</td>
<td>819.81</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Name of Related Party</th>
<th>Name of Director [Relationship]</th>
<th>Nature of Transaction</th>
<th>Aggregate Amount of Security</th>
<th>Limit (Rs. Mn.)</th>
<th>Outstanding as at 31.12.06 (Rs. Mn.)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>Direct</td>
<td>Indirect</td>
</tr>
<tr>
<td><strong>Browns Group Industries Ltd</strong>&lt;br&gt;(till 30.06.2006)</td>
<td>Mr M V Theagarajah&lt;br&gt;Chairman</td>
<td>Letter of Credit</td>
<td>-</td>
<td>-</td>
<td>6.90</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Letter of Credit</td>
<td>-</td>
<td>-</td>
<td>31.03</td>
</tr>
<tr>
<td></td>
<td></td>
<td>One off Letter of Credit</td>
<td>21.00</td>
<td>-</td>
<td>21.00</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Letter of Guarantee</td>
<td>9.64</td>
<td>-</td>
<td>9.64</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td>80.64</td>
<td>-</td>
</tr>
</tbody>
</table>
### 35. RELATED PARTY TRANSACTIONS (Contd.)

#### 35 (e) Transactions with other related parties (Contd.)

**Exposure to Browns Group (Contd.)**

<table>
<thead>
<tr>
<th>Name of Related Party</th>
<th>Name of Director [Relationship]</th>
<th>Nature of Transaction</th>
<th>Aggregate Amount of Security</th>
<th>Nature of Transaction</th>
<th>Aggregate Amount of Security</th>
</tr>
</thead>
<tbody>
<tr>
<td>I.G. Browns Rubber Industries Ltd</td>
<td>Mr M V Theagarajah Chairman (till 30.06.2006)</td>
<td>Letter of Credit</td>
<td>2.50</td>
<td>-</td>
<td>0.94</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Letter of Guarantee</td>
<td>0.40</td>
<td>-</td>
<td>0.40</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Overdraft</td>
<td>0.40</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Lease</td>
<td>2.93</td>
<td>2.93</td>
<td>-</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>6.23</td>
<td>2.93</td>
<td>1.34</td>
</tr>
<tr>
<td>Browns Dimo Industrial Products Ltd</td>
<td>Mr M V Theagarajah Chairman (till 30.06.2006)</td>
<td>Letter of Credit</td>
<td>4.00</td>
<td>-</td>
<td>4.24</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Letter of Guarantee</td>
<td>0.28</td>
<td>-</td>
<td>0.28</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Overdraft</td>
<td>3.00</td>
<td>2.09</td>
<td>-</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Lease</td>
<td>2.16</td>
<td>-</td>
<td>2.16</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>4.28</td>
<td>-</td>
<td>4.52</td>
</tr>
<tr>
<td>Engineering Services Ltd</td>
<td>Mr M V Theagarajah Chairman (till 30.06.2006)</td>
<td>Letter of Credit</td>
<td>6.00</td>
<td>-</td>
<td>7.29</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Letter of Guarantee</td>
<td>5.00</td>
<td>7.98</td>
<td>-</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Overdraft</td>
<td>0.38</td>
<td>0.38</td>
<td>-</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Lease</td>
<td>11.38</td>
<td>8.36</td>
<td>7.29</td>
</tr>
<tr>
<td>Walker &amp; Greig Ltd</td>
<td>Mr M V Theagarajah Chairman (till 30.06.2006)</td>
<td>Letter of Credit</td>
<td>0.80</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Letter of Guarantee</td>
<td>0.80</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Trust Receipt</td>
<td>10.00</td>
<td>7.97</td>
<td>-</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Overdraft</td>
<td>2.50</td>
<td>0.85</td>
<td>-</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>3.30</td>
<td>0.85</td>
<td>-</td>
</tr>
<tr>
<td>Snowcem Products Lanka (Pvt) Ltd</td>
<td>Mr M V Theagarajah Chairman (till 30.06.2006)</td>
<td>Letter of Credit</td>
<td>10.00</td>
<td>-</td>
<td>9.77</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Trust Receipt</td>
<td>10.00</td>
<td>-</td>
<td>9.77</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>111.80</td>
<td>5.38</td>
<td>9.98</td>
</tr>
<tr>
<td>Exposure to Ceylon Biscuits Group</td>
<td></td>
<td>Letter of Credit</td>
<td>99.65</td>
<td>-</td>
<td>9.96</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Lease</td>
<td>1.80</td>
<td>1.80</td>
<td>-</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Lease</td>
<td>10.35</td>
<td>3.58</td>
<td>-</td>
</tr>
<tr>
<td>Ceylon Biscuits Ltd</td>
<td>Mr R T Wijetilleke Director</td>
<td>One off Letter of Credit</td>
<td>8.92</td>
<td>8.92</td>
<td>-</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Lease</td>
<td>8.92</td>
<td>8.92</td>
<td>-</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Lease</td>
<td>8.92</td>
<td>8.92</td>
<td>-</td>
</tr>
<tr>
<td>Plenty Foods [Pvt] Ltd</td>
<td>(Subsidiary of Ceylon Biscuits Ltd)</td>
<td>Lease</td>
<td>15.00</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Soy Foods [Lanka] Ltd.</td>
<td>(Subsidiary of Ceylon Biscuits Ltd)</td>
<td>Overdraft</td>
<td>23.00</td>
<td>-</td>
<td>3.55</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Short Term Loan</td>
<td>20.00</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Letter of Credit</td>
<td>40.00</td>
<td>-</td>
<td>42.11</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>98.00</td>
<td>-</td>
<td>45.66</td>
</tr>
<tr>
<td>Cecil Food (Pvt) Ltd</td>
<td>(Subsidiary of Ceylon Biscuits Ltd)</td>
<td>Lease</td>
<td>0.16</td>
<td>0.16</td>
<td>-</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Lease</td>
<td>0.16</td>
<td>0.16</td>
<td>-</td>
</tr>
</tbody>
</table>
### 35. RELATED PARTY TRANSACTIONS (Contd.)

#### 35 (e) Transactions with other related parties (Contd.)

<table>
<thead>
<tr>
<th>Name of Related Party</th>
<th>Name of Director (Relationship)</th>
<th>Nature of Transaction</th>
<th>Aggregate Amount of Accommodation Limit (Rs. Mn.)</th>
<th>Outstanding as at 31.12.06 (Rs. Mn.)</th>
<th>Security</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Exposure to Sunshine Group</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Sunshine Holdings Ltd.</td>
<td>Mr R T Wijetilleke Chairman</td>
<td>Term Loan</td>
<td>40.55</td>
<td>40.55</td>
<td>Corporate Guarantee</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>40.55</td>
<td>40.55</td>
<td></td>
</tr>
<tr>
<td>Watawala Plantations Ltd.</td>
<td>(Subsidiary of Sunshine Holdings Ltd)</td>
<td>Letter of Credit</td>
<td>5.00</td>
<td>5.00</td>
<td>Mortgage over property</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Overdraft</td>
<td>100.00</td>
<td>57.19</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>Term Loan I</td>
<td>14.00</td>
<td>14.00</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>Term Loan II</td>
<td>14.99</td>
<td>14.99</td>
<td>(Leasehold)</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Leases</td>
<td>15.33</td>
<td>15.33</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>E-Friends Loans</td>
<td>6.40</td>
<td>6.40</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>Packing Credit</td>
<td>50.00</td>
<td>10.57</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>Letters of Guarantee</td>
<td>5.00</td>
<td>10.57</td>
<td></td>
</tr>
<tr>
<td>Swiss Biogenics Ltd.</td>
<td>(Subsidiary of Sunshine Holdings Ltd)</td>
<td>Letter of Credit</td>
<td>145.00</td>
<td>117.29</td>
<td>Inventories</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Import Bills</td>
<td>145.00</td>
<td></td>
<td>Corporate Guarantee</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Import Loans</td>
<td>7.64</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>Overdraft</td>
<td>5.00</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Sunshine Travels &amp; Tours Ltd.</td>
<td>(Subsidiary of Sunshine Holdings Ltd)</td>
<td>Letter of Guarantee</td>
<td>10.00</td>
<td>10.00</td>
<td>Cash Deposits</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Overdraft</td>
<td>5.00</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Sunshine Teas (Pvt) Ltd.</td>
<td>(Subsidiary of Swiss Biogenics Ltd)</td>
<td>Letters of Credit</td>
<td>90.00</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>Short Term Loan</td>
<td>(25.00)</td>
<td>8.97</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>Overdraft</td>
<td>(25.00)</td>
<td>13.33</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>Letter of Guarantee</td>
<td>10.00</td>
<td>8.97</td>
<td>Mortgage over Machinery</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Term Loan US$Mn 0.16</td>
<td>(US$ Mn)</td>
<td>0.16</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>Packing Credit Loans</td>
<td>(US$ Mn)</td>
<td>0.50</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>Export Bill Discounting</td>
<td>(US$ Mn)</td>
<td>1.00</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Nawaloka Hospitals Ltd.</td>
<td>Mr R T Wijetilleke Director</td>
<td>Temporary Overdraft</td>
<td>50.00</td>
<td>49.98</td>
<td>Personal Guarantee of the shareholding Directors</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>50.00</td>
<td></td>
<td></td>
</tr>
<tr>
<td>New Nawaloka Hospitals Ltd.</td>
<td>(Subsidiary of Nawaloka Hospitals Ltd)</td>
<td>Letter of Credit</td>
<td>10.00</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>Term Loan I</td>
<td>71.26</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>Term Loan II</td>
<td>69.99</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>Import LC/ Term Loan</td>
<td>109.18</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>Overdraft</td>
<td>10.00</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>270.43</td>
<td>260.32</td>
<td></td>
</tr>
</tbody>
</table>
### 35. RELATED PARTY TRANSACTIONS (Contd.)

#### 35 (f) Related Party Transaction - Group

#### 35 (f)i Sithma Development (Pvt) Ltd.

**Transactions with related parties**

<table>
<thead>
<tr>
<th>Name of Related Party</th>
<th>Name of Director (Relationship)</th>
<th>Nature of Transaction</th>
<th>Amount (Rs. Mn.)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sri Lanka Insurance Corporation Ltd.</td>
<td>Mr D H S Jayawardena Chairman, Mr R K Obeysekera Deputy Chairman</td>
<td>Insurance premium paid, Debenture interest paid</td>
<td>15.91, 242.61</td>
</tr>
</tbody>
</table>

#### 35 (f)ii HNB Securities Ltd

**Transactions with related parties**

<table>
<thead>
<tr>
<th>Name of Related Party</th>
<th>Name of Director (Relationship)</th>
<th>Nature of Transaction</th>
<th>Cumulative Investment/ Face Value (Rs. Mn)</th>
<th>Cumulative Interest paid/ Recd (Rs. Mn)</th>
<th>Balance Outstanding (Rs. Mn)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Ceylon Biscuits Ltd.</td>
<td>Mr R T Wijetilleke Director</td>
<td>Sale of Treasury Bills, Repurchase Agreements of Treasury Bonds/Bills</td>
<td>25.10, 107.10</td>
<td>-, 0.40</td>
<td>-</td>
</tr>
<tr>
<td>Sunshine Holdings Ltd.</td>
<td>Mr R T Wijetilleke Director</td>
<td>Repurchase Agreements of Treasury Bonds/Bills</td>
<td>16.70, 185.00</td>
<td>0.03, 1.07</td>
<td>5.60</td>
</tr>
<tr>
<td>Colombo Stock Exchange</td>
<td>Mr R T Wijetilleke Director</td>
<td>Repurchase Agreements of Treasury Bonds/Bills</td>
<td>185.00</td>
<td>1.07</td>
<td>-</td>
</tr>
<tr>
<td>Sri Lanka Insurance Corporation Ltd. - Life Fund</td>
<td>Mr D H S Jayawardena Chairman, Mr R K Obeysekera Director</td>
<td>Sale of Treasury Bonds</td>
<td>250.00</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Snowcem Products Lanka (Pvt) Ltd.</td>
<td>Mr M V Theagarajah Chairman (till 30/06/2006)</td>
<td>Repurchase Agreements of Treasury Bonds/Bills</td>
<td>8.00, 13.50</td>
<td>0.18, 0.17</td>
<td>2.00</td>
</tr>
<tr>
<td>Engineering Services Ltd.</td>
<td>Mr M V Theagarajah Chairman (till 30/06/2006)</td>
<td>Sale of Treasury Bills, Purchase of Treasury Bills</td>
<td>31.40, 13.50</td>
<td>-, -</td>
<td>-</td>
</tr>
<tr>
<td>Sunshine Travels &amp; Tours Ltd.</td>
<td>Subsidiary of Sunshine Holdings Ltd.</td>
<td>Repurchase Agreements of Treasury Bonds/Bills</td>
<td>7.20, 13.50</td>
<td>0.17, 0.17</td>
<td>1.30</td>
</tr>
</tbody>
</table>

#### 35(f)iii HNB Stockbrokers (Pvt) Ltd

**Transactions with related parties**

<table>
<thead>
<tr>
<th>Name of Related Party</th>
<th>Name of Director (Relationship)</th>
<th>Nature of Transaction</th>
<th>Amount (Rs. Mn.)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sri Lanka Insurance Corporation Ltd.</td>
<td>Mr D H S Jayawardena Director, Mr R K Obeysekera Director</td>
<td>Brokerage income</td>
<td>4.76</td>
</tr>
<tr>
<td>Sri Lanka Insurance Corporation Ltd. - Life Fund</td>
<td>Mr D H S Jayawardena Director, Mr R K Obeysekera Director</td>
<td>Brokerage income</td>
<td>7.71</td>
</tr>
<tr>
<td>Sunshine Holdings Ltd.</td>
<td>Mr R T Wijetilleke Director</td>
<td>Brokerage income</td>
<td>0.20</td>
</tr>
</tbody>
</table>
### Transactions with related parties

<table>
<thead>
<tr>
<th>Name of Related Party</th>
<th>Name of Director (Relationship)</th>
<th>Nature of Transaction</th>
<th>Amount (Rs. Mn.)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Stassen Exports Ltd</td>
<td>Dr V P Vittachi, Chairman</td>
<td>Non-life insurance business</td>
<td>10.67</td>
</tr>
<tr>
<td></td>
<td>Mr D H S Jayawardena, Managing Director</td>
<td>Claims payable</td>
<td>3.46</td>
</tr>
<tr>
<td></td>
<td>Mr R K Obeyesekera, Director</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Stassen International Ltd.</td>
<td>Dr V P Vittachi, Chairman</td>
<td>Non-life insurance business</td>
<td>0.21</td>
</tr>
<tr>
<td></td>
<td>Mr D H S Jayawardena, Managing Director</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Mr R K Obeyesekera, Director</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Stassen Natural Foods (Pvt) Ltd.</td>
<td>Dr V P Vittachi, Chairman</td>
<td>Non-life insurance business</td>
<td>0.13</td>
</tr>
<tr>
<td></td>
<td>Mr D H S Jayawardena, Managing Director</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Mr R K Obeyesekera, Director</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Texplo Industries Ltd.</td>
<td>Mr D H S Jayawardena, Chairman</td>
<td>Non-life insurance business</td>
<td>0.39</td>
</tr>
<tr>
<td></td>
<td>Mr D H S Jayawardena, Managing Director</td>
<td>Claims payable</td>
<td>0.78</td>
</tr>
<tr>
<td>Milford Exports (Ceylon) Ltd.</td>
<td>Dr V P Vittachi, Chairman</td>
<td>Non-life insurance business</td>
<td>0.02</td>
</tr>
<tr>
<td></td>
<td>Mr D H S Jayawardena, Managing Director</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Mr R K Obeyesekera, Director</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Aitken Spence (Garments) Ltd.</td>
<td>Subsidiary of Aitken Spence &amp; Co. Ltd.</td>
<td>Non-life insurance business</td>
<td>0.20</td>
</tr>
<tr>
<td>Elpitiya Plantations Ltd.</td>
<td>Subsidiary of Aitken Spence Plantation Management Ltd.</td>
<td>Non-life insurance business</td>
<td>0.08</td>
</tr>
<tr>
<td>Sri Lanka Insurance Corporation Ltd.</td>
<td>Mr D H S Jayawardena, Managing Director</td>
<td>Co-insurance</td>
<td>6.13</td>
</tr>
</tbody>
</table>
### 35. RELATED PARTY TRANSACTIONS (Contd.)

#### 35 (f) Related Party Transaction - Group (Contd.)

#### 35(f)iv HNB Assurance Ltd. (Contd.)

<table>
<thead>
<tr>
<th>Name of Related Party</th>
<th>Name of Director</th>
<th>Nature of Transaction</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Brown &amp; Co. Ltd.</td>
<td>Mr M V Theagarajah</td>
<td>Non-life insurance business</td>
<td>0.48</td>
</tr>
<tr>
<td></td>
<td>Chairman</td>
<td>Claims payable</td>
<td>0.32</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Purchase and maintenance</td>
<td>4.24</td>
</tr>
<tr>
<td></td>
<td></td>
<td>of office equipment</td>
<td></td>
</tr>
<tr>
<td></td>
<td>[till 30.06.2006]</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Brown &amp; Co. Ltd.</td>
<td>Mr M V Theagarajah</td>
<td>Non-life insurance business</td>
<td>0.06</td>
</tr>
<tr>
<td></td>
<td>Chairman</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>[till 30.06.2006]</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Browns Group Industries Ltd.</td>
<td>Mr M V Theagarajah</td>
<td>Non-life insurance business</td>
<td>0.11</td>
</tr>
<tr>
<td></td>
<td>Chairman</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>[till 30.06.2006]</td>
<td></td>
<td></td>
</tr>
<tr>
<td>I G Browns Rubber Industries Ltd.</td>
<td>Mr M V Theagarajah</td>
<td>Non-life insurance business</td>
<td>0.02</td>
</tr>
<tr>
<td></td>
<td>Chairman</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>[till 30.06.2006]</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Browns Tours Ltd.</td>
<td>Mr M V Theagarajah</td>
<td>Non-life insurance business</td>
<td>0.02</td>
</tr>
<tr>
<td></td>
<td>Chairman</td>
<td>Purchase of air tickets</td>
<td>0.98</td>
</tr>
<tr>
<td></td>
<td>[till 30.06.2006]</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Browns Dimo Industrial Products (Pvt) Ltd.</td>
<td>Mr M V Theagarajah</td>
<td>Non-life insurance business</td>
<td>0.04</td>
</tr>
<tr>
<td></td>
<td>Chairman</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>[till 30.06.2006]</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Snowcem Products Lanka (Pvt) Ltd.</td>
<td>Mr M V Theagarajah</td>
<td>Non-life insurance business</td>
<td>0.01</td>
</tr>
<tr>
<td></td>
<td>Chairman</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>[till 30.06.2006]</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Engineering Services Ltd.</td>
<td>Mr M V Theagarajah</td>
<td>Non-life insurance business</td>
<td>0.06</td>
</tr>
<tr>
<td></td>
<td>Chairman</td>
<td>Claims payable</td>
<td>0.04</td>
</tr>
<tr>
<td></td>
<td>[till 30.06.2006]</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
### 36. MATURITY ANALYSIS - BANK

An analysis of the total assets and liabilities of the Bank as at 31st December based on the remaining period at the balance sheet date to the respective contractual maturity dates is given below:

<table>
<thead>
<tr>
<th>Maturity</th>
<th>Upto 3 Months</th>
<th>3 to 12 Months</th>
<th>1 to 3 Years</th>
<th>3 to 5 Years</th>
<th>More Than 5 Years</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Rs.000</td>
<td>Rs.000</td>
<td>Rs.000</td>
<td>Rs.000</td>
<td>Rs.000</td>
<td>Rs.000</td>
</tr>
<tr>
<td><strong>Interest earning assets</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Cash and cash equivalent</td>
<td>12,581,512</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>12,581,512</td>
</tr>
<tr>
<td>Balances with Foreign Banks which are interest bearing</td>
<td>8,695,017</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>8,695,017</td>
</tr>
<tr>
<td>Commercial paper</td>
<td>290,667</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>290,667</td>
</tr>
<tr>
<td>Investment securities-Bonds &amp; Debentures</td>
<td>-</td>
<td>2,927,974</td>
<td>16,429,206</td>
<td>517,134</td>
<td>489,000</td>
<td>20,363,314</td>
</tr>
<tr>
<td>Bills of Exchange</td>
<td>1,515,247</td>
<td>338,961</td>
<td>58,644</td>
<td>-</td>
<td>-</td>
<td>1,910,852</td>
</tr>
<tr>
<td>Loans &amp; advances</td>
<td>20,989,773</td>
<td>33,124,124</td>
<td>20,011,820</td>
<td>21,970,673</td>
<td>18,611,984</td>
<td>114,708,374</td>
</tr>
<tr>
<td>Lease rentals receivable</td>
<td>196,382</td>
<td>801,936</td>
<td>3,440,888</td>
<td>6,912,844</td>
<td>201,225</td>
<td>11,552,475</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>44,268,598</td>
<td>37,192,995</td>
<td>39,937,758</td>
<td>29,400,651</td>
<td>25,057,817</td>
<td>196,429,028</td>
</tr>
<tr>
<td><strong>Percentage - 31/12/2006</strong></td>
<td>33.01</td>
<td>31.93</td>
<td>20.33</td>
<td>14.97</td>
<td>12.76</td>
<td>100</td>
</tr>
<tr>
<td><strong>Percentage - 31/12/2005</strong></td>
<td>33.44</td>
<td>22.24</td>
<td>15.79</td>
<td>13.38</td>
<td>100</td>
<td></td>
</tr>
<tr>
<td><strong>Interest bearing liabilities</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Deposits from customers</td>
<td>77,539,614</td>
<td>37,318,429</td>
<td>10,567,860</td>
<td>4,919,296</td>
<td>3,712,719</td>
<td>134,057,918</td>
</tr>
<tr>
<td>Borrowings - Money at call</td>
<td>4,584,620</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>4,584,620</td>
</tr>
<tr>
<td>Borrowings - Reliance</td>
<td>2,481,897</td>
<td>43,068</td>
<td>122,920</td>
<td>355,283</td>
<td>579,419</td>
<td>3,582,587</td>
</tr>
<tr>
<td>Borrowings - Local Banks</td>
<td>-</td>
<td>2,000,000</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>2,000,000</td>
</tr>
<tr>
<td>Borrowings - Foreign Banks</td>
<td>864,294</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>864,294</td>
</tr>
<tr>
<td>Securities sold under repo agreements</td>
<td>6,736,714</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>6,736,714</td>
</tr>
<tr>
<td>Subordinated Debentures</td>
<td>-</td>
<td>1,759,148</td>
<td>2,127,628</td>
<td>1,233,224</td>
<td>5,120,000</td>
<td>9,207,139</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>92,207,139</td>
<td>41,120,645</td>
<td>12,818,408</td>
<td>5,274,579</td>
<td>5,525,342</td>
<td>156,946,133</td>
</tr>
<tr>
<td><strong>Percentage - 31/12/2006</strong></td>
<td>33.01</td>
<td>18.93</td>
<td>20.33</td>
<td>14.97</td>
<td>12.76</td>
<td>100</td>
</tr>
<tr>
<td><strong>Percentage - 31/12/2005</strong></td>
<td>33.44</td>
<td>22.24</td>
<td>15.79</td>
<td>13.38</td>
<td>100</td>
<td></td>
</tr>
<tr>
<td><strong>Non Interest bearing liabilities</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Deposits from customers</td>
<td>13,824,107</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>13,824,107</td>
</tr>
<tr>
<td>Dividend payable</td>
<td>38,103</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>38,103</td>
</tr>
<tr>
<td>Bills payable</td>
<td>1,190,056</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>1,190,056</td>
</tr>
<tr>
<td>Current tax liability</td>
<td>761,729</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>761,729</td>
</tr>
<tr>
<td>Deferred tax liability</td>
<td>313,756</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>313,756</td>
</tr>
<tr>
<td>Other liabilities</td>
<td>10,425,336</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>10,425,336</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>26,553,087</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>26,553,087</td>
</tr>
<tr>
<td><strong>Percentage - 31/12/2006</strong></td>
<td>60.41</td>
<td>20.93</td>
<td>6.53</td>
<td>2.68</td>
<td>9.40</td>
<td>100</td>
</tr>
<tr>
<td><strong>Percentage - 31/12/2005</strong></td>
<td>64.87</td>
<td>16.83</td>
<td>6.70</td>
<td>2.58</td>
<td>9.02</td>
<td>100</td>
</tr>
</tbody>
</table>

"Up to 3 months" deposits include the Bank’s Savings Deposit Base of Rs. 64.3 Bn. (2005 - Rs. 61.5 Bn.).
### Segment Reporting

#### Business segments - Group

<table>
<thead>
<tr>
<th></th>
<th>Banking</th>
<th>Leasing</th>
<th><strong>Dealing</strong></th>
<th>Property</th>
<th>Insurance</th>
<th>Eliminations</th>
<th>Consolidated/Unallocated</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Rs.000</td>
<td>Rs.000</td>
<td>Rs.000</td>
<td>Rs.000</td>
<td>Rs.000</td>
<td>Rs.000</td>
<td>Rs.000</td>
</tr>
<tr>
<td>Revenue from external customers</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Interest</td>
<td>16,835,610</td>
<td>12,907,337</td>
<td>-</td>
<td>-</td>
<td>864,275</td>
<td>624,931</td>
<td>-</td>
</tr>
<tr>
<td>Exchange/Premium</td>
<td>792,303</td>
<td>646,460</td>
<td>-</td>
<td>-</td>
<td>396</td>
<td>(214)</td>
<td>-</td>
</tr>
<tr>
<td>Lease/Brokerage</td>
<td>-</td>
<td>-</td>
<td>1,538,842</td>
<td>1,162,455</td>
<td>97,673</td>
<td>4,889</td>
<td>-</td>
</tr>
<tr>
<td>Commissions/Rent</td>
<td>1,858,180</td>
<td>1,704,334</td>
<td>-</td>
<td>-</td>
<td>5,409</td>
<td>1,098</td>
<td>18,951</td>
</tr>
<tr>
<td>Other</td>
<td>354,100</td>
<td>344,246</td>
<td>-</td>
<td>-</td>
<td>1,215</td>
<td>180,842</td>
<td>-</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total revenue from external customers</td>
<td>19,842,193</td>
<td>15,602,377</td>
<td>1,538,842</td>
<td>1,162,455</td>
<td>968,958</td>
<td>811,376</td>
<td>18,951</td>
</tr>
<tr>
<td>Inter-segment revenue</td>
<td>132,138</td>
<td>150,482</td>
<td>-</td>
<td>-</td>
<td>17,364</td>
<td>55,394</td>
<td>441,653</td>
</tr>
<tr>
<td>Total revenue</td>
<td>19,974,331</td>
<td>15,752,859</td>
<td>1,538,842</td>
<td>1,162,455</td>
<td>1,086,332</td>
<td>866,770</td>
<td>440,604</td>
</tr>
<tr>
<td>Segment result</td>
<td>2,616,096</td>
<td>1,700,873</td>
<td>947,170</td>
<td>662,855</td>
<td>22,391</td>
<td>142,756</td>
<td>58,204</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Unallocated expenses</td>
<td>645,843</td>
<td>622,170</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Profit from operations</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Income from associates</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Income tax expense</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Profit for the period</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Minority interests</td>
<td>(36,530)</td>
<td>(24,116)</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Profit for the Equity Holders of the Bank</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Segment assets</td>
<td>151,943,853</td>
<td>128,035,145</td>
<td>11,552,475</td>
<td>8,864,351</td>
<td>8,268,188</td>
<td>7,597,672</td>
<td>4,820,926</td>
</tr>
<tr>
<td>Investment in associates</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Unallocated assets</td>
<td>30,506,709</td>
<td>26,686,925</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total Assets</td>
<td>206,978,564</td>
<td>154,722,070</td>
<td>11,552,475</td>
<td>8,864,351</td>
<td>8,268,188</td>
<td>7,597,672</td>
<td>4,820,926</td>
</tr>
<tr>
<td>Segment liabilities</td>
<td>137,519,686</td>
<td>121,646,075</td>
<td>11,552,475</td>
<td>8,864,351</td>
<td>7,641,013</td>
<td>6,973,851</td>
<td>3,085,193</td>
</tr>
<tr>
<td>Unallocated liabilities</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total liabilities</td>
<td>193,889,184</td>
<td>128,298,146</td>
<td>11,552,475</td>
<td>8,864,351</td>
<td>8,268,188</td>
<td>7,597,672</td>
<td>4,820,926</td>
</tr>
<tr>
<td>Cash flows from operating activities</td>
<td>(2,318,263)</td>
<td>468,521</td>
<td>4,314</td>
<td>3,295</td>
<td>654</td>
<td>38,022</td>
<td>188,381</td>
</tr>
<tr>
<td>Cash flows from investing activities</td>
<td>(4,456,766)</td>
<td>(314,054)</td>
<td>-</td>
<td>-</td>
<td>(20,206)</td>
<td>3,116</td>
<td>(49,902)</td>
</tr>
<tr>
<td>Cash flows from financing activities</td>
<td>8,878,736</td>
<td>1,134,527</td>
<td>-</td>
<td>-</td>
<td>(53,386)</td>
<td>-</td>
<td>(610)</td>
</tr>
<tr>
<td>Capital Expenditure</td>
<td>504,598</td>
<td>495,594</td>
<td>23</td>
<td>1,017</td>
<td>7,488</td>
<td>7,744</td>
<td>49,012</td>
</tr>
<tr>
<td>Depreciation</td>
<td>430,257</td>
<td>456,837</td>
<td>1,238</td>
<td>392</td>
<td>3,657</td>
<td>3,219</td>
<td>80,724</td>
</tr>
<tr>
<td>Amortization</td>
<td>98,343</td>
<td>36,205</td>
<td>1,773</td>
<td>887</td>
<td>1,517</td>
<td>897</td>
<td>-</td>
</tr>
</tbody>
</table>

**Stock Broking & Securities Dealings**
38. EVENTS OCCURRING AFTER THE BALANCE SHEET DATE

There are no events occurring after the Balance Sheet date, which require adjustments to or disclosures in the financial statements, other than those disclosed below:

38(a) Proposed dividends
Refer Note No. 25

38(b) Issue of Bonus Shares
Board of Directors have recommended an issue of 1:1 bonus shares [one ordinary share for each ordinary share outstanding as at 31st December 2006], which is to be approved at the Annual General Meeting to be held on 29th March 2007.

The Basic Earnings per Share (EPS) disclosed on the Income Statement and in Note No. 9 to the financial statements has not been adjusted for the said bonus issue. If the bonus shares are considered for the EPS computation, the adjusted EPS would be Rs. 9.43 for the Bank and Rs. 9.51 for the Group.

39. COMPARATIVE INFORMATION

Comparative information has been restated, wherever necessary, to conform to the current year’s presentation and classification.

40. DIRECTORS’ RESPONSIBILITY STATEMENT

The Board of Directors is responsible for the preparation and presentation of these financial statements. Please refer page 103 for the statement of the Directors’ Responsibility for Financial Reporting.
The principal objective of the Central Bank of Sri Lanka's Capital Adequacy requirement is to ensure that an adequate level of capital is maintained to withstand any losses which may result from the risks in a Bank's Balance Sheet, in particular, "credit risk" and "market risk". Our risk based capital adequacy requirements are consistent with the international standards of Basel Committee on Banking Regulations and Supervisory Practices. The framework has three basic aspects - the capital base elements, the required capitalisation level and the risk weighting.

The capital base is comprises of two elements, namely Tier 1 and Tier 2 capital after certain deductions.

Tier 1 capital includes paid up ordinary share capital, paid up non cumulative, non redeemable preference shares, share premium, statutory reserve fund, published retained earnings, general and other reserves less Goodwill.

Tier 2 capital includes 50% of asset revaluation reserves, general provision for doubtful debts, hybrid debt/equity instruments and approved subordinated term debts.

Equity investments in unconsolidated banking and financial subsidiaries and investments in capital of other banks/financial associates are deducted from total Tier 1 and 2 in arriving at the capital base. Sri Lankan banks are required to maintain a minimum total risk weighted capital ratio of 10% in respect of domestic (DBU) and off-shore banking operations (FCBU) since 2003. Tier 1 capital must be at least 50% of the minimum capital requirements.

In order to determine the capital adequacy ratio, all assets are risk weighted in order to provide a broad indication of credit risk. Seven risk weightings applicable as at 31st December 2006 are 0%, 10%, 20%, 50%, 55%, 100% and 110% (0%, 10%, 20%, 50% and 100% up to September 2006) and the assets to which those weightings apply are described below. Off balance sheet transactions are converted to credit equivalents, using a credit conversion factor, before being allocated a risk weighting.

To ascertain the credit risk, off balance sheet items are categorised as follows:

- Direct credit substitutes
- Transaction-related contingencies
- Short term self liquidating trade related contingencies
- Sale and Repurchase Agreements & Assets sale with recourse where the credit risk remains with the bank
- Obligations under an On-going Underwriting Agreement
- Other commitments with an original maturity upto one year or which can be unconditionally cancelled at any time
- Other commitments with an original maturity of over one year
- Foreign Exchange and Interest Rate Contracts

With effect from 31st March 2006, all banks were required to compute a capital charge for market risk in keeping with current international practice and the requirements of the Basel Committee as per the directions given by the Monetary Board of the Central Bank of Sri Lanka.

The total of the risk weighted assets for credit risk and market risk together with the risk assessed off balance sheet items is then related to the capital base and resultant risk ratio is used as a measure of capital adequacy.

The following table provides details of Tier 1 & Tier 2 capital position and risk adjusted assets and off-balance sheet exposure.
## Capital Adequacy

### Capital Base as at 31st December

<table>
<thead>
<tr>
<th>Rupees Million</th>
<th>2006</th>
<th>2005</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>TIER 1</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Voting ordinary shares</td>
<td>947</td>
<td>947</td>
</tr>
<tr>
<td>Non-Voting ordinary shares</td>
<td>231</td>
<td>231</td>
</tr>
<tr>
<td>Share premium</td>
<td>2,704</td>
<td>2,704</td>
</tr>
<tr>
<td>Statutory reserve fund</td>
<td>670</td>
<td>625</td>
</tr>
<tr>
<td>Published retained profits</td>
<td>1,736</td>
<td>1,174</td>
</tr>
<tr>
<td>General and other reserves</td>
<td>6,402</td>
<td>5,252</td>
</tr>
<tr>
<td><strong>Total Tier 1 Capital</strong></td>
<td>12,691</td>
<td>10,933</td>
</tr>
<tr>
<td><strong>TIER 2</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Approved assets revaluation reserves (1)</td>
<td>120</td>
<td>153</td>
</tr>
<tr>
<td>General provisions</td>
<td>573</td>
<td>219</td>
</tr>
<tr>
<td>Debentures</td>
<td>2,462</td>
<td>2,119</td>
</tr>
<tr>
<td><strong>Total Tier 2 Capital</strong></td>
<td>3,155</td>
<td>2,491</td>
</tr>
<tr>
<td><strong>Total Tier 1 and Tier 2 Capital</strong></td>
<td>15,846</td>
<td>13,424</td>
</tr>
<tr>
<td>Less: Holdings of other Banks/Financial Associates (2)</td>
<td>1,797</td>
<td>1,808</td>
</tr>
<tr>
<td><strong>Capital Base</strong></td>
<td>14,049</td>
<td>11,616</td>
</tr>
</tbody>
</table>

### Risk Adjusted Capital Ratios

<table>
<thead>
<tr>
<th></th>
<th>2006</th>
<th>2005</th>
</tr>
</thead>
<tbody>
<tr>
<td>Tier 1 (Statutory minimum ratio required is 5%)</td>
<td>10.23</td>
<td>10.87</td>
</tr>
<tr>
<td>Total (Statutory minimum ratio required is 10%)</td>
<td>11.32</td>
<td>11.55</td>
</tr>
</tbody>
</table>

### ADJUSTED ASSETS AND OFF-BALANCE SHEET EXPOSURE

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Rupees Million</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>ASSETS</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Cash, Treasury Bills, statutory reserves with Central Bank</td>
<td>31,263</td>
<td>24,138</td>
<td>0</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Loans secured by cash and guaranteed by Central Bank of Sri Lanka</td>
<td>30,582</td>
<td>26,204</td>
<td>0</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Guaranteed by OECD Central gov./Central banks</td>
<td>1,511</td>
<td>1,176</td>
<td>10</td>
<td>151</td>
<td>118</td>
</tr>
<tr>
<td>Due from Local/Foreign Banks/Financial Institutions</td>
<td>18,216</td>
<td>17,023</td>
<td>20</td>
<td>3,643</td>
<td>3,405</td>
</tr>
<tr>
<td>Loans secured by residential properties</td>
<td>26,628</td>
<td>24,889</td>
<td><strong>55</strong></td>
<td>14,645</td>
<td>12,443</td>
</tr>
<tr>
<td>Loans guaranteed by external agencies</td>
<td>4,812</td>
<td>4,017</td>
<td>50</td>
<td>2,406</td>
<td>2,009</td>
</tr>
<tr>
<td>Loans and advances secured by: Other forms of securities</td>
<td>70,517</td>
<td>56,222</td>
<td><strong>110</strong></td>
<td>77,569</td>
<td>56,222</td>
</tr>
<tr>
<td>Other assets</td>
<td>11,697</td>
<td>10,809</td>
<td>100</td>
<td>11,697</td>
<td>10,809</td>
</tr>
<tr>
<td><strong>Total assets</strong></td>
<td>195,226</td>
<td>164,478</td>
<td>110</td>
<td>110,111</td>
<td>85,006</td>
</tr>
</tbody>
</table>
## OFF-BALANCE SHEET EXPOSURE

<table>
<thead>
<tr>
<th>Rupees Million</th>
<th>Amount of Off-Balance Sheet Items</th>
<th>Credit Equivalent Amount</th>
<th>Risk Weights</th>
<th>Risk Weighted Balance</th>
</tr>
</thead>
<tbody>
<tr>
<td>As at 31st December</td>
<td>2006</td>
<td>2006</td>
<td>% 2006</td>
<td>2005</td>
</tr>
<tr>
<td>Financial guarantees, Bank acceptances and other guarantees</td>
<td>11,355</td>
<td>11,355</td>
<td>0 - 100</td>
<td>11,355</td>
</tr>
<tr>
<td>Performance related guarantees and warranties, stand by credit lines</td>
<td>5,178</td>
<td>2,589</td>
<td>0 - 100</td>
<td>1,495</td>
</tr>
<tr>
<td>Shipping guarantees, Documentary</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Letter of Credit</td>
<td>10,965</td>
<td>2,193</td>
<td>0 - 100</td>
<td>-</td>
</tr>
<tr>
<td>Undrawn term and overdraft facilities</td>
<td>18,594</td>
<td>-</td>
<td>0 - 100</td>
<td>-</td>
</tr>
<tr>
<td>&lt; 1 year</td>
<td>4,321</td>
<td>2,160</td>
<td>0 - 100</td>
<td>194</td>
</tr>
<tr>
<td>&gt; 1 year</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Foreign Exchange Contracts</td>
<td>10,065</td>
<td>201</td>
<td>0 - 100</td>
<td>-</td>
</tr>
<tr>
<td>Foreign Interest rate Contracts</td>
<td>5,532</td>
<td>387</td>
<td>0 - 100</td>
<td>-</td>
</tr>
<tr>
<td>Total off- balance sheet exposures</td>
<td>66,010</td>
<td>18,885</td>
<td>13,044</td>
<td>15,534</td>
</tr>
<tr>
<td>Total risk adjusted assets</td>
<td>110,111</td>
<td>85,006</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

## CAPITAL CHARGE FOR MARKET RISK

(With effect from 31st March 2006)

<table>
<thead>
<tr>
<th>Rupees Million</th>
<th>Capital charge</th>
<th>Risk adjusted assets</th>
</tr>
</thead>
<tbody>
<tr>
<td>As at 31st December</td>
<td>2006</td>
<td>2006</td>
</tr>
<tr>
<td>Interest rate</td>
<td>1.5</td>
<td>15</td>
</tr>
<tr>
<td>Equity</td>
<td>54.6</td>
<td>56</td>
</tr>
<tr>
<td>Foreign Exchange and Gold</td>
<td>34.7</td>
<td>34.7</td>
</tr>
<tr>
<td>Total risk adjusted assets for market risk</td>
<td>90.8</td>
<td>908</td>
</tr>
<tr>
<td>Total risk adjusted assets for credit risk, market risk and off - balance sheet exposure</td>
<td>124,063</td>
<td>100,540</td>
</tr>
</tbody>
</table>

## NOTES:

1. The Central Bank of Sri Lanka permits only 50% of the revaluation gains to be taken to the Tier 2 Capital.

2. Holdings of other Banks/ Financial Associates

<table>
<thead>
<tr>
<th></th>
<th>2006</th>
<th>2005</th>
</tr>
</thead>
<tbody>
<tr>
<td>Rs. Mn.</td>
<td>Rs. Mn.</td>
<td></td>
</tr>
<tr>
<td>Additional Investment in Sithma Development (Pvt) Ltd.</td>
<td>900</td>
<td>900</td>
</tr>
<tr>
<td>Employee share option plan</td>
<td>145</td>
<td>135</td>
</tr>
<tr>
<td>Others</td>
<td>752</td>
<td>773</td>
</tr>
</tbody>
</table>

3. The Capital Adequacy computation has been indicated for the Bank only.

   ** The risk weightings of these two types of assets in year 2005 were 50% and 100%.

   These two weightings have been increased to 55% and 110% respectively with effect from December 2006.
## Income Statement in US Dollars

### For the year ended 31st December 2006

<table>
<thead>
<tr>
<th></th>
<th>Bank</th>
<th>Group</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>2006</td>
<td>2005</td>
</tr>
<tr>
<td></td>
<td>US$.000</td>
<td>US$.000</td>
</tr>
<tr>
<td><strong>INCOME</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Interest income</td>
<td>171,726</td>
<td>138,393</td>
</tr>
<tr>
<td>Less: Interest expenses</td>
<td>91,363</td>
<td>71,311</td>
</tr>
<tr>
<td><strong>Net interest income</strong></td>
<td>80,363</td>
<td>67,082</td>
</tr>
<tr>
<td>Foreign exchange profit</td>
<td>7,374</td>
<td>6,332</td>
</tr>
<tr>
<td>Fee and commission income</td>
<td>16,709</td>
<td>16,293</td>
</tr>
<tr>
<td>Dividend income</td>
<td>716</td>
<td>637</td>
</tr>
<tr>
<td>Other income</td>
<td>3,691</td>
<td>4,019</td>
</tr>
<tr>
<td><strong>OPERATING INCOME</strong></td>
<td>108,853</td>
<td>94,363</td>
</tr>
</tbody>
</table>

Less:

**OPERATING EXPENSES**

<table>
<thead>
<tr>
<th>Expense</th>
<th>Bank</th>
<th>Group</th>
</tr>
</thead>
<tbody>
<tr>
<td>Personnel costs</td>
<td>25,740</td>
<td>23,656</td>
</tr>
<tr>
<td>Premises equipment and establishment expenses</td>
<td>17,730</td>
<td>16,971</td>
</tr>
<tr>
<td>Fee and commission expenses</td>
<td>950</td>
<td>1,142</td>
</tr>
<tr>
<td>Provision for staff retirement benefits</td>
<td>3,715</td>
<td>3,197</td>
</tr>
<tr>
<td>Bad debts written off</td>
<td>114</td>
<td>230</td>
</tr>
<tr>
<td>Provision for loan losses</td>
<td>8,672</td>
<td>17,233</td>
</tr>
<tr>
<td>Provision for fall in value of investment</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Amortization of goodwill/(negative goodwill)</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Other expenses</td>
<td>23,831</td>
<td>13,815</td>
</tr>
<tr>
<td><strong>PROFIT FROM OPERATIONS</strong></td>
<td>80,752</td>
<td>76,244</td>
</tr>
</tbody>
</table>

**PROFIT BEFORE TAXATION**

<table>
<thead>
<tr>
<th></th>
<th>Bank</th>
<th>Group</th>
</tr>
</thead>
<tbody>
<tr>
<td>Share of Associate Companies’ profit before taxation</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td><strong>PROFIT BEFORE TAXATION</strong></td>
<td>28,101</td>
<td>18,119</td>
</tr>
</tbody>
</table>

Less: Income tax expense 7,436 1,914 7,627 2,094

**PROFIT FOR THE PERIOD**

<table>
<thead>
<tr>
<th></th>
<th>Bank</th>
<th>Group</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>PROFIT FOR THE PERIOD</strong></td>
<td>20,665</td>
<td>16,205</td>
</tr>
</tbody>
</table>

**Attributable to:**

<table>
<thead>
<tr>
<th>Category</th>
<th>Bank</th>
<th>Group</th>
</tr>
</thead>
<tbody>
<tr>
<td>Equity Holders of the Bank</td>
<td>20,665</td>
<td>16,205</td>
</tr>
<tr>
<td>Minority Interest</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td><strong>PROFIT FOR THE PERIOD</strong></td>
<td>20,665</td>
<td>16,205</td>
</tr>
</tbody>
</table>

**BASIC EARNINGS PER SHARE (US$)**

<table>
<thead>
<tr>
<th></th>
<th>Bank</th>
<th>Group</th>
</tr>
</thead>
<tbody>
<tr>
<td>0.18</td>
<td>0.15</td>
<td>0.18</td>
</tr>
</tbody>
</table>

**DIVIDEND PER SHARE (US$)**

<table>
<thead>
<tr>
<th></th>
<th>Bank</th>
<th>Group</th>
</tr>
</thead>
<tbody>
<tr>
<td>*0.05</td>
<td>0.04</td>
<td>*0.05</td>
</tr>
</tbody>
</table>

---

*Exchange rate of US$ 1 was Rs. 107.45 as at 31.12.2006 (Rs. 102.10 as at 31.12.2005)*

*Calculated on Interim Dividend paid and Final Dividend proposed, which is to be approved at the Annual General Meeting.*

The Income Statement given on this page is solely for the convenience of the shareholders, bankers, investors, customers and other users of financial statements and do not form part of the audited financial statements.
## Balance Sheet in US Dollars

### As at 31st December

<table>
<thead>
<tr>
<th></th>
<th>2006</th>
<th>2005</th>
<th>2006</th>
<th>2005</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>US$.000</td>
<td>US$.000</td>
<td>US$.000</td>
<td>US$.000</td>
</tr>
<tr>
<td><strong>ASSETS</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Cash and cash equivalents</td>
<td>216,920</td>
<td>207,640</td>
<td>217,253</td>
<td>207,580</td>
</tr>
<tr>
<td>Statutory deposit with Central Bank of Sri Lanka</td>
<td>111,834</td>
<td>83,894</td>
<td>111,834</td>
<td>83,894</td>
</tr>
<tr>
<td>Government Treasury Bills</td>
<td>-</td>
<td>1,365</td>
<td>22,817</td>
<td>19,602</td>
</tr>
<tr>
<td>Commercial papers</td>
<td>2,705</td>
<td>4,251</td>
<td>2,705</td>
<td>4,251</td>
</tr>
<tr>
<td>Securities purchased under re-sale agreements</td>
<td>-</td>
<td>-</td>
<td>40,887</td>
<td>38,014</td>
</tr>
<tr>
<td>Dealing securities</td>
<td>6,875</td>
<td>3,067</td>
<td>9,075</td>
<td>3,131</td>
</tr>
<tr>
<td>Investment securities</td>
<td>195,503</td>
<td>169,294</td>
<td>210,886</td>
<td>184,297</td>
</tr>
<tr>
<td>Bills of Exchange</td>
<td>17,784</td>
<td>19,853</td>
<td>17,784</td>
<td>19,853</td>
</tr>
<tr>
<td>Securities purchased under re-sale agreements</td>
<td>-</td>
<td>-</td>
<td>40,887</td>
<td>38,014</td>
</tr>
<tr>
<td>Dealing securities</td>
<td>6,875</td>
<td>3,067</td>
<td>9,075</td>
<td>3,131</td>
</tr>
<tr>
<td>Investment securities</td>
<td>195,503</td>
<td>169,294</td>
<td>210,886</td>
<td>184,297</td>
</tr>
<tr>
<td>Bills of Exchange</td>
<td>17,784</td>
<td>19,853</td>
<td>17,784</td>
<td>19,853</td>
</tr>
<tr>
<td>Loans and advances</td>
<td>1,047,551</td>
<td>942,629</td>
<td>1,063,535</td>
<td>937,079</td>
</tr>
<tr>
<td>Lease rentals receivable within one year</td>
<td>35,329</td>
<td>30,485</td>
<td>35,329</td>
<td>30,485</td>
</tr>
<tr>
<td>Lease rentals receivable after one year</td>
<td>72,186</td>
<td>56,336</td>
<td>72,186</td>
<td>56,336</td>
</tr>
<tr>
<td>Non-current assets held for sale</td>
<td>1,767</td>
<td>1,722</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Property, Plant and Equipment</td>
<td>27,042</td>
<td>29,966</td>
<td>68,735</td>
<td>73,974</td>
</tr>
<tr>
<td>Intangible assets</td>
<td>2,159</td>
<td>3,045</td>
<td>2,417</td>
<td>3,324</td>
</tr>
<tr>
<td>Other assets</td>
<td>47,784</td>
<td>50,393</td>
<td>47,518</td>
<td>50,389</td>
</tr>
<tr>
<td><strong>Total Assets</strong></td>
<td>1,828,097</td>
<td>1,625,979</td>
<td>1,926,278</td>
<td>1,713,880</td>
</tr>
<tr>
<td><strong>LIABILITIES</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Deposits from customers</td>
<td>1,376,287</td>
<td>1,256,451</td>
<td>1,375,410</td>
<td>1,254,954</td>
</tr>
<tr>
<td>Dividends payable</td>
<td>355</td>
<td>493</td>
<td>355</td>
<td>493</td>
</tr>
<tr>
<td>Borrowings</td>
<td>102,666</td>
<td>102,666</td>
<td>38,951</td>
<td>38,951</td>
</tr>
<tr>
<td>Securities sold under re-purchase agreements</td>
<td>62,696</td>
<td>59,879</td>
<td>129,294</td>
<td>118,549</td>
</tr>
<tr>
<td>Bills payable</td>
<td>11,076</td>
<td>21,809</td>
<td>11,075</td>
<td>21,809</td>
</tr>
<tr>
<td>Long-term insurance funds</td>
<td>-</td>
<td>-</td>
<td>4,725</td>
<td>2,946</td>
</tr>
<tr>
<td>Non-life insurance reserves</td>
<td>-</td>
<td>-</td>
<td>2,974</td>
<td>2,615</td>
</tr>
<tr>
<td>Subordinated debentures</td>
<td>47,650</td>
<td>39,177</td>
<td>65,923</td>
<td>58,539</td>
</tr>
<tr>
<td>Current tax liability</td>
<td>7,089</td>
<td>59</td>
<td>7,204</td>
<td>56</td>
</tr>
<tr>
<td>Deferred tax liability</td>
<td>2,920</td>
<td>3,073</td>
<td>2,957</td>
<td>3,098</td>
</tr>
<tr>
<td>Other liabilities</td>
<td>97,025</td>
<td>96,366</td>
<td>101,816</td>
<td>100,708</td>
</tr>
<tr>
<td><strong>Total Liabilities</strong></td>
<td>1,707,764</td>
<td>1,515,898</td>
<td>1,804,399</td>
<td>1,602,663</td>
</tr>
<tr>
<td><strong>EQUITY</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Share capital - Voting</td>
<td>8,810</td>
<td>9,272</td>
<td>8,810</td>
<td>9,272</td>
</tr>
<tr>
<td>Share capital - Non-Voting</td>
<td>2,150</td>
<td>2,262</td>
<td>2,150</td>
<td>2,262</td>
</tr>
<tr>
<td>Statutory Reserve Fund</td>
<td>6,233</td>
<td>6,119</td>
<td>6,233</td>
<td>6,119</td>
</tr>
<tr>
<td>Retained Earnings</td>
<td>16,160</td>
<td>11,503</td>
<td>16,028</td>
<td>11,182</td>
</tr>
<tr>
<td>Other reserves</td>
<td>86,980</td>
<td>80,925</td>
<td>86,980</td>
<td>80,925</td>
</tr>
<tr>
<td><strong>Total Equity attributable to Equity Holders of the Bank</strong></td>
<td>120,333</td>
<td>110,081</td>
<td>120,201</td>
<td>109,760</td>
</tr>
<tr>
<td>Minority Interest</td>
<td>-</td>
<td>-</td>
<td>1,678</td>
<td>1,457</td>
</tr>
<tr>
<td><strong>Total Equity</strong></td>
<td>120,333</td>
<td>110,081</td>
<td>121,879</td>
<td>111,217</td>
</tr>
<tr>
<td><strong>Total Liabilities and Equity</strong></td>
<td>1,828,097</td>
<td>1,625,979</td>
<td>1,926,278</td>
<td>1,713,880</td>
</tr>
<tr>
<td>Commitments and Contingencies</td>
<td>416,865</td>
<td>438,425</td>
<td>416,865</td>
<td>438,425</td>
</tr>
</tbody>
</table>

Exchange rate of US$ 1 was Rs. 107.45 as at 31.12.2006 (Rs. 102.10 as at 31.12.2005)

The Balance Sheet given on this page is solely for the convenience of the shareholders, bankers, investors, customers and other users of financial statements and do not form part of the audited financial statements.
## Analysis of Deposits

<table>
<thead>
<tr>
<th></th>
<th>2002</th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Local Currency Deposits</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Current</td>
<td>6,191,913</td>
<td>7,929,485</td>
<td>8,852,609</td>
<td>12,511,256</td>
<td>12,635,473</td>
</tr>
<tr>
<td>Savings</td>
<td>30,627,485</td>
<td>36,452,976</td>
<td>42,108,475</td>
<td>47,380,753</td>
<td>50,697,086</td>
</tr>
<tr>
<td>Time</td>
<td>19,872,255</td>
<td>23,502,610</td>
<td>31,920,537</td>
<td>33,587,699</td>
<td>48,869,303</td>
</tr>
<tr>
<td>Certificate of Deposits</td>
<td>6,677,438</td>
<td>5,861,618</td>
<td>4,448,095</td>
<td>3,634,393</td>
<td>3,348,716</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>63,369,091</td>
<td>73,746,689</td>
<td>87,329,716</td>
<td>97,114,101</td>
<td>115,550,578</td>
</tr>
</tbody>
</table>

| **Foreign Currency Deposits** |        |        |        |        |        |
| Current          | 1,679,540 | 1,154,625 | 2,331,555 | 1,013,589 | 1,188,634 |
| Savings          | 11,171,199 | 11,936,063 | 15,009,655 | 14,166,198 | 13,600,463 |
| Time             | 11,664,587 | 14,188,135 | 13,853,008 | 15,989,793 | 17,542,350 |
| **Total**        | 24,515,326 | 27,278,823 | 31,194,218 | 31,169,580 | 32,331,447 |

| **Total Deposits** | 87,884,417 | 101,025,513 | 118,523,934 | 128,283,681 | 147,882,025 |
| **Refinance**     | 1,659,069 | 1,764,014 | 2,066,198 | 2,711,810 | 3,582,587 |
| **Total Deposits and Refinance** | 89,543,486 | 102,789,527 | 120,590,132 | 130,995,491 | 151,464,612 |

---

### Analysis of Local Currency Deposits

#### 2002-2006

- **Current**
- **Savings**
- **Time**

<table>
<thead>
<tr>
<th>Year</th>
<th>Current</th>
<th>Savings</th>
<th>Time</th>
</tr>
</thead>
<tbody>
<tr>
<td>2002</td>
<td>6,191,913</td>
<td>30,627,485</td>
<td>19,872,255</td>
</tr>
<tr>
<td>2003</td>
<td>7,929,485</td>
<td>36,452,976</td>
<td>23,502,610</td>
</tr>
<tr>
<td>2004</td>
<td>8,852,609</td>
<td>42,108,475</td>
<td>31,920,537</td>
</tr>
<tr>
<td>2005</td>
<td>12,511,256</td>
<td>47,380,753</td>
<td>33,587,699</td>
</tr>
<tr>
<td>2006</td>
<td>12,635,473</td>
<td>50,697,086</td>
<td>48,869,303</td>
</tr>
</tbody>
</table>

### Analysis of Foreign Currency Deposits

#### 2002-2006

- **Current**
- **Savings**
- **Time**

<table>
<thead>
<tr>
<th>Year</th>
<th>Current</th>
<th>Savings</th>
<th>Time</th>
</tr>
</thead>
<tbody>
<tr>
<td>2002</td>
<td>1,679,540</td>
<td>11,171,199</td>
<td>11,664,587</td>
</tr>
<tr>
<td>2003</td>
<td>1,154,625</td>
<td>11,936,063</td>
<td>14,188,135</td>
</tr>
<tr>
<td>2004</td>
<td>2,331,555</td>
<td>15,009,655</td>
<td>13,853,008</td>
</tr>
<tr>
<td>2005</td>
<td>1,013,589</td>
<td>14,166,198</td>
<td>15,989,793</td>
</tr>
<tr>
<td>2006</td>
<td>1,188,634</td>
<td>13,600,463</td>
<td>17,542,350</td>
</tr>
</tbody>
</table>

---

### Analysis of Total Deposits

#### 2002-2006

<table>
<thead>
<tr>
<th>Year</th>
<th>Total Deposits</th>
<th>Refinance</th>
</tr>
</thead>
<tbody>
<tr>
<td>2002</td>
<td>87,884,417</td>
<td>1,659,069</td>
</tr>
<tr>
<td>2003</td>
<td>101,025,513</td>
<td>1,764,014</td>
</tr>
<tr>
<td>2004</td>
<td>118,523,934</td>
<td>2,066,198</td>
</tr>
<tr>
<td>2005</td>
<td>128,283,681</td>
<td>2,711,810</td>
</tr>
<tr>
<td>2006</td>
<td>147,882,025</td>
<td>3,582,587</td>
</tr>
</tbody>
</table>

---

### Analysis of Local Currency Deposits

#### Graphs

- **Local Currency Deposits**
- **Foreign Currency Deposits**
- **Total Deposits and Refinance**
### Analysis of Advances

<table>
<thead>
<tr>
<th></th>
<th>2002</th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Rs.000</td>
<td>Rs.000</td>
<td>Rs.000</td>
<td>Rs.000</td>
<td>Rs.000</td>
</tr>
<tr>
<td>Local Currency Advances</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Overdrafts</td>
<td>16,786,380</td>
<td>17,247,347</td>
<td>20,165,063</td>
<td>22,952,834</td>
<td>27,455,224</td>
</tr>
<tr>
<td>Trust Receipts</td>
<td>4,228,258</td>
<td>3,880,713</td>
<td>4,957,006</td>
<td>5,193,080</td>
<td>6,876,898</td>
</tr>
<tr>
<td>Packing Credit</td>
<td>329,217</td>
<td>557,260</td>
<td>521,945</td>
<td>523,517</td>
<td>618,787</td>
</tr>
<tr>
<td>Term Loans</td>
<td>32,757,990</td>
<td>41,880,705</td>
<td>50,714,867</td>
<td>58,657,612</td>
<td>68,451,741</td>
</tr>
<tr>
<td></td>
<td>54,101,845</td>
<td>63,566,025</td>
<td>76,358,881</td>
<td>87,327,043</td>
<td>103,402,650</td>
</tr>
<tr>
<td>Leasing Facilities</td>
<td>4,032,043</td>
<td>5,084,773</td>
<td>6,838,367</td>
<td>8,864,351</td>
<td>11,552,475</td>
</tr>
<tr>
<td>Total</td>
<td>58,133,888</td>
<td>68,650,798</td>
<td>83,197,248</td>
<td>96,191,394</td>
<td>114,955,125</td>
</tr>
<tr>
<td>Foreign Currency Advances</td>
<td>10,195,368</td>
<td>12,314,964</td>
<td>13,702,580</td>
<td>15,381,438</td>
<td>18,412,257</td>
</tr>
<tr>
<td>Total</td>
<td>68,329,256</td>
<td>80,965,762</td>
<td>96,899,828</td>
<td>111,572,832</td>
<td>133,367,382</td>
</tr>
</tbody>
</table>

**Analysis of Advances - 2006**

- Local Currency Advances (86%)
- Foreign Currency Advances (14%)
- Overdrafts (24%)
- Trust Receipts (6%)
- Packing Credit (1%)
- Term Loans (59%)
- Leasing Facilities (10%)

**Analysis of Advances by Security - 2006**

- Secured by cash, quoted shares & other readily realisable assets (16%)
- Secured by mortgage over immovable assets (25%)
- Secured by mortgage over movable assets (23%)
- Others (clean and third party guarantees) (26%)
Provincewise Analysis of Deposits & Advances

as at 31st December 2006

<table>
<thead>
<tr>
<th>Province</th>
<th>No of Customer Centres</th>
<th>Deposits [Rs. Mn.]</th>
<th>%</th>
<th>Advances Including Leasing [Rs. Mn.]</th>
<th>%</th>
<th>Deposit Utilisation %</th>
</tr>
</thead>
<tbody>
<tr>
<td>Western</td>
<td>82</td>
<td>106,612</td>
<td>72</td>
<td>101,520</td>
<td>76</td>
<td>94</td>
</tr>
<tr>
<td>Southern</td>
<td>12</td>
<td>5,498</td>
<td>4</td>
<td>5,744</td>
<td>4</td>
<td>104</td>
</tr>
<tr>
<td>Uva</td>
<td>6</td>
<td>2,884</td>
<td>2</td>
<td>2,642</td>
<td>2</td>
<td>92</td>
</tr>
<tr>
<td>North Central</td>
<td>4</td>
<td>2,239</td>
<td>2</td>
<td>2,058</td>
<td>2</td>
<td>92</td>
</tr>
<tr>
<td>North Western</td>
<td>8</td>
<td>5,136</td>
<td>3</td>
<td>5,275</td>
<td>4</td>
<td>103</td>
</tr>
<tr>
<td>Eastern</td>
<td>8</td>
<td>5,001</td>
<td>3</td>
<td>2,948</td>
<td>2</td>
<td>59</td>
</tr>
<tr>
<td>Northern</td>
<td>7</td>
<td>7,116</td>
<td>5</td>
<td>2,970</td>
<td>2</td>
<td>42</td>
</tr>
<tr>
<td>Sabaragamuwa</td>
<td>9</td>
<td>3,709</td>
<td>3</td>
<td>3,165</td>
<td>3</td>
<td>85</td>
</tr>
<tr>
<td>Central</td>
<td>15</td>
<td>9,687</td>
<td>6</td>
<td>7,045</td>
<td>5</td>
<td>73</td>
</tr>
<tr>
<td>Total</td>
<td>151</td>
<td>147,882</td>
<td>100</td>
<td>133,367</td>
<td>100</td>
<td>90</td>
</tr>
</tbody>
</table>
### Sources of Income

For the year ended 31st December

<table>
<thead>
<tr>
<th>Year</th>
<th>2002</th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Rs.000</td>
<td>Rs.000</td>
<td>Rs.000</td>
<td>Rs.000</td>
<td>Rs.000</td>
</tr>
<tr>
<td>Interest</td>
<td>9,398,781</td>
<td>11,536,552</td>
<td>11,469,335</td>
<td>14,129,874</td>
<td>18,451,961</td>
</tr>
<tr>
<td>Exchange</td>
<td>382,272</td>
<td>506,436</td>
<td>662,176</td>
<td>646,460</td>
<td>792,303</td>
</tr>
<tr>
<td>Commission</td>
<td>755,384</td>
<td>1,241,588</td>
<td>1,519,924</td>
<td>1,663,545</td>
<td>1,795,340</td>
</tr>
<tr>
<td>Investments</td>
<td>303,507</td>
<td>356,830</td>
<td>288,193</td>
<td>329,322</td>
<td>225,722</td>
</tr>
<tr>
<td>Other</td>
<td>959,485</td>
<td>1,189,156</td>
<td>147,730</td>
<td>146,113</td>
<td>247,847</td>
</tr>
<tr>
<td>Total</td>
<td>11,799,429</td>
<td>14,830,562</td>
<td>14,087,357</td>
<td>16,915,314</td>
<td>21,513,173</td>
</tr>
</tbody>
</table>

### Utilisation of Income

For the year ended 31st December

<table>
<thead>
<tr>
<th>Year</th>
<th>2002</th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Rs.000</td>
<td>Rs.000</td>
<td>Rs.000</td>
<td>Rs.000</td>
<td>Rs.000</td>
</tr>
<tr>
<td>Employees</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Salaries and other payments to staff</td>
<td>1,778,250</td>
<td>2,320,427</td>
<td>2,414,137</td>
<td>2,741,656</td>
<td>3,164,917</td>
</tr>
<tr>
<td>Suppliers</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Interest paid</td>
<td>6,257,761</td>
<td>6,909,095</td>
<td>5,962,041</td>
<td>7,280,851</td>
<td>9,816,927</td>
</tr>
<tr>
<td>Other expenses</td>
<td>3,004,516</td>
<td>4,440,289</td>
<td>4,418,999</td>
<td>4,922,800</td>
<td>4,529,175</td>
</tr>
<tr>
<td>Total</td>
<td>9,262,277</td>
<td>11,349,384</td>
<td>10,381,040</td>
<td>12,203,651</td>
<td>14,346,102</td>
</tr>
<tr>
<td>Net Income before Government Taxes &amp; Levies</td>
<td>758,902</td>
<td>1,160,751</td>
<td>1,292,180</td>
<td>1,970,007</td>
<td>4,002,153</td>
</tr>
</tbody>
</table>

### Government

Provision for Income tax, Provision for financial services VAT, Debit Tax and Defence Levy/National Security Levy

| Security Levy| 170,052 | 152,466 | 315,799 | 396,910 | 1,781,665 |

### Shareholders

| Dividends| 214,500 | 286,000 | 350,350 | 471,059 | 588,824 |
| Retained Profit| 374,350 | 722,285 | 626,031 | 1,102,038 | 1,631,665 |
| Total| 11,799,429 | 14,830,562| 14,087,357| 16,915,314| 21,513,173|

**Sources & Utilisation of Income - 2006**

- **Interest (85%)**
- **Exchange (4%)**
- **Commission (8%)**
- **Investment (1%)**
- **Other (2%)**
- **Suppliers (66%)**
- **Employees (15%)**
- **Net income before Taxes & Levies (19%)**
- **Government taxes (46%)**
- **Dividends (7%)**
- **Retained profits (47%)**

Within the context of the economy at large, the Bank acts as a financial intermediary with revenues from customers flowing to employees, depositors, the government and shareholders. The Bank retains part of the shareholder segment to support future growth and investments.
## Value Added Statement

### 2006 | % | 2005 | %
---|---|---|---
**Value added** |  |  |  |
Income earned by providing banking services | 21,248,724 |  | 16,581,974 |  |
Cost of services | 12,882,663 |  | 9,868,421 |  |
Value added by banking services | 8,366,061 |  | 6,713,553 |  |
Non-banking income | 264,449 |  | 333,340 |  |
Provision for bad debts | (931,828) |  | (1,759,444) |  |
**7,698,682** |  |  | **5,287,449** |  |

**Value allocated to employees** |  |  |  |
Salaries, wages and other benefits | 3,164,918 | 41.11 | 2,741,656 | 51.85 |
**To providers of capital** |  |  |  |
Dividends to shareholders | 588,824 | 7.65 | 471,059 | 8.91 |
**To Government** |  |  |  |
Provision for financial services VAT | 972,657 |  | 194,000 |  |
Provision for Income Tax | 798,961 |  | 232,000 |  |
Debit Tax | 8,977 |  | 7,510 |  |
Stamp Duty | 1,070 | 1,781,665 | 23.14 | - | 433,510 | 8.20 |
**To expansion and growth** |  |  |  |
Retained income | 1,631,665 | 21.19 | 1,183,503 | 22.38 |
Depreciation/Amortization | 531,611 | 6.91 | 494,321 | 9.35 |
Deferred taxation | - | - | (36,600) | (0.69) |
**7,698,682** | **100.00** |  | **5,287,449** | **100.00** |

### Analysis of Value Addition

- **Value allocated to employees** 2006 - (41.11%) 2005 - (51.85%)
- **To providers of capital** 2006 - (6.12%) 2005 - (8.91%)
- **To Government** 2006 - (23.14%) 2005 - (8.20%)
- **To expansion and growth** 2006 - (29.63%) 2005 - (31.04%)
### Quarterly Statistics

<table>
<thead>
<tr>
<th></th>
<th>2006</th>
<th></th>
<th>2005</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>December</td>
<td>September</td>
<td>June</td>
<td>March</td>
</tr>
<tr>
<td><strong>Balance Sheet Data</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>(Rs. Million)</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total Assets</td>
<td>196,429</td>
<td>187,196</td>
<td>178,416</td>
<td>174,652</td>
</tr>
<tr>
<td>Loans, Leases and Bills</td>
<td>136,053</td>
<td>129,091</td>
<td>121,327</td>
<td>116,487</td>
</tr>
<tr>
<td>Deposits</td>
<td>147,882</td>
<td>141,063</td>
<td>137,623</td>
<td>133,089</td>
</tr>
<tr>
<td>Shareholders' Funds</td>
<td>12,930</td>
<td>12,347</td>
<td>11,758</td>
<td>11,264</td>
</tr>
<tr>
<td>Average Assets</td>
<td>191,813</td>
<td>182,806</td>
<td>176,534</td>
<td>170,332</td>
</tr>
<tr>
<td><strong>Income Statement Data</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>(Rs.000)</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Net Interest Income</td>
<td>2,386,120</td>
<td>2,270,315</td>
<td>2,166,387</td>
<td>1,915,135</td>
</tr>
<tr>
<td>Foreign Exchange Profit</td>
<td>264,603</td>
<td>186,993</td>
<td>171,738</td>
<td>168,969</td>
</tr>
<tr>
<td>Other Income</td>
<td>756,163</td>
<td>504,157</td>
<td>498,368</td>
<td>366,044</td>
</tr>
<tr>
<td>Total Revenue</td>
<td>3,406,886</td>
<td>2,961,465</td>
<td>2,836,493</td>
<td>2,450,148</td>
</tr>
<tr>
<td>Provision for Loan Losses</td>
<td>(330,012)</td>
<td>(93,717)</td>
<td>(115,211)</td>
<td>(195,973)</td>
</tr>
<tr>
<td>Non-interest Expenses</td>
<td>(1,982,864)</td>
<td>(2,078,764)</td>
<td>(1,997,394)</td>
<td>(1,841,607)</td>
</tr>
<tr>
<td>Provision for Income Tax</td>
<td>(233,864)</td>
<td>(200,615)</td>
<td>(121,248)</td>
<td>(152,062)</td>
</tr>
<tr>
<td><strong>Ordinary Share Information</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Market Price per share (Rs.)</td>
<td>V NV V NV V NV V NV V NV</td>
<td>V NV V NV V NV V NV</td>
<td>161.00 74.25 120.00 53.75 122.00 58.50 133.50 60.75 148.00 65.75 119.00 64.00 85.50 46.00 62.50 45.00</td>
<td></td>
</tr>
<tr>
<td>High</td>
<td>115.75</td>
<td>70.00</td>
<td>59.00</td>
<td>43.00</td>
</tr>
<tr>
<td>Low</td>
<td>109.79</td>
<td>104.84</td>
<td>99.85</td>
<td>95.65</td>
</tr>
<tr>
<td>Closing</td>
<td>115.75</td>
<td>70.00</td>
<td>59.00</td>
<td>43.00</td>
</tr>
<tr>
<td>Book value per Ordinary Share</td>
<td>V NV V NV V NV V NV</td>
<td>V NV V NV V NV V NV</td>
<td>51.75 32.50 78.00 42.50 57.50 37.50 51.75 32.25</td>
<td></td>
</tr>
<tr>
<td>V - Voting NV - Non-Voting</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

### Financial Measures

#### Profitability
- **Return on Average Shareholders' Equity**
  - 6.01% 4.88% 4.44% 2.32%
- **Return on Total Revenue**
  - 5.72% 3.98% 3.55% 2.72%

#### Productivity
- **Non-interest Expenses to Total Revenue**
  - 58.20% 70.19% 70.42% 75.16%
- **Capital**
  - **Risk weighted capital ratios**
    - **Tier 1**
      - 10.23% 9.88% 12.05% 10.78%
    - **Tier (Tier 1 + 2)**
      - 11.32% 10.86% 12.02% 12.32%

#### Asset Quality
- **Provision for Credit losses to average loans**
  - 0.25% 0.07% 0.10% 0.17%
- ***2006 figures are based on both credit risk and market risk**
### Ten Year Statistical Summary

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>OPERATING RESULTS</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Income</strong></td>
<td>6,116</td>
<td>6,704</td>
<td>7,723</td>
<td>9,641</td>
<td>11,564</td>
<td>11,799</td>
<td>14,831</td>
<td>14,087</td>
<td>16,915</td>
<td>21,513</td>
</tr>
<tr>
<td><strong>Interest Income</strong></td>
<td>4,964</td>
<td>5,400</td>
<td>6,480</td>
<td>7,940</td>
<td>9,336</td>
<td>9,399</td>
<td>11,537</td>
<td>11,469</td>
<td>14,130</td>
<td>18,452</td>
</tr>
<tr>
<td><strong>Interest Expenses</strong></td>
<td>3,355</td>
<td>3,316</td>
<td>4,088</td>
<td>7,201</td>
<td>6,258</td>
<td>6,909</td>
<td>5,066</td>
<td>642</td>
<td>792</td>
<td></td>
</tr>
<tr>
<td><strong>Exchange Income</strong></td>
<td>757</td>
<td>868</td>
<td>930</td>
<td>1,337</td>
<td>1,712</td>
<td>2,018</td>
<td>2,788</td>
<td>1,956</td>
<td>2,269</td>
<td></td>
</tr>
<tr>
<td><strong>Operating Expenses</strong></td>
<td>2,036</td>
<td>2,531</td>
<td>2,741</td>
<td>3,411</td>
<td>4,061</td>
<td>4,873</td>
<td>6,830</td>
<td>7,175</td>
<td>7,781</td>
<td>9,817</td>
</tr>
<tr>
<td><strong>Profit before Income Tax</strong></td>
<td>725</td>
<td>858</td>
<td>894</td>
<td>949</td>
<td>301</td>
<td>669</td>
<td>1,092</td>
<td>950</td>
<td>1,850</td>
<td>3,019</td>
</tr>
<tr>
<td><strong>Income Tax on Profit</strong></td>
<td>172</td>
<td>175</td>
<td>176</td>
<td>149</td>
<td>(2)</td>
<td>80</td>
<td>83</td>
<td>26</td>
<td>195</td>
<td>799</td>
</tr>
<tr>
<td><strong>Profit after Taxation</strong></td>
<td>553</td>
<td>683</td>
<td>718</td>
<td>800</td>
<td>303</td>
<td>589</td>
<td>1,008</td>
<td>976</td>
<td>1,655</td>
<td>2,220</td>
</tr>
</tbody>
</table>

| **SHAREHOLDERS’ FUNDS**          |      |      |      |      |      |      |      |      |      |      |
| **Share Capital**                | 200  | 300  | 650  | 650  | 650  | 715  | 1,001 | 1,178 | 1,178 | 1,178 |
| **Reserves**                     | 2,814| 3,237| 4,358| 4,898| 5,103| 6,278| 8,051 | 10,062| 11,752|       |

| **LIABILITIES**                  |      |      |      |      |      |      |      |      |      |      |
| **Customer Deposits**            | 39,303| 46,032| 53,858| 62,758| 75,599| 87,884| 101,026| 118,524| 128,284| 147,882|
| **Refinance Borrowings**         | 954  | 1,129 | 1,636 | 1,655 | 1,565 | 1,659 | 1,764 | 2,066 | 2,712 | 3,583 |
| **Other Liabilities**            | 9,243| 13,805| 15,732| 17,540| 15,999| 19,354| 23,161| 22,788| 23,463| 31,720|

| **ASSETS**                       |      |      |      |      |      |      |      |      |      |      |
| **Bills of Exchange**            | 3,935| 3,824| 3,122| 4,546| 3,153| 2,690| 2,412| 2,077| 2,027| 1,911 |
| **Loans and Advances**           | 28,343| 33,988| 40,328| 46,904| 49,006| 59,991| 71,426| 84,379| 96,242| 114,708|
| **Lease Rentals Receivable**     | 1,947| 2,078| 2,741| 2,969| 2,898| 4,032| 5,085| 6,838| 8,864| 11,552|

| **RATIOS**                       |      |      |      |      |      |      |      |      |      |      |
| **Return on Average Shareholders’ Funds (%)** | 20  | 21  | 17  | 15  | 5   | 10  | 15  | 12  | 16  | 18  |
| **Income Growth (%)**            | 28  | 10  | 15  | 25  | 20  | 2   | 26  | 5   | 20  | 27  |
| **Return on Average Assets (%)** | 1.2 | 1.2 | 1.0 | 1.0 | 0.3 | 0.6 | 0.8 | 0.7 | 1.0 | 1.2 |
| **Rate of Dividends (%)**        | 50  | 45  | 40  | 40  | 15  | 30  | 40  | 35  | 40  | 50  |
| **Dividend Cover (times)**       | 5.5 | 5.1 | 2.8 | 3.1 | 3.1 | 2.8 | 3.5 | 2.8 | 3.5 | 3.8 |
| **Gross Dividends (Rs. Mn.)**    | 100 | 125 | 104 | 104 | 156 | 215 | 286 | 350 | 471 | 589 |
| **Advance to Deposits & Refinance (%)** | 80 | 85 | 82 | 84 | 71 | 76 | 77 | 82 | 85 |       |
| **Property, Plant & Equipment to Shareholders’ Funds (%)** | 48 | 47 | 38 | 41 | 43 | 45 | 49 | 37 | 27 | 22 |
| **Total Assets to Shareholders’ Funds (times)** | 17 | 18 | 15 | 16 | 17 | 19 | 19 | 17 | 15 | 15 |

(As specified in Banking Act No. 30 of 1988)

|   | Capital Funds to Liabilities including Contingent Liabilities (%) | 1.2 | 1.2 | 1.0 | 1.2 | 1.2 | 1.2 | 1.0 | 1.0 | 1.0 | 1.0 |
|   | Liquid Assets to Liabilities (%)                                 | 23 | 27 | 25 | 25 | 28 | 32 | 27 | 25 | 24 | 22 |

| **SHARE INFORMATION**          |      |      |      |      |      |      |      |      |      |      |
| **Market Value per Share (Rs.)** | 225.00 | 174.00 | 87.00 | 46.25 | 52.00 | 79.00 | 69.00 | 57.00 | 112.50 | 155.75 |
| **- Voting**                    | -    | -    | -    | -    | 36.75 | 36.00 | 47.00 | 36.75 | 32.75 | 41.50 |
| **- Non-Voting**                | 7.51 | 9.27 | 9.75 | 10.86 | 4.11 | 8.00 | 13.69 | 12.51 | 15.07 | 18.86 |
| **Earnings per Share (Rs.)**    | 29.96 | 18.77 | 8.92 | 4.26 | 12.65 | 9.88 | 5.04 | 4.56 | 7.46 | 8.26 |
| **Price Earnings Ratio**        | 150.70 | 117.90 | 77.05 | 85.35 | 48.51 | 87.20 | 97.81 | 90.43 | 95.44 | 107.79 |

| **OTHER INFORMATION**          |      |      |      |      |      |      |      |      |      |      |
| **No. of Employees**            | 3,433| 3,744| 4,035| 4,119| 4,137| 4,280| 4,203| 4,180| 4,287 |
| **No. of Customer Centres**     | 92  | 103 | 111 | 117 | 123 | 137 | 138 | 142 | 150  |
| **No. of other Financial Centres** | 61 | 72 | 95 | 104 | 110 | 110 | 110 | 113 | 113  |
The graphs show the distribution of before tax profit segregated into dividends, taxes and profits retained within the business.

The graphs show the growth in deposits, advances, total assets and shareholders’ funds. Year 1996 has been considered as the base year.

The graphs show the growth in deposits and refinance borrowings compared with the volume of advances.
Segmental Analysis

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Rs.000</td>
<td>Rs.000</td>
<td>Rs.000</td>
<td>Rs.000</td>
<td>Rs.000</td>
<td>Rs.000</td>
<td>Rs.000</td>
<td>Rs.000</td>
<td>Rs.000</td>
<td>Rs.000</td>
</tr>
<tr>
<td>Interest</td>
<td>16,913,119</td>
<td>12,947,419</td>
<td>-</td>
<td>-</td>
<td>878,742</td>
<td>680,325</td>
<td>-</td>
<td>52</td>
<td>105,977</td>
<td>64,989</td>
</tr>
<tr>
<td>Exchange</td>
<td>792,303</td>
<td>644,460</td>
<td>-</td>
<td>-</td>
<td>396</td>
<td>(294)</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Lease/Premium/</td>
<td>-</td>
<td>-</td>
<td>1,538,842</td>
<td>1,162,455</td>
<td>100,570</td>
<td>4,889</td>
<td>-</td>
<td>-</td>
<td>817,705</td>
<td>587,927</td>
</tr>
<tr>
<td>Brokering Income</td>
<td>1,895,642</td>
<td>1,734,527</td>
<td>-</td>
<td>-</td>
<td>5,609</td>
<td>1,008</td>
<td>440,604</td>
<td>432,904</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Commissions/Rent</td>
<td>373,267</td>
<td>404,453</td>
<td>-</td>
<td>-</td>
<td>1,215</td>
<td>180,842</td>
<td>-</td>
<td>-</td>
<td>691</td>
<td>816</td>
</tr>
<tr>
<td>Other</td>
<td>-</td>
<td>-</td>
<td>1,538,842</td>
<td>1,162,455</td>
<td>986,332</td>
<td>866,770</td>
<td>440,604</td>
<td>432,956</td>
<td>924,373</td>
<td>653,732</td>
</tr>
</tbody>
</table>

**Stock Broking and Securities Dealings**
1. **Stock Exchange Listing**

The issued ordinary shares of Hatton National Bank Limited are listed with the Colombo Stock Exchange. The audited Profit and Loss account for the year ended 31st December 2006 and the audited Balance Sheet of the Bank as at date have been submitted to the Colombo Stock Exchange within three months of the Balance Sheet date.

Stock exchange code for Hatton National Bank Limited shares is "HNB". Reuter code of Hatton National Bank Limited is "HNBL".

2. **Ordinary Shareholders**

**SHARE INFORMATION - VOTING**

As at 31 December 2006

<table>
<thead>
<tr>
<th>No of share-holders</th>
<th>No of shares</th>
<th>%</th>
<th>No of share-holders</th>
<th>No of shares</th>
<th>%</th>
<th>No of share-holders</th>
<th>No of shares</th>
<th>%</th>
</tr>
</thead>
<tbody>
<tr>
<td>1 - 250</td>
<td>2,069</td>
<td>0.25</td>
<td>26</td>
<td>2,489</td>
<td>0.01</td>
<td>2,095</td>
<td>168,775</td>
<td>0.19</td>
</tr>
<tr>
<td>251 - 500</td>
<td>768</td>
<td>0.40</td>
<td>9</td>
<td>3,860</td>
<td>0.02</td>
<td>777</td>
<td>294,068</td>
<td>0.31</td>
</tr>
<tr>
<td>501 - 1,000</td>
<td>598</td>
<td>0.62</td>
<td>12</td>
<td>9,291</td>
<td>0.04</td>
<td>600</td>
<td>456,631</td>
<td>0.48</td>
</tr>
<tr>
<td>1,001 - 2,000</td>
<td>379</td>
<td>0.79</td>
<td>4</td>
<td>5,575</td>
<td>0.03</td>
<td>383</td>
<td>577,101</td>
<td>0.61</td>
</tr>
<tr>
<td>2,001 - 5,000</td>
<td>344</td>
<td>1.57</td>
<td>15</td>
<td>46,427</td>
<td>0.21</td>
<td>359</td>
<td>1,185,151</td>
<td>1.25</td>
</tr>
<tr>
<td>5,001 - 10,000</td>
<td>203</td>
<td>1.27</td>
<td>11</td>
<td>27,775</td>
<td>0.12</td>
<td>36</td>
<td>847,060</td>
<td>0.89</td>
</tr>
<tr>
<td>10,001 - 20,000</td>
<td>35</td>
<td>1.13</td>
<td>1</td>
<td>27,775</td>
<td>0.12</td>
<td>124</td>
<td>1,692,884</td>
<td>1.79</td>
</tr>
<tr>
<td>20,001 - 50,000</td>
<td>31</td>
<td>0.54</td>
<td>3</td>
<td>13,400</td>
<td>0.05</td>
<td>12</td>
<td>1,510,978</td>
<td>1.57</td>
</tr>
<tr>
<td>50,001 - 100,000</td>
<td>15</td>
<td>0.93</td>
<td>1</td>
<td>50,000</td>
<td>0.22</td>
<td>16</td>
<td>720,401</td>
<td>0.76</td>
</tr>
<tr>
<td>100,001 - 200,000</td>
<td>29</td>
<td>2.73</td>
<td>1</td>
<td>55,000</td>
<td>0.25</td>
<td>30</td>
<td>2,031,414</td>
<td>2.15</td>
</tr>
<tr>
<td>Over 200,000</td>
<td>12</td>
<td>7.95</td>
<td>1</td>
<td>21,887,303</td>
<td>98.38</td>
<td>14</td>
<td>79,567,353</td>
<td>84.05</td>
</tr>
<tr>
<td></td>
<td>4,615</td>
<td>100.00</td>
<td>87</td>
<td>22,247,670</td>
<td>100.00</td>
<td>4,702</td>
<td>94,664,700</td>
<td>100.00</td>
</tr>
</tbody>
</table>

**Analysis of shareholders**

**Resident/Non-Resident**

<table>
<thead>
<tr>
<th>31/12/2006</th>
<th>31/12/2005</th>
</tr>
</thead>
<tbody>
<tr>
<td>No of share-holders</td>
<td>No of shares</td>
</tr>
<tr>
<td>Resident</td>
<td>4,615</td>
</tr>
<tr>
<td>Non-Resident</td>
<td>87</td>
</tr>
<tr>
<td>Total</td>
<td>4,702</td>
</tr>
</tbody>
</table>

**Individuals/Institutions**

<table>
<thead>
<tr>
<th>31/12/2006</th>
<th>31/12/2005</th>
</tr>
</thead>
<tbody>
<tr>
<td>No of share-holders</td>
<td>No of shares</td>
</tr>
<tr>
<td>Individuals</td>
<td>4,439</td>
</tr>
<tr>
<td>Institutions</td>
<td>263</td>
</tr>
<tr>
<td>Total</td>
<td>4,702</td>
</tr>
</tbody>
</table>

As at 31/12/2006, the average size of holding of ordinary shareholding was 20,133 voting shares. (31/12/2005 - 19,078 voting shares)

As per the Rule No. 8.7(h) of the Colombo Stock Exchange, the percentage of public holding as at 31st of December 2006 was 52.70 approximately.
### SHARE INFORMATION - NON VOTING

As at 31 December 2006

<table>
<thead>
<tr>
<th>No of</th>
<th>No of</th>
<th>No of</th>
<th>No of</th>
<th>No of</th>
<th>No of</th>
</tr>
</thead>
<tbody>
<tr>
<td>share-holders</td>
<td>shares</td>
<td>%</td>
<td>share-holders</td>
<td>shares</td>
<td>%</td>
</tr>
<tr>
<td>1 -</td>
<td>250</td>
<td>6,002</td>
<td>740,285</td>
<td>3.27</td>
<td>33</td>
</tr>
<tr>
<td>251 -</td>
<td>500</td>
<td>1,235</td>
<td>466,301</td>
<td>2.06</td>
<td>8</td>
</tr>
<tr>
<td>501 -</td>
<td>1,000</td>
<td>1,777</td>
<td>1,187,171</td>
<td>5.24</td>
<td>11</td>
</tr>
<tr>
<td>1,001 -</td>
<td>2,000</td>
<td>1,711</td>
<td>2,234,851</td>
<td>9.86</td>
<td>23</td>
</tr>
<tr>
<td>2,001 -</td>
<td>5,000</td>
<td>778</td>
<td>2,376,250</td>
<td>10.49</td>
<td>12</td>
</tr>
<tr>
<td>5,001 -</td>
<td>10,000</td>
<td>302</td>
<td>2,152,571</td>
<td>9.50</td>
<td>6</td>
</tr>
<tr>
<td>10,001 -</td>
<td>20,000</td>
<td>141</td>
<td>1,957,342</td>
<td>8.64</td>
<td>2</td>
</tr>
<tr>
<td>20,001 -</td>
<td>30,000</td>
<td>33</td>
<td>807,667</td>
<td>3.56</td>
<td>1</td>
</tr>
<tr>
<td>30,001 -</td>
<td>40,000</td>
<td>12</td>
<td>413,570</td>
<td>1.83</td>
<td>-</td>
</tr>
<tr>
<td>40,001 -</td>
<td>50,000</td>
<td>11</td>
<td>506,822</td>
<td>2.24</td>
<td>-</td>
</tr>
<tr>
<td>50,001 -</td>
<td>100,000</td>
<td>15</td>
<td>976,392</td>
<td>4.31</td>
<td>1</td>
</tr>
<tr>
<td>100,001 -</td>
<td>1,000,000</td>
<td>21</td>
<td>4,378,876</td>
<td>19.32</td>
<td>1</td>
</tr>
<tr>
<td>Over</td>
<td>1,000,000</td>
<td>1</td>
<td>4,461,337</td>
<td>19.69</td>
<td>-</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>12,039</td>
<td>22,659,435</td>
<td>100.00</td>
<td>98</td>
<td>440,565</td>
<td>100.00</td>
</tr>
<tr>
<td>12,137</td>
<td>23,100,000</td>
<td>100.00</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

### Analysis of shareholders

#### Resident/Non-Resident

<table>
<thead>
<tr>
<th>No of share-holders</th>
<th>No of shares</th>
<th>%</th>
</tr>
</thead>
<tbody>
<tr>
<td>Resident</td>
<td>12,039</td>
<td>22,659,435</td>
</tr>
<tr>
<td>Non-Resident</td>
<td>98</td>
<td>440,565</td>
</tr>
<tr>
<td>Total</td>
<td>12,137</td>
<td>23,100,000</td>
</tr>
</tbody>
</table>

#### Individuals/Institutions

<table>
<thead>
<tr>
<th>No of share-holders</th>
<th>No of shares</th>
<th>%</th>
</tr>
</thead>
<tbody>
<tr>
<td>Individuals</td>
<td>11,897</td>
<td>13,547,311</td>
</tr>
<tr>
<td>Institutions</td>
<td>240</td>
<td>9,552,689</td>
</tr>
<tr>
<td>Total</td>
<td>12,137</td>
<td>23,100,000</td>
</tr>
</tbody>
</table>

As at 31/12/2006 the average size of holding of ordinary shareholding was 1,903 voting shares.

As per the Rule No. 8.7 (h) of Colombo Stock Exchange, the percentage of public holding as at 31st December 2006 was 95.42 approximately.

### Share Trading

#### 2006

<table>
<thead>
<tr>
<th>Voting shares</th>
<th>Non-Voting shares</th>
</tr>
</thead>
<tbody>
<tr>
<td>Number of transactions</td>
<td>3,400</td>
</tr>
<tr>
<td>Number of shares traded (Mn.)</td>
<td>5.6</td>
</tr>
<tr>
<td>Rank (as per CSE)</td>
<td>78</td>
</tr>
<tr>
<td>Value of shares traded (Rs. Mn.)</td>
<td>706.7</td>
</tr>
<tr>
<td>Rank (as per CSE)</td>
<td>32</td>
</tr>
</tbody>
</table>

### 3. Share Trading

<table>
<thead>
<tr>
<th>Voting shares</th>
<th>Non-Voting shares</th>
</tr>
</thead>
<tbody>
<tr>
<td>Number of transactions</td>
<td>3,400</td>
</tr>
<tr>
<td>Number of shares traded (Mn.)</td>
<td>5.6</td>
</tr>
<tr>
<td>Rank (as per CSE)</td>
<td>78</td>
</tr>
<tr>
<td>Value of shares traded (Rs. Mn.)</td>
<td>706.7</td>
</tr>
<tr>
<td>Rank (as per CSE)</td>
<td>32</td>
</tr>
</tbody>
</table>
4. **Dividends**

<table>
<thead>
<tr>
<th></th>
<th>2006</th>
<th>2005</th>
</tr>
</thead>
<tbody>
<tr>
<td>Interim</td>
<td>25% Paid in December 2006</td>
<td>20% Paid in December 2005</td>
</tr>
<tr>
<td>Final</td>
<td>25% Proposed in April 2007</td>
<td>20% Paid in April 2006</td>
</tr>
</tbody>
</table>

5. **Earnings**

<table>
<thead>
<tr>
<th></th>
<th>2006</th>
<th>2005</th>
</tr>
</thead>
<tbody>
<tr>
<td>Earnings per share (Rs.)</td>
<td>18.89</td>
<td>15.09</td>
</tr>
<tr>
<td>Price earnings ratio (Times)</td>
<td>8.25</td>
<td>7.46</td>
</tr>
</tbody>
</table>

6. **Market Value**

<table>
<thead>
<tr>
<th></th>
<th>Highest</th>
<th>Lowest</th>
<th>Year End</th>
</tr>
</thead>
<tbody>
<tr>
<td>Rs.</td>
<td>Rs.</td>
<td>Rs.</td>
<td></td>
</tr>
<tr>
<td>2002 - Voting</td>
<td>80.00</td>
<td>42.00</td>
<td>79.00</td>
</tr>
<tr>
<td>- Non Voting</td>
<td>48.50</td>
<td>28.25</td>
<td>47.00</td>
</tr>
<tr>
<td>2003 - Voting</td>
<td>120.00</td>
<td>68.00</td>
<td>69.00</td>
</tr>
<tr>
<td>- Non Voting</td>
<td>75.00</td>
<td>35.00</td>
<td>36.75</td>
</tr>
<tr>
<td>2004 - Voting</td>
<td>80.00</td>
<td>50.25</td>
<td>57.00</td>
</tr>
<tr>
<td>- Non Voting</td>
<td>47.00</td>
<td>30.00</td>
<td>32.75</td>
</tr>
<tr>
<td>2005 - Voting</td>
<td>148.00</td>
<td>51.75</td>
<td>112.50</td>
</tr>
<tr>
<td>- Non Voting</td>
<td>65.75</td>
<td>32.25</td>
<td>41.50</td>
</tr>
<tr>
<td>2006 - Voting</td>
<td>161.00</td>
<td>101.00</td>
<td>155.75</td>
</tr>
<tr>
<td>- Non Voting</td>
<td>74.25</td>
<td>39.25</td>
<td>70.00</td>
</tr>
</tbody>
</table>

7. **Market Capitalisation (As at 31st December)**

<table>
<thead>
<tr>
<th></th>
<th>Capital &amp; Reserves</th>
<th>HNB Market Capitalisation</th>
<th>CSE Market Capitalisation</th>
<th>HNB Market Capitalisation as a % of CSE Market Capitalisation</th>
<th>Market Capitalisation</th>
<th>Market Capitalisation Ranking</th>
</tr>
</thead>
<tbody>
<tr>
<td>Rs. Mn</td>
<td>Rs. Mn</td>
<td>Rs. Mn</td>
<td>Rs. Mn</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2002</td>
<td>6,235</td>
<td>4,345</td>
<td>162,600</td>
<td>2.67</td>
<td>7</td>
<td></td>
</tr>
<tr>
<td>2003</td>
<td>6,993</td>
<td>3,795</td>
<td>262,838</td>
<td>1.44</td>
<td>15</td>
<td></td>
</tr>
<tr>
<td>2004</td>
<td>9,052</td>
<td>4,389</td>
<td>382,065</td>
<td>1.15</td>
<td>20</td>
<td></td>
</tr>
<tr>
<td>2005</td>
<td>11,239</td>
<td>10,649</td>
<td>584,040</td>
<td>1.82</td>
<td>10</td>
<td></td>
</tr>
<tr>
<td>2006</td>
<td>12,930</td>
<td>14,744</td>
<td>834,763</td>
<td>1.76</td>
<td>10</td>
<td></td>
</tr>
</tbody>
</table>
8. Record of Scrip Issues

<table>
<thead>
<tr>
<th>Year</th>
<th>Issue</th>
<th>Basis</th>
<th>No. of Shares</th>
<th>Increase in Share Capital (Rs.)</th>
<th>Share Capital (Rs.)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Prior to public issue</td>
<td></td>
<td>50,000</td>
<td>500,000</td>
<td>500,000</td>
</tr>
<tr>
<td>1971</td>
<td>Public issue</td>
<td></td>
<td>220,000</td>
<td>2,200,000</td>
<td>2,700,000</td>
</tr>
<tr>
<td>1977</td>
<td>Rights issue (@ Rs. 10/-)</td>
<td>42:50</td>
<td>230,000</td>
<td>2,300,000</td>
<td>5,000,000</td>
</tr>
<tr>
<td>1980</td>
<td>Rights issue (@ Rs. 10/-)</td>
<td>1:1</td>
<td>500,000</td>
<td>5,000,000</td>
<td>10,000,000</td>
</tr>
<tr>
<td>1982</td>
<td>Bonus</td>
<td>1:1</td>
<td>1,000,000</td>
<td>10,000,000</td>
<td>20,000,000</td>
</tr>
<tr>
<td>1988</td>
<td>Bonus</td>
<td>1:1</td>
<td>2,000,000</td>
<td>20,000,000</td>
<td>40,000,000</td>
</tr>
<tr>
<td>1990</td>
<td>Bonus</td>
<td>1:2</td>
<td>2,000,000</td>
<td>20,000,000</td>
<td>60,000,000</td>
</tr>
<tr>
<td>1993</td>
<td>Bonus</td>
<td>1:1</td>
<td>6,000,000</td>
<td>60,000,000</td>
<td>120,000,000</td>
</tr>
<tr>
<td>1996</td>
<td>Bonus</td>
<td>2:3</td>
<td>8,000,000</td>
<td>80,000,000</td>
<td>200,000,000</td>
</tr>
<tr>
<td>1998</td>
<td>Bonus</td>
<td>1:2</td>
<td>10,000,000</td>
<td>100,000,000</td>
<td>300,000,000</td>
</tr>
<tr>
<td>1999</td>
<td>Bonus</td>
<td>2:3</td>
<td>20,000,000</td>
<td>200,000,000</td>
<td>500,000,000</td>
</tr>
<tr>
<td>1999</td>
<td>Rights (non-voting @ Rs. 70/-)*</td>
<td>3:10</td>
<td>15,000,000</td>
<td>150,000,000</td>
<td>650,000,000</td>
</tr>
<tr>
<td>2001</td>
<td>Bonus</td>
<td>1:10</td>
<td>6,500,000</td>
<td>65,000,000</td>
<td>715,000,000</td>
</tr>
<tr>
<td>2004</td>
<td>Rights (voting @ Rs. 55/-)</td>
<td>2:5</td>
<td>22,000,000</td>
<td>220,000,000</td>
<td>935,000,000</td>
</tr>
<tr>
<td>2004</td>
<td>Rights (non-voting @ Rs. 33/-)</td>
<td>2:5</td>
<td>6,600,000</td>
<td>66,000,000</td>
<td>1,001,000,000</td>
</tr>
<tr>
<td>2005</td>
<td>Issue of underlying shares for GDR</td>
<td>-</td>
<td>17,664,700</td>
<td>176,647,000</td>
<td>1,177,647,000</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td></td>
<td></td>
<td>117,764,700</td>
<td>1,177,647,000</td>
<td></td>
</tr>
</tbody>
</table>

* Unsubscribed shares were issued to public

9. Price Volume Chart
### 20 Major Voting Shareholders – 31st December 2006

<table>
<thead>
<tr>
<th>Name</th>
<th>% on total capital</th>
<th>No. of shares</th>
<th>2006</th>
<th>2005</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Deutsche Bank Trust Company Americas</td>
<td>15.00%</td>
<td></td>
<td>17,664,700</td>
<td>17,664,700</td>
</tr>
<tr>
<td>2. Brown &amp; Co. Ltd</td>
<td>7.17%</td>
<td></td>
<td>8,441,760</td>
<td>8,441,760</td>
</tr>
<tr>
<td>3. CBD Exports Ltd</td>
<td>6.53%</td>
<td></td>
<td>7,692,300</td>
<td>7,692,300</td>
</tr>
<tr>
<td>4. Milford Exports (Cey) Ltd</td>
<td>6.53%</td>
<td></td>
<td>7,866,525</td>
<td>7,866,525</td>
</tr>
<tr>
<td>5. Stassen Exports Ltd</td>
<td>5.66%</td>
<td></td>
<td>6,662,425</td>
<td>6,662,425</td>
</tr>
<tr>
<td>7. Sri Lanka Insurance Corporation Ltd</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>– Life Fund/Gen. Fund</td>
<td>4.88%</td>
<td></td>
<td>5,749,566</td>
<td>5,749,566</td>
</tr>
<tr>
<td>8. Standard Finance Ltd</td>
<td>4.77%</td>
<td></td>
<td>5,620,360</td>
<td>5,620,360</td>
</tr>
<tr>
<td>9. Taprobane Fund Management (Pvt) Ltd</td>
<td>3.98%</td>
<td></td>
<td>4,685,193</td>
<td>4,685,193</td>
</tr>
<tr>
<td>10. Sonetto Holdings Ltd</td>
<td>3.59%</td>
<td></td>
<td>4,222,603</td>
<td>4,222,603</td>
</tr>
<tr>
<td>11. Distilleries Co. of Sri Lanka Ltd</td>
<td>2.53%</td>
<td></td>
<td>2,980,854</td>
<td>2,980,854</td>
</tr>
<tr>
<td>12. Mr S V Somasundaram</td>
<td>1.42%</td>
<td></td>
<td>1,669,600</td>
<td>692,000</td>
</tr>
<tr>
<td>13. Indra Traders (Pvt) Ltd</td>
<td>0.88%</td>
<td></td>
<td>1,033,300</td>
<td></td>
</tr>
<tr>
<td>14. Mr S Visuvananthan</td>
<td>0.38%</td>
<td></td>
<td>448,832</td>
<td>448,832</td>
</tr>
<tr>
<td>15. Masons Mixture Ltd</td>
<td>0.34%</td>
<td></td>
<td>399,520</td>
<td>399,520</td>
</tr>
<tr>
<td>16. Mr Y S H Indra Kumar Silva</td>
<td>0.34%</td>
<td></td>
<td>397,990</td>
<td>397,990</td>
</tr>
<tr>
<td>17. Associated Battery Manufacturers (Cey) Ltd</td>
<td>0.26%</td>
<td></td>
<td>300,902</td>
<td>300,902</td>
</tr>
<tr>
<td>18. Investment Link (Pvt) Ltd</td>
<td>0.21%</td>
<td></td>
<td>245,800</td>
<td></td>
</tr>
<tr>
<td>19. DPMC Financial Services (Pvt) Ltd A/c No 1</td>
<td>0.20%</td>
<td></td>
<td>240,000</td>
<td>619,900</td>
</tr>
<tr>
<td>20. Mr Narhari Choonilal Bhatt</td>
<td>0.15%</td>
<td></td>
<td>177,480</td>
<td>177,480</td>
</tr>
</tbody>
</table>

Sub Total 69.99% 82,429,181 80,554,381
Balance held by 6,682 Voting Shareholders 10.39% 12,235,519 14,110,319 [4,942 V.Sh]

Total Voting Shares 80.38% 94,664,700 94,664,700
Shares held by 12,137 Non-Voting Shareholders 19.62% 23,100,000 23,100,000 [12,249 NV.Sh]

Total No. of Ordinary Shares 100.00% 117,764,700 117,764,700

### 20 Major Non-Voting Shareholders

<table>
<thead>
<tr>
<th>Name</th>
<th>% on total capital</th>
<th>No. of shares</th>
<th>2006</th>
<th>2005</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Legalink Trustee Services (Pvt) Ltd</td>
<td>3.88%</td>
<td></td>
<td>4,566,637</td>
<td>4,566,637</td>
</tr>
<tr>
<td>2. Nawaloka Developments (Pvt) Ltd</td>
<td>0.61%</td>
<td></td>
<td>715,000</td>
<td>715,000</td>
</tr>
<tr>
<td>3. Mr K V M Fernando &amp; Mrs K W S H Fernando</td>
<td>0.34%</td>
<td></td>
<td>405,300</td>
<td>156,600</td>
</tr>
<tr>
<td>4. DFCC Bank A/c No.1</td>
<td>0.33%</td>
<td></td>
<td>388,800</td>
<td>426,000</td>
</tr>
<tr>
<td>5. Distilleries Co. of Sri Lanka Ltd</td>
<td>0.29%</td>
<td></td>
<td>337,566</td>
<td>337,566</td>
</tr>
<tr>
<td>6. Mr D K Weeratunga &amp; Mr D K A K Weeratunga</td>
<td>0.27%</td>
<td></td>
<td>318,880</td>
<td>216,580</td>
</tr>
<tr>
<td>7. Standard Finance Ltd</td>
<td>0.23%</td>
<td></td>
<td>267,600</td>
<td>267,600</td>
</tr>
<tr>
<td>8. Mr S Visuvananthan</td>
<td>0.19%</td>
<td></td>
<td>220,000</td>
<td>220,000</td>
</tr>
<tr>
<td>9. Mr D F G Dalpethado</td>
<td>0.17%</td>
<td></td>
<td>194,554</td>
<td>267,574</td>
</tr>
<tr>
<td>10. Citygroup Global Markets Financial Products LLC</td>
<td>0.16%</td>
<td></td>
<td>184,400</td>
<td></td>
</tr>
<tr>
<td>11. Hatton National Bank Ltd A/c No.2</td>
<td>0.14%</td>
<td></td>
<td>169,319</td>
<td>169,319</td>
</tr>
<tr>
<td>12. M C A Trading Co. (Pvt) Ltd</td>
<td>0.14%</td>
<td></td>
<td>165,000</td>
<td>165,000</td>
</tr>
<tr>
<td>13. Ms S A Fernando</td>
<td>0.13%</td>
<td></td>
<td>157,200</td>
<td>94,000</td>
</tr>
<tr>
<td>14. Ceylon Grain Elevators Ltd</td>
<td>0.12%</td>
<td></td>
<td>137,500</td>
<td>137,500</td>
</tr>
<tr>
<td>15. Employees Trust Fund Board</td>
<td>0.11%</td>
<td></td>
<td>132,090</td>
<td></td>
</tr>
<tr>
<td>16. Asia Fort Assets Management (Pvt) Ltd</td>
<td>0.10%</td>
<td></td>
<td>120,000</td>
<td></td>
</tr>
<tr>
<td>17. H L L M Nanayakkara</td>
<td>0.10%</td>
<td></td>
<td>117,100</td>
<td></td>
</tr>
<tr>
<td>18. Lanka Synthetic Fibre Co.Ltd</td>
<td>0.09%</td>
<td></td>
<td>110,000</td>
<td>110,000</td>
</tr>
<tr>
<td>19. Mrs S F H Alexander</td>
<td>0.09%</td>
<td></td>
<td>108,970</td>
<td>108,970</td>
</tr>
<tr>
<td>20. Ms W N C Fernando</td>
<td>0.09%</td>
<td></td>
<td>105,200</td>
<td>94,000</td>
</tr>
</tbody>
</table>

Sub Total 7.58% 8,923,116 8,054,366
Balance held by 12,137 Non-Voting Shareholders 12.04% 14,176,884 15,045,654 [12,229 NV.Sh]

Total No. of Ordinary Shares 19.62% 23,100,000 23,100,000
Balance held by 4,702 Voting Shareholders 80.38% 94,664,700 94,664,700 [4,927 NV.Sh]

Total No. of Ordinary Shares 100.00% 117,764,700 117,764,700
### Market Value

<table>
<thead>
<tr>
<th></th>
<th>Highest</th>
<th>Lowest</th>
<th>Year End</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Rs.</td>
<td>Rs.</td>
<td>Rs.</td>
</tr>
<tr>
<td>5 year Fixed Rate (13.75% p.a.)</td>
<td>101.71</td>
<td>93.00</td>
<td>98.00</td>
</tr>
<tr>
<td>5 year Floating Rate (TB + 1.00% p.a.)</td>
<td>96.63</td>
<td>96.50</td>
<td>96.63</td>
</tr>
<tr>
<td>7 year Fixed Rate (14.00% p.a.)</td>
<td>98.00</td>
<td>98.00</td>
<td>98.00</td>
</tr>
<tr>
<td>7 year Floating Rate (TB + 1.10% p.a.)</td>
<td>99.75</td>
<td>99.75</td>
<td>N/T</td>
</tr>
<tr>
<td>10 year Fixed Rate (14.20% p.a.)</td>
<td>104.00</td>
<td>98.05</td>
<td>98.05</td>
</tr>
<tr>
<td>10 year Floating Rate (TB + 1.25% p.a.)</td>
<td>N/T</td>
<td>N/T</td>
<td>N/T</td>
</tr>
</tbody>
</table>

N/T – Not Traded for the period

### Interest Income

<table>
<thead>
<tr>
<th></th>
<th>2006</th>
<th>2005</th>
</tr>
</thead>
<tbody>
<tr>
<td>5 year Fixed Rate (13.75% p.a.)</td>
<td>13.75</td>
<td>13.75</td>
</tr>
<tr>
<td>5 year Floating Rate (TB + 1.00% p.a.)</td>
<td>12.00</td>
<td>12.00</td>
</tr>
<tr>
<td>7 year Fixed Rate (14.00% p.a.)</td>
<td>14.00</td>
<td>14.00</td>
</tr>
<tr>
<td>7 year Floating Rate (TB + 1.10% p.a.)</td>
<td>12.00</td>
<td>12.00</td>
</tr>
<tr>
<td>10 year Fixed Rate (14.20% p.a.)</td>
<td>14.20</td>
<td>14.20</td>
</tr>
<tr>
<td>10 year Floating Rate (TB + 1.25% p.a.)</td>
<td>12.00</td>
<td>12.00</td>
</tr>
</tbody>
</table>

For an investment of Rs. 100/-. The above rupee coupon interest rates are applicable for the next interest payment due on the 15th of February 2007.

### Yield to Maturity of last trade done (% p.a)

<table>
<thead>
<tr>
<th></th>
<th>2006</th>
<th>2005</th>
</tr>
</thead>
<tbody>
<tr>
<td>5 year Fixed Rate (13.75% p.a.)</td>
<td>16.69</td>
<td>15.07</td>
</tr>
<tr>
<td>5 year Floating Rate (TB + 1.00% p.a.)**</td>
<td>N/A</td>
<td>N/A</td>
</tr>
<tr>
<td>7 year Fixed Rate (14.00% p.a.)**</td>
<td>14.77</td>
<td>13.98</td>
</tr>
<tr>
<td>7 year Floating Rate (TB + 1.10% p.a.)**</td>
<td>N/A</td>
<td>N/A</td>
</tr>
<tr>
<td>10 year Fixed Rate (14.20% p.a.)</td>
<td>14.65</td>
<td>14.65</td>
</tr>
<tr>
<td>10 year Floating Rate (TB + 1.25% p.a.)**</td>
<td>N/A</td>
<td>N/A</td>
</tr>
</tbody>
</table>

** The yield to maturity calculation is not applicable for floating rate debentures.

### Yield as at last trade done (% p.a)

<table>
<thead>
<tr>
<th></th>
<th>2006</th>
<th>2005</th>
</tr>
</thead>
<tbody>
<tr>
<td>5 year Fixed Rate (13.75% p.a.)</td>
<td>14.03</td>
<td>14.03</td>
</tr>
<tr>
<td>5 year Floating Rate (TB + 1.00% p.a.)</td>
<td>12.42</td>
<td>12.50</td>
</tr>
<tr>
<td>7 year Fixed Rate (14.00% p.a.)</td>
<td>14.29</td>
<td>14.00</td>
</tr>
<tr>
<td>7 year Floating Rate (TB + 1.10% p.a.)</td>
<td>12.03</td>
<td>12.03</td>
</tr>
<tr>
<td>10 year Fixed Rate (14.20% p.a.)</td>
<td>14.48</td>
<td>14.48</td>
</tr>
<tr>
<td>10 year Floating Rate (TB + 1.25% p.a.)</td>
<td>N/T</td>
<td>N/T</td>
</tr>
</tbody>
</table>

N/T – Not Traded as at ended 31 December

### Yield on Equivalent Government Security (% p.a)

<table>
<thead>
<tr>
<th></th>
<th>2006</th>
<th>2005</th>
</tr>
</thead>
<tbody>
<tr>
<td>5 year Treasury Bond</td>
<td>13.95</td>
<td>11.65</td>
</tr>
<tr>
<td>6 year Treasury Bond</td>
<td>14.00</td>
<td>11.50</td>
</tr>
<tr>
<td>10 year Treasury Bond</td>
<td>N/A</td>
<td>11.75</td>
</tr>
</tbody>
</table>

N/T – Not Traded for the period ended 31 December
HNB DEBENTURES 2003

i) Market Value
12 months ended 31st December 2006

<table>
<thead>
<tr>
<th></th>
<th>Highest</th>
<th>Lowest</th>
<th>Year End</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Rs.</td>
<td>Rs.</td>
<td>Rs.</td>
</tr>
<tr>
<td>5 year Fixed Rate [10.00% p.a.]</td>
<td>94.12</td>
<td>86.00</td>
<td>90.00</td>
</tr>
<tr>
<td>5 year Floating Rate [TB + 2.00% p.a.]</td>
<td>94.93</td>
<td>90.99</td>
<td>90.99</td>
</tr>
</tbody>
</table>

ii) Interest Income
12 months ended 31st December

<table>
<thead>
<tr>
<th></th>
<th>2006</th>
<th>2005</th>
</tr>
</thead>
<tbody>
<tr>
<td>5 year Fixed Rate [10.00% p.a.]</td>
<td>10.00</td>
<td>10.00</td>
</tr>
<tr>
<td>5 year Floating Rate [TB + 2.00% p.a.]</td>
<td>14.39</td>
<td>12.24</td>
</tr>
</tbody>
</table>

For an investment of Rs. 100/-. The above rupee coupon interest rates are applicable for the next interest payment due on the 15th of June 2007.

iii) Yield to Maturity of last trade done (% p.a)

<table>
<thead>
<tr>
<th></th>
<th>2006</th>
<th>2005</th>
</tr>
</thead>
<tbody>
<tr>
<td>5 year Fixed Rate [10.00% p.a.]</td>
<td>17.56</td>
<td>15.77</td>
</tr>
<tr>
<td>5 year Floating Rate [TB + 2.00% p.a.] **</td>
<td>N/A</td>
<td>N/A</td>
</tr>
</tbody>
</table>

** The yield to maturity calculation is not applicable for floating rate debentures.

iv) Yield as at last trade done (% p.a)

<table>
<thead>
<tr>
<th></th>
<th>2006</th>
<th>2005</th>
</tr>
</thead>
<tbody>
<tr>
<td>5 year Fixed Rate [10.00% p.a.]</td>
<td>11.11</td>
<td>11.35</td>
</tr>
<tr>
<td>5 year Floating Rate [TB + 2.00% p.a.]</td>
<td>13.58</td>
<td>N/T</td>
</tr>
</tbody>
</table>

v) Yield on Equivalent Government Security (% p.a)

<table>
<thead>
<tr>
<th></th>
<th>2006</th>
<th>2005</th>
</tr>
</thead>
<tbody>
<tr>
<td>5 year Treasury Bond</td>
<td>13.95</td>
<td>11.45</td>
</tr>
<tr>
<td>6 year Treasury Bond</td>
<td>14.00</td>
<td>11.50</td>
</tr>
<tr>
<td>10 year Treasury Bond</td>
<td>N/A</td>
<td>11.75</td>
</tr>
</tbody>
</table>

N/T – Not Traded for the period ended 31 December

HNB DEBENTURES 2006

6 Yrs [Rs.262.5 Mn] 6 Months net TB rate + 2.25% p.a
7 Yrs [Rs.250.0 Mn] 6 Months net TB rate +2.25% p.a.
8 Yrs [Rs.300.0 Mn] 6 Months net TB rate +2.25% p.a.
15 Yrs [Rs.107.5 Mn] 11.00% p.a. cumulated till maturity
18 Yrs [Rs.200.0 Mn] 11.25% p.a. cumulated till maturity

With a floor of 8% and cap of 16% payable bi-annually

Bi annual interest payment

<table>
<thead>
<tr>
<th>Period</th>
<th>Net TB rate</th>
<th>Applicable rate</th>
</tr>
</thead>
<tbody>
<tr>
<td>01-04-06 to 30-06-06</td>
<td>10.37 %</td>
<td>12.62%</td>
</tr>
<tr>
<td>01-07-06 to 31-12-06</td>
<td>12.70 %</td>
<td>14.95%</td>
</tr>
</tbody>
</table>

Ratios

<table>
<thead>
<tr>
<th></th>
<th>2006</th>
<th>2005</th>
</tr>
</thead>
<tbody>
<tr>
<td>Debt to equity ratio (%)</td>
<td>40%</td>
<td>36%</td>
</tr>
<tr>
<td>Interest cover (Times)</td>
<td>5.73</td>
<td>4.92</td>
</tr>
<tr>
<td>Quick asset ratio (%)</td>
<td>56%</td>
<td>61%</td>
</tr>
</tbody>
</table>
Glossary of Financial/Banking Terms

**BIS Surplus**
The total Capital Adequacy in excess of the minimum stipulated by Basel International Standards and as modified to suit local requirements by the Central Bank of Sri Lanka.

**Capital Reserve**
Capital Reserves consist of revaluation reserves arising from revaluation of properties owned by the Bank and Reserve Fund set aside for specific purposes defined under the Banking Act of 1988 and shall not be reduced or impaired without the approval of the Monetary Board.

**Capital Adequacy Ratio**
The percentage of risk-adjusted assets supported by capital as defined under the framework of risk-based capital standards developed by the Bank for International Settlements (BIS) and as modified to suit local requirements by the Central Bank of Sri Lanka.

**Commitment to Extend Credit**
Credit facilities available to clients either in the form of loans, bankers’ acceptances and other, on-balance sheet financing, or through off-balance sheet products such as guarantees and letters of credit.

**Contingent Liabilities**
Conditions or situations at the balance sheet date, the financial effect of which are to be determined by the future events which may or may not occur.

**Cost Income Ratio**
Operating expenses as a percentage of net income.

**Cost-push Inflation**
A continuous increase in average price levels due to an increase in production costs.

**Deferred Tax**
Sum set aside in the Financial Statements for taxation that may become payable in a financial year other than the current financial year.

**Dividend Yield**
Dividend earned per share as a percentage of its market value.

**Dividend Cover**
Profit after tax divided by gross dividends. This ratio measures the number of times dividend is covered by current year’s distributable profits.

**Documentary Letters of Credit (L/Cs)**
Written undertakings by a bank on behalf of its customer authorising a third party to draw on the bank up to a stipulated amount under specific terms and conditions. Such undertakings are established for the purpose of facilitating international trade.

**Earnings Per Share (EPS)**
Profit attributable to ordinary shareholders divided by the number of ordinary shares in issue.

**Foreign Exchange Income**
The realised gain recorded when assets or liabilities denominated in foreign currencies are translated into Sri Lankan Rupees on the balance sheet date at prevailing rates which differ from those rates in force at inception or on the previous balance sheet date. Foreign exchange income also arises from trading in foreign currencies.
General Provisions
Are established for leasing transactions, housing loans, pawning advances and others for anticipated losses on aggregate exposures where credit losses cannot yet be determined on an individual facility basis.

Gross Dividends
The portion of profit inclusive of tax withheld distributed to shareholders.

Guarantees
Primarily represent irrevocable assurances that a bank will make payments in the event that its customer cannot meet his/her financial obligations to third parties. Certain other guarantees represent non-financial undertakings such as bid and performance bonds.

Impairment
When recoverable amount declines below carrying amount.

Intangible Asset
An identifiable non-monetary asset without physical substance held for use in the production/supply of goods/services or for rental to others or for administrative purposes.

Interest Margin
Net interest income as a percentage of average interest earning assets.

Interest Spread
Represents the difference between the average interest rate earned and the average interest rate paid on funds.

Liquid Assets
Assets that are held in cash or in a form that can be converted to cash readily, such as deposits with other banks, bills of exchange and treasury bills.

Loan Loss Provision (please refer Provision for Bad and Doubtful Debts)

Market Capitalisation
Number of ordinary shares in issue multiplied by the market value of each share at the year end.

Net Asset Value Per Share
Shareholders’ Funds divided by the number of ordinary shares in issue.

Net-Interest Income
The difference between what a bank earns on assets such as loans and securities and what it pays on liabilities such as deposits, refinance funds and inter-bank borrowings.

Non-Performing Advances
All loans are classified as non-performing when a payment is 90 days in arrears.

Non-Performing Advances Cover (NPA Cover)
Cumulative loan provision as a percentage of total Non-Performing Advances (net of Interest in Suspense).

NPA Ratio
Total non-performing advances [net of Interest in Suspense] divided by total advances portfolio (net of Interest in Suspense).

Price Earnings Ratio (P/E Ratio)
Market price of an ordinary share divided by earnings per share (EPS).

 Provision for Bad and Doubtful Debts
A charge to income which is added to the allowance for loan losses. Specific provisions are established to reduce the book value of specific assets (primarily loans) to estimated realisable values.
**Return On Average Assets (ROA)**
Net income expressed as a percentage of average total assets, used along with ROE, as a measure of profitability and as a basis of intra-industry performance comparison.

**Return On Average Equity (ROE)**
Net income, less preferred share dividends if any, expressed as a percentage of average ordinary shareholders’ equity.

**Revenue Reserve**
Reserves set aside for future distribution and investment.

**Reverse Repo**
A purchase of government securities with an agreement to resell them at a given price on a specific future date.

**Risk-Adjusted Assets**
Used in the calculation of risk-based capital ratios. The face amount of lower risk assets is discounted using risk weighting factors in order to reflect a comparable risk per rupee among all types of assets. The risk inherent in off-balance sheet instruments is also recognised, first by adjusting notional values to balance sheet (or credit) equivalents and then by applying appropriate risk weighting factors.

**Rights Issue**
Issue of shares to the existing share holders at an agreed price, generally lower than market price.

**Segment Reporting**
Segment reporting indicates the contribution to the revenue derived from business segments such as banking operations, leasing operations, stock broking & securities dealings, property and insurance.

**Share Premium**
Amount paid by a shareholder, over and above the par value a share.

**Shareholders’ Funds**
Shareholders’ funds consist of issued and fully paid ordinary share capital plus capital and revenue reserves.

**Swaps (Currency)**
The simultaneous purchase of an amount of a currency for spot settlement and the sale of the same amount of the same currency for forward settlement. Alternatively a simultaneous spot sale and forward purchase of a currency.

**Tier 1 Capital**
Consists of the sum total of paid up ordinary shares, non cumulative, non redeemable preference shares, share premium, statutory reserve fund, published retained profits, general and other reserves less goodwill.

**Tier 2 Capital**
Consists of the sum total of revaluation reserves, general provisions, hybrid capital instruments and approved subordinated debentures.

**Total Capital**
Is the sum of Tier 1 and Tier 2 capital.

**Value Added**
Value added is the wealth created by providing banking services less the cost of providing such services. The value added is allocated among the employees, the providers of capital, to government by way of taxes and retained for expansion and growth.
Notice of Meeting

Notice is hereby given that the Thirty Eighth (38th) Annual General Meeting of the Hatton National Bank Limited is convened on the twenty ninth (29) day of March 2007 at the Auditorium on Level 22 of “HNB Towers” at No: 479, T.B. Jayah Mawatha, Colombo 10, at 10.00 in the forenoon when the following Ordinary Business will be transacted.

ORDINARY BUSINESS
To receive and consider the Report of the Directors, the Statement of Accounts and the Balance Sheet of the Company for the year ended 31st December 2006 with the Auditors’ Report thereon.

To declare a final dividend of 25% as recommended by the Directors to the shareholders.

To re-elect Mr R T Wijetilleke who retires by rotation at the Annual General Meeting in terms of Article 87 of the Articles of Association of the Company, as a Director of the Company.

To re-elect Mr D H S Jayawardena who retires by rotation at the Annual General Meeting in terms of Article 87 of the Articles of Association of the Company, as a Director of the Company.

To re-elect Mr M V Theagarajah in terms of Article 93 of the Articles of Association of the Company as a Director of the Company, special notice having been given pursuant to sections 138 & 182 of the Companies Act No.17 of 1982 of the intention to propose the following resolution:-

Resolution
"That Mr Manickam Vallipuram Theagarajah, who has attained the age of 70 years on 13th October 2001 and is of the age of 75 years be and is hereby re-elected as a Director of the Company and it is hereby declared that the age limit of 70 years referred to in Section 181 of the Companies Act No.17 of 1982, shall not apply to the said Director."

To re-appoint Auditors for the ensuing year and to authorise the Directors to fix their remuneration.

To authorise the Directors to determine payments for the year 2007 for charitable and other purposes set out in the Companies Donations Act (Cap. 147).

By Order Of The Board

INDRANI GOONESEKERA
DGM-LEGAL/BOARD SECRETARY
Colombo, Sri Lanka.

Notes:
1. A member entitled to attend or attend and vote at the meeting is entitled to appoint a proxy to attend or attend and vote as the case may be, in his stead.
2. A proxy need not be a member of the Company. The Form of Proxy is enclosed.
3. The completed Form of Proxy should be deposited at the Registered Office of the Company at No: 479, T.B. Jayah Mawatha, Colombo 10 before 10.00 in the forenoon on 27th March, 2007
To request information or submit a comment/query to the Company, please complete the following and return this page to -

Chief Financial Officer,
Hatton National Bank Limited,
No. 479, T.B. Jayah Mawatha (Darley Road)
P.O. Box: 837,
Colombo 10.
Email : nihalke@hnb.lk

Name : ________________________________
Permanent Mailing Address : ________________________________

Contact Numbers - (Tel) : ________________________________
- Country Code : ___________________ Area Code : ___________ Number : ____________
- (Fax) : ________________________________
- Country Code : ___________________ Area Code : ___________ Number : ____________

E-mail : ________________________________
Name of Company (If Applicable) : ________________________________

Designation (If Applicable) : ________________________________

Company Address (If Applicable) : ________________________________

Queries/Comments

Please tick (✓) the appropriate box

Would you like to receive soft copies of the HNB annual and interim reports via e-mail? Yes No
Would you like to receive news and press releases of HNB via e-mail? Yes No
Would you like to receive any information on our products/services? Yes No
Form of Proxy - Voting

I/We ..............................................................................................................................................................................................................

of .............................................................................................................................................................................................................. being a member/members

of the Hatton National Bank Ltd, hereby appoint, Rienzie Theobald Wijetilleke or failing him Vijaya Perera Vittachi or

failing him Rajendra Theagarajah or failing him Don Harold Stassen Jayawardena, or failing him Manickam Vallipuram

Theagarajah, or failing him Rajpal Kumar Obeyesekere or failing him Pamela Christine Cooray, or failing her Ratneswara

Sivaratnam, or failing him Rashid Ghazalli or failing him.......................................................................................................................... of

.............................................................................................................................................................................................................. as my/our proxy, to represent

me/us and to vote for me/us on my/our behalf at the Thirty Eighth (38th) Annual General Meeting of the Company to be

held at the Auditorium on Level 22 of “HNB Towers” at No. 479, T B Jayah Mawatha, Colombo 10 on the 29th day of

March 2007 at 10.00 in the forenoon and at any adjournment thereof and at every poll which may be taken in

consequence thereof to vote :

<table>
<thead>
<tr>
<th>In favour</th>
<th>Against</th>
</tr>
</thead>
<tbody>
<tr>
<td>To declare a final dividend of 25%</td>
<td></td>
</tr>
<tr>
<td>To re-elect Mr R T Wijetilleke, Director who retires by rotation</td>
<td></td>
</tr>
<tr>
<td>To re-elect Mr D H S Jayawardena, Director who retires by rotation.</td>
<td></td>
</tr>
<tr>
<td>To re-elect Mr M V Theagarajah as a Director of the Company</td>
<td></td>
</tr>
<tr>
<td>To re-appoint Auditors for the ensuing year/authorise the Directors to fix their remuneration.</td>
<td></td>
</tr>
<tr>
<td>To authorise the Directors to determine payments for charitable and other purposes</td>
<td></td>
</tr>
</tbody>
</table>

Signed this .................. day ..................... 2007.
Signature/s ............................................................
.............................................................

Please provide the details :

Shareholder’s NIC No./Company Registration No. .................................................................
Folio No./Number of Shares held .................................................................
Proxy holder’s NIC No. (if not a Director) .................................................................
Notes:

i) In terms of Article 67 of the Articles of Association of the Company –

This instrument appointing a proxy shall be in writing and

(a) in the case of an individual shall be signed by the appointor or by his attorney, and

(b) in the case of a company or corporate body shall either be under its Common Seal or signed by its attorney or by an officer on behalf of the Company or corporate body in accordance with the Articles of Association of that Company or corporate body.

The Company may, but shall not be bound to, require evidence of the authority of any such attorney or officer.

In terms of Article 68 of the Articles of Association of the Company –

The instrument appointing a proxy shall be lodged and the Power of Attorney (if any) under which it is signed or a notarially certified copy thereof shall if required be deposited for inspection at the office, in each case not less than forty eight hours before the time appointed for holding the meeting or adjourned meeting, or in the case of a poll before the time appointed for taking of the poll at which the person named in the instrument proposes to vote and in default the instrument of proxy shall not be treated as valid.

In terms of Article 62 of the Articles of Association of the Company –

In the case of joint-holders of a share, the vote of the senior who tenders a vote, whether in person or by proxy or by attorney or by representative, shall be accepted to the exclusion of the votes of the other joint-holders and for this purpose seniority shall be determined by the order in which the names stand in the Register of Members in respect of the joint-holding.

The first joint-holder thereby has power to sign the proxy without the concurrence of the other joint-holders.

ii) The full name and the registered address of the shareholder appointing the proxy should be legibly entered in the form of proxy.

iii) To be valid the completed form of proxy should be deposited with the Board Secretary at the Registered Office of the Company at No: 479, T B Jayah Mawatha, Colombo 10, before 10.00 in the forenoon on 27th March 2007.

iv) Every alteration or addition to the Form of Proxy must be duly authenticated by the full signature of the shareholder signing the Form of Proxy. Such signature should as far as possible be placed in proximity to the alteration or addition intended to be authenticated.
Form of Proxy - Non Voting

I/We ...................................................................................................................................................................................

of ...................................................................................................................................................................................

being a member/members of the Hatton National Bank Ltd, hereby appoint, Rienzie Theobald Wijetilleke or failing him Vijaya Perera Vittachi or failing him Rajendra Theagarajah or failing him Don Harold Stassen Jayawardena, or failing him Manickam Vallipuram Theagarajah, or failing him Rajpal Kumar Obeyesekere or failing him Pamela Christine Cooray, or failing her Ratna Sivaratnam, or failing him Rasheed Ghazalli or failing him........................................................................................................ of ...................................................................................................................................................................................

as my/our proxy, to represent me/us at the Thirty Eighth [38th] Annual General Meeting of the Company to be held at the Auditorium on Level 22 of "HNB Towers" at No. 479, T B Jayah Mawatha, Colombo 10 on the 29th day of March, 2007 at 10.00 in the forenoon and at any adjournment thereof:

Signed this .................. day ...................... 2007.

Signature/s ..........................................................................................................................

Please provide the details:

Shareholder’s NIC No./Company Registration No. ........................................................................................................

Folio No./Number of Shares held ..............................................................................................................................

Proxy holder’s NIC No. (if not a Director) ................................................................................................................
Notes:

i) In terms of Article 67 of the Articles of Association of the Company –

This instrument appointing a proxy shall be in writing and

(a) in the case of an individual shall be signed by the appointor or by his attorney, and

(b) in the case of a company or corporate body shall either be under its Common Seal or signed by its attorney or by an officer on behalf of the Company or corporate body in accordance with the Articles of Association of that Company or corporate body.

The Company may, but shall not be bound to, require evidence of the authority of any such attorney or officer.

In terms of Article 68 of the Articles of Association of the Company –

The instrument appointing a proxy shall be lodged and the Power of Attorney (if any) under which it is signed or a notarially certified copy thereof shall if required be deposited for inspection at the office, in each case not less than forty eight hours before the time appointed for holding the meeting or adjourned meeting.

The first joint-holder thereby has power to sign the proxy without the concurrence of the other joint-holders.

ii) The full name and the registered address of the shareholder appointing the proxy should be legibly entered in the form of proxy.

iii) To be valid the completed form of proxy should be deposited with the Board Secretary at the Registered Office of the Company at No: 479, T B Jayah Mawatha, Colombo 10, before 10.00 in the forenoon on 27th March 2007.

iv) Every alteration or addition to the Form of proxy must be duly authenticated by the full signature of the shareholder signing the form of proxy. Such signature should as far as possible be placed in proximity to the alteration or addition intended to be authenticated.
Driven by a new vision and guided by a new mantra, we set out to achieve certain corporate goals. We are happy to report that we have not merely succeeded in achieving our objectives, but we have exceeded every parameter we had set out to fulfill during our growth process. Receiving the prestigious Bracken Award for the “Sri Lankan Bank of the Year 2006” by globally acclaimed “The Banker” publication is considered a landmark achievement reflecting the commitment and passion of our team to settle for nothing less than the best!

We look back upon the year with positive satisfaction, knowing that we worked tirelessly as one team to drive our Bank to the top most echelons in the industry. Our achievements, we dedicate to the outstanding HNB team, who will continue to power the Bank’s progress into the future.