

## MANAGING DIRECTOR'S REVIEW



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*Where once our arena was limited to our shores it now encompasses the whole world. And yet the whole world now fits in the palm of a hand – often in the form of a mobile phone. Meeting the needs of our customers means competing with the latest technological innovations by smart start-ups and also the biggest brands in the consumer space. Are we prepared for this challenge? We certainly are.*



Through all the storms (both literal and figurative) that affected the region during the year under review, Commercial Bank remained a steadfast beacon in a volatile environment. Our customers find safe haven in us because we remain true to our original ideals of being a banker first and foremost. Adhering to our core business values resulted in substantial core business growth, high levels of stakeholder satisfaction and the ability to attract and retain a loyal base of customers with whom our ideals resonate.

**Banking to the core.** We are one of the few banks that remain true to our original values, focusing totally on pure banking. Our products are sound, uncomplicated, and straightforward, giving customers the confidence that from Commercial Bank they will always receive the attention they need for their banking requirements. As verified by an independent brand health study conducted during the year, Commercial Bank trended upwards, ahead of the industry, in areas such as banking service levels, speed and attentiveness, and employee competency in serving customers.

Our customers appreciate that our conservative ethos, prudence, and integrity provide them with greater security and stability – qualities they now value even more a decade or so after the global financial crisis which, despite having a low impact on Sri Lanka at the time, sent shock waves through the entire industry. Our customers trust us to continue being who we are as we move swiftly into a fast-evolving future.

At end 2017, we recorded Rs. 16.581 Bn. in profit after tax, a growth of 14.25%. Our deposits grew by 14.95% to Rs. 850.128 Bn., an average monthly growth of over Rs. 9.0 Bn., as we continued to maintain our leadership position in deposit growth within the industry. Our loans grew by 19.71%, an average monthly growth of over Rs. 10.0 Bn., supporting net interest income (NII) growth of 18.89%. The growth of deposits and credit, reflects the Bank's strong capacity for financial intermediation and illustrates a deployment of funding resources that is most conducive to the pursuit of productive assets. The main contributor to operating profit, NII, accounts for 78% of total operating income. Net fee and commission income grew by 22.62% thanks to a stellar performance in trade finance, credit cards, and remittances.

Operating costs increased by 6.49% primarily because we invested heavily in the digital technology that is vital for solid growth. With total operating income growing at a higher rate, the cost to income ratio marginally decreased to 49.82%. We continued to strengthen our risk management framework and recovery efforts during the year. This led to further improvement in asset quality with both Gross and Net NPL (non-performing loans) ratios decreasing to 1.88% and 0.92% respectively as at December 31, 2017 from 2.18% and 1.09% respectively a year ago, in turn boosting profitability.

The Personal Banking Division recorded a strong performance, increasing its contribution to profit before tax by 57%, with 16% of asset growth, and 14.6% of liability growth. Likewise, the Corporate Banking Division too grew solidly this year as well, growing its assets base by 23% and liabilities by 10%, thereby increasing its contribution to profit before tax by 25%. Our Treasury Division continued to focus on funding and liquidity, accounting for 24% of assets and 7% of liabilities. During the year, we borrowed USD 100 Mn. from the International Finance Corporation (IFC) to fund business growth. This came at a relatively lower cost and also eased pressure on securing funding from other sources. Further information pertaining to our financial performance is elaborated under "Financial Capital" on [pages 54 to 72](#).

**Banking through headwinds.** While economic stability and business confidence are improving in Sri Lanka, taxation pressures bring with them an element of instability. This especially impacts the banking industry which is perhaps subject to the most stringent regulatory requirements, on capital in particular. A long term view by regulators and the general public is imperative if the country is to benefit from an improving economic scenario.

It goes without saying that banks, by necessity, require capital. Investors who contribute to capital expect reasonable returns for the risks assumed. On one hand, increasing regulatory as well as economic capital requirements in the wake of minimum capital, Basel III, and higher provisioning requirements arising from SLFRS 9 make it necessary to increase profit retention. Yet, on the other hand additional tax burdens imposed on banks limit the internal generation of capital. Both affect the return

to shareholders. Naturally this impact on capital affects Sri Lankan banks with aspirations to expand overseas and bring long-term benefits to the country.

Commercial Bank is a listed company with a track record for transparency, efficiency, and productivity. It has the capacity to further financial inclusion within Sri Lanka and grow beyond our shores, putting Sri Lanka firmly on the map – both regionally and internationally. During the year, we contributed approximately 41% of our profits to the Governments through taxes. This was in addition to over Rs. 2.0 Bn. in taxes we have collected from customers on behalf of the Government. Looking to the future, regulators need to work together and take a longer-term view to ensure that while the necessary checks and balances are in place, banks are not stymied from achieving their full potential.

Given our predilection for prudence and forward planning, we began preparing for SLFRS 9 (which is equivalent to the International Financial Reporting Standard on Financial Instruments) two years ago, bolstering our capital and ensuring our loans and advances were recognised in the books in line with the Standard. We are now fully equipped to implement SLFRS 9 which became effective from January 1, 2018.

With stability as our cornerstone, we are well-prepared for Basel III – the internationally agreed set of measures developed in response to the financial crisis of 2007-09 – both with regard to capital and liquidity. We are comfortably above the minimum requirements prescribed by the regulator in respect of both.

The new Foreign Exchange Act, which replaced Sri Lanka's existing Exchange Control Act takes a more liberalised approach to the transaction of foreign exchange – focusing on management rather than control. While the new Act proved to be a sharp learning curve for banks, there has been reasonable clarity and we believe the Act will have a positive impact in the long term.

**Banking on the future.** Where once our arena was limited to our shores it now encompasses the whole world. And yet the whole world now fits in the palm of a hand – often in the form of a mobile phone. Meeting the needs of our customers means competing with the latest technological

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innovations by smart start-ups and also the biggest brands in the consumer space. Are we prepared for this challenge? We certainly are.

During the year under review, we invested in a digital solution that will cover the entire spectrum from online and mobile banking services to internal systems and processes. To enhance customer service with an optimum level of security, this is a top-of-the-line product from Fiserv, a global leader in financial services technology solutions. The new software solution will allow us to bring the convenience of online and mobile banking to the masses, ensuring that the communities within which we operate are future-ready.

Subject to regulatory approvals, our goal is to provide customers with a completely digital banking experience. Our new mobile banking offering, for example, will sit completely within the customer's phone, allowing them to do anything and everything related to banking wherever they are, whenever they want, without ever visiting any of our outlets at any stage.

In the meantime, with customer enthusiasm for automation growing ever stronger, we will continue to set up automated banking centres (ABCs), and assisted ABCs. All new and newly refurbished branches will feature automated banking divisions to meet growing customer demand. The ABCs are a win-win solution for the Bank and our customers – a cost-efficient way to provide access to banking services around the clock. Such keenness for digital solutions among

the general public bodes well for Sri Lanka's future. Feel free to turn to the section titled 'Outlook for 2018 and Beyond' (on pages 44 to 46) to learn more about our plans for the future.

**Banking beyond our shores.** We continued to expand our business overseas in pursuit of growth and as a strategy to diversify risk exposures. Reflecting our stability and potential, International Operations contributed 17.5% of the profit before tax and accounted for 11% of total assets.

Our ventures overseas began in Bangladesh with the acquisition of Crédit Agricole Indosuez in 2003. With an ever increasing range of customer touch points there, including Internet banking, we continue to make a name for ourselves as a leading regional bank.

Our business in the Maldives has broken even in just over a year of operations and is now making a positive contribution to the Bank's profitability. During the year, we also opened a second branch on the island of Hulhumalé, which is connected by road to the airport island of Hulhulé.

In Myanmar, where we established a Representative Office in June 2015, we received a microfinance license in 2017. In 2018, we will concentrate on building and growing our operations in the country – ensuring that the groundwork for information technology systems, and Human Resources and other processes is well laid out.

Besides our office in Rome, we are now present in eight other cities in Italy. Our license to operate in this country is a European Union license which allows us the opportunity to expand our business across the EU. Naturally, we are actively pursuing opportunities to grow in Europe.

Having revamped our Social and Environmental Management System (SEMS) with technical input from the IFC, we will extend its application to our business in Bangladesh and the Maldives. This means that a greater part of the lending conducted through our International Operations will be evaluated through SEMS. We also worked with an IFC advisory to train our people to be able to identify and focus more on green lending opportunities, adding further value to the communities within which we operate.

**Thanking our stakeholders.** I am very thankful to all our stakeholders for their support – especially our shareholders for the capital that they have entrusted to us – our rights issue in June 2017 was fully subscribed. I am also grateful to our customers whose loyalty is our strength and whose banking needs inspire us to reach new heights in innovative banking every year.

Our success has always pivoted on our winning team and the year under review was no different. With the wisdom and guidance of the Board, for which I am ever grateful, our people continue to build on their reputation for dedication and commitment. Yet again, they have pulled together to produce another strong set of results. The unmatched haul of awards we have received year after year are testament to their engagement and drive, and have made us the Most Awarded Bank in Sri Lanka. These accolades include Best Bank in Sri Lanka (Global Finance Magazine, USA) for the 18th year and our position as the only Sri Lankan bank to be within the Top 1,000 Banks in the World (The Banker Magazine, UK) for the seventh consecutive year.

To all our customers – I thank you for your loyalty and patronage. We will always endeavour to be worthy of it. To the Board whose guidance and visionary leadership I greatly value – I extend my warm appreciation. I am also grateful to the banking and financial services regulatory authorities of Sri Lanka, Bangladesh, Italy, the Maldives and Myanmar for their cooperation. Last, but by no means least, to every single member of staff – my heartfelt thanks for your invaluable contribution.

At Commercial Bank, we take pride in the role we play in furthering financial inclusion in Sri Lanka and our commitment to the community remains as strong as ever. We are aware of and fully prepared to shoulder the hopes and dreams of our stakeholders as we continue banking on the future.

**Jegan Durairatnam**  
Managing Director/CEO

Colombo  
February 23, 2018