

CHAIRMAN'S STATEMENT



The Bank recorded an enhanced overall performance across all business lines and geographies, enabling us to report growth in excess of the industry averages in most of the indicators. This is all the more significant when viewed in the context of the conservative risk profile and prudent growth pursued by the Bank.

Having established ourselves as the leading private sector bank in Sri Lanka, overseas expansion is now one of our foremost strategies which will help us geographically diversify our risk profile.



Dear Friends,

A hallmark of Commercial Bank is its consistent and steady growth over the years. Year 2017 was no exception. The Bank recorded an enhanced overall performance across all business lines and geographies, enabling us to report growth in excess of the industry averages in most of the indicators. This is all the more significant when viewed in the context of the conservative risk profile and prudent growth pursued by the Bank.

Prudent growth

Total assets grew by 12.96% to Rs. 1.143 Tn. as at end 2017 with core business activities of loans and receivables and deposits growing at 19.71% and 14.95% respectively, which augurs well for the Bank's commitment to long term value creation. Five-year compounded annual growth rate in excess of industry growth enabled us to grow our market share in total assets to 11.1% from 10.04% in 2012, further strengthening our leadership position. In August 2017, Fitch Ratings Lanka Ltd. reaffirmed the Bank's rating at AA (lka) with a stable outlook while Credit Rating Information and Services Limited reaffirmed Bangladesh Operations' at AAA in June 2017. Profit before tax grew by 15.62% to Rs. 23.183 Bn. while profit after tax grew by 14.25% to Rs. 16.581 Bn. for the year. The Board of Directors recommended a final dividend of Rs. 2.00 per share for approval by the shareholders at the forthcoming AGM, to be fulfilled by way of a scrip issue of shares, which together with the two interim dividends already paid in cash, add to a total dividend for the year of Rs. 6.50 per share. Taking into account the challenging context in which these robust results were achieved during 2017, I wish to begin this review by extending my warm appreciation and congratulations to the Board and the dedicated team led by our dynamic Managing Director.

Before reviewing our performance further, let me first set the context. Impacted by events in global and domestic markets, 2017 presented a challenging environment for the industry.

Challenging times

Globally, economic activity certainly strengthened when compared to the preceding year, recording a projected growth of 3.7%. While the baseline outlook for 2018 is strengthening, growth remains weak in many countries, with a large number of advanced economies recording inflation that is below the target. Importers of commodities such as fuel, were affected as they adjusted to an increase in prices. While the short-term risks appear to be balancing out, medium-term risks still list downward.

In Sri Lanka, the economy recorded lower than projected growth during the year, primarily due to weather taking a toll on the agricultural sector. Core inflation remained in check, thanks to the Central Bank's tight monetary policy stance, but headline inflation was high. Interest rates were high at the beginning of the year, but gradually declined towards the latter part of the year due to deceleration of credit to the private sector, higher liquidity levels, moderate inflation and lower levels of borrowings by the Government consequent to enhanced revenue collection. Restoration of GSP+ helped boost exports. Credit to the private sector by commercial banks, which grew at a higher rate in 2016 and up to mid 2017, decelerated in the second half of 2017. Asset quality in terms of gross NPL ratio, however, improved marginally from 2.6% at end 2016 to 2.5% at end 2017.

Import expenditure increased during the year and Sri Lanka's trade deficit widened, offsetting the positive impact of improving export earnings. Net inflows to the Government securities market and the Colombo Stock Exchange somewhat eased pressures on external accounts. Depreciation of the Sri Lankan rupee against the US dollar was 2.57% during the year and the Central Bank was able to maintain a flexible exchange rate regime under the enhanced monetary policy framework. Fiscal consolidation is expected to continue in the medium term and therefore we can look forward to experiencing macroeconomic stability in the future. Gross Domestic Product (GDP) too is projected to grow between 5.0%–5.5% in 2018. Overall, we remain positive about the medium term prospects of the Sri Lankan economy.

Within this challenging local and global backdrop we forged ahead, adopting new strategies and exploring new areas of business. More details on the Bank's performance are given in the Managing Director's Review and the Financial Review.

Our SME focus

We are heavily SME (small and medium-sized enterprises) focussed. As I mentioned in my Review last year, we believe that the SME sector is the backbone of the economy and this is reflected in our lending portfolio. Over 12% of our lending is to SMEs. With its potential to make a high contribution to the GDP, employment creation, export revenue, poverty alleviation, and regional development, a strong SME sector spells good health and prosperity for the entire economy. We have taken a number of initiatives during the year to improve the lives and livelihoods of those in this important sector. For instance, the Bank launched Commercial Bank Biz Club allowing SMEs a forum to network and share ideas about their businesses (please ☐ refer page 62 for more details of our focus on this sector).

Regional expansion

Having established ourselves as the leading private sector bank, overseas expansion is now one of our foremost strategies which will help us geographically diversify our risk profile. I am happy to note that within a relatively short period of time, the Bank has established itself as a premier regional foreign bank in Bangladesh and the Maldives. Now completing its fourteenth year in the country, our Bangladesh operations accounted for 11% of our assets and 12% of our profit before tax in 2017. With the gradual expansion of the branch network in this country, the Bank is now ready to gradually attract SME and retail clientele, allowing us to mobilise low cost deposits and improve profitability. Commex Sri Lanka S.R.L. – Italy, our fully owned subsidiary, which was issued with an Authorised Payments Institute License by the Bank of Italy in 2016, has strengthened our remittance business and is already making a positive contribution. This license opens up many avenues for us to make further inroads into Europe and, naturally, we are already making plans to make full use of this opportunity.

The Board also continued to ensure the highest standards of corporate governance and adherence to the Bank's Code of Ethics. Besides ensuring compliance with the applicable rules and regulations true to both the spirit and the letter of the law, the Board keenly monitored progress of implementation of Basel III regulations and SLFRS 9 standard, two developments that promise to strengthen the financial soundness of banks, but will have significant impact on the profitability of banks.



Commercial Bank of Maldives Private Limited was established in 2016 and is a fully-fledged Tier 1 bank under license issued by the Maldives Monetary Authority. This subsidiary too, I am proud to say, is already contributing to the Bank's profits. Our recent microfinance license in Myanmar is another exciting development that will, in due time, contribute to the Bank's profits and geographical diversification.

Digital leadership

As the only Sri Lankan bank to have an extensive reach beyond our shores, we are conscious of the need to stay abreast of global trends in banking and customer service. For us, 2017 was a year in which we intensified our focus on exploring methods that will further increase efficiency and productivity through the use of state-of-the-art technology.

Our efforts encompassed digital banking and automated banking centres, two areas that are fast gaining popularity in Sri Lanka and abroad. We also looked at innovations that would better streamline systems and processes, integrate workflows, and centralise operations. For the customer, these implementations mean greater convenience and uniform service standards no matter where they come into contact with the Bank.

We continue to monitor the many different cases of cyber security breaches around the world with an ever-vigilant eye. They highlight, now more than ever, the importance for caution and agility. It is to safeguard customer wealth and data, as well as our own intellectual capital, that we invested in a top-of-the-line digital banking platform from a world-renowned financial services technology solutions provider during the year.

Indeed, customer centricity and digital leadership are two of five strategic imperatives by which the Bank's operations were steered in 2017. Together with prudent growth, operational excellence, and risk management, these strategic imperatives were supported by a robust governance framework, and adhered to across the Bank at every level with able support from the Board.

Customer centricity

Customer centricity is built into the culture of the Bank.

The Bank is embracing new technology in order to meet the demands for enhanced user experience by customers, millennials in particular, while achieving operational excellence. During the year, the Bank partnered with FISERV, a leading software vendor from the USA for procuring a digital banking solution which is expected to go live by mid 2018. This solution would enable omnichannel presence and provide a true contextual banking experience to customers across web, mobile phones, tablets and wearables. The Bank is looking towards establishing partnerships with global IT players such as Microsoft and IBM in order to provide a better customer experience.

Our Social and Environmental Management System (SEMS)

Demonstrating our commitment as a responsible corporate citizen to the worldwide efforts in protecting society and the environment, we have developed a SEMS incorporating a set of rules and objectives which guide the Bank in its assessment and management of social and environmental risks associated with our operations, lending activities in particular. During the year, we revamped the SEMS with technical input from the International Finance Corporation and strengthened it further by recruiting experts and impanelling consultants from the market. SEMS, as part of the Loan Origination System, now plays a key role in managing the risk profile and making lending and investment activities responsible.

The Bank also worked with an IFC advisory to train staff so that they are able to identify and focus more on green lending opportunities. These are related to alternative energy generation from windmills, solar power and mini hydropower and other environment friendly initiatives such as the implementation of carbon emission reduction programmes, and the installation of more efficient lighting systems in office buildings etc. During the year, the Bank disbursed Rs. 13 Bn. in green loan facilities that will help reduce the environmental footprint of borrowers.

Governance and Board oversight

Ever mindful of its statutory, fiduciary, and regulatory responsibilities, the Board continued to strengthen its oversight responsibilities on the affairs of the Bank. During the year, the Board welcomed two new independent non-executive Directors namely, Justice K Sripavan and Mr T L B Hurulle to fill casual vacancies. They bring with them a wealth of experience from their respective fields, widening the collective knowledge and expertise of the Board.

The Board also continued to ensure the highest standards of corporate governance and adherence to the Bank's Code of Ethics. Besides ensuring compliance with the applicable rules and regulations true to both the spirit and the letter of the law, the Board keenly monitored progress of implementation of Basel III regulations and SLFRS 9 standard, two developments that promise to strengthen the financial soundness of banks, but will have significant impact on the profitability of banks. The Board reviewed the composition and terms of reference of Board and Management committees taking into account developments in the industry and best practice and took measures to strengthen their performance. The composition of Board Related Party Transactions Review Committee was reconstituted to comprise only Non-Executive Directors from January 2018 in line with the requirements of ICASL Code of Best Practice on Corporate Governance. Strategic decisions were made based on the outcomes of reviews of ICAAP (Internal Capital Adequacy Assessment Process), risk profile and risk mitigation measures, and business continuity and disaster recovery plans. In preparation for enhanced capital requirements of the Bank as a Domestic Systemically Important Bank under Basel III, the Bank raised Rs. 10 Bn. through a rights issue.

I take this opportunity to state that, as at the date of publishing, we had complied with all the applicable regulatory requirements and best practices to maintain our position as one of the most compliant financial institutions in Sri Lanka.

The people behind our operational excellence

Adherence to standards and regulations requires the engagement and dedication of our people. This year was no different with employees rising to the occasion and proving their loyalty and commitment. They continued discharging their duties and preparing themselves to make the most of upcoming opportunities, as the Bank put in place the necessary systems and processes to support their work.

It gives me great pleasure to report the finalisation of the new collective agreement which was completed on time and with the concurrence of all parties. Cordial relations continue between our branch of the Ceylon Bank Employees' Union, the Executives' Association of the Bank and the Management. This is an ideal opportunity to thank their collective efforts and great contribution to the progress and success of the Bank.

At the end of another impressive year I would like to give all credit to the entire Commercial Bank team. That they succeeded in winning for the Bank an unparalleled haul of awards – justifying our claim of being the “Most Awarded Bank” – was simply the by-product of an engaged group of hard-working individuals inspiring each other to achieve common goals amidst the challenges of the times. To each one I extend my heartiest thanks as we forge ahead into the future – onwards and upwards!



Dharma Dheerasinghe
Chairman

Colombo
February 23, 2018