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Webinar with investors and analysts

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Corporate participants

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Forward Looking Statements

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Investor Presentation

Rajendra Theagarajah

Good morning ladies and gentlemen, on behalf of the Board and the Management of National Development Bank let me warmly welcome all of you taking time, trouble to dial in on this investor conference call. Last evening we finalized and released the second quarter 2016 financial performance to the stock exchange and I believe that a copy of the investor pack has already been uploaded on the website as well. So what I will try and do is in the next half an hour or so, initially make some general comments on how we performed and then take you through some of the key financial indicators and then, invite questions and answers if there are any.

Slide 6 - Macro Economic Overview

So let me first broadly touch on the macro-economic situation. The private sector credit growth continued at reasonably modest growth. The year-on-year growth is seen close towards the 30% rate at 28%. Despite the policy maker's moderated expectations which came towards the second quarter, looking forwards towards a more reduced level, so I guess the forward look would be to moderate the private sector loan growth expectation within the next two quarters, which again is also a reflection of the liquidity prevalent in the domestic market.

The inflation, both at headline level as well as core, continues to increase, which reflect the demand driven pressure in the market. On the supply side, unfortunately we also saw the destruction which arose due to the unfortunate weather conditions in the country. The Central Bank certainly took a couple of measures to prevent the economy from overheating. We saw the capital reserves ratio increasing by 150 bps, to 7.5% in November 2015, and we saw the policy rates increasing twice during 2016, first in February and then in July, which again signals towards a more tightened policy regime.

Slide 7 – Awards & Accolades

Before we get to the financial numbers, I think the Bank continued to earn its respect among the various stakeholder segments which assess and recognize the Bank in various performance matrices. Euromoney continues to recognize our investment bank as the best investment bank in Sri Lanka for the fifth consecutive year, and in Bangladesh I believe that we won the same award for the third consecutive year, which recognizes the market leadership. The Asian Banking and Finance Awards 2016 again recognized the Bank in four segments, the best retail bank, best SME bank, the award for the outstanding social media interactive initiative for the year as well as the best domestic project finance bank of the year, which again demonstrate the resilience of the Bank.

We were extremely delighted and this is relative and relevant in your space ladies and gentlemen, this year, the CFA Sri Lanka recognized NDB with a gold award, for the highest or the best investor relations and this is not a stock start which we did this year. It is the culmination of a 3-4 year ascend, where we started this journey as way back as 2013 with the bronze, then we went on to the silver, and now it is a gold. So it is a step by step ascending to the pinnacle in terms of transparent, timely, robust and accurate investor information. For that we would thank you as a very important stakeholder group in recognizing NDB for its initiatives. And I would like to invite one of the key drivers in the Finance Team who led this initiative as a part of this investor team, Kumudari Peiris. I would like to on behalf of all of us thank Kumudari and the Finance Team for giving extreme focus in this initiative.

Slide 9 – H1 2016 Performance Summary

Then when we look at the financial performance for the first half, an overall snapshot replicated to some of the highlights, operating income has shown a 6% growth in the first six months. This was a 7% as at the end of the first quarter. So it's almost stable. The operating expenses have grown by a modest 7% in the six months. This number was around 10% in the first quarter, so we have tightened the control of operating expenses even further during the six months period. The profit attributable to ordinary shareholders is just around 1.1 billion which is a drop of 25%. What is very positive about this is, this number was a dip of 37% as at the end of March, so that reduction has come down to a lower 25% and we are hopefully, gradually but progressively reducing that gap during quarter-on-quarter.

On the asset front, the growth has been around 16% year-on-year. Lending has grown at 21% and deposits at 12%, and this is naturally a concern to us, whilst the deposits have grown but we certainly have a challenge given the quality pipeline of lending opportunities we have in the market. First of all our aspiration and growth in that area will be moderated for the exchange of our ability to mobilize deposits in the market. That is a challenge for us.

On the cost to income side, it has been at 53.7% which is reasonably flat in relation to the first half of last year. I think we will be relentless in our focus to try to build on it further. The net interest margins are at around 2.7% and I believe that the industry as a whole has continued to demonstrate downward pressure in margins. I guess we have managed to defend our margins around the same level as last year. The return on average equity has certainly come down to 7.6%, which was the number which we published as at the end of the first quarter, though it is around the same now. But this is not something which is a desired ratio; I think we can double that.

The loans to deposits ratio is around 118% and that is a reflection of the fact that our appetite for lending and the deep pipeline far exceeds the growth in the deposits in the last six months, and that is a challenge we will have to continue to face and then I guess the intelligence will be to what extent we are able to balance our ability to continue to mobilize deposits against our aspiration and thirst to grow the loan book. So I think at some stage, we are already examining the trade-off in this, in terms of perhaps a more moderated loan growth in the second half.

The capital adequacy is at 14.9%, still above the industry- the regulated norm, but as and when we keep on growing the loan book naturally, it will be a drain on the ratio which is something we are mindful of looking towards this. The liquidity ratio is at 21%, and I believe we will talk a bit more about the liquidity coverage ratio as we go on.

Slide 10 – Income Statement

On the income side, more detailed analysis - if I look at the net interest income, we have seen a growth of 11% year-on-year for the first six months. Now this figure was as low as 4% during the first quarter. I think as was demonstrated and as was articulated to you during our previous investor conference our focus on relentless repricing and selectively growing the pool in relation to the repricing initiative is working and will continue to work as demonstrated by this particular indicator. In term of the operating income, we will talk a bit more about that, it has grown by around 6% which is almost same as the first quarter. The impairment figure is 879 million, which is a big jump of 304% in relation to last year. We had dedicated a separate slide toward the middle of this presentation and I would like to spend some time to discuss that as we go on.

The operating expenses have grown by a highly modest 7%, a reduction from the 10% growth in the first three months. Operating profits is at just over 2.14 billion. Whilst it shows a reduction of 19% for the six months, you ladies and gentlemen, you should be mindful that this figure was as high as -34% as end of March. That again demonstrates the progress we have made in reducing that gap.

Taxation, we have seen a reduction in relation to the first half of last year, it has gone down in absolute terms by 17%, but from an effective rate point of view, almost the same. I think we already have a couple of few who have already sent some questions in advance on this subject which I will articulate as we progress in the presentation.

The profit attributable to ordinary shareholders as I said is just under 1.1 billion, which is a drop of 25%, over the same period in 2015. However, you must be mindful that this figure was as low as a -37% at the end of the first quarter 2016. So it is again a progress towards reversing that reduction.

Slide 11 – Net Interest Income

The net interest income, if we look at this again, this particular slide shows that as I said, the number has increased by 11% in relation to the first quarter growth of 4%. I think here the challenge for us has been on the income side. Despite a modest growth in the asset book, the repricing seems to have taken place well. But on the liability side, I think we had two challenges, *a)* the quantum of deposit growth in liabilities was not as high as the appetite on the asset side. So there was a challenge there. Secondly, the market liquidity, there was a war for deposits, which means that the price for term deposits also went up. Given the mismatch between the asset growth and the liability growth, our reliance on the money market continues to be moderately high. With the volatility in the money market rates that also spiked and contributed to a higher increase in the interest expenses which grew by 38% against the interest income which grew by 28%. However, the outcome was that the net interest income itself grew by 11%, which we are moderately happy about.

Slide 12 – Non Interest Income

On the non-interest income, we see the fees and commission at a group level increased by just under 3%. From a Bank's point of view - from the commercial bank point of view, this was a growth of 15%, well contributed by the core banking contributory activities. I think at the Group level, the moderation was because of the capital market condition, some of the opportunities which our Group companies would have seen moderated due to market condition. Hence the Group growth was around 3%. The second figure which is the gain or loss in trading was 456 million which is a dip of 2.5%, which was mainly due to the outcome of forex trading. I think given the market ring-fencing which took place in the last month the opportunities for forex was fairly limited.

In term of the other operating income we have seen a total contribution of 330 million which was a drop of 18% in relation to the previous year. Now this has two components. The 330 million, the first is around 207 million of that coming from ALM contribution/ asset and liability management contribution. The balance 123 million comes in from a combination of dividend income as well as the revaluation of the balance sheet. So again, yes a modest growth in forex and ALM in relation to the previous years. But there again, what we saw last year was ALM, given the agility of the Team, whenever there is a window of opportunity the Bank performs. I think last year towards the end of the year during Q3-Q4 the Team demonstrated its resilience by making use of a specific window of opportunities.

The second thing I would also like to tell you is when we look at this gain or loss from financial - also when we look at the (123 million) in terms of the other income in addition to the dividend income as well as the revaluation, you have the gain on the sale of the government securities. Last year during the first six months we made 62 million, for the first six months and that figure has reduced to as low as half a million rupees. But it was a very moderated opportunity in terms of the capital market and the bond trading.

Slide 13 – Operating Expenses

Then we get to operating expenses. The main component, if we look at personal expenses a modest; I think a well-controlled growth of 4.4%, in relation to the first quarter. In March, this figure was as high as 8.4%. Still below the overall benchmarking which would have been around 10%, so we are very pleased that despite a growth in the network, having opened some 9 or 10 branches during the first six months, personnel expenses have been contained.

Other expenses which are mainly also attributable to branch expansion costs is still modestly controlled at 8.3%, despite having opened the mentioned number of branches in the first half. This figure was at 12.5% as at the end of the first quarter. So again we are demonstrating a downward moderated expenses growth during this year, which was a commitment we gave you earlier in the year.

Slide 14 – Balance Sheet

In terms of the balance sheet, the book itself has seen a fairly modest growth of 2% which is a reflection of, I guess is also of the policy direction of the moderating growth. The loan book has increased really by 5% during the year. Are we happy with it, from an appetite point of view I would say no, because the opportunities have been of plenty. But what reality has told us is, two things to be mindful of.

First thing is our commitment for re-pricing and margin management which has to balance our appetite to grow the book. Secondly to be mindful of the underlying liability base which is available to support the asset growth, so I guess, given those two challenges, the 5% growth for the first six months, in the management's opinion is satisfactory.

In terms of the liabilities, the overall deposit base has shown a moderated growth of 3% and this is what I was telling you about, that the challenge in our growth, we have to be and we continue to be dependent on the ability of mobilizing deposits from an ever drying, ever tightening market. That is a challenge.

Slide 15 – Loans and Advances

If we look at the loan growth itself, on a year-on-year basis, even though the first six months has shown a moderated 5% growth, but still benefiting from the tail end of last year, year-on-year is 21%. In terms of the segmental growth, we are seeing the project finance arm still continuing to grow given the market and country opportunity at as high as 44%. The retail and the SME is showing a pleasing growth, it's pleasing that the network is contributing and growing towards a better contributing retail and SME segment in terms of margins, the growth has been as high as 30%.

What we have seen is that the corporate banking, which is the larger ticket book which comes under greater margin pressures has seen a highly moderated growth of 4%. It was calculated given the challenges and the focus we had on margin management.

Slide 16 – Asset Quality

In terms of asset quality, the gross NPLs are as similar to last quarter at 2.5%. If I look at this figure and the impairment allowance as a percentage of gross loans, it is around 2.4%, well within the risk appetite/ internally agreed by the management and the Board. It is around 2.5%.

What this slide gives you on the bottom right had side is an industry trend. I would like to highlight your attention towards the bottom two bars, which is important, because if you compare those two bars in relation to the actuals which were reflected as at the end of Q1, the first bar which is the agri-sector is now showing a figure of 4.8%, against a 3.6% which was shown in Q1. That 1.2% is due to one particular agri business, in the business of manufacturing and exporting of tuna as well as agri related products; a facility of below 200 million, getting in to NPL status. This by no means is in any undue stress, but it went beyond the 90 days which gave us the need of prudently classifying it, but it is not something which we are threatened by at the moment. If we take that away, the 4.8% actually will be showing a figure of around 3.7%.

Secondly the bottom bar, which is in the textile and apparel sector, shows a figure of 8.6%, and this figure was around 6.9% as at the end of March. Now this might give you the impression that this figure within the last period has shown a 2% growth. But you've got to be mindful that the absolute increase in the NPL on this particular sector is only LKR 43 million. The rise in the percentage was because; the absolute value of the portfolio in this sector has reduced by around 3.2 billion rupees during the quarter. So it was the denominator which actually contributed to a higher percentage and not an absolute increase in the portfolio and, if we take away the adjustment of the portfolio reduction and the two one-offs which we reported in the first quarter, if we take those two away, the adjusted sector percentage is at 4.1%. So the take home for this slide is that the largest bar of 8.6% shown in absolute terms is an increase of only rupees 43 million.

Slide 17 - Customer Deposits

So customer deposits again, as I said the figures have increased by 12%, the main challenge is given the moderated growth in deposits in relation to loans, the challenge is to moderate the asset book.

Slide 18 - Capital Adequacy

Then if we look at capital adequacy, the overall adequacy figure is showing a figure of around 10.9% in terms of Tier I and the total is 14.9 or 15%, which is still healthy but seen as a challenge given the growth in the asset book. So this is something we have to as a Group, continue to address. On leverage times we are at 11%.

End of reference to slides.

Further elaboration on impairment charges

Now I would like to spend some time, focusing also on the impairment numbers. As at the end of March when we reported a PAS of 547 million, the total impairment was around 537 million rupees which had two components. 350 million for individual impairment and 187 million for collective impairment. This figure has increased from 537 in total to 861 million as at the end of Q2. So in absolute terms, the absolute increase in specific/ individual impairment has only increased by 88 million during the last three months, only 88 million. The real jump during the last three months has come in due to the increase in collective impairment. The collective impairment which we have made for the last three months has been 236 million.

As a total, if we look at the overall figures of 861 million for the six month, almost 50% of that which is 423 million comes from collective impairment. 438 million which included the 350 which we provided in

Q1 comes from specific. So the message ladies and gentlemen is, in Q2, the individually significant portfolio impairment has moderated very well down. It has gone down as much as about 1/4 of what we did in the first quarter, which is the positive side. Not so positive side, which is a factor of multitude of things, in terms of the industry economic indicators, as well as our own Board approved Impairment Policy and formula regarding how we compute, the collective impairment on the loan book has increased, due to some of the indicators in terms of probability of loss, as well as loss given default. These are indicators, which keep on shifting based on the amount of data which we drill down as well as the recovery patterns are monitored.

So when we say that the collective impairment for Q2 in absolute terms has been 236 million, yes it is a challenge, what we are mindful of is that this is not a cash charge to P&L. It is a provision. For this provision the way they go up and also come down, because they are not attributable to any single loan. What is important is that we explain the rationale behind these numbers. I would also like to make one other comment that whilst the LDG numbers and the formula which is the internally approved conservative policy, whilst it shows that this increase of 236 million for this quarter, what we did see from an absolute point of view is that as an increase, that provision is an increase of 22% against a modest growth of 5% in the portfolio.

Summary

So I think that brings us to the conclusion of the overall financial performance highlights. But in conclusion my summary take home is, the profit attributable to shareholders of 1.1 billion, whilst being a drop of around 25% year-on-year, is not the best you would like to have seen. But what we are pleased about is, it is a huge improvement in relation to where we were in Q1. So it’s showing a progress which we have committed to.

The second point is our strategy on margins, which for NDB itself has moderated. We have arrested the reduction, if at all it is inching upwards, but given the continuous challenges on the industry, our strategy would continue to be selectively to grow the loan book not at the expense of pricing. So this will continue to be relentlessly followed, also with revenue leakages monitored. So that's a challenge and an opportunity.

Management of deposits growth is certainly more challenging compared to other challenges. But till we get to the level of deposit growth which we like to see, we will have to moderate our loan growth also to reflect our ability to manage the underlying funding. So that's a strategic decision and a strategic challenge which the management will have to collectively address.

We are very pleased at the Bank level to see good growth in fees and income from core banking, even though from a Group point of view, given the capital market challenges, the group has shown moderation, we are happy that the Bank is getting back to core banking growth. So I think it continues to be a challenge given the market limitations but this Bank has been one which has always demonstrated its nimbleness and its agility to perform in specific windows of opportunity, so if there is ever a window which comes up during the last two quarters, the Team will perform.

One other thing I would like to mention is that during the last quarter along with the country downgrade, two of the rating agencies downgraded I think 5-6 banks, and Fitch one of the two rating agencies, included us as well, as a part of the downgrade. So we were downgraded by one notch which certainly is not pleasing, it is a challenge. Saying that, what we were optimistic and positive is that the rating was indicative to us by saying that any rating upgrade would be a reflection or a result of getting our capital augmented to reflect the type of growth we have been entertaining. That is something which the Board is very mindful of. At the right time, the Board would be at a position to announce what it has in mind to address that particular issue. But it is very much within the Board Room conversation at the moment.

So I hope that set of comments have clarified our position I would like to take questions now.

Q & A Session

I would like to take questions now. But before we get on to invitee questions, I would like to specifically address a couple of questions which have been already forwarded to me.

Q1. Despite the Bank adopting VAT at 11% (as per the notes to the financials, due to the court rule), what resulted in a relatively high 2Q2016 and 1H2016 Effective Tax Rates of 48% and 47% respectively for the group? What was the reason?

The reason, I guess was in the first quarter of 2016, that increase was really due to the increase in the financial services VAT paid on Group dividends received at the Bank level - Group dividends which came to the Bank. So we paid VAT on that. Secondly, on the second quarter of 2016, the reason for the again similar level of effective tax rate was not because of a higher Group dividend, but because of a higher collective provision made on the loan book, which had to be added back for the purposes of income tax. Collective provisions are also treated as a permanent difference for deferred income tax.

Q2. Why has the apparel and textile sector bar increased in relation to Q1?

I took that question earlier in the explanation.

Q3. What is your assessment regarding credit cost for the full year of 2016?

I guess what was expected there is the estimate as impairment as a percentage of net loans for 2016. So we believe that as a percentage of gross loans and advances, it could be around 2.5% - 2.6% for the full year.

Q4. What seems to be the reason behind the -3% QoQ contraction behind the deposit base, given that some other banks have shown a higher deposit growth?

There was also reference to Hatton National Bank reporting a 6% deposit growth during the same period. I guess as a smaller bank, a growing bank, with a lower CASA when you have a higher loan growth, you have a challenge to grow the deposits. But you also have a whole pack in the industry going after the same pool of deposits. Our ability to pay a premium for the deposits is certainly more challenging than some of our bigger banks. Because we have a smaller base. We have to intelligently manage the ability of paying a premium - incremental premium for incremental deposits whilst also managing margins. That is a very difficult decision. But I think that is a challenge for leadership - to be able to balance the thirst against reality and that is something we have been constantly battling for the last six months and I would say, no two banks would be able to give a similar solution for the same challenge.

Q5. What are the initiatives the Bank will take to strengthen the Tier I capital base?

The conversation is at the Board room level. It will naturally have to be capital augmentation. Of course the ploughing back will certainly help. Our dividend policy to our shareholders is to pay an exceptionally good dividend, and on the belief that if the story is good and the story behind the appeal is good, the shareholders will also back the capital call. So I guess our strategy would be to engage the shareholders more on a capital top up at some stage, rather than moderating dividends, as a strategy. That is one we have always been consistent with.

Q6. Is there any update on the single individual impairment granted to an apparel company in Q1 2016? Were there recoveries?

The recovery process is continuing, there were some recoveries in terms of asset sales, but there are still some ways to go in reaping the full benefit of the recovery efforts.

Q7. Central Bank has mentioned that they are looking at a LKR 20 billion minimum core capital by 2017. NDB Bank shows as at the second quarter, a 20 billion figure. If this requirement is imposed on banks, I believe there would be a bit of pressure on NDB core capital. Therefore is the Bank looking at equity infusion in the near term. If so, would it be a rights issue or a private placement.

At 20 billion, I think the Bank is well within the - any possible regulatory upward revision which may go from where we today towards 2017. But remember we still have six quarters to get there to the end of 2017, which also includes profit plough back. But certainly as a part of our strategic plan last year the management identified the need for infusion sometime this year and the Board has been kept informed and that conversation is continuing. When at the right moment we will make that announcement to the market. Also let's bear in mind, unlike in some of the other banks which have most of their business in the commercial banking side, as a banking Group, NDB's total Tier I capital is not 20 billion Its 28 billion.

So I guess there is still some bandwidth available if needed to make use of the Group's strength in support of Tier I.

Q8. Why did net fee and commission income dip in Q2 2016?

The figures we showed were at group level and as I said, at the Bank level it was growing as much as by 15%, and I very clearly articulated the 2.8 or 3% dip was mainly because of the moderation we experienced at the group company level because of the capital markets condition which is the reality.

Q9. What is the expected loan growth and deposit growth for full year 2016?

So we are currently re-calibrating the forecast for the next five months which is to be discussed with the Board. But certainly our expectations would be not to go after the 20% plus loan growth for the full year, because it would be meaningless, *a)* when policy directive or the policy indications are to show a moderation in overall credit to the private sector, and secondly the way the management reads the domestic liquidity position. We continue to see a moderation/challenge in the domestic liquidity market. In that situation we also see the opportunity for deposits growth more moderate in relation to our initial expectation. So in that context expecting a 20% or more loan growth is not meaningful. So I think we would look at a more moderated figure between perhaps somewhere in the high 10s - high to mid-10% for the full year.

Q10. What is the maturity classification of time deposits?

Chandana Guniyangoda

The duration of the maturity patter for time deposits is more or less more skewed towards one year maturity. That has not changed significantly over the last quarter.

Q11. On the reasons which you mentioned as to why the charge for collective impairment increased, is it a change in the floor rates or are there changes in your assumptions on what you all are taking for probability of default and loss given default? If it is the latter, can you give us some clarity of what these changers are/ where these assumption changes are?

All I can say is there has been no change in terms of the PD assumption as such. Of course in terms of the Loss Given Default, the LGD, the changes-the charges would change of course with historical data being more improved and as you get more and more granularity in the data, as the loss indicators get more clear. So I think the real challenge is to further improve the quality of historical data which will help us to bucket the categories more effectively rather than make provisions on the entire portfolio based on one set of indicators. I think that is the opportunity for this bank during the next six months or the one year, to further improve the classification by category buckets. Also in terms of the LGD itself, what we believe is that the indications of recoverability would be high, so what we provide today is fine. But as far as we are optimistic that these figures at some stage come back into the P&L, to me it is a conservative strategy. Even though it might hurt today, in terms of P&L, it will come back to us.

***Q*: *Further clarification sought on the question* - I was not clear on that impairment, so you say there is no change in the PD and the LGDs are getting updated with historical data.**

Rajendra Theagarajah

It is happening slowly and it needs far more updating.

***Q*: So then the only explanatory variable is that your floor rates are deteriorating, that means the one month - two month - three month overdue bucket, because if those two other assumptions are not majorly changing, that means that there has been a deterioration in the floor rates.**

Ms. Suvendrini Muthukumarana

What happens is we work out the LGDs quarterly. It is a loss indication where each of the portfolio sector wise, where you will identify to see what are the expected losses. So even if a specific provision is made on a specific loan, we will consider that also to identify the LGDs for the collective portfolio. So if there is some form of loss indication, we are being conservative and we adjust the LGD. So what has happened is we have made a relatively higher LGD to some sectors, but with the improvements in the asset quality and the recovery process, these can reverse in the future.

***Q*: So then are you categorically saying that there has not been any deterioration in the floor rates.**

Ms. Suvendrini Muthukumarana - Yes, because we are doing a fair value for the current portfolio which may be based on our recovery pattern and the asset quality, it will change in the future.

Q12. Your net interest margin is something like 2.7%, one of the lowest in the industry. I also notice that on your liability side 76% in fixed deposits. So I suspect that the reason for that very low NIM is because of your liability structure. You have also been ramping up your branch expansion. So can you give us some clarity of what is happening on that side? What are the strategies you are following in growing your CASA base and what is going on with your branch expansion. How many of them are profitable, and how many of them are dragging. What is your branch strategy, where are you putting these branches, what are you hoping to do, what is the real value proposition that you are bringing in to a fairly crowded market.

Rajendra Theagarajah

See, as a mid-sized bank, playing in a very aggressive high street, we believe that having 80 or 90 branches 3 years ago was not going to get us anywhere, when you are playing with people who have 200+ branches. But I don't think the strategy for this bank was to go up to 200 - 250, but we felt that we need to have an optimum level of maybe 100 -110 branches over a period to *a)* improve its SME penetration in outside the Western province. Secondly to give a good attempt to mobilize more granular deposits from the network, as a bank which is constant and consistently reducing its dependency as a wholesale and corporate bank.

So that was the strategy to you, over the last three years we have progressively increased our branch network, and where ever possible, it has been outside the Western province, focusing on emerging landscapes. This year we saw I think up to June we opened 9 branches. Of those 9 branches, about 4 or

5 were approved last year, but which could not be opened because of various premises challenges. So it was actually from last year. This year of the original plan I think we opened about four of the new ones. As at today we have opened nine new branches. Of the nine I think only one is in what we call the Western province or Greater Colombo. Others are all in spread-out of the country.

The strategy would be to look at perhaps another may be 5 branches or 6 branches during the remainder of this year, even though the plan was for a greater amount. But I think we will moderate that here. Those would entirely be in locations where we see a good opportunity for value chain financing, engaging the SME community and where ever possible opportunities for more granular deposits. I think I did make this call during the first quarter as well. The newer branches which we have been opening have shown pretty good contribution towards CASA. I think, Chandana is prompting me, for this year, the newer branches we have opened on average have shown around 40-45% of CASA in the few months they have opened. That is because unlike some of the more mature branches, from day 01 the mindset of the branch manager and staff have been drilled on the importance and the role of low cost deposits. So it has certainly worked, but of course the challenge has been in an environment with high volatility and less liquidity.

As a strategy, again, if we look at our 102 branches I think in terms of profitability or branches which have been making losses, if we look at the branches, if we look at typically a two year period for break-even, and if we look at the branches which are over two years, if I look at the more mature branches which have been there for more than ten years, of the 102 roughly around 70 - 75 branches fall in to that category. Of that we only have around 10 branches which need churning around. Some of those are not because of break-even mainly the turnaround has come because of two issues. In the early 2011 - 2012 time, when the Bank was embarking on a limited pawning strategy, even though it was not as big as some of the bigger banks this bank also selectively in a few branches got burnt in some of the pawning issues in a few of the branches in the North and East. So couples of those ten branches are still coming out of that lag effect. Along with that we have few other branches which have some impact as a result of a product which was launched about 5 years ago on receivable financing. There some of the SMEs got in to a bit of a challenge.

So those we are now re-working, restructuring and pulling them out. That figure of 10-11 branches was around 18 branches as at the end of last year. So month on month the number of those branches needing turnaround reduce it. So overall I think the newer branches are certainly showing a much healthier break-even within that two year horizon. The strategy for the network would be to intelligently grow it, not to do a burst. That's important. Because, also mind you, that the mobile strategy of the Bank is also slowly taking on.

We launched the newer version of NDB's mobile banking in early February. I think we started on-boarding around 2,000 customers a month. I think now we are today we are as at the end of June we have around 11,000 new customers on-boarded and that is now month on month increasing in numbers. At some stages we will see the on-boarding getting to a different level which will them make the cost structure more meaningful.

Along with that also another initiative worthy of note is our e-statement strategy. I think we were on-boarding again at the rate of about 300-400 customers every month towards the end of last year. Now in the last 10-15 days alone we have about another 2,000 new on-boarding. Every new e-statement customer on-boarded, the monthly saving is around 170 rupees in terms of printing, stationery, mailing cost, etc. Today, the aggregate on-boarding, the last 1- 1.5 years, the saving is between 1.5 - 2 million a month, from nothing.

So these are some of the initiatives which we feel will take us in good stead in the years to come.

Q13. I noted from the Stock Exchange website that there is a notice of an EGM to change Articles of the Bank and then subsequently you all had revoked the EGM. Can you please give a sense of what was the thinking behind, as to why the change was necessary?

The internal rationale was, the basis of the current governance structure which applies to the banking market, there is a Central Bank driven mandatory Code as well as a CSE Code and we are governed by the Central Bank Code, and the Code currently provides for the board to have, where it is a fit and proper member from within the Board, who may not necessarily be independent to be a Chairman, like what we have currently in what I believe at least five local commercial banks. Where we have that, we have a strong independent director designated as the Senior Director to provide the balance. In NDB today, if we look at the composition of the 10 directors, which includes myself and if we take the other nine, six of them are independent. So that the balance has been fairly strong. The Board - and it was an internal unanimous Board decision that it felt that in the interest of driving the succession with the incumbent Chairman intending to step down in the near future on reaching 70 years, that there would be an opportunity for somebody to drive the Board and the strategy from a best point of view, who may not have been independent. Saying that what was restricting that was unfortunately, the internal DNA of the Bank which was its own Articles and not any regulatory framework. So we had to go to the shareholders to get that approval.

At that stage, out of protocol we contacted the regulator as we have done in the past to get the approvals. They came back to us and said, it's good for you to get the shareholder engagement before you come back to us. That is exactly what we did. We called for an EGM as is required under regulation to explain and get the shareholders' approval. But at that stage, before the due date, the indications from some of the larger shareholders was that they were not in favour of this change, because they felt that this standard which they had today, even though it was over and above what was required from the industry, could prevail. So even though it was an internal decision within the Board and the Bank to go in this direction, as a Bank which respects the views of the shareholders, we saw it fit not to proceed with the EGM, because it was meaningless. So that is what we exactly did.

But the rationale behind that was to do something which the Bank felt was in the best interest to drive the Bank forward.

Q14. We are seeing two things going on in the real economy. One is that on the financial system we are seeing a high loan growth. We are also seeing a massive increase in real estate prices. We are seeing a record amount of real estate happening. Large number of new players are entering the market and land prices are going to record levels in a very rapid pace. Do you suspect that a lot of this lending is finding its way perhaps not directly may be not getting caught up in the statistics in terms of mortgages, but through indirect routes like entrepreneurs borrowing for their businesses and speculating in the real estate market, do you think some of this significant part of this credit growth is finding itself in the real estate market?

Ok, for NDB per se as a strategy, no. Because we know while there have been some demands from some of the sectors, our internal credit guys have been vehemently challenging and actually pushing back on that. So I think from NDB's point of view, I think no. Our exposure to real estates has two fronts. One is commercial real estate and the other one is residential. On the residential the strategy is to very much moderate the exposure to the very high end. It is very very moderated and it is more very little in terms of buy to let as opposed to buy to own.

Q: What about business people borrowing in their businesses, because you can't see that right. If you say that you are a rubber company and you borrow on the business, you do not know what the entrepreneur is doing with the money. He is not necessarily using it in this business.

Rajendra Theagarajah - One good thing - well all I can say is one good thing NDB certainly tends to do is, and I think there are one or two other banks who also do that, is wherever possible the overdrafts are used as a minimum tool and it is very much the short term loan and - it is a match funded lending which takes place. Even the apparel sector, I know we were one of the very few banks, we deter people coming and saying give us a packing credit without orders. We used to actually suffer from the fact that these guys would go away and saying that somebody else will give it without order matching.

But I know this Bank and at least one or two other banks which used to very steadfastly say no. Order matching or nothing. So make sure that the intended purpose is as much as possible monitored. But saying that, I'm not sure whether that stands for the industry as a whole. Secondly you are also right, I mean when you go driving past Colombo you see the amount of real estate which is ballooning and some of the prices which we are hearing. To me it appears horrendous and unsustainable. It is a concern as to how much you can get, I mean when you see properties in some roads of Colombo 07, going at 15-18 million a perch, which was may be half that a year ago, it is a concern. But I would not say that we are seeing that included in our balance sheet. But from an industry point of view I think there is lot of relevance.

Q15. And the next question is from your own question, would that have some co-relation to a bubble?

That yes, I think that is something to be mindful of.

Q16. What is the market response to the newly introduced NDB One Account with NDB Wealth Management? How well has that been accepted by the customers?

I think the initial euphoria was very welcoming and I think the people saw the convenience. The on-boarding process has naturally seen a slow start. But I think we are seeing a steady increase. It has still been three months. You need to give it about a year to see how the real impact is. But I think given the simplicity of on-boarding and managing a dashboard of a whole portfolio of products under one account, it is a very compelling proposition.

Q17. The project financing has shown an impressive growth during the first half. How would you explain the sectors?

Yes, a 44% growth. The sectors have been fairly broad based. Energy has been important, not just in Sri Lanka, but also in Bangladesh and some parts in emerging Africa with tried and tested Sri Lankan entrepreneurs who have replicated the model outside. Some agri value addition related capacity building outside the Western province has shown good opportunities for us, which also having a direct impact on value chain is financing on projects. Real estate, yes, we have but we have been very modest and we are cautious. One thing, our credit guys are completely pushing that is to keep on funding people to buy land and fund land as equity. I know that challenge keeps on coming to us, but when we identify the debt to equity contribution as an internal challenge we insist that there is no rolling of the portfolio of development assets by a developer, we try to match fund project by project. So that has been a push back on our side. The other sector in term of - manufacturing selectively has shown good growth. But really I think energy - renewables has been the main champion for us in the last six months. It has a deep pipeline coming in that sector.

Q18. What is the overall private sector credit growth expectation?

All I can say is what was mentioned by the Governor in the recent conversation we had with the Bank CEOs, as a policy expectation they were expecting it to be around 20% from the current 28%. That I guess is public knowledge.

Q19. Please clarify on the AFS marked-to-market gains in this quarter.

Chandana Guniyangoda

Total AFS loss reported is 471 million mainly because of the Treasury Bond portfolio, with the rate movement in the industry, as well as the investment what we have made in 2015; it is in the portfolio of AFS. Marked-to-market loss of around 260-300 million. Altogether the total effect of AFS is 471 million.

Rajendra Theagarajah - Chandana, how would this 471 compare "give or take", with the industry in general. I think it is a good idea to have when we look at our balance sheet, our exposure Vis a Vis the market without commenting on individual banks. With the market, are we comparable, are we below, are we average?

Chandana Guniyangoda - When it comes to Treasury Bonds portfolio, AFS loss of NDB is very much below the industry average. You will see that it is reflected in the net asset value of each share. The net asset value of NDB has not deteriorated over the period of last six months. But when we compare it with some of the peer banks, the net asset value has come down mainly because of the AFS losses.

Q20. What is the outlook for credit lines for NDB?

As at the moment the real hot one there is the ADB credit line, which came in a very unique manner where the ADB appointed one of the top tier accounting firms as an independent arbitrator and went on an auction system inviting all the participative banks to bid for it. I think we were pretty successful in literally mopping the entire pool of money during the first auction. That was around 2 billion. I think the guys have been doing a remarkable job in literally disbursing that entire lot during that last two months. So I think it is a tremendous effort by the guys and the nice thing about that is that it is entirely SME. So it is a very good, positive sign which we are very happy about.

End of Questions and Answers.

Closing Remarks

I guess we have had very interesting and engaging questions following the presentation. Folks thank you very much for being interactive and being with us and I hope will continue this story and the dialog and your understanding and your support is what makes us want to do this in a meaningful manner. A transcript of this will be - on Monday (15 August) it will be posted on our site.

Thank you very much and have a great day.

End of transcript.