

## **NSB Fund Management Company Limited 2016**

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The audit of the financial statements of the NSB Fund Management Company Limited (“the Company”) for the year ended 31 December 2016, comprising the statement of financial position as at 31 December 2016 and the statement of comprehensive income, statement of changes in equity and statement of cash flows for the year then ended and a summary of significant accounting policies and other explanatory information, was carried out under my direction in pursuance of provisions in Article 154(1) of the Constitution of the Democratic Socialist Republic of Sri Lanka.

This report is issued in terms of provisions in Article 154 (6) of the Constitution of the Democratic Socialist Republic of Sri Lanka.

### **1.2 Board’s Responsibility for the Financial Statements**

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Board of Directors (“Board”) is responsible for the preparation and fair presentation of these financial statements in accordance with Sri Lanka Accounting Standards and for such internal controls as the management determine is necessary to enable the preparation of financial statements that are free from material misstatements, whether due to fraud or error.

### **1.3 Auditor’s Responsibility**

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My responsibility is to express an opinion on these financial statements based on my audit. I conducted my audit in accordance with Sri Lanka Auditing Standards. Those Standards require that I comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatements.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor’s judgment, including the assessment of the risk of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the Company’s preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company’s internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my audit opinion.

## **2. Financial Statements**

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### **2.1 Opinion**

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In my opinion, the financial statements give a true and fair view of the financial position of the Company as at 31 December 2016, and of its financial performance and cash flows for the year then ended in accordance with Sri Lanka Accounting Standards.

### **2.2 Report on Other Legal and Regulatory Requirements**

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As required by Section 163(2) of the Companies Act No.7 of 2007, I state the following:

- a) The basis of opinion and scope and limitations of the audit are as stated above.
  
- b) In my opinion:
  - I have obtained all the information and explanations that were required for the audit and, as far as appears from my examinations, proper accounting records have been kept by the Company,
  
  - The financial statements of the Company comply with the requirements of Section 151 of the Companies Act, No. 7 of 2007.

## **3. Financial Review**

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### **3.1 Financial Results**

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According to the financial statements presented, the operations of the Company for the year ended 31 December 2016, had resulted in a pre-tax net profit of Rs.109,141,803 as compared with the corresponding pre-tax net profit of Rs.252,762,389 for the preceding year, thus indicating a decline of Rs.143,620,586 or 57 per cent in the financial results for the year under review.

Increase of interest expenses on repurchase agreement and loss arising on valuation of financial instruments at fair value by Rs. 183,390,059 and Rs. 101,195,961 respectively as compared with the preceding year were the main reasons attributed for this decline in the financial results.

### **3.2 Value Addition**

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Although the profit for the year under review was Rs.79,417,377 the value addition of the Company had decreased from Rs.309,886,722 in the year 2015 to Rs.158,390,087 in the year 2016 after taking into account the personal emoluments, depreciation and tax expenditure aggregating Rs.78,972,710 for the year under review.

### **3.3 Analytical Financial Review**

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#### **3.3.1 Significant Accounting Ratios**

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According to the information made available, some important observations after analyzing the accounting ratios of the Company for the year under review as compared with the preceding year and sector ratios are given below.

- (a) Even though Risk weighted Capital Adequacy Ratio of the Company was higher than sector ratio of 22 per cent, it had decreased by 7 per cent with compared to the year 2015.
- (b) Return on Average Assets and Return on Average Equity of the Company had decreased to 1 per cent and 6 per cent respectively in the year 2016 from 2 per cent and 14 per cent in the year 2015. Further, those ratios are below to the Sector Ratios for the year under review.
- (c) The core capital of the Company had decreased by 2 per cent from Rs. 1,731 million in the year 2015 to Rs.1,691 million in the year 2016. However, core capital was above the minimum requirement of Rs.1,000 million.

### **4. Operating Review**

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#### **4.1 Performance of the Company**

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According to the information made available, the primary objectives of the Company are to:

- (a) Carry on business as a Primary Dealer.
- (b) Engage in secondary market transactions in treasury bills, treasury bonds, and other Government and Central Bank's Securities.
- (c) Promote and develop a secondary market in Treasury Bills, Treasury Bonds, and other Government and Central Bank's Securities.

In order to perform the above objectives, the total investments made in the Primary and Secondary markets as at 31 December 2016 and 2015 as compared with sector information are given below.

Nature of Investments	Sector	The Company	
	2016 Rs. Mn.	2016 Rs. Mn.	2015 Rs. Mn.
Trading Securities	98,100	7,013	4,262
Held to Maturity	106,800	1,801	2,211
Available for Sale	<u>19,300</u>	<u>1,894</u>	<u>2,020</u>
<b>Total Investments</b>	<b><u>224,200</u></b>	<b><u>10,708</u></b>	<b><u>8,493</u></b>

According to the above information, the Company had maintained 65 per cent of its investment portfolio as trading securities to earn higher interest income from Government Securities. However, maintaining such a higher portfolio may create high market risk to the Company.

## 5. **Accountability and Good Governance**

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### 5.1 **Corporate Plan and Action Plan**

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The Company had not prepared a Corporate Plan and an Action Plan for the year 2016 as per Chapter 5 of the Public Enterprises Circular No. PED/12 of 02 June 2003.

## 6. **System and Control**

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Deficiencies observed in systems and controls during the course of audit were brought to the notice of the Chairman of the Company from time to time. Special attention is needed in respect of the following areas of control.

<b>Control Areas</b>	<b>Observations</b>
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(a) Financial Management	The attention should be paid to maintain a healthy return on average assets and average equity in par with industry norms.
(b) Planning	The Company should be prepared a Corporate Plan and an Action Plan in order to achieve its main objectives within the target period.