

Chief Executive's Message

D FCC Bank has a history that spans over half a century of service in the field of development banking in Sri Lanka. The Bank has been the financier of trail blazing Lankan entrepreneurs but more importantly played a pioneering role in supporting small and medium-sized entrepreneurs gain access to funds, fueling innovative investment ideas and growing new economic sectors: the benefits of which have reached thousands of people across the nation, providing sustainable livelihoods and enhancing the quality of life.

Today, not only the local businessman but also a farmer or a teacher in a remote village in Sri Lanka can enjoy our comprehensive package of financial products and services. Our products, be it long term loans or a simple savings account is designed to give people the best a bank can offer in terms of service and returns.

DFCC Bank's social responsibilities are correspondingly various. The Bank's rich history ensures that CSR is in its genes: an integral part of its value delivery process. DFCC's very mission - of nurturing enterprises and creating value for all stakeholders - implies the discharge of a social responsibility; the organisation is committed to being a prime mover of national economic and social development.

This is our maiden report on sustainability. It maps our commitment in the areas

of product innovation, environment responsibility, educational advancement, investment in the community and employee empowerment. In 2008 we made headway in two key areas of sustainability. After many months of collaborating with educators and the Ministry of Education officials, we were able to achieve new milestones in child education with the launch of a new nation wide programme for schools. The programme, which is being implemented through 2009, is designed to prepare young children cope with the challenges of the future. It encompasses teacher training and parent guidance as well.

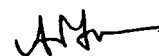
The focus on responsible and clean energy has never been more important. Helping meet Sri Lanka's growing energy needs in economically, environmentally and socially responsible ways has been a priority for DFCC Bank during the last decade. Our commitment to develop sustainable energy began with the support for the country's first grid connected mini hydropower project in Sri Lanka. Since then we have made steady progress resulting in being recognised as the proactive resource center for the country's Renewable Energy sector. In 2008 we assisted the commissioning of another 11.5 Mega Watts of Grid connected power and during 2007 and 2008 carried out overseas consultancy assignments in renewable energy development projects in the Philippines and Uganda.

The concept of sustainable development is gaining in global importance and significance. Whilst increasing shareholder value, the need to do so in a manner that is environmentally, socially and

economically acceptable, will help 'to meet the needs of the present generation without compromising the ability of future generations to meet their own needs.' A culture of doing the right thing in the right way has been critical to our success in the past and we will continue to be committed to doing so in the future whether it is setting high ethical expectations for our employees, providing a progressive and inclusive workplace or delivering products and services that can change lives.

In terms of our own housekeeping we have been focusing on reducing our emissions, recycling waste, conserving water and rising to green challenges. In this report we have strived to offer a balanced view of our organisation's economic, environmental and social performance in 2008 with an outline of our sustainability priorities for the future.

DFCC Bank has been a pioneer in many respects and has been at the core of the country's development for decades. It is a position that demands responsibility and commitment. In the years ahead we will continue our quest to be one of Sri Lanka's leading corporate citizens serving our nation with responsibility.



Nihal Fonseka
Chief Executive
27 May 2009



**WITH LEADERSHIP COMES
RESPONSIBILITY...
ENTERPRISES HAVE THUS
THE RESPONSIBILITY OF BUILDING
A STRONG FRAMEWORK OF GOVERNANCE...
HIGH ETHICS... AND SUSTAINABLE LIVING FOR ALL...**

ENVIRONMENT

■ Rising to Green Challenges

The Bank defines 'environment' in a broader sense to encompass not only ecological criteria but also social aspects. There are four aspects to DFCC Bank's environmental responsibility.

First the Bank pays special attention to the environmental aspects of the projects it finances, focusing on applying the Environmental and Social Impact Assessment policy and practice of the Bank, assessing the potential impact, adequacy of mitigating measures, resource utilisation, and energy efficiency of proposed technologies or processes. As a minimum, the Bank ensures that the projects it finances are compliant with the laws and regulations of the Central Environmental Authority of Sri Lanka.

Second, the Bank identifies and develops sectors and businesses that are specifically targeted at protecting and improving the environment with special focus on climate change, the sustainable use of natural resources and the management of waste. Going beyond, the Bank also identifies and provides funds to existing high risk projects which require the installation of pollution mitigating measure.

The third dimension is for the Bank to assume responsibility for its corporate environmental footprint. Even though DFCC own footprint is not of the same magnitude as the footprint from the projects it finances, the Bank works continuously to improve the environmental performance of the buildings and its offices.

The fourth aspect is the Bank's commitment to create awareness, educate and urge the public on matters relating to environment protection/conservation and appreciation.

■ Responsible Lending

All projects above a threshold value or in defined sector which DFCC considers for financing undergo an environmental and social impact analysis. Amongst other criteria, generally this would mean an assessment of whether the project has been designed to prevent or minimise pollution, waste recycling, water & energy conservation, climate protection and product stewardship. It also encompasses projects focused on the development and implementation of environment-friendly technology. The social aspects being, whether the project is in line with the labour laws of the country and good international practices which include the provision of

worker health and safety, prevention of child labour, non-discrimination at work place, checks on sexual harassment and minimising impact on local communities.

The Bank is working on an environmental classification for its new projects depending on the level of potential environmental impact. Currently all loans, whatever the risk level, are provided on market terms. However, for projects that need to put in place further mitigating measures, the Bank offers concessionary loans under 'e-Friends'.

During the year, loans amounting to Rs140 million were approved under 'e-friends' for 15 environmentally friendly projects.

The environmental management system is integrated into the Bank's project management system. A dedicated cell headed by a full-time environmental engineer works on assessing large projects whilst all loan officers are engaged in the environmental appraisals as well as management of the loans with input from the cell. Loan officers at the main office and at all branches are being provided with periodic training on the subject locally and overseas. The cell is also

tasked with integrating the Bank's strategy on environment sustainability with the business strategy.

DFCC Bank's Environmental and Social Impact Assessment Policy and Practice, which specifies the internal processes and practices of the Bank in relation to environmental aspects of project appraisal, was revised, during the year, to better reflect the Bank's standing in relation to its business strategy, as well as to harmonise the policy with the principles of bilateral and multilateral funding agencies. A draft of the revised policy will be posted for two months running on the Bank's website, for public comment, before being adopted by the Board of Directors in December 2009.

Nurturing Environmentally Sustainable Business Sectors

The increased focus on the challenges of climate change has moved energy to the top of the agenda of Development Financing Institutions around the world. In response, DFCC Bank established a special lending window for renewable energy related projects more than a decade ago, the first bank in the country to do so. Further DFCC fully supported the country's first Grid-Connected mini hydro power project in Dickoya. However, real growth of the sector

was mostly realised during the last seven years with the Government policy framework being made operational to buy energy to the National Grid at competitive rates.

DFCC Bank's pioneering work in renewable energy takes a three dimensional approach to developing the sector. Firstly, the Bank functions as the Administrative Unit for several credit lines extended to the Government of Sri Lanka by the World Bank amounting to US\$134.7 million and two grants amounting to US\$11.8 million from the Global Environment Facility and US\$108.9 million from other funding sources. The credit lines aim to improve the quality of rural life by promoting access to electricity through off-grid renewable energy technologies and to add capacity to the national grid through private sector participation in power generation using renewable sources. As at end 2008, completed grid-connected projects include 61 mini hydro projects having 136.2 MW of aggregate capacity. Off-grid projects include the electrification of 6460 rural homes through village hydro schemes and 125,985 homes using solar home systems.

Secondly, the Bank acts as a participating credit institution to identify and approve

funds from the above credit lines for renewable energy projects. DFCC has disbursed funds amounting to Rs2,769 million to 39 grid-connected mini hydro projects through the credit lines. As a result of the Bank's pioneering work in this sector, DFCC is recognised as the resource centre for renewable energy in the country.

The third dimension is for the Bank to utilise its sector expertise to undertake consulting assignments on renewable energy development through its subsidiary DFCC Consulting (Pvt) Limited. The Company has completed several assignments for overseas markets such as Nepal, Philippines and Uganda. The Bank also identifies, guides and promotes potential local entrepreneurs to take on renewable energy projects in overseas markets.

Good Housekeeping

Increasing awareness that the world is warming, due largely to the emissions of carbon dioxide and other greenhouse gasses from human activity, has drawn the Bank's attention to 'good housekeeping' through the practice of an internal environment management system which is being improved year on year.

Consumption	2008/09 Units	2007/08 Units	Increase/ Decrease %
Electricity (Kwh)/Avg.per branch	134,932	118,071	14
Water (m3)/Avg.per branch	1,032	986	5
Fuel (liters)/(Head Office)	44,803	39,351	14
No. of Km/(Head Office)	330,851	284,798	16
Hired Vehicles - No. of Km	5,603	9,598	(42)
White Paper (pkts)	2,470	2,450	1
Newspapers/(Head Office)	675	700	(4)
Average No. of Km per Executive	3,823	3,271	
Average No. of Km per Liter	7.38	7.24	

The Bank has been adopting various measures to reduce the consumption of electricity, water, paper and fuel. The data set out in the above table indicate increases in electricity (14%), fuel (14%) and travel (16%) whilst white paper and Newspaper consumption has been maintained/ decreased.

As a result of keeping the pool vehicles in peak condition, average number of kilo meters per liter has increased only marginally. Whilst there are no unusual increases in the consumption levels, measures would be adopted to maintain consumption at this year's levels.

DFCC has not been fined or been non-compliant with environmental laws and regulations of the country. The Bank

is working towards formalising its internal environmental guidelines for office practices, facilities management and procurement and setting performance goals for 2009/10.

■ Educating the Public

The scientific community has been warning the world for some time that the climate change problem requires all segments of society - businesses, consumers and governments to take meaningful action urgently. There is strong consensus that temperature increases of this magnitude will bring changes in rainfall patterns, rise in sea levels, risk of droughts and floods, threats to biodiversity and a range of public health challenges. It is crucial that the

corporate community do all they can to 'heal the earth'. However small the action may be, every little helps!

During the year, DFCC commenced a programme to educate young children in primary schools across the county on environment stewardship covering the '3R' principles of reduce, reuse & recycle and waste management. Specific projects are being organised periodically to put into practice what they learn in the classroom. During Vesak, focus was drawn to a competition in schools to build Lanterns using eco-friendly material. Several such projects and environmental awareness programmes for schools are in the pipeline for 2009/2010.



The winning team of the environment-friendly Vesak Lanterns competition of Godagama Subharathi Junior School, Homagama. Similar competitions were held in other schools where the 'Six-S' programme is being implemented.

An amateur photography competition and exhibition was held in October 2008 titled 'Sobha' based on the theme of flora, fauna and sights of Sri Lanka. It was an effort at cultivating an appreciation for nature amongst the public and a reminder that conservation of its habitat will help preserve this beauty for other generations to enjoy.



A section of nearly 2000 photographs exhibited at 'Sobha' 2008, nature photography exhibition and competition held at the Lionel Wendt, Colombo 07.

raising the awareness levels of the Bank's clientele on matters relating to the environment and how they can reduce the carbon foot print and contribute to 'heal the earth'. DFCC will also focus on developing other renewable energy options such as wind and biomass.

■ **Going Forward**

In 2009, DFCC will focus on implementing its revised environmental policy, integrating environmental considerations into the Bank's business planning process. Further sharpening this focus, the Bank will put at the disposal of project owners the expertise and experience, that DFCC has gained over five decades of development banking, to integrate environmental sustainability in to their businesses. This will include

NURTURING SMALL AND MEDIUM ENTERPRISES

Small and Medium-sized Enterprises (SMEs) are a major source of employment, entrepreneurial skills and innovation. They are the backbone of developing economies. SMEs also support economic and social cohesion. In Sri Lanka, quite early in the evolution of the country's economy, the SME sector was identified as an important strategic sector with potential to create employment at a lower investment cost, reduce inequality in income distribution, assist in diversifying the production base, alleviate poverty and develop the regions.

The SME sector in Sri Lanka has its own set of problems. Systemic constraints such as lack of eligibility to gain access to finance and modern technology, lack of managerial and marketing skills, obsolete machinery and equipment, weaknesses in support programmes to compensate for these bottlenecks are some key problems that affect the development of sustainable SMEs.

Taking the Risky Route

Given these circumstances, supporting SMEs is seen as taking a risky path. However a development bank should really

be doing what an ordinary bank would be willing to do only at outrageous rates and conditions. Therefore, support for SMEs has been a key priority for DFCC Bank since its inception and later in 1978, when it set up a separate business unit with special focus on developing the sector. As risky as it may be, it has been DFCC's policy to promote successful entrepreneurship and improve the business environment for SMEs in order to help them to meet the challenges faced in today's global, knowledge based economy and realise their full potential. Many trail blazing Lankan entrepreneurs who have built their enterprises to what they are today began the journey as SMEs and was supported by DFCC during their risky early stages.

The Bank's SME activity has provided support for an estimated 23,000 businesses mostly in the regions. During the year, triggered by the global economic slow down, the demand for credit for SMEs was low. However, nearly half of credit facilities approved were for 600 small and medium enterprises in the provinces, generating approximately 3000 direct jobs. The Bank increased its penetration in

sectors such as health care, construction, education, agriculture based industries and commercial transport which are economically and socially important to the country.

Support Where it is Needed Most

DFCC's strategy for SMEs is three fold. First, the Bank strives to develop internal capabilities of SMEs, improving their eligibility and ability to gain access to finance. DFCC targets sectors that have the potential to impact favourably on regional economies and builds internal managerial capabilities of SMEs through conducting workshops and seminars on management practices, accounting, improving service quality, marketing etc.

Second, DFCC provides SMEs with accessibility to concessionary credit giving them a competitive advantage. Since its early days DFCC has been actively supporting the SME sector by channelling concessionary credit from bilateral and multilateral organisations, especially to small businesses located in rural areas of the country. The Bank has taken the lead in utilising credit made available through these organisations,

becoming the highest lender for most credit lines available for the sector.

Third, the Bank guides small businesses in the effective use of credit to build sustainable businesses that can withstand economic setbacks. Credit alone does not ensure the survival of small enterprises. Close monitoring and guidance is a key aspect of managing the SME portfolio. The Bank has over 65% of its project officers operating in 14 branches located close to the projects and the officers spend a significant amount of their time advising and visiting businesses. Workshops and seminars are conducted to improve managerial and technical skills of clients and the Bank's multi disciplinary staff guides businesses in boost productivity, competitiveness and innovation.

Now more than ever, SMEs need DFCC's expertise and guidance on weathering the effects of the economic crisis. The Bank will focus on a plan of action to guide its current SME customer base through troubled waters. The Bank proactively supports disruptions to cash flows of the SME sector.



A group of clients of DFCC at a regional workshop on soft skills development in SMEs.

TRANSFORMING EDUCATION

■ Beyond Basic Education

DFCC Bank in association with Sri Lanka's Ministry of Education commenced implementation of a new programme in January 2009 to introduce the Japanese management discipline 'Five-S' to Schools Island wide. This discipline aims to improve attitudes and behaviour of children in order to increase their efficiency and productivity levels through keeping the working environment clean and organised. DFCC bank has augmented this concept with a sixth 'S', for 'safety' - the necessity for integrating this added dimension has been widely recognised and is specially relevant in the case of children.

Education is a top priority worldwide. In Sri Lanka, even if we do simple things like give computers to schools, equip a laboratory or library, supplement the curriculum with field trips, seminars and workshops for children or merely provide water, sanitation and other basic infrastructure where needed, we recognise that helping to educate a child has lasting effects on the nation.

DFCC Bank believes that students, especially in rural underprivileged schools, deserve to have the skills they need to be part of the knowledge-based economy. When a country takes care of its children, and for the whole of its children - not just the physical feeding- but the health of its children as a whole, mentally strong, emotionally robust and physically fit, we will see choices being made that bring about change for the common good.

Investment in children is never wasted. With that in view DFCC Bank and its subsidiary Vardhana Bank will place top priority on working with educators and the government on programmes to empower children through a holistic approach to education.



Enterprising students of Maliththa Maha Vidyalyaya, Bandarawela selling the Vesak Lanterns made by them to raise funds. The Lanterns were sold in front of the DFCC Branch premises to clients as well as pedestrians.

The programme focuses on educating and training teachers and primary school pupils from selected public schools on the theoretical and practical application of the 'Six-S' concept and the '3R' (reduce, reuse, recycle) principles on environment stewardship. It's a year long programme whereby each step will be introduced and put into practice every two months. The bank has engaged an expert who has extensive experience working with children to train and guide schools in the implementation. Four months into the programme, we have seen considerable improvements in the school environment, classrooms as well as the behaviour and attitudes of students.

The parent's of children constitute a secondary group, based on the insight that the values of 'Six-S' should not be restricted in their application but should be followed at home and elsewhere as well as at school. Parents are invited for the training sessions in schools and also to assist in the activities related to the implementation of the five steps.

At the end of one year a panel of judges will select the best schools. The schools will be recognised and rewarded handsomely at a gala ceremony.



Students of the Daluwakotuwa St. Annes Primary School, Negombo anxiously getting ready to start their day in a clean and organized classroom arranged in accordance with 'Six-S' guidelines.

■ Employee Volunteerism

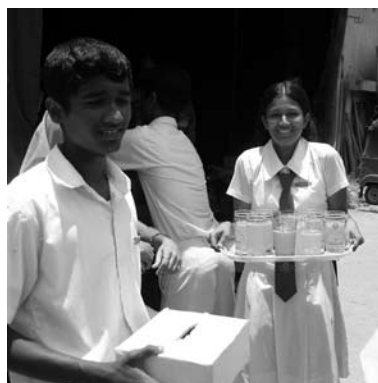
Generally most community projects initiated by Corporates do not go beyond the funding aspect. That's what differentiates this project from most others. Funding is only one part of the programme. What is more important is the involvement of our staff, with the teachers and children in schools, which contributes to building a culture of volunteerism. Even though the Bank has hired a consultant to guide the school staff, it is the 240 volunteers from the DFCC Group who are working with schools to creatively implement the programme that's making the difference.

Most schools are located within a 20-kilometer radius from DFCC and DFCC Vardhana Bank's branch offices, which makes it easier for volunteers to work with the respective schools. Each school has a dedicated team of DFCC volunteers who are competing to upgrade their school to

be the best in the programme. We also see this involvement as being beneficial to our staff in terms of practical training in team building and professional development. During the year, on average an active volunteer put in approximately four hours of work for a month, which we hope to increase as the project rolls out to a mature stage.

■ Entrepreneurship for Children

Lack of funding for the day-to-day management of premises and classrooms is a problem faced by most rural schools resulting in the resistance of school staff to new programmes. As a measure of helping schools overcome the issue, the Bank



The students of the Kaduruwela Nagara Vidyalaya expressing their entrepreneurial skills by organising a mobile 'Saruwath Kade' within the city limits of Polonnaruwa.

has begun a 'Matching Grant' programme tied with the 'Six-S' implementation. The project revolves around cultivating an entrepreneurial spirit among children from a young age. The Bank advises and guides the schools on launching enterprising projects to raise funds, the proceeds of which will be matched by DFCC up to a maximum ceiling. During April and May 2009 five schools carried out projects and most were based on the Vesak theme. A school in Polnnaruwa conducted a 'Saruwath Kade' during the very warm month of April. Badulla, Naulla Madya Maha Vidyalaya is making preparations to stage their own drama. Several others held 'Pola's. On average each school has raised around Rs60,000/- from such activities.

■ Moving Forward

Working with and for children on various projects over a period of time has given DFCC Bank a chance to make a difference in an important area of our community. The 'Six-S' project with its many facets is not only a sustainable programme but also one with potential to touch the lives of a vast number of children by laying positive foundations, which will benefit them as adults. An estimated 25,000 children between the ages of 5-13 years will benefit from the first programme. Its success, measured by a set of predetermined criteria at the end of the programme, will be a deciding factor for the expansion of the programme to other schools.

EMPLOYEE EMPOWERMENT

■ Engaging Talent

DFCC Bank has always regarded its valuable pool of well qualified and trained human resources as a key competitive advantage in holding its place in an increasingly challenging financial landscape. A continuously refined recruitment process has been the first step in building up such a pool of talent that has contributed to placing the Bank consistently at the top end of league tables on the criterion of profit per employee.

For quite sometime now, sourcing staff with the required set of skills to fulfil immediate functional requirements but more importantly possessing inherent competencies to take on higher levels of responsibility and leadership roles in the medium term has been posing a challenge not only to DFCC Bank but to the entire banking industry. Especially in this context and also considering the downturn in the economy following the global financial crisis, incremental staff numbers have been kept at an essential minimum. Despite substantial expansion in the scale and diversity of operations during the past five decades, DFCC Bank has been successful in limiting its staff numbers to 415 as at FYE March 31, 2009. In an attempt to

build capacity in all aspects of commercial banking, DFCC Bank has seconded 21 of their staff to its commercial banking subsidiary, DFCC Vardhana Bank (DVB). Additionally DFCC Vardhana Bank has a head count of 389 to support its branch operations that have been built up over the last four years.

■ Fostering Individual Growth and Harnessing Potential

The Bank has set in place an environment that is conducive to the development and growth of its staff. Quite apart from extensive training, the Bank has initiated special programmes to nurture its professional staff by offering them access to a wide range of development opportunities.

Last year, all managers were encouraged to formulate individual development plans for their executive level direct reports by making it a measure of their own performance. This year, managers were required to critically assess these plans in discussion with their direct reports and 'build' on them with the twin objectives of developing the employees themselves and also aligning such plans with the Bank's goals and priorities. In

addition to identification of formal training requirements, these plans included project specific assignments, cross-functional stretch assignments, role expansion and job rotation. Through this process, managers devote more time to coaching and mentoring and staff are provided with regular feedback on their strengths and development needs. The initiatives formulated to address development gaps provide staff with opportunities to learn and expand their functional capabilities.

These plans together with feedback from departments/ branches are used as the basis for training needs analysis and formulation of the annual training plan of the Bank.

During the year under review, DFCC Bank invested approximately Rs15.4 million on staff training and provided 16,466 man-hours of training translating to about 40 hours of training per employee. The quantum of training opportunities provided to staff of DVB increased by almost 70% to 12,790 man-hours made available to 910 participants. The investment in training and development amounted to Rs27,600/- per group employee.

We continued to focus on developing job specific technical skills with emphasis on capacity building in integrated risk management and Basel II requirements with an intensive residential programme being conducted by two international experts for a selected staff representing a cross section of departments and branches. In addition, about 30 knowledge enhancement sessions on this topic were conducted throughout the year.

We remain committed to providing our staff with diverse exposures and opportunities for specialised training and in this context 65 executives participated in overseas programmes. Post-training evaluation mechanisms are used to assess the return on investment on training.

■ Retaining Talent

Retaining high performers can be as challenging as recruiting them though this is currently less of an issue given the slowdown in skilled migration and the freeze on employment by most businesses. Creating an excellent climate to nurture and develop talent and providing the best of working conditions would not be sufficient by themselves to retain especially

the better performers. The Bank is mindful of the need to align its remuneration levels with that of competition. From time to time, the Bank engages external consultants to carry out market surveys and make recommendations for improving on remuneration and benefits.

In 2008 we engaged internationally reputed HR consultants - Hewitt Associates to conduct a comprehensive benchmarking study of remuneration structures of DFCC and DVB *vis-à-vis* comparator institutions. Based on findings, adjustments were made to remuneration packages to ensure better alignment with the market. However, the Bank does not compete on the basis of being the highest payer.

The bank is committed to providing a healthy work-life balance enabling our staff to benefit in terms of both personal and professional development. Over the years, formal and informal opportunities have been made available for greater staff interaction. Today, we have in place a dynamic social environment driven primarily by the staff themselves and this in turn helps them integrate better with the Bank culture.

■ Perspectives on the Year Ahead

With the world still in recession and likely to be so well into the year ahead, bank staff will be challenged to deal with unusually difficult times and contend with a different set of issues and circumstances. This will require adjustments in staff deployments and re-training some of the staff to cater to the shift in emphasis. The year ahead will be dedicated to enhancing productivity of the Bank's lean staff team while pruning costs through a freeze on recruitment.

Despite challenging economic conditions, there will be no compromise on staff development with the Bank remaining committed to providing its employees with targeted and value adding training opportunities and avenues for growth. Our achievements in the past are primarily attributable to the quality and commitment of our staff and we firmly believe that continuing to invest in staff development today will help propel the Bank to scale even greater heights and profit from the economic crisis confronting all banks and commercial establishments.

Staff Productivity	Rs'000				
	2009	2008	2007	2006	2005
Income Per Employee	23,884	22,998	16,319	14,403	13,649
PBT per employee	4,845	4,733	4,420	4,418	5,934
Assets per employee	141,267	151,215	144,409	127,306	121,078