

CIRCULAR TO SHAREHOLDERS

IMPORTANT: THIS DOCUMENT IS OF VALUE

IF YOU ARE IN ANY DOUBT AS TO THE ACTION YOU SHOULD TAKE YOU SHOULD CONSULT YOUR STOCKBROKER OR OTHER PROFESSIONAL ADVISOR IMMEDIATELY

Dear Shareholder:

RIGHTS ISSUE OF 373,217,717 ORDINARY VOTING SHARES AT LKR 6.00 PER ORDINARY VOTING SHARE

The Board of Directors of Merchant Bank of Sri Lanka & Finance PLC (hereinafter sometimes referred to as "MBSL" or "the Company") resolved at the Board Meeting held on 09th June 2021 to recommend to the Shareholders to raise a sum up to **Rupees Two Billion Two Hundred and Thirty Nine Million Three Hundred and Six Thousand Three Hundred and Two (LKR 2,239,306,302)** through a Rights Issue of **Three Hundred and Seventy Three Million Two Hundred and Seventeen Thousand Seven Hundred and Seventeen (373,217,717)** Ordinary Voting Shares of the Company at a price of **Rupees Six (LKR 6/-) per share** and to list the said Shares on the Colombo Stock Exchange (CSE) subject to obtaining the necessary approvals relating thereto. These shares will be offered to the holders of the issued Ordinary Voting Shares of the Company as at end of trading on 18th August 2021 (the date of the Extraordinary General Meeting of the Company) in the proportion of **Nine (09) new Ordinary Voting Shares of the Company for every Four (04) Ordinary Voting Shares** held by them in the Company as at that date.

Where the Delivery vs Payment (DVP) is enabled, the shareholders of the Company who hold their shares in their respective CDS accounts/ in the share ledger as at end of trading on the third (3rd) market day from and excluding the date of the general meeting (i.e. the "Record date") will be entitled to this issuance of shares.

Your Board has also resolved that, in its opinion the Issue Price / consideration of **Rupees Six (LKR 6/-)** per Ordinary Voting Share is fair and reasonable to the Company and to all existing Shareholders.

MBSL by letter dated 12th March 2021 is in receipt of approval from the Director Department of Supervision of Non-Banking Financial Institutions of Central Bank of Sri Lanka (CBSL) to proceed with the Rights Issue in terms of the Finance Companies (Structural Changes) Direction No. 01 of 2013, subject to compliance with all statutory and regulatory requirements.

OBJECTIVE OF THE ISSUE

CBSL has introduced a new capital framework as given below for Non-Banking Financial Institutions under and in terms of the Finance Business Act Direction No 3 of 2018 dated 06 June 2018 as amended by their Circular dated 31 March 2020 issued to all licensed Finance Companies (relief given after COVID 19 pandemic)

	01.07.2018	01.07.2019	01.07.2020	01.07.2021	01.07.2022
Tier I	6.00%	6.50%	6.50%	7.00%	8.50%
Tier II	10.00%	10.50%	10.50%	11.00%	12.50%

Presently the Company is not in compliance with the aforesaid Capital Adequacy requirements.

The Company intends to raise a sum of **LKR 2,239,306,302** from the proposed Rights Issue of Shares to meet the Capital Adequacy requirements of the Company.

The Company intends to utilize the proceeds of the Rights Issue amounting to a sum upto **LKR 2,239,306,302** to increase the lending portfolio of the Company. The allocation of funds among the various products of the lending portfolio will be decided by the management upon taking into consideration of the risk factors, market conditions and

regulatory requirements. The Company intends to utilize these funds within a period of Twelve (12) months from the date of closure of the Rights Issue of Shares.

Until the funds are fully utilised for lending purpose the Company will invest the funds in Government securities, Money market instruments or any other form to generate sufficient income for the Company with the guidance of the Asset & Liability Management Committee (ALCO) which is headed by the Chief Executive Officer. The expected Rate of Return from such interim investments is the prevailing overnight REPO rate.

It is expected that the improvement in capital adequacy levels through the fund raising would enhance the stability of business operations of the Company thereby enabling MBSL to expand its loan portfolio. The proposed capital infusion would extend an opportunity for the shareholders to be part of the growth of the Company and benefit from the returns in future through improvement in expected profitability.

Capital Adequacy ratios of the Company pre and post Rights Issue of Shares are given below:

Item	Pre Rights Issue As at 31.12.2019 (Audited)	Pre Rights Issue As at 31.12.2020 (Audited)	Pre Rights Issue As at 31.03.2021 (Actual)	Post Rights Issue As at 31.12.2021
Tier I	5.64	3.30	3.39	11.06
Tier II	8.64	5.92	5.01	16.52

The above ratios are calculated assuming that the Rights Issue will be fully subscribed.

SPECIFIC RISKS ASSOCIATED WITH THE PURPOSE

The primary objective of the proposed Rights issue of shares is to raise funds to meet the Capital Adequacy requirements of the Company.

Our parent the Bank Of Ceylon has confirmed to MBSL that the BOC will subscribe for BOC's Rights entitlement to the value of **LKR 1.7 Bn.** In the event any other shareholders do not subscribe for their Rights entitlement and if the Rights Issue is under subscribed, the Company intends to meet the shortfall through a Private Placement of shares, subject to obtaining the necessary approvals relating thereto. This will enable the Company to overcome the risk associated with the under subscription of the Rights Issue of Shares. In the event the Company contemplate on private placement of shares to raise capital, the Company will make necessary market disclosures to the shareholders in accordance with the CSE Listing Rules as appropriate.

As BOC will be subscribing to their rights entitlement to the value of LKR 1.7Bn, the Company will be complied with the Capital Adequacy Ratio stipulated by the CBSL as at 31 December 2021. Hence the time gap in between the Rights Issue being undersubscribed and raising the shortfall of funds through a Private Placement of shares will not have a major impact on the Company. In the event of undersubscription of the Rights issue the Company intends to meet the shortfall through a Private Placement of shares.

Due to the low interest rate scenario and the expected credit growth of the country, the Company is not foreseeing any difficulty of lending the amount raised through the Rights Issue of Shares during the stipulated time period. Monthly average lending of the Company is around LKR 1.5Bn for the last 6 months (January 2021 to June 2021).

However, if there is any change in the utilization of funds mentioned above or if the Company couldn't utilize the funds in the stipulated time period, the Company will make necessary disclosures to the Shareholders through the Colombo Stock Exchange and thereafter obtain the necessary approvals from the relevant parties, including the Shareholders, as appropriate at that point of time.

The Company has no intention to lend or invest the proceeds of the Rights Issue with related parties as at the date of this circular and the proceeds will be utilized for lending in the normal course of business.

If the Company decides to lend or invest part of the proceeds of the Rights issue it will be done in compliance with directions issued by the CBSL under the Finance Business Act and the Section 9 of the Listing Rules of the Colombo Stock Exchange as applicable pertaining to related party transactions.

Capital infusion through the proposed Rights Issue will not amount to a "major transaction" of the Company as per the Companies Act No.07 of 2007.

DISCLOSURE IN THE FINANCIAL STATEMENTS AND THE ANNUAL REPORTS

Information as per the format given below will be disclosed in the Interim Financial Statements and the Annual Report/s of the Company from the date of raising funds until the funds are fully utilized by the Company.

Rights issue proceeds utilization as at dd.mm.yyy

Objective Number	Objective as per the Circular to the shareholders	Amount allocated as per the Circular to the shareholders in LKR	Proposed date of utilization as per the circular	Amount allocated from proceed in LKR (A)	% of total proceeds	Amount utilized in LKR (B)	% of utilization against allocation (B/A)	Clarification if not fully utilized including where the funds are invested (eg. whether lend to related party/ies etc.)

STATED CAPITAL

If the Rights issue is fully subscribed, subsequent to the Rights Issues of shares the Stated Capital of the Company will be increased from **LKR 2,124,457,307 to LKR 4,363,763,609** and the total number of shares in issue will be increased from 165,874,541 Ordinary Voting Shares to 539,092,258 Ordinary Voting Shares.

PERFORMANCE OF MBSL SHARE PRICE DURING THE PRECEDING 03 MONTHS

	Apr 2021	May 2021	June 2021
Highest (LKR)	7.50	9.40	9.40
Lowest (LKR)	6.00	6.80	6.00
Last Traded (LKR)	7.10	8.70	6.70

DIVIDEND HISTORY

MBSL has not declared any dividend during the last three financial years immediately preceding the date of this Circular.

TOP 20 SHAREHOLDERS

Top 20 Shareholders of the Company as at **31 March 2021** are set out below;

No.	Name of the Shareholder	No. of Shares	Holding %
01	Bank of Ceylon No. 1 Account	123,562,267	74.49%
02	Bank of Ceylon A/C Ceybank Unit Trust	11,798,960	7.11%
03	People's Leasing & Finance PLC/Mr.D.M.P.Disanayake	2,238,068	1.35%
04	Mr. A.M. Weerasinghe	839,201	0.51%
05	Hatton National Bank PLC/Ravindra Erle Ramukwelle	756,703	0.46%
06	People's Leasing & Finance PLC/L.P.Hapangama	571,654	0.34%
07	Merrill J Fernando & Sons (Pvt) Limited	526,165	0.32%
08	Mr. W.A.S.P. De Saram	500,778	0.30%

09	Mrs. R. Jothy	460,274	0.28%
10	Mr. T. Loganathan	428,340	0.26%
11	Mr. W.L.T. Anandawansa	400,100	0.24%
12	Seylan Bank PLC/Spice of Life (Pvt) Ltd	395,234	0.24%
13	Hatton National Bank PLC/Dinesh Nagendra Sellamuttu	386,301	0.23%
14	Mr.N. Balasingam	381,400	0.23%
15	Prime Lands (Pvt) Ltd	375,000	0.23%
16	Mr. B.T.Prathapasinghe	345,000	0.21%
17	Mr. A.Chelliah (deceased)	333,800	0.20%
18	Citizens Development Business finance PLC/ D. P. Tharindu Charuka Dissanayaka	308,212	0.19%
19	Mr. D.S.Tennakoon	303,600	0.18%
20	Mrs. S Tennakoon	300,000	0.18%
	TOTAL	145,211,057	87.54%

PUBLIC HOLDING

No. of Shares held by the public as at 31.03.2021	%
41,312,240	25.51

FINANCIAL HIGHLIGHTS

Summary of the financial performance of MBSL

(LKR '000)	3 months ended 31 March 2021 (Un Audited)	Year ended 31 Dec 2020 (Audited)	Year ended 31 Dec 2019 (Audited)	Year ended 31 Dec 2018 (Audited)
Total Income	1,483,790	5,188,013	6,839,015	6,549,905
Net interest income	717,807	1,417,848	2,201,454	2,442,466
Net fee and commission Income	33,032	94,822	183,081	208,142
Total operating income	769,488	1,633,152	2,481,893	2,795,401
Net operating income	901,324	1,069,721	2,202,220	2,660,870
Profit/(Loss) before income tax	311,037	(1,342,905)	57,194	446,676
Profit/(Loss) after Income Tax	260,838	(1,108,305)	102,584	181,285
Total assets	32,878,425	32,359,209	36,975,116	35,659,527
Total liabilities	31,149,736	30,891,358	34,367,328	33,135,423
Total equity	1,728,689	1,467,851	2,607,788	2,524,104
Net assets value per share (LKR)	10.42	8.85	15.72	15.22

The Company has incurred a loss of LKR 1.1Bn for the period ended 31st December 2020. This loss is primarily as a result of the increase in the Non-Performing loans, Loan impairment provision, and decrease in the projected interest income growth, which was impacted by the COVID -19 pandemic.

Furthermore, moratorium relief granted to customers who were eligible for concessionary terms on loan repayment as per the criteria stipulated by CBSL also resulted in a short term decrease in interest income. Despite same your Company has taken proactive measures to mitigate these factors and to provide continuous business support as well as uninterrupted service to its customers.

CONTINGENT LIABILITIES

The contingent liabilities of the Company as at 31st December 2020 and 31st March 2021 are set out in Note No. 49 of the Audited Financial Statements of the Company for the Financial year ended on 31 December 2020 and in page 4 of the Interim Financial Statements of the Company for the period ended 31 March 2021.

IMPACT OF THE COVID 19 PANDEMIC

The impact of the Covid 19 pandemic to the Company and its operations are setout in Note No. 50.4 of the Audited Financial Statements of the Company for the Financial year ended on 31

December 2020 and in page 7 of the Interim Financial Statements of the Company for the period ended 31 March 2021.

APPLICATIONS FOR RIGHTS

The offer to subscribe for the rights shares will be made by the Company by way of sending a Letter of Provisional Allotment, with provision for renouncing such rights in favour of the Central Depository Systems (Private) Limited (CDS). The manner in which the Letter of Provisional Allotment should be dealt with will be fully set out therein.

In allotting rights shares provisionally, the shareholding as appearing in the CDS and the shareholders register maintained by the Company Secretary will be amalgamated at the end of trading on the date of EGM.

New ordinary voting shares, not subscribed for as at the last date of acceptance and payment specified in the Provisional Letter of Allotment and any fractional share entitlements, will be deemed to have been declined and such declined shares will be pooled together and be allotted to the respective holders of shares who have applied for additional shares on a reasonable basis to be decided by the Board of Directors, or depending on the availability of shares, in full satisfaction of their request for additional rights, at the same price. The fractional entitlement referred to herein shall mean the fractions arising after applying the following formula.

Number of shares held by a shareholder as at end of trading on the date of the EGM/ Record date x 9

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In the event of an oversubscription, the Directors reserve the right of accepting or rejecting any application for additional shares in whole or in part.

The rights shares will be provisionally allotted on the date of the Extraordinary General Meeting of the Company (EGM) which will be the date of entitlement of the Rights shares and the Provisional Letters of Allotment will be dispatched within Five (5) Market Days from and excluding the date of entitlement. Trading of the "Rights" shall commence on the Fourth (4th) Market Day from and excluding the date of dispatch of Letters of Provisional Allotment. Such trading shall continue throughout the period of the renunciation of the Rights entitlement to the CDS.

Where Delivery vs Payment (DVP) is enabled, the shareholders of the Company who hold their shares in their respective CDS accounts/in the share ledger as at end of trading on the third (3rd) market day from and excluding the date of the EGM (i.e. "Record date") will be entitled to this issuance of shares.

Due to the current postal delay and some areas being under isolation and travel restrictions being imposed in the country due to the Covid 19 pandemic, taking in to account the practical difficulties that may be faced by the shareholders in receiving / physical transmission of the Provisional Letter of Allotment, the Company has decided to upload the Provisional Letter of Allotment (for both CDS and Ledger shareholders as applicable) to the websites of MBSL (www.mbslbank.com) and the CSE (www.cse.lk) in addition to posting the requisite Provisional Letter of Allotment, for the purpose of facilitating the shareholders to apply for the Rights Issue.

In terms of the Directive issued by the Securities & Exchange Commission of Sri Lanka made under the Circular No. 08/2010 dated 22 November 2010 and Circular No.13 /2010 issued by the Central Depository Systems (Pvt) Limited dated 30 November 2010, all new securities arising from the proposed Rights Issue will be directly deposited to the respective shareholders' CDS Account, within Twelve (12) Market days from the last date of acceptance and payment. **NO SHARE CERTIFICATE WILL BE ISSUED TO ANY SHAREHOLDERS.**

In the event of non-availability of the CDS Account Number, the new shares to be allotted, will only be registered in the share ledger maintained by the Company and **will not be entitled** to a share certificate and then it will **not be possible to trade** with the new securities, until such time the same has been deposited with the CDS. Therefore, please ensure strict adherence to the Directive issued by the SEC. Consequent to the opening of the CDS account by such shareholder, the new shares will be credited to such CDS account. Direct uploads pertaining to written requests received from shareholders to deposit such shares will be done every fortnight.

Kindly note that the timelines stipulated herein may differ when DVP is enabled. In such a situation the Company will make a market announcement on such changes.

DATES OF THE RIGHTS ISSUE

Subject to the approval of the shareholders being obtained for the Rights Issue, the date of provisional allotment shall be the same date as the date of the EGM. The shareholders duly registered in the Company's books including those holding shares in the CDS as at end of trading on the date of the EGM, shall be entitled to the Rights Issue.

The Company's shares shall trade ex-rights (XR) from the Market Day after the date of the Provisional allotment, until the date for the acceptance and payment for the Rights shares.

Rights "Entitlement" of the shareholders whose shares are held in the CDS, will be directly uploaded to the CDS Account and shareholders who do not have a CDS Account are requested to open a CDS Account and lodge their Shares prior to 18th August 2021 to facilitate trading from 31st August 2021 to 7th September 2021 (being the period of Renunciation).

Trading of Rights shall commence on 31st August 2021 the fourth (4th) market day from and excluding the date of dispatch of the Provisional Letter of Allotment, and trading shall continue throughout the period of Renunciation to Central Depository Systems (Private) Limited (From 31st August 2021 to 7th September 2021).

The last date for acceptance and payment for rights shares shall be 8th September 2021 being the 10th Market Day from and excluding the date of dispatch of the provisional letter of allotment.

When the CDS shareholders are required to subscribe the Rights Entitlement (partly or fully) they are required to send the remittance to their Stockbroker / Custodian Bank, not later than 4.30 p.m. on 7th September 2021 (being the last date of Renunciation to CDS) for onward transmission to the Registrars to the Issue.

The remittance must be made by online fund transfer or depositing a cheque/bank draft drawn upon any commercial bank operating in Sri Lanka and payable to **"MBSL Rights Issue Account"** maintained at Bank of Ceylon, Corporate Branch, Colombo.

Application for additional shares will be permitted. However, such additional shares will be available for allotment only in the event any of the existing shareholders do not take up their rights entitlement in part or in full or if the Letter of Acceptance and Registration is rejected by the Company as being invalid.

The direct remittance (with advice) should be forwarded with the Form of Acceptance & Registration (Form A) by the ledger shareholders and a separate direct remittance (with advice) should be forwarded with the Form of Application for Additional Ordinary Voting Shares (Form C) by CDS shareholders and ledger shareholders.

The remittance from Foreign/ Non-Resident shareholders must be made only out of an Inward Investment Account (IIA) maintained with a Commercial Bank operating in Sri Lanka. Such applications must be accompanied by a letter from the respective Commercial Bank confirming same.

All incomplete application/s with incorrect details will be rejected. Refunds in respect of the rejected applications shall be paid as expeditiously as possible but not exceeding ten (10) Market Days from the last date for acceptance and payment for the Rights shares.

The shares issued in respect of the Rights Issue will be directly deposited to the respective CDS Accounts of the Shareholders within Twelve (12) Market days from the last date for acceptance and payment for the rights shares. The relevant shareholders will be notified of such direct deposits within two (02) market days of the direct deposit.

Kindly note that the time lines stipulated herein may differ when DVP is enabled. In such a situation the Company will make a market announcement on such changes.

UNDERWRITING AGREEMENT

The Company has not entered into any Underwriting Agreement in relation to this Rights Issue.

In the event the issue is under subscribed, subscribers who have applied for rights and any additional rights applied for shall be allotted to the extent of the amount applied for in full.

In such event the Company intends to meet the shortfall through a Private Placement of shares, subject to making a market announcement and obtaining the necessary approvals relating thereto.

APPROVALS FOR LISTING

Approval in principle has been obtained from the Colombo Stock Exchange (CSE) to issue and list the new Ordinary Shares on the CSE. The listing of the new Ordinary Shares on the CSE will in no way be reflective of the merits of the issue. The CSE assume no responsibility for the correctness of any of the statements made, opinion expressed, or reports included herein.

DECLARATION BY THE DIRECTORS

The Directors of the Company, collectively and individually accept full responsibility for the accuracy of the information given and confirm, having made all reasonable inquiries, that to the best of their knowledge and belief that there are no other facts, the omission of which would render any statement in the Circular misleading.

MANAGERS TO THE RIGHTS ISSUE

Corporate Advisory & Capital Markets Division of Merchant Bank of Sri Lanka & Finance PLC of Level 18, "BOC Merchant Tower" 28, St Michael's Road, Colombo 03, Sri Lanka has been appointed as the Managers to the Issue.

REGISTRARS TO THE RIGHTS ISSUE

Central Depository Systems (Pvt) Ltd of No. 341/5, M & M Centre, Kotte Road, Rajagiriya, has been appointed as the Registrars to the Rights Issue.

EXTRAORDINARY GENERAL MEETING

An Extraordinary General Meeting (EGM) of the Shareholders of the Company is convened in terms of the attached Notice, at which the shareholders are requested to consider and if thought fit pass the requisite Resolution set out therein to give effect to the above stated matters.

In the current circumstances due to the Covid 19 pandemic and directives issued by the Health Authorities the Board of Directors of the Company has decided to convene the EGM as a virtual meeting in the best interest of protecting its shareholders and the society against the spread of Covid 19.

The Company will be taking steps to connect the shareholders to the EGM via audio or audio and visual means through electronic platform. Please refer the notes to the Notice of Meeting detailing "Guidelines and Special Instructions to Shareholders" for detailed information.

Yours faithfully,

By Order of the Board
MERCHANT BANK OF SRI LANKA & FINANCE PLC


Karnika Jayatilake
DGM Legal/ Head of Corporate Advisory
& Capital Markets Division


Lalangi Goonewardena
Chief Manager – Corporate Advisory
& Capital Markets Division

Managers to the Issue

On this 3rd day of August 2021