

2020-21

ANNUAL REPORT

FIRST CAPITAL FIXED INCOME FUND



First Capital
A Janashakthi Group Company

First Capital Asset Management Limited

About First Capital Asset Management Limited

First Capital Asset Management Limited is a subsidiary of First Capital Holdings PLC, a Janashakthi Group Company. First Capital provides a diverse range of financial advisory services and products through our integrated business platform in four specialised segments - Capital Markets Advisory, Wealth Management, Fixed Income and Equities. First Capital Holdings PLC is listed on the Colombo Stock Exchange (CSE) since 1994 (Ticker: CFVF), and exemplifies requisite financial transparency and governance standards. Reflecting credit fundamentals including a robust capital structure, liquidity, risk controls and earnings profile, we have been rated “A” by ICRA Lanka Limited.

First Capital Asset Management Limited has two business segments namely, Investment (Portfolio) Management and Management of Unit Trust Funds regulated by the Securities and Exchange Commission of Sri Lanka (SEC). The Bank of Ceylon (BOC) acts as the Trustee for our Unit Trust Funds.

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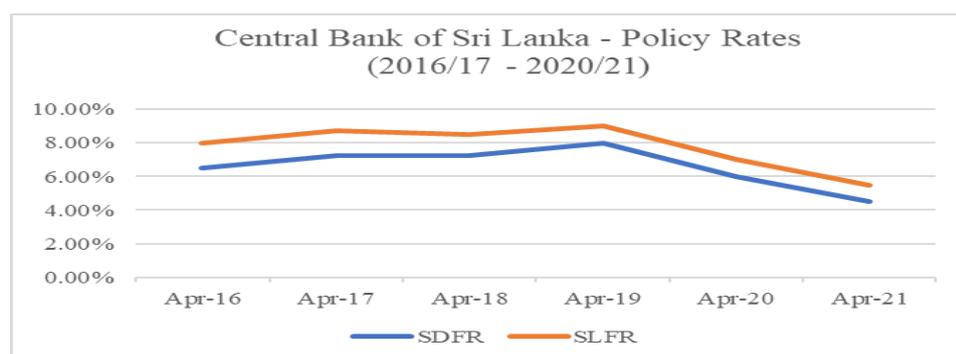
REPORT OF THE MANAGER

We have pleasure in presenting to you the Audited Financial Statements of First Capital Fixed Income Fund for the year ended 31st March 2021.

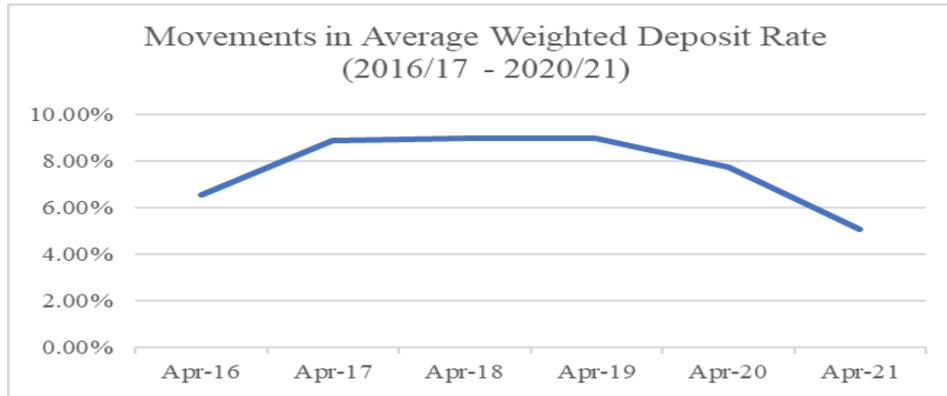
Economic and Industry Overview

Sri Lanka confronted a severe economic shrinkage in 2020, recording 3.6% contraction in GDP in the midst of persisted COVID-19 pandemic woes. The economy began to stabilise during the second half of the year with lifting of lockdowns and gradual resurrection of business operations along with the consumer demand, that was dimmed by the re-surge of 2nd wave of the pandemic occurred towards the end of the year 2020. The country is going through another lockdown amidst the 3rd wave of COVID-19 potentially slowing down economic activity. Nonetheless, the country wide rapid vaccination programmes increased private consumption amidst prevailing low-interest rates and the anticipated future foreign direct investments are expected to fasten the economic recovery in 2021 and beyond.

The market liquidity remained positive throughout 2020 and surged up to over LKR 200Bn during December 2020, while the domestic interest rates were kept low through the continuous injection of liquidity by the Central Bank of Sri Lanka (CBSL). Meanwhile, the private credit growth improved to 7.5% in March 2021 (year-on-year) indicating a gradual revival amidst rising uncertainty. The CBSL continued to extend relief measures to households and businesses affected by the economic distress via adopting an accommodative monetary policy, concessional credit schemes, debt moratorium, etc. to induce private sector credit growth.



The unit trust industry exhibited a significant growth during 2020 owing to the interest rates bottoming out that shifted the client focus towards alternative investments that yield substantial returns, thereby making fixed deposits and bank savings less attractive amidst the rising wealth supported by the excess liquidity, blended with the extensive market awareness campaigns.



During 2020/21, there were 16 licensed unit trust management companies with 67 funds in operation. Total assets under management were Rs. 221Bn as at 31st March 2021 (Source: The Unit Trust Association of Sri Lanka).

Fund Performance

First Capital Fixed Income Fund reported a Profit after Tax of Rs. 113Mn for the year ended 31st March 2021 compared to Rs. 88Mn in the previous year (2019/20).

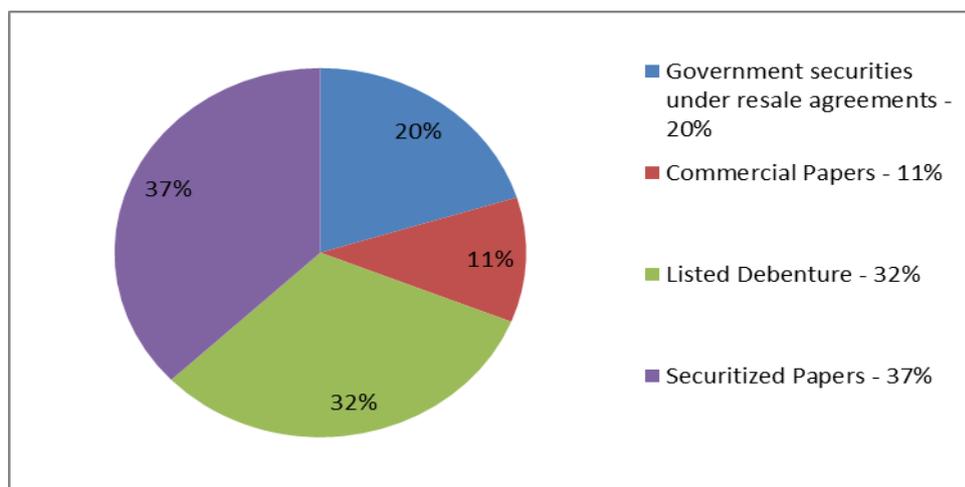
The Fund reported an Annualised Return of 13.71% for the year ended 31st March 2021 compared to the average 5-year treasury bond yield (base yield) of 7% (source: Central Bank of Sri Lanka - *Monthly Economic Indicators*; <https://www.cbsl.gov.lk/statistics/economic-indicators/monthly-indicators>). 5-year treasury bond (risk free return) is used to evaluate the performance of the Fund which denotes the return over the risk-free return since there is no appropriate benchmark index for the Fund).

The Annualised Return reported in the previous year (2019/20) was 11.81% compared to the average 5-year treasury bond yield (base yield) of 10% (source: Central Bank of Sri Lanka - *Monthly Economic Indicators*; <https://www.cbsl.gov.lk/statistics/economic-indicators/monthly-indicators>). The Funds under Management as at 31st March 2021 were Rs. 939Mn compared to Rs. 826 Mn as at 31st March 2020.

In accordance with Sri Lanka Financial Reporting Standards, the Fund is accounted for on a marked-to-market basis wherein the return to investors reduces during periods of rising interest rates and increases when interest rates are decline.

The asset allocation of the Fund as at the reporting date is as follows.

Asset Allocation as at 31st March 2021



Future Outlook

As a result of the COVID-19 pandemic, Sri Lanka's economy contracted by 3.6% in 2020. The Central Bank of Sri Lanka anticipates that growth estimates to be revised to below 5.0% from an earlier expectation of 6.0% amidst extensive restrictions on businesses, livelihoods, and many aspects of everyday lives resulting in a heavier toll on the economy. However, the economy is expected to recover in the short to medium term supported by the Government's stimulus measures introduced, improved business sentiments fueled by the COVID-19 vaccination drive and improving prospects of the global economy. Nevertheless, the effort to maintain the prevailing low interest rate environment will be contested to a certain extent with Sri Lanka's challenging medium-term debt service requirement.

Appreciations

We take this opportunity to thank our valued unitholders for the confidence placed in us. We also place on record our appreciation for the unstinted support extended by the Securities and Exchange Commission of Sri Lanka and our Trustee, Bank of Ceylon.

We convey our sincere thanks to the Board of Directors, Management Team and Staff of First Capital Asset Management Limited for their enthusiasm and hard work which has contributed towards our performance.

INDEPENDENT AUDITOR'S REPORT TO THE UNITHOLDERS OF FIRST CAPITAL FIXED INCOME FUND

Report on the Audit of the Financial Statements

Opinion

We have audited the financial statements of First Capital Fixed Income Fund ("the Fund"), which comprise the statement of financial position as at 31 March 2021, and the statement of profit or loss and other comprehensive income, statement of changes in unitholders' funds and statement of cash flows for the year then ended, and notes to the financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying financial statements give a true and fair view of the financial position of the fund as at 31 March 2021, and of its financial performance and its cash flows for the year then ended in accordance with Sri Lanka Accounting Standards.

Basis for Opinion

We conducted our audit in accordance with Sri Lanka Auditing Standards (SLAuSs). Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Statements* section of our report. We are independent of the fund in accordance with the ethical requirements of the Code of Ethics issued by CA Sri Lanka (Code of Ethics) that are relevant to our audit of the financial statements, and we have fulfilled our other ethical responsibilities in accordance with the Code of Ethics. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Other Information

The fund management company is responsible for the other information. The other information comprises the report of the manager but does not include in the financial statements and our auditor's report thereon.

Our opinion on the financial statements does not cover the other information included in the Manager's report and we will not, express any form of assurance conclusion thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information identified above and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated.

If, based on the work we have performed on the other information that we obtained prior to the date of this auditor's report, we conclude that there is a material misstatement of this other information, we are required to communicate the matter to those charged with governance. We have nothing to report in this regard.

Responsibilities of Management and Those Charged with Governance for the Financial Statements

The fund management company is responsible for the preparation of financial statements that give a true and fair view in accordance with Sri Lanka Accounting Standards and for such internal control as the management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, Fund manager is responsible for assessing the fund's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless fund manager either intends to liquidate the fund or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the fund's financial reporting process.

Auditor's Responsibilities for the Audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with SLAuSs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

As part of an audit in accordance with SLAuSs, we exercise professional judgment and maintain professional skepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit 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 fund's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by fund manager.
- Conclude on the appropriateness of fund manager's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the fund's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the fund to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

Report on Other Legal and Regulatory Requirements

These financial statements also comply with the requirements of the Rule 27(3) of the Unit Trust Code of September 2011 issued by the Securities and Exchange Commission of Sri Lanka under the Act No. 36 of 1987 and the trust deed.

SJMS Associates

SJMS ASSOCIATES
Chartered Accountants
Colombo
30 June 2021

FIRST CAPITAL FIXED INCOME FUND
STATEMENT OF PROFIT OR LOSS AND OTHER COMPREHENSIVE INCOME
FOR THE YEAR ENDED 31 MARCH 2021

| | Note | 2020/2021 Rs. | 2019/2020 Rs. |
|---|---------------|--------------------|-------------------|
| Income | 7 | 99,994,847 | 89,409,300 |
| Direct expenses | 8 | (468) | (542,873) |
| Net trading income | | 99,994,379 | 88,866,427 |
| Gain on fair valuation of financial assets - fair value through profit or loss | | 19,940,389 | 7,705,646 |
| | | 119,934,768 | 96,572,073 |
| Administration expenses | 9 | (6,785,247) | (6,196,581) |
| Other operating expenses | 10 | (11,000) | (1,972,402) |
| Provision / (reversal) for impairment of financial assets at amortised cost | 14.3.1 | 139,600 | (8,705) |
| Profit before taxation | | 113,278,121 | 88,394,385 |
| Income tax expenses | 11 | - | - |
| Profit for the year | | 113,278,121 | 88,394,385 |
| Other comprehensive income | | - | - |
| Total comprehensive income for the year | | 113,278,121 | 88,394,385 |

Figures in bracket indicate deductions.

The attached notes from 1 to 25 form an integral part of these financial statements.

**FIRST CAPITAL FIXED INCOME FUND
STATEMENT OF FINANCIAL POSITION
AS AT 31 MARCH 2021**

| | Note | 31.03.2021 Rs. | 31.03.2020 Rs. |
|--|------|--------------------|--------------------|
| Assets | | | |
| Cash at bank | 12 | 235,775 | 786,867 |
| Financial assets -at fair value through profit or loss | 13 | 743,474,234 | 589,269,610 |
| Financial assets - at amortised cost | 14 | 190,149,392 | 236,185,044 |
| Taxes receivable | 15 | - | - |
| Other receivable | 16 | 6,825,645 | 1,385,033 |
| Total Assets | | 940,685,046 | 827,626,554 |
| Unit holders' funds and liabilities | | | |
| Liabilities | | | |
| Accrued expenses and other liabilities | 17 | 1,223,653 | 1,443,282 |
| Total Liabilities | | 1,223,653 | 1,443,282 |
| Unit holders' funds | | | |
| Net assets attributable to unit holders | | 939,461,393 | 826,183,272 |
| | | 939,461,393 | 826,183,272 |
| Total unit holders' funds and liabilities | | 940,685,046 | 827,626,554 |
| Net assets per unit (Rs.) | 18 | 1,873.80 | 1,647.86 |

The attached notes from 1 to 25 form an integral part of these financial statements.

The Management Company of First Capital Fixed Income Fund is responsible for the preparation and presentation of these financial statements in accordance with the Sri Lanka Accounting Standards.

Approved by the Fund Management Company on 30 June 2021.



Mangala Jayashantha
Chief Financial Officer
First Capital Asset Management Limited
Fund Management Company



Dilshan Wirasekara
Director / Chief Executive Officer
First Capital Asset Management Limited
Fund Management Company



Dinesh Schaffter
Managing Director
First Capital Asset Management Limited
Fund Management Company

FIRST CAPITAL FIXED INCOME FUND
STATEMENT OF CHANGES IN UNIT HOLDERS' FUNDS
FOR THE YEAR ENDED 31 MARCH 2021

| | Unit Capital Rs. | Retained Earnings Rs. | Total Equity Rs. |
|---|---------------------------------|--------------------------------------|-----------------------------|
| Balance as at 1 April 2019 | 596,746,323 | 201,042,564 | 797,788,887 |
| Capital infused during the year | - | - | - |
| Capital withdrawals during the year | (60,000,000) | - | (60,000,000) |
| Increase in net assets attributable to unit holders | - | 88,394,385 | 88,394,385 |
| Balance as at 31 March 2020 | 536,746,323 | 289,436,949 | 826,183,272 |
| Balance as at 1 April 2020 | 536,746,323 | 289,436,949 | 826,183,272 |
| Capital infused during the year | - | - | - |
| Capital withdrawals made during the year | - | - | - |
| Increase in net assets attributable to unit holders | - | 113,278,121 | 113,278,121 |
| Balance as at 31 March 2021 | 536,746,323 | 402,715,070 | 939,461,393 |

Figures in brackets indicate deductions.

The attached notes from 1 to 25 form an integral part of these financial statements.

FIRST CAPITAL FIXED INCOME FUND
STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED 31 MARCH 2021

| | 2020/2021 Rs. | 2019/2020 Rs. |
|--|-------------------|---------------------|
| Cash flows from operating activities | | |
| Profit before taxation | 113,278,121 | 88,394,385 |
| Adjustment for : | | |
| Gain on fair valuation of financial assets at fair value through profit or loss | (19,940,389) | (7,705,646) |
| Provision for tax receivable (<i>Note 14</i>) | - | 1,945,002 |
| (Reversal) / provision for impairment of financial assets at amortised cost (<i>Note 13.3.1</i>) | (139,600) | 8,705 |
| Operating profit before working capital changes | 93,198,132 | 82,642,446 |
| (Increase) / decrease in financial assets -at fair value through profit or loss | (134,264,235) | (64,939,910) |
| Decrease in financial investments -at amortised cost | 46,175,252 | 40,389,407 |
| (Increase) / decrease in other receivables | (5,440,612) | 757,069 |
| (Decrease) / increase in accrued expenses and other liabilities | (219,629) | 663,423 |
| Cash flows (used in) / from operating activities | (551,092) | 59,512,435 |
| Tax paid | - | - |
| Net cash flows (used in) / from operating activities | (551,092) | 59,512,435 |
| Net cash flows from / (used in) investing activities | - | - |
| Cash flows from financing activities | | |
| Capital infused by unit holders | - | - |
| Capital redeemed by by unit holders | - | (60,000,000) |
| Net cash flows used in financing activities | - | (60,000,000) |
| Net (decrease) / increase in cash and cash equivalents for the year | (551,092) | (487,565) |
| Cash and cash equivalents at the beginning of the period | 786,867 | 1,274,432 |
| Cash and cash equivalents at the end of the period (<i>Note 12</i>) | 235,775 | 786,867 |

Figures in bracket indicate deductions.

The attached notes from 1 to 25 form an integral part of these financial statements.

**FIRST CAPITAL FIXED INCOME FUND
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 MARCH 2021**

1. Reporting entity

First Capital Fixed Income Fund is an Open-Ended Unit Trust approved by the Securities and Exchange Commission of Sri Lanka on 25th April 2014.

The registered office/ place of business of the Unit Trust is located at No. 2, Deal Place, Colombo 03. First Capital Asset Management is the Managing Company of First Capital Fixed Income Fund while Bank of Ceylon has been appointed as the Trustee.

1.1. Principal activities

The Unit Trust engages in investment in fixed income securities (i.e. Government Securities and Corporate Debt Securities) on behalf of its clients. The operations of the Trust commenced on 25th July 2014.

The Objective of the First Capital Fixed Income Fund is to yield superior returns to Unit Holders while minimizing their risk through investments in Fixed Income Securities placed according to the parameters stated in the Unit Trust Code.

There were no significant changes in the nature of the principle activities of the Unit Trust during the year under review.

1.2. Approval of financial statements

The financial statements of the fund for the year ended 31st March 2021 were authorised for issue by the Fund Management Company and the Trustee on 30 June 2021.

2. Basis of preparation

2.1. Statement of compliance

The financial statements of the Unit Trust which comprise the statement of financial position, statement of profit or loss and other comprehensive income, statement of changes in unit holders' funds, statement of cash flows and notes thereto have been prepared in accordance with the Sri Lanka Accounting Standards (SLFRS and LKAS) laid down by the Institute of Chartered Accountants of Sri Lanka and adopted as directed by the Securities and Exchange Commission of Sri Lanka.

The statement of financial position is presented on a liquidity basis and assets and liabilities are presented in decreasing order of liquidity and are not distinguished between current and non-current.

2.2. Basis of measurement

The financial statements have been prepared on the historical cost basis and applied consistently with no adjustments being made for inflationary factors affecting the financial statements, except for the financial assets at fair value through profit or loss.

2.3. Functional and presentation currency

The financial statements are presented in Sri Lankan Rupees, which is the Unit Trust's functional currency.

2.4. Use of estimates and judgments

The preparation of financial statements in conformity with the Sri Lanka Accounting Standards requires management to make judgments, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised and in any future periods affected.

FIRST CAPITAL FIXED INCOME FUND
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 MARCH 2021

2.4 Use of estimates and judgments – (Contd..)

Information about significant areas of estimation, uncertainty and critical judgments in applying accounting policies that have the most significant effect on the amounts recognised in the financial statements are described in the relevant Notes as follows.

- Recognition and measurement of financial instruments (Note 4.1.1 to 4.1.5)
- Identification, measurement and assessment of impairment (Note 4.1.6)

2.5 Going Concern

The management has made an assessment of the Unit Trust's ability to continue as a going concern and is satisfied that it has the resources to continue in business for the foreseeable future. Furthermore, management is not aware of any material uncertainties that may cast significant doubt upon the Unit Trust's ability to continue as a going concern. Therefore, the Financial Statements continue to be prepared on the going concern basis.

3. Materiality and presentation

Each material class of similar item is presented separately in the financial statements. Items of dissimilar nature or function are presented separately unless they are immaterial.

Assets and liabilities are grouped by nature and listed in an order that reflects their relative liquidity and maturity pattern. Where appropriate, the significant accounting policies are disclosed in the succeeding notes.

Assets and liabilities are offset and the net amount reported in the Statement of Financial Position, only when there is a legally enforceable right to offset the recognised amounts and there is an intention to settle on a net basis or to realise the assets and settle the liabilities simultaneously. Income and expenses are not offset in the Income Statement, unless required or permitted by Sri Lanka Accounting Standards.

4. Significant accounting policies

4.1 Financial Instruments

4.1.1. Initial recognition

Financial assets and liabilities are initially recognized on the trade date, i.e. the date that the Fund becomes a party to the contractual provisions of the instrument. This includes purchases or sales of financial assets that require delivery of assets within the time frame generally established by regulation or convention in the market place.

4.1.2. Initial measurement of financial instrument

The classification of financial instruments at initial recognition depends on their contractual terms and the business model for managing the instruments. At initial recognition, the Fund measures a financial asset at its fair value plus transaction costs that are directly attributable to the acquisition of the financial asset. Transaction costs of financial assets carried at FVPL are expensed in the statement of profit or loss.

4.1.3. Measurement categories of financial assets and liabilities

The Fund classifies all its financial assets in the following measurement categories:

- those to be measured at amortised cost
- those to be measured at fair value through profit or loss

Financial liabilities of the Fund are measured at amortised cost, and includes all financial liabilities, other than those measured at fair value through profit or loss. The financial liabilities of the Fund include accrued expenses and other payables.

**FIRST CAPITAL FIXED INCOME FUND
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 MARCH 2021**

4.1.4. Subsequent measurement

Amortised cost: A debt instrument is measured at amortised cost if it is held within a business model whose objective is to hold financial assets in order to collect contractual cash flows and its contractual terms give rise to cash flows that are solely payments of principal and interest on the principal amount outstanding.

Debt instruments at amortised cost in the statement of financial position comprise of investments in Resale agreements against Government Securities and Fixed Deposits. Any gain or loss arising on de-recognition is recognised directly in profit or loss and presented in realised gain/(loss) on debt instruments held at amortised cost.

FVPL: A financial asset is measured at fair value through profit or loss if:

- (a) Its contractual terms do not give rise to cash flows on specified dates that are solely payments of principal and interest on the principal amount outstanding
Or
- (b) It is not held within a business model whose objective is either to collect contractual cash flows, or to both collect contractual cash flows and sell
Or
- (c) At initial recognition, it is irrevocably designated as measured at FVPL when doing so eliminate or significantly reduces a measurement or recognition inconsistency that would otherwise arise from measuring assets or liabilities or recognising the gains and losses on them on different bases.

A gain or loss on a debt investment that is subsequently measured at FVPL is recognised in profit or loss and presented net within unrealised gains/(losses) in the period in which it arises. Financial assets at fair value through profit or loss at statement of financial position comprise of investment in Government Securities and Corporate Debt Securities.

4.1.5. Financial liabilities

a) Initial recognition and measurement

The Fund determines the classification of its financial liabilities at initial recognition. The Fund's financial liabilities comprise of accrued expenses and other payables in the Statement of Financial Position.

b) Subsequent measurement

The measurement of financial liabilities depends on their classification as described below:

Other financial liabilities

After initial recognition, other financial liabilities are subsequently measured at amortised cost using the EIR method. Gains and losses are recognised in the profit or loss and other comprehensive income statement when the liabilities are derecognised as well as through the EIR amortisation process.

4.1.6. Identification, measurement and assessment of impairment

The Fund assesses on a forward-looking basis, the expected credit losses (ECLs) associated with its debt instruments not held at fair value through profit or loss. The impairment methodology applied depends on whether there has been a significant increase in credit risk.

ECLs are based on the difference between the contractual cash flows due in accordance with the contract and all the cash flows that the Fund expects to receive, discounted at an approximation of the original effective interest rate.

**FIRST CAPITAL FIXED INCOME FUND
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 MARCH 2021**

4.1.6. Identification, measurement and assessment of impairment(Contd..)

ECLs are recognized in two stages. For credit exposures for which there has not been a significant increase in credit risk since initial recognition, ECLs are provided for credit losses that result from default events that are possible within the next 12-months (a 12-month ECL). For those credit exposures from which there has been a significant increase in credit risk since initial recognition, a loss allowance is required for credit losses expected over the remaining life of the exposure, irrespective of the timing of the default (a lifetime ECL).

The Fund uses the ratings from either Fitch Rating Lanka Limited or ICRA Lanka Limited as applicable to determine the significant deterioration in credit risk and to estimate the ECLs.

Consistent with the policies of the Fund, investments when rated below BBB- are considered as non-investment grade investments and the Fund considers such investments as having incurred significantly deteriorated credit risk. Such investments are considered for lifetime ECL calculation. Further, movements within the ratings of the investment grade stipulate significant deterioration of credit risk. Significant deterioration is measured through a two notches downgrade of the external credit rating of the counterparty since the origination of the instrument.

For debt instruments at amortized cost issued by Sovereign, the Fund applies the low risk simplification.

At each reporting date the Unit Trust assesses whether there is objective evidence that financial assets not carried at fair value through profit or loss are impaired. A financial asset or a group of financial assets is impaired when objective evidence demonstrates that a loss event has occurred after the initial recognition of the asset(s), and that the loss event has an impact on the future cash flows of the asset(s) that can be estimated reliably.

Objective evidence that financial assets (including equity securities) are impaired can include significant financial difficulty of the borrower or issuer, default or delinquency by a borrower, restructuring of a loan or advance by the Unit Trust on terms that the Unit Trust would not otherwise consider, indications that a borrower or issuer will enter bankruptcy, the disappearance of an active market for a security, or other observable data relating to a group of assets such as adverse changes in the payment status of borrowers or issuers in the group, or economic conditions that correlate with defaults in the group.

The Unit Trust considers evidence of impairment for financial assets at amortised cost at both a specific asset and collective level. All individually significant financial assets at amortised cost are assessed for specific impairment. All individually significant financial assets at amortised cost found not to be specifically impaired are then collectively assessed for any impairment that has been incurred but not yet identified. Financial assets at amortised cost that are not individually significant are collectively assessed for impairment by grouping together financial assets at amortised cost with similar risk characteristics.

In assessing collective impairment, the Unit Trust uses of historical trends of the probability of default, adjusted for management's judgment as to whether current economic and credit conditions are such that the actual losses are likely to be greater or less than suggested by historical data.

Impairment loss on assets carried at amortised cost is measured as the difference between the carrying amount of the financial asset and the present value of estimated future cash flows discounted at the asset's original effective interest rate. Impairment loss is recognised in profit or loss and reflected in an allowance account against loans and advances. Interest on impaired assets continues to be recognised through the unwinding of the discount. When a subsequent event causes the amount of impairment loss to decrease, the decrease in impairment loss is reversed through profit or loss.

**FIRST CAPITAL FIXED INCOME FUND
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 MARCH 2021**

4.1.6. Identification, measurement and assessment of impairment(Contd..)

Impairment loss on financial asset at fair value through other comprehensive income is recognised by transferring the cumulative loss that has been recognised in other comprehensive income to profit or loss as a reclassification adjustment. The cumulative loss that is reclassified from other comprehensive income to profit or loss is the difference between the acquisition cost, net of any principal repayment and amortisation, and the current fair value, less any impairment loss previously recognised in profit or loss. Changes in impairment provisions attributable to time value are reflected as a component of interest income.

If, in a subsequent period, the fair value of an impaired financial asset at fair value through other comprehensive income increases and the increase can be objectively related to an event occurring after the impairment loss was recognised in profit or loss, then the impairment loss is reversed, with the amount of the reversal recognised in profit or loss. However, any subsequent recovery in the fair value of an impaired financial asset at fair value through other comprehensive income equity security is recognised in other comprehensive income.

The Unit Trust writes off certain loans and advances and investment securities when they are determined to be uncollectible.

4.1.7. Sale and repurchase agreements

Securities sold subject to repurchase agreements (repos) remain on the Statement of Financial Position, the counterparty liability is included under borrowings. Securities purchased under agreements to resell (reverse repos) are recorded as loans and advances. The difference between sale and repurchase price is treated as interest and accrued over the life of the agreements using the effective interest method.

4.1.8. Impairment of non-financial assets

The carrying amounts of the Unit Trust's non-financial assets, other than deferred tax assets, are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists, then the asset's recoverable amount is estimated. The recoverable amount of an asset or cash generating unit is the greater of its value in use and its fair value less costs to sell. For intangible assets that have indefinite useful lives, the recoverable amount is estimated each year. An impairment loss is recognised if the carrying amount of an asset exceeds its estimated recoverable amount. Impairment loss is recognised in profit or loss.

An impairment loss recognised in prior periods is assessed at each reporting date for any indication that the loss has decreased or no longer exists. An impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised.

4.1.9 De-recognition

A financial asset is de-recognised when,

- 1) The rights to receive cash flows from the asset have expired.
- 2) The Fund has transferred its rights to receive cash flows from the asset or has assumed an obligation to pay the received cash flows in full without material delay to a third party under a 'pass-through' arrangement; and either,
 - The Fund has transferred substantially all the risks and rewards of the asset or
 - The Fund has neither transferred nor retained substantially all the risks and rewards of the asset but has transferred control of the asset.

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4.1.10 Offsetting of financial instruments

Financial assets and financial liabilities are offset, and the net amount reported in the statement of financial position if, and only if:

- there is a currently enforceable legal right to offset the recognised amounts and
- there is an intention to settle on a net basis, or to realise the assets and settle the liabilities simultaneously

4.2. Dividend payable

Dividend payable is recognised at the time the dividend recommended and declared by the Board of Directors.

4.3. Provision

A provision is recognised if, as a result of a past event, the Unit Trust has a present legal or constructive obligation that can be estimated reliably, and it is probable that an outflow of economic benefits will be required to settle the obligation.

4.4. Commitments and contingencies

All discernible risks are accounted for in determining the amount of all known liabilities.

Contingent liabilities are possible obligations whose existence will be confirmed only by uncertain future events or present obligations where the transfer of economic benefit is not probable or cannot be reliably measured. Contingent liabilities are not recognised in the Statement of Financial Position but are disclosed unless they are remote.

4.5. Interest

Interest income and expenses are recognised in profit or loss using the effective interest method. The effective interest rate is the rate that exactly discounts the estimated future cash payments and receipts through the expected life of the financial asset or liability (or, where appropriate, a shorter period) to the carrying amount of the financial asset or liability. When calculating the effective interest rate, the Unit Trust estimates future cash flows considering all contractual terms of the financial instrument, but not future credit losses.

Interest income and expenses presented in the Statement of Comprehensive Income include interest on financial assets and financial liabilities measured at amortised cost calculated on an effective interest basis and fair value changes in financial asset measured at fair value through profit and loss.

Fair value changes on all other financial assets and liabilities carried at fair value through profit or loss, are presented in net trading income in the statement of comprehensive income.

Interest income is recognised on net of withholding tax up to 31st December 2019 and on gross basis with effect from 1st January 2020 in line with notice issued by Department of Inland Revenue on changes to Inland Revenue Act No. 24 of 2017.

4.6. Gain/ (loss) on securities

i. Unrealised gains / (losses) on financial assets at FVTPL

Unrealised gains / (losses) on financial assets at FVTPL includes all gains and losses that arise from changes in fair value of the financial assets at FVTPL as at the reporting date.

ii. Realised gains / (losses) on financial assets at FVTPL

Realised gains / (losses) on financial assets at FVTPL includes realised trading gains and losses on sale of quoted equity securities.

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4.7. Income tax expenses

The provision for income tax is based on the elements of income and expenditure as reported in the financial statements and computed in accordance with the provisions of Inland Revenue Act.

The tax rates and tax laws used to compute the amount are those that are enacted or substantively enacted, at the reporting date. The fund is not liable to pay income tax as at the reporting date in accordance with the Inland Revenue Act No. 24 of 2017. The fund's income generated through investment business are treated as "pass through vehicles" under the provisions of Inland Revenue Act No. 24 of 2017.

4.8. Offsetting

Current tax assets and liabilities and deferred tax assets and liabilities are offset only to the extent that they relate to income taxes imposed by the same taxation authority, there is a legal right and intentions to settle on a net basis and it is allowed under the tax law of the relevant jurisdiction.

4.9. Statement of cash flows

The statement of cash flows has been prepared using the "Indirect Method" of preparing cash flows in accordance with the Sri Lanka Accounting Standard LKAS 7 - "Statement of Cash Flows". Cash and cash equivalents comprise short term, highly liquid investments that are readily convertible to known amounts of cash and are subject to an insignificant risk of changes in value.

Presentation

Assets and liabilities are grouped by nature and listed in an order that reflects their relative liquidity and maturity pattern. Where appropriate, the significant accounting policies are disclosed in the succeeding notes.

4.12. Events occurring after the reporting period

Events occurring after the reporting period are those events, favorable and unfavorable, that occur between the reporting date and the date the Financial Statements are authorised for issue.

All material and important events that occurred after the reporting date have been considered and appropriate disclosures are made in the financial statements.

5. Comparative information

The comparative information is re-classified wherever necessary to conform with the current year's classification in order to provide a better presentation.

6. New Accounting Standard amendments issued but not effective as at reporting date

The Institute of Chartered Accountants of Sri Lanka has issued following new Sri Lanka Accounting Standard amendments (SLFRSs/LKASs) which will become applicable for financial periods beginning after on or after 1 April 2021. Accordingly, the Fund has not applied the following new standard amendments in preparing these Financial Statements.

The following amended standards are not expected to have a significant impact on the Fund's financial statements.

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6.1. Interest Rate Benchmark Reform (IBOR) (Amendments to SLFRS 9 and SLFRS 7)

IBOR reform is expected to result in a change to the basis for determining contractual cash flows of impacted assets and liabilities of the Fund. The amendments provide a practical expedient to account for a change in the basis for determining the contractual cash flows as a result of IBOR reform by updating the effective interest rate.

The standard includes amendments in respect of:

- Modification of a financial asset or a financial liability measured at amortised cost
- Additional relief for hedging relationships

On 15 January 2021, the CA Sri Lanka issued Interest Rate Benchmark Reform (Phase 1 and Phase 2) which is mandatory for application in respect of annual periods beginning on or after 1 January 2021.

6.2. Onerous Contracts - Cost of fulfilling the contract (Amendments to LKAS 37 - Provisions, Contingent Liabilities and Contingent Assets)

The amendment specifies that the ‘cost of fulfilling’ a contract comprises the ‘costs that relate directly to the contract’. Costs that relate directly to a contract can either be incremental costs of fulfilling that contract (direct labour, materials) or an allocation of other costs that relate directly to fulfilling contracts (allocation of the depreciation charge for an item of property, plant and equipment used in fulfilling the contract).

The above amendment to Standard will be effective for annual reporting periods beginning on or after 1 January 2022.

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| | 2020/2021 | 2019/2020 |
|--|-------------------|-------------------|
| | Rs. | Rs. |
| 7. Income | | |
| Interest income on financial assets at fair value through profit and loss | 84,277,521 | 61,482,332 |
| Interest income on financial assets - at amortised cost | 14,522,805 | 26,558,884 |
| Placement fee | 1,194,521 | 1,368,084 |
| | 99,994,847 | 89,409,300 |
| 8. Direct expenses | | |
| Interest expense on repurchase agreements | 468 | 542,873 |
| | 468 | 542,873 |
| 9. Administration expenses | | |
| Management fee | 4,458,705 | 4,013,184 |
| Trustee fee | 2,118,776 | 1,988,997 |
| Auditor's remuneration | 207,766 | 194,400 |
| | 6,785,247 | 6,196,581 |
| 10. Other operating expenses | | |
| Provision for Tax Receivable (<i>Note 10.1</i>) | - | 1,945,002 |
| Bank charges | 11,000 | 27,400 |
| | 11,000 | 1,972,402 |
| 10.1 Provision for tax receivable | | |
| Provision had made for the remaining withholding tax receivable of the Fund in prior year since the recoverability is remote in line with the prevailing tax legislation. No any tax receivables identified during 2020/2021 period. The Fund is not subject to income tax as an entity. | | |
| 11. Income tax expenses | | |
| First Capital Fixed Income Fund is a Unit Trust licensed by the Securities and Exchange Commission of Sri Lanka. Unit Trust is defined as "Pass through vehicle" and is not taxed as an entity in accordance with the Inland Revenue Act, No. 24 of 2017 and the amendments thereto (2019/20 - nil). | | |
| Reconciliation between current tax expense and the accounting profit | | |
| Accounting profit from ordinary activities before tax | 113,278,121 | 88,394,385 |
| Less:- Exempted income | (113,278,121) | (88,394,385) |
| Taxable income | - | - |
| Income tax provision for the year | - | - |
| As at | 31.03.2021 | 31.03.2020 |
| | Rs. | Rs. |
| 12. Cash at bank | | |
| Bank of Ceylon - Corporate Branch (<i>Note 12.1</i>) | 235,775 | 786,867 |
| | 235,775 | 786,867 |

12.1 Bank balances are maintained only to settle day to day operations. Excess cash balances are reviewed on a daily basis and transferred the same to investment account. Remaining cash at bank represent current account balance with banks, which are due on demand. Accordingly no impairment provision is required.

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| | 31.03.2021 | 31.03.2020 |
|--|--------------------|--------------------|
| | Rs. | Rs. |
| 13. Financial assets at fair value through profit or loss | | |
| Securitized Papers (<i>Note 13.1</i>) | 340,532,947 | 291,005,977 |
| Debentures (<i>Note 13.2</i>) | 299,772,010 | 298,263,633 |
| Commercial Papers (<i>Note 13.3</i>) | 103,169,277 | - |
| | <u>743,474,234</u> | <u>589,269,610</u> |

13.1 Securitized papers

| Name of the Issuer | 31.03.2021 | | 31.03.2020 | |
|-----------------------------------|-------------------------------|---|-------------------------------|---|
| | Market value (Rs.) | Percentage exposure to each issuer against the Net Value of the Fund | Market value (Rs.) | Percentage exposure to each issuer against the Net Value of the Fund |
| Commercial Credit and Finance PLC | 122,504,824 | 13% | 106,166,613 | 13% |
| Prime Finance PLC | 94,200,450 | 10% | 80,554,779 | 10% |
| LOLC Development Finance PLC | 123,827,673 | 13% | 104,284,585 | 13% |
| Total | <u>340,532,947</u> | | <u>291,005,977</u> | |

13.2 Debentures

| Name of the Issuer | 31.03.2021 | | | 31.03.2020 | | |
|---------------------------|---------------------------------|-------------------------------|---|---------------------------------|-------------------------------|---|
| | Number of Debentures | Market value (Rs.) | Percentage exposure to each issuer against the Net Value of the Fund | Number of Debentures | Market value (Rs.) | Percentage exposure to each issuer against the Net Value of the Fund |
| Janashakthi Limited | 1,300,000 | 129,488,710 | 14% | 1,349,200 | 136,827,633 | 17% |
| Softlogic Capital PLC | 1,500,000 | 170,283,300 | 18% | 1,500,000 | 161,436,000 | 20% |
| Total | | <u>299,772,010</u> | | | <u>298,263,633</u> | |

All above investments as at 31 March 2021 and as at 31 March 2020 represent Credit rating of (BBB-) and above.

13.3 Commercial papers

| Name of the Issuer | 31.03.2021 | | 31.03.2020 | |
|---------------------------|-------------------------------|---|-------------------------------|---|
| | Market value (Rs.) | Percentage exposure to each issuer against the Net Value of the Fund | Market value (Rs.) | Percentage exposure to each issuer against the Net Value of the Fund |
| LOLC Holdings PLC | 103,169,277 | 11% | - | - |
| Total | <u>103,169,277</u> | | <u>-</u> | |

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| | 31.03.2021 | 31.03.2020 |
|--|--------------------|--------------------|
| | Rs. | Rs. |
| 14. Financial investments - at amortised cost | | |
| Government securities under resale agreements (<i>Note 14.1</i>) | 190,149,392 | 131,844,704 |
| Investments in fixed deposits (<i>Note 14.2</i>) | - | 104,340,340 |
| | 190,149,392 | 236,185,044 |

14.1 This represent investment in Resale agreements entirely backed by Government securities. No impairment provisions derived through these investments.

14.2 Investments in fixed deposits

| | 31.03.2021 | | 31.03.2020 | |
|--|-------------------|--|--------------------|--|
| | Value - Net | Percentage exposure to each issuer against the Net Value of the Fund | Value - Net | Percentage exposure to each issuer against the Net Value of the Fund |
| Merchant Bank of Sri Lanka & Finance PLC | - | | 104,340,340 | 13% |
| Total | - | | 104,340,340 | |

Above investment as at 31 March 2020 represent credit rating of (A-).

| | 31.03.2021 | 31.03.2020 |
|---|-------------------|--------------------|
| | Rs. | Rs. |
| 14.2.1 Investments in fixed deposits | - | 104,479,940 |
| Less :- Provision for impairment (<i>Note 14.3</i>) | - | (139,600) |
| | - | 104,340,340 |

14.3 Impairment of investment in fixed deposit as at 31 March 2021 represents " Stage 2" in accordance with SLFRS 9. Accordingly, individual impairment provision has been made for lifetime expected loss.

| | | |
|-----------------------------------|----------|----------------|
| Stage 1 - 12 months expected loss | - | - |
| Stage 2 - Lifetime expected loss | - | 139,600 |
| Total | - | 139,600 |

14.3.1. Movement in provision for expected credit loss

| | | |
|---------------------------------------|-----------|----------------|
| Balance as the beginning of the year | 139,600 | 130,895 |
| Provision/(Reversal) for the year | (139,600) | 8,705 |
| Balance at the end of the year | - | 139,600 |

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| | 31.03.2021 | 31.03.2020 |
|---|-------------------|-------------------|
| | Rs. | Rs. |
| 15. Taxes receivable | | |
| Balance at the beginning of the year | - | 1,945,002 |
| Provision for tax receivable | - | (1,945,002) |
| Balance at the end of the year | <u>-</u> | <u>-</u> |
| 16. Other receivable | | |
| Other receivable | 2,768,085 | 1,385,033 |
| Coupon interest receivable | 4,057,560 | - |
| | <u>6,825,645</u> | <u>1,385,033</u> |
| 17. Accrued expenses and other liabilities | | |
| Management fee payable | 397,505 | 671,770 |
| Trustee fee payable | 188,895 | 165,691 |
| Auditor's remuneration | 213,840 | 194,399 |
| Other payables | 423,413 | 411,422 |
| | <u>1,223,653</u> | <u>1,443,282</u> |
| 18. Net assets per unit | | |
| Net assets (Rs.) | 939,461,393 | 826,183,272 |
| Total number of units | 501,367 | 501,367 |
| Net assets per unit (Rs.) | <u>1,873.80</u> | <u>1,647.86</u> |

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19. Analysis of financial instrument by measurement basis

The following tables compare the fair values of the financial instruments with their carrying values.

| As at 31 March 2021 | Measured at Fair Value Rs. | Carried at Cost Rs. | Amortised Cost Rs. | Total Rs. |
|--|---|------------------------------------|-----------------------------------|----------------------|
| <u>Assets</u> | | | | |
| Cash at bank | - | - | 235,775 | 235,775 |
| Financial assets | | | | |
| Financial assets recognised through profit or loss | 743,474,234 | - | - | 743,474,234 |
| Financial assets - at amortised cost | - | - | 190,149,392 | 190,149,392 |
| Total | 743,474,234 | - | 190,385,167 | 933,859,401 |
| <u>Liabilities</u> | | | | |
| Accrued expenses and other liabilities | - | 1,223,653 | - | 1,223,653 |
| Total | - | 1,223,653 | - | 1,223,653 |
| | | | | |
| As at 31 March 2020 | Measured at Fair Value Rs. | Carried at Cost Rs. | Amortised Cost Rs. | Total Rs. |
| <u>Assets</u> | | | | |
| Cash at bank | - | - | 786,867 | 786,867 |
| Financial assets | | | | |
| Financial assets recognised through profit or loss - measured at fair value | 589,269,610 | - | - | 589,269,610 |
| Financial assets - at amortised cost | - | - | 236,185,044 | 236,185,044 |
| Total | 589,269,610 | - | 236,971,911 | 826,241,521 |
| <u>Liabilities</u> | | | | |
| Accrued expenses and other payables | - | 1,443,282 | - | 1,443,282 |
| Total | - | 1,443,282 | - | 1,443,282 |

20. Determining of fair value and hierarchy of fair value

The following tables show an analysis of financial instruments at fair value and by level of fair value hierarchy.

| As at 31 March 2021 | Level 1 Rs. | Level 2 Rs. | Level 3 Rs. | Total fair value Rs. |
|---|------------------------|------------------------|------------------------|-------------------------------------|
| Financial assets measured at fair value | | | | |
| Financial assets at fair value through profit or loss | | | | |
| - Investment in debentures | - | 299,772,010 | - | 299,772,010 |
| - Investment in securitized papers | - | 340,532,947 | - | 340,532,947 |
| - Investment in commercial papers | - | 103,169,277 | - | 103,169,277 |
| | - | 743,474,234 | - | 743,474,234 |
| | | | | |
| As at 31 March 2020 | Level 1 Rs. | Level 2 Rs. | Level 3 Rs. | Total fair value Rs. |
| Financial assets measured at fair value | | | | |
| Financial assets at fair value through profit or loss | | | | |
| - Investment in listed debentures | - | 298,263,633 | - | 298,263,633 |
| - Investment in treasury bills | - | 291,005,977 | - | 291,005,977 |
| | - | 589,269,610 | - | 589,269,610 |

Level 1 - Financial Instruments that are measured in whole or in part by reference to published quotes in an active market. A Financial Instrument is regarded as quoted in an active market if quoted prices are readily and regularly available from an exchange and those prices represent actual and regularly occurring market transactions on an arm's length basis.

Level 2 - Financial instruments that are measured at fair value on regular basis. As market quotes generally are not readily available or accessible for these securities, their fair value measures are determined using relevant information generated by the market transactions involving comparable securities.

Level 3 - Financial Instruments that are not supported by observable market prices information.

Due to the nature of short term maturity, carrying value of the financial assets at amortised cost are approximated to their fair value.

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20.1 Measurement of fair values

20.1 (1) Valuation techniques and significant unobservable inputs

The following table show the valuation techniques used in measuring Level 2 fair values, as well as the significant unobservable inputs used.

Financial instruments measured at fair value

| Type | Valuation technique | Significant Unobservable inputs |
|----------------------------------|---|---|
| Investment in Debenture | The valuation model is based on Yield Curve of the Government Securities. Yields relating to Government Securities based on the maturities of the respective debentures is interpolated in the valuation considering the initial risk premiums (at the time of issue) of the investee companies are constant as at the reporting date. | Risk premium of the investee companies (5.20% - 6.09%) |
| Investment in Securitized papers | The valuation model is based on Yield Curve of the Government Securities. Yields relating to Government Securities based on the maturities of the respective Securitized paper is interpolated in the valuation considering the initial risk premiums (at the time of issue) of the investee companies are constant as at the reporting date. | Risk premium of the investee companies (4.35% - 5.79%) |
| Investment in Commercial papers | The valuation model is based on Yield Curve of the Government Securities. Yields relating to Government Securities based on the maturities of the respective Securitized paper is interpolated in the valuation considering the initial risk premiums (at the time of issue) of the investee companies are constant as at the reporting date. | Risk premium of the investee companies (3.77%) |

20.1.1 (a) Sensitivity of the Market Yield on Financial Instruments measured at Fair Value is as follows.

| | (-) 0.5% Decrease (Effect in Rs.) | (+) 0.5% Increase (Effect in Rs.) |
|----------------------------------|---|--------------------------------------|
| Investment in Debentures | 3,729,860 | (3,889,620) |
| Investment in Securitized Papers | 1,781,204 | (1,779,471) |
| Investment in Commercial Papers | 300,694 | (305,044) |

Financial instruments for which fair value approximates carrying value

For financial assets and financial liabilities that have a short term maturity (original maturity less than a year), it is assumed that the carrying amount approximates their fair values. This assumption is also applied to lending without specific maturity or revolving nature.

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21. Financial risk management

Overview

The Unit Trust has exposure to the following risks via financial instruments.

- Market Risk
- Liquidity Risk
- Credit Risk
- Operational Risk

This Note presents information about the Unit Trust's exposure to each of the above risks and the objectives, policies and processes for measuring and managing risk.

21.1 Risk management framework

The Board of Directors of the fund manager has the overall responsibility for the establishment and oversight of the Unit Trust's risk management framework. The Managing Company has established an Enterprise Risk Management Committee (ERMC) of the fund manager which is tasked with reviewing wide-ranging risk categories that includes market, liquidity, credit and operational risk. The committee members have been assigned the responsibility to manage these risks prudently.

Unit Trust's risk management policies are established to identify and analyse the risk confronted by the Unit Trust, to set appropriate risk limits and controls and to monitor risk and adherence to limits. Risk management policies and systems are reviewed regularly to reflect changes in market conditions, products and services offered.

21.1(a) Market risk

Market risk is the risk that changes in market prices, such as interest rates will affect the Unit Trust's income or the value of its holdings of financial instruments. The objective of market risk management is to manage and control market risk exposures within acceptable parameters, while optimising the return on risk.

Management of market risk includes the following elements.

- Overall authority for managing market risk is vested with the Board of Directors of the fund manager.
- The operational authority for managing market risk is vested with the Investment Committee (IC) of the fund manager.
- Interest rate risk is managed within the approved limits by the Investment Committee of the fund manager.

21.1(b) Liquidity Risk

Liquidity risk is the risk that the Unit Trust will not have adequate financial resources to meet Unit Trusts' obligations as when they fall due. This risk arises from mismatches in the timing of cash flows.

Management of liquidity risk includes the following elements:

Taking steps to ensure, as far as possible, that it will always have adequate financial resources to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the Unit Trust's reputation.

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Maturity analysis of the financial assets and financial liabilities

| As at 31 March 2021 | Carrying amount Rs. | Up to 3 months Rs. | 3 Months to 1 year Rs. | 1-3 years Rs. | 3-5 years Rs. | Over 5 years Rs. |
|---|------------------------------------|-----------------------------------|---------------------------------------|--------------------------|--------------------------|-----------------------------|
| <u>Assets</u> | | | | | | |
| Cash at bank | 235,775 | 235,775 | - | - | - | - |
| Financial assets at fair value through profit or loss | 743,474,234 | - | 255,528,811 | 317,662,123 | 170,283,300 | - |
| Financial assets - at amortised cost | 190,149,392 | 190,149,392 | - | - | - | - |
| Total financial assets | 933,859,401 | 190,385,167 | 255,528,811 | 317,662,123 | 170,283,300 | - |

As at 31 March 2020

| | | | | | | |
|---|--------------------|--------------------|--------------------|--------------------|--------------------|----------|
| <u>Assets</u> | | | | | | |
| Cash at bank | 786,867 | 786,867 | - | - | - | - |
| Financial assets at fair value through profit or loss | 589,269,610 | - | 136,827,633 | 291,005,977 | 161,436,000 | - |
| Financial assets - at amortised cost | 236,185,044 | 131,844,704 | 104,340,340 | - | - | - |
| Total financial assets | 826,241,521 | 132,631,571 | 241,167,973 | 291,005,977 | 161,436,000 | - |

21.1(c) Credit Risk

Credit risk is the risk of financial loss to the Unit Trust if a client or counterparty to a financial instrument fails to meet its contractual obligations and arises principally from the Unit Trust's investment in corporate debt securities and investment in reverse repo agreements.

Management of credit risk includes the following components:

- Formulating credit policies in consultation with business units covering collateral requirements, credit assessment, risk grading and reporting, documentary and legal procedures and compliance with regulatory and statutory requirements.
- Establishing the authorisation structure for the approval and renewal of credit facilities.
- Limiting concentration of exposures to counterparties.
- Reviewing compliance through regular audits by internal audit.

Credit quality by class of financial assets

| As at 31 March 2021 | 12 Month Expected Credit Losses Rs. | Life Time Expected Credit Losses not credit impaired Rs. | Life Time Expected Credit Losses credit impaired Rs. | Total Rs. |
|--------------------------------------|--|---|---|----------------------|
| <u>Assets</u> | | | | |
| Cash at bank | 235,775 | - | - | 235,775 |
| Financial assets - at amortised cost | 190,149,392 | - | - | 190,149,392 |
| Total financial assets | 190,385,167 | - | - | 190,385,167 |

As at 31 March 2020

| As at 31 March 2020 | 12 Month Expected Credit Losses Rs. | Life Time Expected Credit Losses not credit impaired Rs. | Life Time Expected Credit Losses credit impaired Rs. | Total Rs. |
|--------------------------------------|--|---|---|----------------------|
| <u>Assets</u> | | | | |
| Cash at bank | 786,867 | - | - | 786,867 |
| Financial assets - at amortised cost | 236,185,044 | - | - | 236,185,044 |
| Total financial assets | 236,971,911 | - | - | 236,971,911 |

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Analysis of concentration risk

The following table shows the risk concentration by sector for the components of the Statement of Financial Position.

| As at 31 March 2021 | Cash at Bank | Financial assets recognised through profit or loss - measured at fair value | Financial assets - at amortised cost | Total Financial Assets |
|------------------------------|----------------|---|--|---------------------------|
| | Rs. | Rs. | Rs. | Rs. |
| <u>Sector wise breakdown</u> | | | | |
| Government | 235,775 | - | - | 235,775 |
| Corporate | - | 743,474,234 | 190,149,392 | 933,623,626 |
| Total | <u>235,775</u> | <u>743,474,234</u> | <u>190,149,392</u> | <u>933,859,401</u> |
| | | | | |
| As at 31 March 2020 | | | | |
| <u>Sector wise breakdown</u> | | | | |
| Government | 786,867 | - | - | 786,867 |
| Corporate | - | 589,269,610 | 236,185,044 | 825,454,654 |
| Total | <u>786,867</u> | <u>589,269,610</u> | <u>236,185,044</u> | <u>826,241,521</u> |

21.1 (d) Interest rate Risk

Interest rate risk is the risk that the value of a financial instrument will fluctuate as a result of changes in market interest rates.

The Fund's interest bearing financial assets expose it to risks associated with the effects of fluctuations in the prevailing levels of market interest rates on its financial position and cash flows. The risks is measured using sensitivity analysis. However, due to the short term nature of the, it is reasonably expected that the fluctuation in interest rate will not materially impact the net assets value of the fund.

The following table demonstrates the sensitivity of the statement of comprehensive income to reasonably possible changes in interest rates, with all other variables held constant.

| | Increase/(decrease) in basis points | Effect on the profit for the year ended 31.03.2021 (LKR) | Effect on the profit for the year ended 31.03.2020 (LKR) |
|-----------------------|--|--|--|
| Increased in interest | +0.5% | (5,974,135) | (5,691,622) |
| Decreased in interest | -0.5% | 5,811,758 | 5,790,873 |

FIRST CAPITAL FIXED INCOME FUND
NOTES TO THE FINANCIAL STATEMENTS
AS AT 31 MARCH 2021

21.1 (e) Operational Risk

Operational risk is the risk of direct or indirect loss arising from a wide variety of causes associated with the company's involvement with financial instruments, including processes, personnel, technology and infrastructure, and from external factors other than credit, market and liquidity risks such as those arising from legal and regulatory requirements and generally accepted standards of corporate behaviour.

The Unit Trust's objective is to manage operational risk so as to balance the avoidance of financial losses and damage to the business reputation with overall cost effectiveness and to avoid control procedures that restrict initiative and creativity.

The primary responsibility for the development and implementation of controls to address operational risk is assigned to senior management within each business unit. This responsibility is supported by the development of overall Unit Trust's standards for the management of operational risk in the following areas:

- Requirements for appropriate segregation of duties, including the independent authorisation of transactions
- Requirements for the reconciliation and monitoring of the transaction
- Compliance with regulatory and other legal requirements
- Documentation of controls and procedures.
- Development of business contingency plans
- Training and professional development
- Ethical and business standards.
- Risk mitigation, including insurance where this is effective

Compliance with Unit Trust's internal controls and procedures is supported by a programme of periodic reviews undertaken by Internal Audit. The results of internal audit reviews are discussed with the management of the business unit with summaries submitted to the Audit Committee of the Fund manager.

**FIRST CAPITAL FIXED INCOME FUND
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 MARCH 2021**

22. Related party disclosures

22.1 Directorships in other companies

The Directors of First Capital Asset Management Limited (Managing Company of the Unit Trust) and First Capital Holdings PLC (Parent Company of the Business Cluster) are also Directors of the following companies.

| Name of the company | Relationship | Mr. Nishan Fernando | Mr. Dinesh Schaffter | Mr. Dilshan Wirasekara | Mr. Eardley Perera | Ms. Minette Perera | Mr. Chandana Lal de Silva | Dr. Nishan de Mel | Mr. Prakash Schaffter | Mr. Ramesh Schaffter |
|---|-----------------------------------|---------------------|----------------------|------------------------|--------------------|--------------------|---------------------------|-------------------|-----------------------|-----------------------------|
| Janashakthi Limited | Ultimate Parent | - | Director | - | Director | - | Chairman | - | Deputy Chairman | Managing Director/Group CEO |
| Janashakthi Insurance PLC | Subsidiary of the Ultimate Parent | - | - | - | Director | - | - | - | Chairman | Director |
| Janashakthi Capital Limited | Subsidiary of the Ultimate Parent | - | - | - | - | - | - | - | Director | Director |
| Orient Finance PLC | Subsidiary of the Ultimate Parent | - | - | - | - | Director | - | - | Director | Director |
| Orient Capital Limited | Subsidiary of the Ultimate Parent | - | - | - | - | - | - | - | Director | Director |
| First Capital Limited | Immediate Parent | Chairman | Managing Director | Director/CEO | Director | Director | Director | Director | - | - |
| First Capital Treasuries PLC | Subsidiary of Immediate Parent | Chairman | Managing Director | Director/CEO | - | Director | Director | Director | Director | Director |
| First Capital Markets Limited | Subsidiary of Immediate Parent | Chairman | Managing Director | Director/CEO | Director | Director | Director | Director | - | - |
| First Capital Equities (Private) Limited | Subsidiary of Immediate Parent | Chairman | Managing Director | Director | Director | Director | Director | Director | - | - |
| First Capital Trustee Services | Subsidiary of Immediate Parent | - | Managing Director | Director/CEO | - | - | - | - | - | - |
| Kelsey Developments PLC | Subsidiary of the Ultimate Parent | - | Director | - | Chairman | - | Director | - | Director | Director |
| Kelsey Homes (Private) Limited | Subsidiary of the Ultimate Parent | - | Managing Director | - | Director | - | Director | - | - | - |
| K H L Corporate Services Limited | Subsidiary of the Ultimate Parent | - | Director | - | - | - | - | - | Director | Director |
| Kelsey Homes (Central Park) Limited (formerly Twid Capital (Private) Limited) | Subsidiary of the Ultimate Parent | - | Director | - | Director | - | Director | - | - | - |
| Premier Synthetic Leather Manufacturers (Private) Limited | Related party through KMP | - | Director | - | - | - | - | - | Director | Director |
| Thornton Engineering (Private) Limited | Related party through KMP | - | Director | - | - | - | Director | - | - | - |
| Nextventures Limited | Related party through KMP | - | Director | - | - | - | - | - | - | - |

First Capital Asset Management Limited manages licensed Unit Trusts namely First Capital Wealth Fund, First Capital Fixed Income Fund, First Capital Gilt Edged Fund, First Capital Money Market Fund and First Capital Equity Fund which are also treated as Related Parties of the Company.

The Fund carries out transactions with parties who are defined as related parties as per Sri Lanka Accounting Standard (LKAS 24), "Related Party Disclosure", in the ordinary course of its business. The details of such transactions are reported below. The pricing applicable to such transactions is based on the assessment of risk and pricing model of the Fund and is comparable with what is applied to transactions between the Fund and its unrelated customers. Related party transactions were made on terms equivalent to those that prevail in arm's length transactions.

**FIRST CAPITAL FIXED INCOME FUND
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 MARCH 2021**

22.2 Transaction with managing company

| Name of the company | Nature of the Transaction | Year ended 31.03.2021 | | Year ended 31.03.2020 | |
|--|---------------------------|-----------------------|---|-----------------------|---|
| | | 2020/21 | Amounts owed (to) / by the Related Party as at 31-03-2021 | 2019/20 | Amounts owed (to) / by the Related Party as at 31-03-2020 |
| First Capital Asset Management Limited | Management fee | 4,458,705 | (397,505) | 4,013,184 | (671,770) |
| | Bank deposit made | - | (60,158) | - | (60,158) |

22.3 Transaction with ultimate parent company/ parent company/ immediate parent company, subsidiaries of the immediate parent of the managing company

Nature of transaction

| | | | | |
|-------------------------------|-------------|---------------|------------|---------------|
| Interest income | 11,221,796 | - | 37,666,793 | - |
| Interest expense | 468.49 | - | - | - |
| Resale agreements | - | 190,149,392 | - | 131,844,705 |
| Investment in debentures | - | 129,488,710 | - | 136,827,633 |
| Investment in unit trust | - | (939,355,474) | - | (826,088,311) |
| Benefit accrued on Unit Trust | 113,267,163 | - | 85,842,407 | - |

22.4 Transactions with key management personnel (KMP) and their close family members (CFM)

According to Sri Lanka Accounting Standard LKAS 24 - "Related Party Disclosures", Key Management Personnel, are those having authority and responsibility for planning, directing and controlling the activities of the entity, directly or indirectly, including any director (whether executive or otherwise) of that entity. Accordingly, the Board of Directors has been classified as key management personnel of the entity.

Close Family Members of a Key Management Person are those family members who may be expected to influence, or be influenced by, that individual in their dealings with the Entity. They may include;

- a. The individual's domestic partner and children;
- b. Children of the individual's domestic partner; and
- c. Dependants of the Individual or the individual's domestic partner

Close Family Members are related parties to the Entity.

| Transactions with KMP/CFM | Year ended 31.03.2021 | | Year ended 31.03.2020 | |
|-------------------------------|-----------------------|---|-----------------------|---|
| | 2020/21 | Amounts owed (to) / by the Related Party as at 31-03-2021 | 2019/20 | Amounts owed (to) / by the Related Party as at 31-03-2020 |
| Investment in Unit Trust | - | (1,818) | - | (1,598) |
| Benefit accrued on Unit Trust | 220 | - | 164 | - |

**FIRST CAPITAL FIXED INCOME FUND
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 MARCH 2021**

23. Capital commitments and contingent liabilities

There were no material capital commitments and contingent liabilities as at the reporting date which require disclosure in the financial statements.

24. Events occurring after the reporting period

There were no material events after the reporting period, which require adjustments to or disclosures in the financial statements.

25. Impact on COVID-19 Pandemic

The World Health Organisation declared COVID 19 as a Global Pandemic situation on 11th March 2020. The pandemic significantly affected the Sri Lankan economy as well as the business environment. The situation is being continued effecting many aspects of the country. With the declaration of COVID 19 as a Global Pandemic situation and in response to the serious threat imposed on public health and safety, Sri Lankan Government enforced several measures to control the pandemic in March 2020.

The Country began to stabilise during the second half of year 2020 with lifting of lockdowns and gradual resurrection of business operations along with the consumer demand, that was lowered by the re-surge of 2nd wave of the pandemic occurred towards the end of year 2020. The Country has been going through another distress as a result of 3rd wave of COVID 19 since April 2021.

COVID-19 Pandemic had a low impact on the Company's general business routines. The Company followed the government guidelines and acted to ensure the safety of employees, stakeholder and business partners. The Company was equipped with a strong Business Continuity Plan. Accordingly, the Company was better prepared and equipped to face such contingent situations when the Government initially imposed curfew in March 2020. The Company had adequate infrastructure in place to face such emergency and therefore the impact on the business operations was minimal. The outbreak of COVID-19 does not have a significant impact on the performance, liquidity and valuation of assets of the Company.

FIRST CAPITAL FIXED INCOME FUND
RECONCILIATION OF NET ASSET VALUE REPORTED AS AT 31ST MARCH 2021

| | Rs. |
|--|--------------------|
| Net Asset Value as per Monthly Return | 939,471,159 |
| | |
| Adjustment on Under provision for Audit Fee | (9,766) |
| | |
| Net Asset Value as per Audited Financial Statements | 939,461,393 |

CORPORATE INFORMATION

NAME OF THE FUND (UNIT TRUST)

First Capital Fixed Income Fund

FUND MANAGING COMPANY

First Capital Asset Management Limited (PB 187)

TRUSTEE OF THE FUND

Bank of Ceylon

REGISTERED OFFICE OF FUND MANAGING COMPANY

No. 2, Deal Place
Colombo 3
Sri Lanka

BOARD OF DIRECTORS OF FUND MANAGING COMPANY

Mr. Nishan Fernando
Mr. Dinesh Schaffter
Mr. Dilshan Wirasekara
Mr. Eardley Perera
Ms. Minette Perera
Mr. Chandana de Silva
Dr. Nishan de Mel

SECRETARIES

K H L Corporate Services Limited
No. 15, Walukarama Road
Colombo 3

EXTERNAL AUDITORS

Messrs SJMS Associate (Deloitte)
Chartered Accountants
No. 11, Castle Lane
Colombo 4

INTERNAL AUDITORS

Messrs PricewaterhouseCoopers
Chartered Accountants
No. 100, Braybrooke Place
Colombo 2

PRINCIPAL BANKERS

Bank of Ceylon
Sampath bank