



Development Finance Ltd.

Management Discussion & Analysis

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Results and expectations

The results for 2006 were adversely affected by delays in realizations on major Impaired Loans and by diminution in the value of the investment in the Microfinance subsidiary by \$ 1.7 Million. Capital and Reserves grew by 7.4% to \$ 144 Million in 2006 (\$ 9.9 Million on 2005) thereby expanding our lending capability and providing a strong platform of financial soundness. Based on the core underlying performance going into 2007 and expected recoveries from major Impaired Loans, we expect a substantial increase in profitability boosted by growth in the loan portfolio and by income from the provision of financial services in 2007.

Role in the Caribbean

Development Finance Ltd (DFL) has been in existence for 35 years. The business environment in which the Company operates has evolved considerably over the years, especially in Trinidad and Tobago. Our home country now has an Investment Grade rating and is a major exporter of natural gas, petro-chemicals and oil. However, the purpose of the Company has remained the same. That has driven the Company to raise its standards as a licensed financial institution and to widen its scope of operations. The Company has also developed in step with the new economic environment envisaged in the Caribbean's vision of a Single Market and Economy.

DFL is now a regional development bank, a first-class financial institution serving the Southern and Eastern Caribbean.

The company's vision, core business and strategy

Over the years, the Company expanded through subsidiaries into Private equity, Management services and Microfinance. During 2006, its investment in those subsidiaries were transferred to DFL Caribbean Holdings Ltd. DFL is dedicated to lending to Small and Medium-sized Enterprises. Growth and diversification of the financial system, especially in the commercial banking industry, was expected to reduce the need for a large-scale, specialist lender to SME in the Caribbean. That view has since changed. Over the years, changes in the volume of DFL's loan portfolio, especially in the manufacturing and tourism sectors, have tended to be counter-cyclical reflecting economic cycles driven by commodity prices.

Now there is a more fundamental need caused by globalization processes. While globalization shortened the horizons of Caribbean investors in the last decade compared with earlier entrepreneurs, it has also encouraged a new spirit of entrepreneurship, a new generation.

Many firms in the manufacturing sector have to re-structure in order to orient their business in harmony with fundamental changes in market dynamics and supply lines. The Tourism sector in the Caribbean is being re-shaped by the ultra-wide and all-inclusive definition of "tourist". Developments in the Northern Caribbean, especially in the Turks and Caicos, and in Barbados have brought new investors and non-traditional services into the industry served adequately by real estate financing. Yet there are new opportunities for business. On the traditional side, many hotels remain under-capitalized and unable to

renew their product and up-grade plant. Agro-industry has not developed synergistically with the tourism industry but now has its importance viewed in the perspective of "food security". Services in all sectors must now rise to international standards and require different modes of organization and talent as well as financing. In small economies, involvement in these sectors once more represents a heightened level of risk for lenders. That puts DFL back in the same business as when it first started 35 years ago. However, it is a New Beginning and we have developed a new business model.

Key performance drivers and capabilities

The ability of DFL to carry out its Mission over the next three years, and achieve its financial objectives, will rest firmly on three fundamental strengths.

1. The Company has a strong operational and risk management framework that will support twice the current size of the Company while achieving a cost efficiency ratio of less than 55% with total assets of less than US\$ 100 Million
2. The Company has a sustainable international credit rating of BB that provides access to a wide range of financial markets and funding sources supported by a Capital Adequacy Ratio in excess of 20% using a risk weighting of 150 for SME loans.
3. The Company has a strong knowledge base of relevant experience and a wide network of contacts in the Southern and Eastern Caribbean

These fundamental strengths place DFL in a highly competitive, long term position that clearly defines its strategies. The Company is organized to scale up its operations as required by counter-cyclical demand. DFL can respond quickly and on the down-side, has a proven capability to manage impaired loans that are a likely outcome of its business. It has strongly demonstrated that capability in the last five years, especially in 2006. In other words, DFL is adequately equipped to be a regional development bank and its management is firmly focused on its role.

The risks that may affect the achievement of results

The significant risks that will always challenge the Company are described in Note 2 (Disclosure Notes) of the Notes to the Financial Statements in accordance with IFRS 7. In 2007, we expect that two factors, inflation and the sharp, sudden effects of World Cup Cricket, will create some economic disequilibrium in the Caribbean business environment. Secondly, rising operating costs will adversely affect the cost efficiency of financial institutions while a surge in the supply of external funding will tighten the lending market.

Therefore, changes in the region's financial system are inevitable, especially in the commercial banking sector. The confluence of events will have a positive impact on liquidity and likely effects on exchange rates and interest rates. That makes it even more difficult to speculate about consumer spending or the continuation of the construction boom around the Caribbean. We cannot forecast the demand for funding by SME but we are aware that there will be new opportunities that will challenge DFL's appraisal and financial structuring skills. Management also believes that once more, because of counter-cyclical demand, the volume of DFL's loan portfolio, and the risk inherent in its operations, will increase in 2007.

Responsibility for the Management Discussion and Analysis

The Board of Directors has reviewed the Discussion and Analysis prepared by Management, and the Independent Auditors have noted, but not audited, its contents. The oversight role of the Audit Committee and the Board provides a degree of assurance of relevance and reasonableness. However, it is Management's responsibility to present to the best of its ability, fair and balanced views based on the effectiveness of systems, controls and procedures that ensure that information used internally and disclosed externally is reliable.



Gerard Pemberton
Managing Director