Habib Bank AG Zurich
UAE Branches

Financial statements
31 December 2017

Habib Bank AG Zurich - UAE Branches

Financial statements
31 December 2017

Contents	***Page***

KPMG

KPMG Lower Gulf Limited
Level 13, Boulevard Plaza Tower One
Mohammed Bin Rashid Boulevard, Downtown Dubai, UAE
Tel. +971 (4) 403 0300, Fax +971 (4) 330 1515

Independent Auditors' Report

To the Chief Executive Officer of Habib Bank AG Zurich – UAE Branches

Report on the Audit of Financial Statements

Opinion

We have audited the financial statements of Habib Bank AG Zurich – UAE Branches ("the Bank"), which comprise the statement of financial position as at 31 December 2017, the statement of profit or loss and other comprehensive income, changes in head office capital & reserves and cash flows for the year then ended, and notes, comprising significant accounting policies and other explanatory information.

In our opinion, the accompanying financial statements present fairly, in all material respects, the financial position of the Bank as at 31 December 2017, and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards (IFRS).

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (ISAs). 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 Bank in accordance with the International Ethics Standards Board for Accountants' Code of Ethics for Professional Accountants (IESBA Code) together with the ethical requirements that are relevant to our audit of the financial statements in the United Arab Emirates, and we have fulfilled our other ethical responsibilities in accordance with the IESBA Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

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

Management is responsible for the preparation and fair presentation of the financial statements in accordance with IFRSs and their preparation in compliance with the applicable provisions of the UAE Federal Law No. (2) of 2015, and for such internal control as 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, management is responsible for assessing the Bank'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 management either intends to liquidate the Bank or to cease operations, or has no realistic alternative but to do so.

Those charged with Governance are responsible for overseeing the Bank'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 auditors' 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 ISAs 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 ISAs, we exercise professional judgment and maintain professional scepticism 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 Bank's internal control.

- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.

- Conclude on the appropriateness of management'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 Bank's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditors' 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 auditors' report. However, future events or conditions may cause the Bank 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

Further, as required by the UAE Union Law No (10) of 1980, as amended, we report that we have obtained all the information and explanations we considered necessary for the purposes of our audit.

KPMG Lower Gulf Limited

Vijendra Nath Malhotra
Registration Number: 48
Dubai, United Arab Emirates
Date: 28 MAR 2018

Habib Bank AG Zurich – UAE Branches

Statement of financial position
as at 31 December

	Note	**2017 AED 000**	2016 AED 000
ASSETS			
Cash and balances with UAE Central Bank	*4*	**2,685,446**	2,709,883
Due from banks	*5*	**3,932,281**	4,570,113
Due from related parties	*24*	**103,183**	116,375
Loans and Islamic financing receivables	*6*	**3,684,831**	3,643,097
Investments	*7*	**1,330,141**	842,569
Property and equipment	*8*	**56,220**	51,571
Customers' indebtedness for acceptances		**70,326**	62,940
Deferred tax assets	*9*	**41,067**	48,172
Other assets	*10*	**112,446**	91,589
Total assets		**12,015,941**	12,136,309
LIABILITIES			
Deposits from customers	*11*	**10,096,332**	10,380,895
Due to banks	*12*	**74,872**	10,475
Due to related parties	*24*	**49,190**	53,416
Liabilities under acceptances		**70,326**	62,940
Other liabilities	*13*	**250,492**	238,844
Total liabilities		**10,541,212**	10,743,570
CAPITAL AND RESERVES			
Allocated capital	*14*	**100,000**	100,000
Legal reserve	*15*	**50,000**	50,000
Retained earnings		**1,330,098**	1,245,853
Fair value reserve		**(5,369)**	(3,114)
Total capital and reserves		**1,474,729**	1,392,739
Total liabilities, capital and reserves		**12,015,941**	12,136,309
Contingent liabilities and other commitments	*16*	**677,598**	750,820

The notes on pages 8 to 62 form an integral part of these financial statements.

These financial statements were approved on 28 MAR 2018.

Chief Executive Officer

The independent auditors' report is set out on page 1 - 3.

Habib Bank AG Zurich – UAE Branches

Statement of profit or loss and other comprehensive income

for the year ended 31 December

	Note	**2017 AED 000**	2016 AED 000
Interest income and income from Islamic financing	*17*	**280,621**	278,726
Interest expense and distribution to Islamic depositors	*18*	**(26,518)**	(28,757)
Net interest income and income from Islamic financing		**254,103**	249,969
Fee and commission income (net)	*19*	**66,347**	71,853
Other income	*20*	**62,088**	60,895
Operating income		**382,538**	382,717
General and administrative expenses	*21*	**(231,936)**	(209,931)
Impairment allowance (net)	*6(c)*	**(42,054)**	(72,580)
Profit for the year before taxation		**108,548**	102,206
Taxation	*22*	**(24,303)**	(22,208)
Profit for the year after taxation		**84,245**	79,998
Other comprehensive income			
Available for sale investments – net change in fair value		**(2,255)**	(3,114)
Total comprehensive income for the year		**81,990**	76,884

The notes on pages 8 to 62 form an integral part of these financial statements.

The independent auditors' report is set out on page 1 - 3.

Habib Bank AG Zurich – UAE Branches

Statement of changes in Head Office capital and reserves
for the year ended 31 December

	Allocated Capital AED'000	Legal Reserve AED'000	Retained Earnings AED'000	Fair Value Reserve AED'000	Total AED'000
As at 1 January 2016	**100,000**	**50,000**	**1,165,855**	**-**	**1,315,855**
Profit for the year	-	-	79,998	-	79,998
Other comprehensive income	-	-	-	(3,114)	(3,114)
As at 31 December 2016	**100,000**	**50,000**	**1,245,853**	**(3,114)**	**1,392,739**
As at 1 January 2017	**100,000**	**50,000**	**1,245,853**	**(3,114)**	**1,392,739**
Profit for the year	-	-	84,245	-	84,245
Other comprehensive income	-	-	-	(2,255)	(2,255)
As at 31 December 2017	**100,000**	**50,000**	**1,330,098**	**(5,369)**	**1,474,729**

The notes on pages 8 to 62 form an integral part of these financial statements.

The independent auditors' report is set out on page 1 - 3.

Habib Bank AG Zurich – UAE Branches

Statement of cash flows

for the year ended 31 December

	Note	**2017** **AED 000**	2016 AED 000
Operating activities			
Profit for the year before taxation		**108,548**	102,206
Adjustments for:			
Impairment allowance on loans and Islamic financing receivables (net)		**38,600**	67,492
Impairment allowance on other assets (net)		**3,454**	5,088
Depreciation on property and equipment	*8*	**5,319**	4,682
Discount / Premium on Investments (net)		**11,992**	12,409
Loss on disposal of property and equipment		**153**	1
Operating profit before changes in net operating assets		**168,066**	191,878
Change in UAE Central Bank certificates of deposit with maturity over three months	*29*	**240,000**	(589,000)
Change in statutory reserve with UAE Central Bank	*29*	**(36,962)**	(93,521)
Change in bank placements with maturity over three months	*29*	**997,832**	(940,740)
Change in loans and Islamic financing receivables		**(80,334)**	(114,372)
Change in other assets		**(24,311)**	1,946
Change in deposits from customers		**(284,563)**	50,313
Change in other liabilities		**18,209**	27,088
		997,937	(1,466,408)
Income tax paid		**(20,759)**	(30,822)
Net cash generated/(used) in operating activities		**977,178**	(1,497,230)
Investing activities			
Purchase of property and equipment	*8*	**(10,124)**	(4,810)
Sale proceeds from disposal of property and equipment		**3**	-
Net proceeds from redemption of investments		**149,587**	264,921
Purchase of investments		**(651,406)**	(348,473)
Net cash used in investing activities		**(511,940)**	(88,362)
Balance at 1 January		**3,897,851**	5,483,443
Increase/(decrease) in cash and cash equivalents		**465,238**	(1,585,592)
Balance at 31 December	*29*	**4,363,089**	3,897,851

The notes on pages 8 to 62 form an integral part of these financial statements.

The independent auditors' report is set out on page 1 - 3.

1 Legal status and activities

Habib Bank AG Zurich, UAE Branches ("the Bank") operates in the Emirates of Abu Dhabi, Dubai and Sharjah under a full commercial banking license issued by the Central Bank of United Arab Emirates. The Head Office of the Bank is Habib Bank AG Zurich ("Head Office") incorporated in Switzerland. The registered address of the Bank is PO Box 3306, Dubai, United Arab Emirates.

These financial statements represent the combined financial position and results of the eight branches of the Bank in the United Arab Emirates.

The main activities of the Bank in the United Arab Emirates consist of providing retail, commercial and Islamic banking services.

2 Basis of preparation

(a) Statement of compliance

These financial statements have been prepared in accordance with the International Financial Reporting Standards ('IFRSs') and applicable provisions of UAE Federal law no. 2 of 2015.

(b) Basis of measurement

The financial statements have been prepared on the historical basis except for the following which are stated at fair value:

- Derivative financial instruments; and
- Available-for-sale financial instruments.

(c) Functional and presentation currency

These financial statements are presented in United Arab Emirates Dirhams ("AED") which is the Bank's functional and presentation currency. Except as otherwise indicated, financial information presented in AED has been rounded to the nearest thousand.

(d) Critical accounting estimates and judgments in applying accounting policies

Use of estimates and judgments

The preparation of the Bank's financial statements in conformity with IFRS requires management to make certain judgments, estimates and assumptions that affect the reported amount of financial assets and liabilities and the resultant allowances for impairment and fair values. In particular, considerable judgment by management is required in the estimation of the amount and timing of future cash flows and profits when determining the level of allowances required for impaired loans and Islamic financing receivables as well as deferred tax. Estimates and judgments are continually evaluated and are based on historical experience and other factors including expectations of future events that are believed to be reasonable under the circumstances.

2 Basis of preparation (continued)

(d) Critical accounting estimates and judgments in applying accounting policies (continued)

Use of estimates and judgments (continued)

Significant items where the use of estimates and judgments are required are outlined below:

(i) *Allowances for impairment of loans and Islamic financing receivables and Held to maturity (HTM) investments*

The Bank reviews its loan and Islamic financing portfolio to assess impairment on a regular basis. In determining whether an allowance for impairment should be recorded in the statement of profit or loss and other comprehensive income, the Bank makes judgments as to whether there is any observable data indicating that there is a measurable decrease in the contractual future cash flows from a loan or homogenous group of loans. The methodology and assumptions used for estimating both the amount and timing of future cash flows are reviewed regularly to reduce any differences between loss estimates and actual loss.

In addition to specific allowance against individually significant loans and Islamic financing receivables and HTM investments, the Bank also makes a collective impairment allowance to recognise that at any reporting date, there will be an amount of loans and Islamic financing receivables and HTM investments which are impaired even through a specific trigger point for recognition of the loss has not yet occurred (known as the "emergence period").

This collective allowance considers deterioration in the internal rating of the loan or investment since it was granted or acquired. These internal ratings take into consideration factors such as any deterioration in country risk, industry and technological obsolescence, as well as identified structural weaknesses or deterioration in cash flows.

(ii) *Fair value of derivatives and unquoted securities*

The fair values of financial assets that are not quoted in active markets are determined by using valuation techniques. Where valuation techniques (such as models) are used to determine fair values, these are tested before they are used and models are calibrated to ensure that outputs reflect actual data, and to the extent practicable, models use only observable data. However, areas such as credit risk (both own and counterparty), volatilities and correlations require management to make estimates. Changes in assumptions about these factors could affect reported fair value of financial assets.

(iii) *Income taxes/ Deferred tax asset*

The Bank is subject to income taxes in each of the three Emirates in the UAE that it operates in. There are certain transactions and calculations for which ultimate tax determination is uncertain during the ordinary course of business. The Bank recognises liabilities for anticipated tax audit issues based on estimates of whether additional taxes will be due. Where the final tax outcome of these matters is different from the amounts that were initially recorded, such differences will impact the income tax and deferred tax provisions in the period in which such determination is made.

2 Basis of preparation (continued)

(d) Critical accounting estimates and judgments in applying accounting policies (continued)

Use of estimates and judgments (continued)

(iv) *Classification of financial assets*

The classification and measurement of the financial assets depends on the Bank's business model for managing its financial assets and on the contractual cash flow characteristics of the financial assets assessed.

Financial assets that are measured at amortised cost are those assets that are held within a business model whose objective is to hold assets in order to collect contractual cash flows and the contractual terms give rise on specified dates to cash flows that are solely payments of principal and interest.

Financial assets that are measured at Available for sale are investments in quoted bonds that are not held to benefit from changes in their fair value and are not held for trading. The Bank believes that designating these instruments at Available for sale provides a more meaningful presentation of its medium to long-term interest in its investments than holding the investments at fair value through profit and loss.

Financial assets that are measured at Held to maturity are non-derivative financial assets with fixed or determinable payments and fixed maturity. In making this judgment, the Bank evaluates its intention and ability to hold such investment securities to maturity. In the event the Bank fails to keep these investments to maturity other than for specific circumstances, such as selling an insignificant amount close to maturity, it will be required to reclassify the entire class as available for sale and the Bank will be prevented from classifying investment securities as held-to-maturity for the current and the following two financial years unless one-off exempted circumstances.

(v) *Contingent liability arising from litigations*

Due to nature of its operations the Bank may be involved in litigation arising in the ordinary course of business. Provision for contingent liabilities arising from litigation is based on the probability of outflow of economic resources and reliability of estimating such outflow. Such matters are subject to many uncertainties and the outcome of individual matters is not predictable with assurance.

3 Significant accounting policies

The Bank has consistently applied the following accounting policies to all periods presented in these financial statements.

(a) Revenue recognition

Interest income and expense for all interest bearing financial instruments is recognised in the statement of profit or loss and other comprehensive income using the effective interest rate of the asset or liability or an applicable floating rate. The effective interest rate is the rate that exactly discounts the estimated future cash flows through the expected life of the financial asset or liability to the carrying amount of the financial asset or liability. The carrying amount of the financial asset or financial liability is adjusted if the Bank revises its estimates of payments or receipts. The adjusted carrying amount is calculated based on the original effective interest rate and the change in carrying amount is recorded as interest income or expense. Interest on impaired loans and Islamic financing receivables is recognised on their residual value using original effective interest rates.

Fee and commission income is accounted for on the accrual basis.

Recoveries in respect of loans that have been identified as fully impaired are accounted for on cash receipt basis.

(b) Financial instruments

(i) Recognition and measurement

Financial assets and liabilities are recognised when the Bank becomes a party to the contractual provisions of the instrument.

Financial assets and liabilities are initially measured at fair value. Transaction costs that are directly attributable to the acquisition or issue of financial assets and liabilities (other than financial assets and financial liabilities at fair value through profit or loss) are added to or deducted from the fair value of the financial assets or financial liabilities, as appropriate, on initial recognition. Transaction costs directly attributable to the acquisition of financial assets or financial liabilities at fair value through profit or loss are recognised immediately in the statement of profit or loss and other comprehensive income.

(ii) Classification

See accounting policies 3(d), 3(e) and 3(f).

(iii) Derecognition

The Bank derecognises a financial asset when the contractual rights to the cash flows from the financial asset expired, or when it transfers the rights to receive the contractual cash flows on the financial asset in a transaction in which substantially all the risks and the rewards of ownership of the financial asset are transferred. Any interest in transferred financial assets that is created or retained by the Bank is recognised as a separate asset or liability.

The Bank derecognises a financial liability when its contractual obligations are discharged or cancelled or expired.

The Bank writes off loans and Islamic financing receivables when they are determined to be uncollectible.

3 Significant accounting policies (continued)

(b) Financial instruments (continued)

(iv) Offsetting

Financial assets and liabilities are set off and the net amount presented in the statement of financial position when, and only when, the Bank has a legally enforceable right to set off the amounts and intends either to settle on a net basis or to realise the asset and settle the liability simultaneously.

Income and expenses are presented on a net basis only when permitted under IFRSs, or for gains and losses arising from a group of similar transactions.

(v) Amortised cost measurement

The amortised cost of a financial asset or liability is the amount at which the financial asset or liability is measured at initial recognition, minus principal repayments, plus or minus the cumulative amortisation using the effective interest method of any difference between the initial amount recognised and the maturity amount, minus any reduction for impairment.

(vi) Fair value measurement

'Fair value' is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date in the principal or, in its absence, the most advantageous market to which the Bank has access at that date. The fair value of a liability reflects its non-performance risk.

When available, the Bank measures the fair value of an instrument using the quoted price in an active market for that instrument. A market is regarded as active if transactions for the asset or liability take place with sufficient frequency and volume to provide pricing information on an ongoing basis.

The best evidence of the fair value of a financial instrument at initial recognition is normally the transaction price – i.e. the fair value of the consideration given or received. If the Bank determines that the fair value at initial recognition differs from the transaction price and the fair value is evidenced neither by a quoted price in an active market for an identical asset or liability nor based on a valuation technique that uses only data from observable markets, then the financial instrument is initially measured at fair value, adjusted to defer the difference between the fair value at initial recognition and the transaction price. Subsequently, that difference is recognised in profit or loss on an appropriate basis over the life of the instrument but no later than when the valuation is wholly supported by observable market data or the transaction is closed out.

If an asset or a liability measured at fair value has a bid price and an ask price, then the Bank measures assets and long positions at a bid price and liabilities and short positions at an ask price.

The fair value of a demand deposit is not less than the amount payable on demand, discounted from the first date on which the amount could be required to be paid.

3 Significant accounting policies (continued)

(b) Financial instruments (continued)

The Bank recognises transfers between levels of the fair value hierarchy as of the end of the reporting period during which the change has occurred.

Investments in unlisted funds and securities are fair valued internally by using valuation techniques. Where valuation techniques (such as models) are used to determine fair values these are tested before they are used and models are calibrated to ensure that outputs reflects actual data and comparative market prices.

(vii) Identification and measurement of impairment

Financial assets (including loans and Islamic financing receivables, held to maturity investments, balances due from banks and financial institutions, and balances with central banks and other assets) that are measured at amortised cost are assessed for impairment at each reporting date. Financial assets measured at amortised cost are considered to be impaired when there is objective evidence that, as a result of one or more events that occurred after the initial recognition of the financial assets, the estimated future cash flows of the asset have been affected.

Objective evidence of impairment includes, but not limited to:

- significant financial difficulty of the issuer or counterparty;
- breach of contract, such as a default or delinquency in profit or principal payments;
- it becoming probable that the customer will enter bankruptcy or financial re-organisation; or
- the disappearance of an active market for that financial asset because of financial difficulties.

The amount of the impairment loss recognised is the difference between the asset's carrying amount and the present value of estimated future cash flows reflecting the amount of collateral and guarantee, calculated using the financial asset's original effective interest rate.

The carrying amount of the financial asset measured at amortised cost is reduced by the impairment loss directly for all financial assets. Subsequent recoveries of amounts previously written off are credited against the impairment allowance account. Changes in the carrying amount of the impairment allowance account are recognised in the statement of profit or loss and other comprehensive income.

If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised, the previously recognised impairment loss is reversed through the statement of profit or loss and other comprehensive income to the extent that the carrying amount of the asset at the date the impairment is reversed does not exceed what the amortised cost would have been had the impairment not been recognised.

3 Significant accounting policies (continued)

(c) Cash and cash equivalents

Cash and cash equivalents consist of cash in hand and unrestricted cash balances with the UAE Central Bank, deposits and other balances due from/to banks, Head Office and other branches with original maturity of three months or less from the acquisition date, which are subject to insignificant credit risk, and are used by the Bank in the management of its short term commitments.

Cash and cash equivalents are carried at amortised cost.

(d) Derivatives

The Bank enters into derivative instruments which comprise forward foreign exchange contracts and interest rate swaps. Derivatives are stated at fair value. The fair value of a derivative is the equivalent of the unrealised gain or loss from marking to market the derivative using prevailing market rates or internal pricing models. Derivatives with positive market values (unrealised gains) are included in other assets and derivatives with negative market values (unrealised losses) are included in other liabilities in the statement of financial position.

(e) Loans and Islamic financing receivables

Loans and Islamic financing receivables are non-derivative financial asset with fixed or determinable payments that are not quoted in the active market. They arise when the Bank provides money, goods or services directly to a debtor with no intention of trading the receivable.

Loans and Islamic financing receivables are initially measured at fair value plus incremental direct transaction costs, and subsequently measured at their amortised cost using the effective interest method.

Murabaha

A contract whereby the Group (the "Seller") sells an asset to its customer (the "Purchaser"), on a deferred payment basis, after purchasing the asset and gaining possession thereof and title thereto, where the Seller has purchased and acquired that asset, based on a promise received from the Purchaser to buy the asset once purchased according to specific Murabaha terms and conditions. The Murabaha sale price comprises the cost of the asset and a pre-agreed profit amount. Murabaha profit is internally accounted for on a time-apportioned basis over the period of the contract based on the principal amount outstanding. The Murabaha sale price is paid by the Purchaser to the Seller on an instalment basis over the period of the Murabaha as stated in the contract.

(f) Investments

Investment securities are initially measured at fair value plus, in case of investment securities not at fair value through profit or loss, incremental direct transaction costs, and subsequently accounted for depending on their classification as either held to maturity, or available-for-sale.

3 Significant accounting policies (continued)

(f) Investments (continued)

(i) Held-to-maturity ("HTM")

HTM assets are non-derivative financial assets with fixed or determinable payments and fixed maturity that the Bank has the intent and ability to hold to maturity. These include certain debt instruments.

HTM investments are carried at amortised cost (less impairment, if any) using the effective interest method.

Sale of HTM investments is allowed only under the following circumstances:

- The investment is close enough to maturity as to have no impact on fair value;
- The principal is substantially received;
- Isolated events beyond the Bank's control;
- Significant credit deterioration; and
- Major business combination or disposal

(ii) Available for sale ("AFS")

These assets are initially measured at fair value plus any directly attributable transaction costs. Subsequent to initial recognition, they are measured at fair value and changes therein, other than impairment losses and foreign currency differences on debt instruments, are recognised in other comprehensive income and accumulated in the fair value reserve. When these assets are derecognised, the gain or loss accumulated in equity is reclassified to profit or loss.

(g) Foreign currencies

Foreign currency transactions are recorded at rates of exchange ruling at the value dates of the transactions. Monetary assets and liabilities denominated in foreign currencies are translated to UAE Dirhams at the exchange rates prevailing at the reporting date. Non-monetary assets and liabilities that are measured at fair value in a foreign currency are translated to UAE Dirhams at the exchange rates prevailing at the date of transaction. Non-monetary items that are measured based on historical cost in a foreign currency are not translated. Gains or losses are taken to the statement of profit or loss and other comprehensive income. Forward exchange contracts are valued at market rates applicable to the respective maturity.

(h) Income tax

Income tax expense comprises current and deferred tax. Income tax expense is recognised in the statement of profit or loss and other comprehensive income except to the extent that it relates to items recognised directly in equity, in which case it is recognised in equity.

Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantially enacted at the reporting date, and any adjustment to tax payable in respect of previous years.

Deferred tax is accounted for using the asset and liability method. Deferred tax assets and liabilities are recognised for the full tax consequences of all temporary differences between

3 Significant accounting policies (continued)

(h) Income tax (continued)

the financial statements carrying amounts of existing assets and liabilities and their respective tax bases. Recognition of deferred tax assets are, however, restricted to the extent that it is probable that sufficient taxable profits will be available against which the deductible temporary differences can be utilised. Deferred tax assets and liabilities are measured using tax rates that are expected to apply to the period in which the asset is expected to realise or the liability is expected to settle.

Deferred tax assets are reviewed at the end of each year to reduce the carrying amount by the extent to which it is no longer probable that sufficient taxable profits will be available to utilise the differences.

(i) Property and equipment and depreciation

Property and equipment are stated at cost less accumulated depreciation and impairment allowance, if any. Historical cost includes expenditure that is directly attributable to the acquisition of the items.

Subsequent costs are included in the asset's carrying amount or are recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Bank and the cost of the item can be measured reliably. All other repairs and maintenance are charged to the profit or loss during the financial period in which they are incurred.

Depreciation is charged for all property and equipment items (except land) at rates calculated to write off the cost of each asset over its expected useful life. Where the carrying value of the asset is greater than its estimated recoverable amount, it is written down immediately to its recoverable amount. Gains and losses on disposal are taken into account in determining net income.

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at each reporting date. The estimated useful lives for the various types of assets are as follows:

	Useful life
Building	25 years
Furniture and office equipment	4 to 7 years
Computer system	4 years
Motor vehicles	5 years

(j) Impairment of non-financial assets

The carrying amount of the Bank'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 indication exists, then the asset's recoverable amount is estimated.

An impairment loss is recognised if the carrying amount of an asset or its cash-generating unit exceeds its recoverable amount. A cash-generating unit is the smallest identifiable groups of assets that generates cash flows that largely are independent of the cash flows from other

3 Significant accounting policies (continued)

(j) Impairment of non-financial assets (continued)

assets or groups of assets. Impairment losses are recognised in the statement of profit or loss and other comprehensive income.

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. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset.

(k) Provisions

A provision is recognised if, as a result of a past event, the Bank 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. Provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and, where appropriate, the risks specific to the liability.

(l) Financial guarantees

Financial guarantees are contracts that require the Bank to make specified payments to reimburse the holder for a loss it incurs because a specified debtor fails to make payment when due in accordance with the terms of a debt instrument.

Financial guarantee liabilities are initially recognised at their fair value, and the initial fair value is amortised over the life of the financial guarantee. The guarantee liability is subsequently carried at the higher of this amortised amount and the present value of any expected payment (when a payment under the guarantee has become probable).

(m) Staff terminal benefits

The Bank provides for staff terminal benefits to its expatriate employees in accordance with UAE Labour Law. The entitlement to these benefits is based upon the employees' final salary and length of service, subject to the completion of a minimum service period. The expected costs of these benefits are accrued over the period of employment.

The Bank contributes to pension scheme for UAE nationals under the UAE pension and social security law. This is a defined contribution pension plan and Bank's contributions are charged to the statement of income in the period to which they relate. In respect of this scheme, the Bank has a legal or constructive obligation to pay the fixed contributions as they fall due and no obligations exist to pay the future benefits.

(n) Acceptances

Acceptances are recognised as financial liability in the consolidated statement of financial position with a contractual right of reimbursement from the customer as a financial asset. Therefore, commitments in respect of acceptances have been accounted for as financial assets and financial liabilities.

(o) Standards and interpretation adopted for accounting periods beginning on 1 January 2017

The Bank has adopted the following new standards and amendments to standards, including any consequential amendments to other standards, with a date of initial application of 1 January 2017. The changes did not have a material impact on the Bank's financial statements.

- Disclosure initiatives (Amendment to IAS 7)
- Annual improvements to IFRSs 2014-2016 cycle – various standards (Amendment to IFRS 12)

(p) New standards and interpretations not yet adopted

A number of new standards, amendments to standards and interpretations are effective for annual periods beginning after 1 January 2016 and earlier application is permitted, however the Bank has not adopted the following new or amended standards and have not applied these in preparing the financial statements.

IFRS 15	Revenue from Contracts with Customers	(effective 1 January 2018)
IFRS 9	Financial Instruments	(effective 1 January 2018)
IFRS 16	Leases	(effective 1 January 2018)

IFRS 15 Revenue from Contracts with Customers

On 28 May 2014, the IASB issued IFRS 15 Revenue from Contracts with Customers, which replaces the previous revenue standard IAS 18 Revenue, and the related Interpretations on revenue recognition. The standard is a control-based model as compared to the existing revenue standard which is primarily focused on risks and rewards, and provides a single principle based framework to be applied to all contracts with customers that are in scope of the standard. Under the new standard, revenue is recognized when a customer obtains control of a good or service. Transfer of control occurs when the customer has the ability to direct the use of, and obtain the benefits of the good or service. The standard introduces a new five step model to recognize revenue as performance obligations in a contract are satisfied. The standard scopes out contracts that are considered to be lease contracts, insurance contracts and financial instruments, and as such will impact the businesses that earn fee and commission revenue.

On 12 April, 2016, the IASB issued amendments to IFRS 15 Revenue from Contracts with Customers. The amendments provide additional clarification on the identification of a performance obligation in a contract, determining the principal and agent in an agreement, and determining whether licensing revenues should be recognized at a point in time or over a specific period. The amendments also provide additional practical expedients that can be used on transition to the standard.

The Bank will adopt the standard and its amendments as of 1 January 2018 and plans to use the modified retrospective approach. Under this approach, the Bank will recognize the cumulative effect of initially applying the standard as an adjustment to the opening balances of retained earnings as of 1 January 2018, without restating comparative periods. Additional disclosures will be required in order to explain any significant changes between reported results and results had the previous revenue standard been applied.

3 Significant accounting policies (continued)

(p) New standards and interpretations not yet adopted (continued)

The standard does not apply to revenue associated with financial instruments, and therefore, will not impact the majority of the Bank's revenue, including interest income, interest expense, trading revenue and securities gains which are covered under IFRS 9 Financial Instruments. The implementation of the standard is being led by Credit and Finance Department in coordination with the business segments. The areas of focus for the Bank's assessment of impact are fees and commission income. The Bank has been working to identify and review the customer contracts within the scope of the new standard. While the assessment is not complete, the timing of the Bank's revenue recognition of fees and commissions within the scope of this standard is not expected to materially change. The Bank is also evaluating the additional disclosures that may be relevant and required.

IFRS 9 Financial Instruments

IFRS 9 was issued in July 2014 and has an effective date of 1 January 2018. In October 2017, the IASB published an amendment to IFRS 9, Prepayment Features with Negative Compensation, which is effective from 1 January 2019, with earlier application permitted.

IFRS 9 replaces IAS 39 Financial Instruments: Recognition and Measurement, introducing new requirements for the classification and measurement of financial instruments, the recognition and measurement of credit impairment provisions, and providing for a simplified approach to hedge accounting. The Bank has elected to continue hedge accounting in line with the IAS 39 requirements and has not therefore applied the IFRS 9 hedging requirements. The Bank will, however, adopt these revised disclosures set out in IFRS 7, which includes those relating to hedge accounting. The changes in measurement arising on initial application of IFRS 9 will be incorporated through an adjustment to the opening reserves and retained earnings position as at 1 January 2018.

Although IFRS 9 will be retrospectively applied, the Bank is only permitted to restate comparatives if, and only if, it is possible without the use of hindsight. The Bank does not consider it possible to restate comparatives for impairment without the use of hindsight.

Classification and measurement of financial instruments

There are three measurement classifications under IFRS 9: amortised cost, fair value through profit or loss (FVTPL) and, for financial assets, fair value through other comprehensive income (FVOCI). The existing IAS 39 financial asset categories are replaced by the new categories under IFRS 9. Financial assets are classified into these categories based on the business model within which they are held, and their contractual cash flow characteristics. The business model reflects how groups of financial assets are managed to achieve a particular business objective. Financial assets can only be held at amortised cost if the instruments are held in order to collect the contractual cash flows ('hold to collect'), and where those contractual cash flows are solely payments of principal and interest (SPPI). Principal represents the fair value of the instrument at the time of initial recognition.

Interest in this context represents compensation for the time value of money and associated credit risks together with compensation for other risks and costs consistent with a basic lending arrangement and a profit margin. This requires an assessment at initial recognition of the contractual terms to determine whether it contains a term that could change the timing or amount of cash flows in a way that is inconsistent with the SPPI criteria. Assets may be sold

3 Significant accounting policies (continued)

(p) New standards and interpretations not yet adopted (continued)

out of 'hold to collect' portfolios where there is an increase in credit risk. Disposals for other reasons are permitted but such sales should be insignificant in value or infrequent in nature.

Financial asset debt instruments where the business model objectives are achieved by collecting the contractual cash flows and by selling the assets ('hold to collect and sell') and that have SPPI cash flows are held at FVOCI, with unrealised gains or losses deferred in reserves until the asset is derecognised. In certain circumstances, non-trading equity instruments can be irrevocably designated as FVOCI but both unrealised and realised gains or losses are recognised in reserves and no amounts other than dividends received are recognised in the income statement. All other financial assets will mandatorily be held at FVTPL. Financial assets may be designated at FVTPL only if doing so eliminates or reduces an accounting mismatch.

There has been no change to the requirements in respect of the classification and measurement of financial liabilities. The derecognition requirements have also been carried forward unchanged from IAS 39.

Impairment

The adoption of IFRS 9 will have a significant impact on the Bank's impairment methodology. The IFRS 9 expected credit loss (ECL) model is forward looking compared to the current incurred loss approach. Expected credit losses reflect the present value of all cash shortfalls related to default events either (i) over the following twelve months or (ii) over the expected life of a financial instrument depending on credit deterioration from inception. ECL should reflect an unbiased, probability-weighted outcome as opposed to the single best estimate allowed under the current approach. The probability-weighted outcome considers multiple scenarios based on reasonable and supportable forecasts.

IFRS 9 Impairment model uses a three stage approach based on the extent of credit deterioration since origination:

Stage 1 – 12-month ECL applies to all financial assets that have not experienced a significant increase in credit risk (SICR) since origination and are not credit impaired. The ECL will be computed using a 12-month PD that represents the probability of default occurring over the next 12 months. For those assets with a remaining maturity of less than 12 months, a PD is used that corresponds to remaining maturity. This Stage 1 approach is different than the current approach which estimates a collective allowance to recognize losses that have been incurred but not reported on performing loans.

Stage 2 – When a financial asset experiences a SICR subsequent to origination but is not credit impaired, it is considered to be in Stage 2. This requires the computation of ECL based on lifetime PD that represents the probability of default occurring over the remaining estimated life of the financial asset. Provisions are higher in this stage because of an increase in risk and the impact of a longer time horizon being considered compared to 12 months in Stage 1.

Stage 3 – Financial assets that have an objective evidence of impairment will be included in this stage. Similar to Stage 2, the allowance for credit losses will continue to capture the lifetime expected credit losses.

3 Significant accounting policies (continued)

(p) New standards and interpretations not yet adopted (continued)

Some of the key concepts in IFRS 9 that have the most significant impact and require a high level of judgement are:

Assessment of Significant Increase in Credit Risk

The assessment of a significant increase in credit risk is done on a relative basis. To assess whether the credit risk on a financial asset has increased significantly since origination, the Bank mainly compares the risk of default occurring over the expected life of the financial asset at the reporting date to the corresponding risk of default at origination, using key risk indicators that are used in the Bank's existing risk management processes and forward looking information. At each reporting date, the assessment of a change in credit risk will be individually assessed for those considered individually significant. This assessment is symmetrical in nature, allowing credit risk of financial assets to move back to Stage 1 if the increase in credit risk since origination has reduced and is no longer deemed to be significant.

Macroeconomic Factors, Forward Looking Information (FLI) and Multiple Scenarios

IFRS 9 requires an unbiased and probability weighted estimate of credit losses by evaluating a range of possible outcomes that incorporates forecasts of future economic conditions.

Macroeconomic factors and FLI are required to be incorporated into the measurement of ECL as well as the determination of whether there has been a significant increase in credit risk since origination. Measurement of ECLs at each reporting period should reflect reasonable and supportable information at the reporting date about past events, current conditions and forecasts of future economic conditions.

The Bank will use three scenarios that will be probability weighted to determine ECL, leveraging its existing Enterprise Wide Stress Test modeling framework.

Experience Credit Judgment

The Bank's ECL allowance methodology, requires the Bank to use its experienced credit judgement to incorporate the estimated impact of factors not captured in the modelled ECL results, in all reporting periods.

Expected Life

When measuring ECL, the Bank must consider the maximum contractual period over which the Bank is exposed to credit risk. All contractual terms should be considered when determining the expected life, including prepayment options and extension and rollover options. For certain revolving credit facilities that do not have a fixed maturity, the expected life is estimated based on the period over which the Bank is exposed to credit risk and where the credit losses would not be mitigated by management actions.

Definition of Default and Write-off

Under IFRS 9, the Bank considers a financial asset to be in default when:

- the borrower is unlikely to pay its credit obligations to the Bank in full, without recourse by the Bank to actions such as realising security (if any is held);
- the borrower is past due more than 89 days on any credit obligation to the Bank; or

3 Significant accounting policies (continued)

(p) New standards and interpretations not yet adopted (continued)

- cross product default resulting in provision against other product holdings for the customer.

The Bank does not expect to rebut the presumption in IFRS 9 that loans which are 90 days past due are in default for retail loans. For Non-Retail loans, 90 days past due is generally used as the default definition with any exceptional cases being approved via Risk Management keeping in view on-going discussions with customer regarding payments/restructuring. The policy on the write-off of loans remains unchanged.

Transition impact

The Bank will record an adjustment to its opening retained earnings as at 1 January 2018, to reflect the application of the new requirements of Impairment and will not restate comparative period.

The Bank's current estimate of the impact of IFRS 9 transition indicates a reduction of net shareholders' equity by 8% to 10% as at 1 January 2018. The estimated impact relates primarily to the implementation of the ECL requirements. The Bank continues to revise, refine and validate the impairment models and related process controls leading up to the 31 March 2018 reporting date. Accordingly, the actual impact of adopting the standard at 1 January 2018 may change.

IFRS 16 Leases

IFRS 16 introduces a single lessee accounting model and requires a lessee to recognise assets and liabilities for all leases with a term of more than 12 months, unless the underlying asset is of low value. A lessee is required to recognise a right-of-use asset representing its right to use the underlying leased asset and a lease liability representing its obligation to make lease payments. IFRS 16 substantially carries forward the lessor accounting requirements in IAS 17 Leases. Accordingly, a lessor continues to classify its leases as operating leases or finance leases, and to account for those two types of leases differently. The impact of the standard is currently being assessed and it is not yet practicable to quantify the effect of IFRS 16 on these financial statements. The Bank will have a balance sheet increase in lease liabilities and right-of-use assets on adoption of IFRS 16.

4 Cash and balances with UAE Central Bank

	2017 AED 000	2016 AED 000
Cash in hand	**69,973**	56,667
Balances with UAE Central Bank:		
- Certificates of deposit	**1,120,000**	1,350,000
- Clearing account	**300,952**	310,657
- Statutory reserve	**1,029,521**	992,559
- Islamic deposits	**165,000**	-
	2,685,446	2,709,883

The statutory reserve represents mandatory interest free reserve deposits, which are not available to finance the Bank's day to day operations.

5 Due from banks

	2017 AED 000	2016 AED 000
Time	**3,504,158**	3,985,652
Demand	**428,123**	584,461
	3,932,281	4,570,113

6 Loans and Islamic financing receivables

(a) The composition of the loans and Islamic financing receivables portfolio is as follows:

	2017			2016		
	UAE AED 000	**Others AED 000**	**Total AED 000**	UAE AED 000	Others AED 000	Total AED 000
Trade	**1,043,573**	**-**	**1,043,573**	1,076,458	-	1,076,458
Other commercial & business sector	**1,890,520**	**41,227**	**1,931,747**	1,749,338	26,781	1,776,119
Personal	**919,447**	**14,933**	**934,380**	1,021,772	30,683	1,052,455
Gross receivables – net of Interest in suspense	**3,853,540**	**56,160**	**3,909,700**	3,847,568	57,464	3,905,032
Allowance for impairment						
- Specific			**(112,742)**			(176,292)
- Collective			**(112,127)**			(85,643)
Net receivables			**3,684,831**			3,643,097

Loans and Islamic financing receivables include Murabaha financing activities amounting to AED 0.10 million (*2016: Nil*) provided through a Shari'a compliant Islamic window.

(b) The movement in allowance for impairment on loans and Islamic financing receivables is as follows:

	2017			2016		
	Specific AED 000	**Collective AED 000**	**Total AED 000**	Specific AED 000	Collective AED 000	Total AED 000
As at 1 January	**176,292**	**85,643**	**261,935**	112,840	102,672	215,512
Amount written off	**(75,666)**	**-**	**(75,666)**	(21,069)	-	(21,069)
Charge/ (releases) during the year	**12,116**	**26,484**	**38,600**	84,521	(17,029)	67,492
Impairment allowance	**112,742**	**112,127**	**224,869**	176,292	85,643	261,935

6 Loans and Islamic financing receivables (continued)

(c) The charge to the statement of profit or loss and other comprehensive income for impairment allowance consists of the following:

	2017	2016
	AED 000	AED 000
Net specific allowance for impairment on loans and Islamic financing receivables	**12,116**	84,521
Net collective allowance for impairment on loans and Islamic financing receivables	**26,484**	(17,029)
Total allowance for impairment on loans and Islamic financing receivables	**38,600**	67,492
Allowance for impairment on other assets (Note 10)	**3,454**	5,088
Total allowance for impairment for the year	**42,054**	72,580

7 Investments

	2017	2016
	AED 000	AED 000
Available for sale investments		
Investments in un-listed equities	**1,197**	1,283
Bond – Quoted (refer note 7a) *	**1,105,511**	642,998
Held to maturity		
Bond – Quoted *	**223,433**	198,288
Total investments	**1,330,141**	842,569

* The above investments include bonds guaranteed by the Government of Dubai, other corporates including international banks and financial institutions, denominated in USD and UAE Dirhams.

Income from investment taken to the statement of profit or loss and other comprehensive income is as follows:

	2017	2016
	AED 000	AED 000
Interest income and Income from Islamic financing (Note 17)	**26,044**	21,563
Other income		
Realised gain on Investment securities designated as fair value through profit & loss	535	138
	535	138

7 Investments (continued)

(a) Available for sale investments

The table below sets out the investment securities at their carrying and fair values:

Bond – Quoted

	2017 AED 000	2016 AED 000
Opening balance	**642,998**	-
Transferred from HTM	-	583,549
Acquired during the year	**605,735**	121,772
Redeemed during the year	**(131,222)**	(48,214)
Amortisation of premium	**(9,745)**	(10,995)
Fair Value movement	**(2,255)**	(3,114)
Available for sale investment	**1,105,511**	642,998

8 Property and equipment

	Building	Furniture and office equipment	Computer system	Motor vehicles	Total
	AED 000	AED 000	AED 000	AED 000	AED 000
Cost					
At 1 January 2016	52,184	25,998	11,961	6,265	96,408
Additions	-	3,650	130	1,030	4,810
Disposals and write-offs	-	(539)	(377)	(360)	(1,276)
At 31 December 2016	**52,184**	**29,109**	**11,714**	**6,935**	**99,942**
At 1 January 2017	52,184	29,109	11,714	6,935	99,942
Additions	-	5,536	3,164	1,424	10,124
Disposals and write-offs	-	(1,353)	(164)	(626)	(2,143)
At 31 December 2017	**52,184**	**33,292**	**14,714**	**7,733**	**107,923**
Accumulated depreciation					
At 1 January 2016	8,502	20,696	11,558	4,208	44,964
Charge for the year	2,122	1,391	226	943	4,682
Disposals and write-offs	-	(538)	(377)	(360)	(1,275)
At 31 December 2016	**10,624**	**21,549**	**11,407**	**4,791**	**48,371**
At 1 January 2017	10,624	21,549	11,407	4,791	48,371
Charge for the year	2,122	1,376	946	875	5,319
Disposals and write-offs	-	(1,198)	(163)	(626)	(1,987)
At 31 December 2017	**12,746**	**21,727**	**12,190**	**5,040**	**51,703**
Net book value					
At 31 December 2017	**39,438**	**11,565**	**2,524**	**2,693**	**56,220**
At 31 December 2016	**41,560**	**7,560**	**307**	**2,144**	**51,571**

9 Deferred tax assets

Deferred tax assets are attributable to the following:

	2017 AED 000	2016 AED 000
Allowances for impairment	**41,067**	48,018
Others	**-**	154
	41,067	48,172

Movements in temporary differences during the year are as follows:

	Opening Balance AED 000	Recognised in statement of profit or loss and other comprehensive income AED 000	Recognised in equity AED 000	Closing Balance AED 000
2017				
Allowances for impairment	**48,018**	**(6,951)**	**-**	**41,067**
Others	**154**	**(154)**	**-**	**-**
	48,172	**(7,105)**	**-**	**41,067**
2016				
Allowances for impairment	39,314	8,704	-	48,018
Others	244	(90)	-	154
	39,558	8,614	-	48,172

10 Other assets

	2017 AED 000	2016 AED 000
Accrued interest / profit	**34,770**	27,182
Prepayments and deposits	**47,010**	37,658
Precious metal	**3,387**	633
Positive fair value of derivatives (refer note 23)	**-**	-
Custodian collection	**23,718**	26,116
Others	**3,561**	-
	112,446	91,589

Prepayments include operating lease of AED 28.4 million (2016: AED 30 million) pertaining to the Zonal Head Office to be amortised over the remaining life of 22 years.

10 Other assets (continued)

Other assets consists of assets acquired in settlement of debt which have been fully impaired. The additional assets acquired in settlement of debt during 2017 amounted to AED 3.45 million. The total assets acquired in settlement of debt as at year ended 31 December 2017 were AED 16.91 million (2016: AED 13.45 million) and the impairment allowance on these was AED 16.91 million (2016: AED 13.45 million).

11 Deposits from customers

	2017 AED 000	2016 AED 000
Business accounts		
Demand deposits	**3,321,276**	3,271,166
Time deposits	**848,921**	881,092
Call deposits	**757,232**	788,040
Savings deposits	**147,286**	185,054
Margin deposits	**116,551**	135,431
	5,191,266	5,260,783
Individual customers		
Demand deposits	**1,557,399**	1,416,446
Time deposits	**2,131,308**	2,418,706
Call deposits	**293,230**	230,364
Savings deposits	**922,693**	1,052,098
Margin deposits	**436**	2,498
	4,905,066	5,120,112
Total	**10,096,332**	10,380,895

Deposits from customers include Islamic customer deposits amounting to AED 161.6 million (*2016: Nil*) undertaken through a Sharia'a compliant Islamic window.

12 Due to banks

	2017 AED 000	2016 AED 000
Demand deposits	**74,872**	10,475
	74,872	10,475

The average interest rate paid on the above was Nil (*2016: Nil*)

13 Other liabilities

	2017 AED 000	2016 AED 000
Accrued interest and Islamic profit payable	**22,813**	22,630
Staff terminal benefits	**32,330**	32,843
Accrued expenses payable	**3,253**	2,433
Tax payable	**20,587**	30,822
Bills payable	**102,695**	122,343
Negative fair value of derivatives (refer note 23)	**-**	-
Others	**68,814**	24,773
	250,492	235,844

14 Allocated capital

In accordance with article 80 of the Union Law No. 10 of 1980 as amended, the allocated capital represents the deposit of AED 100 million contributed by Head Office as assigned capital for the UAE branches.

15 Legal reserve

In accordance with article 82 of the Union Law No. 10 of 1980 as amended, 10% of the net profit for the year should be transferred to a non-distributable legal reserve, until such time as this reserve equals 50% of the allocated capital.

16 Contingent liabilities and other commitments

The contractual amounts of the Bank's off-balance sheet financial instruments that commit it to extend credit to customers are as follows:

	2017 AED 000	2016 AED 000
a) Direct credit substitutes including general guarantees of indebtedness and standby letters of credit serving as financial guarantees for loans and securities	**210,233**	201,975
b) Transaction-related contingencies including performance bonds, bid bonds and standby letters of credit related to particular transactions	**199,365**	227,371
c) Short-term self-liquidating trade-related contingencies arising from the movement of goods, such as documentary credits where the underlying shipment is used as security	**268,000**	321,474
	677,598	750,820

17 Interest income and Income from Islamic Financing

	2017 AED 000	2016 AED 000
Loans and Islamic financing receivables	**194,658**	216,885
Certificates of Deposits with U.A.E. Central Bank	**11,701**	6,435
Due from related parties	**538**	790
Due from banks	**47,680**	33,053
Investment securities	**26,044**	21,563
	280,621	278,726

This includes income from Islamic activities amounting to AED 2.3 million (*2016: Nil*) for the year ended 31 December 2017.

18 Interest expense and distribution to Islamic depositors

	2017 AED 000	2016 AED 000
Due to banks	**28**	33
Deposits from customers	**26,390**	23,719
Due to related parties	**100**	5
	26,518	28,757

This includes distribution to Islamic depositors amounting to AED 0.19 million (*2016: Nil*) for the year ended 31 December 2017.

19 Fee and commission income (net)

	2017 AED 000	2016 AED 000
Fee and commission income	**69,654**	75,162
Fee and commission expense	**(3,307)**	(3,309)
	66,347	71,853

20 Other income

	2017 AED 000	2016 AED 000
Foreign exchange income	**28,877**	28,245
Telex charges recovery	**18,134**	17,966
Courier charges recovery	**5,189**	5,147
Insurance charges recovery	**775**	782
Other miscellaneous income	**9,113**	8,755
	62,088	60,895

21 General and administrative expenses

	2017 AED 000	2016 AED 000
Staff salaries and benefits	**99,173**	86,097
Depreciation	**5,319**	4,682
Telephone, telex and courier expenses	**7,069**	6,638
Head office charges	**21,418**	20,819
Office rent	**15,973**	12,178
Repairs and maintenance expenses	**5,259**	4,363
Printing and stationery	**1,552**	1,304
Insurance and travel	**2,999**	3,477
(Recovery) / charge for operational losses	**(514)**	847
Other miscellaneous expenses (including expenses reimbursed to a related party- refer note 24)	**73,688**	67,526
	231,936	207,931

The total numbers of employees as at 31 December 2017 were 336 (2016: 306) of which 122 (2016: 117) were UAE Nationals.

22 Taxation

Provision is made for tax in the Emirates of Abu Dhabi, Dubai (except for Jebel Ali which is a tax free zone) and Sharjah in accordance with the respective tax legislation in these Emirates. Tax expense for the year comprises:

	2017 AED 000	2016 AED 000
Current tax expense	**17,026**	30,822
Additional tax paid for previous year	172	-
Deferred tax expense		
- Reversal / (origination) of temporary differences	**7,105**	(8,614)
Total taxation	**24,303**	22,208

The Bank recognises deferred tax asset/liability for all deductible temporary differences to the extent that it is probable that future taxable profit will be available against which the deductible temporary difference can be utilised.

Reconciliation of effective tax rate:

	2017 AED 000	2016 AED 000
Profit for the year before taxation	**108,548**	102,206
Tax calculated using UAE tax rates (20%)	**21,710**	20,441
Prior year tax	**-**	-
Tax exempt income	**(1,470)**	(1,764)
Non-deductible expenses	**4,063**	3,531
Total tax expense	**24,303**	22,208
Effective tax rate	**22.39%**	21.73%

23 Derivatives

Derivative product types

Forwards are contractual agreements to either buy or sell a specified currency, commodity or financial instrument at a specific price and date in the future. Forwards are customised contracts transacted in the over-the-counter market.

Derivative related credit risk

Credit risk in respect of derivative financial instruments arises from the potential for a counter party to default on its contractual obligations and is limited to the positive fair value of instruments that are favourable to the Bank.

24 Related party transactions

In the case of the Bank, related parties, as defined under the International Accounting Standard 24, include Head Office, branches abroad, subsidiaries and associates of Habib Bank AG Zurich outside the United Arab Emirates.

In the normal course of business, the Bank enters into various transactions with related parties. The Bank's management believes that all such transactions with related parties are carried out on mutually agreed terms.

Key management personnel are those persons, having authority and responsibility for planning, directing and controlling the activities of the Bank, directly or indirectly.

The balances and income/expense arising from transactions with Head Office, branches abroad and subsidiaries are set out below:

	2017 **AED 000**	2016 AED 000
Due from		
- Head office	**23,827**	27,559
- Branches (other than UAE)	**-**	3,653
- Subsidiaries of the Habib Group	**79,356**	85,163
	103,183	116,375
Due to		
- Head office	**40,603**	35,876
- Branches (other than UAE)	**1,177**	1,901
- Subsidiaries of the Habib Group	**7,409**	15,639
	49,190	53,416
Loan to HBZ Services LLC	**29,102**	30,544
Deposit from HBZ Services LLC	**11,390**	10,696

24 Related party transactions (continued)

Transactions with Related Parties

	2017 AED 000	2016 AED 000
Interest income (including on Loan to HBZ Services LLC)	**1,866**	2,118
Interest expense	**100**	5
Head Office charges	**21,418**	20,819
Expenses reimbursed to HBZ Services LLC (note 24.1)	**56,077**	52,089

Deposits from other related parties

	2017 AED 000	2016 AED 000
Deposits at 1 January	**72,166**	52,936
Deposits received and rollover during the year	**170,642**	55,331
Deposits repaid during the year	**(100,928)**	(36,101)
Deposits at 31 December	**141,880**	72,166
Interest expense for the Bank during the year	**927**	574

Key management compensations

	2017 AED 000	2016 AED 000
Short term employment benefits	**4,250**	4,600
Post-employment benefits	**116**	148

24.1 Under an outsourcing agreement, HBZ Services LLC provides back office and support services to the Bank including transaction banking, information technology and internal audit.

25 Geographical concentration of assets and liabilities

	Total assets AED 000	Loans & Islamic Financing Receivables AED 000	Investments AED 000
31 December 2017			
U.A.E.	**9,226,405**	**3,629,268**	**207,876**
Other countries	**2,789,536**	**55,563**	**1,122,265**
Total	**12,015,941**	**3,684,831**	**1,330,141**
31 December 2016			
U.A.E.	9,078,141	3,585,697	229,630
Other countries	3,058,168	57,400	612,939
Total	12,136,309	3,643,097	842,569

26 Financial assets and liabilities

The table below set out the Bank's classification of financial assets and liabilities and the carrying and fair value as at 31 December:

	Designated at fair value AED 000	Available for sale AED 000	Held to maturity AED 000	Amortised cost AED 000	Total carrying amount AED 000	Fair value AED 000
At 31 December 2017						
Assets						
Cash and balances with UAE Central Bank	-	-	-	**2,685,446**	**2,685,446**	**2,685,446**
Due from banks	-	-	-	**3,932,281**	**3,932,281**	**3,932,281**
Due from related parties	-	-	-	**103,183**	**103,183**	**103,183**
Loans and Islamic financing receivables	-	-	-	**3,684,831**	**3,684,831**	**3,684,831**
Customers' indebtedness for acceptances	-	-	-	**70,326**	**70,326**	**70,326**
Investments	-	**1,106,708**	**223,433**	-	**1,330,141**	**1,329,071**
Other assets	-	-	-	**67,330**	**67,330**	**67,330**
	-	**1,106,708**	**223,433**	**10,543,397**	**11,873,538**	**11,872,468**
Liabilities, capital and reserves						
Deposits from customers	-	-	-	**10,096,332**	**10,096,332**	**10,096,332**
Due to banks	-	-	-	**74,872**	**74,872**	**74,872**
Due to related parties	-	-	-	**49,190**	**49,190**	**49,190**
Liabilities under acceptances	-	-	-	**70,326**	**70,326**	**70,326**
Other liabilities	-		-	**218,162**	**218,162**	**218,162**
	-	-	-	**10,508,882**	**10,508,882**	**10,508,882**

26 Financial assets and liabilities (continued)

	Designated at fair value AED 000	Available for sale AED 000	Held to maturity AED 000	Amortised cost AED 000	Total carrying amount AED 000	Fair value AED 000
At 31 December 2016						
Assets						
Cash and balances with UAE Central Bank	-	-	-	2,709,883	2,709,883	2,709,883
Due from banks	-	-	-	4,570,113	4,570,113	4,570,113
Due from related parties	-	-	-	116,375	116,375	116,375
Loans and Islamic financing receivables	-	-	-	3,643,097	3,643,097	3,643,097
Customers' indebtedness for acceptances	-	-	-	62,940	62,940	62,940
Investments	-	644,281	198,288	-	842,569	840,794
Other assets	-	-	-	54,640	54,640	54,640
	-	644,281	198,288	11,157,048	11,999,617	11,997,842
Liabilities, capital and reserves						
Deposits from customers	-	-	-	10,380,895	10,380,895	10,380,895
Due to banks	-	-	-	10,475	10,475	10,475
Due to related parties	-	-	-	53,416	53,416	53,416
Liabilities under acceptances	-	-	-	62,940	62,940	62,940
Other liabilities	-		-	203,001	203,001	203,001
	-	-	-	10,710,727	10,710,727	10,710,727

26 Financial assets and liabilities (continued)

All financial assets and liabilities are measured at amortised cost except for derivatives, investments which are designated as fair value through profit or loss and available for sale investments which are measured at fair value by reference to published price quotations in an active market or from prices quoted by counterparties or through use of valuation techniques such as discounted cash flow method.

'Fair value' is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date in the principal or, in its absence, the most advantageous market to which the Bank has access at that date. The fair value of a liability reflects its non-performance risk.

The fair value of due from banks, due to banks, and deposits from customers, which are predominantly short term in tenure and issued at market rates, are considered to reasonably approximate their book value.

The Bank estimates that the fair value of its loans and advances portfolio is not materially different from its book value since majority of loans and advances carry floating markets rates of interest and are frequently re-priced. For loans considered impaired, expected cash flows, including anticipated realisation of collateral, were discounted using an appropriate rate and considering the time of collection, the net result of which is not materially different from the carrying value.

27 Fair Value hierarchy

Fair value hierarchy

The fair values of financial assets and financial liabilities that are traded in active markets are based on quoted market prices or dealer price quotations. For all other financial instruments, the Bank determines fair values using other valuation techniques.

The Bank measures fair values using the following fair value hierarchy, which reflects the significance of the inputs used in making the measurements.

- Level 1: Quoted market price (unadjusted) in an active market for an identical instrument.
- Level 2: Inputs other than quoted prices included within Level 1 that are observable either directly (i.e. as prices) or indirectly (i.e. derived from prices). This category includes instruments valued using: quoted market prices in active markets for similar instruments; quoted prices for identical or similar instruments in markets that are considered less than active; or other valuation techniques in which all significant inputs are directly or indirectly observable from market data.
- Level 3: Inputs that are unobservable. This category includes all instruments for which the valuation technique includes inputs not based on observable data and the unobservable inputs have a significant effect on the instrument's valuation. This category includes instruments that are valued based on quoted prices for similar instruments for which significant unobservable adjustments or assumptions are required to reflect differences between the instruments.

27 Fair Value hierarchy (continued)

The Bank recognises transfers between levels of the fair value hierarchy at the end of the reporting period during which the change has occurred.

Valuation techniques include net present value and discounted cash flow models, comparison to similar instruments for which market observable prices exist, and other valuation models. Assumptions and inputs used in valuation techniques include risk-free and benchmark profit rates, credit spreads in estimating discount rates, bond and equity prices, foreign currency exchange rates, equity and equity index prices and expected price volatilities and correlations. The objective of valuation techniques is to arrive at a fair value measurement that reflects the price that would be received to sell the asset or paid to transfer the liability in an orderly transaction between market participants at the measurement date.

The table below analyses financial instruments, measured at fair value at the end of reporting period, by level into fair value hierarchy into which the fair value measurement is categorised:

	Level 1 AED 000	Level 2 AED 000	Level 3 AED 000	Total AED 000
At 31 December 2017				
Financial assets				
Investments	1,105,511	-	1,197	1,106,708
Forward foreign Exchange contracts	-	-	-	-
	1,105,511	**-**	**1,197**	**1,106,708**
Financial liabilities				
Forward foreign Exchange contracts	-	-	-	-
	-	-	-	-

	Level 1 AED 000	Level 2 AED 000	Level 3 AED 000	Total AED 000
At 31 December 2016				
Financial assets				
Investments	642,998	-	1,283	644,281
Forward foreign Exchange contracts	-	-	-	-
	642,998	**-**	**1,283**	**644,281**
Financial liabilities				
Forward foreign Exchange contracts	-	-	-	-
	-	-	-	-

27 Fair Value hierarchy (continued)

The following table sets out the fair values of financial instruments not measured at fair value and analyses them by the level in the fair value hierarchy into which each fair value measurement is categorised.

At 31 December 2017	Level 1 AED'000	Level 2 AED'000	Level 3 AED'000	Fair value AED'000	Carrying amount AED'000
Financial assets					
Cash and balances with UAE Central Bank	-	**2,685,446**	-	**2,685,446**	**2,685,446**
Due from banks	-	**3,932,281**	-	**3,932,281**	**3,932,281**
Due from related parties	-	-	**103,183**	**103,183**	**103,183**
Loans and Islamic financing receivables	-	-	**3,684,831**	**3,684,831**	**3,684,831**
Investments	**222,361**	-	-	**222,361**	**223,433**
Customers' indebtedness for acceptances	-	-	**70,326**	**70,326**	**70,326**
Other assets	-	-	**67,330**	**67,330**	**67,330**
	222,361	**6,617,727**	**2,925,670**	**10,765,758**	**10,766,830**
Financial liabilities					
Deposits from customers	-	-	**10,096,332**	**10,096,332**	**10,096,332**
Due to banks	-	**74,872**	-	**74,872**	**74,872**
Due to related parties	-	-	**49,190**	**49,190**	**49,190**
Customers' liabilities under acceptances	-	-	**70,326**	**70,326**	**70,326**
Other liabilities	-	-	**218,163**	**218,163**	**218,163**
	-	**74,872**	**10,434,011**	**10,508,883**	**10,508,883**

At 31 December 2016	Level 1 AED'000	Level 2 AED'000	Level 3 AED'000	Fair value AED'000	Carrying amount AED'000
Financial assets					
Cash and balances with UAE Central Bank	-	2,709,883	-	2,709,883	2,709,883
Due from banks	-	4,570,113	-	4,570,113	4,570,113
Due from related parties	-	-	116,375	116,375	116,375
Loans and Islamic financing receivables	-	-	3,643,097	3,643,097	3,643,097
Investments	196,514	-	-	196,514	198,288
Customers' indebtedness for acceptances	-	-	62,940	62,940	62,940
Other assets	-	-	54,640	54,640	54,640
	196,514	7,279,996	3,993,467	11,273,463	11,355,336
Financial liabilities					
Deposits from customers	-	-	10,380,895	10,380,895	10,380,895
Due to banks	-	10,475	-	10,475	10,475
Due to related parties	-	-	53,416	53,416	53,416
Customers' liabilities under acceptances	-	-	62,940	62,940	62,940
Other liabilities	-	-	203,001	203,001	203,001
	-	10,475	10,700,252	10,710,727	10,710,727

27 Fair Value hierarchy (continued)

- In respect of those financial assets and financial liabilities measured at amortised cost, which are of short term nature (up to 1 year), management believes that carrying amount is equivalent to its fair value.
- Financing to customers are fair valued based on DCF which takes into account original underlying cash borrower credit grading and expected prepayments. These features are used to estimate expected cash flows and discounted at risk-adjusted rates. However, this technique is subject to inherent limitations, such as estimation of the appropriate risk-adjusted discount rate, and different assumptions and inputs would yield different results.
- Fair values of customer deposits and due to banks is estimated using discounted cash flow techniques, applying the rates that are offered for deposits of similar maturities and terms. The fair value of deposits payable on demand is the amount payable at the reporting date.

28 Risk management

The Bank is exposed to the following risks from its use of financial instruments:

- Credit risk
- Market risk
- Liquidity risk
- Operational risk

The core business of the Bank is long established, with risk levels easily identifiable and well known to the management. Comprehensive limits are established which are changed from time to time by Board resolutions. The overall risk position is evaluated at Head Office from the standard monthly reporting of the branches and compliance with Bank limits monitored on a regular basis. Measurement is based on compliance with limits and/ or by means of risk weightage as defined for capital adequacy purpose by the Central Bank of UAE and the Bank for International Settlement ('BIS').

The Bank engages in new, large-scale business operations only where limits for such transactions have been approved by the Board of Directors ('the Board'). This approval will only be given after submission of a report by the management setting out the purpose and composition of the proposed product or transaction, together with a clear analysis of the anticipated profitability, resources required and the risks involved. Limits are set taking into account the BIS risk weightage and the guidelines of the Central Bank of UAE. The Board has also set discretionary limits for management below which level minor, non-recurring transactions may be made, or new products tested on a limited basis, without referral to the Board.

(a) Credit risk

Credit risk is the risk of financial loss to the Bank if a customer or counterparty to a financial instrument fails to meet its contractual obligations, and arises principally from the Bank's lending and investing activities and in cases where it acts as an intermediary on behalf of customers or other third parties or issues guarantees.

28 Risk management (continued)

(a) Credit risk (continued)

The Bank's primary exposure to credit risk arises through its loans and Islamic Financing receivables to customers. The amount of credit exposure in this regard is represented by the carrying amounts of the assets on the statement of financial position. In addition, the Bank is exposed to off-balance sheet credit risk through commitments to extend credit and guarantees issued.

The Bank is further exposed to credit risk on various other financial assets, including derivative instruments and debt investments. The current credit exposure in respect of these instruments is equal to the carrying amount of these assets in the statement of financial position. Investment securities are those guaranteed by investment grade banks in order to keep credit risks to a minimum. Should an investment fall outside this category prior to maturity, an immediate report is made to General Management at Head Office with proposals for rectifying the situation.

The responsibility for management of credit risk lies with Zonal Credit Committee, Branch Credit committee and Credit Risk Management department. The Credit risk management department is responsible for the following:

- 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. Authorisation limits are allocated to various credit committees. Larger facilities require approval by management as appropriate;
- Reviewing and assessing credit risk: Credit Risk Management department assesses all credit exposure in excess of designated limits, prior to facilities being committed to customers. Renewals and reviews of facilities are subject to the same review process;
- Limiting concentration of exposure to counterparties, geographies and industries
- Developing and maintaining the risk grading in order to categorise exposures according to the degree of risk of financial loss faced and to focus management on the attendant risk; the risk grading system is used in determining where impairment provisions may be required against specific credit exposures. Risk grades are subject to regular reviews; and
- Reviewing compliance of business units with agreed exposure limits, including those for selected industries, country risk and product types.

Transaction and position limits by instrument and/or by counterparty are set by General Management based in Head Office, within the overall limits set by the Board. These limits are subject to annual review. Comprehensive reporting is to be made to the Board at Head office prior to such review.

Credit risk of individual counterparties or issuers are checked and monitored by management in accordance with internal rules.

Regular audits of business units and credit processes are undertaken by Internal Audit.

28 Risk management (continued)

(a) Credit risk (continued)

Exposure to credit risk:

The credit quality of the financial assets is managed by the Bank using internal credit ratings. The table below shows the credit quality by class of financial assets based on the Bank's credit rating system:

	Loans and Islamic financing receivables		Due from banks		Investments	
	2017	2016	**2017**	2016	**2017**	2016
	AED 000	AED 000	**AED 000**	AED 000	**AED 000**	AED 000
Individually Impaired						
Substandard	**95,291**	38,120	-	-	**1,197**	1,283
Doubtful	**207,748**	222,707	-	-	-	-
Loss	**100**	-	-	-	-	-
Gross amount	**303,139**	260,827	-	-	**1,197**	1,283
Interest in suspense	**(3,137)**	(4,436)	-	-	-	-
Specific allowance for impairment	**(112,742)**	(176,292)	-	-	-	-
Carrying Amount	**187,260**	80,099	-	-	**1,197**	1,283
Past due but not impaired						
Watch list – overdue by less than 60 days	**127,779**	149,431	-	-	-	-
Interest suspended	-	-	-	-	-	-
Specific allowance for impairment	-	-	-	-	-	-
Carrying Amount	**127,779**	149,431	-	-	-	-
Neither past due nor impaired						
Low / fair risk	**3,481,919**	3,499,210	**3,932,281**	4,570,113	**1,328,944**	841,286
Collective allowance for impairment	**(112,127)**	(85,643)	-	-	-	-
Carrying amount	**3,684,831**	3,643,097	**3,932,281**	4,570,113	**1,330,141**	842,569

28 Risk management (continued)

(a) Credit risk (continued)

Exposure to credit risk (continued):

Credit risk exposure of the Bank's investment portfolio as per the external risk rating is as follows:

	S&P equivalent rating	Total 2017 AED'000	Total 2016 AED'000
Low risk	AAA to A-	**543,192**	298,836
Fair risk	BBB+ to B-	**785,752**	542,450
High risk	CCC+ to D	**-**	-
	Unrated	**1,197**	1,283
		1,330,141	842,569

Past due but not impaired

For corporate loans, the entire outstanding exposure of a facility which has been past due is disclosed. Based on an individual assessment, the Bank determines that impairment on the total outstanding is not required considering the borrower's ability to pay, past track record, overall exposure levels, materiality of the past due, types of collaterals, quality of borrower's receivables and/or the stage of collection of the amounts owed to the Bank. Amounts that were past due and settled in a short period after the balance sheet date due to matters of an operational nature have been excluded.

Definition of impaired financial assets

A counterparty is marked as impaired if:

(a) In case of corporate exposures, the Bank considers the counterparty unlikely to pay the full amount outstanding under the original terms of the contract due to one of the following conditions:

- A material credit obligation has been put on non-accrual status;
- Distressed restructuring of a credit obligation;
- Selling of a credit obligation at an economic loss; or
- The Bank or a third party has filed for the counterparty's bankruptcy.

(b) In case of consumer, if the exposure is past due for more than 60 days.

28 Risk management (continued)

(a) Credit risk (continued)

Impairment assessment

The asset portfolio is reviewed at least quarterly at a minimum or as often as necessitated. The accrual or non-accrual status of the asset is re-assessed and appropriately risk graded as per the credit policy on risk grades. Impaired assets are classified as such through approvals on a credit memorandum and reported at least on quarterly intervals to the Board sub committees.

Assessment of specific impairment

Corporate loans: The Bank determines the impairment appropriate for each individually significant loan or advance on an individual basis in line with Central Bank of the UAE and IFRS requirements. The Bank classifies those accounts where recovery is considered doubtful and ensures provisions are made accordingly. The impairment losses are evaluated on an ongoing basis. Credit exposures are classified by exercising mature judgment in line with Central Bank of the UAE regulations and IFRS requirements. Specific impairment is assessed when it shows a significant perceived decline in the credit quality or when an obligation is past due or over-limit for more than 90 days. Delinquent accounts are broadly classified as Substandard, Doubtful or Loss. The following general guidelines are followed for account classification into non-impaired and impaired:

- Loans and advances which bear normal banking risk, whereby information available to the bank assures repayment as agreed are classified as normal loans;

- Loans and advances which show some weaknesses in the borrower's financial condition and credit worthiness, requiring more than normal attention but not allocation of provisions are classified as Watch list loans;

- Those accounts where adverse factors may hinder repayment or weaken security or lead to some loss are classified as "Substandard accounts". In general these are credit exposures where agreed payments of principal and/or interest are more than 90 consecutive days in arrears;

- Those accounts where full recovery of interest and principal seems doubtful on the basis of information available, leading generally to a loss of part of these loans are classified as "Doubtful accounts"; and

- Those accounts where the bank has exhausted all courses of action available but failed to recover anything or where there is a possibility that nothing shall be recovered are classified as "Loss accounts".

All accounts classified as "Sub Standard", "Doubtful" and "Loss" constitute "Non-Performing Accounts"

28 Risk management (continued)

(a) Credit risk (continued)

Assessment of collective impairment

Provisions for collective impairment are made based on the IFRS and Central Bank of the UAE guidelines. Impairments that cannot be identified with an individual loan are estimated on a portfolio basis. The Bank has adopted the following methodologies for determining the collective portfolio impairment provisions:

Historical loss rates for different industry sectors are considered to determine the collective impairment provisions for the corporate portfolios. To ensure that the impact of economic cycles are incorporated, the loss rates are benchmarked against published default histories observed over economic cycles in different markets. Industry specific adjustments are made to reflect the current market conditions. A number of stress scenarios are run to ensure that the reserves are adequate and reflect a realistic level of collective impairment provisions.

Write offs

Corporate: Facilities where partial loss of principal is expected and full recovery of interest and fees is not expected or which are overdue for 180 days or more are transferred on a case-by-case basis to the Specialised Loans Bank for specialised remedial management and, where appropriate, written off as approved by the Management.

Consumer: Consumer loans are written off in the event of a compromise settlement agreed between the Bank and the customer.

The Bank generally waits until all legal and other remedies are exhausted before writing-off fully provisioned loans.

Collateral Management

Credit risk assessment identifies the primary sources of repayment which are the obligor's normal business cash flows and/ or normal personal income. Where credit facilities are secured by collateral, the Bank seeks to ensure the enforceability of the collateral.

Acceptable collateral includes deposits marked with lien, mortgages over land and property, movable assets including inventory, securities, investment grade bonds, gold and guarantees. The maximum lending value and the valuation frequencies are documented in the credit policy.

Collaterals are revalued as a general rule as per the Bank's credit policy. However, adhoc valuations are also carried out depending on the nature of collateral and general economic condition. This enables the Bank to assess the fair market value of the collateral and ensure that risks are appropriately covered.

Collaterals and guarantees are effectively used as mitigating tools by the Bank. The quality of collateral is continuously monitored and assessed.

28 Risk management (continued)

(a) Credit risk (continued)

Analysis by economic activity:

The Bank monitors concentrations of credit risk by economic activity sector. The analysis on significant credit risk by economic activity is as follows:

	2017		2016	
	Loans & Receivables AED 000	**Due from Banks & Investment AED 000**	Loans & receivables AED 000	Due from Banks & Investment AED 000
Manufacturing	**636,490**	**-**	562,567	-
Construction and real estate	**1,043,219**	**-**	1,030,773	-
Trade	**1,043,920**	**-**	1,078,990	-
Transport and communication	**46,556**	**-**	42,748	-
Services	**156,225**	**-**	135,321	-
Sovereign	**-**	**225,583**	-	209,689
Personal	**980,525**	**-**	1,053,057	-
Banks & other financial institutions	**5,902**	**4,663,724**	6,012	5,004,422
Others	**-**	**373,115**	-	198,571
Total gross assets	**3,912,837**	**5,262,422**	3,909,468	5,412,682
Less Impairment provisions				
- Specific provisions	**(112,742)**	**-**	(176,292)	-
- Collective provisions	**(112,127)**	**-**	(85,643)	-
Interest in suspense	**(3,137)**	**-**	(4,436)	-
Total net assets	**3,684,831**	**5,262,422**	3,643,097	5,412,682

28 Risk management (continued)

(a) Credit risk (continued)

Impairment

The Bank's past due loans and advances by industry segment and geographical location at 31 December 2016, as defined by the Central Bank of the UAE are as follows:

	Past due but not impaired AED 000	Individually impaired AED 000	Total AED 000	Specific provision and IIS AED 000	Past due loans AED 000
As at 31 December 2017					
Industry Segment					
Mining and quarrying	-	-	-	-	-
Manufacturing	**22,020**	**21,768**	**43,788**	**(19,987)**	**23,801**
Construction	**33,195**	**127,366**	**160,561**	**(54,307)**	**106,254**
Trade	**7,345**	**21,723**	**29,068**	**(21,561)**	**7,507**
Transport and communication	-	**1,229**	**1,229**	**(1,264)**	**(35)**
Services	-	**1,203**	**1,203**	**(1,201)**	**2**
Sovereign	-	-	-	-	-
Personal	**65,219**	**124,404**	**189,623**	**(14,203)**	**175,420**
Real Estate	-	-	-	-	-
Financial institutions	-	**5,446**	**5,446**	**(3,356)**	**2,090**
Others	-	-	-	-	-
Total	**127,779**	**303,139**	**430,918**	**(115,879)**	**315,039**
Concentration by Geography					
United Arab Emirates	**127,779**	**298,337**	**426,116**	**(115,249)**	**310,867**
Others	-	**4,802**	**4,802**	**(630)**	**4,172**
Total	**127,779**	**303,139**	**430,918**	**(115,879)**	**315,039**
As at 31 December 2016	149,431	260,827	410,258	(180,728)	229,530

28 Risk management (continued)

(a) Credit risk (continued)

Collateral

The Bank holds collateral against loans and Islamic financing receivables in the form of cash, guarantees, mortgages and liens over properties or other securities over assets. Estimates of fair value are based on the value of collateral assessed at the time of borrowing, and are subsequently monitored on a periodic basis.

Analysis of the collateral type is presented in the following table:

	2017 AED'000	2016 AED'000
Pledged deposits	**611,596**	515,884
Debt / Equity securities	**75,216**	71,854
Property	**1,726,268**	1,480,495
Vehicles	**153,116**	210,183
Bank guarantees	**369**	1,149
Total	**2,566,565**	2,279,565

The above represents values restricted to the lower of loan balance or collateral value, and includes AED 163.9 million (2016: AED 93.5 million) collateral held against impaired loans and financing receivables.

28 Risk management (continued)

(a) Credit risk (continued)

Analysis of the Bank's exposure at 31 December 2017 based on BASEL II standardised approach is as follows:

	On & Off balance Sheet	Credit risk mitigation ("CRM")			Risk weighted assets
Assets classes	**Gross outstanding AED 000**	**Exposure before CRM AED 000**	**CRM AED 000**	**Exposure after CRM AED 000**	**Total AED 000**
31 December 2017					
Claims on sovereign	**2,782,308**	**2,782,308**	**-**	**2,782,308**	**9,669**
Claims on (PSEs)	**58,747**	**58,747**	**-**	**58,747**	**-**
Claims on banks	**4,801,151**	**4,801,151**	**-**	**4,773,265**	**1,831,730**
Claims on corporate	**2,744,763**	**2,741,176**	**(374,205)**	**1,995,847**	**1,558,606**
Claims included in retail portfolio	**934,203**	**919,689**	**(237,760)**	**872,354**	**560,520**
Claims secured by residential property	**767,203**	**767,084**	**-**	**767,084**	**474,893**
Claims secured by commercial real estate	**684,253**	**684,253**	**-**	**684,253**	**684,253**
Past due loans	**436,550**	**315,155**	**-**	**312,889**	**384,808**
Other assets	**296,614**	**279,708**	**-**	**279,708**	**206,347**
Total	**13,505,792**	**13,349,271**	**(611,965)**	**12,526,455**	**5,710,826**
31 December 2016					
Claims on sovereign	2,802,966	2,802,966	-	2,802,966	9,415
Claims on (PSEs)	59,939	59,939	-	59,939	-
Claims on banks	5,237,477	5,237,477	-	5,165,166	1,973,071
Claims on corporate	2,574,702	2,574,702	(272,262)	1,573,364	1,573,364
Claims included in retail portfolio	1,002,324	1,002,324	(233,466)	941,004	594,150
Claims secured by residential property	1,077,455	1,077,455	(11,305)	1,077,455	697,837
Claims secured by commercial real estate	546,276	546,276	-	546,276	546,276
Past due loans	414,746	234,018	-	232,259	250,957
Other assets	261,451	247,999	-	247,999	190,699
Total	13,977,336	13,783,156	(517,033)	12,646,428	5,517,658

28 Risk management (continued)

(a) Credit risk (continued)

Risk weighted capital requirement

The Bank has adopted the standardised approach for credit risk, market risk and operational risk for regulatory reporting purposes. The Bank's risk weighted capital requirement for credit, market and operation risk are given below:

Risk weights for credit risk

The Bank has a diversified funded and unfunded credit portfolio. The exposures are classified as per the Standard Portfolio approach mentioned under the Central Bank of UAE Basel II Capital Adequacy Framework covering the standardised approach for credit risk. The descriptions of the counterparty classes along with the risk weights used to derive the risk weighted assets are as follows:

Funded exposure

Claims on sovereigns
These pertain to exposures to governments and their central banks. Claims on central banks and sovereigns are risk weighted in accordance with their ratings from acceptable External Credit Assessment Institutions ('ECAIs'), except that, for all Gulf Cooperation Council ('GCC') sovereigns a 0% weight has been applied.

Claims on public sector entities (PSEs)
Domestic currency claims on GCC non-commercial PSE were treated as claims on GCC sovereign if their Central Bank or monetary authority treats them as such. Foreign currency claims on GCC PSE were treated one grade less favourable than its sovereign i.e. 20% risk weight were applied. Claims on other foreign non-commercial PSE were treated one grade less favourable than its sovereign. Claims on commercial PSE were treated as claims on corporate.

Claims on multilateral development banks (MDBs)
All MDBs are risk weighted in accordance with the Bank's credit rating except for those members listed in the World Bank which are risk weighted at 0%.

Claims on banks
Claims on banks are risk weighted based on the ratings assigned to them by external rating agencies, however, short term claims denominated in local currency were assigned more favourable risk weighting.
No claim on an unrated bank would receive a risk weight lower than that applied to claims on its sovereign of incorporation.

Claims on corporate portfolio
Claims on corporate are risk weighted in accordance with ratings from acceptable ECAIs. Risk weightings for unrated corporate claims are assigned at 100%.

Claims on regulatory retail exposures
Retail claims that are included in the regulatory retail portfolio are assigned risk weights of 75% (except for past due loans), if it meets the criteria mentioned in the Central Bank of UAE BASEL-II guidelines.

28 Risk management (continued)

(a) Credit risk (continued)

Claims secured by residential property
A preferential risk weight of 35% was applied on claims that did not exceed AED 10 million and the claim was secured by residential property with LTV of up to 85%. Other claims secured on residential property were risk weighted 100%.

Claims secured by commercial property
100% risk weight was applied on claims secured by commercial property.

Past due exposures
The unsecured portion of any loan (other than a qualifying residential mortgage loan) that is past due for more than 90 days, net of specific provisions (including partial write-offs), is risk weighted as follows :

- 150% risk weight when specific provisions are less than 20% of the outstanding amount of the loan; and
- 100% risk weight when specific provisions are greater than 20% of the outstanding amount of the loan.

Other exposures
These are risk weighted at 100%.

Unfunded exposure

For credit-related contingent items, the nominal value is converted to an exposure through the application of Credit Conversions Factors (CCF). The CCF is at 20%, 50% or 100% depending on the type of contingent item, and is used to convert off balance sheet notional amounts into an equivalent on balance sheet exposure.

Undrawn commitments to extend credit represent commitments that have not been drawn down or utilised at the reporting date. The nominal amount provides the calculation base to which the CCF is applied for calculating the exposure. CCF range between 20% and 50% for commitment with original maturity of up to one year and over one year respectively and 0% CCF is applicable for commitments which can be unconditionally cancelled at any time.

28 Risk management (continued)

(a) Credit risk (continued)

The Bank's exposure and credit risk mitigation at 31 December 2017 is summarised as follows:

	2017	2016
	AED 000	AED 000
Gross exposure prior to credit risk mitigation	**13,349,271**	13,783,156
Less: exposure covered by eligible financial collateral	**611,596**	515,884
Less: exposure covered by guarantees	**369**	1,149
Net exposure after credit risk mitigation	**12,737,306**	13,266,123
Risk Weighted Assets	**5,710,826**	5,517,658

(b) Market risk

Market risk is the risk that changes in market prices, such as interest rate, equity prices, foreign exchange rates and credit spreads (not relating to changes in the obligor's/ issuer's credit standing) will affect the Bank'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. The prohibition on speculative trading on the Bank's own behalf is designed to ensure that such risks are kept to a minimum.

Market risks are managed on a continuing basis by Area Management based on limits set by the Board and General Management at Head Office. Aggregation at the total Bank level is carried out on a monthly basis as part of the normal month-end reporting procedures.

Foreign currency risk

The Bank is exposed to currency risk through transactions in foreign currencies. The Bank's transactional exposure gives rise to foreign currency gains and losses that are recognised in the statement of profit or loss and other comprehensive income. These exposures comprise the monetary assets and monetary liabilities of the Bank that are not denominated in the measurement currency of the Bank. The Bank ensures that its foreign currency exposure is kept at an acceptable level by buying and selling foreign currencies at spot rates when appropriate.

28 Risk management (continued)

(b) Market risk (continued)

Foreign currency risk (continued)

The table below summarises the Bank's exposure towards various currencies:

At 31 December 2017	AED AED 000	USD AED 000	GBP AED 000	Others AED 000	Total AED 000
Assets					
Cash and balances with UAE Central Bank	**2,331,636**	**353,810**	**-**	**-**	**2,685,446**
Due from banks	**2,464,198**	**948,319**	**291,327**	**228,437**	**3,932,281**
Due from related parties	**-**	**18,808**	**7,050**	**77,325**	**103,183**
Loans and Islamic financing receivables	**3,530,382**	**145,410**	**4,793**	**4,246**	**3,684,831**
Investments	**1,197**	**1,306,630**	**-**	**22,314**	**1,330,141**
Property and equipment	**56,220**	**-**	**-**	**-**	**56,220**
Customers' indebtedness for acceptances	**18,533**	**47,543**	**-**	**4,250**	**70,326**
Deferred tax assets	**41,067**	**-**	**-**	**-**	**41,067**
Other assets	**84,090**	**5,378**	**275**	**22,703**	**112,446**
Total assets	**8,527,323**	**2,825,898**	**303,445**	**359,275**	**12,015,941**
Liabilities, capital and reserves					
Deposits from customers	**6,783,672**	**2,665,743**	**303,958**	**342,959**	**10,096,332**
Due to banks	**4,583**	**70,222**	**-**	**67**	**74,872**
Due to related parties	**29,383**	**19,807**	**-**	**-**	**49,190**
Liabilities under acceptances	**18,533**	**47,543**	**-**	**4,250**	**70,326**
Other liabilities	**236,735**	**5,802**	**900**	**7,055**	**250,492**
Capital and reserves	**1,474,729**	**-**	**-**	**-**	**1,474,729**
Total liabilities, capital and reserves	**8,547,635**	**2,809,117**	**304,858**	**354,331**	**12,015,941**
Net position	**(20,312)**	**16,781**	**(1,413)**	**4,944**	**-**
At 31 December 2016					
Total assets	8,367,474	2,933,409	408,354	427,072	12,136,309
Total liabilities, capital and reserves	8,422,150	2,884,037	407,318	422,804	12,136,309
Net position	(54,676)	49,372	1,036	4,268	-

28 Risk management (continued)

(b) Market risk (continued)

Foreign currency risk (continued)

The Bank's functional currency is the UAE Dirham. The Bank is exposed to currency risk through transactions in spot and forward contracts. Forward transactions are done to accommodate customer requirements and not for any speculative purposes. At 31 December, the Bank had the following net exposures denominated in foreign currencies.

Currency	**Net spot position 2017 AED 000**	**Forward position 2017 AED 000**	**Net exposure 2017 AED 000**	Net exposure 2016 AED 000
US Dollar	**16,781**	**(19,747)**	**(2,966)**	51,769
GBP	**(1,413)**	**864**	**(549)**	(88)
Others	**4,944**	**118**	**5,062**	2,995

Interest rate risk

The Bank's operations are subject to the risk of interest rate fluctuations to the extent that interest-earning assets and interest-bearing liabilities mature or reprice at different times or in different amounts. In the case of floating rate assets and liabilities, the Bank is also exposed to basis risk, which is the difference in repricing characteristics of the various floating rate indices. Risk management activities are aimed at optimising net interest income, given market interest rate levels consistent with Bank's business strategies. The interest sensitivity of the Bank can be illustrated as follows:

Shift in yield curve	**2017 AED 000**	2016 AED 000
+200 b.p.	**104,060**	99,776
-200 b.p.	**(104,060)**	(99,776)

A substantial portion of the Bank's assets and liabilities are re-priced within one year. Accordingly there is limited exposure to interest rate risk. The interest rate sensitivities set out above are illustrative only and employ simplified scenarios. They are based on AED 11 billion of monthly average interest bearing assets and AED 5.4 billion of monthly average interest bearing liabilities (31 Dec 2016: AED 11 billion average interest bearing assets and AED 6 billion average interest bearing liabilities.) The sensitivity does not incorporate actions that could be taken by the management to mitigate the effect of interest rate movements.

28 Risk management (continued)

(b) Market risk (continued)

Interest rate risk

A summary of the Bank's interest rate gap position on non-trading portfolios is as follows:

As at 31 December 2017	Up to 3 months AED 000	3 – 12 months AED 000	1 – 5 year AED 000	Over 5 years AED 000	Non interest bearing AED 000	Carrying amount AED 000
Assets						
Cash and balances with UAE Central Bank	**800,000**	**485,000**	-	-	**1,400,446**	**2,685,446**
Due from banks	**2,784,920**	**719,238**	-	-	**428,123**	**3,932,281**
Due from related parties	**16,836**	-	-	-	**86,347**	**103,183**
Loans and Islamic financing receivables	**3,467,484**	**24,694**	**152,735**	**25,446**	**14,472**	**3,684,831**
Investments	**55,146**	**208,299**	**937,820**	**128,876**	-	**1,330,141**
Property and equipment	-	-	-	-	**56,220**	**56,220**
Customers' indebtedness for acceptances	-	-	-	-	**70,326**	**70,326**
Deferred tax assets					**41,067**	**41,067**
Other assets	-	-	-	-	**112,446**	**112,446**
Total assets	**7,124,386**	**1,437,231**	**1,090,555**	**154,322**	**2,209,447**	**12,015,941**
Liabilities, capital and reserves						
Deposits from customers	**2,508,989**	**1,261,808**	**310,333**	-	**6,015,202**	**10,096,332**
Due to banks	-	-	-	-	**74,872**	**74,872**
Due to related parties	**1,091**	-	-	-	**48,099**	**49,190**
Liabilities under acceptances	-	-	-	-	**70,326**	**70,326**
Other liabilities	-	-	-	-	**250,492**	**250,492**
Capital and reserves	-	-	-	-	**1,474,729**	**1,474,729**
Total liabilities and capital and reserves	**2,510,080**	**1,261,808**	**310,333**	-	**7,933,720**	**12,015,941**
Interest rate sensitivity gap						
2017	**4,614,306**	**175,423**	**780,222**	**154,322**	**(5,724,273)**	-
2016	4,918,608	(267,312)	566,299	42,149	(5,259,744)	-
Cumulative interest rate sensitivity gap						
2017	**4,614,306**	**4,789,729**	**5,569,951**	**5,724,273**	-	-
2016	4,918,608	4,651,296	5,217,595	5,259,744	-	-

Repricing of assets and liabilities has been determined on the basis of contractual pricing or maturity dates, whichever is earlier.

28 Risk management (continued)

(c) Liquidity risk

Liquidity risk is the risk that a bank will encounter difficulty in raising funds to meet commitments associated with financial instruments. Liquidity risk may result from an inability to sell a financial asset at close to its fair value.

The Asset Liability Committee of the Bank meets regularly and monitors the liquidity requirements. The Bank's liquidity management policies are designed to ensure that even under adverse conditions the Bank should be in a position to meet its obligations. The Bank's conservative lending policy and risk averse approach to funding has resulted in a significant mitigation of the Liquidity Risk on the Bank's books, thereby justifying enough liquidity and Capital Adequacy.

Daily liquidity management is carried out through comprehensive reporting by Finance Department and Treasury Department that gives relevant information to the Bank's Management regarding liquidity risk. Excess funds after meeting customer advances and other requirements are placed with Central Bank of the UAE and other good quality internationally rated banks to maintain an optimal short and medium term liquidity position.

The following table shows the undiscounted cash flows on the Bank's financial liabilities and unrecognised loan commitments on the basis of their earliest possible contractual maturity.

	Carrying amount AED 000	Inflow / (Outflow) AED 000	0 – 3 months AED 000	3 months to 1 year AED 000	1 year to 5 years AED 000
At 31 December 2017					
Financial Liabilities					
Deposits from customers	**10,096,332**	**(10,126,664)**	**(8,544,060)**	**(1,268,661)**	**(313,943)**
Due to banks	**74,872**	**(74,878)**	**(74,878)**	-	-
Due to related parties	**49,190**	**(49,192)**	**(49,192)**	-	-
	10,220,394	**(10,250,734)**	**(8,668,130)**	**(1,268,661)**	**(313,943)**
Unrecognised loan commitments	**677,598**	**677,598**	**433,969**	**181,961**	**61,668**
At 31 December 2016					
Financial Liabilities					
Deposits from customers	10,380,895	(10,411,516)	(8,646,903)	(1,380,158)	(384,455)
Due to banks	10,475	(10,476)	(10,476)	-	-
Due to related parties	53,416	(53,418)	(53,418)	-	-
	10,444,786	(10,475,410)	(8,710,797)	(1,380,158)	(384,455)
Unrecognised loan commitments	750,820	750,820	523,225	159,156	68,439

28 Risk management (continued)

(c) Liquidity risk (continued)

The Bank's expected cash flows on these instruments vary significantly from this analysis. For example, demand deposits from customers are expected to maintain a stable or increasing balance; and unrecognised loan commitments are not all expected to be drawn down immediately.

The table below summarises the maturity profile of the Group's assets and liabilities analysed according to when they are expected to be recovered or settled.

As at 31 December 2017	Up to 3 months AED 000	3 – 12 months AED 000	1 – 5 year AED 000	Over 5 years AED 000	No maturity AED 000	Total amount AED 000
Assets						
Cash and balances with UAE Central Bank	**800,000**	**485,000**	-	-	**1,400,446**	**2,685,446**
Due from banks	**2,784,920**	**719,238**	-	-	**428,123**	**3,932,281**
Due from related parties	**16,836**	-	-	-	**86,347**	**103,183**
Loans and Islamic financing receivables	**1,191,095**	**508,291**	**1,612,120**	**40,579**	**332,746**	**3,684,831**
Investments	**55,146**	**163,032**	**983,087**	**128,876**	-	**1,330,141**
Property and equipment	-	-	-	-	**56,220**	**56,220**
Customers' indebtedness for acceptances	**57,396**	**12,930**	-	-	-	**70,326**
Deferred tax assets	-	-	-	-	**41,067**	**41,067**
Other assets	-	-	-	-	**112,446**	**112,446**
Total Assets	**4,905,393**	**1,888,491**	**2,595,207**	**169,455**	**2,547,395**	**12,015,941**
Liabilities, capital and reserves						
Deposits from customers	**2,575,537**	**1,261,808**	**310,333**	-	**5,948,654**	**10,096,332**
Due to banks	-	-	-	-	**74,872**	**74,872**
Due to related parties	**1,091**	-	-	-	**48,099**	**49,190**
Liabilities under acceptances	**57,396**	**12,930**	-	-	-	**70,326**
Other liabilities	-	-	-	-	**250,492**	**250,492**
Capital and reserves	-	-	-	-	**1,474,729**	**1,474,729**
Total liabilities and capital and reserves	**2,634,024**	**1,274,738**	**310,333**	-	**7,796,846**	**12,015,941**
Maturity gap						
2017	**2,271,369**	**613,753**	**2,284,874**	**169,455**	**(5,339,451)**	-
2016	2,674,699	610,810	1,700,551	46,247	(5,032,307)	-

28 Risk management (continued)

(d) Operational Risk

Operational Risk is defined as the risk of loss resulting from inadequate or failed internal processes, people or systems or from external events. This definition comprises legal risk including regulatory fines and settlements, but excludes strategic and reputation risk.

The Bank has an Independent Department in charge of the management of operational risks. This function is responsible for the development of strategies for the identification, assessment, monitoring, control and mitigation of operational risks. The function is also responsible for the development and implementation of a method to assess and report operational risks and systematically collecting the operational risk data relevant for the Bank's operations.

The operational risk department is an integral part of the overall risk management strategy of the Bank. The Bank has sound documentation of all the standard procedures, policies and standardised approaches for all the generic and key processes. Majority of the coverage as to the Management of Operational Risk at the Bank is also effected through system controls.

(e) Capital risk management

Capital allocation

The Bank's lead regulator, the Central Bank of the UAE, sets and monitors regulatory capital requirements.

The Bank's objectives when managing capital are as follows:

- Safeguarding the Bank's ability to continue as a going concern and increase return for shareholders; and
- Comply with regulatory capital set by Central Bank of UAE.

The Bank's policy is to maintain a strong capital base so as to maintain investor, creditor and market confidence and to sustain future development of the business. The impact of the level of capital on shareholders' return is also recognised and the Bank recognises the need to maintain a balance between the higher returns that might be possible with greater gearing and the advantages and security afforded by a sound capital position.

28 Risk management (continued)

(e) Capital risk management (continued)

The Bank also assesses its capital requirements internally taking into consideration growth requirements and business plans, and quantifies its Regulatory and Risk/ Economic Capital requirements within its integrated Internal Capital Adequacy Process ("ICAAP") Framework. Risks such as Interest Rate Risk in the Banking Book, Concentration Risk, Strategic Risk, Legal and Compliance Risk, Stress Risk, Insurance Risk and Reputational Risk are all part of the ICAAP.

The Bank also calculates the Risk Adjusted Return on Capital (RAROC) for credit applications that are priced on a risk-adjusted basis. RAROC calculations are also built into the implemented Credit Appraisal System.

The Bank's regulatory capital adequacy ratio is set by the Central Bank of UAE ('the Central Bank'). The Bank has determined its regulatory capital as recommended by the New Basel II Capital Accord, in line with the guidelines of the UAE Central Bank with effect from 2007. The Bank has adopted a standardised approach for Credit risk and Market risk and a Basic Indicator approach for Operational Risk. The Bank has complied with all externally imposed capital requirements throughout the period. There have been no material changes in the Bank's management of capital during the year and comply with the Central Bank who has advised that the capital adequacy ratio should be increased to 11% analysed into two Tiers, of which Tier 1 capital adequacy must not be less than 7% by 30 September 2009 and 12% analysed into two Tiers, of which Tier 1 capital adequacy must not be less than 8% by 30 June 2010.

The Bank's regulatory capital is analysed into two tiers:

- Tier 1 capital, which includes ordinary share capital, translation reserve and retained earnings; and
- Tier 2 capital, which includes fair value reserves relating to unrealised gains/ losses on investments classified as available-for-sale and derivatives held as cash flow hedges, general provision and subordinated term loans. The following limits have been applied for Tier 2 capital :
  - Total tier 2 capital shall not exceed 67% of Tier 1 capital;
  - Subordinated liabilities shall not exceed 50% of total Tier 1 capital;
  - General provision shall not exceed 1.25% of total risk weighted assets.

28 Risk management (continued)

(e) Capital risk management (continued)

As at 31 December 2017, the Bank's regulatory capital position is as follows:

	2017 AED 000	2016 AED 000
TIER 1 CAPITAL		
Share capital	**100,000**	100,000
Legal reserves	**50,000**	50,000
Retained earnings	**1,330,098**	1,245,853
Total tier 1 capital	**1,480,098**	1,395,853
TIER 2 CAPITAL		
General provisions	**71,341**	68,971
Fair value reserve	**(5,369)**	(3,114)
Total tier 2 capital	**65,972**	65,857
Total regulatory capital (Sum of tier 1 and 2 capital)	**1,546,070**	1,461,710
RISK WEIGHTED ASSETS		
Credit risk	**5,710,826**	5,517,658
Market risk	**4,063**	1,725
Operational risk	**753,793**	753,793
Total risk weighted assets (RWA)	**6,468,682**	6,273,176
Total regulatory capital expressed as % of RWA	**23.90%**	23.30%
Total tier 1 capital expressed as % of RWA	**22.88%**	22.25%

28 Risk management (continued)

(e) Capital risk management (continued)

Risk weights for market risk

Capital requirement for market risk is calculated using standardised approach. The capital requirement for market risk is analysed into capital requirement for interest rate risk, equity risk, foreign exchange risk and option risk.

Risk weight for operation risk

Capital requirement for operation risk is calculated using basic indicator approach. The total capital requirement is calculated as 15% of last three years average income.

Total capital requirement for market risk under standardised approach as per BASEL II Pillar 3 is as follows:

	2017		2016	
	Capital required AED 000	**Risk weighted assets AED 000**	Capital required AED 000	Risk weighted assets AED 000
Interest rate risk	**-**	**-**	-	-
Equity position risk	**-**	**-**	-	-
Foreign exchange risk	**488**	**4,063**	207	1,725
Commodity risk	**-**	**-**	-	-
	488	**4,063**	207	1,725

Basel III capital regulations (unaudited)

The Central Bank of UAE ('CBUAE') issued Basel III capital regulations, which came into effect from 1 February 2017 (parallel reporting for Q2 2017 and Q3 2017 and Primary reporting from Q4 2017 onwards) introducing minimum capital requirements at three levels, namely common Equity Tier1capital ratio (CET1), Tier1 capital ratio (T1) and Total capital ratio.

The additional capital buffers (Capital Conservation Buffer (CCB) and Countercyclical Capital Buffer (CCyB) - maximum up to 2.5% of each buffer) introduced are over and above the minimum CET1 requirement of 7%.

28 Risk management (continued)

(e) Capital risk management (continued)

Basel III capital regulations (unaudited) (continued)

For 2017, CCB is effective in transition arrangement and is required to be maintained at 1.25% of the Capital base. For 2018, CCB will be required at 1.88% and from 2019; it will be required to be maintained at 2.5% of the Capital base. CCyB is not yet in effect and is not required to be maintained for 2017.

The capital adequacy ratio as per Basel III capital regulation is given below:

Capital Ratio	**2017 (unaudited)**	Minimum capital requirement for 2017
Total capital ratio	**22.90%**	10.50%
Tier 1 capital ratio	**22.88%**	8.50%
CET1 capital ratio	**22.88%**	7.00%

29 Cash and cash equivalents

Analysis of the balances of cash and cash equivalent items:

	2017 AED 000	2016 AED 000	Change in year AED 000
Cash and deposits with UAE Central Bank	**2,685,446**	2,709,883	(24,437)
Less: Certificates of deposit with maturity of over 3 months from original maturity	**(485,000)**	(725,000)	240,000
Less: Statutory reserve	**(1,029,521)**	(992,559)	(36,962)
Due from banks	**3,932,281**	4,570,113	(637,832)
Less: Bank placements with maturity of over 3 months from original maturity	**(719,238)**	(1,717,070)	997,832
Due from related parties	**103,183**	116,375	(13,192)
Due to banks	**(74,872)**	(10,475)	(64,397)
Due to related parties	**(49,190)**	(53,416)	4,226
	4,363,089	3,897,851	465,238

30 Custody accounts

The Bank provides custody, trustee and administration services to third parties in relation to a wide range of financial instruments. Those assets that are held in a fiduciary capacity are not included in these financial statements. At the reporting date, the Bank has investment custody accounts aggregating to approximately AED 1,298 million (2016: AED 1,338 million).

31 Comparative figures

Certain comparative figures have been reclassified to conform to the presentation adopted in these financial statements.