Al Khaliji France S.A.
United Arab Emirates Branches

Independent auditor's report
and financial statements
for the year ended 31 December 2018

Al Khaliji France S.A. - United Arab Emirates Branches

Contents

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INDEPENDENT AUDITOR'S REPORT

To the Head Office of
Al Khaliji France S.A.
United Arab Emirates Branches
United Arab Emirates

Report on the Audit of the Financial Statements

Opinion

We have audited the financial statements of **Al Khaliji France S.A., United Arab Emirates Branches** (the "Branches"), **United Arab Emirates,** which comprise the statement of financial position as at 31 December 2018, and the statement of profit or loss, statement of comprehensive income, statement of changes in equity and statement of cash flows for the year then ended, and a summary of 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 Al Khaliji France S.A., United Arab Emirates Branches as at 31 December 2018, and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards ("IFRSs").

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 Branches in accordance with the International Ethics Standards Board for Accountants' *Code of Ethics for Professional Accountants* (IESBA Code) together with the other ethical requirements that are relevant to our audit of the Branches' financial statements in the United Arab Emirates, and we have fulfilled our other ethical responsibilities in accordance with these requirements and 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 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 Articles of Association of the Branches and U.A.E. 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 Branches' 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 Branches or to cease operations, or has no realistic alternative but to do so.

Management is responsible for overseeing the Branches' financial reporting process.

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INDEPENDENT AUDITOR'S REPORT (continued)

Auditor's Responsibilities for the Audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with 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 skepticism throughout the audit. We also

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than the one resulting from error, as fraud may involve collusion, forgery, intentional omission, 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 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 Branches' ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Branches 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 management 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. We also provide management with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

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INDEPENDENT AUDITOR'S REPORT (continued)

Report on Other Legal and Regulatory Requirements

As required by the U.A.E. Federal Law No. (2) of 2015, we report that:

- we have obtained all the information we considered necessary for the purposes of our audit;
- the financial statements of the Branches have been prepared and comply, in all material respects, with the applicable provisions of the U.A.E. Federal Law No. (2) of 2015;
- the Branches have maintained proper books of account;
- the Branches have not purchased or invested in any shares during the year ended 31 December 2018;
- note 6 to the financial statements of the Branches discloses material related party transactions and the terms under which they were conducted; and
- based on the information that has been made available to us nothing has come to our attention which causes us to believe that the Branches have contravened during the financial year ended 31 December 2018, with any of the applicable provisions of the U.A.E. Federal Law No. (2) of 2015 or of its Memorandum and Articles of Association which would materially affect its activities or its financial position as at 31 December 2018.

Furthermore, as required by Article 114 of the Decretal Federal Law No. (14) of 2018, we report that we have obtained all the information and explanations we consider necessary for the purpose of our audit.

Deloitte & Touche (M.E.)

Musa Ramahi
Registration No. 872
31 March 2019
Dubai
United Arab Emirates

Statement of financial position
As at 31 December 2018

	Notes	31 December 2018 AED'000	31 December 2017 AED'000
ASSETS			
Cash and balances with the Central Bank of the U.A.E.	5	**230,761**	564,571
Due from related parties	6	**153,998**	43,503
Deposits and balances due from banks and financial institutions	7	**62,627**	15,638
Investment securities	8	**96,535**	154,076
Loans and advances to customers	9	**1,382,815**	1,846,495
Other assets	10	**60,025**	80,253
Property and equipment	11	**889**	1,520
Intangible assets	12	**5,306**	6,621
Total assets		**1,992,956**	2,712,677
LIABILITIES AND EQUITY			
Liabilities			
Deposits and balances due to banks and financial institutions	13	**3,363**	212,869
Customers' deposits	14	**1,303,028**	1,523,034
Due to related parties	6	**8,962**	281,263
Other liabilities	15	**44,051**	66,023
Total liabilities		**1,359,404**	2,083,189
Equity			
Assigned capital	16(a)	**375,000**	375,000
Statutory reserve	16(b)	**55,758**	55,352
Retained earnings		**202,794**	199,136
Total Equity		**633,552**	629,488
Total liabilities and Equity		**1,992,956**	2,712,677

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Gilles Dermaux
General Manager

The accompanying notes form an integral part of these financial statements.

Statement of profit or loss
for the year ended 31 December 2018

	Notes	2018 AED'000	2017 AED'000
Interest income		**102,588**	124,004
Interest expense		**(25,742)**	(39,163)
Net interest income		**76,846**	84,841
Fee and commission income		**20,238**	25,020
Fee and commission expenses		**(924)**	(509)
Net fee and commission income		**19,314**	24,511
Net gain from foreign currency transactions		**2,765**	3,664
Operating income for the year		**98,925**	113,016
General and administrative expenses	17	**(40,969)**	(47,812)
Allowance for impairment, net	18	**(43,652)**	(33,377)
Net operating expenses		**(84,621)**	(81,189)
Profit before tax		**14,304**	31,827
Income tax expense	19	**(10,240)**	(3,368)
Net profit for the year		**4,064**	28,459

The accompanying notes form an integral part of these financial statements.

Statement of comprehensive income
for the year ended 31 December 2018

	2018 AED'000	2017 AED'000
Profit for the year	**4,064**	28,459
Other comprehensive income	-	-
Other comprehensive income for the year	-	-
Total comprehensive income for the year	**4,064**	28,459

The accompanying notes form an integral part of these financial statements.

Statement of changes in Equity
for the year ended 31 December 2018

	Assigned capital AED'000	Statutory reserve AED'000	Retained earnings AED'000	Total AED'000
Balance at 1 January 2017	375,000	52,506	173,523	601,029
Profit for the year	-	-	28,459	28,459
Other comprehensive income for the year	-	-	-	-
Total comprehensive income for the year	-	-	28,459	28,459
Transfer to statutory reserve	-	2,846	(2,846)	-
Balance at 31 December 2017	375,000	55,352	199,136	629,489
Impact of adopting IFRS 9 (Note 2.1)	-	-	-	-
Restated as at 1 January 2018	**375,000**	**55,352**	**199,136**	**629,489**
Profit for the year	-	-	4,064	4,064
Other comprehensive income for the year	-	-	-	-
Total comprehensive income for the year	-	-	4,064	4,064
Transfer to statutory reserve	-	406	(406)	-
Balance at 31 December 2018	**375,000**	**55,758**	**202,794**	**633,552**

The accompanying notes form an integral part of these financial statements.

Statement of cash flows
for the year ended 31 December 2018

	2018 AED'000	2017 AED'000
Cash flows from operating activities		
Profit before tax	**14,304**	31,827
Adjustments for:		
Allowance for impairment, net	**43,652**	33,377
Depreciation and amortisation	**3,253**	3,770
Provision for employees' end-of-service benefits	**1,184**	1,355
Operating profit before changes in operating assets and liabilities	**62,393**	70,329
Decrease in cash reserve with the Central Bank of the U.A.E.	**26,692**	26,920
Decrease in loans and advances	**420,028**	444,926
(Increase)/decrease in other assets	**(1,959)**	1,597
Decrease in customers' deposits	**(220,006)**	(1,224,704)
Increase/decrease) in other liabilities	**153**	(23,010)
Cash generated from/(used in) operations	**287,301**	(703,942)
Tax paid	**(8,642)**	(18,705)
Employees' end-of-service benefits paid	**(1,946)**	(6,426)
Net cash generated from/(used in) operating activities	**276,713**	(729,073)
Cash flows from investing activities		
Purchase of property and equipment	**(465)**	(16)
Purchase of intangibles	**(916)**	(969)
Proceeds from sale of property and equipment	**-**	479
Purchase of investment securities	**(470)**	(37,527)
Proceeds from maturity/sale of investment securities	**57,320**	122,663
Net cash from investing activities	**55,469**	84,630
Net increase/(decrease) in cash and cash equivalents	**332,182**	(644,443)
Cash and cash equivalents, at the beginning of the year	**26,265**	670,708
Cash and cash equivalents, at the end of the year (Note 20)	**358,447**	26,265

The accompanying notes form an integral part of these financial statements.

Notes to the financial statements
for the year ended 31 December 2018

1. Status and activities

Al Khaliji France S.A. is a French registered bank with its Head Office in Paris, France (the "Head Office"). It commenced its operations in the United Arab Emirates in 1973 as a retail bank and currently has four branches, one in each Emirate of Dubai, Abu Dhabi, Ras Al Khaimah and Sharjah. The ultimate parent and controlling party is Al Khalij Commercial Bank, Doha, Qatar (the "Ultimate Parent Company").

The Bank's regional office in Dubai is responsible for managing the operations of the United Arab Emirates Branches. The regional office's registered address is P.O. Box 4207, Dubai, United Arab Emirates.

These financial statements reflect the activities of the branches of Al Khaliji France S.A. in the United Arab Emirates only (the "Branches") and exclude all transactions, assets and liabilities of the Head Office and Ultimate Parent Company's branches.

2. Application of new and revised International Financial Reporting Standards ("IFRSs")

2.1 New and revised IFRS applied with material effect on the financial statements

a. New standards, amendments and interpretations effective from 1 January 2018

The following standards, amendments and interpretations, which became effective as of 1 January 2018, are relevant to the Branches:

IFRS 9 Financial Instruments	1 January 2018
IFRS 15 Revenue from Contracts with Customers	1 January 2018
IFRIC 22 Foreign Currency Transactions and Advance Consideration	1 January 2018

The adoption of the above did not result in any changes to previously reported net profit or equity of the Branches, except as mentioned below.

IFRS 9 *Financial Instruments*

The Branches has adopted IFRS 9, as issued by the IASB in July 2014 with a date of transition of 1 January 2018, which resulted in changes in accounting policies and adjustments to the amounts previously recognised in the financial statements as of and for the year ended 31 December 2017.

The adoption of IFRS 9 has resulted in changes in the accounting policies for recognition, classification and measurement of financial assets and financial liabilities and impairment of financial assets. IFRS 9 also significantly amends other standards dealing with financial instruments such as IFRS 7 '*Financial Instruments: Disclosures*'.

2. Application of new and revised International Financial Reporting Standards ("IFRS") (continued)

2.1 New and revised IFRS applied with material effect on the financial statements (continued)

IFRS 9 *Financial Instruments* (continued)

Classification of financial assets and financial liabilities

IFRS 9 contains three principal classification categories for financial assets: measured at amortised cost, fair value through other comprehensive income (FVOCI) and fair value through profit or loss (FVTPL). IFRS 9 classification is generally based on the business model in which a financial asset is managed and its contractual cash flows. The standard eliminates the existing IAS 39 categories of held-to-maturity, loans and receivables and available-for-sale.

Under IFRS 9, derivatives embedded in contracts where the host is a financial asset in the scope of the standard are never bifurcated. Instead, the whole hybrid instrument is assessed for classification.

IFRS 9 largely retains the existing requirements in IAS 39 for the classification of financial liabilities. However, although under IAS 39 all fair value changes of liabilities designated under the fair value option were recognised in the consolidated income statement, under IFRS 9 fair value changes are generally presented as follows:

- The amount of change in the fair value that is attributable to changes in the credit risk of the liability is presented in OCI; and
- The remaining amount of change in the fair value is presented in the consolidated income statement.

Impairment of financial assets

IFRS 9 replaces the 'incurred loss' model in IAS 39 with an 'expected credit loss' model. The new impairment model also applies to certain loan commitments and financial guarantee contracts but not to equity investments. Under IFRS 9, credit losses are recognised earlier than under IAS 39.

The Branches applies three-stage approach to measuring expected credit losses (ECL) on financial assets carried at amortised cost and debt instruments classified as FVOCI. Assets migrate through the following three stages based on the change in credit quality since initial recognition.

Stage 1: 12 months ECL - not credit impaired

Stage 1 includes financial assets on initial recognition and that do not have a significant increase in credit risk since the initial recognition or that have low credit risk. For these assets, ECL are recognised on the gross carrying amount of the asset based on the expected credit losses that result from default events that are possible within 12 months after the reporting date. Interest is computed on the gross carrying amount of the asset.

Stage 2: Lifetime ECL - not credit impaired

Stage 2 includes financial assets that have had a significant increase in credit risk (SICR) since initial recognition but that do not have objective evidence of impairment. For these assets, lifetime ECL are recognised, but interest is still calculated on the gross carrying amount of the asset. Lifetime ECL are the expected credit losses that result from all possible default events over the expected life of the financial instrument.

Notes to the financial statements
for the year ended 31 December 2018 (continued)

2. Application of new and revised International Financial Reporting Standards ("IFRS") (continued)

2.1 New and revised IFRS applied with material effect on the financial statements (continued)

IFRS 9 *Financial Instruments* (continued)

Impairment of financial assets (continued)

Stage 3: Lifetime ECL - credit impaired

Stage 3 includes financial assets that have objective evidence of impairment at the reporting date. For these assets, lifetime ECL are recognised.

Transition

Changes in accounting policies resulting from the adoption of IFRS 9 have been applied retrospectively, except as described below.

(a) As permitted by the transitional provisions of IFRS 9 and UAE CB regulations, the Branches elected not to restate comparative figures. Differences in the carrying amounts of financial assets and financial liabilities resulting from the adoption of IFRS 9 are recognised in retained earnings and reserves as at 1 January 2018. Accordingly, the information presented for 2017 does not reflect the requirements of IFRS 9 and therefore is not comparable to the information presented for 2018 under IFRS 9.

(b) The following assessments have been made on the basis of the facts and circumstances that existed at the date of initial application.

- The determination of the business model within which a financial asset is held.
- If a debt security had low credit risk at the date of initial application of IFRS 9, then the Branches have assumed that credit risk on the asset had not increased significantly since its initial recognition.

The Branches performed a detailed analysis of its business models for managing financial assets as well as analysing their cash flow characteristics.

Notes to the financial statements
for the year ended 31 December 2018 (continued)

2. Application of new and revised International Financial Reporting Standards ("IFRS") (continued)

2.1 New and revised IFRS applied with material effect on the financial statements (continued)

IFRS 9 *Financial Instruments* (continued)

Impairment of financial assets (continued)

(a) Classification and Measurement of Financial Instruments

The below table reconciles the original measurement categories and carrying amounts of financial assets and liabilities in accordance with IAS 39 and the new measurement categories under IFRS 9 as at 1 January 2018.

			Original carrying amount AED'000	Impact of IFRS 9 Re-measurement AED'000	Impact of IFRS 9 Re-classification AED'000	New carrying amount AED'000
Financial assets						
Cash and balances with the Central Bank of the U.A.E.	Loans and receivables	Amortised cost	564,571	-	-	**564,571**
Due from related parties	Loans and receivables	Amortised cost	43,503	-	-	**43,503**
Due from banks and financial institutions	Loans and receivables	Amortised cost	15,638	-	(2)	**15,636**
Investment securities	Held to maturity	Amortised cost	154,076	-	(1,106)	**152,970**
Loans and advances to customers	Loans and receivables	Amortised cost	1,846,495	-	1,153	**1,847,648**
Other financial assets	Loans and receivables	Amortised cost	77,436	-	-	**77,436**
Foreign currency forward contracts	FVTPL	FVTPL	73	-	-	**73**
			2,701,792	-	45	**2,701,837**
Financial liabilities						
Due to banks and financial institutions	Amortised cost	Amortised cost	212,869	-	-	**212,869**
Customers' deposits	Amortised cost	Amortised cost	1,523,034	-	-	**1,523,034**
Due to related parties	Amortised cost	Amortised cost	281,263	-	-	**281,263**
Other liabilities	Amortised cost	Amortised cost	21,184	-	45	**21,229**
			2,038,350	-	45	**2,038,395**

Notes to the financial statements for the year ended 31 December 2018 (continued)

2. Application of new and revised International Financial Reporting Standards ("IFRS") (continued)

2.1 New and revised IFRS applied with material effect on the financial statements (continued)

IFRS 9 *Financial Instruments* (continued)

Financial liabilities

There were no changes to the classification and measurement of financial liabilities.

IFRS 15 *Revenue from Contracts with Customers*

The Branches implemented this new revenue recognition standard with effect from 1 January 2018. IFRS 15 provides a principles-based approach for revenue recognition, and introduces the concept of recognising revenue for performance obligations, as they are satisfied. The Branches has assessed the impact of IFRS 15 and concluded that the standard has no material effect on the financial statements of the Branches.

2.2 New and revised IFRS in issue but not yet effective

A number of standards and amendments to standards are issued but not yet effective and the Branches has not adopted these in the preparation of these financial statements. The below standards may have a significant impact on the Branches' financial statements, however, the Branches is currently evaluating the impact of these new standards. The Branches will adopt these new standards on the respective effective dates.

New and revised IFRSs	Effective for annual periods beginning on or after
IFRS 16 *Leases*	1 January 2019
Annual Improvements to IFRSs 2015-2017 Cycle amending IFRS 3 *Business Combinations*, IFRS 11 *Joint Arrangements*, IAS 12 *Income Taxes* and IAS 23 *Borrowing costs.*	1 January 2019
IFRIC 23 *Uncertainty over Income Tax Treatments*	1 January 2019
Amendments in IFRS 9 *Financial Instruments* relating to prepayment features with negative compensation.	1 January 2019
Amendment to IAS 19 *Employee Benefits* relating to amendment, curtailment or settlement of a defined benefit plan	1 January 2019
Amendments in IAS 28 *Investments in Associates and Joint Ventures* relating to long-term interests in associates and joint ventures.	1 January 2019
Amendments to References to the Conceptual Framework in IFRS Standards - amendments to IFRS 2, IFRS 3, IFRS 6, IFRS 14, IAS 1, IAS 8, IAS 34, IAS 37, IAS 38, IFRIC 12, IFRIC 19, IFRIC 20, IFRIC 22, and SIC-32 to update those pronouncements with regard to references to and quotes from the framework or to indicate where they refer to a different version of the Conceptual Framework	1 January 2020
Amendment to IFRS 3 *Business Combinations* relating to definition of a business	1 January 2020

2. Application of new and revised International Financial Reporting Standards ("IFRS") (continued)

2.2 New and revised IFRS in issue but not yet effective (continued)

New and revised IFRSs	Effective for annual periods beginning on or after
Amendments to IAS 1 and IAS 8 relating to definition of material	1 January 2020
IFRS 17 *Insurance Contracts*	1 January 2021
Amendments to IFRS 10 financial statements and IAS 28 *Investments in Associates and Joint Ventures* (2011) relating to the treatment of the sale or contribution of assets from and investor to its associate or joint venture.	Effective date deferred indefinitely. Adoption is still permitted.

Management anticipates that these new standards, interpretations and amendments will be adopted in the Branches' financial statements as and when they are applicable and adoption of these new standards, interpretations and amendments, except for IFRS 16 as highlighted in next paragraphs, may have no material impact on the financial statements of the Branches in the period of initial application.

IFRS 16 Leases

The Branches will adopt IFRS 16 Leases on its mandatory adoption date of 1 January 2019. The new standard will result in some leases being recognised on the statement of financial position by lessees, as the distinction between operating and finance leases is removed.

Under the new standard, an asset (the right to use the leased item) and a financial liability to pay rentals are recognised. The only exceptions are short-term and low-value leases. The Branches intends to apply the simplified transition approach and does not expect to restate comparative amounts for the year prior to first adoption. Right-of-use assets will be measured on transition as if the new rules had always been applied. Management is currently performing a detailed analysis of the impact of the application of these Standards and hence has not yet quantified the extent of the impact, which is expected to be immaterial.

3. Significant accounting policies

The accounting policies set out below have been applied consistently to all periods presented in these financial statements except for the effects of adoption of IFRS 9 and IFRS 15 on 1 January 2018, as described in note 3(a), and have been applied consistently by the Branches. Additionally, the Branches has adopted consequential amendments to IFRS 7 Financial Instruments: Disclosures that are applied to disclosures for 2018, but have not been applied to the comparative information.

Statement of compliance

The financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB"), the applicable provisions of the Central Bank of the UAE regulations.

Notes to the financial statements
for the year ended 31 December 2018 (continued)

3. Significant accounting policies (continued)

Basis of preparation

The financial statements have been prepared on the historical cost basis at the end of each reporting period, as explained in the accounting policies below.

Historical cost is generally based on the fair value of the consideration given in exchange for goods and services.

Functional and presentation currency

These financial statements are presented in Arab Emirates Dirham (AED) and all values are rounded to the nearest thousands dirham, except when otherwise indicated.

Financial instruments

Recognition and initial measurement

Financial assets and financial liabilities are recognised when the Branches become a party to the contractual provisions of the instrument.

Financial assets and financial liabilities are initially measured at fair value. Transaction costs that are directly attributable to the acquisition or issue of financial assets and financial liabilities (other than financial assets and financial liabilities at fair value through profit and 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 and loss are recognised immediately in the statement of profit or loss.

Financial assets - policy applicable from 1 January 2018

On initial recognition, a financial asset is classified as measured at: amortised cost, FVOCI or FVTPL.

A financial asset is measured at amortised cost if it meets both of the following conditions and is not designated as at FVTPL:

- The asset is held within a business model whose objective is to hold assets to collect contractual cash flows; and
- The contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

A debt instrument is measured at FVOCI only if it meets both of the following conditions and is not designated as at FVTPL:

- The asset is held within a business model whose objective is achieved by both collecting contractual cash flows and selling financial assets; and
- The contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

On initial recognition of an equity investment that is not held for trading, the Branches may irrevocably elect to present subsequent changes in fair value in OCI. This election is made on an investment-by-investment basis.

3. Significant accounting policies (continued)

Financial instruments (continued)

Financial assets - policy applicable from 1 January 2018 (continued)

All other financial assets are classified as measured at FVTPL.

In addition, on initial recognition, the Branches may irrevocably designate a financial asset that otherwise meets the requirements to be measured at amortised cost or at FVOCI as at FVTPL, if doing so eliminates or significantly reduces an accounting mismatch that would otherwise arise.

Business model assessment

The Branches makes an assessment of the objective of a business model in which an asset is held at a portfolio level because this best reflects the way the business is managed and information is provided to management. The information considered includes:

- The stated policies and objectives for the portfolio and the operation of those policies in practice;
- How the performance of the portfolio is evaluated and reported to the Branches' management;
- The risks that affect the performance of the business model (and the financial assets held within that business model) and how those risks are managed;
- How managers of the business are compensated (e.g. whether compensation is based on the fair value of the assets managed or the contractual cash flows collected); and
- The frequency, volume and timing of sales in prior periods, the reasons for such sales and its expectations about future sales activity. However, information about sales activity is not considered in isolation, but as part of an overall assessment of how the Branches' stated objective for managing the financial assets is achieved and how cash flows are realised.

Financial assets that are held for trading or managed and whose performance is evaluated on a fair value basis are measured at FVTPL because they are neither held to collect contractual cash flows nor held both to collect contractual cash flows and to sell financial assets.

Assessment whether contractual cash flows are solely payments of principal and interest

For the purposes of this assessment, 'principal' is defined as the fair value of the financial asset on initial recognition. 'Interest' is defined as consideration for the time value of money and for the credit risk associated with the principal amount outstanding during a particular period of time and for other basic lending risks and costs (e.g. liquidity risk and administrative costs), as well as profit margin.

In assessing whether the contractual cash flows are solely payments of principal and interest ("the SPPI test"), the Branches considers the contractual terms of the instrument. This includes assessing whether the financial asset contains a contractual term that could change the timing or amount of contractual cash flows such that it would not meet this condition. In making the assessment, the Branches considers contingent events that would change the amount and timing of cash flows, prepayment and extension terms, terms that limit the Branches' claim to cash flows from specified assets and features that modify consideration of the time value of money. Instruments failing SPPI will be measured at FVTPL.

Reclassifications

Financial assets are not reclassified subsequent to their initial recognition, except in the period after the Branches changes its business model for managing financial assets. The reclassification takes place from the start of the first reporting period following the change.

Notes to the financial statements
for the year ended 31 December 2018 (continued)

3. Significant accounting policies (continued)

Financial instruments (continued)

Financial assets - applicable up to 31 December 2017

All regular way purchases or sales of financial assets are recognised and derecognised on a trade date basis. Regular way purchases or sales are purchases or sales of financial assets that require delivery of assets within the time frame established by regulation or convention in the marketplace.

Classification of financial assets

Financial assets are classified as 'held to maturity investments' and 'loans and advances'. The classification depends on the nature and purpose of the financial assets and is determined at the time of initial recognition.

Held to maturity investments

Held to maturity financial investments are non-derivative financial assets with fixed or determinable payments and fixed maturities, which the Branches have the intention and ability to hold to maturity. After initial measurement, held to maturity financial investments are measured at amortised cost using the effective interest method less any impairment, with revenue recognised on an effective yield basis.

The 'investment securities' includes:

Debt investment securities measured at amortised cost; these are initially measured at fair value plus incremental direct transaction costs, and subsequently at their amortised cost using the effective interest method.

Loans and advances

Loans and advances are non-derivative financial assets originated or acquired by the Branches with fixed or determinable payments that are not quoted in an active market. Loans and advances are initially recognised when cash is advanced to borrowers at the fair value on the commitment date, plus directly attributable incremental transaction costs. They are subsequently carried at amortised cost using the effective interest method less any amounts written-off and allowance for impairment.

Effective interest method

The effective interest method is a method of calculating the amortised cost of a debt instrument and of allocating interest income over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash receipts (including all fees and points paid or received that form an integral part of the effective interest rate, transaction costs and other premiums or discounts) through the expected life of the debt instrument, or, where appropriate, a shorter period, to the net carrying amount on initial recognition.

Income is recognised on an effective interest basis for debt instruments (other than those financial assets designated as FVTPL) and are measured subsequently at amortised cost. Interest income is recognised in the statement of profit or loss.

Notes to the financial statements
for the year ended 31 December 2018 (continued)

3. Significant accounting policies (continued)

Financial instruments (continued)

Cash and cash equivalents

Cash and cash equivalents include cash on hand and deposits with the Central Bank of the U.A.E. (except mandatory cash reserves), amounts due from related parties and due from banks and financial institutions. Cash equivalents comprise highly liquid investments that are convertible into cash with an insignificant risk of changes in value with original maturities of less than three months.

Impairment of financial assets

Financial assets that are measured at amortised cost are assessed for impairment at the end of each reporting period. Financial assets 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 could include:

- significant financial difficulty of the issuer or counterparty;
- breach of contract, such as a default or delinquency in interest or principal payments;
- it becoming probable that the borrower 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, discounted at the financial asset's original effective interest rate.

The carrying amount of the financial asset is reduced by the impairment loss directly for all financial assets with the exception of loans and advances and due from banks, where the carrying amount is reduced through the use of an allowance account. When a loan is considered uncollectible, it is written off against the allowance account. Subsequent recoveries of amounts previously written off are credited against the allowance account. Changes in the carrying amount of the allowance account are recognised in the statement of profit or loss.

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 to the extent that the carrying amount of the financial asset at the date the impairment is reversed does not exceed what the amortised cost would have been had the impairment not been recognised.

Impairment of loans and advances measured are assessed by the Branches as follows:

Notes to the financial statements
for the year ended 31 December 2018 (continued)

3. Significant accounting policies (continued)

Financial instruments (continued)

Individually assessed loans

These represent mainly corporate loans, which are assessed individually by the Branches' Credit Department in order to determine whether there exists any objective evidence that a loan is impaired.

Impaired loans are measured based on the present value of expected future cash flows discounted at the loan's effective interest rate or at the loan's observable market price, if available, or at the fair value of the collateral if the recovery is entirely collateral dependent.

Impairment loss is calculated as the difference between the loan's carrying value and its present value calculated as above.

Collectively assessed loans

Impairment losses of collectively assessed loans include the allowances on:

Performing commercial and other loans

Where individually assessed loans are evaluated and no evidence of loss is present or has been identified, there may be losses based upon risk rating and expected migrations, product or industry characteristics.

Impairment covers losses which may arise from individual performing loans that are impaired at the reporting date but were not specifically identified as such until sometime in the future.

The estimated impairment is calculated by the Branches' management for each identified portfolio and based on historical experience, credit rating and expected migrations in addition to the assessed inherent losses which are reflected by the economic and credit conditions.

Retail loans with common features are assessed on a portfolio basis and where individual loan amounts are not significant

Impairment of retail loans is calculated by applying a systematic approach whereby a provision of 25% of loan balance is made when it is past due by more than 90 days and a provision of 50% of loan balance is made when it is past due by more than 120 days. All loans that are past due by more than 180 days are provided in full.

Impairment

Policy applicable from 1 January 2018

The Branches recognises loss allowances for expected credit losses (ECL) on the following financial instruments that are not measured at FVTPL:

- Financial assets that are classified at amortized costs
- Financial assets that are debt instruments; and
- Loan commitments and financial guarantee contracts.

Notes to the financial statements
for the year ended 31 December 2018 (continued)

3. Significant accounting policies (continued)

Financial instruments (continued)

Impairment (continued)

Policy applicable from 1 January 2018 (continued)

The Branches measures loss allowances at an amount equal to lifetime ECL, except for the following, for which they are measured as 12-month ECL:
- debt investment securities that are determined to have low credit risk at the reporting date; and
- other financial instruments on which credit risk has not increased significantly since their initial recognition

12-month ECL are the portion of ECL that result from default events on financial instruments that are possible with the 12 months after the reporting date.

Measurement of ECL

ECL are a probability-weighted estimate of credit losses. They are measured as follows:
- Financial assets that are not credit-impaired at the reporting date: as the present value of all cash shortfalls (i.e. the difference between the cash flows due to the entity in accordance with the contract and the cash flows that the Branches expects to receive);
- Financial assets that are credit-impaired at the reporting date: as the difference between the gross carrying amount and the present value of estimated future cash flows;
- Undrawn loan commitments: as the present value of the difference between the contractual cash flows that are due to the Branches if the commitment is drawn down and the cash flows that the Branches expects to receive; and
- Financial guarantee contracts: the expected payments to reimburse the holder less any amounts that the Branches expects to recover.

Restructured financial assets

If the terms of a financial asset are renegotiated or modified or an existing financial asset is replaced with a new one due to financial difficulties of the borrower, then an assessment is made of whether the financial asset should be derecognised and ECL are measured as follows.
- If the expected restructuring will not result in derecognition of the existing asset, then the expected cash flows arising from the modified financial asset are included in calculating the cash shortfalls from the existing asset.
- If the expected restructuring will result in derecognition of the existing asset, then the expected fair value of the new asset is treated as the final cash flow from the existing financial asset at the time of its derecognition. This amount is included in calculating the cash shortfalls from the existing financial asset that are discounted from the expected date of derecognition to the reporting date using the original effective interest rate of the existing financial asset.

Credit-impaired financial assets

At each reporting date, the Branches assesses whether financial assets carried at amortised cost and debt financial assets carried at FVOCI are credit impaired. A financial asset is 'credit-impaired' when one or more events that have a detrimental impact on the estimated future cash flows of the financial asset have occurred.

Notes to the financial statements
for the year ended 31 December 2018 (continued)

3. Significant accounting policies (continued)

Policy applicable from 1 January 2018 (continued)

Credit-impaired financial assets (continued)

Evidence that a financial asset is credit-impaired includes the following observable data:

- Significant financial difficulty of the borrower or issuer;
- A breach of contract such as a default or past due event;
- The restructuring of a loan or advance by the Branches on terms that the Branches would not consider otherwise;
- It is becoming probable that the borrower will enter bankruptcy or other financial reorganisation; or
- The disappearance of an active market for a security because of financial difficulties.

De-recognition of financial assets

The Branches derecognise a financial asset only when the contractual rights to the cash flows from the asset expire, or when it transfers the financial asset and substantially all the risks and rewards of ownership of the asset to another entity. If the Branches neither transfer nor retain substantially all the risks and rewards of ownership and continue to control the transferred asset, the Branches recognise its retained interest in the asset and an associated liability for amounts it may have to pay. If the Branches retain substantially all the risks and rewards of ownership of a transferred financial asset, the Branches continue to recognise the financial asset and also recognise a collateralised borrowing for the proceeds received.

On derecognition of financial assets measured at amortised cost, the difference between the asset's carrying amount and the sum of the consideration received or receivable is recognised in the statement of profit or loss.

Renegotiated loans

The contractual terms of a loan may be modified for a number of reasons, and not limited to credit deterioration of the customer. When determining whether a renegotiated loan should be derecognised and a new loan to be recognised, the Branches perform a quantitative and qualitative evaluation of whether the changes to the original contractual terms result in a substantially different financial instrument, in which case an existing loan is derecognised and the renegotiated loan is recognised at fair value. For loans under credit deterioration, irrespective of whether the loan is derecognised on renegotiation, it remains disclosed at same risk grade until there is sufficient evidence of improvement.

Write-off policy

The Branches write off a loan (and any related allowances for impairment losses) when Branches' Credit Committee determines that the loan is uncollectible in whole or in part. This determination is reached after all avenues for recovery have failed. For smaller balance standardised loans, charge off decisions generally are based on a product specific past due status.

3. Significant accounting policies (continued)

Policy applicable up to 31 December 2017

Impairment is calculated on the basis of discounted estimated future cash flows or by applying a certain percentage on the performing unclassified loan based on market trend and historical pattern of defaults. For retail loans and advances impairment is calculated based on a formulaic approach depending on past due instalments and payments.

The allowance for loan losses is established through charges to the statement of profit or loss in the form of an allowance for loan loss. Increases and decreases in the allowance due to changes in the measurement of the impaired loans are included in the allowance for loan losses and affect the statement of profit or loss accordingly.

Individually assessed loans

Impairment losses for individually assessed loans are determined by an evaluation of exposure on a case-by-case basis. This procedure is applied to all classified corporate loans and advances which are individually significant accounts or are not subject to, the portfolio-based approach.

The following factors are considered when determining impairment losses on individually assessed accounts:

1. The customer's aggregate borrowings.
2. The customer's risk rating, i.e. ability to perform profitable business and generate sufficient cash to repay the borrowed amount.
3. The value of the collateral and the probability of successful repossession.
4. The cost involved to recover the debts.

The Branches' policy requires regular review of the level of impairment allowances on individual facilities.

Impaired loans continue to be classified as impaired unless they are brought fully current and the collection of scheduled interest and principal is considered probable.

Collectively assessed loans

The management of the Branches assess, based on historical experience and the prevailing economical and credit conditions, the magnitude of loans and advances which may be impaired but not identified as of the reporting date.

These portfolio allowances are reassessed on a periodical basis and allowances are adjusted accordingly based on the judgment of management and guidance received from the Central Bank of the UAE.

Collectively assessed allowances are also made in respect of losses incurred in portfolios of retail loans with common features and where individual loan amounts are not significant.

Impairment of retail loans is calculated by applying a formulaic approach whereby a provision of 25% of loan balance is made when it is past due by more than 90 days and a provision of 50% of loan balance is made when is past due by more than 120 days and less than 180 days. All loans that are past due by more than 180 days are provided in full.

3. Significant accounting policies (continued)

Financial instruments (continued)

Financial liabilities and equity instruments

Classification as debt or equity

Debt and equity instruments issued by the Branches are classified as either financial liabilities or as equity in accordance with the substance of the contractual arrangement and the definitions of a financial liability and an equity instrument.

Equity instruments

An equity instrument is any contract that evidences a residual interest in the assets of an entity after deducting all of its liabilities. Equity instruments issued by the Branches are recognised at the proceeds received, net of direct issue costs.

Financial liabilities

Financial liabilities are classified as other financial liabilities which include borrowings and customer deposits, are initially measured at fair value, net of transaction costs. Other financial liabilities are subsequently measured at amortised cost using the effective interest method, with interest expense recognised on an effective yield basis.

Financial guarantees

A financial guarantee contract is a contract that requires the issuer to make specified payments to reimburse the holder for a loss it incurs because a specified debtor fails to make payments when due in accordance with the terms of a debt instrument.

Financial guarantee contracts issued by the Branches are initially measured at their fair values and, if not designated at fair values, are subsequently measured at the higher of:

- the amount of the obligation under the contract, as determined in accordance with IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*; and
- the amount initially recognised less, where appropriate, cumulative amortisation recognised in accordance with the revenue recognition policies.

Any increase in the liability relating to financial guarantees is recorded in the statement of profit or loss. The premium received is recognised in the statement of profit or loss in fees and commission income on a straight line basis over the life of the guarantee.

De-recognition of financial liabilities

The Branches derecognise financial liabilities when, and only when, the Branches' obligations are discharged, cancelled or they expire. The difference between the carrying amount of the financial liability derecognised and the consideration paid and payable, including any non-cash assets transferred or liabilities assumed, is recognised in statement of profit or loss.

Notes to the financial statements
for the year ended 31 December 2018 (continued)

3. Significant accounting policies (continued)

Financial instruments (continued)

Financial liabilities and equity instruments (continued)

Fair values

All financial instruments are recognised initially at fair value. The fair value of a financial instrument on initial recognition is normally the transaction price, i.e. the fair value of the consideration given or received.

- The fair value of financial assets and financial liabilities with standard terms and conditions and traded on active liquid markets is determined with reference to quoted market prices;
- The fair value of other financial assets and financial liabilities (excluding derivative instruments) is determined in accordance with generally accepted pricing models based on discounted cash flow analysis using prices from observable current market transactions and dealer quotes for similar instruments; and
- The fair value of derivative instruments is calculated using quoted prices. Where such prices are not available, use is made of discounted cash flow analysis using the applicable yield curve for the duration of the instruments for non-optional derivatives, and option pricing models for optional derivatives.

Offsetting of financial assets and liabilities

Financial assets and liabilities are offset and reported net in the statement of financial position only when there is a legally enforceable right to set off the recognised amounts or when the Branches intend to settle on a net basis, or to realize the asset and settle the liability simultaneously.

Derivative financial instruments and hedge accounting

The Branches use derivative financial instruments pertaining to forward foreign exchange contracts.

Derivative financial instruments are initially measured at cost, being the fair value at contract date, and are subsequently re-measured at fair value. All derivatives are carried at their fair values as assets where the fair values are positive and as liabilities where the fair values are negative.

Fair values are generally obtained by reference to quoted market prices, discounted cash flow models and recognised pricing models as appropriate.

Embedded derivatives

Derivatives embedded in other financial instruments or other host contracts are treated as separate derivatives when their risks and characteristics are not closely related to those of the host contract and the host contract is not carried at fair value with unrealised gains or losses reported in the statement of profit or loss.

Notes to the financial statements
for the year ended 31 December 2018 (continued)

3. Significant accounting policies (continued)

Revenue recognition

Interest income and interest expense

The Branches recognise interest income and interest expense in the statement of profit or loss for all interest bearing financial instruments classified as held to maturity, available-for-sale and loans and receivables using the effective interest method, which is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument or a shorter period, where appropriate, to the net carrying amount of the financial asset or financial liability on initial recognition. When there is doubt in the collection of the principal or the interest, the recognition of interest income ceases. Interest income from financial assets measured at FVTPL is recognised on accrual basis. Recoveries in respect of loans fully provided for are accounted for on a cash receipt basis.

Fees and commission income and expenses

Fees and commission income and expenses are generally recognised in the statement of profit or loss on accrual basis as the related services are provided except those that are integral to the effective interest rate calculations. Fees and commission included in the effective interest rate calculation are those that are incremental and directly attributable to the origination of the product and which are integral to the yield of the product.

Other fees and commission expense relate mainly to transaction and service fees, which are expensed as the services are received.

Fee income from providing transaction services fees arising from negotiating or participating in the negotiation of a transaction for a third party, such as the arrangement of the acquisition of shares or other securities or the purchase or sale of businesses, are recognised on completion of the underlying transaction. Fees or components of fees that are linked to a certain performance are recognised after fulfilling the corresponding criteria.

Foreign currency transactions

The financial statements of the Branches are expressed in Arab Emirates Dirhams ('AED'), which is the functional currency of the Branches and the presentation currency for the financial statements.

In preparing the financial statements of the Branches, transactions in currencies other than the Branches' functional currency (foreign currencies) are recorded at the rates of exchange prevailing at the dates of the transactions. At the end of the reporting period, monetary items denominated in foreign currencies are retranslated at the rates prevailing at the end of the reporting period. Non-monetary items carried at fair value that are denominated in foreign currencies are retranslated at the rates prevailing at the date when the fair value was determined. Non-monetary items that are measured in terms of historical cost in a foreign currency are not retranslated.

Exchange differences are recognised in statement of profit or loss in the period in which they arise.

3. Significant accounting policies (continued)

Property and equipment

Property and equipment are stated at cost less accumulated depreciation and accumulated impairment loss, if any. Additions and subsequent expenditures are capitalised only to the extent that they enhance the future economic benefits expected to be derived from the assets.

Depreciation is determined using the straight-line method over the estimated useful lives of the respective assets, as follows:

	Years
Office equipment	3 - 5
Furniture and fittings	3 - 5
Vehicles	3
Leasehold improvements	5 - 7

The depreciable amount is the gross carrying amount, less the estimated residual value at the end of its useful economic life.

The useful lives, methods and the residual values underlying the calculation of depreciation of items of property and equipment are reviewed at each reporting date to take account of any change in circumstances.

An item of property and equipment is derecognised upon disposal or when no future economic benefits are expected to arise from the continued use of the asset. Any gain or loss arising on the disposal or retirement of an item of property and equipment is determined as the difference between the sales proceeds and the carrying amount of the asset and is recognised in the statement of profit or loss.

Gain or loss on disposal is determined by comparing the proceeds with the carrying amount and are recognised in the statement of profit or loss.

Capital work-in-progress is carried at cost, less any recognised impairment loss. Such properties are classified to the appropriate categories of property and equipment when completed and ready for intended use. Depreciation of these assets, on the same basis as other property assets, commences when the assets are ready for their intended use.

Intangible assets

Intangible assets acquired separately are measured on initial recognition at cost. Following initial recognition, intangible assets are carried at cost less any accumulated amortisation and any accumulated impairment losses. Additions and subsequent expenditures are capitalised only to the extent that they enhance the future economic benefits expected to be derived from the assets. Intangible assets with finite lives are amortised over the useful economic life and assessed for impairment whenever there is an indication that the intangible asset may be impaired. The amortisation period and the amortisation method for an intangible asset with a finite useful life is reviewed at least at each financial year end. Changes in the expected useful life or the expected pattern of consumption of future economic benefits embodied in the asset is accounted for by changing the amortisation period or method, as appropriate, and treated as changes in accounting estimates. The amortisation expense on intangible assets with finite lives is recognised in the statement of profit or loss in the expense category consistent with the function of the intangible asset.

Notes to the financial statements
for the year ended 31 December 2018 (continued)

3. Significant accounting policies (continued)

Impairment of tangible and intangible assets

At each reporting period, the Branches review the carrying amounts of its tangible and intangible assets to determine whether there is any indication that those assets have suffered an impairment loss. If any such indication exists, the recoverable amount of the assets is estimated in order to determine the extent of the impairment loss (if any). Where it is not possible to estimate the recoverable amount of an individual asset, the Branches estimate the recoverable amount of the cash-generating unit to which the asset belongs.

Recoverable amount is the higher of fair value less costs to sell and value in use. 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 for which the estimates of future cash flows have not been adjusted.

If the recoverable amount of an asset (or cash-generating unit) is estimated to be less than its carrying amount, the carrying amount of the asset (cash-generating unit) is reduced to its recoverable amount. An impairment loss is recognised in the statement of profit or loss, unless the relevant asset is carried at a revalued amount, in which case the impairment loss is treated as a revaluation decrease.

Where an impairment loss subsequently reverses, the carrying amount of the asset (cash-generating unit) is increased to the revised estimate of its recoverable amount, such that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognised for the asset (cash-generating unit) in prior years. A reversal of an impairment loss is recognised in the statement of profit or loss, unless the relevant asset is carried at revalued amount, in which case the reversal of the impairment loss is treated as a revaluation increase.

Employees' end-of-service benefits

Provision for employees' end-of-service indemnity is made based on current remuneration and cumulative years of service at the end of each reporting period. The provision is made in accordance with the Branches' policy which is not less than the liability arising under the U.A.E. labour laws.

Pension and national insurance contributions for U.A.E. citizens are made by the Branches in accordance with Federal Law No.7 of 1999.

Operating leases

Leases of assets under which all the risks and rewards of ownership are effectively retained by the lessor are classified as operating leases. Where the Branches is the lessee and the leased assets are not recognised on reporting period, rentals payable and receivable under operating leases are accounted for on a straight-line basis over the periods of the leases.

Notes to the financial statements
for the year ended 31 December 2018 (continued)

3. Significant accounting policies (continued)

Income tax

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

Current tax is the expected tax payable or receivable on the taxable profit or loss for the year, calculated using tax rates enacted or substantively enacted at the reporting date. The Branches provide for potential current tax liabilities that may arise on the basis of the amounts expected to be paid to the tax authorities.

Deferred tax is recognised on temporary differences between the carrying amounts of assets and liabilities in the statement of financial position and the amounts attributed to such assets and liabilities for tax purposes. Deferred tax liabilities are generally recognised for all taxable temporary differences and deferred tax assets are recognised to the extent that it is probable that future taxable profits will be available against which deductible temporary differences can be utilised. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no long probable that the related tax benefit will be realised.

Deferred tax is calculated using the tax rates expected to apply in the periods in which the assets will be realised or the liabilities settled, based on tax rates and laws enacted, or substantively enacted, by the reporting date.

Provisions

Provisions are recognised when the Branches have a present obligation (legal or constructive) as a result of a past event, it is probable that the Branches will be required to settle the obligation, and a reliable estimate can be made of the amount of the obligation.

The amount recognised as a provision is the best estimate of the consideration required to settle the present obligation at the end of the reporting period, taking into account the risks and uncertainties surrounding the obligation. When a provision is measured using the cash flows estimated to settle the present obligation, its carrying amount is the present value of those cash flows.

When some or all of the economic benefits required to settle a provision are expected to be recovered from a third party, a receivable is recognised as an asset if it is virtually certain that reimbursement will be received and the amount of the receivable can be measured reliably.

Present obligations arising under onerous contracts are recognised and measured as provisions. An onerous contract is considered to exist where the Branches have a contract under which the unavoidable costs of meeting the obligations under the contract exceed the economic benefits expected to be received from the contract.

Acceptances

Acceptances are recognised as financial liability in the 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.

Notes to the financial statements
for the year ended 31 December 2018 (continued)

3. Significant accounting policies (continued)

Documentary credits

Documentary credits, issued on behalf of the customers of the Branches, are contracts whereby the Branches guarantee to pay on behalf of the customers' money to the holder for goods supplied to the customers of the Branches. The payment would be made only on submission of documents as prescribed in the credit by the holder through his bank.

The income received for the issue of the credit and subsequent handling of the bills under the credit is recognised as fee income as and when received.

Commitments to extend credit

These are firm commitments made by the Branches to its customers to extend credit as per the terms of the agreement and are considered as an off balance sheet liability.

4. Critical accounting judgments and key sources of estimation uncertainty

In the application of the Branches' accounting policies, which are described in Note 3, the management is required to make judgments, estimates and assumptions about the carrying amounts of assets and liabilities that are not readily apparent from other sources. The estimates and associated assumptions are based on historical experience and other factors that are considered to be relevant. Actual results may differ from these estimates.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised if the revision affects only that period, or in the period of the revision and future periods if the revision affects both current and future periods. Significant areas where management has used estimates, assumptions or exercised judgments are as follows:

Business model assessment

The Branches makes an assessment of the objective of a business model in which an asset is held at a portfolio level because this best reflects the way the business is managed and information is provided to management. The information considered includes:

- The stated policies and objectives for the portfolio and the operation of those policies in practice;
- How the performance of the portfolio is evaluated and reported to the Branches' management;
- The risks that affect the performance of the business model (and the financial assets held within that business model) and how those risks are managed;
- How managers of the business are compensated (e.g. whether compensation is based on the fair value of the assets managed or the contractual cash flows collected); and
- The frequency, volume and timing of sales in prior periods, the reasons for such sales and its expectations about future sales activity. However, information about sales activity is not considered in isolation, but as part of an overall assessment of how the Branches' stated objective for managing the financial assets is achieved and how cash flows are realised.

Financial assets that are held for trading or managed and whose performance is evaluated on a fair value basis are measured at FVTPL because they are neither held to collect contractual cash flows nor held both to collect contractual cash flows and to sell financial assets.

Notes to the financial statements
for the year ended 31 December 2018 (continued)

4. Critical accounting judgments and key sources of estimation uncertainty (continued)

Assessment whether contractual cash flows are solely payments of principal and interest

For the purposes of this assessment, 'principal' is defined as the fair value of the financial asset on initial recognition. 'Interest' is defined as consideration for the time value of money and for the credit risk associated with the principal amount outstanding during a particular period of time and for other basic lending risks and costs (e.g. liquidity risk and administrative costs), as well as profit margin.

In assessing whether the contractual cash flows are solely payments of principal and interest ("the SPPI test"), the Branches considers the contractual terms of the instrument. This includes assessing whether the financial asset contains a contractual term that could change the timing or amount of contractual cash flows such that it would not meet this condition. In making the assessment, the Branches considers contingent events that would change the amount and timing of cash flows, prepayment and extension terms, terms that limit the Branches' claim to cash flows from specified assets and features that modify consideration of the time value of money. Instruments failing SPPI will be measured at FVTPL.

Inputs, assumptions and techniques used for estimating impairment

Significant increase in credit risk

When determining whether the risk of default on a financial instrument has increased significantly since initial recognition, the Branches considers reasonable and supportable information that is relevant and available without undue cost or effort. This includes both quantitative and qualitative information and analysis including internal credit risk grading system, external risk ratings, where available, delinquency status of accounts, credit judgement and, where possible, relevant historical experience. The Branches may also determine that an exposure has undergone a significant increase in credit risk based on particular qualitative indicators that it considers are indicative of such and whose effect may not otherwise be fully reflected in its quantitative analysis on a timely basis.

In determining whether credit risk has increased significantly since initial recognition following criteria's are considered:

i. Two notches downgrade for ratings from Aaa to Baa or one notch downgrade for ratings from Ba to Caa.
ii. Facilities restructured during previous twelve months.
iii. Facilities overdue by 30 days as at the reporting date.

Credit risk grades

Credit risk grades are defined using qualitative and quantitative factors that are indicative of risk of default. These factors vary depending on the nature of the exposure and the type of borrower. Exposures are subject to on-going monitoring, which may result in an exposure being moved to a different credit risk grade.

Generating the term structure of Probability of Default (PD)

The Branches employs statistical models to analyse the data collected and generate estimates of PD of exposures and how these are expected to change as a result of the passage of time. This analysis includes the identification and calibration of relationships between changes in default rates and changes in key macro-economic factors, across various geographies in which the Branches has exposures.

4. Critical accounting judgments and key sources of estimation uncertainty (continued)

Generating the term structure of Probability of Default (PD) (continued)

Renegotiated financial assets

The contractual terms of a loan may be modified for a number of reasons, including changing market conditions, customer retention and other factors not related to a current or potential credit deterioration of the customer. An existing loan whose terms have been modified may be derecognised and the renegotiated loan recognised as a new loan at fair value. Where possible, the Branches seeks to restructure loans rather than to take possession of collateral, if available. This may involve extending the payment arrangements and documenting the agreement of new loan conditions. Management continuously reviews renegotiated loans to ensure that all criteria are met and that future payments are likely to occur.

The accounts which are restructured due to credit reasons in past 12 months will be classified under Stage 2.

Definition of default

The Branches considers a financial asset to be in default when:

- the borrower is unlikely to pay its credit obligations to the Branches in full, without recourse by the Branches to actions such as realising security (if any is held); or
- the borrower is past due more than 90 days on any material credit obligation to the Branches; or
- the borrower is rated 9 or 10.

In assessing whether a borrower is in default, the Branches also considers indicators that are:

- quantitative - e.g. overdue status and non-payment on another obligation of the same issuer to the Branches; and
- based on data developed internally and obtained from external sources.

Inputs into the assessment of whether a financial instrument is in default and their significance may vary over time to reflect changes in circumstances. The definition of default largely aligns with that applied by the Branches for regulatory capital purposes

Incorporating forward looking information increases the level of judgement as to how changes in these macroeconomic factors will affect the Expected Credit Loss (ECL) applicable to the stage 1 and stage 2 exposures which are considered as performing. The methodologies and assumptions involved, including any forecasts of future economic conditions, are reviewed periodically

Forward-looking information incorporated in the ECL models

The assessment of SICR and the calculation of ECL both incorporate forward-looking information. The Branches has performed historical analysis and identified the key economic variables impacting credit risk and expected credit losses for each portfolio.

The Branches employs statistical models to incorporate macro-economic factors on historical default rates. In the case that none of the macro-economic parameters are statistically significant or the results of forecasted PDs are too deviated from the present forecast of the economic conditions, qualitative PD overlay is used by management based on portfolio analysis.

Notes to the financial statements
for the year ended 31 December 2018 (continued)

4. Critical accounting judgments and key sources of estimation uncertainty (continued)

Forward-looking information incorporated in the ECL models (continued)

Incorporating forward looking information increases the level of judgement as to how changes in these macroeconomic factors will affect the ECL applicable to the stage 1 and stage 2 exposures. The methodologies and assumptions involved, including any forecasts of future economic conditions, are reviewed periodically.

These economic variables and their associated impact on the PD, EAD and LGD vary by financial instrument. Expert judgment has also been applied in this process. Forecasts of these economic variables (the "base economic scenario") are based on available information and include mean reversion approaches for long-term forecasts. The impact of these economic variables on the PD, EAD and LGD has been determined by performing statistical regression analysis to understand the impact changes in these variables have had historically on default rates and on the components of LGD and EAD.

5. Cash and balances with the Central Bank of the U.A.E.

	2018 **AED'000**	2017 AED'000
Cash on hand	**14,288**	15,324
Balances with the Central bank of the U.A.E.		
Current accounts	**139,850**	215,932
Statutory reserve	**76,623**	103,315
Certificates of deposit	**-**	230,000
	230,761	564,571

The Branches are required to maintain statutory reserve with the Central Bank of the U.A.E., which is not available for use in the day-to-day operations. Certificate of deposit held with the Central Bank of the U.A.E. have been matured during the year.

6. Related party transactions

The Branches enter into transactions with entities that fall within the definition of a related party in accordance with International Accounting Standard 24: *Related Party Disclosures*. Related parties comprise of Head Office and Ultimate Parent Company outside the U.A.E. Transactions with such related parties are made on substantially the same terms, as those prevailing at the same time for comparable transactions with external customers and parties.

The Branches maintain certain deposits with the Head Office and the Ultimate Parent Company and conducts banking transactions with them as part of its normal activities.

The Head Office provides administrative and management support to the Branches (Note 17) for which the Branches were charged a fee for the year ended 31 December 2018 of AED 2.2 million (2017: AED 1.9 million).

Notes to the financial statements
for the year ended 31 December 2018 (continued)

6. Related party transactions (continued)

	2018 AED'000	2017 AED'000
Due from related parties comprise:		
Current accounts		
Ultimate Parent Company	**286**	247
Head Office	**40,393**	16,829
Term placement /deposit		
Ultimate Parent Company	**91,725**	-
Head Office*	**21,596**	26,427
	154,000	43,503
Less: Impairment allowance (Note 18)	**(2)**	-
	153,998	43,503

* Term placement/deposit with the Head Office has maturity of less than 3 months and carry the interest rate of 0.09% p.a. (2017: 0.1% p.a.).

	2018 AED'000	2017 AED'000
Due to related parties comprise:		
Current accounts		
Ultimate Parent Company	**7,208**	3,009
Head Office	**1,754**	2,266
Term deposits*		
Ultimate Parent Company	-	110,175
Head Office	-	165,263
Entity under common control		
Qatar Capital Limited, State of Qatar	-	550
	8,962	281,263

* Term deposits from the Head Office and ultimate Parent Company had maturity of less than 3 months and carried the interest rate of 1.75%-2.5% p.a.

Notes to the financial statements
for the year ended 31 December 2018 (continued)

6. Related party transactions (continued)

Profit for the year includes related party transactions as follows:

	2018 AED'000	2017 AED'000
Interest income	**831**	855
Interest expense	**4,213**	740
Head Office charges (Note 17)	**2,226**	1,891

	2018 AED'000	2017 AED'000
Key management personnel compensation:		
Salaries, bonuses and other benefits	**2,951**	4,525

7. Deposits and balances due from banks and financial institutions

	2018 AED'000	2017 AED'000
Due from banks and financial institutions outside the U.A.E.	**6,727**	14,945
Due from banks and financial institutions in the U.A.E.	**55,907**	693
	62,634	15,638
Less: Impairment allowance (Note 18)	**(7)**	-
	62,627	15,638

8. Investment securities

	2018 AED'000	2017 AED'000
Investments at amortized cost	**97,226**	154,076
Less: Impairment allowance (Note 18)	**(691)**	-
	96,535	154,076

Notes to the financial statements
for the year ended 31 December 2018 (continued)

8. Investment securities (continued)

Gross investments securities by geographic concentration are as follows:

	2018 AED'000	2017 AED'000
- Within the U.A.E.	**76,812**	115,160
- Outside the U.A.E.	**20,414**	38,916
	97,226	154,076

The analysis of gross investments securities by industry sector is as follows:

	2018 AED'000	2017 AED'000
Government and public sector	**60,274**	98,614
Financial institutions	**36,952**	55,462
	97,226	154,076

9. Loans and advances to customers

a) Loans and advances to customers comprise of the following:

	2018 AED'000	2017 AED'000
Loans and advances	**1,551,167**	2,094,557
Less: Impairment allowance (Note 18)	**(168,352)**	(248,062)
	1,382,815	1,846,495

At 31 December 2018, the fair value of collateral held against loans and advances to customers was AED 1,819 million (2017: AED 1,723 million) an analysis of which is provided in Note 26.

b) The movement of the allowance for impairment of loans and advances to customers is as follows:

	2018 AED'000	2017 AED'000
At 1 January	**248,062**	234,999
Impact of adoption of IFRS 9	**(1,153)**	-
Impairment allowance for the year	**121,619**	107,098
Amounts written off during the year	**(149,865)**	(49,653)
Reversal of impairment allowance	**(13,308)**	(39,700)
Recoveries during the year	**(37,003)**	(4,682)
At 31 December	**168,352**	248,062

Impairment allowance for the year includes AED 33.2 million of suspended interest (2017: AED 29.7 million) and 3.4 million recoveries of suspended interest during the year (2017: AED 0.4 million).

Notes to the financial statements
for the year ended 31 December 2018 (continued)

9. Loans and advances to customers (continued)

c) Analysis of gross loans and advances to customers by class:

	2018 AED'000	2017 AED'000
Corporate lending	**838,054**	1,158,290
Small business lending	**436,607**	595,441
Retail lending	**276,506**	340,826
	1,551,167	2,094,557

d) Gross loans and advances by geographical area were as follows:

	2018 AED'000	2017 AED'000
Within the U.A.E.	**1,247,449**	1,768,637
Outside the U.A.E.	**303,718**	325,920
	1,551,167	2,094,557

e) Gross loans and advances by industry were as follows:

	2018 AED'000	2017 AED'000
Real estate	**424,746**	522,298
Services	**308,376**	284,499
Transport and communication	**230,288**	93,374
Manufacturing	**179,679**	393,340
Wholesale and retail trade	**168,376**	474,223
Financial Institutions	**136,664**	81,064
Construction	**49,726**	157,662
Personal loans	**34,992**	62,173
Electricity	**18,320**	25,924
	1,551,167	2,094,557

10. Other assets

	2018 AED'000	2017 AED'000
Deferred tax asset (i)	**23,706**	38,877
Interest receivable	**12,529**	10,389
Assets under acceptances	**10,992**	22,940
Prepaid expenses	**2,596**	2,744
Others	**10,202**	5,303
	60,025	80,253

Notes to the financial statements
for the year ended 31 December 2018 (continued)

10. Other assets (continued)

i) The movement in deferred tax asset during the year was as follows:

	2018 AED'000	2017 AED'000
Balance at the beginning of the year	**38,877**	35,063
Net movement during the year	**(15,171)**	3,814
Balance at the end of the year	**23,706**	38,877

Tax authorities in the U.A.E. review the tax calculation of the Branches on a periodical basis. As a result of the review, the authorities rejected to recognise impairment allowances for loans and advances as an expense for certain customers, based on their assessment. These rejected amounts create a temporary difference in the tax base resulting in deferred tax assets, which will be utilised when tax authorities accept to recognise the allowances as an expense in the statement of profit or loss.

Notes to the financial statements
for the year ended 31 December 2018 (continued)

10. Other assets (continued)

	Opening balance AED'000	**Additions & written off AED'000**	**Release AED'000**	**Ending balance AED'000**	**Deferred tax assets as of 31 December 2018 AED'000**	**Movement in statement of profit or loss during the year AED'000**	**Deferred tax assets as of 31 December 2017 AED'000**
Impairment allowance for loans and advances to customers	**162,257**	**(32,597)**	**(33,483)**	**96,177**	**19,235**	**(13,216)**	**32,451**
Suspended interest	**32,129**	**(7,708)**	**(2,070)**	**22,351**	**4,471**	**(1,955)**	**6,426**
	194,386	**(40,305)**	**(35,553)**	**118,528**	**23,706**	**(15,171)**	**38,877**

	Opening balance AED'000	Additions AED'000	Release AED'000	Ending balance AED'000	Deferred tax assets as of 31 December 2017 AED'000	Transferred to statement of profit or loss during the year AED'000	Deferred tax assets as of 31 December 2016 AED'000
Impairment allowance for loans and advances to customers	157,524	33,745	(29,012)	162,257	32,451	946	31,505
Suspended interest	17,789	14,537	(197)	32,129	6,426	2,868	3,558
	175,313	48,282	(29,209)	194,386	38,877	3,814	35,063

Notes to the financial statements
for the year ended 31 December 2018 (continued)

11. Property and equipment

	Office equipment AED'000	Furniture and fittings AED'000	Vehicles AED'000	Leasehold improvements AED'000	Capital work-in-progress AED'000	Total AED'000
Cost						
At 1 January 2017	6,247	1,165	425	5,627	313	13,777
Additions during the year	16	-	-	-	-	16
Transfer of CWIP	313	-	-	-	(313)	-
Disposals during the year	(156)	-	-	(896)	-	(1,052)
At 31 December 2017	6,420	1,165	425	4,731	-	12,741
Additions during the year	421	4	-	40	-	465
Transfer of CWIP	-	-	-	-	-	-
Disposals during the year	(32)	-	-	116	-	84
At 31 December 2018	**6,809**	**1,169**	**425**	**4,887**	**-**	**13,290**
Accumulated depreciation						
At 1 January 2017	4,113	1,146	402	4,802	-	10,463
Charge for the year	1,056	7	23	245		1,331
Eliminated on disposals	(156)	-	-	(417)	-	(573)
At 31 December 2017	5,013	1,153	425	4,630	-	11,221
Charge for the year	1,015	8	-	73	-	1,096
Eliminated on disposals	(32)	-	-	116	-	84
At 31 December 2018	**5,996**	**1,161**	**425**	**4,819**	**-**	**12,401**
Carrying amount						
At 31 December 2018	**813**	**8**	**-**	**68**	**-**	**889**
At 31 December 2017	1,407	12	-	101	-	1,520

Notes to the financial statements for the year ended 31 December 2018 (continued)

12. Intangible assets

	Software AED'000	Intangibles work-in-progress AED'000	Total AED'000
Cost			
At 1 January 2017	17,422	2,928	20,350
Additions	969	-	969
Transfers	2,862	(2,862)	-
At 31 December 2017	21,253	66	21,319
Additions	828	88	916
Transfers	(3,637)	(78)	(3,715)
At 31 December 2018	**18,444**	**76**	**18,520**
Accumulated amortization			
At 1 January 2017	12,259	-	12,259
Charge for the year	2,439	-	2,439
At 31 December 2017	14,698	-	14,698
Charge for the year	2,157	-	2,157
Transfers	(3,641)	-	(3,641)
At 31 December 2018	**13,214**	-	**13,214**
Carrying amount			
At 31 December 2018	**5,230**	**76**	**5,306**
At 31 December 2017	6,555	66	6,621

13. Deposits and balances due to banks and financial institutions

	2018 AED'000	2017 AED'000
Due to banks and financial institutions outside the U.A.E.	**3,363**	212,869
	3,363	212,869

Notes to the financial statements
for the year ended 31 December 2018 (continued)

14. Customers' deposits

	2018 AED'000	2017 AED'000
Current accounts	**418,138**	517,989
Saving accounts	**15,775**	10,634
Time deposits	**772,219**	874,668
Margin accounts	**96,896**	119,743
	1,303,028	1,523,034

Time deposits held under lien as security for loans and advances (funded and unfunded) as at 31 December 2018 amounted to AED 292 million (2017: AED 376 million).

	2018 AED'000	2017 AED'000
Customers' deposits by geographic area were as follows:		
- Within the U.A.E.	**1,278,053**	1,508,055
- Outside the U.A.E.	**24,975**	14,979
	1,303,028	1,523,034

15. Other liabilities

	2018 AED'000	2017 AED'000
Provision for employees' end-of-service indemnity (i)	**12,495**	13,257
Banker's draft and other	**11,336**	16,485
Liabilities under acceptances	**10,992**	22,940
Interest payable	**6,625**	4,699
Impairment loss allowance on commitments and financial guarantees	**2,603**	-
Income tax provision (Note 19)	**-**	8,642
	44,051	66,023

i) The movements in provision for end-of-service benefits during the year were as follows:

	2018 AED'000	2017 AED'000
Balance at the beginning of the year	**13,257**	18,328
Charge for the year	**1,184**	1,355
Payments during the year	**(1,946)**	(6,426)
Balance at the end of the year	**12,495**	13,257

Notes to the financial statements
for the year ended 31 December 2018 (continued)

16. Assigned capital and statutory reserve

(a) Assigned capital

During the year, the Branches maintained the assigned capital at AED 375 million.

(b) Statutory reserve

In accordance with Article (82) of Union Law No. 10 of 1980, Federal Commercial Companies Law, the Branches has to establish a statutory reserve by appropriation of 10% of net profit for each year until the reserve equals 50% of the assigned capital. This reserve is not available for distribution.

17. General and administrative expenses

	2018 **AED'000**	2017 AED'000
Salaries and employees related expenses	**22,124**	29,707
Depreciation and amortisation	**3,253**	3,770
Head Office charges (Note 6)	**2,226**	1,891
Other	**13,366**	12,444
	40,969	47,812

Notes to the financial statements
for the year ended 31 December 2018 (continued)

18. Allowance for impairment, net

18.1.The following tables show reconciliations from the opening to the closing balance of the loss allowance by class of financial instruments including net impairment loss on financial assets for the year. Comparative amounts represent allowance account for credit losses and reflect measurement basis under IAS 39.

2018	Loans and advances to customers AED'000	Investment securities AED'000	Financial commitments and guarantees AED'000	*Other financial assets AED'000	Total AED'000
At 1 January	248,062	-	-	-	248,062
Impact of adoption of IFRS 9	(1,153)	1,106	45	2	-
Opening balance - restated	246,909	1,106	45	2	248,062
Net impairment charge for the year	88,401	(415)	2,558	7	90,551
Reversal of impairment allowance	(13,308)	-	-	-	(13,308)
Recoveries during the year	(33,591)	-	-	-	(33,591)
Allowance for impairment, net	**41,502**	**(415)**	**2,558**	**7**	**43,652**
Interest in suspense net of recoveries	29,806	-	-	-	29,806
Amounts written off during the year	(149,865)	-	-	-	(149,865)
	168,352	**691**	**2,603**	**9**	**171,655**
2017					
At 1 January	234,999	-	-	-	234,999
Net impairment charge for the year	77,389	-	-	-	77,389
Reversal of impairment allowance	(39,700)	-	-	-	(39,700)
Recoveries during the year	(4,312)	-	-	-	(4,312)
Allowance for impairment, net	33,377	-	-	-	33,377
Interest in suspense net of recoveries	29,339	-	-	-	29,339
Amounts written off during the year	(49,653)	-	-	-	(49,653)
	248,062	-	-	-	248,062

Notes to the financial statements
for the year ended 31 December 2018 (continued)

18. Allowance for impairment (continued)

18.2 Allocation of impairment allowance as of 31 December 2018 and 2017 are as follows:

2018	Stage 1 AED'000	Stage 2 AED'000	Stage 3 AED'000	Total AED'000
Loans and advances to customers	8,817	12,501	147,034	168,352
Investments securities	691	-	-	691
Financial commitments and guarantees	1,771	832	-	2,603
*Other financial assets	6	3	-	9
Total	**11,285**	**13,336**	**147,034**	**171,655**

2017	Stage 1 AED'000	Stage 2 AED'000	Stage 3 AED'000	Total AED'000
Loans and advances to customers	23,381	17,783	205,745	246,909
Investments securities	1,050	56	-	1,106
Financial commitments and guarantees	45	-	-	45
*Other financial assets	1	1	-	2
Total	24,477	17,840	205,745	248,062

*This represents impairment charge on due from related parties and deposits and balances due from banks and financial institutions.

The CBUAE issued its IFRS 9 guidance on 30 April 2018 via notice No.: CBUAE/BSD/2018/458 addressing various implementation challenges and practical implications for banks adopting IFRS 9 in the UAE ("the Guidance").

Pursuant to clause 6.4 of the Guidance, the reconciliation between general and specific provision under Circular 28/2010 of CBUAE and IFRS 9 is as follows:

	2018 AED'000
Impairment reserve: General	
General provisions under Circular 28/2010 of CBUAE	24,621
Less: Stage 1 and Stage 2 provisions under IFRS 9	24,621
General provision transferred to the regulatory impairment reserve	-

Notes to the financial statements
for the year ended 31 December 2018 (continued)

18. Allowance for impairment (continued)

Impairment reserve: Specific	
Specific provisions under Circular 28/2010 of CBUAE	**147,034**
Less: Stage 3 provisions under IFRS 9	**147,034**
Specific provision transferred to the regulatory impairment reserve	**-**
Total provision transferred to the regulatory impairment reserve	**-**

In the case where provisions under IFRS 9 exceed provisions under CBUAE, no amount shall be transferred to the impairment reserve.

19. Income tax - net

The Branches are subject to taxation at the rate of 20% of the taxable income for the year. The taxable income is calculated after adding back certain provisions to the net profit before taxation, which management believes are likely to be disallowed as deductions by the tax authorities:

Income tax expense for the year shown in the statement of profit or loss represents the following:

	2018 AED'000	2017 AED'000
In respect of the current year	**(4,931)**	7,060
In respect of the prior year	**-**	122
	(4,931)	7,182
Deferred tax (Note 10)	**15,171**	(3,814)
Total income tax expenses recognised in the current year	**10,240**	3,368

(a) The movements in income tax provision during the year were as follows:

	2018 AED'000	2017 AED'000
Balance, at the beginning of the year	**8,642**	18,583
In respect of the current year	**-**	8,642
In respect of the prior year	**-**	122
Paid during the year	**(8,642)**	(18,705)
Balance, at the end of the year (note 15)	**-**	8,642

Notes to the financial statements
for the year ended 31 December 2018 (continued)

19. Income tax - net (continued)

(b) Relationship between tax expense and accounting profit:

	2018 AED'000	2017 AED'000
Profit before tax	14,304	31,827
Income not subject to tax	-	(1,219)
Items not allowed as tax deductions	(66,320)	5,257
Adjustment of carry forward tax losses*	27,255	-
Others	107	(564)
Taxable (loss)/profit	(24,654)	35,301
Income tax rate	20%	20%
Income tax (income)/expense	(4,931)	7,060

*The recognition of deferred tax assets is subject to specific requirements of IAS 12 *"Income Taxes"*. These require a deferred tax asset to be recognized to the extent that it is probable that the deferred tax asset will be recovered in near future. However, management has assessed that the tax losses realized in one of the Branch amounting to AED 27.5 million will be difficult to recover within 2 years as allowed by the Tax Authorities in UAE, hence, will not recognize a deferred tax amount on subject losses.

20. Cash and cash equivalents

	2018 AED'000	2017 AED'000
Cash and balances with the Central Bank of the U.A.E.	154,138	231,256
Cash reserves and certificates of deposit with the Central Bank of the U.A.E.	76,623	333,315
Due from related parties	154,000	43,503
Due from banks and financial institutions	62,634	15,638
	447,395	623,712
Due to related parties	(8,962)	(281,263)
Due to banks and financial institutions	(3,363)	(212,869)
Statutory reserve and certificate of deposit with the Central Bank of the U.A.E.	(76,623)	(103,315)
Total cash and cash equivalents	358,447	26,265

Notes to the financial statements
for the year ended 31 December 2018 (continued)

21. Concentrations of assets, liabilities, equity and off balance sheet items

	31 December 2018			31 December 2017		
	Assets AED'000	**Liabilities and equity AED'000**	**Off balance sheet items AED'000**	Assets AED'000	Liabilities and equity AED'000	Off balance sheet items AED'000
Geographic regions						
U.A.E.	**1,643,106**	**1,946,825**	**700,275**	2,368,782	2,196,454	947,686
Other Middle East countries	**259,955**	**39,113**	**16,689**	267,565	320,001	39,057
O.E.C.D.	**89,895**	**6,447**	**11,419**	76,330	193,266	19
Other	**-**	**571**	**-**	-	2,956	-
Total	**1,992,956**	**1,992,956**	**728,383**	2,712,677	2,712,677	986,762
Industry Sector						
Government and public sector	**294,030**	**862**	**-**	673,785	50,426	-
Commercial and business	**963,401**	**811,016**	**696,638**	1,421,808	1,061,366	946,947
Personal	**276,459**	**334,216**	**219**	340,639	372,593	321
Financial institutions	**389,550**	**182,854**	**31,526**	195,667	555,721	39,494
Other	**69,516**	**664,008**	**-**	80,778	672,571	-
Total	**1,992,956**	**1,992,956**	**728,383**	2,712,677	2,712,677	986,762

Notes to the financial statements
for the year ended 31 December 2018 (continued)

22. Classification of financial assets and financial liabilities

The table below sets out the Branches' classification of each class of financial assets and financial liabilities and their carrying amounts as at 31 December 2018:

	Amortized cost 2018 AED'000	Amortized cost 2017 AED'000
Financial assets		
Cash and balances with the Central Bank of the U.A.E.	**230,761**	564,571
Due from related parties	**153,998**	43,503
Due from banks and financial institutions	**62,627**	15,638
Investments securities	**96,535**	154,076
Loans and advances to customers	**1,382,815**	1,846,495
Other assets	**46,437**	54,569
Total	**1,973,173**	2,678,852
Financial liabilities		
Due to banks and financial institutions	**3,363**	212,869
Customer deposits	**1,303,028**	1,523,034
Due to related parties	**8,962**	281,263
Other liabilities	**17,961**	21,184
Total	**1,333,314**	2,038,350

Notes to the financial statements
for the year ended 31 December 2018 (continued)

23. Liquidity profile

(a) The following table summarises the maturity profile of the Branches' assets and liabilities based on contractual repayment arrangements. The contractual maturities of assets and liabilities have been determined on the basis of the remaining period at the reporting date to the contractual maturity date:

	Less than 3 months AED'000	3 Months to 1 year AED'000	Over 1 year AED'000	Total AED'000
2018				
Assets				
Cash and balances with the Central Bank of the U.A.E.	154,138	-	76,623	230,761
Due from related parties	153,998	-	-	153,998
Due from banks and financial institutions	62,627	-	-	62,627
Investments securities	-	2,077	94,458	96,535
Loans and advances to customers	290,842	205,927	886,046	1,382,815
Other assets	47,967	1,094	10,964	60,025
Property and equipment	-	-	889	889
Intangibles	-	-	5,306	5,306
Total assets	709,572	209,098	1,074,286	1,992,956
Liabilities and equity				
Due to banks and financial institutions	3,363	-	-	3,363
Customers' deposits	937,422	365,606	-	1,303,028
Due to related parties	8,962	-	-	8,962
Other liabilities	31,288	267	12,496	44,051
Equity	-	-	633,552	633,552
Total liabilities and equity	981,035	365,873	646,048	1,992,956

Notes to the financial statements
for the year ended 31 December 2018 (continued)

23. Liquidity profile (continued)

	Less than 3 months AED'000	3 Months to 1 year AED'000	Over 1 year AED'000	Total AED'000
2017				
Assets				
Cash and balances with the Central Bank of the U.A.E.	461,256	-	103,315	564,571
Due from related parties	43,503	-	-	43,503
Due from banks and financial institutions	15,638		-	15,638
Investments securities	-	57,392	96,684	154,076
Loans and advances to customers	547,457	276,113	1,022,925	1,846,495
Other assets	20,027	18,004	42,222	80,253
Property and equipment	-	-	1,520	1,520
Intangibles	-	-	6,621	6,621
Total assets	1,087,881	351,509	1,273,287	2,712,677
Liabilities and equity				
Due to banks and financial institutions	187,162	-	25,707	212,869
Customers' deposits	1,145,329	377,705	-	1,523,034
Due to related parties	281,263	-	-	281,263
Other liabilities	49,853	2,913	13,257	66,023
Equity	-	-	629,488	629,488
Total liabilities and equity	1,663,607	380,618	668,452	2,712,677

Notes to the financial statements
for the year ended 31 December 2018 (continued)

23. Liquidity profile (continued)

(b) Liquidity profile - undiscounted cash flows of the financial liabilities

The following table details the Branches contractual maturity for non-derivative financial liabilities. The table below is the undiscounted cash flow of financial liabilities based on the earliest date on which the Branches can be required to pay.

	Weighted average effective interest rate %	**Less than 3 months AED'000**	**3 Months to 1 year AED'000**	**Over 1 year AED'000**	**Total AED'000**
2018					
Financial liabilities					
Due to banks and financial institutions	**2.4**	**3,363**	**-**	**-**	**3,363**
Customers' deposits	**1.4**	**940,309**	**375,042**	**116**	**1,315,467**
Due to related parties	**2.4**	**8,962**	**-**	**-**	**8,962**
Other liabilities	**-**	**31,288**	**267**	**12,496**	**44,051**
Total		**983,922**	**375,309**	**12,612**	**1,371,843**
2017					
Financial liabilities					
Due to banks and financial institutions	1.2	187,359	26,303	-	213,662
Customers' deposits	1.5	1,146,325	382,492	329	1,529,146
Due to related parties	1.2	281,638	-	-	281,638
Other liabilities	-	49,853	2,913	13,257	66,023
Total		1,665,175	411,708	13,586	2,090,469

24. Fair value of financial instruments

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, regardless of whether that price is directly observable or estimated using another valuation technique. In estimating the fair value of an asset or a liability, the Branches take into account the characteristics of the asset or liability if market participants would take those characteristics into account when pricing the asset or liability at the measurement date.

In addition, for financial reporting purposes, fair value measurements are categorised into Level 1, 2 or 3 based on the degree to which the inputs to the fair value measurements are observable and the significance of the inputs to the fair value measurement in its entirety, which are described as follows:

- Level 1 inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities that the entity can access at the measurement date;
- Level 2 inputs are inputs, other than quoted prices included within Level 1, that are observable for the asset or liability, either directly or indirectly; and
- Level 3 inputs are unobservable inputs for the asset or liability.

Valuation techniques and assumptions applied for the purposes of measuring fair value

The fair values of financial assets and financial liabilities are determined as follows.

- The fair values of financial assets and financial liabilities with standard terms and conditions and traded on active liquid markets are determined with reference to quoted market prices; and
- The fair values of other financial assets and financial liabilities are determined in accordance with generally accepted pricing models based on discounted cash flow analysis using prices from observable current market transactions and dealer quotes for similar instruments.

Fair value of the Branches' financial assets that are measured at amortised cost on recurring basis

Some of the Branches' financial assets are measured at amortised cost at the end of the reporting period. Except as detailed in the following table, the management considers that the carrying amounts of financial assets and financial liabilities recognised in the financial statements approximate their fair values.

	Carrying Amount AED'000	**Fair value**			
		Level 1 AED'000	**Level 2 AED'000**	**Level 3 AED'000**	**Total AED'000**
2018					
Financial assets					
At amortized cost	**96,535**	**92,985**	**-**	**2,092**	**95,077**
2017					
Financial assets					
Held to maturity investments	154,076	152,371	-	2,232	154,603

Notes to the financial statements
for the year ended 31 December 2018 (continued)

25. Capital management

The Branches' lead regulator, the Central Bank of the U.A.E., sets and monitors regulatory capital requirements.

The Branches' objectives when managing capital are:

- To safeguard the Branches' ability to continue as a going concern and to increase returns for shareholders; and
- To comply with regulatory capital requirements set by the Central Bank of the U.A.E.

In implementing current capital requirements, the Branches calculates its capital adequacy ratio in accordance with the guidelines issued by the Central Bank of the U.A.E. that essentially prescribe that this is a ratio of capital to risk weighted assets.

Regulatory capital

The Central Bank of U.A.E. sets and monitors capital requirements for the Branches as a whole.

Effective from 2017, the capital is computed using the Basel III framework of the Basel Committee on Banking Supervision ('Basel Committee'), after applying the amendments advised by the Central Bank of U.A.E., within national discretion. The Basel III framework, is structured around three 'pillars': minimum capital requirements, supervisory review process and market discipline.

Minimum Capital Requirements

The Central Bank of U.A.E. issued Basel III capital regulations, which came into effect from 1 February 2017 introducing minimum capital requirements at three levels, namely Common Equity Tier 1 ('CET1'), Additional Tier 1 ('AT1') and Total Capital.

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

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

The Branches' capital base is divided into three main categories, namely CET1, AT1 and Tier 2 ('T2'), depending on their characteristics.

- CET1 capital is the highest quality form of capital, comprising share capital, share premium, legal, statutory and other reserves, retained earnings, after deductions for intangibles and other regulatory adjustments relating to items that are included in equity but are treated differently for capital adequacy purposes under 'CBUAE' guidelines.
- AT 1 capital comprises eligible non-common equity capital instruments.
- T2 capital comprises collective impairment allowance.

25. Capital management (continued)

Regulatory capital **(continued)**

Various limits are applied to elements of the capital base:

- Tier 2 capital cannot exceed 67% of tier 1 capital;
- Tier 1 capital must be a minimum of 7% of risk weighted assets; and
- Qualifying subordinated capital cannot exceed 50% of tier 1 capital.

The Branches assets are risk weighted as to their relative credit, market, and operational risk. Credit risk includes both on and off-balance sheet risks. Market risk is defined as the risk of losses in on and off-balance sheet positions arising from movements in market prices and includes interest rate risk, foreign exchange risk, equity exposure risk, and commodity risk. Operational risk is defined as the risk of loss resulting from inadequate or failed internal processes, people or systems, or from external events.

Capital adequacy and the use of regulatory capital are monitored on a regular basis by the Branch's management, employing techniques based on the guidelines developed by the Basel Committee and the Central Bank of U.A.E.

No changes have been made to the objectives, policies and processes from the previous year. However, they are under constant review by the management. During the years ended 31 December 2018 and 2017, the Branches complied in full with all its externally imposed capital requirements.

During the years ended 31 December 2018 and 2017, all banks operating in the U.A.E. were required to maintain a capital adequacy ratio at 12.375% and 11.75% inclusive of capital conservation buffer respectively. The Branches is computing and reporting Basel III ratios in accordance with guidelines of the Central Bank of U.A.E.

25. Capital management (continued)

Regulatory capital (continued)

The Branches' regulatory capital position is as follows:

	2018 AED'000	2017 AED'000
Tier 1 capital		
Assigned capital	**375,000**	375,000
Statutory reserve	**55,758**	55,352
Retained earnings	**202,794**	199,136
Less: Regulatory deductions	**(5,306)**	(6,621)
Total	**628,246**	622,867
Tier 2 capital		
Collective provision for impairment	**20,517**	27,931
Total capital base	**648,763**	650,798
Risk-weighted assets		
Credit risk	**1,641,321**	2,234,454
Operational risk	**223,331**	264,589
Market risk	**175**	618
Total risk-weighted assets	**1,864,827**	2,499,661
Capital adequacy ratio	**34.79%**	26.04%
CET 1 Ratio	**33.69%**	24.94%

Capital allocation

The allocation of capital between specific operations and activities is, to a large extent, driven by optimisation of the return achieved on the capital allocated. The amount of capital allocated to each operation or activity is based on the inherent risk it carries. The process of allocating capital to specific operations and activities is undertaken independently of those responsible for the operation.

Although maximisation of the return on risk-adjusted capital is the principal basis used in determining how capital is allocated within the Branches to particular operations or activities, it is not the sole basis used for decision making. Account also is taken of synergies with other operations and activities, the availability of management and other resources, and the fit of the activity with the Branches' longer term strategic objectives. The Branches' policies in respect of capital management and allocation are reviewed regularly.

Notes to the financial statements
for the year ended 31 December 2018 (continued)

26. Risk management

The Branches have set up a strong risk management infrastructure supported by adoption of certain practices in the field of risk management to manage and monitor the following major risks arising out of its day to day operations:

- Credit risk
- Liquidity risk
- Market risk
- Interest rate risk
- Operational risk

Risk management framework

The Head Office of the Branches has overall responsibility for the oversight of the risk management framework. It has established detailed policies and procedures in this regard along with senior management committees to ensure adherence to the approved policies and close monitoring of different risks within the Branches.

The Credit, Risk and Management Committees work under the mandate of the Head Office to set up risk limits and manage the overall risk in the Branches.

These committees are responsible for developing risk policies in line with the Branches' appetite. Highly experienced and trained managers have delegated authority within the risk management framework to approve credit risk transactions and monitor market and operational risk.

Credit risk management

Policies relating to credit are reviewed and approved by the Branches' Risk Committee. All credit lines are approved centrally for the Branches. Loans in general, are secured by acceptable forms of collateral in order to mitigate credit risk. The Branches further limit risk through diversification of its assets by industry sectors.

All credit facilities are administered and monitored by the Credit Administration Department. Periodic reviews are conducted by Credit Examination teams from the Audit, Review and Compliance and obligors are risk graded based on criterion established in the Credit Policy Manual.

The Credit Committees are responsible for setting credit policy of the Branches. It also establishes industry caps, approves policy exceptions and conducts periodic portfolio reviews to ascertain portfolio quality.

Different credit underwriting procedures are followed for retail and commercial lending as described below.

26. Risk management (continued)

Credit risk management (continued)

Retail lending

Each retail credit application is considered for approval according to a product program, which is devised in accordance with guidelines set out in the product policy approved by the Branches' Credit Committee. Different authority levels are specified for approving product programs and exceptions thereto, and individual loans/credits under product programs. Each product program contains detailed credit criteria (such as customer demographics and income eligibility) and regulatory, compliance and documentation requirements, as well as other operating requirements.

Commercial lending

All credit applications for commercial lending are subject to the Branches' credit policies, underwriting standards and industry caps (if any) and to regulatory requirements, as applicable from time to time. The Branches do not lend to companies operating in industries that are considered by the Branches inherently risky and where specialised industry knowledge is required. In addition, the Branches set credit limits for all customers based on an evaluation of their creditworthiness.

All credit lines or facilities extended by the Branches are made subject to prior approval pursuant to a set of delegated credit authority limits approved by the Branches' Head Office.

Credit review procedures and loan classification

The Branches' Credit Risk Team (the 'CRT'), subjects the Branches' risk assets to an independent quality evaluation on a regular basis in conformity with the guidelines of the Central Bank of the U.A.E. and Branches' internal policies in order to assist in the early identification of accrual and potential performance problems. The CRT validates the risk ratings of all commercial clients, provides an assessment of portfolio risk by product and segment for retail customers and monitors observance of all approved credit policies, guidelines and operating procedures across the Branches.

If a credit is overdue for 90 days or more, interest is suspended and is not credited to income. Specific allowance for impairment of classified assets is made based on recoverability of outstanding and risk ratings of the assets.

The Branches also comply with IFRSs, in accordance with which it assesses the need for any impairment losses on its loan portfolio by calculating the net present value of the expected future cash flows for each loan or its recoverability based either on collateral value or the market value of the asset where such price is available.

26. Risk management (continued)

Impaired loans and advances

Impaired loans and advances are loans and advances for which the Branches determine that it is probable that it will be unable to collect all principal and interest due according to the contractual terms of the loan/advances agreement(s). These loans are graded fair, OLEM, substandard, doubtful or loss in the Branches' internal credit risk grading system.

Past due but not impaired loans

Loans and advances where contractual interest or principal payments are past due but the Branches believe that impairment is not appropriate on the basis of the level of security/collateral available and/or the stage of collection of amounts owed to the Branches.

Allowances for impairment

The Branches establish an allowance for impairment losses that represents its estimate of incurred losses in its loan portfolio. The main components of this allowance are a specific loss component that relates to individually significant exposures, and a collective loan loss allowance established for Branchess of homogeneous assets in respect of losses that have been incurred but have not been identified on loans subject to individual assessment for impairment.

Write-off policy

The Branches write off a loan (and any related allowances for impairment losses) when Branches' Credit Committee determines that the loan is uncollectible in whole or in part. This determination is reached after all avenues for recovery have failed. For smaller balance standardised loans, charge off decisions generally are based on a product specific past due status.

Inputs, assumptions and techniques used for estimating impairment

Significant increase in credit risk

When determining whether the risk of default on a financial instrument has increased significantly since initial recognition, the Branches considers reasonable and supportable information that is relevant and available without undue cost or effort. This includes both quantitative and qualitative information and analysis including internal credit risk grading system, external risk ratings, where available, delinquency status of accounts, credit judgement and, where possible, relevant historical experience. The Branches may also determine that an exposure has undergone a significant increase in credit risk based on particular qualitative indicators that it considers are indicative of such and whose effect may not otherwise be fully reflected in its quantitative analysis on a timely basis.

26. Risk management (continued)

Inputs, assumptions and techniques used for estimating impairment (continued)

Significant increase in credit risk (continued)

In determining whether credit risk has increased significantly since initial recognition following criteria's are considered:

i. Two notches downgrade for ratings from Aaa to Baa or one notch downgrade for ratings from Ba to Caa
ii. Facilities restructured during previous twelve months
iii. Facilities overdue by 30 days as at the reporting date

Credit risk grades

Credit risk grades are defined using qualitative and quantitative factors that are indicative of risk of default. These factors vary depending on the nature of the exposure and the type of borrower. Exposures are subject to on-going monitoring, which may result in an exposure being moved to a different credit risk grade.

Generating the term structure of Probability of Default (PD)

The Branches employs statistical models to analyse the data collected and generate estimates of PD of exposures and how these are expected to change as a result of the passage of time. This analysis includes the identification and calibration of relationships between changes in default rates and changes in key macro-economic factors, across various geographies in which the Branches has exposures.

Renegotiated financial assets

The contractual terms of a loan may be modified for a number of reasons, including changing market conditions, customer retention and other factors not related to a current or potential credit deterioration of the customer. An existing loan whose terms have been modified may be derecognised and the renegotiated loan recognised as a new loan at fair value. Where possible, the Branches seeks to restructure loans rather than to take possession of collateral, if available. This may involve extending the payment arrangements and documenting the agreement of new loan conditions. Management continuously reviews renegotiated loans to ensure that all criteria are met and that future payments are likely to occur.

The accounts which are restructured due to credit reasons in past 12 months will be classified under Stage 2.

Definition of default

The Branches considers a financial asset to be in default when:

- the borrower is unlikely to pay its credit obligations to the Branches in full, without recourse by the Branches to actions such as realising security (if any is held); or
- the borrower is past due more than 90 days on any material credit obligation to the Branches; or
- the borrower is rated 9 or 10.

26. Risk management (continued)

Definition of default (continued)

In assessing whether a borrower is in default, the Branches also considers indicators that are:

- quantitative - e.g. overdue status and non-payment on another obligation of the same issuer to the Branches; and
- based on data developed internally and obtained from external sources.

Inputs into the assessment of whether a financial instrument is in default and their significance may vary over time to reflect changes in circumstances. The definition of default largely aligns with that applied by the Branches for regulatory capital purposes.

Incorporating forward looking information increases the level of judgement as to how changes in these macroeconomic factors will affect the Expected Credit Loss (ECL) applicable to the stage 1 and stage 2 exposures which are considered as performing. The methodologies and assumptions involved, including any forecasts of future economic conditions, are reviewed periodically

Forward-looking information incorporated in the ECL models

The assessment of SICR and the calculation of ECL both incorporate forward-looking information. The Branches has performed historical analysis and identified the key economic variables impacting credit risk and expected credit losses for each portfolio.

The Branches employs statistical models to incorporate macro-economic factors on historical default rates. In the case that none of the macro-economic parameters are statistically significant or the results of forecasted PDs are too deviated from the present forecast of the economic conditions, qualitative PD overlay is used by management based on portfolio analysis.

Incorporating forward looking information increases the level of judgement as to how changes in these macroeconomic factors will affect the ECL applicable to the stage 1 and stage 2 exposures. The methodologies and assumptions involved, including any forecasts of future economic conditions, are reviewed periodically.

These economic variables and their associated impact on the PD, EAD and LGD vary by financial instrument. Expert judgment has also been applied in this process. Forecasts of these economic variables (the "base economic scenario") are based on available information and include mean reversion approaches for long-term forecasts. The impact of these economic variables on the PD, EAD and LGD has been determined by performing statistical regression analysis to understand the impact changes in these variables have had historically on default rates and on the components of LGD and EAD.

26. Risk management (continued)

Forward-looking information incorporated in the ECL models (continued)

In addition to the base economic scenario, other possible scenarios are assessed along with scenario weightings. The number of other scenarios used is set based on the analysis of each major product type to ensure non-linearities are captured. At 1 January 2018 and 31 December 2018, the Branches concluded that three scenarios appropriately captured non-linearities for all portfolios. The scenario weightings are determined by a combination of statistical analysis and expert credit judgement, taking account of the range of possible outcomes each chosen scenario is representative of. The assessment of SICR is performed using the Lifetime PD under each of the base, and the other scenarios, multiplied by the associated scenario weighting, along with qualitative and backstop indicators. This determines whether the whole financial instrument is in Stage 1, Stage 2, or Stage 3 and hence whether 12-month or lifetime ECL should be recorded. Following this assessment, the Branches measures ECL as either a probability weighted 12 month ECL (Stage 1), or a probability weighted lifetime ECL (Stages 2 and 3).

These probability-weighted ECLs are determined by running each scenario through the relevant ECL model and multiplying it by the appropriate scenario weighting (as opposed to weighting the inputs).

As with any economic forecasts, the projections and likelihoods of occurrence are subject to a high degree of inherent uncertainty and therefore the actual outcomes may be significantly different to those projected. The Branches considers these forecasts to represent its best estimate of the possible outcomes.

Economic variable assumptions

The most significant period-end assumption used for the ECL estimate as at 31 December 2018 is the oil price index, given the high level of correlation between this and other economic indicators. The scenarios "base", "upside" and "downside" were used for all portfolios.

The weightings assigned to each economic scenario at 31 December 2018 were as follows:

	Base	**Upside**	**Downside**
All portfolios	70%	15%	15%

Other forward-looking considerations not otherwise incorporated within the above scenarios, such as the impact of any regulatory, legislative or political changes, have also been considered, but are not deemed to have a material impact and therefore no adjustment has been made to the ECL for such factors. This is reviewed and monitored for appropriateness on a quarterly basis.

Measurement of ECL

The key inputs into the measurement of ECL are the term structure of the following variables:
- probability of default (PD);
- loss given default (LGD);
- exposure at default (EAD).

26. Risk management (continued)

Measurement of ECL (continued)

These parameters are generally derived from internally developed statistical models and other historical data. They are adjusted to reflect forward-looking information as described above.

PD estimates are estimates at a certain date, which are calculated based on statistical rating models. These statistical models are primarily based on internally compiled data comprising both quantitative and qualitative factors and are supplemented by external credit assessment data where available.

LGD is the magnitude of the likely loss if there is a default. The Branches estimates LGD parameters based on a consistent rate for unsecured facilities and considers the impact of collateral for secured facilities.

Credit quality

Pursuant to the adoption of IFRS 9, the Branches has mapped its internal credit rating scale to Moody's rating scale, the table below provides an analysis of counterparties by rating grades and credit quality of the Branches' credit risk, based on Moody's ratings (or their equivalent) as at 31 December 2018.The following table sets out information about the credit quality of financial assets, commitments and financial guarantees.

Credit quality (continued)

	Stage 1	**Stage 2**	**Stage 3**	**2018 Total**	2017 Total
	AED'000	**AED'000**	**AED'000**	**AED'000**	AED'000
Cash and balances with the Central Bank of the U.A.E (excluding cash on hand) and due from related parties and deposit and balances due from banks and financial institutions					
AAA to AA-	271,560	-	-	271,560	549,608
A+ to A-	95,777	-	-	95,777	7,464
BBB to BBB-	3,407	-	-	3,407	1,050
BB+ to B-	37	-	-	37	63
Unrated	62,156	170	-	62,326	50,203
Total	**432,937**	**170**	-	**433,107**	608,388
Expected credit losses - IFRS 9	(6)	(3)	-	(9)	-
Impairment - IAS 39	-	-	-	-	-
Carrying amount	**432,931**	**167**	-	**433,098**	608,388

Notes to the financial statements
for the year ended 31 December 2018 (continued)

26. Risk management (continued)

Credit quality (continued)

	Stage 1	Stage 2	Stage 3	2018 Total	2017 Total
	AED'000	AED'000	AED'000	AED'000	AED'000
Loans and advances to customers					
AAA to AA-	-	-	-	-	-
A+ to A-	-	-	-	-	-
BBB to BBB-	-	-	-	-	-
BB+ to B-	-	-	-	-	-
Unrated	1,058,532	271,077	221,558	1,551,167	2,094,557
Total	**1,058,532**	**271,077**	**221,558**	**1,551,167**	2,094,557
Expected credit losses - IFRS 9	(8,817)	(12,501)	(147,034)	(168,352)	-
Impairment - IAS 39	-	-	-	-	(248,062)
Carrying amount	**1,049,715**	**258,576**	**74,524**	**1,382,815**	1,846,495

	Stage 1	Stage 2	Stage 3	2018 Total	2017 Total
	AED'000	AED'000	AED'000	AED'000	AED'000
Investment securities					
AAA to AA-	-	-	-	-	-
A+ to A-	-	-	-	-	55,223
BBB to BBB-	18,630	-	-	18,630	37,024
BB+ to B-	20,414	-	-	20,414	2,169
Unrated	58,182	-	-	58,182	59,660
Total	**97,226**	-	-	**97,226**	154,076
Expected credit losses - IFRS 9	(691)	-	-	(691)	-
Impairment - IAS 39	-	-	-	-	-
Carrying amount	**96,535**	-	-	**96,535**	154,076

	Stage 1	Stage 2	Stage 3	2018 Total	2017 Total
	AED'000	AED'000	AED'000	AED'000	AED'000
Financial commitments and guarantees					
AAA to AA-	-	-	-	-	-
A+ to A-	13,639	-	-	13,639	-
BBB to BBB-	-	-	-	-	20
BB+ to B-	-	-	-	-	13,639
Unrated	539,370	168,829	6,545	714,744	973,103
Total	**553,009**	**168,829**	**6,545**	**728,383**	986,762
Expected credit losses - IFRS 9	(1,771)	(832)	-	(2,603)	-
Impairment - IAS 39	-	-	-	-	-
Carrying amount	**551,238**	**167,997**	**6,545**	**725,780**	986,762

Notes to the financial statements
for the year ended 31 December 2018 (continued)

26. Risk management (continued)

Set out below is an analysis of the gross and net (of allowances for impairment) amounts of impaired assets by risk grade.

	Due from banks and financial institutions		Loans and advances to customers		Investment securities	
	2018 AED'000	2017 AED'000	**2018 AED'000**	2017 AED'000	**2018 AED'000**	2017 AED'000
Impaired						
Substandard	-	-	**47,042**	61,041	-	-
Doubtful	-	-	**19,242**	13,651	-	-
Loss	-	-	**155,274**	269,062	-	-
Gross amount	-	-	**221,558**	343,754	-	-
Interest suspended	-	-	**(27,449)**	(39,888)	-	-
Specific allowance for impairment	-	-	**(119,585)**	(165,857)	-	-
	-	-	**74,524**	138,009	-	-
Past due but not impaired						
Loans by less than 180 days	-	-	**1,408**	3,103	-	-
Past due loans less than 30 days	-	-	**6,234**	3,469	-	-
	-	-	**7,642**	6,572	-	-
Neither past due nor impaired						
Gross amount	**62,634**	15,638	**1,321,967**	1,744,231	**97,226**	154,076
Collective allowance for Impairment	**(7)**	-	**(21,318)**	(42,317)	**(691)**	-
	62,627	15,638	**1,300,649**	1,701,914	**96,535**	154,076
Carrying amount	**62,627**	15,638	**1,382,815**	1,846,495	**96,535**	154,076

Notes to the financial statements
for the year ended 31 December 2018 (continued)

26. Risk management (continued)

The Branches hold collateral against loans and advances to customers in the form of mortgage interests over property, other registered securities over assets, and guarantees. Estimates of fair value are based on the value of collateral assessed at the time of borrowing, and generally are not updated except when a loan is individually assessed as impaired. Collateral generally is not held over amounts due from banks and financial institutions. Collateral usually is not held against investment securities, and no such collateral was held at 31 December 2018 or 2017.

At 31 December, the fair value of collateral held was as follows:

	Loans and advances to customers	
	2018	2017
	AED'000	AED'000
Property	**1,624,773**	1,562,120
Cash	**85,091**	150,115
Others	**108,675**	10,933
Total	**1,818,539**	1,723,168

Notes to the financial statements
for the year ended 31 December 2018 (continued)

26. Risk management (continued)

Geographical sectors

The following tables break down the Bank's credit risk exposure at their net carrying amounts (without taking into account any collateral held or other credit support), as categorized by geographical region. For this table, the Bank has allocated exposures to regions based on the country of domicile of its counterparties.

	U.A.E. AED'000	Middle East countries AED'000	O.E.C.D AED'000	Other countries AED'000	Impairment allowance AED'000	Total AED'000
At 31 December 2018						
Balances with the Central Bank of U.A.E. - excluding cash	216,472	-	-	-	-	216,472
Due from related parties	-	92,012	61,988	-	(2)	153,998
Deposits and balances due from banks and financial institutions	55,907	506	6,221	-	(7)	62,627
Loans and advances to customers	1,384,638	163,290	3,239	-	(168,352)	1,382,815
Investment securities	76,812	2,092	18,322	-	(691)	96,535
Other assets	21,330	2,097	124	-	-	23,551
Total exposure	**1,755,159**	**259,997**	**89,894**	**-**	**(169,052)**	**1,935,998**

	U.A.E. AED'000	Middle East countries AED'000	O.E.C.D AED'000	Other countries AED'000	Impairment allowance AED'000	Total AED'000
At 31 December 2017						
Balances with the Central Bank of U.A.E. - excluding cash	549,247	-	-	-	-	549,247
Due from related parties	-	247	43,256	-	-	43,503
Deposits and balances due from banks and financial institutions	693	1,225	13,720	-	-	15,638
Loans and advances to customers	1,849,701	243,922	934	-	(248,062)	1,846,495
Investment securities	115,160	20,606	18,310	-	-	154,076
Other assets	31,750	1,564	111	-	-	33,425
Total exposure	2,546,551	267,564	76,331	-	(248,062)	2,642,384

Notes to the financial statements
for the year ended 31 December 2018 (continued)
26. Risk management (continued)

Concentration of risks of financial assets with credit risk exposure - off balance sheet

Geographical sectors

	U.A.E. AED'000	Middle East countries AED'000	O.E.C.D AED'000	Other countries AED'000	Total AED'000
At 31 December 2018					
Guarantees	668,900	13,639	11,419	3,050	697,008
Letters of credit	31,375	-	-	-	31,375
Total exposure	**700,275**	**13,639**	**11,419**	**3,050**	**728,383**
At 31 December 2017					
Guarantees	908,784	13,639	20	25,417	947,860
Letters of credit	38,902	-	-	-	38,902
Total exposure	947,686	13,639	20	25,417	986,762

The distributions by geographical concentration of impaired loans and advances and impairment allowance for credit losses are as follows:

	U.A.E. AED'000	Middle East countries AED'000	O.E.C.D AED'000	Other countries AED'000	Total AED'000
2018					
Non-performing loans	**221,558**	-	-	-	**221,558**
Impairment allowance for credit losses	**(111,889)**	-	-	-	**(111,889)**
Interest in suspense	**(27,449)**	-	-	-	**(27,449)**
2017					
Non-performing loans	343,754	-	-	-	343,754
Impairment allowance for credit losses	(165,857)	-	-	-	(165,857)
Interest in suspense	(39,888)	-	-	-	(39,888)

Notes to the financial statements
for the year ended 31 December 2018 (continued)

26. Risk management (continued)

The following table depicts the interest rate sensitivity position and interest rate gap position based on contractual repricing arrangement as at 31 December 2018:

Interest rate sensitivity gap:

	Within 3 months AED'000	From 3 to 6 months AED'000	From 6 to 12 months AED'000	Over one year AED'000	Non-interest sensitive AED'000	Total AED'000
Assets						
Cash and balances with the Central Bank - of the U.A.E.	-	-	-	-	230,761	230,761
Due from related parties	146,065	-	-	-	7,933	153,998
Due from banks and financial institutions	55,090	-	-	-	7,537	62,627
Investment securities	-	-	2,077	94,458	-	96,535
Loans and advances to customers	563,992	239,228	72,971	422,811	83,813	1,382,815
Other assets	-	-	-	-	60,025	60,025
Property and equipment	-	-	-	-	889	889
Intangibles	-	-	-	-	5,306	5,306
Total assets	**765,147**	**239,228**	**75,048**	**517,269**	**396,264**	**1,992,956**
Liabilities and Equity						
Due to banks and financial institutions	-	-	-	-	3,363	3,363
Customers' deposits	448,564	274,200	91,406	-	488,858	1,303,028
Due to related parties	-	-	-	-	8,962	8,962
Other liabilities	-	-	-	-	44,051	44,051
Equity	-	-	-	-	633,552	633,552
Total liabilities and Equity	**448,564**	**274,200**	**91,406**	**-**	**1,178,786**	**1,992,956**
On balance sheet gap	**316,583**	**(34,972)**	**(16,358)**	**517,269**	**(782,522)**	**-**
Cumulative interest rate sensitivity gap	**316,583**	**281,611**	**265,253**	**782,522**	**-**	**-**

Notes to the financial statements
for the year ended 31 December 2018 (continued)

26. Risk management (continued)

The following table depicts the interest rate sensitivity position and interest rate gap position based on contractual repricing arrangement as at 31 December 2017:

Interest rate sensitivity gap:

	Within 3 months AED'000	From 3 to 6 months AED'000	From 6 to 12 months AED'000	Over one year AED'000	Non-interest sensitive AED'000	Total AED'000
Assets						
Cash and balances with the Central Bank - of the U.A.E.	230,000	-	-	-	334,571	564,571
Due from related parties	36,836	-	-	-	6,667	43,503
Due from banks and financial institutions	-	-	-	-	15,638	15,638
Investment securities	-	-	57,392	96,684	-	154,076
Loans and advances to customers	849,072	322,071	100,904	434,850	139,598	1,846,495
Other assets	-	-	-	-	80,253	80,253
Property and equipment	-	-	-	-	1,520	1,520
Intangibles	-	-	-	-	6,621	6,621
Total assets	1,115,908	322,071	158,296	531,534	584,868	2,712,677
Liabilities and Equity						
Due to banks and financial institutions	183,625	-	25,707	-	3,537	212,869
Customers' deposits	541,075	254,357	123,328	-	604,274	1,523,034
Due to related parties	275,438	-	-	-	5,825	281,263
Other liabilities	-	-	-	-	66,023	66,023
Equity	-	-	-	-	629,488	629,488
Total liabilities and Equity	1,000,138	254,357	149,035	-	1,309,147	2,712,677
On balance sheet gap	115,770	67,714	9,261	531,534	(724,279)	-
Cumulative interest rate sensitivity gap	115,770	183,484	192,745	724,279	-	-

Notes to the financial statements
for the year ended 31 December 2018 (continued)

26. Risk management (continued)

Liquidity risk

Liquidity risk is the risk that the Branches will encounter difficulty in meeting obligations from its financial liabilities at a point of time.

Management of liquidity risk

The Branches' approach to managing liquidity is to ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the Branches' reputation.

Treasury receives information from other business units regarding the liquidity profile of their financial assets and liabilities and details of other projected cash flows arising from projected future business. Treasury then maintains a portfolio of short-term liquid assets, largely made up of loans and advances to banks and other inter-bank facilities, to ensure that sufficient liquidity is maintained within the Branches.

The daily liquidity position is monitored regularly and liquidity stress testing is conducted covering both normal and more severe market conditions. Liquidity policies and procedures are subject to review and approval by Head Office. Reports of the Branches liquidity positions are reviewed daily. A summary report including any exceptions and remedial action taken is also reviewed daily.

The Central bank of U.A.E. through its circular no. 33/2015 dated 27 May 2015 announced new Regulations regarding Liquidity at Banks followed by a Guidance Manual. The above mentioned regulations introduced a new Liquidity ratio called Eligible Liquid Assets ratio ("ELAR") applicable from 1 July 2015.

The key measure used by the Branches for managing liquidity risk is the ratio of net liquid assets to deposits from customers. For this purpose net liquid assets are considered as including cash and cash equivalents and investment grade debt securities for which there is an active and liquid market less any deposits from banks, other borrowings and commitments maturing within the next month. A similar, but not identical, calculation is used to measure the Branches' compliance with the liquidity limit established by the Branches' lead regulator. The other indicators closely monitored on regular basis are Advances to Deposit Ratio, Utilization of funds to stable resources and stress testing of liquid funds against unexpected withdrawal of liabilities and the recently implemented ELAR.

Market risk management

Market risk is the risk that the fair value or future cash flows of the financial instruments will fluctuate due to changes in market variables such as interest rates, foreign exchange rates, and equity prices. The Branches classify exposures to market risk into either trading or non-trading or banking-book.

The Branches carry a limited amount of market risk as a policy preference and it is continuously monitored. Foreign exchange for the account of the Branches is managed properly.

26. Risk management (continued)

Market risk - Non Trading or Banking Book

Market risk on non-trading or banking positions mainly arises from the interest rate and foreign currency exposures.

i) Interest rate risk management

Interest rate risk arises from the possibility that changes in interest rates will affect the value of financial instruments. The Branches are exposed to interest rate risk as a result of mismatches or gaps in the amounts of assets and liabilities.

The Branches use monitoring tools to periodically measure and monitor interest rate sensitivity. The results are analysed and monitored by Local Management Committee. Since a portion of the Branches' assets and liabilities have floating rates, deposits and loans generally repriced simultaneously providing a natural hedge, which reduces interest rate exposure. Moreover, the majority of the Branches' assets and liabilities are repriced within one year, thereby further limiting interest rate risk. The following paragraphs depicts the sensitivity to a reasonable possible change in interest rates, with other variables held constant, on the Branches' statement of profit or loss or Equity. The sensitivity of the income is the effect of the assumed changes in interest rates on the net interest income for one year, based on the floating rate non-trading financial assets and financial liabilities held as at 31 December 2018, including the effect of hedging instruments. The sensitivity of equity is analysed by maturity of the asset or swap. All the banking book exposures are monitored and analysed in currency concentrations and relevant sensitivities are disclosed in AED million.

The impact of 1% sudden movement in benchmark interest rate on net income over a 12 months period as at 31 December 2018 would have been a decrease in net income by -20.11% (in case of decrease of interest rate) and would have been an increase in net income by +20.11% (in case of increase of interest rate) [2017: -5.93% and +5.93%] respectively.

The effective interest rate on bank placements, financial institutions, investments and certificates of deposits with the Central Bank of the U.A.E. was 1.28% (2017: 1.37%), on loans and advances was 5.96% (2017: 5.64%), on customer deposits was 1.44% (2017: 1.53%) and on bank borrowings was 2.43% (2017: 2.73%).

ii) Currency risk

Currency risk represents the risk of change in the value of financial instruments due to changes in foreign exchange rates. The Head Office has set limits on positions by currencies, which are monitored daily, and hedging strategies are also used to ensure that positions are maintained within the limits.

The Branches' assets are typically funded in the same currency as that of the business transacted in order to eliminate foreign exchange exposure. The Branches' manage exposure to the effects of fluctuations in prevailing foreign currency exchange rates on its financial position and cash flows. The Branches' Head Office sets limits on the level of exposure by currency and in total for both overnight and intra-day positions, which are monitored daily. At the end of the year, the Branches' had the following significant net exposures denominated in foreign currencies:

Notes to the financial statements
for the year ended 31 December 2018 (continued)

26. Risk management (continued)

Market risk management (continued)

ii) Currency risk (continued)

	Net spot position AED'000	Forward position AED'000	Total 2018 AED'000	Total 2017 AED'000
Euro	**16**	**-**	**16**	494
Sterling Pounds	**13**	**-**	**13**	13
Lebanese Pounds	**63**	**-**	**63**	58
Kuwaiti Dinars	**33**	**-**	**33**	16
Japanese Yens	**-**	**-**	**-**	3
Canadian Dollars	**12**	**-**	**12**	3
Swiss Francs	**17**	**-**	**17**	6
Australian Dollars	**10**	**-**	**10**	2
Jordanian Dinars	**11**	**-**	**11**	23
Total	**175**	**-**	**175**	618

The exchange rate of AED against US Dollar is pegged since November 1980 and the Branches' exposure to currency risk is limited to that extent.

Operational risk

The Branches' manage and undertake to minimise operational losses as follows:

Identify and assess the operational risk inherent in all material products, activities, processes and systems, and ensure that before new products, activities, processes and systems are introduced or undertaken, the inherent operational risk in them is subject to adequate assessment procedures.

Implement a process to monitor operational risk profiles and material exposures to losses on a regular basis.

Establish and implement policies, processes and procedures to mitigate and/or control material operational risks. Periodically review organisational risk limitation and control strategy and adjust its operational risk profile using appropriate strategies in the context of the Branches' overall risk appetite and profile.

Ensure contingency and business continuity plans are in place to ensure the Branches' ability to operate on an ongoing basis and to limit losses in the event of severe business interruption, disruption or loss.

Notes to the financial statements
for the year ended 31 December 2018 (continued)

27. Contingent liabilities and commitments

	2018 AED'000	2017 AED'000
a) Contingent liabilities		
Guarantees	**697,008**	947,860
Letters of credit	**31,375**	38,902
	728,383	986,762

The outstanding unutilised facilities as of 31 December 2018 amounted to AED 271 million (2017: AED 1,143 million).

The outstanding unused portion of commitments can be revoked unilaterally at any time by the Branches provided there are reasonable grounds as per contract terms.

b) Contingent liabilities - maturity profile

The maturity profile of the Branches' contingent liabilities was as follows:

	Within 3 months AED'000	From 3 to 6 months AED'000	From 6 to 12 months AED'000	Over 1 year AED'000	Total AED'000
2018					
Guarantees	**527,565**	**75,318**	**61,403**	**32,722**	**697,008**
Letters of credit	**24,078**	**3,457**	**3,840**	**-**	**31,375**
	551,643	**78,775**	**65,243**	**32,722**	**728,383**
2017					
Guarantees	697,284	80,288	135,291	34,997	947,860
Letters of credit	27,784	11,118	-	-	38,902
	725,068	91,406	135,291	34,997	986,762

The analysis of commitments and contingencies by industry sector is shown in Note 26.

28. Approval of financial statements

The financial statements were approved by the Board of Directors of the Head Office and authorised for issue on 31 March 2019.