FAB Q4/FY’17 Financial Results

- *Pro forma Financial Statements*
- *Audited Financial Statements*

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بنــك أبـوظبــي الأول

FAB

First Abu Dhabi Bank

Pro forma Condensed Consolidated Financial Statements

December 31, 2017

PRO FORMA CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

The following pro forma condensed consolidated financial statements ("Pro forma financial statements") illustrates the effects on the statement of financial position and financial performance of the combination (Merger) between National Bank of Abu Dhabi and its subsidiaries (together referred to as "NBAD") and First Gulf Bank and its subsidiaries (together referred to as "FGB").

The Pro forma financial statements consists of the audited Pro Forma Condensed Consolidated Statement of Financial Position of NBAD and FGB (together referred to as "the Group") as at 31 December 2017, and its audited Pro forma Condensed Consolidated statement of Profit or Loss for the year then ended. These statements are prepared as if the Merger has taken place as at 1 Jan 2016.

The purpose of the Pro forma financial statements is to show the material effects that the Merger of NBAD and FGB would have had on the historical consolidated statement of financial position if the Group had already existed in the structure created by the Merger as at 31 December 2017 and on the historical consolidated statement of profit or loss for the financial year ended 31 December 2017. They are not representative of the financial situation and performance that could have been observed if the indicated business combination had been undertaken at an earlier date.

The presentation of the Pro forma financial statements of the Group is based on certain pro forma assumptions and has been prepared for illustrative purposes only and, because of its nature, the pro forma consolidated statement of financial position and financial performance addresses a hypothetical situation and, therefore, does not represent and may not give a true picture of the financial position and financial performance of the Group. Furthermore, the Pro forma financial statements are only meaningful in conjunction with the historical consolidated financial statements of NBAD and FGB as at and for the financial year ended 31 December 2016.

The Pro forma financial statements have been compiled based on the accounting policies adopted by the Group for the preparation of 31 December 2017 financial statements. Any impact due to change in the accounting policy and adjustment have been reflected in prior comparative periods. The Pro forma financial statements does not take into consideration the effects of expected synergies or costs incurred to achieve these synergies as a result of the Merger. The Pro forma financial statements gives no indication of the results and future financial situation of the activities of the Group.

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FAB First Abu Dhabi Bank

Pro forma Condensed consolidated statement of financial position

As at 31 December

Assets	2017 AED'000	2016 AED'000
Cash and balances with central banks	**138,111,054**	123,441,316
Investments at fair value through profit or loss	**19,320,764**	11,381,851
Due from banks and financial institutions	**13,829,490**	17,308,257
Reverse repurchase agreements	**21,346,974**	14,278,842
Derivative financial instruments	**11,399,432**	13,796,739
Loans and advances	**330,465,888**	334,430,035
Non-trading investments	**88,457,710**	92,855,423
Investment properties	**6,927,692**	6,468,106
Property and equipment	**3,535,501**	4,594,230
Intangibles	**19,901,374**	14,304,189
Other assets	**15,672,416**	16,261,635
Total assets	**668,968,295**	649,120,623
Liabilities		
Due to banks and financial institutions	**30,576,336**	48,401,950
Repurchase agreements	**37,674,016**	29,594,535
Commercial paper	**24,124,097**	13,725,897
Derivative financial instruments	**14,941,331**	16,040,059
Customer accounts and other deposits	**395,843,664**	379,165,290
Term borrowings	**42,145,718**	46,830,945
Subordinated notes	**420,381**	355,987
Other liabilities	**21,033,339**	17,571,983
Total liabilities	**566,758,882**	551,686,646
Equity		
Share capital	**10,897,545**	10,897,545
Share premium	**53,026,644**	52,771,684
Treasury shares	**(42,433)**	(48,746)
Statutory and special reserves	**7,081,074**	5,254,545
Other reserves	**962,736**	725,067
Tier 1 capital notes	**10,754,750**	10,754,750
Share option scheme	**256,265**	228,349
Convertible notes - equity component	**108,265**	108,265
Retained earnings	**18,677,552**	16,309,736
Total equity attributable to shareholders of the Group	**101,722,398**	97,001,195
Non-controlling interest	**487,015**	432,782
Total Equity	**102,209,413**	97,433,977
Total liabilities and equity	**668,968,295**	649,120,623

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بنك أبوظبي الأول
FAB
First Abu Dhabi Bank

Pro forma Condensed consolidated statement of profit or loss

For the year ended 31 December

	Note	2017 AED'000	2016 AED'000
Interest income	*1*	**18,846,918**	18,687,450
Interest expense	*2*	**(5,740,867)**	(5,137,679)
Net interest income		**13,106,051**	13,549,771
Fee and commission income		**4,765,261**	5,287,914
Fee and commission expense		**(1,403,397)**	(1,401,978)
Net fee and commission income	*3*	**3,361,864**	3,885,936
Net foreign exchange gain	*4*	**1,003,284**	1,053,368
Net gain on investments and derivatives	*5*	**1,582,442**	969,792
Other operating income	*6*	**479,344**	843,517
Operating income		**19,532,985**	20,302,384
General, administration and other operating expenses	*7*	**(5,875,349)**	(5,922,299)
Profit before net impairment charge and taxation		**13,657,636**	14,380,085
Net impairment charge	*8*	**(2,384,334)**	(2,663,691)
Profit before taxation		**11,273,302**	11,716,394
Overseas income tax expense		**(323,538)**	(350,552)
Net profit for the period		**10,949,764**	11,365,842
Profit attributable to:			
Shareholders of the Group		**10,915,157**	11,322,268
Non-controlling interests		**34,607**	43,574
		10,949,764	11,365,842

Segmental information

	Business Segment					Geographic Segment				
	Corporate and Investment Banking AED'000	Personal Banking AED'000	Subsidiaries AED'000	Head Office AED'000	Total AED'000	UAE AED'000	Middle East And Africa AED'000	Europe and Americas AED'000	Asia - Pacific AED'000	Total AED'000
For the year ended 31 December 2017										
Net Interest income	5,853,942	5,094,817	566,567	1,590,725	**13,106,051**	11,503,407	611,806	716,768	274,070	**13,106,051**
Net non-interest income	3,520,781	1,766,935	742,020	397,198	**6,426,934**	5,597,194	345,730	297,434	186,576	**6,426,934**
Operating income	9,374,723	6,861,752	1,308,587	1,987,923	**19,532,985**	17,100,601	957,536	1,014,202	460,646	**19,532,985**
General administration and other operating expenses	2,014,741	2,642,111	545,009	673,488	**5,875,349**	5,022,857	344,768	328,017	179,707	**5,875,349**
Net impairment charge	299,678	1,770,465	521,195	(207,004)	**2,384,334**	2,304,790	85,185	(4,481)	(1,160)	**2,384,334**
Profit before taxation	7,060,304	2,449,176	242,383	1,521,439	**11,273,302**	9,772,954	527,583	690,666	282,099	**11,273,302**
Overseas taxation	184,647	114,408	21,973	2,510	**323,538**	5,263	116,818	170,452	31,005	**323,538**
Net profit for the period	6,875,657	2,334,768	220,410	1,518,929	**10,949,764**	9,767,691	410,765	520,214	251,094	**10,949,764**
As at 31 December 2017										
Segment total assets	450,430,907	97,980,652	21,782,636	126,431,598	**696,625,793**	544,299,763	21,240,671	129,441,066	23,406,626	**718,388,126**
Inter segment balances					**(27,657,498)**					**(49,419,831)**
Total assets					**668,968,295**					**668,968,295**
Segment total liabilities	438,220,833	95,001,870	11,430,776	49,643,868	**594,297,347**	456,642,219	13,808,673	126,033,661	19,694,270	**616,178,823**
Inter segment balances					**(27,538,475)**					**(49,419,951)**
Total liabilities					**566,758,872**					**566,758,872**

Segmental information *(continued)*

	Business Segment					Geographic Segment				
	Corporate and Investment Banking AED'000	Personal Banking AED'000	Subsidiaries AED'000	Head Office AED'000	Total AED'000	UAE AED'000	Middle East And Africa AED'000	Europe and Americas AED'000	Asia - Pacific AED'000	Total AED'000
For the year ended 31 December 2016										
Net Interest income	6,040,346	5,708,783	514,558	1,286,084	**13,549,771**	11,950,828	803,449	551,345	244,149	**13,549,771**
Net non-interest income	3,776,509	1,751,524	1,147,654	76,926	**6,752,613**	5,782,985	316,146	436,768	216,714	**6,752,613**
Operating income	9,816,855	7,460,307	1,662,212	1,363,010	**20,302,384**	17,733,813	1,119,595	988,113	460,863	**20,302,384**
General administration and other operating expenses	2,265,236	3,024,107	452,002	180,954	**5,922,299**	5,043,529	393,729	300,395	184,646	**5,922,299**
Net impairment charge	134,877	1,926,936	452,546	149,332	**2,663,691**	2,911,036	15,165	63,596	(326,106)	**2,663,691**
Profit before taxation	7,416,742	2,509,264	757,664	1,032,724	**11,716,394**	9,779,248	710,701	624,122	602,323	**11,716,394**
Overseas taxation	215,771	108,057	26,805	(81)	**350,552**	(1,647)	167,218	173,920	11,061	**350,552**
Net profit for the period	7,200,971	2,401,207	730,859	1,032,805	**11,365,842**	9,780,895	543,483	450,202	591,262	**11,365,842**
As at 31 December 2016										
Segment total assets	422,013,912	101,349,880	24,919,474	158,874,736	**707,158,002**	530,916,692	22,251,895	111,357,266	26,808,386	**691,334,239**
Inter segment balances					(58,037,379)					**(42,213,616)**
Total assets					649,120,623					**649,120,623**
Segment total liabilities	411,167,120	98,520,038	14,310,867	85,726,000	**609,724,025**	446,830,495	16,160,476	109,214,755	21,694,536	**593,900,262**
Inter segment balances					(58,037,379)					**(42,213,616)**
Total liabilities					551,686,646					**551,686,646**

Notes to the condensed consolidated Pro-forma financial statements

1 Interest income

	2017 AED'000	2016 AED'000
Interest from:		
Central banks	**393,633**	234,600
Banks and financial institutions	**534,255**	476,351
Reverse repurchase agreements	**297,671**	165,767
Investments at fair value through profit or loss	**425,735**	405,099
Non-trading investments	**2,129,967**	2,487,719
Loans and advances	**15,065,657**	14,917,914
	18,846,918	18,687,450

2 Interest expense

	2017 AED'000	2016 AED'000
Interest to:		
Banks and financial institutions	**698,074**	982,528
Repurchase agreements	**409,014**	316,236
Commercial paper	**178,992**	63,617
Customer accounts and other deposits	**3,029,734**	2,617,693
Term borrowings	**1,404,651**	1,133,762
Subordinated notes	**20,402**	23,843
	5,740,867	5,137,679

3 Net fees and commission income

	2017 AED'000	2016 AED'000
Fee and commission income		
Trade finance	**998,445**	1,113,582
Collection services	**43,241**	54,640
Brokerage income	**49,245**	53,718
Asset management and investment services	**116,331**	127,085
Investments, derivatives and risk participation	**8,115**	17,725
Retail and corporate lending	**1,171,248**	1,580,422
Cards and e-services	**1,896,355**	1,866,671
Accounts related services	**59,397**	51,038
Commission on transfers	**116,571**	117,649
Others	**306,313**	305,384
Total fee and commission income	**4,765,261**	5,287,914
Fee and commission expense		
Brokerage commission	**35,553**	28,204
Handling charges	**30,618**	29,721
Credit card charges	**1,025,697**	980,369
Retail and corporate lending	**262,840**	338,423
Others	**48,689**	25,261
Total fee and commission expense	**1,403,397**	1,401,978
Net fee and commission income	**3,361,864**	3,885,936

4 Net foreign exchange gain

	2017 AED'000	2016 AED'000
Trading and retranslation gain on foreign exchange and related derivatives	**626,664**	657,146
Dealings with customers	**376,620**	396,222
	1,003,284	1,053,368

5 Net gain on investments and derivatives

	2017 AED'000	2016 AED'000
Net realised and unrealised gain on investments at fair value through profit or loss and derivatives	**630,797**	133,678
Net gain from sale of non-trading Investments	**913,064**	816,326
Dividend income	**38,581**	19,788
	1,582,442	969,792

6 Other Operating Income

	2017 AED'000	2016 AED'000
Investment property income	**215,631**	550,682
Leasing related income	**103,590**	184,483
Other income	**160,123**	108,352
	479,344	843,517

7 General, administration and other operating expenses

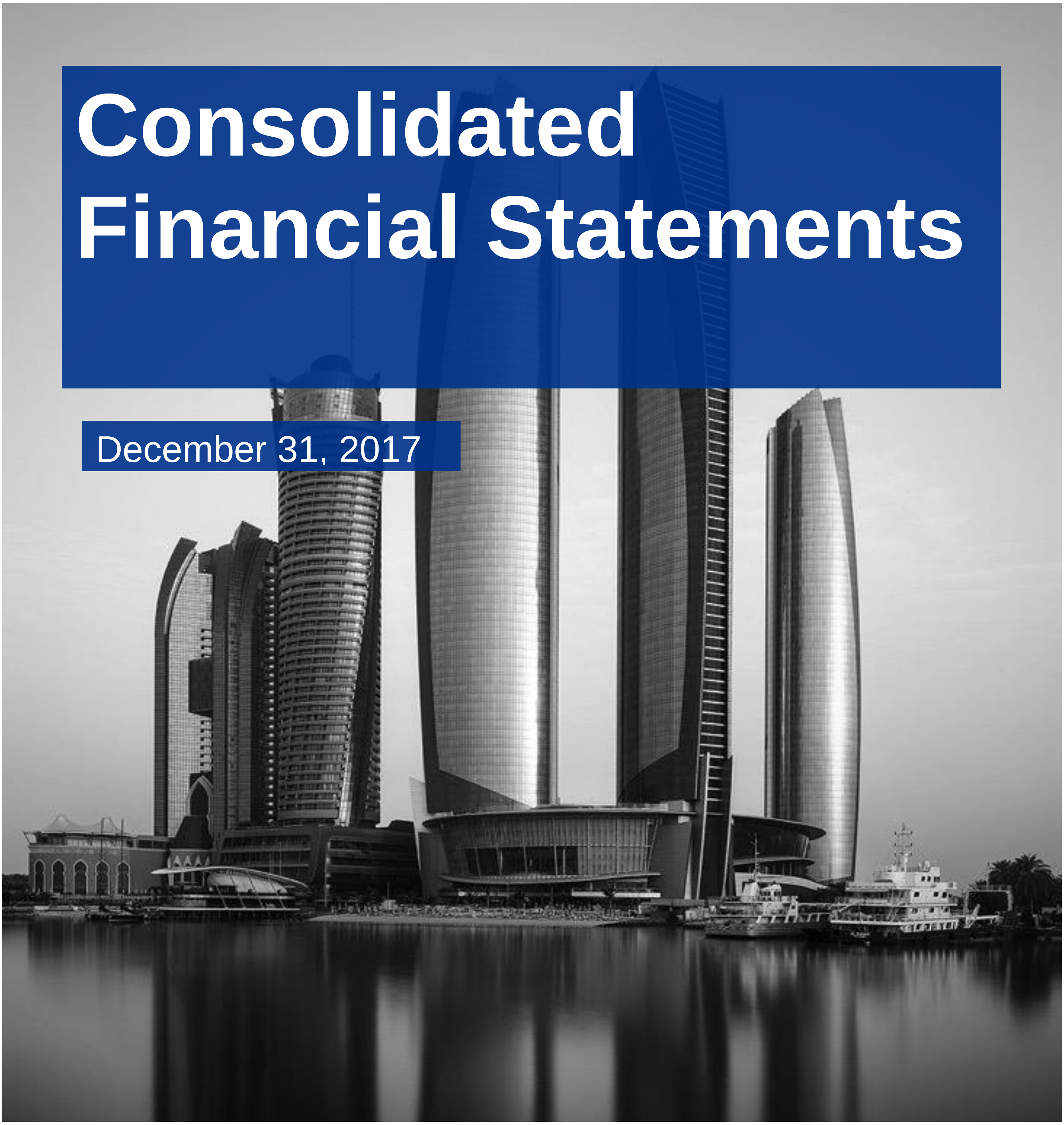
	2017 AED'000	2016 AED'000
Staff costs	**3,422,654**	3,944,851
Other general and administration expenses	**1,877,303**	1,576,394
Depreciation	**374,101**	341,085
Intangible amortisation	**159,156**	21,118
Sponsorships and donations	**42,135**	38,851
	5,875,349	5,922,299

8 Net impairment charge

	2017 **AED'000**	2016 AED'000
Collective provision for loans and advances	**(360,879)**	1,148,986
Specific provision for loans and advances	**3,614,458**	2,404,961
Recoveries	**(903,320)**	(956,536)
Write-off of impaired financial assets	**33,118**	58,463
Provisions for investment and others	**957**	7,817
	2,384,334	2,663,691

Consolidated Financial Statements

December 31, 2017



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The audited Consolidated Financial Statements are approved by the Central Bank of UAE

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Independent Auditors’ Report

To the Shareholders of First Abu Dhabi Bank P.J.S.C.

Report on the audit of the consolidated financial statements

Opinion

We have audited the consolidated financial statements of First Abu Dhabi Bank P.J.S.C. (the “Bank”) and its subsidiaries (the “Group”), which comprise the consolidated statement of financial position as at 31 December 2017, the consolidated statements of profit or loss and other comprehensive income, changes in equity and cash flows for the year then ended, and notes, comprising significant accounting policies and other explanatory information.

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

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (“ISAs”). Our responsibilities under those standards are further described in the *Auditors’ Responsibilities for the Audit of the Consolidated Financial Statements* section of our report. We are independent of the Group in accordance with International Ethics Standards Board for Accountants Code of Ethics for Professional Accountants (“IESBA Code”) together with the ethical requirements that are relevant to our audit of the consolidated 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.

Key Audit Matters

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the consolidated financial statements of the current period. These matters were addressed in the context of our audit of the consolidated financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

Key Audit Matters (continued)

Impairment of Loans and Advances

Refer to note 11 to the consolidated financial statements

Impairment is a subjective area due to the level of judgment applied by management in determining impairment allowance. Due to the significance of loans and advances and the related estimation uncertainty, this is considered a key audit matter.

Judgment is applied to determine appropriate parameters and assumptions used to calculate impairment, for example, the assumption of customers that will default, the valuation of collateral for secured financing and the viability of future cash flows of corporate customers.

Our response

Our audit procedures included the assessment of controls over the approval, recording and monitoring of Loans and Advances, and evaluating the methodologies, inputs and assumptions used by the Group in assessing the adequacy of impairment allowances for individually assessed Loans and Advances, and calculating collectively assessed impairments.

We used our local knowledge to assess trends in the local credit environment and considered the likely impact on the Group's exposures to focus our testing on key risk areas.

1) For corporates, our procedures included:

- testing the key controls over the internal credit grading and monitoring process, to assess if the risk grades allocated to counterparties were appropriately identified and updated on a timely basis;

- substantive testing of a sample of credit grades to test the appropriateness of the credit grades at a given point in time; and

- performing credit assessments for a sample of facilities in credit grades substandard, doubtful, loss and watchlist categories. We assessed the reasonableness of the forecast of recoverable cash flows, realisation of collateral and other possible sources of payment/settlement. We compared key assumptions to progress against business plans and our own understanding of the relevant industries and business environment. We also compared them, where possible, to externally derived evidence such as business performance and real estate valuations for assessing the appropriateness of the collateral values held by the Bank.

Key Audit Matters (continued)

Impairment of Loans and Advances (continued)

Our response (continued)

2) for retail customers, the impairment process is based on models accounting for the number of days past due on each customer. Our procedures included understanding management's basis for determining whether a financing receivable is impaired and assessing the reasonableness using our understanding of the Group's Loans and Advances and our broader industry knowledge.

3) for Portfolio (collective) impairment provision, our procedures included:

- testing of key controls over the impact of underlying data into the models;

- evaluating the methodology and the key assumptions used in determining the estimate and wherever possible, we compared the key assumptions used to externally available industry, financial and economic data; and

- for judgemental overlays, we challenged management to provide evidence that the overlays were appropriate.

4) for the key underlying systems used for the processing of transactions, we involved our information technology specialists to test a selection of automated controls within these systems.

5) we assessed the consolidated financial statement disclosures to ensure that they appropriately reflect the Group's exposure to credit risk.

Acquisition Accounting

Refer to note 42 to the consolidated financial statements

On 7 December 2016, Shareholders of National Bank of Abu Dhabi PJSC ("NBAD") and First Gulf Bank PJSC ("FGB") approved the merger of the two banks (the "transaction") with an effective date of this merger being 1 April 2017. This transaction has been accounted for in accordance with IFRS 3 _Business Combinations_ which requires it to be accounted for using the acquisition method, resulting in this transaction being accounted for as a reverse acquisition whereby FGB is determined to be the accounting acquirer of NBAD.

Purchase Price Allocation ("PPA"), required to be carried out as part of business combination accounting, is complex and inherently judgmental. In particular, due the specialized nature of most intangible assets, measuring the fair value using the market approach may not always be possible. Hence, a number of management assumptions were made using the appropriate methodology, assumptions and valuation techniques. Due to the uncertainty in determining the fair value of assets acquired and liabilities assumed, data used in order to calculate PPA and all its related disclosures, this is considered as a key audit matter.

Key Audit Matters (continued)

Acquisition Accounting (continued)

Our response

We involved our valuation specialists in the audit of the PPA. We challenged the appropriateness of the methodology, assumptions and valuation techniques used to value assets and liabilities, the adequate identification of Cash Generating Units ("CGU") and the appropriateness of the useful lives assigned to the identified intangible assets, having regard to the expected use of these assets.

Our audit procedures included:

- validation of fair value adjustment recognized by management confirming that they are in accordance with the requirements of IFRS 3;
- challenging management assumptions used in determining CGUs;
- assessing management's assumptions in relation to the accounting for the transaction as a reverse acquisition in accordance with the requirements of IFRS 3;
- testing the process and controls to ensure the existence and accuracy of the assets and liabilities on the merger date; and
- assessing the appropriateness of related disclosures.

IT systems and controls over financial reporting

Following the merger, we assessed the Group's IT systems, including controls over financial reporting due to the increased risk of error arising from the integration of some financial accounting and reporting systems ("systems") in the current financial year and also maintaining separate systems after the merger, in accordance with the phasing of the system integration plan, resulting in the existence of manual elements within the process of consolidation of the financial information from various sources. Those systems are dependent on complex technology due to the extensive volume and variety of transactions which are processed daily and there is a risk that automated accounting procedures and related internal controls are not accurately designed and operating effectively. Due to the complexity involved in the IT environment, heightened by changes in the systems as a result of the merger, it is considered as a key audit matter.

Our response

Our audit approach relies on automated controls and therefore our procedures are designed to test access and control over IT systems. We performed a combination of controls testing and substantive testing in order to determine whether we could place reliance on the completeness and accuracy of system generated information. We involved our IT audit specialists in the audit of the Group's IT systems.

Our audit procedures included:

- assessing and testing the design and operating effectiveness of the controls over the continued integrity of the IT systems that are relevant to financial reporting;

Key Audit Matters (continued)

IT systems and controls over financial reporting (continued)

Our response (continued)

- reviewing management's plan of the IT systems integration as a result of the merger;
- reviewing the governance framework over the Group's IT organization and testing the controls over program development and changes, access to programs and data and IT operations, including compensating controls where required;
- assessing the IT security environment;
- identifying and assessing migration procedures and manual processes in preparing a single Bank view from two separate platforms; and
- testing the consolidation process and reconciling the audited component information to the consolidation workings of the Group to verify completeness of the information in the financial reporting systems used to prepare the consolidated financial statements.

Other Matter

The consolidated financial statements of the Group as at and for the year ended 31 December 2016 were audited by the predecessor auditor, whose report dated 31 January 2017 expresses an unmodified audit opinion.

Other information

Management is responsible for the other information. The other information comprises the Chairman's letter, but does not include the consolidated financial statements and our audit report thereon, which we obtained prior to the date of this audit report, and the Bank's Annual report which are expected to be made available to us after that date.

Our opinion on the consolidated financial statements does not cover the other information and we do not express any form of assurance conclusion thereon.

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

If, based on the work we have performed on the other information that we have obtained prior to the date of this auditors' report, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

Responsibilities of management and those charged with governance for the consolidated financial statements

Management is responsible for the preparation and fair presentation of the consolidated financial statements in accordance with IFRS and their preparation in compliance with the applicable provisions of the UAE Federal Law No. (2) of 2015, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

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

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

Auditors' responsibilities for the audit of the consolidated financial statements

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditors' report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these consolidated 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 consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.

- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Group's internal control.

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

Auditors' responsibilities for the audit of the consolidated financial statements (continued)

- 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 Group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditors' report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditors' report. However, future events or conditions may cause the Group to cease to continue as a going concern.

- Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

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

We also provide those charged with governance with a statement that we have complied with relevant ethical requirements regarding independence, and communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

From the matters communicated with those charged with governance, we determine those matters that were of most significance in the audit of the consolidated financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditors' report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

Report on other legal and regulatory requirements

Further, as required by the UAE Federal Law No. (2) of 2015, we report that:

i) we have obtained all the information and we considered necessary for the purposes of our audit;

ii) the consolidated financial statements have been prepared and comply, in all material respects, with the applicable provisions of the UAE Federal Law No. (2) of 2015;

iii) the Group has maintained proper books of account;

iv) the financial information included in the Chairman's letter, in so far as it relates to these consolidated financial statements, is consistent with the books of account of the Group;

v) as disclosed in notes 8 and 12 to the consolidated financial statements, the Group has purchased or invested in shares during the financial year ended 31 December 2017;

vi) note 41 to the consolidated financial statements discloses material related party transactions and the terms under which they were conducted;

vii) based on the information that has been made available to us, nothing has come to our attention which causes us to believe that the Group has contravened during the financial year ended 31 December 2017 any of the applicable provisions of the UAE Federal Law No.(2) of 2015 or in respect of the Bank, its Articles of Association, which would materially affect its activities or its consolidated financial position as at 31 December 2017; and

viii) note 33 to the consolidated financial statements discloses the social contributions made during the year.

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

KPMG Lower Gulf Limited

Richard Ackland

Registration number: 1015

Abu Dhabi, United Arab Emirates

Date 29 JAN 2018

Grow Stronger

FAB First Abu Dhabi Bank

Consolidated statement of financial position
As at 31 December

Assets	Note	2017 AED'000	2016 AED'000
Cash and balances with central banks	*7*	**138,111,054**	24,776,717
Investments at fair value through profit or loss	*8*	**19,320,764**	899,524
Due from banks and financial institutions	*9*	**13,829,490**	12,932,570
Reverse repurchase agreements	*10*	**21,346,974**	5,449,019
Derivative financial instruments	*38*	**11,399,432**	1,953,003
Loans and advances	*11*	**330,465,888**	134,650,001
Non-trading investments	*12*	**88,457,710**	28,413,499
Investment properties	*13*	**6,927,692**	6,422,502
Property and equipment	*14*	**3,535,501**	1,528,255
Intangibles	*15*	**19,901,374**	170,398
Other assets	*16*	**15,672,416**	6,784,453
Total assets		**668,968,295**	223,979,941
Liabilities			
Due to banks and financial institutions	*17*	**30,576,336**	11,585,628
Repurchase agreements	*18*	**37,674,016**	13,109,155
Commercial paper	*19*	**24,124,097**	10,016,916
Derivative financial instruments	*38*	**14,941,331**	2,835,008
Customer accounts and other deposits	*20*	**395,843,664**	125,782,798
Term borrowings	*21*	**42,145,718**	18,294,545
Subordinated notes	*22*	**420,381**	-
Other liabilities	*23*	**21,033,339**	4,698,919
Total liabilities		**566,758,882**	186,322,969
Equity			
Share capital	*24*	**10,897,545**	4,500,000
Share premium		**53,026,644**	-
Treasury shares		**(42,433)**	-
Statutory and special reserves		**7,081,074**	11,030,110
Other reserves	*24*	**962,736**	725,064
Tier 1 capital notes	*25*	**10,754,750**	4,000,000
Share option scheme	*26*	**256,265**	-
Convertible notes - equity component		**108,265**	-
Retained earnings		**18,677,552**	16,969,016
Total equity attributable to shareholders of the Bank		**101,722,398**	37,224,190
Non-controlling interest		**487,015**	432,782
Total Equity		**102,209,413**	37,656,972
Total liabilities and equity		**668,968,295**	223,979,941

These consolidated financial statements were approved by the Board of Directors and authorized for issue on 29 January 2018 and signed on its behalf :

Chairman | Group Chief Executive Officer | Group Chief Financial Officer

The notes 1 to 46 are an integral part of these consolidated financial statements.
The independent auditor's report on audit of consolidated financial statements is set out on pages 2 to 9.

Consolidated statement of profit or loss

For the year ended 31 December

	Note	2017 AED'000	2016 AED'000
Interest income	*27*	**16,331,787**	8,513,560
Interest expense	*28*	**(4,935,594)**	(2,159,931)
Net interest income		**11,396,193**	6,353,629
Fee and commission income		**4,026,061**	2,111,097
Fee and commission expense		**(1,128,206)**	(308,102)
Net fee and commission income	*29*	**2,897,855**	1,802,995
Net foreign exchange gain	*30*	**928,188**	222,656
Net gain on investments and derivatives	*31*	**686,131**	402,735
Other operating income	*32*	**472,090**	778,828
		2,086,409	1,404,219
Operating income		**16,380,457**	9,560,843
General, administration and other operating expenses	*33*	**(4,901,496)**	(1,976,183)
Profit before net impairment charge and taxation		**11,478,961**	7,584,660
Net impairment loss	*34*	**(2,086,717)**	(1,473,014)
Profit before tax		**9,392,244**	6,111,646
Overseas income tax expense	*35*	**(224,989)**	(41,846)
Profit for the year		**9,167,255**	6,069,800
Profit attributable to:			
Shareholders of the Bank		**9,132,648**	6,026,226
Non-controlling interests		**34,607**	43,574
		9,167,255	6,069,800
Basic earnings per share (AED)	*40*	**0.91**	1.04
Diluted earnings per share (AED)	*40*	**0.91**	1.04

The notes 1 to 46 are an integral part of these consolidated financial statements.
The independent auditors' report on audit of consolidated financial statements is set out on pages 2 to 9.

Consolidated statement of comprehensive income

For the year ended 31 December

	2017 AED'000	2016 AED'000
Profit for the year	**9,167,255**	6,069,800
Other comprehensive income		
Items that are or may subsequently be reclassified to consolidated statement of profit or loss		
Exchange difference on translation of foreign operations	**44,878**	(29,795)
Net change in fair value reserve during the year	**212,420**	2,152
Items that will not be subsequently be reclassified to consolidated statement of profit or loss		
Re-measurement of defined benefit obligations	**(7,102)**	-
Board of Director's remuneration	**(49,000)**	(51,000)
Other comprehensive income for the year	**201,196**	(78,643)
Total comprehensive income for the year	**9,368,451**	5,991,157
Comprehensive income attributable to:		
Shareholders of the Bank	**9,314,218**	5,958,814
Non-controlling interest	**54,233**	32,343
Total comprehensive income for the year	**9,368,451**	5,991,157

The notes 1 to 46 are an integral part of these consolidated financial statements.
The independent auditors' report on audit of consolidated financial statements is set out on pages 2 to 9.

Consolidated statement of cash flows
For the year ended 31 December

	Note	2017 AED'000	2016 AED'000
Cash flows from operating activities			
Profit before taxation		**9,392,244**	6,111,646
Adjustments for:			
Depreciation and amortisation	14,15	**470,575**	140,979
Gain on revaluation of investment properties	13	**(179,916)**	5,651
Gain on sale of investment property		**(35,715)**	(550,682)
Gain on sale of fixed assets		**(2,214)**	-
Impairment of other financial charges		**843**	20,852
Net impairment charges	34	**2,383,651**	1,452,162
Accreted interest		**84,952**	4,695
Foreign currency translation adjustment		**425,056**	(86,110)
Share option scheme		**20,466**	-
		12,559,943	7,099,193
Changes in:			
Investments at fair value through profit or loss		**(2,343,581)**	(326,559)
Due from central banks, banks and financial institutions		**(2,286,988)**	(5,390,892)
Reverse repurchase agreements		**1,978,416**	(3,121,470)
Loans and advances		**9,340,457**	(4,884,772)
Other assets		**29,166**	955,767
Due to banks and financial institutions		**(21,993,151)**	1,776,169
Repurchase agreements		**17,964,674**	4,795,590
Customer accounts and other deposits		**(2,933,193)**	2,612,404
Derivative financial instruments		**645,189**	(15,571)
Other liabilities		**1,586,364**	(1,342,530)
		14,547,288	2,157,329
Overseas income tax paid, net of recoveries		**(286,493)**	(19,924)
Directors' remuneration paid		**(49,000)**	(45,000)
Net cash from operating activities		**14,211,795**	2,092,405
Cash flows from investing activities			
Net purchase of non-trading investments		**(12,721,340)**	(6,250,316)
Purchase of investment property		**(553,203)**	(798,856)
Sale proceeds from disposal of investment property		**263,644**	3,253,726
Cash and cash equivalents of subsidiary acquired		**121,258,636**	-
Purchase of property and equipment, net of disposals		**(430,038)**	(252,535)
Net cash from / (used) investing activities		**107,817,699**	(4,047,981)
Cash flows from financing activities			
Proceeds from issue of shares under share option scheme	26	**34,025**	-
Dividend paid	24	**(4,489,524)**	(4,423,230)
Net movement of commercial paper		**2,130,547**	7,182,108
Issue of term borrowings	21	**3,135,955**	2,524,805
Repayment of term borrowings		**(11,433,020)**	(1,524,834)
Repayment of Sukuk		**-**	(2,387,450)
Payment on Tier 1 capital notes	25	**(381,089)**	(138,256)
Net cash (used) / from in financing activities		**(11,003,106)**	1,233,143
Net increase / (decrease) in cash and cash equivalents		**111,026,390**	(722,433)
Cash and cash equivalents at 1 January		**23,579,527**	24,301,960
Cash and cash equivalents at 31 December	36	**134,605,917**	23,579,527

The notes 1 to 46 are an integral part of these consolidated financial statements.
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Consolidated statement of changes in equity

For the year ended 31 December

	Share capital (AED '000)	Share Premium (AED '000)	Treasury shares (AED '000)	Statutory and special reserves (AED '000)	General reserve (AED '000)	Tier 1 capital notes (AED '000)	Share option scheme (AED '000)	Fair value reserve (AED '000)	Foreign currency translation reserve (AED '000)	Reval-uation reserve (AED '000)	Convertible notes - equity component (AED '000)	Retained earnings (AED '000)	Equity attributable to share-holders of the Group (AED '000)	Non-Controllin g interest (AED '000)	Total (AED '000)
Balance at 1 January 2016	4,500,000	-	-	11,030,110	120,000	4,000,000	-	410,638	(69,763)	280,601	-	15,632,046	35,903,632	400,439	36,304,071
Profit for the year	-	-	-	-	-	-	-	-	-	-	-	6,026,226	6,026,226	43,574	6,069,800
Other comprehensive income for the year	-	-	-	-	-	-	-	2,152	(18,564)	-	-	(51,000)	(67,412)	(11,231)	(78,643)
Transactions with owners of the Group															
Dividend for the year 2015	-	-	-	-	-	-	-	-	-	-	-	(4,500,000)	(4,500,000)	-	(4,500,000)
Payment on Tier 1 capital notes *(note 25)*	-	-	-	-	-	-	-	-	-	-	-	(138,256)	(138,256)	-	(138,256)
Balance at 31 December 2016	4,500,000	-	-	11,030,110	120,000	4,000,000	-	412,790	(88,327)	280,601	-	16,969,016	37,224,190	432,782	37,656,972
Balance at 1 January 2017	**4,500,000**	**-**	**-**	**11,030,110**	**120,000**	**4,000,000**	**-**	**412,790**	**(88,327)**	**280,601**	**-**	**16,969,016**	**37,224,190**	**432,782**	**37,656,972**
Profit for the year	-	-	-	-	-	-	-	-	-	-	-	9,132,648	9,132,648	34,607	9,167,255
Other comprehensive income for the year	-	-	-		-	-	-	212,420	25,252	-	-	(56,102)	181,570	19,626	201,196
Business combination transaction *(note 42)*	6,397,545	52,997,018	(46,832)	(5,775,566)	-	6,754,750	235,798	-	-	-	108,265	-	60,670,978	-	60,670,978
Accounting policy alignment *(note 43)*	-	-	-	-	-	-	-	-	-	-	-	(659,283)	(659,283)	-	(659,283)
Transfer during the year				1,826,530								(1,826,530)	-		
Transactions with owners of the Group															
Zakat	-	-	-	-	-	-	-	-	-	-	-	(1,108)	(1,108)	-	(1,108)
Share options exercised *(note 26)*	-	29,626	4,399	-	-	-	-	-	-	-	-	-	34,025	-	34,025
Dividend for the year 2016	-	-	-	-	-	-	-	-	-	-	-	(4,500,000)	(4,500,000)	-	(4,500,000)
Options granted to staff	-	-	-	-	-	-	20,467	-	-	-	-	-	20,467	-	20,467
Payment on Tier 1 capital notes *(note 25)*	-	-	-	-	-	-	-	-	-	-	-	(381,089)	(381,089)	-	(381,089)
Balance at 31 December 2017	**10,897,545**	**53,026,644**	**(42,433)**	**7,081,074**	**120,000**	**10,754,750**	**256,265**	**625,210**	**(63,075)**	**280,601**	**108,265**	**18,677,552**	**101,722,398**	**487,015**	**102,209,413**

The notes 1 to 46 are an integral part of these consolidated financial statements.
The independent auditors' report on audit of consolidated financial statements is set out on pages 2 to 9.

Notes to the consolidated financial statements

1 Legal status and principal activities

On 7 December 2016, Shareholders of National Bank of Abu Dhabi PJSC ("NBAD") and First Gulf Bank PJSC ("FGB") approved the merger of the two banks pursuant to Article 283(1) of UAE Federal Law No. 2 of 2015 Concerning Commercial Companies (the Law). The merger was effected through the issuance of 1.254 new NBAD shares for every 1 share in FGB on close of business 30 March 2017, subsequent to which FGB shares were delisted from Abu Dhabi Securities Exchange. On 25 April 2017, NBAD shareholders approved the proposal to change the name of the combined bank to 'First Abu Dhabi Bank' (the "Bank") and have its registered office in FAB Building, Khalifa Business Park 1 Al Qurum P. O Box 6316 Abu Dhabi, United Arab Emirates. This transaction is accounted for as a reverse acquisition as per *IFRS 3 - Business Combinations*, (*refer to Note 42 for details*) and therefore the comparatives in the financial statements are of FGB.

These consolidated financial statements as at and for the year ended 31 December 2017 comprises the Bank and its subsidiaries (together referred to as the "Group"). The Group is primarily engaged in corporate, retail, private and investment banking activities, management services, Islamic banking activities, real estate activities; and carries out its operations through its local and overseas branches, subsidiaries and representative offices located in the United Arab Emirates, Bahrain, Brazil, Cayman Islands, China, Egypt, France, Hong Kong, India, Jordan, Kuwait, Lebanon, Libya, Malaysia, Oman, Qatar, Singapore, South Korea, Sudan, Switzerland, the United Kingdom and the United States of America..

The Group's Islamic banking activities are conducted in accordance with Islamic Sharia'a laws issued by the Sharia'a Supervisory Board.

The Group is listed on the Abu Dhabi Securities Exchange (Ticker: FAB).

The consolidated financial statements of the Group as at and for the year ended 31 December 2017 are available upon request from the Group's registered office or at http://www.bankfab.com

2 Basis of Preparation

(a) Statement of Compliance

These consolidated financial statements have been prepared on going concern basis in accordance with International Financial Reporting Standards as issued by the International Accounting Standards Board (IASB) and the requirements of applicable laws in the UAE.

On 1 April 2015, a new UAE Federal Law No 2 for Commercial Companies ("UAE Companies Law of 2015") was issued with effective date 1 July 2015. The Group is compliant with applicable sections of the UAE Companies Law of 2015 as at the date thereof.

These consolidated financial statements were authorised for issue by the Board of Directors on 29 January 2018.

(b) Business combinations

Business combinations are accounted for using the acquisition method. The cost of an acquisition is measured as the aggregate of the consideration transferred measured at acquisition date fair value and the amount of any non-controlling interests in the acquiree. Acquisition-related costs are expensed as incurred and included in administrative expenses, except if related to the issue of debt or equity securities.

When the Group acquires a business, it assesses the financial assets and liabilities assumed for appropriate classification and designation in accordance with the contractual terms, economic circumstances and pertinent conditions as at the acquisition date. This includes the separation of embedded derivatives in host contracts by the acquiree.

If the business combination is achieved in stages, any previously held equity interest is re-measured at its acquisition date fair value and any resulting gain or loss is recognised in profit or loss. It is then considered in the determination of goodwill.

Notes to the consolidated financial statements *(continued)*

2 Basis of Preparation *(continued)*

(b) Business combinations *(continued)*

Any contingent consideration to be transferred by the acquirer will be recognised at fair value at the acquisition date. Contingent consideration classified as an asset or liability that is a financial instrument and within the scope of IAS 39 Financial Instruments: Recognition and Measurement, is measured at fair value with changes in fair value recognised either in either profit or loss or as a change to other comprehensive income. If the contingent consideration is not within the scope of IAS 39, it is measured in accordance with the appropriate standards. Contingent consideration that is classified as equity is not re-measured and subsequent settlement is accounted for within equity.

Goodwill is initially measured at cost, being the excess of the aggregate of the consideration transferred and the amount recognised for non-controlling interests, and any previous interest held, over the net identifiable assets acquired and liabilities assumed. If the fair value of the net assets acquired is in excess of the aggregate consideration transferred or in an excess of the fair value of net assets acquired over the aggregate consideration transferred, then the gain is recognised in profit or loss.

After initial recognition, goodwill is measured at cost less any accumulated impairment losses. For the purpose of impairment testing, goodwill acquired in a business combination is, from the acquisition date, allocated to each of the Group's cash-generating units that are expected to benefit from the combination, irrespective of whether other assets or liabilities of the acquiree are assigned to those units.

Where goodwill has been allocated to a cash-generating unit and part of the operation within that unit is disposed of, the goodwill associated with the disposed operation is included in the carrying amount of the operation when determining the gain or loss on disposal. Goodwill disposed in these circumstances is measured based on the relative values of the disposed operation and the portion of the cash-generating unit retained.

(c) Basis of measurement

These consolidated financial statements are prepared under the historical cost basis except for the following:

- investments at fair value through profit or loss are measured at fair value;
- derivative financial instruments are measured at fair value;
- non-trading investments classified as available-for-sale are measured at fair value;
- recognised assets and liabilities designated as hedged items in qualifying hedge relationships are adjusted for changes in fair value attributable to the risk being hedged; and
- non-financial assets acquired in settlement of loans and advances are measured at the lower of their fair value less costs to sell and the carrying amount of the loan and advances.

(d) Functional and presentation currency

These consolidated financial statements are presented in United Arab Emirates Dirhams ("AED"), which is the Group's functional currency. All amounts have been rounded to the nearest thousand, unless otherwise indicated. Items included in the financial statements of each of the Bank's overseas subsidiaries and branches are measured using the currency of the primary economic environment in which they operate.

(e) Use of estimates and judgements

The preparation of consolidated financial statements requires management to make judgements, estimates and assumptions that affect the application of accounting policies and reported amounts of assets and liabilities, income and expense. Actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised prospectively.

Information about significant areas of estimation uncertainty and critical judgements in applying accounting policies that have the most significant effect on the amounts recognised in these consolidated financial statements are described in note 5.

Notes to the consolidated financial statements *(continued)*

3 Significant accounting policies

The accounting policies applied by the Group in these consolidated financial statements are the same as those applied by the Group in its consolidated financial statements as at and for the year ended 31 December 2016 except for the effect of accounting policy change as mentioned in note 43 and the adoption of the following amendments to standards and new standards as of 1 January 2017.

New standards and interpretations adopted

- Amendments to IAS 12 Income Taxes relating to the recognition of deferred tax assets for unrealised losses.
- Amendments to IAS 7 Statement of Cash Flows to provide disclosures that enable users of financial statements to evaluate changes in liabilities arising from financing activities.
- Annual Improvements to IFRS Standards 2014–2016 Cycle – Amendments to IFRS 12.

(a) Basis of consolidation

(i) Subsidiaries

IFRS 10 governs the basis for consolidation where it establishes a single control model that applies to all entities including special purpose entities or structured entities. The definition of control is such that an investor controls an investee when it is exposed to, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee. To meet the definition of control in IFRS 10, all three criteria must be met, including:

(a) the investor has power over an investee;
(b) the investor has exposure to, or rights, to variable returns from its involvement with the investee; and
(c) the investor has the ability to use its power over the investee to affect the amount of the investor's returns.

Subsidiaries are entities that controlled by the Group. The Group controls the investee if it meets the control criteria set out above. The Group reassesses whether it has control if, there are changes to one or more of the elements of control. This includes circumstances in which protective rights held become substantive and lead to the Group having power over an investee. The financial statements of subsidiaries are included in these consolidated financial statements from the date that control commences until the date that control ceases.

The consolidated financial statements comprise the financial statements of the Group and those of its following subsidiaries:

Legal Name	**Country of incorporation**	**Principal activities**	**Holding % 2017**
NBAD Americas N.V. *(formerly Abu Dhabi International Bank N.V.)*	Curacao	Banking	100%
NBAD Securities LLC	United Arab Emirates	Brokerage	100%
Abu Dhabi National Leasing LLC	United Arab Emirates	Leasing	100%
Abu Dhabi National Properties PJSC	United Arab Emirates	Property Management	100%
NBAD Private Bank (Suisse) SA	Switzerland	Banking	100%
Abu Dhabi National Islamic Finance Pvt. JSC	United Arab Emirates	Islamic Finance	100%
Ample China Holdings Limited	Hong Kong	Leasing	100%
Abu Dhabi Brokerage Egypt	Egypt	Brokerage	96%
National Bank of Abu Dhabi Malaysia Berhad	Malaysia	Banking	100%
NBAD Employee Share Options Limited	United Arab Emirates	Shares and Securities	100%
SAS 10 Magellan	France	Leasing	100%
NBAD Global Multi-Strategy Fund	Cayman Island	Fund Management	100%

Notes to the consolidated financial statements *(continued)*

3 Significant accounting policies *(continued)*

(a) Basis of consolidation *(continued)*

(i) Subsidiaries (continued)

Legal Name	Country of incorporation	Principal activities	Holding % 2017
National Bank of Abu Dhabi Representações Ltda	Brazil	Representative office	100%
NBAD Financial Markets (Cayman) Limited	Cayman Islands	Financial Institution	100%
Nawat Management Services	United Arab Emirates	Services	100%
Mismak Properties Co. LLC (Mismak)	United Arab Emirates	Real estate investments	100%
First Merchant International LLC	United Arab Emirates	Real estate investments	100%
FGB Sukuk Company Limited	Cayman Islands	Special purpose vehicle	100%
FGB Sukuk Company II Limited	Cayman Islands	Special purpose vehicle	100%
First Gulf Libyan Bank *	Libya	Banking services	50%
FGB Global Markets Cayman Limited	Cayman Islands	Financial Institution	100%
First Gulf Properties LLC	United Arab Emirates	Management and brokerage of real estate properties	100%
Aseel Finance PJSC	United Arab Emirates	Islamic finance	100%
Dubai First PJSC	United Arab Emirates	Credit card finance	100%
First Gulf Information Technology LLC	United Arab Emirates	IT Services	100%

* Although the Bank owns 50% of the outstanding shares of First Gulf Libyan Bank, the investment has been classified as a subsidiary as the Bank exercises control over the investee because it casts the majority of the votes on the board of directors.

(ii) Structured entities

A structured entity is established by the Group to perform a specific task. Structured entities are designed so that their activities are not governed by way of voting rights. In assessing whether the Group acts as a principal or has power over investees in which it has an interest, the Group considers factors such as the purpose and design of the investee, its practical ability to direct the relevant activities of the investee; the nature of its relationship with the investee; and the size of its exposure to the variability of returns of the investee.

The Group acts as fund manager to a number of investment funds. Determining whether the Group controls such an investment fund usually focuses on the assessment of the aggregate economic interests of the Group in the fund. Whilst assessing control, the Group reviews all facts and circumstances to determine whether as a fund manager the Group is acting as agent or principal. If deemed to be a principal, the Group controls the fund and would consolidate them else as an agent the Group would account for them as investments in funds.

The Group's interest in investment funds in which it act as an agent is set out below, these funds are included as part of investments.

Type of Structured Entity	Nature and purpose	Interest held by the Group
Investment Funds	Generate fees from managing assets on behalf of third-party investors	Investments in units issued by the fund amounting to AED 20,069 thousand *(2016: nil)*

3 Significant accounting policies *(continued)*

(iii) Joint Arrangements and Investments in Associates

An Associate is an investee over which the Group has significant influence. Significant influence is the power to participate in the financial and operating policy decisions of the investee but not control or joint control over those policies. Investment in associates is accounted under the equity method of accounting.

A joint arrangement is an arrangement between the Group and other parties where the Group along with one or more parties has joint control by virtue of a contractual agreement. Joint arrangement may be a joint operation or a joint venture. A joint operation is a joint arrangement whereby the parties that have joint control of the arrangement have rights to and record their respective share of the assets, and obligations for the liabilities, relating to the arrangement. A joint venture is a joint arrangement whereby the parties that have joint control of the arrangement, have rights to the net assets of the arrangement and, thus, are accounted under the equity method of accounting.

Under the equity method, the investment in an associate is initially recognised at cost, which includes transaction costs. Subsequent to initial recognition, the consolidated financial statements include the Group's share of the profit or loss and OCI of equity accounted investees, until the date on which significant influence or joint control ceases. Goodwill relating to the associate is included in the carrying amount of the investment and is neither amortised nor individually tested for impairment. The consolidated statement of income reflects the Group's share of the results of operations of the associates. Any change in other comprehensive income of those investees is presented as part of the Group's other comprehensive income. In addition, when there has been a change recognised directly in the equity of the associate, the Group recognises its share of any changes, when applicable, in the consolidated statement of changes in equity.

The aggregate of the Group's share of profit or loss of an associate is shown on the face of the consolidated statement of income. The financial statements of the associate are prepared for the same reporting period as the Group. When necessary, adjustments are made to bring the accounting policies in line with those of the Group.

After application of the equity method, the Group determines whether it is necessary to recognise an impairment loss on its investment in its associate. At each reporting date, the Group determines whether there is objective evidence that the investment in the associate is impaired. If there is such evidence, the Group calculates the amount of impairment as the difference between the recoverable amount of the associate and its carrying value, and then recognises the loss in the consolidated statement of income.

(iv) Loss of control

When the Group loses control over a subsidiary, it derecognises the assets and liabilities of the subsidiary, any non-controlling interests and the other components of equity related to the subsidiary. Any surplus or deficit arising on the loss of control is recognised in consolidated statement of profit or loss. If the Group retains any interest in the former subsidiary, then such interest is measured at fair value when control is lost.

(v) Transactions eliminated on consolidation

The carrying amount of the Group's investment in each subsidiary and the equity of each subsidiary are eliminated on consolidation. All significant intra-group balances, transactions and unrealised income and expenses (except for foreign currency transaction gains or losses) arising from intra-group transactions are eliminated on consolidation. Unrealised losses are eliminated in the same way as unrealised gains, but only to the extent that there is no evidence of impairment.

(b) Financial assets and liabilities

(i) Recognition

The Group initially recognises loans and advances, deposits, debt securities issued and subordinated liabilities on the date on which they are originated. All other financial instruments (including regular way purchases and sales of financial assets) are recognised on the trade date, which is the date on which the Group becomes a party to the contractual provisions of the instrument.

All *regular way* purchases and sales of financial assets are recognised on the settlement date, i.e. the date the asset is delivered to or received from the counterparty. *Regular way* purchases or sales of financial assets are those that require delivery of assets within the time frame generally established by regulation or convention in the market place.

Notes to the consolidated financial statements *(continued)*

3 Significant accounting policies *(continued)*

(b) Financial assets and liabilities *(continued)*

(ii) The Group classifies its financial assets into one of the following categories:

(a) *Fair value through profit or loss*

(i) *Designation at fair value through profit or loss*
The Group designates financial assets and liabilities at fair value through profit or loss when either:

- the assets or liabilities are managed, evaluated and reported internally on a fair value basis; or
- the designation eliminates or significantly reduces an accounting mismatch which would otherwise arise.

(ii) *Held for trading*
Trading assets are those assets that the Group acquires for the purpose of selling in the near term, or holds as part of a portfolio that is managed together for short-term profit taking.

Fair value through profit or loss assets is not reclassified subsequent to their initial recognition.

(b) *Loans and receivables*
Loans and receivables include cash and balances with central banks, due from bank and financial institutions, finance lease receivables, reverse repurchase agreements and loans and advances. These are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market and that the Group does not intend to sell immediately or in the near term.

(c) *Held-to-maturity*
Held-to-maturity investments are non-derivative assets with fixed or determinable payments and fixed maturity that the Group has the positive intent and ability to hold to maturity.

(d) *Available-for-sale*
The Group has non-derivative financial assets designated as available-for-sale when these are not classified as loans and receivables, held-to-maturity investments or financial assets at fair value through profit or loss. Available for sale assets are intended to be held for an indefinite period of time and may be sold in future to manage liquidity requirements or in response to market fluctuation in interest rates or pricing of the financial assets.

(e) *Financial liabilities*
The Group classifies its financial liabilities, other than financial guarantees and loan commitments, as measured at amortised cost or fair value through profit or loss.

(iii) *De-recognition*
The Group derecognises a financial asset when the contractual rights to the cash flows from the financial asset expire, or when it transfers the rights to receive the contractual cash flows on the financial asset in a transaction in which substantially all the risks and rewards of ownership of the financial asset are transferred or in which the Group neither transfers nor retains substantially all the risks and rewards of ownership and it does not retain control of the financial asset.

The Group derecognises a financial liability when its contractual obligations are discharged or cancelled or expire.

The Group enters into transactions whereby it transfers assets recognised on its consolidated statement of financial position, but retains either all or substantially all of the risks and rewards of the transferred assets or a portion of them. In such transactions, the transferred assets are not derecognised from the consolidated statement of financial position. Transfers of assets with retention of all or substantially all risks and rewards include repurchase transactions.

The Group also derecognises certain assets when it writes off balances pertaining to the assets deemed to be uncollectible.

Notes to the consolidated financial statements *(continued)*

3 Significant accounting policies *(continued)*

(b) Financial assets and liabilities *(continued)*

(iv) *Offsetting*

As per IAS 32, financial assets and liabilities are offset and the net amount presented in the consolidated statement of financial position when, and only when, the Group has a legal right to set off the amounts and intend either to settle on a net basis, or to realise the asset and settle the liability simultaneously.

Income and expenses are presented on a net basis only when permitted under IFRS, or for gains and losses arising from a group of similar transactions such as in the Group's trading activity

(v) *Amortised cost measurement*

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

The effective interest rate is the rate that exactly discounts estimated future cash receipts or payments through the expected life of the financial instrument or, where appropriate, a shorter period, to the net carrying amount of the financial asset or financial liability. When calculating the effective interest rate, the Group estimates cash flows considering all contractual terms of the financial instrument but excluding future credit losses. The calculation includes all amounts paid or received by Group that are an integral part of the effective interest rate of a financial instrument, including transaction costs and all other premiums or discounts.

(vi) *Fair value measurement*

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date in the principal, or in its absence, the most advantageous market to which the Group has access at that date. The fair value of a liability reflects its non-performance risk. When available, the Group measures the fair value of an instrument using the quoted price in an active market for that instrument. A market is regarded as active if transactions for the asset or liability take place with sufficient frequency and volume to provide pricing information on an on-going basis.

If there is no quoted price in an active market, then the Group uses the valuation techniques that maximize the use of relevant observable inputs and minimize the use of unobservable inputs. The chosen valuation technique incorporates all the factors that market participants would take into account in pricing a transaction. The best evidence of the fair value of a financial instrument at initial recognition is normally the transaction price – i.e. the fair value of the consideration given or received. If the Group determines that the fair value at initial recognition differs from the transaction price and the fair value is evidenced neither by a quoted price in an active market for an identical asset or liability nor based on a valuation technique that uses only data from observable markets, the financial instrument is initially measured at fair value, adjusted to defer the difference between the fair value at initial recognition and the transaction price. Subsequently, that difference is recognized in the consolidated statement of profit or loss on an appropriate basis over the life of the instrument but no later than when the valuation is supported wholly by observable market data or the transaction is closed out.

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

Portfolios of financial assets and financial liabilities that are exposed to market risk and credit risk that are managed by the Group on the basis of the net exposure to either market or credit risk, are measured on the basis of a price that would be received to sell a net long position or paid to transfer a net short position for a particular risk exposure. These portfolio level adjustments are allocated to the individual assets and liabilities on the basis of the relative risk adjustment of each of the individual instruments in the portfolio.

The fair value of investments in mutual funds, private equity funds or similar investment vehicles are based on the last net asset value published by the fund manager. For other investments, a reasonable estimate of the fair value is determined by reference to the price of recent market transactions involving similar investments, are based on the expected discounted cash flows.

3 Significant accounting policies *(continued)*

(b) Financial assets and liabilities *(continued)*

(vi) Fair value measurement (continued)

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

The Group recognizes transfers between levels of the fair value hierarchy as at the end of the reporting period during which the change has occurred.

(vii) Identification and measurement of impairment

An assessment is made at each reporting date and periodically during the year to determine whether there is any objective evidence that financial assets not carried at fair value through profit or loss, are impaired. Financial assets are impaired when objective evidence indicates that a loss event has occurred after the initial recognition of the asset and that the loss event has an impact on the future cash flows of the asset that can be estimated reliably.

Objective evidence that financial assets are impaired can include significant financial difficulty of the borrower or issuer, default or delinquency by a borrower, restructuring of a loan or an advance by the Group on terms that the Group would not otherwise consider, indications that a borrower or issuer will enter bankruptcy, the disappearance of an active market for a security, or other observable data relating to a group of assets such as adverse changes in the payment status of borrowers or issuers in the group, or economic conditions that correlate with defaults in the group. In addition, for an investment in an equity security, a significant or prolonged decline in its fair value below its cost is objective evidence of impairment.

The Group considers evidence of impairment for loans and advances and held to maturity investment securities at both specific and collective levels. All individually significant assets are assessed for specific impairment. All individually significant assets found not to be specifically impaired are required to be collectively assessed for any impairment that has been incurred but not yet identified. Assets that are not individually significant are collectively assessed for impairment by grouping together financial assets with similar risk characteristics.

In assessing collective impairment the Group uses IFRS and Central Bank of UAE guidelines to establish a statistical modelling which incorporates historical trends of the probability of default, timing of recoveries and the amount of loss incurred, adjusted for management's judgement as to whether current economic and credit conditions are such that the actual losses are likely to be greater or lesser than suggested by historical modelling. Default rates, loss rates and the expected timing of future recoveries are regularly benchmarked against actual outcomes to ensure that they remain appropriate.

Impairment losses on financial assets carried at amortised cost are measured as the difference between the carrying amount of the financial assets and the present value of estimated cash flows discounted at the original effective interest rate. Impairment losses are recognised in the consolidated statement of profit or loss and reflected in an allowance account against such financial assets. When a subsequent event causes the amount of impairment loss to decrease, the decrease in impairment loss is reversed through the consolidated statement of profit or loss.

Impairment losses on available-for-sale financial assets are recognised by reclassifying the losses accumulated in the fair value reserve to profit or loss. The amount reclassified is the difference between the acquisition cost (net of any principal repayment and amortisation) and the current fair value, less any impairment loss previously recognised in profit or loss. If the fair value of an impaired available-for-sale debt security subsequently increases and the increase can be related objectively to an event occurring after the impairment loss was recognised, then the impairment loss is reversed through profit or loss. Impairment losses recognised in profit or loss for an investment in an equity instrument classified as available-for-sale are not reversed through profit or loss.

Impairment losses on an unquoted equity instruments that are carried at cost because their fair value cannot be reliably measured, are measured as the difference between the carrying amount of the financial assets and the present

3 Significant accounting policies *(continued)*

(b) Financial assets and liabilities *(continued)*

(vii) Identification and measurement of impairment (continued)

values of estimated future cash flows discounted at the current market rate of return for similar financial assets. Such impairment losses shall not be reversed.

(c) Cash and cash equivalents

For the purpose of consolidated statement of cash flows, cash and cash equivalents comprise cash, balances with central banks and due from banks and financial institutions with original maturities of less than three months, which are subject to insignificant risk of changes in fair value, and are used by the Group in the management of its short-term commitments.

Cash and cash equivalents are non-derivative financial assets stated at amortised cost in the consolidated statement of financial position.

(d) Investments at fair value through profit or loss

These are financial assets classified as held for trading or designated as such upon initial recognition.

Held for trading financial assets includes debt securities, treasury bills, equity securities, short positions in securities and funds. They have been acquired or incurred principally for the purpose of selling or repurchasing in the near term, or they form part of a portfolio of identified financial instruments that are managed together and for which there is evidence of a recent pattern of short-term profit-taking. In addition, derivatives that are not effective accounting hedging instruments are carried at fair value through profit or loss.

Financial assets designated at fair value through profit or loss applies to groups of financial assets where performances are evaluated and managed on a fair value basis in accordance with a documented risk management or investment strategy.

These financial assets are initially recognised and subsequently measured at fair value with transaction costs taken directly to the consolidated statement of profit or loss. All related realised and unrealised gains or losses are included in net gain on investments.

(e) Due from banks and financial institutions

These are non-derivative financial assets that are stated at amortised cost, less any allowance for impairment.

(f) Reverse repurchase agreements

Assets purchased with a simultaneous commitment to resell at a fixed price on a specified future date are not recognised. The amount paid to the counterparty under these agreements is shown as reverse repurchase agreements in the consolidated statement of financial position. The difference between purchase and resale price is treated as interest income and accrued over the life of the reverse repurchase agreement and charged to the consolidated statement of profit or loss using the effective interest rate method.

(g) Loans and advances

Loans and advances are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market and that the Group does not intend to sell immediately or in the near term.

Loans and advances include loans and advances originated by the Group which is not classified as held for trading or designated at fair value. Loans and advances are recognised when cash is advanced to a borrower. They are derecognised when either the borrower repays its obligations, or the loans are sold or written off. These are initially measured at fair value (being the transaction price at inception) plus incremental direct transaction costs and subsequently measured at amortised cost using the effective interest rate method, adjusted for effective fair value hedges for the risk being hedged, net of interest suspended and provisions for impairment.

Notes to the consolidated financial statements *(continued)*

3 Significant accounting policies *(continued)*

(g) Loans and advances *(continued)*

Loans and advances include direct finance provided to customers such as overdrafts, credit cards, term loans, finance lease receivables and commercial bills.

When the Group is the lessor in a lease agreement that transfers substantially all of the risks and rewards incidental to ownership of the asset to the lessee, the arrangement is classified as a finance lease and a receivable equal to the net investment in the lease is recognised and presented within loans and advances.

In determining whether an arrangement is a lease, the Group ascertains the substance of the arrangement and assesses whether the fulfilment of the arrangement is dependent on the use of a specific asset or assets and whether the arrangement conveys a right to use the assets.

(h) Islamic financing and investing contracts

The Group engages in Sharia'a compliant Islamic banking activities through various Islamic instruments such as Ijara, Murabaha, Mudaraba and Wakala.

(i) Definitions

Ijara
Ijara consists of Ijara muntahia bitamleek.

Ijara financing is an agreement whereby the Group (lessor) leases or constructs an asset based on the customer's (lessee) request and promise to lease the assets for a specific period against certain rent instalments. Ijara could end in transferring the ownership of the asset to the lessee at the end of the lease period. Also, the Group transfers substantially all the risks and rewards related to the ownership of the leased asset to the lessee. Ijara income is recognised on an effective profit rate basis over the lease term.

Murabaha
A sale contract whereby the Group sells to a customer commodities and other assets at an agreed upon profit mark up on cost. The Group purchases the assets based on a promise received from customer to buy the item purchased according to specific terms and conditions. Profit from Murabaha is quantifiable at the commencement of the transaction. Such income is recognised as it accrues over the period of the contract on effective profit rate method on the balance outstanding.

Mudaraba
A contract between the Group and a customer, whereby one party provides the funds (Rab Al Mal) and the other party (the Mudarib) invests the funds in a project or a particular activity and any profits generated are distributed between the parties according to the profit shares that were pre-agreed in the contract. The Mudarib would bear the loss in case of default, negligence or violation of any of the terms and conditions of the Mudaraba, otherwise, losses are borne by the Rab Al Mal. Income is recognised based on expected results adjusted for actual results on distribution by the Mudarib, whereas if the Group is the Rab Al Mal the losses are charged to the Group's consolidated income statement when incurred.

Wakala
An agreement between the Group and customer whereby one party (Rab Al Mal) provides a certain sum of money to an agent (Wakil), who invests it according to specific conditions in return for a certain fee (a lump sum of money or a percentage of the amount invested). The agent is obliged to guarantee the invested amount in case of default, negligence or violation of any of the terms and conditions of the Wakala. The Group may be Wakil or Rab Al Mal depending on the nature of the transaction.
Estimated income from Wakala is recognised on the effective profit rate basis over the period, adjusted by actual income when received. Losses are accounted for when incurred.

Notes to the consolidated financial statements *(continued)*

3 Significant accounting policies *(continued)*

(h) Islamic financing and investing contracts *(continued)*

(ii) Revenue recognition

Ijara
Income from Ijara is recognised on a declining-value basis, until such time a reasonable doubt exists with regard to its collectability.

Murabaha
Income from Murabaha is recognised on a declining-value basis, until such time a reasonable doubt exists with regard to its collectability.

Mudaraba
Income or losses on Mudaraba financing are recognised on an accrual basis if they can be reliably estimated. Otherwise, income is recognised on distribution by the Mudarib, whereas the losses are charged to the consolidated statement of profit or loss on their declaration by the Mudarib.

Wakala
Estimated income from Wakala is recognised on an accrual basis over the period, adjusted by actual income when received. Losses are accounted for on the date of declaration by the agent.

(i) Non-trading investments

Included in non-trading investments are available-for-sale assets (debt and equity) which are initially recognised at fair value plus incremental transaction costs directly attributable to the acquisition.

After initial recognition, these investments are re-measured at fair value. For investments which are not part of an effective hedge relationship, unrealised gains or losses are recognised in other comprehensive income until the investment is derecognised or until the investment is determined to be impaired, at which time the cumulative gain or loss previously recognised in other comprehensive income, is included in the consolidated statement of profit or loss for the year. For investments which are part of an effective fair value hedge relationship, any unrealised gain or loss arising from a change in fair value is recognised directly in the consolidated statement of profit or loss to the extent of the changes in fair value being hedged.

Interest income is recognised on available-for-sale debt securities using the effective interest rate, calculated over the asset's expected life. Premiums and/or discounts arising on the purchase of debt investment securities are included in the calculation of their effective interest rates. Dividends on equity instruments are recognised in the statement of profit or loss when the right to receive payment has been established.

For the purpose of recognising foreign exchange gains and losses, an available-for-sale financial asset is treated as if it were carried at amortised cost in the foreign currency. Accordingly, for such a financial asset, exchange differences are recognised in the consolidated statement of profit or loss.

For unquoted equity investments where fair value cannot be reliably measured, these are carried at cost less provision for impairment in value. Upon de-recognition, the gain or loss on sale is recognised in the consolidated statement of profit or loss for the year.

Included in non-trading investments are held-to-maturity assets which are non-derivative assets with fixed or determinable payments and fixed maturity and that the Group has the positive intent and ability to hold them till maturity. These are initially recorded at fair value plus any directly attributable transaction costs, and are subsequently measured at amortised cost using the effective interest rate method, less any impairment losses.

A sale or reclassification of a more than insignificant amount of held-to-maturity investments would result in the reclassification of all held-to-maturity investments as available-for-sale, and would prevent the Group from classifying investment securities as held-to-maturity for the current and the following two financial years. However, sales and reclassifications in any of the following circumstances would not necessarily trigger a reclassification:

Notes to the consolidated financial statements *(continued)*

3 Significant accounting policies *(continued)*

(i) Non-trading investments *(continued)*

- sales or reclassifications that are so close to maturity that changes in the market rate of interest would not have a significant effect on the financial asset's fair value;
- sales or reclassifications after the Group has collected substantially all of the asset's original principal; and
- sales or reclassifications, which are attributable to non-recurring isolated events beyond the Group's control that could not have been reasonably anticipated.

(j) Investment properties

Investment properties are measured initially at cost, including transaction costs. Subsequent to initial recognition, investment properties are stated at fair value which reflects market conditions at the balance sheet date. Gains or losses arising from changes in the fair values of investment properties are included in the consolidated income statement under 'other income' in the year in which they arise.

Investment properties are derecognised when either they have been disposed of or when the investment property is permanently withdrawn from use and no future economic benefit is expected from its disposal. Any gains or losses on the retirement or disposal of an investment property are recognised in the consolidated income statement in the year of retirement or disposal.

(k) Property and equipment

(i) Recognition and measurement

All items of property and equipment are measured at cost less accumulated depreciation and impairment losses, if any, except for land, which is measured at fair value. Capital projects in progress are initially recorded at cost and regularly tested for impairment and upon completion are transferred to the appropriate category of property and equipment and thereafter depreciated.

Cost includes expenditures that are directly attributable to the acquisition of the asset. Purchased software that is integral to the functionality of the related equipment is capitalised as part of that equipment.

Gains and losses on disposal of an item of property and equipment are determined by comparing the proceeds from disposal with the carrying amount of property and equipment and are recognised net within other operating income in the consolidated statement of profit or loss.

Subsequent expenditures are only capitalised when it is probable that the future economic benefits of such expenditures will flow to the Group. On-going expenses are charged to consolidated statement of profit or loss as incurred.

(ii) Depreciation

Depreciation is recognised in the consolidated statement of profit or loss on a straight-line basis over the estimated useful lives of all property and equipment. Freehold land and capital work in progress are not depreciated.

The estimated useful lives of assets for the current and comparative period are as follows:

Buildings and villas	20 to 50 years
Office furniture and equipment	1 to 7 years
Alterations to premises	5-10 years
Safes	10 to 20 years
Computer systems and equipment	3 to 7 years
Vehicles	3 years

Depreciation methods, useful lives and residual values are reassessed at every reporting date.

Notes to the consolidated financial statements *(continued)*

3 Significant accounting policies *(continued)*

(k) Property and equipment *(continued)*

(iii) Capital work in progress

Capital work in progress assets are assets in the course of construction for production, supply or administrative purposes, are carried at cost, less any recognised impairment loss. Cost includes all direct cost attributable to design and construction of the property capitalised in accordance with Group's accounting policy. When the assets are ready for the intended use, the capital work in progress is transferred to the appropriate property and equipment category and is depreciated in accordance with the Group's policies.

(iv) Impairment of non-financial assets

At each reporting date, the Group reviews the carrying amounts of its non-financial assets (other than investment properties and deferred tax assets) to determine whether there is any indication of impairment. If any such indication exists, then the asset's recoverable amount is estimated. Goodwill is tested annually for impairment.

For impairment testing, assets are grouped together into smallest group of assets that generates cash inflows from continuing use that is largely independent of the cash inflows of other assets or CGUs. Goodwill arising from a business combination is allocated to CGUs or group of CGUs that are expected benefit from the synergies of the combination.

The 'recoverable amount' of an asset or CGU is the greater of its value in use and its fair value less cost to sell. 'Value in use' is based on the estimated future cash flows, discounted to their present value using pre-tax discount rate that reflects current market assessments of the time value of money and the risk specific to the asset or CGU.

An impairment loss is recognized if the carrying amount of an asset or CGU exceeds its recoverable amount.

The Group's corporate assets do not generate separate cash inflows and are used by more than one CGU. Corporate assets are allocated to CGUs on a reasonable and consistent basis and tested for impairment as part of the testing of the CGUs to which the corporate assets are allocated.

Impairment losses are recognized in profit or loss. They are allocated first to reduce the carrying amount of any goodwill allocated to the CGU, and then to reduce the carrying amounts of any other assets in the CGU on a prorate basis.

An impairment loss in respect of goodwill is not reversed. For other assets, an impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortization, if no impairment loss had been recognized.

(l) Intangible assets

Goodwill arises on the acquisition represents the excess of the consideration transferred, the amount of any non-controlling interest in the acquiree and the acquisition-date fair value of any previous equity interest in the acquiree over the fair value of the identifiable net assets acquired. If the total of consideration transferred, non-controlling interest recognised and previously held interest measured at fair value is less than the fair value of the net assets of the subsidiary acquired in case of a bargain purchase, the difference is recognised directly in the income statement.

For the purpose of impairment testing, goodwill acquired in a business combination is allocated to each of the CGUs, or groups of CGUs, that is expected to benefit from the synergies of the combination. Each unit or group of units to which the goodwill is allocated represents the lowest level within the entity at which the goodwill is monitored for internal management purposes. Goodwill is monitored at the operating segment level.

Goodwill impairment reviews are undertaken annually or more frequently if events or changes in circumstances indicate a potential impairment. The carrying value of the CGU containing the goodwill is compared to the recoverable amount, which is the higher of value in use and the fair value less costs of disposal. Any impairment is recognised immediately as an expense and is not subsequently reversed.

Notes to the consolidated financial statements *(continued)*

3 Significant accounting policies *(continued)*

(l) Intangible assets *(continued)*

The Group's intangible assets other than goodwill include intangible assets arising out of business combinations. The cost of intangible assets acquired in a business combination is their fair value at the date of acquisition. 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 accumulated impairment losses.

The useful lives of intangible assets are assessed as either finite or indefinite. 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 are reviewed at least at the end of each reporting period. Changes in the expected useful life or the expected pattern of consumption of future economic benefits embodied in the asset are considered to modify the amortisation period or method, as appropriate, and are treated as changes in accounting estimates. The amortisation expense on intangible assets with finite lives is recognised in the consolidated income statement.

The estimated useful lives of the intangible assets for the calculation of amortisation are as follows:

Brand	20 years
Customer relationships	7.5 – 15 years
Core deposits	2.5 years – 15 years

(m) Collateral pending sale

Real estate and other collateral may be acquired as the result of settlement of certain loans and advances and are recorded as assets held for sale and reported in "Other assets". The asset acquired is recorded at the lower of its fair value less costs to sell and the carrying amount of the loan (net of impairment allowance) at the date of exchange. No depreciation is provided in respect of assets held for sale. Any subsequent write-down of the acquired asset to fair value less costs to sell is recorded as an impairment loss and included in the consolidated statement of profit or loss. Any subsequent increase in the fair value less costs to sell, to the extent this does not exceed the cumulative impairment loss, is recognised in the consolidated statement of profit or loss. The Group's collateral disposal policy is in line with the respective regulatory requirement of the regions in which the Group operates.

(n) Due to banks and financial institutions, Customer accounts and other deposits and Commercial Paper

Due to banks and financial institutions, customer deposits and Commercial Paper are financial liabilities and are initially recognised at their fair value minus the transaction costs and subsequently measured at their amortised cost using the effective interest rate method.

(o) Repurchase agreements

Assets sold with a simultaneous commitment to repurchase at a fixed price on a specified future date are not derecognised. The liability to the counterparty for amounts received under these agreements is shown as repurchase agreements in the consolidated statement of financial position. The difference between sale and repurchase price is treated as interest expense and accrued over the life of the repurchase agreement and charged to the consolidated statement of profit or loss using the effective interest rate method.

(p) Term borrowings and subordinated notes

Term borrowings and subordinated notes include convertible notes that can be converted into share capital at the option of the holder, where the number of shares issued do not vary with changes in their fair value, are accounted for as compound financial instruments. The equity component of the convertible notes is calculated as the excess of issue proceeds over the present value of the future interest and principal payments, discounted at the market rate of interest applicable to similar liabilities that do not have a conversion option.

Notes to the consolidated financial statements *(continued)*

3 Significant accounting policies *(continued)*

(p) Term borrowings and subordinated notes *(continued)*

Term borrowings and subordinated notes without conversion option and that are not designated at fair value through profit or loss are financial liabilities which are initially recognised at their fair value minus the transaction costs and subsequently measured at their amortised cost using the effective interest rate method and adjusted to the extent of fair value changes for the risks being hedged.

(q) Treasury shares

Own equity instruments which are acquired (treasury shares) are deducted from the equity and accounted for at weighted average cost. No gain or loss is recognised in the consolidated income statement on the purchase, sale, issue or cancelation of the Bank's own equity instruments. Any difference between the carrying amount and the consideration, if reissued, is recognised in share premium. If treasury shares are distributed as part of a bonus share issue, the cost of the shares is charged against retained earnings. Voting rights relating to treasury shares are nullified for the Group and no dividends are allocated to them respectively.

(r) Fiduciary assets

Assets held in trust or in a fiduciary capacity are not treated as assets of the Group and accordingly are not included in these consolidated financial statements.

(s) Share option scheme

On the grant date fair value of options granted to staff is estimated and the cost is recognised as staff cost, with a corresponding increase in equity, over the period required for the staff to become unconditionally entitled to the options. The amount recognised as an expense is adjusted to reflect the number of share options for which the related service conditions are expected to be met; as such the amount ultimately recognised as an expense is based on the number of share options that do meet the related service and non-market performance conditions at the vesting date. These shares may contribute to the calculation of dilutive EPS once they are deemed as potential ordinary shares.

(t) Interest income and expense

Interest income and expense are recognised in the consolidated statement of profit or loss using the effective interest rate method. The effective interest rate is the rate that exactly discounts estimated future cash receipts or payments through the expected life of the financial instrument or, where appropriate, a shorter period, to the net carrying amount of the financial asset or financial liability. When calculating the effective interest rate, the Group estimates cash flows considering all contractual terms of the financial instrument but excluding future credit losses. The calculation includes all amounts paid or received by Group that are an integral part of the effective interest rate of a financial instrument, including transaction costs and all other premiums or discounts. Transaction costs include incremental costs that are directly attributable to the acquisition or issue of a financial asset or liability.

Interest income and expense presented in the consolidated statement of profit or loss include:

- interest on financial assets and liabilities at amortised cost on an effective interest rate basis;
- interest on available-for-sale investment securities on an effective interest rate basis;
- interest on held for trading securities and derivative financial instruments on an effective interest rate basis; the effective portion of fair value changes in qualifying hedging derivatives designated in cash flow hedges of variability in interest cash flows, in the same period as hedged cash flows affect interest income/expense; and
- the effective portion of fair value changes in qualifying hedging derivatives designated in fair value hedges of interest rate risk.

(u) Income from Islamic financing activities

Ijara income is recognised on a time-proportion basis over the lease term.

Notes to the consolidated financial statements *(continued)*

3 Significant accounting policies *(continued)*

(u) Income from Islamic financing activities *(continued)*

Murabaha income is recognised on a time apportioned basis over the period of the contract based on the principal amounts outstanding. Mudaraba income is recognised based on expected results adjusted for actual results on distribution by the Mudarib, whereas if the Group is the Rab Al Mal the losses are charged to the Group's consolidated income statement when incurred.

(v) Depositors' share of profit

Depositors' share of profit is amount accrued as expense on the funds accepted from banks and customers in the form of wakala and mudaraba deposits and recognised as expenses in the consolidated statement of profit or loss. The amounts are calculated in accordance with agreed terms and conditions of the wakala deposits and Sharia'a principles.

(w) Fee and commission income

The Group earns fee and commission income from a diverse range of services provided to its customers. The basis of accounting treatment of fees and commission depends on the purposes for which the fees are collected and accordingly the revenue is recognised in consolidated statement of profit or loss. Fee and commission income is accounted for as follows:

- income earned from the provision of services is recognised as revenue as the services are provided;
- income earned on the execution of a significant act is recognised as revenue when the act is completed;
- income which forms an integral part of the effective interest rate of a financial instrument is recognised as an adjustment to the effective interest rate and recorded in "Interest income".

Fee and commission expense relates mainly to transaction and service fees which are expensed as the services are received.

(x) Zakat

Zakat represents Islamic business zakat payable by the Group on behalf of its shareholders to comply with the principles of Sharia'a and is approved by the Sharia'a Supervisory Board. The Group's appointed Zakat Committee is mandated to recommend zakat distribution.

(y) Net gain/loss on investments and derivatives

Net gain on investments and derivatives comprises realised and unrealised gains and losses on investments at fair value through profit or loss and derivatives, realised gains and losses on non-trading investments and dividend income. Net gain on investment at fair value through profit or loss includes changes in the fair value of financial assets and financial liabilities held for trading and net income from investments designated at fair value.

Gains and losses arising from changes in fair value of available for sale assets are recognised in the statement of other comprehensive income and recorded in fair value reserve with the exception of impairment losses, interest calculated using the effective interest rate method and foreign exchange gains and losses on monetary assets which are recognised directly in the consolidated statement of profit or loss. Where the investment is sold or realised, the cumulative gain or loss previously recognised in equity under fair value reserve is reclassified to the consolidated statement of profit or loss.

Non-trading investment includes available for sale and held to maturity instruments.

Held to maturity investments, which are not close to their maturity are not ordinarily sold. However when they are sold or realised, the gain or loss is recognised in the consolidated statement of profit or loss.

Dividend income is recognised when the right to receive payment is established.

3 Significant accounting policies *(continued)*

(z) Foreign currency

(i) Foreign currency transactions

Transactions in foreign currencies are translated into the respective functional currencies of the Group entities at spot exchange rates at the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies at the reporting date are retranslated to the functional currency at the spot exchange rates at the reporting date. The foreign currency gain or loss on monetary items is the difference between amortised cost in the functional currency at the beginning of the period, adjusted for effective interest and payments during the period, and the amortised cost in foreign currency translated at the exchange rate at the end of the period.

Non-monetary assets and liabilities that are measured at fair value in a foreign currency are translated into the functional currency at the spot exchange rate at the date on which the fair value is determined. Non-monetary assets and liabilities that are measured in terms of historical cost in a foreign currency are translated using the exchange rate at the date of the transaction.

Foreign currency differences arising on transaction are generally recognized in profit or loss. However, foreign currency differences arising from the transaction arising from the translation of the following item are recognized in OCI.
- available for sale equity instruments
- a financial liability designated as a hedge of the net investment in a foreign operation to the extent that the hedge is effective
- qualifying cash flow hedges to the extent that the hedge is effective.

(ii) Foreign operations

The activities of subsidiaries and branches based outside the UAE are not deemed an integral part of the head office operations, as they are financially and operationally independent of the head office. The assets and liabilities of the foreign operations are translated into UAE Dirhams at rates of exchange at the reporting date. The income and expense of foreign operations are translated at average rates, as appropriate. Exchange differences (including those on transactions which hedge such investments) arising from retranslating the opening net assets, are taken directly to foreign currency translation adjustment account in other comprehensive income.

When a foreign operation is disposed of such that control is lost, the cumulative amount in the translation reserve related to the foreign operation is reclassified to profit or loss as part of the gain or loss on disposal. If the Group disposes of only part of its interest in a subsidiary that includes a foreign operation while retaining control, then the relevant proportion of the cumulative amount is reattributed to NCI.

If the settlement of a monetary receivable from or payable to a foreign operation is neither planned nor likely in the foreseeable future, then foreign currency differences arising on the item form part of the net investment in the foreign operation and recognized in OCI, and accumulated in the translation reserve in the equity.

(aa) Overseas income tax expense

Income tax expense comprises of the current and deferred tax. It is recognized in profit or loss except the extent it relates to items recognized directly in equity or OCI.

Current tax is provided for in accordance with fiscal regulations of the respective countries in which the Group operates and is recognised in the consolidated statement of profit or loss. Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantively enacted at the reporting date and any adjustment to tax payable in respect of previous years.

Deferred tax is recognised in respect of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred tax is not recognised for the following temporary differences: the initial recognition of goodwill, the initial recognition of assets or liabilities in a transaction that is not a business combination and that affects neither accounting nor taxable profit or loss, and differences relating to investments in subsidiaries to the extent that they probably will not reverse in the foreseeable

Notes to the consolidated financial statements *(continued)*

3 Significant accounting policies *(continued)*

(aa) Overseas income tax expense *(continued)*

future. Deferred tax is measured at the tax rates that are expected to apply to the period when the asset is realised or the liability is settled, based on laws that have been enacted at the reporting date.

A deferred tax asset is recognised only to the extent that it is probable that future taxable profits will be available against which the asset can be utilised. The carrying amount of deferred tax assets is reviewed at each reporting date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred tax asset to be utilised.

The measurement of deferred tax reflects the tax consequences that would follow the manner in which the Group expects, at the reporting date, to recover or settle the carrying amount of its assets and liabilities.

In determining the amount of current and deferred tax, the Group considers the impact of tax exposures, including whether additional taxes and interest maybe due. This assessment relies on estimates and assumptions and may involve a series of judgements about future events. New information may become available that causes the Group to change its judgement regarding the adequacy of existing tax liabilities; such changes to tax liabilities would impact tax expense in the period in which such a determination is made.

(ab) Derivative financial instruments and hedging

Derivatives are initially recognised, and subsequently measured at fair value with transaction costs taken directly to the consolidated statement of profit or loss. The fair value of a derivative is the equivalent of the unrealised gain or loss from marking to market the derivative or using valuation techniques, mainly discounted cash flow models.

The method of recognising the resulting fair value gains or losses depends on whether the derivative is held for trading, or is designated as a hedging instrument and, if so, the nature of the risk being hedged. All gains and losses from changes in fair value of derivatives held for trading are recognised in the consolidated statement of profit or loss. When derivatives are designated as hedges, the Group classifies them as either: (i) fair value hedges which hedge the exposure to changes in the fair value of a recognised asset or liability; (ii) cash flow hedges which hedge exposure to variability in cash flows that is either attributable to a particular risk associated with a recognised asset or liability or a highly probable forecast transaction; (iii) hedge of net investment which are accounted similarly to a cash flow hedge. Hedge accounting is applied to derivatives designated as hedging instruments in a fair value or cash flow, provided the criteria are met.

Embedded derivatives
Derivatives may be embedded in another contractual arrangement (a host contract). The Group accounts for an embedded derivative separately from the host contract when the host contract is not itself carried at fair value through profit or loss, the terms of the embedded derivative would meet the definition of a derivative if they were contained in a separate contract, and the economic characteristic and risks of the embedded derivative are not closely related to the economic characteristics and risk of the host contract. Separated embedded derivatives are measured at fair value, with all changes in fair value recognised in profit or loss unless they form part of a qualifying cash flow or net investment hedging relationship, and are presented separately from host contract in the consolidated statement of financial position.

Hedge accounting
It is the Group's policy to document, at the inception of a hedge, the relationship between hedging instruments and hedged items, as well as risk management objective and strategy. The policy also requires documentation of the assessment, at inception and on an on-going basis, of the effectiveness of the hedge.

The Group makes an assessment, both at the inception of the hedge relationship as well as on an on-going basis, as to whether the hedging instrument(s) is (are) expected to be highly effective in offsetting the changes in the fair value or cash flows of the respective hedged item(s) during the period for which the hedge is designated, and whether the actual results of each hedge are within a range of 80-125 percent. The Group makes an assessment for a cash flow hedge of a forecast transaction, as to whether the forecasted transaction is highly probable to occur and presents an exposure to variations in cash flows that could ultimately affect profit or loss.

Notes to the consolidated financial statements *(continued)*

3 Significant accounting policies *(continued)*

(ab) Derivative financial instruments and hedging *(continued)*

Fair value hedge
In relation to fair value hedges, any gain or loss from re-measuring the hedging instrument to fair value, as well as related changes in fair value of the item being hedged, are recognised immediately in the consolidated statement of profit or loss together with the changes in the fair value of the hedged item that are attributable to the hedged risk. Hedge accounting is discontinued when the hedging instrument expires or is sold, terminated or exercised, or no longer qualifies for hedge accounting. However if the derivative is novated to a central counterparty by both parties as a consequence of laws or regulations without changes in its terms except for those that are necessary for the novation, then the derivative is not considered as expired or terminated. Any adjustment up to that period to the hedged item for which effective interest rate method was used is amortised to the consolidated statement of profit or loss as a part of the recalculated effective interest rate of the then hedged item over its remaining life.

Cash flow hedge
When a derivative is designated as the hedging instrument in a hedge of the variability in cash flow attributable to a particular risk associated with a recognized assets or liability that could affect profit or loss, the effective portion of changes in the fair value of the derivatives is recognized in OCI and presented in the hedging reserve within equity. Any ineffective portion of changes in the fair value of the derivative is recognized immediately in the profit or loss. The amount recognized in OCI is reclassified to profit or loss as a reclassification adjustment in the same period as the hedged cash flows affect profit or loss and in the same line in the statement of profit or loss and OCI. If the hedging derivative expires of sold, terminated or exercised or the hedge, no longer meets the criteria for cash flow hedge accounting the hedge accounting is discounted prospectively. However if the derivative is novated to a central counterparty by both parties as a consequence of laws or regulations without changes in its terms except for those that are necessary for the novation, then the derivative is not considered as expired or terminated

Net investments hedges
When a derivative instrument or a non-derivative financial liability is designated as the hedging instrument in a hedge of a net investment in a foreign operation, the effective portion of the changes in the fair value of the hedging instrument is recognised in other comprehensive income in the translation reserve. Any ineffective portion of the changes in the fair value of the derivative is recognised immediately in the consolidated statement of profit or loss. The amount recognised under other comprehensive income is reclassified to statement of profit or loss on disposal of the foreign operation.

Other derivatives
All gains and losses from changes in the fair values of derivatives that do not qualify for hedge accounting or are not designated as such are recognised immediately in the consolidated statement of profit or loss as a component of net gain on investments and derivatives or net foreign exchange gain.

(ac) Provisions

A provision is recognised if, as a result of a past event, the Group has a present legal or constructive obligation that can be estimated reliably, and it is probable that an outflow of economic benefits will be required to settle the obligation. Where the effect of time value of money is material, provisions are determined by discounting the expected future cash flows, at a pre-tax rate, that reflects current market assessments of the time value of money and, where appropriate, the risks specific to the liability.

(ad) Employees' end of service benefit

The Group provides end of service benefits for its employees. The entitlement to these benefits is based upon the employees' length of service and completion of a minimum service period. The expected costs of these benefits are accrued over the period of employment.

With respect to its UAE national employees, the Group makes contributions to the relevant government pension scheme calculated as a percentage of the employees' salaries. The Group's obligations are limited to these contributions, which are expensed when due.

Notes to the consolidated financial statements *(continued)*

3 Significant accounting policies *(continued)*

(ad) Employees' end of service benefit *(continued)*

Defined contribution plan
A defined contribution plan is a post-employment benefit plan under which an entity pays fixed contributions into a separate entity or to a government organisation and will have no legal or constructive obligation to pay further amounts. Obligations for contributions to defined contribution pension plans are recognised as an employee benefit expense in consolidated statement of profit or loss in the periods during which services are rendered by employees.

Pension and national insurance contributions for eligible employees are made by the Group to Pensions and Benefits Fund in accordance with the applicable laws of country where such contributions are made.

Defined benefit plan
A defined benefit plan is a post-employment benefit plan other than a defined contribution plan. The liability recognised in the statement of financial position in respect of defined benefit gratuity plans is the present value of the defined benefit obligation at the end of the reporting period together with adjustments for unrecognised past-service costs. The defined benefit obligation is calculated annually by independent actuaries using the projected unit credit method. The present value of the defined benefit obligation is determined by discounting the estimated future cash outflows using interest rates of high-quality corporate bonds that are denominated in the currency in which the benefits will be paid, and that have terms to maturity approximating to the terms of the related pension obligation.

Remeasurements of the net defined benefit liability, which comprise actuarial gains and losses, the return on plan assets (excluding interest) and the effect of the asset ceiling (if any, excluding interest), are recognised immediately in OCI. Net interest expense and other expenses related to defined benefit plans are recognised in Staff cost in consolidated statement of profit or loss. When the benefits of a plan are changed or when a plan is curtailed, the resulting change in benefit that relates to past service or the gain or loss on curtailment is recognised immediately to profit or loss. The Group recognises gains and losses on the settlement of a defined benefit plan when the settlement occurs.

(ae) Directors' remuneration

Pursuant to Article 118 of the Commercial Companies Law No. 8 of 1984 and in accordance with the Bank's Articles of Association, Directors' shall be entitled for remuneration which shall not exceed 10% of the net profits after deducting depreciation, reserves and distribution of dividends not less than 5% of capital to shareholders.

(af) Fiduciary activities

Assets held in a fiduciary capacity are not treated as assets of the Group as they are only held in trust where the Group acts as a custodian on customers' behalf. The Group has no liability or obligations towards the customer on these assets held in trust. Accordingly, these assets are not included in these consolidated financial statements.

(ag) Earnings per share

The Group presents basic and diluted earnings per share (EPS) data for its ordinary shares. Basic EPS is calculated by dividing the profit or loss attributable to ordinary shareholders of the Group by the weighted average number of ordinary shares outstanding during the year. Diluted EPS is determined by adjusting the profit or loss attributable to ordinary shareholders and the weighted average number of ordinary shares outstanding for the effects of all dilutive potential ordinary shares, which comprise of convertible notes and share options granted to staff.

(ah) Financial guarantees

Financial guarantees are contracts that require the Group to make specified payments to reimburse the holder for a loss it incurs because a specified party fails to meet its obligation when due in accordance with the contractual terms.

Certain financial guarantee contracts in the nature of credit default guarantees are not held for proprietary trading purposes and are treated as insurance contracts and accounted for under IFRS 4.

3 Significant accounting policies *(continued)*

(ah) Financial guarantees *(continued)*

For other financial guarantee contracts, these are initially recognised at their fair value (which is the premium received on issuance). The received premium is amortised over the life of the financial guarantee. The guarantee liability is subsequently carried at the higher of this amortised amount and the present value of any expected payment (when a payment under the guarantee has become probable). The premium received on these financial guarantees is included within other liabilities.

Financial guarantees are reviewed periodically so as to determine the credit risk to which they are exposed and, if appropriate, to consider whether a provision is required. The credit risk is determined by application of criteria similar to those established for quantifying impairment losses on loans and advances. If a specific provision is required for financial guarantees, the related unearned commissions recognised under other liabilities in the consolidated balance sheet are reclassified to the appropriate provision.

(ai) Segment reporting

An operating segment is a component of the Group that engages in business activities from which it may earn revenues and incur expenses, including revenues and expenses that relate to transactions with any of the Group's other components. All operating segments' operating results are reviewed regularly by the Group's Chief Executive, being the chief operating decision maker, to make decisions about resources to be allocated to the segment and to assess its performance for which discrete financial information is available. Segment results that are reported to the Group Chief Executive include items directly attributable to a segment as well as those that can be allocated on a reasonable basis.

(aj) Lease payments

Finance leases, which transfer to the Group substantially all the risks and benefits incidental to ownership of the leased item, are capitalised at the inception of the lease at the fair value of the leased asset or, if lower, at the present value of the minimum lease payments. Lease payments are apportioned between the finance charges and reduction of the lease liability so as to achieve a constant rate of interest on the remaining balance of the liability. Finance charges are charged directly against income. Capitalised leased assets are depreciated over the shorter of the estimated useful life of the asset or the lease term.

Leases where the lessor retains substantially all the risks and benefits of ownership of the asset are classified as operating leases. Operating lease payments are recognised as an expense in the consolidated income statement on a straight line basis over the shorter of the lease term or the estimated useful life of the asset.

(ak) Settlement date accounting

Purchases and sales of financial assets are recognised on the settlement date, i.e. the date that the Group settles the purchase or sale of an asset.

(al) Taxes

Current income tax assets and liabilities for the current period are measured at the amount expected to be recovered from or paid to the taxation authorities. The tax rates and tax laws used to compute the amount are those that are enacted or substantively enacted, at the reporting date in the countries where the Group operates and generates taxable income. Taxable profit differs from profit as reported in the consolidated income statement because it excludes items of income or expense that are taxable or deductible in other years and it further excludes items that are never taxable or deductible.

Deferred income tax is provided using the liability method on temporary differences at the reporting date between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes. Deferred income tax assets are recognised for all deductible temporary differences, carry forward of unused tax credits and unused tax losses, to the extent that it is probable that taxable profits will be available against which the deductible temporary differences, and the carry forward of unused tax credits and unused tax losses can be utilised.

Notes to the consolidated financial statements *(continued)*

3 Significant accounting policies *(continued)*

(am) New standards and interpretations not yet adopted

A number of new standards are effective for annual periods beginning after 1 January 2017 and earlier application is permitted; however, the Group has not early adopted the new or amended standards in preparing these consolidated financial statements.

The following standards are expected to have a material impact on the Group's financial statements in the period of initial application.

IFRS 15 — *Revenue from contracts with customer:* issued in May 2014 and establishes a five-step model to account for revenue arising from contracts with customers. Under IFRS 15, revenue is recognised at an amount that reflects the consideration to which an entity expects to be entitled in exchange for transferring goods or services to a customer. It replaces all existing revenue recognition guidance, including IAS 18 Revenue, IAS 11 Construction Contracts and IFRIC Customer loyalty programmes.

IFRS 15 is effective for annual period beginning on or after 1 January 2018, with early adoption permitted. The Group has assessed the potential impact of this standard and believes that it will not have any material impact on its consolidated financial statements.

IFRS 16 — IFRS 16 was issued in January 2016. It will result in almost all leases being recognised on the balance sheet, 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.

IFRS 16 is effective for annual period beginning on or after 1 January 2019, with early adoption permitted. The Group is still in the process of assessing the impact.

IFRS 9 — On July 24, 2014, the IASB issued IFRS 9 Financial Instruments ("the Standard"), which will replace IAS 39. The Standard covers three broad topics: Classification and Measurement, Impairment and Hedging.

<u>Governance and project management</u>
The adoption of IFRS 9 is a significant initiative for the Group, involving substantial finance, risk management and technology resources. The project was managed through a detailed governance structure across risk management, finance, technology, and the business units. The Group's existing system of internal controls will be refined and revised where required to meet the requirements of IFRS 9. The Group has applied many components of its existing governance framework to ensure that appropriate validations and controls will be in place over new key processes and significant areas of judgment. Adoption of IFRS 9 in 2018 has resulted in revisions to accounting policies and procedures, changes and amendments to internal control documents, applicable credit risk manuals, development of new risk models and associated methodologies and new processes within risk management. Periodic reporting on the progress against plan and results of parallel run was provided to the Group's senior management throughout 2017.

The following is a summary of some of the more significant items that are likely to be important in understanding the impact of the implementation of IFRS 9:

<u>Classification and measurement</u>

The Standard introduces new requirements to determine the measurement basis of financial assets, involving the cash flow characteristics of assets and the business models under which they are managed. Accordingly, the basis of measurement for the Bank's financial assets may change. The Standard affects the accounting for available-for-sale equity securities, requiring a designation, by portfolio, between recording both unrealized and realized gains either through (i) OCI with no recycling to income or (ii) Income Statement. As a result, the amount of equity securities gains recorded through income is expected to be lower than current levels and levels recorded in recent

3 Significant accounting policies *(continued)*

(am) New standards and interpretations not yet adopted *(continued)*

years except for the private equity portfolio. For other financial instruments, the Bank does not expect the implementation will result in a significant change in the classification and measurement of the Bank's financial assets, between Amortized cost, Fair Value through OCI and Fair Value through Income Statement.

<u>Hedge Accounting</u>
IFRS 9 also incorporates new hedge accounting rules that intend to align hedge accounting with risk management practices. IFRS 9 includes an accounting policy choice to defer the adoption of IFRS 9 hedge accounting and to continue with IAS 39 hedge accounting. The Group has decided to exercise this accounting policy choice. However, the Group will implement the revised hedge accounting disclosures that are required by the IFRS 9 related amendments to IFRS 7 "Financial Instruments: Disclosures" in its 2018 Annual Report.

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

The Bank has developed new methodologies and models taking into account the relative size, quality and complexity of the portfolios. IFRS 9 considers the calculation of ECL by multiplying the Probability of default (PD), Loss Given Default (LGD) and Exposure at Default (EAD).

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

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

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

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

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

3 Significant accounting policies *(continued)*

(am) New standards and interpretations not yet adopted *(continued)*

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

Macroeconomic Factors, Forward Looking Information (FLI) and Multiple Scenarios
IFRS 9 requires an unbiased and probability weighted estimate of credit losses by evaluating a range of possible outcomes that incorporates forecasts of future economic conditions.

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

The Bank will use three scenarios that will be probability weighted to determine ECL.

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

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

Definition of Default and Write-off
Default definition followed by the Bank for impairment assessment remains in line with the guidelines of IFRS 9, without any recourse to the assumptions. IFRS 9 presumption of default is currently under internal review and might differ for the actual results subsequently where a reasonable justification exists to rebut the presumption. Inputs into the assessment of whether a financial instrument is in default and their significance may vary over time to reflect changes in circumstances.

Transition impact
The Group will record an adjustment to its opening January 1, 2018 retained earnings and OCI, to reflect the application of the new requirements of Impairment and Classification and Measurement at the adoption date and will not restate comparative periods.

The Group estimates the IFRS 9 transition amount will reduce shareholders' equity in the range of 2.8% to 3.2% of total shareholders' equity and common equity Tier 1 ratio by 57bps to 68bps The estimated impact relates primarily to the implementation of the ECL requirements. The assessment made by the Group is preliminary and as part of the implementation of the new standard the Group will continue to refine its model assumptions, accounting policies, governance framework and estimation techniques employed leading up to 31 March 2018 reporting.

Notes to the consolidated financial statements *(continued)*

3 Significant accounting policies *(continued)*

(am) New standards and interpretations not yet adopted *(continued)*

Transition impact *(continued)*
The Group's available for sale investments includes investments in private equity and shares in non-listed companies. As part of IFRS 9 transitional provision, investment in private equity will be classified to investment at fair value through profit or loss and mark to marked changes in the investment going forward shall be accounted in profit or loss which would result in volatility in profit or loss. Equity shares in non-listed companies that are held for the foreseeable future shall be accounted through other comprehensive income and this application will not have significant impact in Group's performance.

Loans as well as receivables are held to collect contractual cash flows and are expected to give rise to cash flows representing solely payments of principal and interest. Thus, the Group expects that these will continue to be measured at amortised cost under IFRS 9. However, the Group will further analyse the contractual cash flow characteristics of those instruments in more detail before concluding whether all those instruments meet the criteria for amortised cost measurement under IFRS 9.

Hedge accounting
The Group believes that all existing hedge relationships that are currently designated in effective hedging relationships will still qualify for hedge accounting under IFRS 9. As IFRS 9 does not change the general principles of how an entity accounts for effective hedges, the Group does not expect a significant impact as a result of applying IFRS 9. The Group will assess possible changes related to the accounting for the time value of options, forward points or the currency basis spread in more detail in the future.

IFRS 9 is effective for annual periods beginning on or after 1 January 2018. Except for hedge accounting, retrospective application is required but providing comparative information is not compulsory. For hedge accounting, the requirements are generally applied prospectively, with some limited exceptions. The Group plans to adopt the new standard on the required effective date.

Implementation status
The Group continues to progress with the Global IFRS 9 implementation project with the documentation of Group accounting policy, assessment of business models, the build and testing of risk modeling methodologies for the calculation of impairment currently ongoing. The implementation is overseen by Project Steering Committee comprising of key stakeholders from Finance, Risk and Technology.

4 Financial risk management

Introduction and overview

Risk management framework

The primary objective of the Group is to manage risk and provide returns to the shareholders in line with the accepted risk profile. In the course of doing its regular business activities, the Group gets exposed to multiple risks notably credit risk, market risk, liquidity and funding risk, interest rate risk, operational risk and other risks like compliance risk, strategic risk, reputation risk, information security risk and business continuity. A well-established risk governance and ownership structure ensures oversight and accountability of the effective management of risk at the Group. The Risk management tone is set right at the top from the Board of Directors ("BOD") and gets implemented through a well-defined risk management structure and framework.

Composition of Board

The Board of Directors ("BOD") BOD is responsible for the overall direction, supervision and control of the Group. The day-to-day management of the Group is conducted by the BOD committees, and the Chief Executive Officer ("CEO"). The BOD has overall responsibility for the Group including approving and overseeing the implementation of its strategic objectives, risk strategy, corporate governance and corporate values within the agreed framework in accordance with relevant statutory and regulatory structures. The BOD currently comprises nine members. Each Director holds his position for three years, which may then be renewed for a further three year term. The Board of Directors of the Bank's subsidiaries has the same responsibilities towards their respective entities as the Group's Directors have towards the Bank.

Corporate Governance Framework

The Group has a comprehensive corporate governance framework that puts in place rules, processes and policies through which BOD and Senior Management manages of the Group. The BOD drives the implementation of the corporate governance standards and is the custodian of the corporate governance manual. The Group's corporate governance standards bind its signatories to the highest standards of professionalism and due diligence in the performance of their duties. The Group Chief Risk Officer ("GCRO") is the custodian of the Corporate Governance Manual.

Risk Management Structure

The BOD approves risk management plans for the Bank, its subsidiaries, its associates and international offices including representative offices and overseas branches. Under authority delegated by the BOD, Board level risk committee – Board Risk and Compliance Committee ("BRCC") through its separately convened risk management meetings formulates high-level enterprise risk management policy, exercises delegated risk authorities and oversees the implementation of risk management framework and controls. The GCRO functionally reports to this committee.

Board Level Committees within the Group

<u>Board Management Committee ("BMC")</u>

BMC comprises three members of the BOD and the CEO. BMC oversees execution of the Group's business plan as per the strategy approved by the Board and oversees and reviews material aspects of the business of the Group. The Committee meets quarterly or more frequently as deemed necessary. The composition, guiding principles and detailed roles and responsibilities are covered in the BMC charter.

<u>Board Risk and Compliance Committee ("BRCC")</u>

BRCC comprises three members of the BOD and the CEO and is responsible for recommending and setting the Group risk strategy, risk appetite, policy guidelines and subsequent monitoring adherence The Committee meets quarterly or more frequently as deemed necessary. The composition, guiding principles and detailed roles and responsibilities are covered in the BRCC's charter.

Notes to the consolidated financial statements *(continued)*

4 Financial risk management *(continued)*

Risk management framework *(continued)*

Board Level Committees within the Group *(continued)*

Board Audit Committee ("BAC")
BAC comprises three members of the BOD and the CEO. BAC ensures oversight of the effectiveness of the internal control systems and the quality and integrity of financial statements and financial reporting. The Committee meets quarterly or more frequently as deemed necessary. The composition, guiding principles and detailed roles and responsibilities are covered in the Board Audit Committee's charter.

Remuneration and Nomination Committee ("REMCO")
REMCO comprises three members of the BOD and the CEO. REMCO recommends and oversees the appointment and termination of Directors and where appropriate members of the Group Executive Committee and ensures that they discharge their responsibilities in the interests of the shareholders and Group. The Committee also approves and oversees reward design and ensures it is appropriate and consistent with the Group's culture, values, business performance and risk strategy. The Committee meets at least twice a year or more frequently as deemed necessary. The composition, guiding principles and detailed roles and responsibilities are covered in REMCO's charter.

Management Level Committees within the Group

Management committees are responsible for implementing the Risk management framework. The major functions of the five management committees are listed below:

Group Executive Committee ("EXCO")
EXCO is the most senior management committee operating under a delegated authority from the Board. It is responsible for managing strategic, financial and capital, risk and operational issues affecting the Group. The Group CEO and the Executive Management team (EXCO members) are principally responsible for executing the agreed business strategy, controlling and monitoring the risk within the agreed risk appetite. EXCO consists of the executive management team and is chaired by the Group Chief Executive Officer. The composition, guiding principles and detailed roles and responsibilities of EXCO are covered in the EXCO's charter.

Corporate & Investment Banking Credit Committee ("CIBCC")
CIBCC assists EXCO in the development and implementation of the Group's Corporate & Investment Banking business credit strategy and policies and procedures. The purpose of the CIBCC is to oversee the credit and lending strategies and objectives of the Group, including identifying and managing the Group's Corporate & Investment Banking credit exposures and its response to trends affecting those exposures. It also assists in reviewing the quality and performance of the Group's credit portfolio; and overseeing the Corporate & Investment Banking credit function of the Group, including reviewing internal credit risk and credit policies and establishing portfolio limits. The composition, guiding principles and detailed roles and responsibilities of CIBCC are covered in the CIBCC's charter.

Personal Banking Credit Committee ("PBCC")
PBCC assists EXCO in the development and implementation of credit strategy, for personal banking businesses. The Committee has been set up in order to ensure a holistic overview of the business strategies across the Personal Banking businesses of the Group. The Committee oversees the credit and lending strategies, Identifies and manages business credit strategy and strategic response to trends affecting the businesses; reviews the quality and performance of the portfolio; and Oversees the credit risk management function including establishing product portfolio limits. The composition, guiding principles and detailed roles and responsibilities of PBCC are covered in the PBCC's Charter.

Group Risk & Compliance Committee ("GRCC")
GRCC operates under a delegated authority from the EXCO and also assists the BRCC. The GRCC defines, develops and monitors the Group's risk appetite taking into account the Group's strategy and business planning. In addition, the GRCC is accountable to highlight, discuss and monitor key regulations, both local and international and as they apply to all businesses where the Group operates. The GRCC reports relevant matters to the EXCO and as appropriate to the BRCC, advising and informing them as required on the Group's risk appetite and framework and on key compliance and other regulatory risk matters. The composition, guiding principles and detailed roles and responsibilities of GRCC are covered in the GRCC's Charter.

Notes to the consolidated financial statements *(continued)*

4 Financial risk management *(continued)*

Risk management framework *(continued)*

Management Level Committees within the Group *(continued)*

<u>Group Asset Liability Management Committee ("GALCO")</u>
GALCO assists the BOD and Board Committees in fulfilling its responsibility to oversee the Group's asset and liability management (ALM) related responsibilities. GALCO is directly accountable to the BRCC for ensuring that the risks within the Group Asset and Liability position are prudently managed by way of strong Group policy and procedures and an appropriate risk framework. The objective of GALCO is balance sheet management design and strategy and constant oversight of interest rate risk and liquidity risk with the primary goal of achieving optimal return while ensuring adequate levels of liquidity within an effective risk control framework. The composition, guiding principles and detailed roles and responsibilities of GALCO are covered in the GALCO's charter.

<u>Human Resources Steering Committee ("HRSC")</u>
HRSC assists the EXCO and the REMCO in fulfilling its duties with regard to implementing strategic as well as operational HR initiatives in order to deliver long term value. The Committee is formed to provide a forum to discuss and approve HR initiatives and policies to ensure that the needs of the organization from an employee perspective are considered and changes, as necessary, are approved or are submitted for approval to the relevant governance body. The Committee is the formal sponsor of all material HR initiatives across FAB in line with its Employee Value Proposition ("EVP"). The composition, guiding principles and detailed roles and responsibilities of HRSC are covered in the HRSC's charter.

<u>Real Estate Committee ("RECO")</u>
RECO operates under a delegated authority from the EXCO and oversees and approves the Group's real estate investment activities, in line with effective market and liquidity risk management practices and in accordance with relevant Group risk policies. The composition, guiding principles and detailed roles and responsibilities of RECO are covered in the RECO's charter.

<u>Islamic Banking Committee ("ISBC")</u>
ISBC has been appointed by the EXCO to oversee and direct the Islamic Banking businesses of FAB conducted by its business units and subsidiary companies Abu Dhabi National Islamic Finance and Aseel Finance. The ISBC also provide clear direction of the Islamic banking market / businesses and issues that may arise including market conditions and trends across the UAE and beyond; considered responses to external trends and events on the Islamic businesses; common governance, legal or shariah compliance issues; potential synergies across the organization to aid and the future direction of the business; and updates on significant changes. The composition, guiding principles and detailed roles and responsibilities of ISBC are covered in the ISBC's charter.

<u>International Banking Committee ("IBC")</u>
IBC has been appointed under a delegated authority from EXCO to assist the EXCO in defining, developing and monitoring the holistic strategy for the FAB international business and evaluation of the international regions in line with the FAB's strategy and group-wide principles, including the need to meet the requirements of local laws and regulations. A key objective of the Committee is to set and approve the country strategies, structures, senior management, business review, systems and controls needed to drive the operations and business growth of the respective countries. The composition, guiding principles and detailed roles and responsibilities of IBC are covered in the IBC's charter.

<u>Group Operations & Technology Committee ("GOTC")</u>
GOTC has been appointed under a delegated authority from EXCO to provide leadership and governance over the Operations and Technology activities for the FAB group entities and ensure its effective strategy and plans are implemented within the FAB Group. The composition, guiding principles and detailed roles and responsibilities of GOTC are covered in the GOTC's charter.

Notes to the consolidated financial statements *(continued)*

4 Financial risk management *(continued)*

Risk management framework *(continued)*

Management Level Committees within the Group *(continued)*

Integration Steering Committee ("ISC")
ISC has been appointed under a delegated authority from EXCO to provide direction on all matters relating to the post-Merger integration process. It is the main approving authority for all post-Merger integration policies and procedures and, as such, all lower-level integration committees report to the Group ISC. The Group ISC meets fortnightly and is chaired by the GCEO. The composition, guiding principles and detailed roles and responsibilities of ISC are covered in the ISC's charter.

Group Risk Management and Compliance Function
The Group has a centralized Risk Management, Compliance & Legal functions led by the GCRO. The Risk Management function comprises Enterprise Risk, Credit Risk, Operational and Fraud Risk Management Unit, Market & Liquidity Risk Management Unit, Information Security and Business Continuity Management unit. The Compliance function comprises Regulatory compliance, Financial Crime Compliance, Business Compliance units. The Legal function supports business & enabling functions through dedicated units.

Enterprise Risk Management Policy Framework
FAB's Enterprise Risk Management Policy (ERMP) framework aims to accomplish its core values and purpose of being a world class organization maximizing its risk adjusted returns for all stakeholders by establishing an enterprise wide risk management framework across FAB including local and international branches, subsidiaries, associates and foreign representative offices. Core objective of ERMP is to provide a reasonable degree of assurance to the BOD that the risks threatening FAB achievement of its core purpose are being identified, measured, monitored and controlled through an effective integrated risk management system. The ERMP framework consists of specific policy documents covering all material risks across FAB; which include ERM policy, Risk Appetite Policy, Corporate and Investment banking credit policy, Personal banking credit policy, Market risk Master policy and its associated operating policies, Liquidity risk policy, Interest rate risk policy, Operational risk policy, Fraud risk policy, Compliance risk policy, AML and Sanctions Policy, IT and Information Security risk policy, BCM Policy, Internal Capital Adequacy Assessment Process ("ICAAP") policy, New Products Approval policy, Model governance policy, etc. In addition to these risk management policies, the Group has also put in place detailed operational policies, procedures and programs wherever needed. Other relevant risks such as reputation risk and strategy risk are covered under the ERM policy

FAB manages risks using three lines of defense comprising of business units, control units and Internal Audit. Business units, as the first line of defense, identify and manage risk in their day-to-day activities by ensuring that activities are within the Group's risk appetite and are in compliance with all relevant internal policies and processes. Group Credit, Group Risk and Legal & Compliance division, as the second line of defense, establishes risk controls comprising of policies and processes while also providing oversight and independent challenge to the first line of defense. The Group Chief Risk Officer ("GCRO") has a direct reporting line to the BRCC to ensure the independence of Group Risk from business. Internal audit, as the third line of defense, provides assurance to management and the Board of the effectiveness of risk management practices employed by the first two lines of defense. The Group Chief Audit Officer has a direct reporting line to the Board Audit Committee.

(a) Credit risk

Credit risk is the risk that a customer or counterparty to a financial asset fails to meet its contractual obligations and cause the Group to incur a financial loss. It arises principally from the Group's loans and advances, due from banks and financial institutions, reverse repurchase agreements and non-trading debt investments, derivative financial instruments and certain other assets.

Notes to the consolidated financial statements *(continued)*

4 Financial risk management *(continued)*

Risk Management Framework *(continued)*

(a) Credit risk *(continued)*

Management of credit risk

Credit risk identification and assessment at FAB Group is carried out through a comprehensive mechanism comprising three levels of defense. The first level of defense lies with the business units and is responsible for maintaining a sound credit quality of Assets in line with the approved business strategy and credit risk appetite. The second level of defense is with the Group Credit Unit that assesses the risk on a customer & facility level and ensures proper documentation of customer, facility and security documents along with Group Risk management unit that assesses credit risk on a portfolio basis and maintains credit risk policies and credit risk rating models up to date. Internal Audit acts as a third level of defense with regular reviews of credit analysis and the risk functions to check the compliance with policies and procedures of the Group. The unit also reviews the policy documents on a regular basis.

As a part of credit risk monitoring and control framework, regular risk monitoring at both individual and portfolio levels is carried out along several parameters which include credit quality, provisioning levels, exposure limits across several dimensions, financial and operating performance, account conduct, end use of funds, adequacy of credit risk mitigants, adherence to financial and non-financial covenants, recovery performance, rating system performance among others.

The Group has set up a framework for credit risk mitigation as a means towards reducing credit risk in an exposure, at facility level, by a safety net of tangible and realizable securities including approved third-party guarantees/ insurance. The types of Credit Risk Mitigation (CRM) include netting agreements, collaterals, guarantees, credit derivatives, Stand by Letter of Credit (SBLC) and Comfort Letters. The Group ensures that all documentation used in collateralized transactions and for documenting on and off-balance sheet netting, guarantees, credit derivatives and collateral is binding on all parties and is legally enforceable in all relevant jurisdictions. The Group also ensures that all the documents are reviewed by appropriate authority and have appropriate legal opinions to verify and ensure its enforceability. In certain cases, the Group may also close out transactions or assign them to other counterparties to mitigate credit risk.

The Group uses an internal risk rating system to assess the credit quality of corporate borrowers and counterparties. Each corporate borrower is assigned a rating, including classified accounts. The risk rating system has 11 grades, further segregated into 24 notches. Grades 1-8 are performing and Grades 9 -11 are non – performing. Non-performing grades are classified based on the below criteria:

Grade	Classification	Criteria	
		Corporate loans	Retail loans
9	Sub-standard loans	Arrears 90 days or more and shows some loss due to adverse factors that hinder repayment	Arrears 90 days or more
10	Doubtful loans	Based on available information, full recovery seems doubtful, leading to a loss on portion of these loans	Arrears 120 days or more
11	Loss loans	Probability of no recovery; after all available courses of action are exhausted	Arrears 180 days or more

Notes to the consolidated financial statements *(continued)*

4 Financial risk management *(continued)*

(a) Credit risk *(continued)*

Maximum exposure to credit risk without taking account of any collateral and other credit enhancements
The table below shows the maximum exposure to credit risk for the components of the balance sheet, including derivatives. The maximum exposure is shown gross, before the effect of mitigation through the use of master netting and collateral agreements.

	Notes	***Gross maximum exposure 2017 AED 000***	*Gross maximum exposure 2016 AED 000*
Balances with Central Bank	7	**136,332,892**	24,329,649
Investments at fair value through profit or loss	8	**18,761,276**	827,558
Due from banks and financial institutions	9	**13,829,490**	12,932,570
Reverse repurchase agreements	10	**21,346,974**	5,449,019
Loans and advances	11	**345,089,058**	139,685,075
Non-trading investments	12	**86,057,723**	26,556,764
Other assets	16	**15,542,116**	6,733,506
Total		**636,959,529**	216,514,141
Derivatives held for trading		**10,874,605**	1,877,755
Derivatives held for hedging		**524,827**	75,248
Total		**11,399,432**	1,953,003
Contingent liabilities	37	**152,437,597**	60,155,516
Commitment	37	**48,555,452**	19,460,113
Total		**200,993,049**	79,615,629
Total credit risk exposure		**849,352,010**	298,082,773

Where financial instruments are recorded at fair value the amounts shown above represent the current credit risk exposure but not the maximum risk exposure that could arise in the future as a result of changes in values.

Notes to the consolidated financial statements *(continued)*

4 Financial risk management *(continued)*

(a) Credit risk *(continued)*

The Group also measures its exposure to credit risk by reference to the gross carrying amount of financial assets less amounts offset, interest suspended and impairment losses, if any. The carrying amount of financial assets represents the credit exposure.

	Due from banks and financial institutions		Loans and advances		Non-trading debt investments	
	2017	2016	**2017**	2016	**2017**	2016
	AED'000	AED'000	**AED'000**	AED'000	**AED'000**	AED'000
Individually impaired						
Substandard	**-**	-	**2,695,901**	1,467,173	**-**	-
Doubtful	**-**	-	**5,035,135**	997,208	**-**	-
Loss	**-**	-	**4,761,119**	1,791,115	**-**	-
Gross amount	**-**	-	**12,492,155**	4,255,496	**-**	-
Interest in Suspense	**-**	-	**(1,895,059)**	(567,014)	**-**	-
Specific allowance for impairment	**-**	-	**(4,581,263)**	(1,870,123)	**-**	-
Carrying amount	**-**	-	**6,015,833**	1,818,359	**-**	-
Past due but not impaired						
Past due comprises:						
Less than 30 days	**-**	-	**1,397,938**	2,186,041	**-**	-
31 – 60 days	**-**	-	**2,138,504**	650,345	**-**	-
61 – 90 days	**-**	-	**1,305,531**	571,782	**-**	-
More than 90 days	**-**	-	**4,143,607**	1,085,638	**-**	-
Carrying amount	**-**	-	**8,985,580**	4,493,806	**-**	-
Neither past due nor impaired	**13,829,490**	12,932,570	**323,611,323**	130,935,773	**86,057,723**	26,556,764
Collective allowance for impairment	**-**	-	**(8,146,848)**	(2,597,937)	**-**	-
Carrying amount	**13,829,490**	12,932,570	**330,465,888**	134,650,001	**86,057,723**	26,556,764

4 Financial risk management *(continued)*

(a) Credit risk *(continued)*

Impaired loans and advances and non-trading investments
Impaired loans and advances and non-trading investments are financial assets for which the Group determines that there is objective evidence that a loss event has occurred after the initial recognition of the asset and that the loss event has an impact on the estimated future cash flows of the financial asset that can be reliably estimated.

Past due but not impaired
Past due but not impaired are accounts where either contractual principal or interest cash flows are past due but the assets are not impaired. When these accounts show weakness in the borrower's financial position and creditworthiness, and requires more than normal attention such weakness is specifically monitored to ensure that the quality of the asset does not further deteriorate. On this class of asset the Group believes that specific impairment is not appropriate at the current condition.

Loans with renegotiated terms
Loans with renegotiated terms are loans that have been restructured due to deterioration in the borrower's financial position and where the Group has made material concessions that it would not otherwise consider. Once a loan is restructured, it remains in this category for a minimum period of twelve months, in order to establish satisfactory track record of performance under the restructuring agreement. The Group determines the twelve-month period to commence from the date of signing of the agreement for restructuring. On this class of asset the Group believes that specific impairment may not be required. As at the reporting date, the Group has renegotiated the following exposures:

	2017 **AED'000**	2016 AED'000
Renegotiated loans	**4,492,817**	1,711,799

Allowances for impairment
The Group establishes an allowance for impairment losses on assets carried at amortised cost 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 loss allowance. In assessing the collective loss allowance, the Group applies IFRS and the central bank guidelines to cover incurred but not identified losses established for groups of homogeneous assets with similar risk characteristics that are indicative of the debtor's ability to pay amounts due according to the contractual terms on the basis of a credit risk evaluation or grading process that considers asset type, industry, geographical location, collateral type, past due status and other relevant factors. Future cash flows in a group of financial assets that are collectively evaluated for impairment are estimated on the basis of historical loss experience for assets with credit risk characteristics similar to those in the group.

Individually assessed loans are required to be classified as impaired as soon as there is objective evidence that an impairment loss has been incurred. Objective evidence of impairment includes observable data such as when contractual payment of principal or interest is overdue and there is known difficulties in the cash flows of counterparties, credit rating downgrades or original terms of the contractual repayment are unable to be met.

Write-off policy
The Group writes off a loan or investment balance (and any related allowances for impairment losses) when it determines that the loans or investments are uncollectible. This is determined after all possible efforts of collecting the amounts have been exhausted.

Notes to the consolidated financial statements *(continued)*

4 Financial risk management *(continued)*

(a) Credit risk *(continued)*

Credit Risk Mitigants
The Group has set up a framework for credit risk mitigation as a means towards reducing credit risk in an exposure, at facility level, by a safety net of tangible and realizable securities including approved third-party guarantees/ insurance. The types of Credit Risk Mitigation ("CRM") include netting agreements, collaterals, guarantees, credit derivatives, Stand by Letter of Credit ("SBLC") and Comfort Letters. The Group ensures that all documentation used in collateralized transactions and for documenting on and off-balance sheet netting, guarantees, credit derivatives and collateral is binding on all parties and is legally enforceable in all relevant jurisdictions. The Group also ensures that all the documents are reviewed by the appropriate authority and have appropriate legal opinions to verify and ensure its enforceability. In certain cases, the Group may also close out transactions or assign them to other counterparties to mitigate credit risk.

An estimate of the collateral coverage against non-performing loans and advances is shown below:

	2017	2016
	AED'000	AED'000
Collateral value cover		
0 – 50%	**5,941,948**	3,634,971
50 – 100%	**1,777,719**	368,610
Above 100%	**4,772,488**	251,915
Total Gross non-performing loans	**12,492,155**	4,255,496

While the Group might not have repossessed significant amount of collateral in 2016 and 2017, maintaining repossession rights assist the Group in the restructuring and settlement of non-performing loans.

The Group monitors concentrations of credit risk by industry sector, counterparty and geographic location. An analysis of concentrations of credit risk at the reporting date is shown below:

Notes to the consolidated financial statements *(continued)*

4 Financial risk management *(continued)*

(a) Credit risk *(continued)*

Concentrations by industry sector

	Loans and advances		Investments		Reverse repurchase agreements		Undrawn loan Commitments	
	2017 AED'000	2016 AED'000	**2017 AED'000**	2016 AED'000	**2017 AED'000**	2016 AED'000	**2017 AED'000**	2016 AED'000
Agriculture	**435,808**	258,554	**-**	-	**-**	-	**-**	-
Energy	**24,225,459**	7,468,852	**13,169,794**	2,560,093	**-**	-	**7,510,896**	1,795,219
Manufacturing	**20,178,714**	6,478,057	**392,044**	447,780	**-**	-	**4,653,908**	522,760
Construction	**12,034,840**	6,521,141	**72,941**	-	**-**	-	**952,194**	75,104
Real estate	**90,530,386**	16,654,545	**750,167**	1,125,675	**-**	-	**13,361,067**	736,602
Trading	**22,877,522**	16,863,044	**126,687**	-	**-**	-	**2,170,578**	1,808,187
Transport and communication	**26,421,661**	12,644,751	**5,077,269**	833,764	**-**	-	**5,196,425**	505,970
Banks	**21,099,155**	4,528,512	**26,090,385**	6,408,978	**17,970,093**	4,479,020	**6,239,227**	8,795,550
Other financial institutions	**26,641,128**	6,322,747	**17,883,900**	5,274,623	**3,376,881**	969,999	**2,709,145**	894,474
Services	**24,228,514**	23,772,663	**485,699**	2,051,174	**-**	-	**2,185,704**	2,508,576
Government	**5,006,234**	268,002	**43,354,376**	8,880,810	**-**	-	**1,159,921**	313,743
Personal – Loans & Credit cards	**71,221,315**	37,853,660	**-**	-	**-**	-	**1,754,283**	269,478
Others	**188,322**	50,547	**375,212**	1,730,126	**-**	-	**662,104**	1,234,450
	345,089,058	139,685,075	**107,778,474**	29,313,023	**21,346,974**	5,449,019	**48,555,452**	19,460,113

The above numbers are presented on a gross basis and are not adjusted for provisions or interest in suspense if any.
Included within investments are equity instruments where the credit risk is not applicable.

Notes to the consolidated financial statements *(continued)*

4 Financial risk management *(continued)*

(a) Credit risk *(continued)*

Concentration by location:

	UAE AED'000	Europe AED'000	Arab countries AED'000	Americas AED'000	Asia AED'000	Others AED'000	Total AED'000
As at 31 Dec 2017							
Cash and balances with central banks	**41,841,692**	**57,579,526**	**7,174,336**	**31,450,850**	**64,650**	**-**	**138,111,054**
Investments at fair value through profit or loss	**6,357,372**	**2,007,556**	**4,327,245**	**163,758**	**6,359,273**	**105,560**	**19,320,764**
Due from banks and financial institutions	**159,496**	**10,394,394**	**1,630,653**	**765,592**	**805,596**	**73,759**	**13,829,490**
Reverse repurchase agreements	**2,631,845**	**14,204,929**	**3,198,329**	**143,116**	**801,455**	**367,300**	**21,346,974**
Derivative financial instruments	**2,099,778**	**7,527,951**	**1,060,508**	**59,158**	**616,860**	**35,177**	**11,399,432**
Loans and advances	**225,405,728**	**41,443,951**	**26,839,708**	**26,629,511**	**21,368,849**	**3,401,312**	**345,089,058**
Non trading investments	**32,994,218**	**16,035,290**	**15,681,376**	**11,951,579**	**11,084,991**	**710,256**	**88,457,710**
	311,490,129	**149,193,597**	**59,912,155**	**71,163,564**	**41,101,674**	**4,693,364**	**637,554,482**
As at 31 Dec 2016							
Cash and balances with central banks	21,518,665	-	3,218,512	-	39,540	-	24,776,717
Investments at fair value through profit or loss	472,297	96,866	131,607	88,282	92,038	18,434	899,524
Due from banks and financial institutions	5,107,732	2,322,276	414,390	1,707,300	3,359,589	21,283	12,932,570
Reverse repurchase agreements	1,212,812	3,979,378	-	256,829	-	-	5,449,019
Derivative financial instruments	906,498	917,156	75,514	652	41,576	11,607	1,953,003
Loans and advances	101,812,066	5,556,248	5,480,982	13,580,520	11,144,021	2,111,238	139,685,075
Non trading investments	6,868,946	2,247,595	2,918,619	8,700,291	5,944,037	1,734,011	28,413,499
	137,899,016	15,119,519	12,239,624	24,333,874	20,620,801	3,896,573	214,109,407

Concentration by location for investments is measured based on the location of the issuer of the security. Concentration by location for all others is measured based on the residential status of the borrower. The above numbers are presented on a gross basis and are not adjusted for provisions or interest in suspense if any. Concentration by location for undrawn commitments is stated in note 37 of these consolidated financial statements.

4 Financial risk management *(continued)*

(a) Credit risk *(continued)*

Classification of investments as per their external ratings:

	Non-trading investments		Investments at fair value through profit or loss	
	2017	2016	**2017**	2016
	AED'000	AED'000	**AED'000**	AED'000
AAA	**13,736,429**	6,062,533	**93,281**	7,356
AA to A	**55,568,380**	10,371,173	**12,451,229**	549,436
BBB to B	**14,561,101**	9,966,687	**5,924,467**	270,766
CCC and below	**26,535**	-	**27**	-
Unrated	**4,565,265**	2,013,106	**851,760**	71,966
	88,457,710	28,413,499	**19,320,764**	899,524

Unrated investments primarily consist of investments in Private equity funds and investments in equity which doesn't carry credit risk. Investments at fair value through profit or loss are neither past due nor impaired.

Classification of investments as per their counterparties:

	Non-trading investments		Investments at fair value through profit or loss	
	2017	2016	**2017**	2016
	AED'000	AED'000	**AED'000**	AED'000
Government sector	**38,956,577**	8,822,043	**4,397,799**	58,767
Supranational	**3,180,983**	2,762,447	**915,279**	7,356
Public Sector	**23,521,158**	5,742,681	**2,287,703**	125,627
Banking sector	**15,019,621**	5,961,822	**11,070,764**	447,156
Corporate / private sector	**7,779,371**	5,124,506	**649,219**	260,618
	88,457,710	28,413,499	**19,320,764**	899,524

Settlement risk

The Group's activities may give rise to risk at the time of settlement of transactions and trades. Settlement risk is the risk of loss due to the failure of counterparty to honour its obligations to deliver cash, securities or other assets as contractually agreed. Any delay in settlement is rare and monitored.

Derivative related credit risk

Credit risk in respect of derivative financial instruments arises from the potential for a counterparty to default on its contractual obligations and is limited to the positive market value of instruments that are favourable to the Group. The positive market value is also referred to as the "replacement cost" since it is an estimate of what it would cost to replace transactions at prevailing market rates if a counterparty defaults. The majority of the Group's derivative contracts are entered into with other banks and financial institutions.

4 Financial risk management *(continued)*

(b) Liquidity risk

Liquidity risk is defined as the risk that the Group is unable to meet its financial obligations as and when they fall due or that it can only do so at an excessive cost.

Liquidity risk arises from cash flows generated by assets and liabilities, including derivatives and other off-balance sheet commitments, not being matched in currency, size, and term. FAB ensures that all liabilities can be met as they fall due under both businesses as usual and stress conditions without incurring undue cost.

Management of liquidity risk
The Group has defined the liquidity risk appetite at a level so as to ensure that the Group has a controlled liquidity risk position with adequate cash or cash-equivalents to be able to meet its financial obligations, in all foreseeable circumstances and without incurring substantial additional costs, for a rolling period of three months. . The risk appetite is supported by a comprehensive risk management framework that includes Group ALCO approved limits for key funding and liquidity metrics, stress testing and a contingency funding plan.

The liquidity risk appetite is also defined at a level to ensure continued compliance with current and proposed liquidity regulation from both domestic and international regulators, and aligned to support the Group's external credit rating objectives.

One of the critical means to measure adequacy of liquidity as per extant global regulation is through Liquidity Coverage Ratio ("LCR"). FAB has been internally reporting Basel III LCR numbers for a considerable period of time, and has invested heavily in ensuring systems and controls framework is in place to comply with all the qualitative and quantitative aspects of Basel III. In addition the Group also ensures that it is compliant with UAE Central Bank liquidity regulation on Eligible Liquid Assets Ratio ("ELAR") at all times.

Liquidity limits are defined at the Group level and are cascaded down throughout the organisation to ensure that the Group complies with the defined Group Liquidity Risk appetite. Similarly International limits are cascaded to ensure compliance with any additional local regulatory requirements on liquidity management.

All liquidity policies and procedures are subject to review and approval by G-ALCO.

Exposure to liquidity risk
The contractual asset and liability maturity mismatch report without considering the Group's retention history is detailed below.

Notes to the consolidated financial statements *(continued)*

4 Financial risk management *(continued)*

(b) Liquidity risk *(continued)*

The maturity profile of the assets and liabilities as at 31 December 2017

	Total AED'000	Up to 3 months AED'000	3 months to 1 year AED'000	1 to 3 years AED'000	3 to 5 years AED'000	Over 5 years AED'000	Unspecified maturity AED'000
Assets							
Cash and balances with central banks	138,111,054	129,444,974	8,666,080	-	-	-	-
Investments at fair value through profit or loss	19,320,764	5,332,119	6,777,244	4,610,671	1,113,740	927,502	559,488
Due from banks and financial institutions	13,829,490	13,827,603	1,887	-	-	-	-
Reverse repurchase agreements	21,346,974	13,396,537	7,950,437	-	-	-	-
Derivative financial instruments[1]	11,399,432	1,821,287	1,456,835	2,248,883	2,428,292	3,444,135	-
Loans and advances	330,465,888	64,252,351	37,974,179	57,478,522	62,089,240	108,671,596	-
Non-trading investments	88,457,710	3,148,594	4,379,228	19,239,841	20,814,826	38,475,234	2,399,987
Investment properties	6,927,692	-	-	-	-	-	6,927,692
Property and equipment	3,535,501	-	-	-	-	-	3,535,501
Intangibles	19,901,374	-	-	-	-	-	19,901,374
Other assets	15,672,416	11,754,312	3,918,104	-	-	-	-
	668,968,295	242,977,777	71,123,994	83,577,917	86,446,098	151,518,467	33,324,042
Liabilities and equity							
Due to banks and financial institutions	30,576,336	25,375,102	4,980,891	220,343	-	-	-
Repurchase agreements	37,674,016	37,055,277	618,739	-	-	-	-
Commercial Paper	24,124,097	19,931,271	4,192,826	-	-	-	-
Derivative financial instruments[1]	14,941,331	2,049,661	1,466,528	2,812,421	2,976,936	5,635,785	-
Customer accounts and other deposits	395,843,664	340,455,577	50,526,974	3,622,508	1,083,074	155,531	-
Term borrowings	42,145,718	3,198,475	2,704,263	22,395,771	3,527,616	10,319,593	-
Subordinated notes	420,381	-	-	-	-	420,381	-
Other liabilities	21,033,339	15,787,256	5,246,083	-	-	-	-
Equity	102,209,413	-	-	-	-	-	102,209,413
	668,968,295	443,852,619	69,736,304	29,051,043	7,587,626	16,531,290	102,209,413
Undrawn commitments to extend credit	48,555,452	8,397,720	11,189,943	15,505,443	8,394,354	5,067,992	-
Trade contingencies	152,437,597	63,054,997	21,827,746	24,919,436	11,349,322	31,286,096	-

[1] *The Group has the option to liquidate the derivatives at any point of time.*

4 Financial risk management *(continued)*

(b) Liquidity risk *(continued)*

The maturity profile of the assets and liabilities as at 31 December 2016:

	Total AED'000	Up to 3 months AED'000	3 months to 1 year AED'000	1 to 3 years AED'000	3 to 5 years AED'000	Over 5 years AED'000	Unspecified maturity AED'000
Assets							
Cash and balances with central banks	24,776,717	20,326,717	2,950,000	1,500,000	-	-	-
Investments at fair value through profit or loss	899,524	518,630	196,382	92,937	19,608	-	71,967
Due from banks and financial institutions	12,932,570	12,932,570	-	-	-	-	-
Reverse repurchase agreements	5,449,019	5,449,019	-	-	-	-	-
Derivative financial instruments[1]	1,953,003	266,261	292,309	568,683	454,359	371,391	-
Loans and advances	134,650,001	28,129,233	20,286,382	20,976,572	19,798,824	45,458,990	-
Non-trading investments	28,413,499	6,806,345	1,217,458	8,554,715	7,546,469	2,431,777	1,856,735
Investment properties	6,422,502	-	-	-	-	-	6,422,502
Property and equipment	1,528,255	-	-	-	-	-	1,528,255
Intangibles	170,398						170,398
Other assets	6,784,453	5,088,341	1,696,112	-	-	-	-
	223,979,941	79,517,116	26,638,643	31,692,907	27,819,260	48,262,158	10,049,857
Liabilities and equity							
Due to banks and financial institutions	11,585,628	7,982,369	3,603,259	-	-	-	-
Repurchase agreements	13,109,155	10,469,838	2,639,317	-	-	-	-
Commercial Paper	10,016,916	7,669,957	2,346,959	-	-	-	-
Derivative financial instruments[1]	2,835,008	526,868	490,704	869,664	405,888	541,884	-
Customer accounts and other deposits	125,782,798	97,442,786	27,284,948	934,618	120,446	0	-
Term borrowings	18,294,545	5,509,500	2,387,450	4,838,511	3,572,086	1,986,998	-
Other liabilities	4,698,919	4,698,919	-	-	-	-	-
Equity	37,656,972	-	-	-	-	-	37,656,972
	223,979,941	134,300,237	38,752,637	6,642,793	4,098,420	2,528,882	37,656,972
Undrawn commitments to extend credit	19,460,113	12,344,459	6,418,124	374,853	260,971	61,706	-
Trade contingencies	60,155,516	42,796,041	6,691,209	7,720,591	1,466,588	1,481,087	-

[1]*The Group has the option to liquidate the derivatives at any point of time.*

Notes to the consolidated financial statements *(continued)*

4 Financial risk management *(continued)*

(b) Liquidity risk *(continued)*

The table below summarizes the maturity profile of the Group's financial liabilities based on contractual undiscounted repayment obligations.

Liabilities	Total AED'000	Gross nominal cash flows AED'000	Up to 3 months AED'000	3 months to 1 year AED'000	1 to 3 years AED'000	3 to 5 years AED'000	Over 5 years AED'000
As at 31 December 2017							
Due to banks and financial institutions	**30,576,336**	**30,728,564**	**25,451,000**	**5,057,221**	**-**	**220,343**	**-**
Repurchase agreements	**37,674,016**	**37,806,050**	**37,182,253**	**623,797**	**-**	**-**	**-**
Commercial Paper	**24,124,097**	**24,159,369**	**19,938,576**	**4,220,793**	**-**	**-**	**-**
Customer accounts and other deposits	**395,843,664**	**397,574,720**	**340,875,246**	**51,346,184**	**3,864,764**	**1,267,010**	**221,516**
Term borrowings	**42,145,718**	**43,240,770**	**1,316,898**	**1,791,189**	**17,085,268**	**2,123,748**	**20,923,667**
Subordinated notes	**420,381**	**737,500**	**-**	**23,685**	**47,565**	**47,630**	**618,620**
	530,784,212	**534,246,973**	**424,763,973**	**63,062,869**	**20,997,597**	**3,658,731**	**21,763,803**
Undrawn commitments to extend credit[1]	**48,555,452**	**48,555,452**	**8,397,720**	**11,189,943**	**15,505,443**	**8,394,354**	**5,067,992**
Trade contingencies	**152,437,597**	**152,437,597**	**63,054,997**	**21,827,746**	**24,919,436**	**11,349,322**	**31,286,096**
As at 31 December 2016							
Due to banks and financial institutions	11,585,628	11,631,764	6,906,884	4,724,880	-	-	-
Repurchase agreements	13,109,155	13,167,923	10,479,991	2,627,212	60,720	-	-
Commercial Paper	10,016,916	10,036,605	7,679,386	2,357,219	-	-	-
Customer accounts and other deposits	125,782,798	126,693,705	94,842,685	28,234,096	2,934,060	612,520	70,344
Term borrowings	18,294,545	20,116,899	1,942,973	2,709,702	9,088,210	3,742,474	2,633,540
Subordinated notes	-	-	-	-	-	-	-
	178,789,042	181,646,896	121,851,919	40,653,109	12,082,990	4,354,994	2,703,884
Undrawn commitments to extend credit[1]	19,460,113	19,460,113	12,344,459	6,418,124	374,853	260,971	61,706
Trade contingencies	60,155,516	60,155,516	42,796,041	6,691,209	7,720,591	1,466,588	1,481,087

[1]Calculated as per the contractual maturity profile.

4 Financial risk management *(continued)*

(c) Market risk

Market risk is the risk that the Group's income or capital will fluctuate on account of changes in the value of a financial instrument because of movements in market factors such as interest rates, credit spreads, foreign exchange rates and market prices of equity and commodity.

Management of market risk

The Group separates its exposure to market risk between trading, investment and non-trading portfolios. Trading and investment portfolios are held by the Wholesale - Global Markets Division and are managed on a fair value basis.

Investment Management Committee (IMCO) is responsible for oversight and guidance to Global Markets' trading and investment activities. It ensures effective management of market risks in accordance with the principles laid down in the market risk management policy. IMCO acts a sub-committee of Group Risk & Compliance Committee (GRCC) which has the overall authority and responsibility to manage market risks.

Market Risk Group is responsible for the development and implementation of detailed market risk appetite, risk management methodologies & policies including the control framework that is reviewed by IMCO and submitted to GRCC & BRCC for approval.

Exposure to market risks – trading portfolios

The principal analytical tool used to measure and control market risk exposure within the Group's trading portfolios which comprise of investments at fair value through profit or loss and trading derivatives is Value at Risk ("VaR"). The VaR of a trading portfolio is the estimated loss that will arise on the portfolio over a specified period of time (holding period) from an adverse market movement with a specified probability (confidence level). The VaR model uses historical simulation based on a 99% confidence level and assumes a 1-day holding period. Using market data from the previous two years, and observed relationships between different markets and prices, the model generates a wide range of plausible future scenarios for market price movements.

The Group uses VaR limits for foreign exchange, interest rate and credit spread. The overall structure of Trading VaR limits is subject to review and approval by the IMCO and then ratified at GRCC. VaR limits are then cascaded down to trading desks.

VaR is driven by actual historical observations and hence, it is not an estimate of the maximum loss that the Group could experience from an extreme market event. As a result of this limitation the VaR is further supplemented with other position and sensitivity limit structures, including limits to address potential concentration risks within each trading portfolio. Moreover the trading activity at Group and desk level is subject to Management Action Triggers ("MAT") that are limits on maximum losses that trigger actions from management. The VaR is as follows:

	2017 AED'000
VaR – Trading Book	**19,018**
Foreign exchange	**11,596**
Interest Rate	**13,312**
Credit	**4,002**
Equity	**511**
Diversification benefit	**(10,403)**

Commodity risk is not currently captured in the VaR model. This is under regular monitoring by the Risk Group through a set of market risk sensitivities, notional limits, and management action triggers.

Notes to the consolidated financial statements *(continued)*

4 Financial risk management *(continued)*

(c) Market risk *(continued)*

Exposure to market risk – banking portfolios

Exposure to Market Risk in the banking portfolios which comprise of non-trading investments, reverse repurchase agreements and certain derivative instruments which are designated as hedging instruments arise primarily from the investment portfolios, interest rate gaps in the banking book, and the Group's overall FX positions.

The principal analytical tool used to measure and control the investment risk exposure within the Group is Value at Risk ("VaR"). The VaR model is the same as the one used for the trading portfolios. The Group uses VaR limits for controlling the overall investment risk, including foreign exchange, interest rate and credit spread. The overall structure of Banking VaR limits is subject to review and approval by IMCO and then ratified by GRCC & GALCO. VaR limits are then cascaded to different Investment desks. The investment risk VaR is as follows:

	2017 AED'000
VaR – Banking Book	**121,157**
Foreign exchange	**14,794**
Interest Rate	**55,306**
Credit	**128,809**
Diversification benefit	**(77,752)**

Interest rate risk

Interest rate risk arises from interest bearing financial instruments and reflects the possibility that changes in interest rates will adversely affect the value of the financial instruments and the related income. The Group manages this risk principally through monitoring interest rate gaps and by matching the re-pricing profile of assets and liabilities. Overall interest rate risk positions are managed by using derivative instruments to manage overall position arising from the Group's interest bearing financial instruments. The use of derivatives to manage interest rate risk is described in note 38.

Interest rate risk is also assessed by measuring the impact of reasonable possible change in interest rate movements. The Group assumes a fluctuation in interest rates of 50 basis points (2016: 50 basis points) and estimates the following impact on the net profit for the year and equity at that date:

	Net profit for the year		**Equity**	
	2017 AED'000	2016 AED'000	**2017 AED'000**	2016 AED'000
Fluctuation in yield	**±547,255**	± 139,906	**±494,890**	± 290,008

The interest rate sensitivities set out above are illustrative only and employ simplified scenarios. They are based on AED 498,775 million *(2016: AED 160,575 million)* interest bearing assets and AED 402,248 million *(2016: AED 134,902 million)* interest bearing liabilities with interest re-pricing less than one year, for assessing the impact on net profit. The impact on equity includes the impact on net profit and the interest rate sensitivity on the available for sale portfolio. The sensitivity does not incorporate actions that could be taken by management to mitigate the effect of interest rate movements.

Notes to the consolidated financial statements *(continued)*

4 Financial risk management *(continued)*

(c) Market risk *(continued)*

The Group's interest rate gap and sensitivity position based on contractual re-pricing arrangements at 31 December 2017 was as follows:

	Total AED'000	Up to 3 months AED'000	3 months to 1 year AED'000	1 to 3 years AED'000	3 to 5 years AED'000	Over 5 years AED'000	Non-interest bearing AED'000
Assets							
Cash and balances with central banks	138,111,054	120,755,325	8,666,080	-	-	-	8,689,649
Investments at fair value through profit or loss	19,320,764	8,785,020	5,744,846	2,363,842	1,074,972	792,596	559,488
Due from banks and financial institutions	13,829,490	10,277,717	110,190	-	-	-	3,441,583
Reverse repurchase agreements	21,346,974	13,396,536	7,950,438	-	-	-	-
Derivative financial instruments	11,399,432	-	-	-	-	-	11,399,432
Loans and advances	330,465,888	279,399,268	33,135,204	8,444,686	3,473,496	11,824,783	(5,811,549)
Non-trading investments	88,457,710	6,104,190	4,450,640	18,941,715	18,633,642	37,832,551	2,494,972
Investment properties	6,927,692	-	-	-	-	-	6,927,692
Intangible assets	19,901,374	-	-	-	-	-	19,901,374
Property and equipment	3,535,501	-	-	-	-	-	3,535,501
Other assets	15,672,416	-	-	-	-	-	15,672,416
	668,968,295	438,718,056	60,057,398	29,750,243	23,182,110	50,449,930	66,810,558
Liabilities and equity							
Due to banks and financial institutions	30,576,336	22,745,363	4,980,891	220,343	-	-	2,629,739
Repurchase agreements	37,674,016	37,055,277	618,739	-	-	-	-
Commercial Paper	24,124,097	19,931,271	4,192,826	-	-	-	-
Derivative financial instruments	14,941,331	-	-	-	-	-	14,941,331
Customer accounts and other deposits	395,843,664	259,294,389	38,848,293	5,190,391	637,712	155,531	91,717,348
Term borrowings	42,145,718	14,098,549	482,264	14,033,474	3,211,838	10,319,593	-
Other liabilities	21,033,339	-	-	-	-	-	21,033,339
Subordinated notes	420,381	-	-	-	-	420,381	-
Equity	102,209,413	-	-	-	-	-	102,209,413
	668,968,295	353,124,849	49,123,013	19,444,208	3,849,550	10,895,505	232,531,170
On statement of financial position gap		85,593,207	10,934,385	10,306,035	19,332,560	39,554,425	(165,720,612)
Off statement of financial position gap		39,660,765	(11,324,517)	7,497,522	(11,413,602)	(24,420,168)	-
Total interest rate sensitivity gap		125,253,972	(390,132)	17,803,557	7,918,958	15,134,257	(165,720,612)
Cumulative interest rate sensitivity		125,253,972	124,863,840	142,667,397	150,586,355	165,720,612	-

Notes to the consolidated financial statements *(continued)*

4 Financial risk management *(continued)*

(c) Market risk *(continued)*

The Group's interest rate gap and sensitivity position based on contractual re-pricing arrangements at 31 December 2016 was as follows:

	Total AED'000	Up to 3 months AED'000	3 months to 1 year AED'000	1 to 3 years AED'000	3 to 5 years AED'000	Over 5 years AED'000	Non-interest bearing AED'000
Assets							
Cash and balances with central banks	24,776,717	12,085,116	2,950,000	1,500,000	-	-	8,241,601
Investments at fair value through profit or loss	899,524	899,524	-	-	-	-	-
Due from banks and financial institutions	12,932,570	12,494,080	400,041	603	37,510	336	-
Reverse repurchase agreements	5,449,019	5,449,019	-	-	-	-	-
Derivative financial instruments	1,953,003	-	-	-	-	-	1,953,003
Loans and advances	134,650,001	100,037,878	17,127,427	4,756,906	2,277,771	15,515,062	(5,065,043)
Non-trading investments	28,413,499	7,910,733	1,220,872	8,462,912	6,692,956	2,207,243	1,918,783
Investment properties	6,422,502	-	-	-	-	-	6,422,502
Property and equipment	1,528,255	-	-	-	-	-	1,528,255
Intangibles	170,398	-	-	-	-	-	170,398
Other assets	6,784,453	-	-	-	-	-	6,784,453
	223,979,941	138,876,350	21,698,340	14,720,421	9,008,237	17,722,641	21,953,952
Liabilities and equity							
Due to banks and financial institutions	11,585,628	6,878,217	4,707,411	-	-	-	-
Repurchase agreements	13,109,155	10,453,373	2,655,782	-	-	-	-
Commercial Paper	10,016,916	7,669,957	2,346,959	-	-	-	-
Derivative financial instruments	2,835,008	-	-	-	-	-	2,835,008
Customer accounts and other deposits	125,782,798	66,951,378	24,925,278	3,061,957	120,446	-	30,723,739
Term borrowings	18,294,545	5,926,611	2,387,450	4,569,174	3,446,346	1,964,964	-
Other liabilities	4,698,919	-	-	-	-	-	4,698,919
Equity	37,656,972	-	-	-	-	-	37,656,972
	223,979,941	97,879,536	37,022,880	7,631,131	3,566,792	1,964,964	75,914,638
On statement of financial position gap		40,996,814	(15,324,540)	7,089,290	5,441,445	15,757,677	(53,960,686)
Off statement of financial position gap		5,728,198	171,512	(1,388,234)	(1,653,480)	(2,857,996)	-
Total interest rate sensitivity gap		46,725,012	(15,153,028)	5,701,056	3,787,965	12,899,681	(53,960,686)
Cumulative interest rate sensitivity		46,725,012	31,571,984	37,273,040	41,061,005	53,960,686	-

Notes to the consolidated financial statements *(continued)*

4 Financial risk management *(continued)*

(c) Market risk *(continued)*

Foreign exchange risk

Foreign exchange risk is the risk that the value of a financial instrument will fluctuate due to changes in foreign exchange rates and arises from financial instruments denominated in a foreign currency. The Group's functional currency is the UAE Dirham. The Board of Directors has set limits on positions by currency. Positions are closely monitored and hedging strategies are used to ensure positions are maintained within established limits. At 31 December, the Group had the following significant net exposures denominated in foreign currencies:

	Net spot position (short)/long AED'000	**Forward position (short)/long AED'000**	**Total 2017 (short)/long AED'000**	Total 2016 (short)/long AED'000
Currency				
US Dollar	27,925,843	14,267,865	**42,193,708**	(2,249,437)
UK Sterling Pound	(23,056,386)	23,990,456	**934,070**	(57,376)
Euro	53,331,952	(50,797,102)	**2,534,850**	2,440,349
Kuwaiti Dinar	254,327	(546,777)	**(292,450)**	860
Saudi Riyal	(869,623)	(2,821,384)	**(3,691,007)**	1,717
Japanese Yen	5,010,841	(4,855,121)	**155,720**	54,031
Swiss Franc	(1,066,098)	1,131,805	**65,707**	3,953
Qatari Riyal	497,920	(341,602)	**156,318**	6,489
Bahraini Dinar	640,186	(844,215)	**(204,029)**	379
Egyptian Pound	447,656	(391,179)	**56,477**	13
Jordanian Dinar	582,753	(249,390)	**333,363**	220
Indian Rupees	2,492,980	(97,284)	**2,395,696**	(573,390)
Malaysian Ringgit	(36,649)	101,635	**64,986**	159
Libyan Dinar	323,140	-	**323,140**	305,959
Others	(5,064,504)	5,420,100	**355,596**	(9,303)

As AED, SAR and QAR are pegged against US Dollar, the Group's risk exposure to these currencies is limited to that extent. Exposure to other foreign currencies is insignificant.

The tables below indicate the currencies to which the Group had significant exposure at 31 December 2017 and 2016 on its monetary assets, liabilities and net derivatives forward position. The analysis estimates the effect of a reasonably possible movement of AED against other currencies, with all other variables held constant on the consolidated income statement.

Currency	EUR	GBP	JPY	Libyan Dinar
Assumed change in exchange rates	1%	1%	1%	1%
Impact on net income in exchange rate:				
2017 (AED 000)	**± 25,348**	**± 9,341**	**± 1,557**	**± 3,231**
2016 (AED 000)	± 867	± 574	± 540	± 3,060

At 31 December 2017 and 2016, the effect of the assumed changes in exchange rates on equity is insignificant.

Notes to the consolidated financial statements *(continued)*

4 Financial risk management *(continued)*

(c) Market risk *(continued)*

Equity price risk

FAB is exposed to equity price risk on equity investments, either through holding of equities of another entity or through equity derivatives such as forward contracts, options or swaps. The fair value of these instruments will fluctuate due changes in the market price of the underlying equity instruments. The Group manages this risk through setting Equity Delta, Vega and Gamma limits. The Group also enforces diversification of investments in terms of geographical distribution and industry concentration.

The following table estimates the sensitivity to a possible change in equity markets on the Group's income statement. The sensitivity of the income statement is the effect of the assumed change in the reference equity benchmark on the fair value of investments carried at fair value through the income statement.

	Assumed level of change %	**Impact on net income 2017 AED 000**	Impact on net income 2016 AED 000
Investments carried at fair value through profit or loss			
Reference equity benchmarks:			
Dubai Financial Market Index	5%	**23,747**	-
Net asset value of managed funds	5%	**2,786**	2,549
Other equity exchanges	5%	**1,079**	680
Unquoted	5%	**362**	369
		27,974	3,598

The effect on equity as a result of a change in the fair value of equity instruments held as available for sale at 31 December 2017 and 2016, due to a reasonably possible change in equity indices, with all other variables held constant, is as follows:

	Assumed level of change %	**Impact on net income 2017 AED 000**	Impact on net Income 2016 AED 000
Non-trading investments (excluding investment in associates and joint ventures)			
Reference equity benchmarks:			
Abu Dhabi Securities Exchange Index	5%	**11,480**	789
Dubai Financial Market Index	5%	**4,237**	771
Net asset value of managed funds	5%	**85,763**	76,282
Other equity exchanges	5%	**6,801**	5,458
Unquoted	5%	**8,230**	7,468
		116,511	90,768

Notes to the consolidated financial statements *(continued)*

4 Financial risk management *(continued)*

(d) Operational risk

Operational risk is defined as the risk of losses resulting from inadequate or failed processes, people & systems or from external events.

Operational risks arise across all businesses in the Group. The primary responsibility to ensure that risks are managed and monitored resides with the businesses within the Group. Group's businesses are supported by Embedded risk resources and Group Operational Risk Management as 'second line of defense' to ensure robust risk management.

Further, there are reviews conducted by Group Internal Audit as the 'third line of defense'. The results of internal audit reviews are discussed with the management of the respective divisions and summaries are submitted to the Board Audit Committee.

The Group has an established Operational Risk framework consisting of policies and procedures to identify, assess, monitor, control, report and to manage risks and to notify, identify and rectify incidents. The Operational Risk framework also provides the interrelation with other risk categories. Where appropriate, risk is mitigated by way of insurance.

Typically, Operational Risk events are classified as:

- Internal fraud: Risk of unauthorized activity and fraud perpetrated by employees
- External fraud: Risk of fraud or breach of system security by an external party
- Employee practices & workplace safety: Risk of failures in employee relations, diversity and discrimination, and health and safety risks across the Group
- Damage to physical assets: Risk of impact to the Group due to natural disasters
- Clients, Products & Business Practices: Risk of failing in assessing client suitability, fiduciary responsibilities, improper business practices, flawed products and advisory activities.
- Business Disruption & System failures: Risk of not planning and testing business continuity and disaster recovery for systems
- Execution delivery and process management: Risk of failed transaction execution, customer intake and documentation, vendor management and monitoring and reporting.

The Board has oversight responsibilities for operational risk management across the Group. These responsibilities are delegated and exercised through the Group Risk & Compliance Committee, which is the senior management forum responsible for the oversight of Operational Risk.

Key responsibilities of Operational Risk Committee with regards to Operational risk include to ensure:

- Approval of the Group Operational Risk Management Framework and oversight over its implementation
- Approve the strategy and direction for Operational Risk across the Group.
- Establish an effective Governance structure across the Group

4 Financial risk management *(continued)*

(e) Capital management

CBUAE regulations govern regulatory capital requirements for the Group; in addition the overseas branches and subsidiaries may be directly supervised by their local regulators. The capital management process for the Group is linked to the overall business strategy to ensure that capital is adequate to the level of inherent risk in the business and within the firm's capital risk appetite The Group conducts capital planning in conjunction with the financial budgeting exercise.

The Board and top management define the long term strategic direction for the Group. This provides the framework for the development of a bottom up plan based on the projections from individual business units. The bottom up plan is an input to the annual budgeting process and is conducted at a business unit and country level. These are consolidated for each business division and finally, for the entire Group. Business units, within each division, develop forecasted balance sheet and P&L statements for the next year, by considering the following key parameters:

- the short term (one year) goals
- risk appetite & strategy
- target growth rates
- target returns

The Group's capital management policies aim to ensure that it has sufficient capital to cover the risks associated with its activities and the allocation of capital across the Group The assessment of the various risks across the Group and their likely impact is carried out in conjunction with ICAAP undertaken annually. As part of the ICAAP process, Group Risk function identifies the various risks the Group is exposed to as part of its day-to-day operations. Next, the Group assesses these risks against the existing policies and procedures, frameworks and methodologies, contingency plans and other processes to measure, manage and mitigate the impact of such risks. Finally the Group determines the capital requirements for the material risk exposures.

The key objectives of the Group's capital management process are:

- Maintain sufficient capital to meet minimum capital requirement set by CBUAE as well as to ensure transition to Basel III in terms of capital ratios.
- Maintain sufficient capital to support Group's Risk Appetite and strategic objectives as per long-term strategic plan.
- Maintain adequate capital to withstand stress scenarios including increased capital requirements determined through ICAAP.
- To support the Group's credit rating.

The Group conducts regular stress test exercises in which the Balance Sheet and Profit or Loss statements are determined for base case and stress scenarios. The risk factors are impacted by the assumptions made for the base and stress scenarios and the corresponding impact on the capital adequacy is determined. The Group uses macroeconomic stress tests in order to project capital need and capital levels under various unfavourable scenarios. The tests are perceived as an important tool in internal capital planning. The stress test result during 2017 shows that the Group has adequate capital even under adverse scenarios.

4 Financial risk management *(continued)*

(e) Capital management *(continued)*

The Group's regulatory capital adequacy ratio, set by the Central Bank of the UAE at a minimum level of 12% *(2016: 12%)*, of which Tier 1 is to be 8% *(2016: 8%)* is analysed into two tiers as follows; Ratios presented below is without considering the impact of proposed dividend.

	Basel II 2017 AED'000	Basel II 2016 AED'000
Tier 1 capital		
Ordinary share capital	**10,897,545**	4,500,000
Share premium	**53,026,643**	-
Retained earnings	**18,677,552**	16,969,016
Statutory and special reserve	**7,081,084**	11,723,501
General reserve and share option scheme	**120,000**	120,000
Foreign currency translation reserve	**(63,075)**	(88,327)
Tier 1 capital notes	**10,754,750**	4,000,000
Deductions from Tier 1 capital	**(62,586)**	(5,193,391)
Non-controlling Interests	**487,015**	432,782
Less : Goodwill and Intangible assets	**(20,263,462)**	(170,398)
Total	**80,655,466**	32,293,183
Tier 2 capital		
Fair value reserve	**281,345**	185,755
Qualifying subordinated liabilities	**420,381**	-
Allowance for collective impairment	**5,270,024**	2,113,568
Deductions from Tier 2 capital	**(20,152)**	
	5,951,598	2,299,323
Total regulatory capital base	**86,607,064**	34,592,506
Risk weighted assets:		
Credit risk	**421,602,405**	169,085,422
Market risk	**28,054,810**	3,077,212
Operational risk	**35,619,434**	16,567,283
Risk weighted assets	**485,276,649**	188,729,917
Tier 1 capital ratio	**16.6%**	17.1%
Capital adequacy ratio	**17.8%**	18.3%

The Group and its overseas branches and subsidiaries have complied with all externally imposed capital requirements for all periods presented.

Notes to the consolidated financial statements *(continued)*

4 Financial risk management *(continued)*

(e) Capital management (Unaudited) *(continued)*

	Basel III 2017 AED'000
Tier 1 capital	
Ordinary share capital	10,897,545
Share premium	53,026,643
Retained earnings	18,677,552
Statutory and special reserve	7,081,084
General reserve and share option scheme	120,000
Fair value reserve	281,345
Non-controlling Interests	487,015
Eligible Tier 1 capital (a)	90,571,184
Deductions:	
Foreign currency translation reserve	(63,075)
Treasury shares	(42,434)
Deferred tax assets	(36,585)
Goodwill and Intangible assets	(20,263,462)
Total deductions	(20,405,556)
Less: Transitional Deduction from CET 1 (b)	(16,324,445)
	74,246,739
Additional Tier 1	
Tier 1 capital notes	10,754,750
Transitional Deduction from AT1	(2,040,556)
Additional Tier 1 (d)	8,714,194
	82,960,933
Tier 2 capital	
Qualifying subordinated liabilities	420,381
Allowance for collective impairment	5,270,024
Transitional Deduction from AT1	(2,040,556)
	3,649,849
Total regulatory capital base	86,610,782
Risk weighted assets:	
Credit risk	421,666,579
Market risk	28,054,810
Operational risk	35,619,434
Risk weighted assets	485,340,823
Ratios with transition impact:	
CET 1 ratio	15.3%
Tier 1 capital ratio	17.1%
Capital adequacy ratio	17.8%

Notes to the consolidated financial statements *(continued)*

4 Financial risk management *(continued)*

(f) Country risk

Country risk is the likelihood of economic, social, and political events in a foreign country negatively influencing the willingness or ability of state owned and/or privately owned customers in that country to pay their debts on time.

The Group undertakes a detailed qualitative analysis pertaining to country risk as a part of the business decision process (credit risk modelling). These factors include economic, social and political stability in each country, the monetary policy, the foreign exchange control measure, the transparency of information, the financial and market structure, banking regulations and supervision, the legal system, and the accounting standards among others. Country risks are monitored and controlled using country limits set by the Group; these limits are in accordance with overall business strategy, capital adequacy and provisions for potential risks, risk rating of each country, acceptable level of risk, and business opportunities in each country.

(g) Strategic risk

Strategic risk refers to the risk of current or prospective impact on the Group’s earnings, capital, reputation or standing arising from changes in the environment the Group operates in and from adverse strategic decisions, improper implementation of decisions, or lack of responsiveness to industry, economic or technological changes. It is a function of compatibility of Group’s strategic goals, strategies developed to achieve those goals, resources deployed to meet those goals and the quality of implementation.

The Group uses several factors to identify and assess impact of strategic risk on its books, including level of integration of risk management policies and practices in the strategic planning process, aggressiveness of strategic goals and compatibility with developed business strategies, capital support for the strategic initiatives to take care of earnings volatility, effectiveness of communication and consistency of application of strategic goals, objectives, corporate culture, and behaviour throughout the Group.

Strategic risks are monitored and controlled as part of the strategic planning process wherein the Group reviews the progress on strategic initiatives vis-à-vis the plan and considers whether the progress is in line with the plan and the external business environment. The strategic plan is periodically reviewed and updated subject to an approval process which is also a part of the strategic planning process.

(h) Compliance risk

Compliance Risk refers to the risk to earnings or capital or reputation or continued business existence arising from violations of or non-conformance with laws, rules, regulations, prescribed practices, or ethical standards.

The Group, on a continuous basis, identifies and assesses such risks inherent in all new and existing “material” products, activities, processes and systems. The assessment includes risks assessment on non-conformance with laws, rules, regulations, prescribed practices, or ethical standards. The Enterprise Risk Management function has a group-wide compliance unit that develops internal controls to manage such risks and it is supported by the Internal Audit and Legal functions.

In order to monitor compliance and anti-money laundering risks, the Group has set in place the due diligence processes, reviews of policies and procedures across the Group, implementation of an integrated compliance and AML system which manages name clearance, transaction monitoring and payment monitoring activities, assessment through compliance check-lists etc.

Compliance risk is largely mitigated by way of focused policies and procedures, extensive checklist based and on-spot due diligence and regular training sessions.

4 Financial risk management *(continued)*

(i) Reputation risk

Reputation risk is the risk to earnings or capital arising from negative public opinion. This can be due to external or internal events.

The Group identifies and assesses reputation risk by clearly defining types of risks to be captured, establishing key sources of reputation risk it may be exposed to, based on individual circumstances, describing the risks identified in terms of the nature of risk and the potential consequences that the risks may bring to its reputation. The Group also refers to other relevant information for risk identification purposes. Such information may be sourced from media reports, stakeholder analysis reports, internal audit and compliance reports, management exception reports, or other early warning indicators.

For reputation risks, apart from the regular monitoring of external and internal events that can result in possible reputation risks the Group also has processes to track risks that may affect its reputation. These processes allow the BOD and senior management to take prompt corrective actions to address any anticipated reputation event in advance.

In order to manage reputation risks, the Group has set in place a mechanism that entails drawing up action plans to identify reputation risk events and facilitate subsequent monitoring of the progress made; for those risks that may be very difficult or too costly to eliminate entirely the mechanism requires development of contingency plans as response actions.

5 Use of estimates and judgements

In the process of applying the Group's accounting policies, IFRS require the management to select suitable accounting policies, apply them consistently and make judgements and estimates that are reasonable and prudent and would result in relevant and reliable information. The management, based on guidance in IFRS and the IASB's Framework for the Preparation and Presentation of Financial Statements has made these estimates and judgements. Listed below are those estimates and judgement which could have the most significant effect on the amounts recognised in the consolidated financial statements.

Key sources of estimation uncertainty

(a) Going concern

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

(b) Impairment charge on loans and advances and non-trading investments

Impairment losses are evaluated as described in accounting policy 3(b) (vii) and 4(a).

The Group evaluates impairment on loans and advances and non-trading investments on an ongoing basis and a comprehensive review on a quarterly basis to assess whether an impairment charge should be recognised in the consolidated statement of profit or loss. In particular, considerable judgement by management is required in the estimation of the amount and timing of future cash flows when determining the level of impairment charge required. In estimating these cash flows, management makes judgements about counterparty's financial situation and other means of settlement and the net realisable value of any underlying collateral. Such estimates are based on assumptions about several factors involving varying degrees of judgement and uncertainty, and actual results may differ resulting in future changes to such impairment charges.

5 Use of estimates and judgements *(continued)*

(c) Collective impairment charge

Collective impairment charge is evaluated as described in accounting policy 3(b) (vii) and 4(a).

In addition to specific impairment charge against individually impaired assets, the Group also maintains a collective impairment allowance against portfolios of loans and advances with similar economic characteristics which have not been specifically identified as impaired. In assessing the need for collective impairment charge, management considers concentrations, credit quality, portfolio size and economic factors. In order to estimate the required allowance, assumptions are made to define the way inherent losses are modelled and to determine the required input parameters, based on historical and current economic conditions.

(d) Impairment charge on property and equipment

Impairment losses are evaluated as described in accounting policy 3(k) (iv).

In determining the net realisable value, the Group uses the selling prices determined by external independent valuer companies, having appropriate recognised professional qualifications and recent experience in the location and category of property being valued. The selling prices are based on market values, being the estimated amount for which a property could be exchanged on the date of the valuation between a willing buyer and a willing seller in an arm's length transaction.

(e) Contingent liability arising from litigations

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

(f) Share option scheme

The fair value of the share option scheme is determined using the Black-Scholes model. The model inputs comprise of share price, exercise price, share price volatility, contractual life of the option, dividend yield and risk-free interest rate.

(g) Valuation of financial instruments

The valuation techniques of financial instruments may require certain unobservable inputs to be estimated by the management. These are discussed in detail in note 6.

(h) Defined benefit plan

The present value of the defined benefit obligation depends on a number of factors that are determined on an actuarial basis using a number of assumptions. The assumptions used in determining the net cost (income) for obligations include the discount rate. Any changes in these assumptions would impact the carrying amount of the defined benefit obligation.

The Group determines the appropriate discount rate at the end of each year. This is the interest rate that should be used to determine the present value of the estimated future cash flows expected to be required to settle the future obligations. In determining the appropriate discount rate, the Group considers interest rate of high quality corporate bonds that are denominated in the currency in which the benefits will be paid and that have the terms to maturity approximating the terms of related benefit obligation.

Other key assumptions for defined benefit obligations are based in part on current market conditions. Additional information on these assumptions is disclosed in note 21.

Notes to the consolidated financial statements *(continued)*

5 Use of estimates and judgements *(continued)*

Critical accounting judgements in applying the Group's accounting policies include:

(a) Financial asset and liability classification

The Group's accounting policies provide scope for financial assets and liabilities to be designated on inception into different accounting categories in certain circumstances:

In classifying financial assets as "fair value through profit or loss", "held-to-maturity" or "available-for-sale", the Group has determined it meets the description as set out in policy 3(b) (ii).

(b) Qualifying hedge relationships

In designating financial instruments as qualifying hedge relationships, the Group has determined that it expects the hedge to be highly effective over the life of the hedging relationship.

(c) Determination of fair value hierarchy of financial instruments

The Group's determination of fair value hierarchy of financial instruments is discussed in note 6.

(d) Structured entities

For all funds managed by the Group, the investors are able to vote by simple majority to remove the Group as fund manager, and the Group's aggregate economic interest in each fund is not material. As a result, the Group has concluded that it acts as agent for the investors in these funds, and therefore has not consolidated these funds.

(e) Operating segments

In preparation of the segment information disclosure, the management has made certain assumptions to arrive at the segment reporting. These assumptions would be reassessed by the management on a periodic basis. Operating segments are detailed in note 39.

6 Financial assets and liabilities

(a) Valuation control framework

The Group has an established control framework with respect to the measurement of fair value. This framework includes a Valuation Committee that reports to the Group Risk Committee. The Group also has control functions to support this framework (Product Control, Independent Price Verification, Model Validation and Group Market Risk) that are independent of front office management. Specific controls include:

- Independence in valuation process between risk taking units and control units;
- System for valuations;
- Verification of observable pricing;
- Review and approval process for new models and changes to models;
- Analysis and investigation of significant daily valuation movements; and
- Review of significant unobservable inputs, valuation adjustments and significant changes to the fair value measurement of Level 3 instruments.

The fair values of due from banks and financial institutions, reverse repurchase agreement , due to banks and financial institutions, repurchase agreements and Customer accounts and other deposits which are predominantly short term in tenure and issued at market rates, are considered to reasonably approximate their carrying value.

The Group estimates that the fair value of its loans and advances portfolio is not materially different from its carrying value since the majority of loans and advances carry floating market rates of interest and are frequently re-priced. For

Notes to the consolidated financial statements *(continued)*

6 Financial assets and liabilities *(continued)*

(a) Valuation control framework *(continued)*

loans considered impaired, expected cash flows, including anticipated realisation of collateral, were discounted using an appropriate rate and considering the time to collect, the net result of which is not materially different from the carrying value.

(b) Determination of fair values

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date in the principal, or in its absence, the most advantageous market to which the Group has access at that date. The fair value of a liability reflects its non-performance risk. Consequently, differences can arise between book values and the fair value estimates. Underlying the definition of fair value is the presumption that the Group is a going concern without any intention or requirement to materially curtail the scale of its operation or to undertake a transaction on adverse terms.

The Group measures fair values using the following fair value hierarchy that reflects the significance of the inputs used in making the measurements:

Level 1: Quoted market price (unadjusted) in active market for an identical instrument.

Level 2: Valuation techniques based on observable inputs, either directly (i.e. as prices) or indirectly (i.e. derived from prices). This category includes instruments valued using: quoted market prices in active markets for similar instruments; or other valuation techniques where all significant inputs are directly or indirectly observable from market data.

Level 3: Valuation techniques using unobservable inputs. This category includes all instruments where the valuation technique includes input not based on observable data and the unobservable input have a significant impact on the instrument's valuation. This category includes instruments that are valued based on quoted prices of similar instruments after making adjustments based on unobservable inputs that are necessary to reflect fair value of the instrument.

(c) Valuation techniques

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

Fair value of financial assets and liabilities that are traded in active market are based on quoted market price or dealer price quotations. For all other financial instruments, the Group determines fair value using valuation techniques, such as discounted cash flow models, benchmarking against similar instruments for which observable market prices exist, Black-Scholes model or other valuation models. Each valuation technique models the behaviour of underlying market factors. These market factors include interest rates, credit spreads and other inputs used in estimating discount rates, bond prices, foreign exchange rates, equity and equity index prices, volatilities and correlations.

The objective of valuation techniques is to arrive at a fair value determination that reflects the price of the financial instrument at the reporting date that would have been determined by market participants acting at arm's length.

The Group uses widely recognised valuation models for determining the fair value of common financial instruments, such as interest rate and currency swaps that use only observable market data. Observable prices or model inputs are usually available in the market for listed debt and equity securities, exchange-traded derivatives and simple over-the-counter derivatives such as interest rate swaps. Availability of observable market prices and model inputs reduces the need for management judgement and estimation and also reduces the uncertainty associated with determining fair values. Availability of observable market prices and inputs varies depending on the products and markets and is prone to changes based on specific events and general conditions in the financial markets.

For more complex instruments, the Group uses third party valuation models, which are developed from recognised valuation models. These valuation models require expert judgement for the selection of the most appropriate valuation model to be used including input market data and underlying assumptions for the determination of fair value.

Notes to the consolidated financial statements *(continued)*

6 Financial assets and liabilities *(continued)*

(c) Valuation techniques *(continued)*

Model inputs and parameters can be calibrated for market prices for plain vanilla instruments, published forecasts and current or recent observed transactions in similar instruments. This calibration process is inherently subjective and it yields ranges of possible inputs and estimates of fair value, and expert judgement is required to select the most appropriate point in the range.

(d) Fair Value adjustments

Credit Valuation Adjustments ("CVA")
The Group modelled the CVA adjustment in 2016 taking into account trades subject to collateral and netting agreements. The methodology for CVA calculation relies on three components: a loss given default assumption is used for the exposures, the probability of default of the counterparty is implied from credit default spreads or sector curves determined by combining the rating, the sector and the region, the expected positive exposure is calculated using simulation methodology. The methodology does not account for wrong way risk.

Model-related adjustments
Model related adjustments are applied when either model inputs are overly simplified or the model has limitations deriving the fair value of a position. These adjustments are required to correct existing model weaknesses or deficiencies that were highlighted during the model review process.

Notes to the consolidated financial statements *(continued)*

6 Financial assets and liabilities *(continued)*

(e) Fair value of financial instruments

The table below sets out the Group's classification of each class of financial assets and liabilities and their carrying amounts as at 31 December 2017:

	Designated at fair value through profit or loss AED'000	Held for trading AED'000	Available for sale AED'000	Held to maturity AED'000	Loans and receivables AED'000	Amortised cost AED'000	Carrying amount AED'000
Financial Assets							
Cash and balances with central banks	-	-	-	-	138,111,054	-	138,111,054
Investments at fair value through profit or loss	11,122	19,309,642	-	-	-	-	19,320,764
Due from banks and financial institutions	-	-	-	-	13,829,490	-	13,829,490
Reverse repurchase agreements	-	-	-	-	21,346,974	-	21,346,974
Derivative financial instruments	524,827	10,874,605	-	-	-	-	11,399,432
Loans and advances	-	-	-	-	330,465,888	-	330,465,888
Non-trading investments	-	-	81,312,483	7,075,467	-	-	88,387,950
Other assets	-	-	-	-	15,542,116	-	15,542,116
	535,949	30,184,247	81,312,483	7,075,467	519,295,522	-	638,403,668
Financial Liabilities							
Due to banks and financial institutions	-	-	-	-	-	30,576,336	30,576,336
Repurchase agreements	-	-	-	-	-	37,674,016	37,674,016
Commercial Paper	-	-	-	-	-	24,124,097	24,124,097
Derivative financial instruments	4,975,181	9,966,150	-	-	-	-	14,941,331
Customer accounts and other deposits	-	-	-	-	-	395,843,664	395,843,664
Term borrowings	-	-	-	-	-	42,145,718	42,145,718
Other liabilities[1]	-	1,814,526	-	-	-	18,145,142	19,959,668
Subordinated notes	-	-	-	-	-	420,381	420,381
	4,975,181	11,780,676	-	-	-	548,929,354	565,685,211

[1] *Other liabilities that are held for trading are classified as level 1 in the fair value hierarchy.*

Notes to the consolidated financial statements *(continued)*

6 Financial assets and liabilities (continued)

(e) Fair value of financial instruments *(continued)*

The table below sets out the Group's classification of each class of financial assets and liabilities and their carrying amounts as at 31 December 2016:

	Designated at fair value through profit or loss AED'000	Held for trading AED'000	Available for sale AED'000	Held to maturity AED'000	Loans and receivables AED'000	Amortised cost AED'000	Carrying amount AED'000
Financial Assets							
Cash and balances with central banks	-	-	-	-	24,776,717	-	24,776,717
Investments at fair value through profit or loss	-	899,524	-	-	-	-	899,524
Due from banks and financial institutions	-	-	-	-	12,932,570	-	12,932,570
Reverse repurchase agreements	-	-	-	-	5,449,019	-	5,449,019
Derivative financial instruments	75,248	1,877,755	-	-	-	-	1,953,003
Loans and advances	-	-	-	-	134,650,001	-	134,650,001
Non-trading investments	-	-	25,942,164	2,431,305	-	-	28,373,469
Other assets	-	-	-	-	6,733,506	-	6,733,506
	75,248	2,777,279	25,942,164	2,431,305	184,541,813	-	215,767,809
Financial Liabilities							
Due to banks and financial institutions	-	-	-	-	-	11,585,628	11,585,628
Repurchase agreements	-	-	-	-	-	13,109,155	13,109,155
Commercial Paper	-	-	-	-	-	10,016,916	10,016,916
Derivative financial instruments	653,675	2,181,333	-	-	-	-	2,835,008
Customer accounts and other deposits	-	-	-	-	-	125,782,798	125,782,798
Term borrowings	-	-	-	-	-	18,294,545	18,294,545
Other liabilities[1]	-	-	-	-	-	4,293,545	4,293,545
	653,675	2,181,333	-	-	-	183,082,587	185,917,595

[1] *Other liabilities that are held for trading are classified as level 1 in the fair value hierarchy.*

Notes to the consolidated financial statements *(continued)*

6 Financial assets and liabilities *(continued)*

(e) Fair value of financial instruments *(continued)*

The Group's financial assets and financial liabilities that are classified as loans and receivables and at amortised cost, are categorised under Level 3 in the fair value hierarchy, as there is no active market for such assets and liabilities. The Group considers these to have a fair value approximately equivalent to their net carrying value as the majority of such financial instrument carries variable interest rates and relatively short tenor of maturity.

Financial instruments measured at fair value - hierarchy

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

	Level 1	Level 2	Level 3	Total
	AED'000	AED'000	AED'000	AED'000
As at 31 December 2017				
Financial assets held for trading	**17,170,765**	**2,131,636**	**7,241**	**19,309,642**
Designated at fair value through profit and loss	**11,122**	**-**	**-**	**11,122**
Available-for-sale financial assets	**76,177,486**	**3,266,871**	**1,868,126**	**81,312,483**
Derivative financial instruments (Assets)	**32,592**	**11,366,840**	**-**	**11,399,432**
	93,391,965	**16,765,347**	**1,875,367**	**112,032,679**
Derivative financial instruments (Liabilities)	**133,073**	**14,808,258**	**-**	**14,941,331**
As at 31 December 2016				
Financial assets held for trading	841,151	50,990	7,383	899,524
Available-for-sale financial assets	22,902,396	1,363,431	1,676,337	25,942,164
Derivative financial instruments (Assets)	674	1,952,329	-	1,953,003
	23,744,221	3,366,750	1,683,720	28,794,691
Derivative financial instruments (Liabilities)	-	2,835,008	-	2,835,008

Notes to the consolidated financial statements *(continued)*

6 Financial assets and liabilities *(continued)*

During the year, due to changes in market conditions for certain investment securities, quoted prices in active markets were available for these securities. Therefore, these securities, with a carrying amount of AED 279 million classified as available for sale financial assets and AED 344 million classified as financial assets held for trading were transferred from level 2 to level 1 of the fair value hierarchy.

The valuation techniques and inputs used in these consolidated financial statements are same as those prescribed in the Group as at and for the year ended 31 December 2016. Except for the fair value adjustments mentioned in Note 30.

Level 3 investment primarily include investments in private equity funds, and their valuations are based on the last net asset published by the fund manager.

The following table shows a reconciliation of instruments measured at fair value and classified as Level 3:

	2017 **AED'000**	2016 AED'000
Balance as at 1 January	**1,683,720**	1,663,598
Additions	**369,324**	52,167
Effect of business combination	**13,935**	-
Settlements and other adjustments	**(191,612)**	(32,045)
Balance as at 31 December	**1,875,367**	1,683,720

7 Cash and balances with central banks

	2017 **AED'000**	2016 AED'000
Cash on hand	**1,778,162**	447,068
Central Bank of the UAE		
cash reserve deposits	**20,732,467**	5,892,907
certificates of deposits	**14,987,010**	13,954,750
other balances	**4,505,644**	1,226,211
Balances with other central banks		
cash reserve deposits	**1,031,581**	-
other deposits and balances	**95,076,190**	3,255,781
	138,111,054	24,776,717

Cash reserve deposits are not available for the day to day operations of the Group.

Notes to the consolidated financial statements *(continued)*

8 Investments at fair value through profit or loss

	2017 AED'000	2016 AED'000
Investments in managed funds	**55,719**	50,990
Investments in equities	**503,769**	20,976
Debt securities	**18,761,276**	827,558
	19,320,764	899,524

Equity instruments include investments designated at fair value through profit or loss amounting to AED 11,122 thousand *(2016: Nil).*

9 Due from banks and financial institutions

	2017 AED'000	**2016 AED'000**
Current, call and notice deposits	**4,492,834**	2,796,646
Margin deposits	**7,491,982**	1,767,346
Fixed deposits	**1,844,674**	8,368,578
	13,829,490	12,932,570

10 Reverse repurchase agreements

The Group enters into reverse repurchase agreements in the normal course of business in which the third party transfers financial assets to the Group for short term financing. The carrying amount of financial assets at the reporting date amounted to AED 21,347 million *(2016: AED 5,449 million).*

No allowances for impairment have been recognised against reverse repurchase agreements during the year *(2016: nil)*.

At 31 December 2017, the fair value of financial assets accepted as collateral that the Group is permitted to sell or re-pledge in the absence of default was AED 20,985 million *(2016: AED 3,721 million).*

At 31 December 2017, the fair value of financial assets accepted as collateral that have been sold or re-pledged was AED 13,965 million *(2016: AED 351.1 million)*. The Group is obliged to return equivalent securities.

These transactions are conducted under terms that are usual and customary to standard lending, and securities borrowing and lending activities.

11 Loans and advances

	2017 AED'000	2016 AED'000
Gross loans and advances	**345,089,058**	139,685,075
Less: interest suspended	**(1,895,059)**	(567,014)
Less: allowance for impairment	**(12,728,111)**	(4,468,060)
Net loans and advances	**330,465,888**	134,650,001

Notes to the consolidated financial statements *(continued)*

11 Loans and advances *(continued)*

	2017 AED'000	2016 AED'000
By counterparty:		
Government sector	**5,006,234**	268,002
Public sector	**54,586,399**	14,788,945
Banking sector	**21,099,155**	4,528,512
Corporate / private sector	**193,175,957**	82,245,956
Personal / retail sector	**71,221,313**	37,853,660
Gross loans and advances	**345,089,058**	139,685,075

	2017 AED'000	2016 AED'000
By product:		
Overdrafts	**15,200,956**	8,458,421
Term loans	**216,493,775**	92,095,571
Trade related loans	**22,970,550**	7,616,625
Real estate	**32,926,373**	3,507,711
Mortgage loans	**17,907,513**	3,410,319
Personal loans	**30,246,430**	17,617,376
Credit cards	**8,035,270**	6,789,481
Vehicle financing loans	**1,148,140**	14,009
Others	**160,051**	175,562
Gross loans and advances	**345,089,058**	139,685,075

The movement in the allowance for impairment during the year is shown below:

	2017 AED'000	2016 AED'000
Beginning of the year	**4,468,060**	4,419,577
Increase due to acquisition and other adjustment	**8,919,060**	-
Impact of accounting policy alignment	**325,260**	-
Reversal of collective provision for the year	**(356,854)**	110,228
Net charge for specific provision	**2,719,151**	1,469,078
Amounts written off	**(3,346,566)**	(1,530,823)
End of the year	**12,728,111**	4,468,060

The Group provides lending against investment in equity securities and funds. The Group is authorised to liquidate these instruments if their coverage falls below the certain agreed threshold. The carrying value of such loans is AED 9,316 million *(2016: AED 2,645 million)* and the fair value of instruments held as collateral against such loans is AED 19,379 million *(2016: AED 4,774 million)*. During the year, the Group has liquidated insignificant amount of collateral due to fall in the coverage ratio.

Notes to the consolidated financial statements *(continued)*

11 Loans and advances *(continued)*

Islamic financing

Included in the above loans and advances are the following Islamic financing contracts:

	2017 AED'000	2016 AED'000
Ijara	**7,051,924**	1,008,563
Murabaha	**19,500,917**	9,823,352
Mudaraba	**218,177**	154,737
Others	**168,561**	279,819
Total Islamic financing contracts	**26,939,579**	11,266,471
Less: allowance for impairment	**(453,034)**	(62,158)
Less: suspended profit	**(32,671)**	(8,147)
	26,453,874	11,196,166

12 Non-trading Investments

	2017 AED'000	2016 AED'000
Available-for-sale investments	**81,312,483**	25,942,164
Held-to-maturity investments	**7,075,467**	2,431,305
Investment in associates and joint venture	**69,760**	40,030
	88,457,710	28,413,499

An analysis of non-trading investments by type at the reporting date is shown below:

	2017 AED'000			2016 AED'000		
	Quoted	**Unquoted**	**Total**	Quoted	Unquoted	Total
Equity investments	**450,356**	**234,364**	**684,720**	140,368	189,383	329,751
Investments in private equity funds	**-**	**1,703,524**	**1,703,524**	-	1,526,984	1,526,984
Debt investments	**84,330,388**	**1,727,335**	**86,057,723**	24,281,152	2,275,612	26,556,764
Funds	**11,743**	**-**	**11,743**	-	-	-
	84,792,487	**3,665,223**	**88,457,710**	24,421,520	3,991,979	28,413,499

Debt instruments under repurchase agreements included in non-trading investments at 31 December 2017 amounted to AED 23, 781 million *(31 December 2016: AED 12,601 million)*.

12 Non-trading investments *(continued)*

The non-trading investments include the following investments in associates of the Group:

	Percentage of holding	
	2017	2016
Green Emirates Properties PJSC	**40%**	40%
Midmak Properties LLC	**16%**	16%
Emirates Digital Wallet LLC	**23%**	-
MERCURY	**30%**	-

Green Emirates Properties PJSC ("GEP") is a private joint stock company incorporated in the Emirate of Abu Dhabi and engaged mainly in the management and brokerage of real estate properties in United Arab Emirates and overseas.

Midmak Properties LLC ("Midmak") is a limited liability company incorporated in the Emirate of Abu Dhabi. Midmak is involved in real estate activities. Although the Group owns 16% of the outstanding shares of Midmak, the investment has been classified as an associate as the Group exercises significant influence due to representation of the Board of Directors.

MERCURY is a limited liability company incorporated in the Emirate of Abu Dhabi to carry on business of investments and payment service schemes.

Emirates Digital Wallet LLC, established in 2017, is jointly owned by 16 of the leading UAE national banks, supported by the UAE Central Bank.

13 Investment Properties

	2017 **AED'000**	2016 AED'000
Beginning of the year	**6,422,502**	8,242,190
Additions	**553,203**	798,856
Business Combination transaction	**45,106**	-
Disposals / transfers	**(273,035)**	(2,612,893)
Fair value adjustment	**179,916**	(5,651)
End of the year	**6,927,692**	6,422,502

Amounts recognised in the consolidated statement of income in respect of net rental income of investment properties are as follows:

	2017 **AED'000**	2016 AED'000
Rental income derived from investment properties	**34,642**	150,994
Operating expenses	**(29,035)**	(55,584)
Net rental income from investment properties	**5,607**	95,410

Investment properties are stated at fair value which represents the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants under prevailing market conditions at the measurement date.

The Group's investment properties consist of land, buildings and properties under development in Abu Dhabi and Dubai. Management determined that these investment properties consist of two classes of commercial and retail assets, based on the nature, characteristics and risks of each property.

Notes to the consolidated financial statements *(continued)*

13 Investment properties *(continued)*

As at 31 December 2017 and 2016, fair value of the properties is based on the valuations performed by third party valuers and all are level 3 under fair value hierarchy. The valuers are accredited with recognised and relevant professional qualifications and with recent experience in the location and category of investment properties being valued. The fair values have been determined based on varying valuation models depending on the intended use of the investment properties; in accordance with the Royal Institution of Chartered Surveyors (RICS) Valuation Standards.

Description of valuation techniques used and key inputs to valuation on investment properties as at 31 December 2017 and 2016:

	Valuation technique	***Significant unobservable inputs***
Buildings	Comparable and Residual Method Sales Comparison Method	Comparable transactions Current market price of similar assets
Land	Comparable and Residual Method	Cost of construction Developer's profit Financing cost
Properties under development	Discounted cash flow method	Discount rate Cash inflows Cash outflows

Notes to the consolidated financial statements *(continued)*

14 Property and equipment

	Land, buildings and alterations AED'000	Computer systems and equipment AED'000	Furniture, equipment, safes and vehicles AED'000	Capital work -in-progress AED'000	Total AED'000
Cost					
At 1 January 2016	1,284,006	491,298	157,607	128,817	2,061,728
Additions	185,387	154,835	44,708	18,330	403,260
Allocations from CWIP	53,913	-	-	(53,913)	-
Disposals, transfers and write offs[1]	(367,961)	(20,546)	(7,057)	(1,480)	(397,044)
At 31 December 2016	1,155,345	625,587	195,258	91,754	2,067,944
Business Combination transaction (note 42)	**1,808,495**	**418,224**	**232,444**	**449,371**	**2,908,534**
Additions	**40,067**	**553,037**	**69,350**	**285,379**	**947,833**
Allocations from CWIP	**51,015**	**107,907**	**5,624**	**(164,546)**	**-**
Disposals, transfers and write offs[1]	**(100,307)**	**(244,234)**	**(16,804)**	**(161,635)**	**(522,980)**
At 31 December 2017	**2,954,615**	**1,460,521**	**485,872**	**500,323**	**5,401,331**
Accumulated depreciation and impairment losses					
At 1 January 2016	197,840	257,050	121,106	-	575,996
Charge for the year	29,648	72,087	18,125	-	119,860
Disposals, transfers and write offs[1]	(128,895)	(20,505)	(6,767)	-	(156,167)
At 31 December 2016	98,593	308,632	132,464	-	539,689
Business Combination transaction (note 42)	**477,026**	**405,027**	**185,174**	**-**	**1,067,227**
Charge for the year	**73,318**	**201,851**	**36,250**	**-**	**311,419**
Disposals, transfers and write offs[1]	**(2,395)**	**(45,741)**	**(4,369)**	**-**	**(52,505)**
At 31 December 2017	**646,542**	**869,769**	**349,519**	**-**	**1,865,830**
Carrying amounts					
At 31 December 2016	1,056,752	316,955	62,794	91,754	1,528,255
At 31 December 2017	**2,308,073**	**590,752**	**136,353**	**500,323**	**3,535,501**

[1] *adjusted for foreign exchange translation impact*

Notes to the consolidated financial statements *(continued)*

15 Intangibles

	2017 AED'000	2016 AED'000
Goodwill	**17,317,445**	36,868
Customer relationship	**1,813,517**	170,000
Core deposits	**976,038**	10,000
Brand	**22,000**	22,000
	20,129,000	238,868
Amortisation	**(227,626)**	(68,470)
	19,901,374	170,398

16 Other assets

	2017 AED'000	2016 AED'000
Interest receivable	**7,195,037**	1,385,187
Acceptances	**5,463,959**	3,906,933
Sundry debtors and other receivables	**2,976,835**	1,492,333
Deferred tax asset	**36,585**	-
	15,672,416	6,784,453

The Group does not perceive any significant credit risk on interest receivable and acceptances.

Acceptances arise when the Group is under an obligation to make payments against documents drawn under letters of credit. After acceptance, the instrument becomes an unconditional liability of the Group and is therefore recognised as a financial liability in the consolidated statement of financial position. However, every acceptance has a corresponding contractual right of reimbursement from the customer which is recognised as a financial asset.

17 Due to banks and financial institutions

	2017 AED'000	2016 AED'000
Banks and financial institutions		
Current, call and notice deposits	**3,445,932**	806,065
Margin	**1,131,317**	11,394
Fixed deposits	**12,303,765**	10,768,169
	16,881,014	11,585,628
Central banks		
Current and call deposits	**77,417**	-
Fixed and certificate of deposits	**13,617,905**	-
	13,695,322	-
	30,576,336	11,585,628

Due to banks and financial institutions are denominated in various currencies and carry a rate of interest in the range of -0.6% to 5.15% *(2016: -3.25% to 3.08%)*.

Notes to the consolidated financial statements *(continued)*

18 Repurchase agreements

The Group enters into repurchase agreements in the normal course of business by which it transfers recognised financial assets directly to third parties.

The carrying value that is also the fair value of financial assets collateralised at the reporting date amounted to AED 23,784 million *(2016: AED 12,601 million)* and their associated financial liabilities amounted to AED 37,674 million *(2016: AED 13,109 million).* The net difference between the fair value of the financial assets collateralised and the carrying value of the repurchase agreement is a shortage AED 13,891 million *(2016: shortage AED 508 million)*. The shortage is covered by re-pledging financial assets received as collateral against reverse repurchase agreements or through security borrowing arrangement from custodian.

19 Commercial paper

The Bank has established two Euro Commercial Paper Programmes with programme limits totaling up to USD 10.5 billion in aggregate. The Bank has a "US Dollar commercial paper programme" with a programme limit of USD 5 billion.

The notes outstanding as at the end of the reporting date amounted to AED 24,124,097 thousand (2016: AED 10,016,916 thousand) and have maturity period of less than 12 months.

The Group has not had any defaults of principal, interests, or other breaches with respect to its Commercial Paper during 2017.

20 Customer accounts and other deposits

	2017 AED'000	2016 AED'000
By account:		
Current accounts	**102,711,909**	30,700,398
Savings accounts	**13,323,504**	2,478,958
Margin accounts	**5,744,664**	1,226,395
Notice and time deposits	**239,389,966**	89,381,646
	361,170,043	123,787,397
Certificates of deposit	**34,673,621**	1,995,401
	395,843,664	125,782,798

	2017 AED'000	2016 AED'000
By counterparty:		
Government sector	**78,639,783**	7,513,728
Public sector	**74,303,858**	29,938,237
Corporate / private sector	**135,281,622**	65,185,805
Personal / retail sector	**72,944,780**	21,149,627
	361,170,043	123,787,397
Certificates of deposit	**34,673,621**	1,995,401
	395,843,664	125,782,798

Notes to the consolidated financial statements *(continued)*

20 Customer accounts and other deposits *(continued)*

	2017 AED'000	2016 AED'000
By location:		
UAE	**253,909,510**	89,063,630
Europe	**45,941,151**	2,795,887
Arab countries	**28,292,139**	5,889,136
Americas	**22,494,992**	10,843,200
Asia	**8,711,746**	14,725,736
Others	**1,820,505**	469,808
	361,170,043	123,787,397
Certificates of deposit	**34,673,621**	1,995,401
	395,843,664	125,782,798

Islamic customers' deposits

Included in the above Customer accounts and other deposits are the following Islamic term deposits:

	2017 AED'000	2016 AED'000
Wakala deposits	**781,321**	502,672
Mudaraba deposits	**623,727**	1,177,785
	1,405,048	1,680,457

21 Term borrowings

	2017 AED'000	2016 AED'000
Convertible notes	**1,830,006**	-
Other term notes	**40,315,712**	**18,294,545**
	42,145,718	**18,294,545**

Convertible notes include USD 500 million notes that mature in March 2018 and carry a fixed coupon that is paid semi-annually in arrears. The value of the conversion option at inception was AED 108,265 thousand and as such has been classified as a part of equity under convertible note – equity component reserve.

During the year, the Group has issued various fixed and floating rate notes. The Group hedges its currency and interest rate exposure on these notes. The nominal values of the notes issued during the year are stated below:

Notes to the consolidated financial statements *(continued)*

21 Term Borrowings *(continued)*

	2017 **AED'000**	2016 AED'000
Fixed rate		
AED	**96,830**	-
AUD	**-**	79,513
CHF	**565,454**	-
CNH	**62,015**	137,003
EUR	**-**	96,563
USD	**-**	3,107,358
Floating rate		
USD	**2,227,724**	9,939,138
EUR	**-**	231,752
	2,952,023	**13,591,327**

The Group has hedged the interest rate and foreign currency exposure on term borrowings. The nominal value hedged are AED 27.84 billion *(2016: AED 7.22 billion)* and the risks being hedged have a net negative fair value of AED 301.59 million *(2016: net positive fair value of AED 61.7 million)*. The Group has not had any defaults of principal, interests, or other breaches with respect to its term borrowings during 2017 and 2016.

21 Term Borrowings *(continued)*

Currency	Interest	2017 Up to 3 months AED'000	2017 3 months to 1 year AED'000	2017 1 to 3 years AED'000	2017 3 to 5 years AED'000	2017 Over 5 Years AED'000	2017 Total AED'000	2016 Up to 3 months AED'000	2016 3 months to 1 year AED'000	2016 1 to 3 years AED'000	2016 3 to 5 years AED'000	2016 Over 5 Years AED'000	2016 Total AED'000
AED	Equity linked	-	96,830	-	-	-	96,830	-	-	-	-	-	-
AED	3 month EIBOR + 80 bps to 156.5 bps p.a.	-	-	49,936	-	-	49,936	-	-	49,853	-	-	49,853
AUD	Fixed rate of 3.17% to 5.00% p.a.	861,918	-	1,983,239	84,717	-	2,929,874	-	-	656,344	-	-	656,344
AUD	3 month AUD BBSW + 110 bps to 142 bps p.a.	-	-	57,268	71,812	-	129,080	-	-	52,517	-	-	52,517
CHF	Fixed rate of 0.16% to 0.625% p.a.	-	-	-	754,538	556,742	1,311,280	-	-	-	735,396	-	735,396
CNH	Fixed rate of 4.5% to 5% p.a.	73,324	355,185	572,242	-	-	1,000,751	-	-	-	-	-	-
CNY	Fixed rate of 4.50% to 5.00% p.a.	-	-	-	-	-	-	-	205,060	418,294	-	-	623,354
EUR	Fixed rate of 0.516% to 3.00% p.a.	-	-	111,017	-	580,853	691,870	-	-	-	-	421,379	421,379
EUR	3 month EURIBOR + (33 bps to 36 bps) p.a.	66,128	-	263,084	-	-	329,212	-	58,136	-	-	-	58,136
HKD	Fixed rate of 2.37% to 4.45% p.a.	-	-	303,202	238,052	567,182	1,108,436	-	-	149,022	-	376,285	525,307
JPY	Fixed rate of 0.86% to 2.60% p.a.	-	-	325,853	-	347,592	673,445	-	-	315,826	-	-	315,826
MXN	Fixed rate of 0.50% p.a.	-	-	-	-	1,960	1,960	-	-	-	-	-	-
MYR	Fixed rate of 4.90% p.a.	-	-	453,894	-	-	453,894	-	-	-	-	-	-
SGD	Fixed rate of 2.10% p.a.	-	30,249	-	-	-	30,249	-	28,138	-	-	-	28,138
USD	Fixed rate of till 5.10% p.a.	1,830,007	-	10,284,027	2,134,531	8,265,264	22,513,829	1,836,500	2,387,450	3,477,479	-	453,937	8,155,366
USD	1-3 Month LIBOR + (5 bps to 185 bps) p.a.	367,098	2,221,999	7,992,009	243,966	-	10,825,072	3,673,000	-	2,853,042	146,887	-	6,672,929
		3,198,475	2,704,263	22,395,771	3,527,616	10,319,593	42,145,718	5,509,500	2,678,784	7,972,377	882,283	1,251,601	18,294,545

21 Term borrowings *(continued)*

During the year, the Group has issued various fixed and floating rate notes. The nominal values of the notes issued during the year are stated below:

	2017 AED'000	2016 AED'000
Beginning of the year	**18,294,545**	19,873,195
Increase due to acquisition	**31,308,591**	-
New issuances	**3,135,955**	2,519,939
Redemptions	**(11,433,020)**	(3,912,284)
Exchange and other adjustments	**839,647**	(186,305)
End of the year	**42,145,718**	18,294,545

22 Subordinated notes

	2017 AED'000	2016 AED'000
10 December 2012 issue *(maturity date: 9 December 2027)*	**420,381**	-

The Group has hedged the interest rate and foreign currency exposure on the subordinated notes. The Group has not had any defaults of principal, interests, or other breaches with respect to its subordinated notes during the year ended 31 December 2017.

23 Other liabilities

	2017 AED'000	2016 AED'000
Interest payable	**6,108,042**	674,520
Acceptances - net of discounting *(note 16)*	**2,506,422**	1,900,952
Provision employees' end of service benefits	**512,346**	75,934
Accounts payable, sundry creditors and other liabilities	**11,745,645**	2,047,513
Overseas income tax	**160,884**	-
	21,033,339	4,698,919

Employees end of service benefits

Defined benefit obligations

The Group provides for end of service benefits for its eligible employees. An actuarial valuation has been carried out as at December 31, 2017 to ascertain present value of the defined benefit obligation. A registered actuary in the UAE was appointed to evaluate the same. The present value of the defined benefit obligation, and the related current and past service cost, were measured using the Projected Unit Credit Method.

The following key assumptions (weighted average rates) were used to value the liabilities:

	2017
Discount rate	**3.39 % per annum**
Salary increase rate	**1.67 % per annum**

Notes to the consolidated financial statements *(continued)*

23 Other liabilities *(continued)*

Demographic assumptions for mortality, withdrawal and retirement were used in valuing the liabilities and benefits under the plan. Because of the nature of the benefit, which is a lump sum payable on exit due to any cause, a combined single decrement rate has been used.

A shift in the in the discount rate assumption by +/- 50 basis points would impact the liability by AED 4,508 thousand and AED 15,748 thousand respectively. Similarly, a shift in the salary increment assumption by +/- 50 basis points would impact the liability by AED 15,877 thousand and AED 4,723 thousand respectively.

The movement in the employees' end of service obligation was as follows:

	2017 AED'000	2016 AED'000
Balance at 1 January	**75,934**	72,801
Increase due to acquisition	**455,300**	
Net charge during the year	**47,920**	19,882
Paid during the year	**(69,761)**	(16,749)
Other adjustments	**2,953**	-
Balance at 31 December	**512,346**	75,934

Defined contribution plan
The Group pays contributions for its eligible employees which are treated as defined contribution plans. The charge for the year in respect of these contributions is AED 91,472 thousand *(2016: AED 21,970 thousand)*. As at the reporting date, pension payable of AED 16,576 thousand has been classified under other liabilities.

Overseas income tax
The Group has provided for overseas income tax in accordance with management's estimate of the total amount payable based on tax rates enacted or substantially enacted as at the reporting date. Where appropriate the Group has made payments of tax on account in respect of these estimated liabilities.

The overseas income tax charge for the year is calculated based upon the adjusted net profit for the year. The movement in the provision was as follows:

	2017 AED'000	2016 AED'000
At 1 January	**42,680**	18,896
Increase due to acquisition	**171,411**	--
Charge for the year	**224,989**	41,846
Overseas income tax paid, net of recoveries	**(278,196)**	(18,062)
At 31 December	**160,884**	42,680

24 Capital and reserves

Share Capital

The Merger between NBAD and FGB was effected by a capital issuance of 5,643 million shares of AED 1 by NBAD to the shareholders of FGB, in a share swap transaction at the exchange rate of 1.254 shares of NBAD for each share of FGB. Pursuant to the transaction, the shares of FGB were delisted from Abu Dhabi Stock Exchange and replaced with the new issued share capital. The newly issued share capital added to the outstanding shares of NBAD already in issue (being the share capital of the surviving legal entity at the time of merger) to constitute the share capital of the merged entity (First Abu Dhabi Bank).

Notes to the consolidated financial statements *(continued)*

24 Capital and reserves *(continued)*

The table below represents the effect of the merger transaction on share capital of the Group as of the date of the merger.

	Units in (AED'000)	%
Outstanding shares of FGB	4,500,000	
Exchange ratio	1.254	
Number of shares issued by NBAD to FGB	5,643,000	52.01
Outstanding shares of NBAD (Net of treasury shares)	5,207,713	47.99
Total shares of FAB post combination (Net of treasury shares)	10,850,713	100.00
Treasury shares	46,832	
Total shares of FAB post combination	10,897,545	
Effect of business combination transaction on share capital	6,397,545	

The general reserve is available for distribution to the shareholders at the recommendation of the Board of Directors. The following table illustrates the impact of business combination on share premium:

	AED'000
FGB Capital pre combination	4,500,000
Total consideration	53,572,167
Capital post combination	58,072,167
Adjustment to legal reserve	5,775,564
Total paid-in capital	63,847,731

The total paid-in capital comprises:

	AED'000
Share capital of the Bank after merger	10,897,545
Treasury shares on the date of merger	(46,832)
Share premium	52,997,018
Total paid-in capital	63,847,731

Statutory and special reserves

In accordance with the Bank's Articles of Association and the requirements of the Union Law No. (10) of 1980, a minimum of 10% of the annual net profit should be transferred to both statutory and special reserve until each of these reserves equal to 50% of the paid-up share capital. The Statutory and special reserve are not available for distribution to the shareholders.

Notes to the consolidated financial statements *(continued)*

24 Capital and reserves *(continued)*

Dividends

The following dividends were paid by the Group during the year ended 31 December:

	2017 AED'000	2016 AED'000
Dividend on ordinary shares paid during the year	**4,489,524**	4,423,230

Other reserves

Other reserves include the following:

(i) General reserve

The general reserve is available for distribution to the shareholders at the recommendation of the Board of Directors.

(ii) Fair value reserve

The fair value reserve includes the cumulative net change in the fair value of non-trading investments, until the investment is derecognised or impaired, and cash flow hedge reserve.

	2017 AED'000	2016 AED'000
Revaluation reserve – available-for-sale investments		
At 1 January	**413,171**	410,638
Net unrealised gains during the year	**635,883**	319,936
Net cumulative realised gains recognised in the consolidated statement of profit or loss during the year	**(371,559)**	(317,403)
At 31 December	**677,495**	413,171
Hedging reserve – cash flow hedge		
At 1 January	**(381)**	(19,791)
Changes in fair value	**(51,904)**	19,410
At 31 December	**(52,285)**	(381)
Total at 31 December	**625,210**	412,790

The hedging reserve comprises the effective portion of the cumulative net change in the fair value of cash flow hedging instruments related to hedged transactions. During the year, there has been no significant transfer from cash flow hedge reserve to profit or loss.

(iii) Revaluation reserve

The revaluation reserve of AED 280,601 thousand *(2016: AED 280,601 thousand)* is related to land included under property and equipment

24 Capital and reserves *(continued)*

Other reserves *(continued)*

(iv) Foreign currency translation reserve

Foreign currency translation reserve represents the exchange differences arising from translation of the net investment in foreign operations. During the year, there has been no transfer from foreign currency translation reserve to profit or loss.

25 Tier 1 capital notes

		2017 AED'000	2016 AED'000
Government of Abu Dhabi Notes (6 month EIBOR plus 2.3 percent per annum)	AED	**8,000,000**	4,000,000
USD 750 million Notes (5 year mid swap rate plus 3.35 percent per annum)	USD	**2,754,750**	-
		10,754,750	4,000,000

Tier 1 capital notes are perpetual, subordinated, unsecured and carry a fixed coupon during the initial period and are paid semi-annually in arrears. The Group may elect not to pay a coupon at its own discretion. The note holder does not have a right to claim the coupon and an election by the Group not to service coupon is not considered an event of default. In addition, there are certain circumstances under which the Group is prohibited from making a coupon payment on a relevant coupon payment date.

If the Group makes a non-payment election or a non-payment event occurs, then the Group will not (a) declare or pay any distribution or dividend or (b) redeem, purchase, cancel, reduce or otherwise acquire any of the share capital or any securities of the Group ranking pari passu with or junior to the Notes except securities, the term of which stipulate a mandatory redemption or conversion into equity, in each case unless or until two consecutive coupon payments have been paid in full.

During the year, coupon payment election was made by the Group in the amount of AED 381,089 thousand *(31 December 2016: AED* 138,256 *thousand)*.

26 Share option scheme

NBAD had introduced in 2008 a share based payment scheme (the "Scheme") for selected employees which would vest over three years and can be exercised within the next three years after the vesting period. The key vesting condition is that the option holder is in continued employment with the Group until the end of the vesting period. The options lapse six years after their date of grant irrespective of whether they are exercised or not.

The Group established a subsidiary to issue shares when the vested option is exercised by the employee. These shares are treated as treasury shares until exercised by the option holders.

As part of the merger, the Group has continued the scheme with the same terms and conditions. Employees exercising under the NBAD share option scheme shall be granted shares of the new entity.

Post-merger and up to the date of statement of financial position, 4,399 thousand options *(31 December 2016: None)* had been exercised by the option holders resulting in an increase in the total share capital by AED 4,399 thousand *(31 December 2016: Nil)* and share premium by AED 29,626 thousand *(31 December 2016: Nil)*.

Notes to the consolidated financial statements *(continued)*

27 Interest income

	2017 AED'000	2016 AED'000
Interest from:		
Central banks	**339,797**	69,006
Banks and financial institutions	**452,859**	160,853
Reverse repurchase agreements	**261,919**	37,587
Investments at fair value through profit or loss	**352,009**	64,152
Non-trading investments	**1,738,032**	615,568
Loans and advances	**13,187,171**	7,566,394
	16,331,787	8,513,560

28 Interest expense

	2017 AED'000	2016 AED'000
Interest to:		
Banks and financial institutions	**583,820**	253,341
Repurchase agreements	**373,651**	111,185
Commercial paper	**163,419**	30,784
Customer accounts and other deposits	**2,648,424**	1,278,398
Term borrowings	**1,150,740**	486,223
Subordinated notes	**15,540**	-
	4,935,594	2,159,931

29 Net fee and commission income

	2017 AED'000	2016 AED'000
Fee and commission income		
Trade finance	**855,577**	515,073
Collection services	**34,756**	8,523
Brokerage income	**32,806**	7,911
Asset management and investment services	**82,837**	2,214
Investments, derivatives and risk participation	**4,516**	-
Retail and corporate lending	**1,012,525**	682,137
Cards and e-services	**1,595,675**	687,933
Accounts related services	**84,023**	21,616
Commission on transfers	**96,318**	27,477
Others	**227,028**	158,213
Total fee and commission income	**4,026,061**	2,111,097
Fee and commission expense		
Brokerage commission	**28,224**	-
Handling charges	**22,740**	-
Credit card charges	**815,540**	140,128
Retail and corporate lending	**228,016**	167,974
Others	**33,686**	-
Total fee and commission expense	**1,128,206**	308,102
Net fee and commission income	**2,897,854**	1,802,995

Asset management and investment service fees include fees earned by the Group on trust and fiduciary activities where the Group holds or invests assets on behalf of its customers.

30 Net foreign exchange gain

	2017 AED'000	2016 AED'000
Trading and retranslation gain on foreign exchange and related derivatives[1]	**640,543**	198,476
Dealings with customers	**287,645**	24,180
	928,188	222,656

[1] Due to effective hedging strategies, the offsetting impact of hedging instruments is reflected in the net gains from sale of non-trading investments *(note 32)*.
Includes negative interest income of AED 213 million arising from placement with ECB.

31 Net gain on investments and derivatives

	2017 AED'000	2016 AED'000
Net realised and unrealised gain on investments at fair value through profit or loss and derivatives	**294,021**	80,217
Net gain from sale of non-trading Investments	**371,559**	317,403
Dividend income	**20,551**	5,115
	686,131	402,735

32 Other Operating Income

	2017 AED'000	2016 AED'000
Investment property income	**215,631**	550,682
Leasing related income	**95,824**	148,645
Other income	**160,635**	79,501
	472,090	778,828

33 General, administration and other operating expenses

	2017 AED'000	2016 AED'000
Staff costs	**2,782,316**	1,282,358
Other general and administration expenses	**1,611,022**	549,781
Depreciation (note14)	**311,418**	112,293
Intangible amortisation (note 15)	**159,156**	21,118
Sponsorships and donations	**37,584**	10,633
	4,901,496	1,976,183

Notes to the consolidated financial statements *(continued)*

34 Net impairment charge

	2017 AED'000	2016 AED'000
Collective provision for loans and advances	**(356,854)**	110,228
Specific provision for loans and advances	**2,719,151**	1,469,078
Recoveries	**(297,777)**	(127,144)
Write-off of impaired financial assets	**21,354**	-
Provisions for investment and others	**843**	20,852
	2,086,717	1,473,014

35 Overseas income tax expense

In addition to adjustments relating to deferred taxation, the charge for the year is calculated based upon the adjusted net profit for the year at rates of tax applicable in respective overseas locations.

The charge to the consolidated statement of profit or loss for the year was as follows:

	2017 AED'000	2016 AED'000
Charge for the year	**224,989**	41,846

36 Cash and cash equivalents

	2017 AED'000	2016 AED'000
Cash and balances with Central Banks	**138,111,054**	24,776,717
Due from banks and financial institutions	**13,829,490**	12,932,570
	151,940,544	37,709,287
Less: Balances with Central Banks maturing after three months of placement	**(10,186,771)**	(12,280,365)
Less: Due from banks and financial institutions maturing after three months of placement	**(7,147,856)**	(1,849,395)
	134,605,917	23,579,527

Notes to the consolidated financial statements *(continued)*

37 Commitments and contingencies

The Group, in the ordinary course of business, enters into various types of transactions that involve undertaking certain commitments such as letters of credit, guarantees and undrawn loan commitments.

There were no other significant changes in contingent liabilities and commitments during the year other than those arising out of normal course of business.

	2017 AED'000	2016 AED'000
Letter of credit	**48,863,532**	14,769,639
Letters of guarantees	**102,810,624**	45,385,877
Financial guarantees	**763,441**	-
Trade contingencies	**152,437,597**	60,155,516
Undrawn commitment to extend credit	**48,555,452**	19,460,113
Commitments for future capital expenditure	**347,537**	492,827
Commitments for future private equity investments	**985,495**	1,049,799
Commitments for operating lease payments	**169,950**	-
	50,058,434	21,002,739
Total commitments and contingencies	**202,496,031**	81,158,255

Credit risk characteristics of these unfunded facilities closely resemble the funded facilities as described in note 4 are neither past due nor impaired.

Letters of credit and guarantee ("Trade contingencies") commit the Group to make payments on behalf of customers' contingent upon the production of documents or the failure of the customer to perform under the terms of the contract.

Commitments to extend credit represent contractual commitments to extend loans and revolving credits. Commitments generally have fixed expiration dates or other termination clauses and may require a payment of a fee. Since commitments may expire without being drawn upon, the total contracted amounts do not necessarily represent future cash requirements.

Commitments for operating lease payments are payable as follows:

	2017 AED'000	2016 AED'000
Less than one year	**94,707**	-
Between one and five year	**61,662**	-
More than five year	**13,581**	-
Total commitments	**169,950**	-

Financial guarantee contracts includes credit default agreements entered with banks and financial institutions amounting to AED 165 million *(2016: nil)* which are primarily denominated in US Dollars.

Notes to the consolidated financial statements *(continued)*

37 Commitments and contingencies *(continued)*

Financial guarantee contracts mainly pertain to the banks and financial institutions.

Concentration by location:

	Undrawn loan Commitments		Trade contingencies	
	2017	2016	**2017**	2016
	AED'000	AED'000	**AED'000**	AED'000
UAE	**20,758,149**	8,653,096	**105,597,814**	45,221,453
Europe	**10,837,450**	3,689,740	**22,886,522**	2,998,876
Arab countries	**4,379,838**	1,692,840	**8,366,824**	2,234,464
Americas	**4,070,740**	-	**5,843,811**	46,764
Asia	**3,035,226**	1,379,328	**8,954,804**	5,497,031
Others	**5,474,049**	4,045,109	**787,822**	4,156,928
	48,555,452	19,460,113	**152,437,597**	60,155,516

38 Derivative financial instruments

In the ordinary course of business the Group enters into various types of transactions that involve derivative financial instruments. Derivatives are financial instruments that derive their value from the price of underlying items such as equities, bonds, interest rates, foreign exchange, credit spreads, commodities and equity or other indices. Derivatives enable users to increase, reduce or alter exposure to credit or market risks. Derivative financial instruments include forwards, futures, swaps and options. These transactions are primarily entered with banks and financial institutions.

Forwards and futures
Currency forwards represent commitments to purchase foreign and/or domestic currencies, including non-deliverable spot transactions (i.e. the transaction is net settled). Forward rate agreements are individually negotiated interest rate futures that call for a cash settlement at a future date for the difference between a contracted rate of interest and the current market rate, based on a notional principal amount. Foreign currency and interest rate futures are contractual obligations to receive or pay a net amount based on changes in currency rates or interest rates, or to buy or sell foreign currency or a financial instrument on a future date at a specified price, established in an organised financial market. The credit risk for futures contracts is negligible, as they are collateralised by cash or marketable securities, and changes in the futures' contract value are settled daily with the exchange.

Swaps
Currency and interest rate swaps are commitments to exchange one set of cash flows for another. Swaps result in an economic exchange of currencies or interest rates (for example, fixed rate for floating rate) or a combination of all these (i.e., cross-currency interest rate swaps). No exchange of principal takes place, except for certain cross currency swaps. The Group's credit risk represents the potential loss if counterparties fail to fulfil their obligation. This risk is monitored on an ongoing basis with reference to the current fair value, notional amount of the contracts and the liquidity of the market. To control the level of credit risk taken, the Group assesses counterparties using the same techniques as for its lending activities.

Notes to the consolidated financial statements *(continued)*

38 Derivative financial instruments *(continued)*

Options

Options are contractual agreements under which the seller (writer) grants the purchaser (holder) the right, but not the obligation, either to buy (a call option) or sell (a put option) at or by a set date or during a set period, a specific amount of a financial instrument at a predetermined price. The seller receives a premium from the purchaser in consideration for the assumption of risk. Options may be either exchange-traded or negotiated between the Group and a customer over the counter (OTC).

Derivatives are measured at fair value by reference to published price quotations in an active market. Where there is no active market for an instrument, fair value is derived from prices for the derivative's components using appropriate pricing or valuation models like counterparty prices or valuation techniques such as discounted cash flows, market prices, yield curves and other reference market data.

The table below shows the positive and negative fair values of derivative financial instruments, which are equivalent to their fair values, together with the notional amounts analysed by the term to maturity. The notional amount is the amount of a derivative's underlying, reference rate or index and is the basis upon which changes in the value of derivatives are measured. The notional amounts indicate the volume of transactions outstanding at year end and are neither indicative of the market risk nor credit risk.

38 Derivative financial instruments *(continued)*

31 December 2017

	Positive market value	Negative market value	Notional amount	Notional amounts by term to maturity: Less than three months	From three months to one year	From one year to three years	From three years to five years	Over five years
	AED'000	AED'000	AED'000	AED'000	AED'000	AED'000	AED'000	AED'000
***Held for trading**:*								
Interest rate derivatives								
Swaps	6,742,787	6,262,503	837,892,379	83,721,947	134,243,557	283,292,685	183,526,708	153,107,482
Forwards & Futures	4,213	2,349	39,465,202	12,120,055	23,672,514	3,672,633	-	-
Options & Swaptions	399,934	281,381	73,110,496	3,267,796	7,085,758	10,556,309	10,893,947	41,306,686
Foreign exchange derivatives								
Forwards	2,863,604	2,730,662	370,178,971	221,271,826	112,078,707	33,509,940	2,562,315	756,183
Options	563,748	394,103	132,404,746	44,551,147	67,697,369	19,114,805	1,041,425	-
Other derivatives contracts	300,319	295,152	7,276,322	3,186,012	1,389,224	492,237	2,208,849	-
	10,874,605	9,966,150	1,460,328,116	368,118,783	346,167,129	350,638,609	200,233,244	195,170,351
Held as fair value hedges:								
Interest rate derivatives								
Swaps	500,489	4,284,555	84,701,044	1,328,588	3,732,969	19,483,570	20,063,436	40,092,481
Swaptions	24,267	269,498	7,805,757	-	-	-	-	7,805,757
	524,756	4,554,053	92,506,801	1,328,588	3,732,969	19,483,570	20,063,436	47,898,238
Held as cash flow hedges								
Interest rate derivatives								
Swaps	2	414,382	5,023,946	-	173,736	3,850,664	999,546	-
Foreign exchange derivatives								
Forwards	69	6,746	2,918,877	2,918,877	-	-	-	-
	71	421,128	7,942,823	2,918,877	173,736	3,850,664	999,546	-
Total	11,399,432	14,941,331	1,560,777,740	372,366,248	350,073,834	373,972,843	221,296,226	243,068,589

Notes to the consolidated financial statements *(continued)*

38 Derivative financial instruments *(continued)*

31 December 2016				Notional amounts by term to maturity				
	Positive market value	Negative market value	Notional amount	Less than three months	From three months to one year	From one year to three years	From three years to five years	Over five years
	AED'000	AED'000	AED'000	AED'000	AED'000	AED'000	AED'000	AED'000
***Held for trading**:*								
Interest rate derivatives								
Swaps	588,981	517,092	57,769,253	1,301,604	8,291,452	11,967,781	17,903,968	18,304,448
Forwards & Futures	-	-	459,125	459,125	-	-	-	-
Options & Swaptions	132,927	147,190	5,963,789	229,272	326,401	988,894	3,564,419	854,803
Foreign exchange derivatives								
Forwards	565,366	810,433	58,718,836	29,439,509	24,070,588	2,603,410	2,267,480	337,849
Options	378,763	495,553	18,250,870	2,864,462	7,398,289	7,178,219	533,570	276,330
Other derivatives contracts	211,718	211,065	4,571,588	1,667,668	846,311	1,576,115	481,494	-
	1,877,755	2,181,333	145,733,461	35,961,640	40,933,041	24,314,419	24,750,931	19,773,430
Held as fair value hedges:								
Interest rate derivatives								
Swaps	75,248	653,392	13,350,546	609,795	202,379	2,465,924	4,057,275	6,015,173
Swaptions	-	283	65,259	-	-	65,259	-	-
	75,248	653,675	13,415,805	609,795	202,379	2,531,183	4,057,275	6,015,173
Held as cash flow hedges								
Interest rate derivatives								
Swaps	-	-	-	-	-	-	-	-
Forwards	-	-	-	-	-	-	-	-
	-	-	-	-	-	-	-	-
Total	1,953,003	2,835,008	159,149,266	36,571,435	41,135,420	26,845,602	28,808,206	25,788,603

Notes to the consolidated financial statements *(continued)*

38 Derivative financial instruments *(continued)*

The positive / negative fair value in respect of derivatives represents the gain/loss respectively, arising on fair valuation of the trading and hedging instrument. These amounts are not indicative of any current or future losses, as a similar positive / negative amount has been adjusted to the carrying value of the hedged loans and advances, non-trading investments, term borrowings and subordinated notes.

As at December 31, 2017, the Group received cash collateral of AED 1,017.2 million against positive fair value of derivative assets from certain counterparties. Correspondingly, the Group placed cash collateral of AED 7,722.1 million against the negative fair value of derivative liabilities.

Derivative related credit risk:

This is limited to the positive fair value of instruments that are favourable to the Group. These transactions are primarily entered with banks and financial institutions.

Derivatives held for trading

The Group uses derivatives, not designated in a qualifying hedge relationship, to manage its exposure to foreign currency, interest rate and credit risks or initiates positions with the expectation of profiting from favourable movement in prices, rates or indices. The instruments used mainly include interest rate and currency swaps and forward contracts. The fair values of those derivatives are shown in the table above.

Derivatives held as fair value hedge

The Group uses derivative financial instruments for hedging purposes as part of its asset and liability management strategy by taking offsetting positions in order to reduce its own exposure to fluctuations in exchange and interest rates. The Group uses interest rate swaps to hedge against the changes in fair value arising from specifically identified interest bearing assets such as loans and advances, non-trading investments, term borrowings and subordinate notes. The Group uses forward foreign exchange contracts and currency swaps to hedge against specifically identified currency risks.

Derivatives held as cash flow hedge

The Group uses forward contracts to hedge the foreign currency risk arising from its financial instruments. The Group has substantially matched the critical terms of the derivatives to have an effective hedge relationship.

39 Segmental information

The operating structure consists of four key Business segments across Geographic segments that are driving the business strategy, customer value propositions, products and channel development and customer relationships in addition to supporting the delivery of the Group's financial performance.

Business segments

Corporate & Investment Banking ("CIB")
Covers corporate and institutional clients through dedicated client segments (Corporate Banking, Institutional Banking, Commercial Banking, Privileged Clients Groups and Financial Institutions). CIB offers Credit facilities, Global Transaction Services, Corporate Finance, Islamic Finance and Global Markets products to both UAE and international clients.

Personal Banking ("PB")
Business targets retail, affluent and high net worth customers. Product offering ranges from every day banking products such as current accounts, deposits, credit cards and loans to sophisticated investments solutions and business banking products and services. Personal Banking Group is structured on the basis of the differing needs of the targeted broad customer base covering Retail, Affluent, Private banking and SME customer segments. The business furnishes variety of distribution and sales channels, including mobile and internet banking, branches and direct sales agents.

Subsidiaries
Business includes diversified business model supported by complementary offerings provided across real estate and property management, brokerage, conventional and Islamic consumer finance. This business covers subsidiaries partially or fully owned by the Group, it includes Dubai first, Aseel, ADNIF, FGP, ADNP, Mismak, NBAD Securities and First Gulf Libyan Bank.

Head office
The Group provides centralized human resources, information technology, operations, finance, strategy, investor relations, risk management, credit management, corporate communications, legal & compliance, internal audit, procurement, treasury operations, integration management office and administrative support to all of its businesses units.

Geographic segments
The Group will be managing its various business segments through a network of branches, subsidiaries and representative offices within the two defined geographic segments which are UAE and International. International business is further sub-divided into three sub-segments which are Middle East and Africa ("MEA"), Asia Pacific ("APAC") and Europe and Americas ("E&A").

- **MEA**
  FAB network in the MEA region is operated through its presence in Oman, Bahrain, Qatar, Egypt, Sudan, Kuwait, Lebanon, Jordan and Libya.

- **APAC**
  FAB's business in the Asia region is run through its presence in Singapore, Hong Kong, Korea, China, Malaysia and India.

- **E&A**
  FAB European and America coverage is carried out via its operational presence in United States of America, Brazil, United Kingdom, France and Switzerland.

Notes to the consolidated financial statements *(continued)*

39 Segmental information *(continued)*

	Business Segment					Geographic Segment				
	Corporate and Investment Banking AED'000	Personal Banking AED'000	Subsidiaries AED'000	Head Office AED'000	Total AED'000	UAE AED'000	Middle East And Africa AED'000	Europe and Americas AED'000	Asia - Pacific AED'000	Total AED'000
For the year ended 31 December 2017										
Net Interest income	5,156,214	4,330,597	514,366	1,395,016	11,396,193	10,097,926	469,649	574,330	254,288	11,396,193
Net non-interest income	2,754,503	1,492,222	721,569	15,970	4,984,264	4,353,583	298,250	191,805	140,626	4,984,264
Operating income	7,910,717	5,822,819	1,235,935	1,410,986	16,380,457	14,451,509	767,899	766,135	394,914	16,380,457
General administration and other operating expenses	1,556,779	2,060,853	488,210	795,654	4,901,496	4,229,458	270,110	252,289	149,639	4,901,496
Net impairment loss	296,647	1,584,569	503,000	(297,499)	2,086,717	1,985,085	83,435	7,486	10,711	2,086,717
Profit before tax	6,057,291	2,177,397	244,725	912,831	9,392,244	8,236,966	414,354	506,360	234,564	9,392,244
Overseas income tax expense	135,963	65,523	21,973	1,530	224,989	3,864	91,605	103,310	26,210	224,989
Net profit for the year	5,921,328	2,111,874	222,752	911,301	9,167,255	8,233,102	322,749	403,050	208,354	9,167,255
As at 31 December 2017										
Segment total assets	450,430,907	97,980,652	21,782,636	126,431,598	696,625,793	544,299,763	21,240,671	129,441,066	23,406,626	718,388,126
Inter segment balances					(27,657,498)					(49,419,831)
Total assets					668,968,295					668,968,295
Segment total liabilities	438,220,833	95,001,870	11,430,776	49,762,901	594,416,380	456,642,109	13,808,673	126,033,661	19,694,270	616,178,713
Inter segment balances					(27,657,498)					(49,419,831)
Total liabilities					566,758,882					566,758,882

Notes to the consolidated financial statements *(continued)*

39 Segmental information *(continued)*

	Business Segment					Geographic Segment				
	Corporate and Investment Banking AED'000	Personal Banking AED'000	Subsidiaries AED'000	Head Office AED'000	Total AED'000	UAE AED'000	Middle East And Africa AED'000	Europe and Americas AED'000	Asia - Pacific AED'000	Total AED'000
For the year ended 31 December 2016										
Net Interest income	3,073,078	2,533,174	278,628	468,749	6,353,629	6,043,498	89,015	22,961	198,155	6,353,629
Net non-interest income	1,533,284	601,370	1,073,199	(639)	3,207,214	2,886,964	170,607	8,386	141,257	3,207,214
Operating income	4,606,362	3,134,544	1,351,827	468,110	9,560,843	8,930,462	259,622	31,347	339,412	9,560,843
General administration and other operating expenses	385,472	515,602	248,936	826,174	1,976,184	1,873,813	38,601	2,803	60,967	1,976,184
Net impairment loss	162,163	955,674	336,736	18,441	1,473,014	1,741,667	59,914	5,896	(334,463)	1,473,014
Profit before tax	4,058,727	1,663,268	766,155	(376,504)	6,111,646	5,314,982	161,107	22,648	612,909	6,111,646
Overseas income tax expense	15,041	-	26,805	-	41,846	15,041	-	26,805	-	41,846
Net profit for the year	4,043,686	1,663,268	739,350	(376,504)	6,069,800	5,299,941	161,107	(4,157)	612,909	6,069,800
As at 31 December 2016										
Segment total assets	129,074,064	33,887,920	14,133,347	74,231,790	251,327,121	220,535,977	8,522,667	1,049,293	16,328,544	246,436,481
Inter segment balances					(27,347,180)					(22,456,540)
Total assets					223,979,941					223,979,941
Segment total liabilities	124,413,036	32,627,745	5,809,079	50,820,289	213,670,149	191,341,995	4,776,987	743,783	11,916,744	208,779,509
Inter segment balances					(27,347,180)					(22,456,540)
Total liabilities					186,322,969					186,322,969

Notes to the consolidated financial statements *(continued)*

40 Earnings per share

Earnings per share is calculated by dividing the net profit for the period after deduction of Tier 1 capital notes payment by the weighted average number of ordinary shares in issue during the period as set out below:

	2017	2016
Basic earnings per share:		
Net profit for the year (AED'000)	**9,132,648**	6,026,226
Less: payment on Tier 1 capital notes (AED'000)	**(381,089)**	(138,256)
Net profit after payment of Tier 1 capital notes (AED'000)	**8,751,559**	5,887,970
Weighted average number of ordinary shares:		
Number of shares issued / deemed to be outstanding from the beginning of the period ('000)	**5,643,000**	5,643,000
Weighted average number of shares deemed to be issued on reverse acquisition ('000)	**3,923,620**	-
Weighted average number of shares exercised under the share options scheme ('000)	**3,473**	-
Weighted average number of ordinary shares ('000)	**9,570,093**	5,643,000
Basic earnings per share (AED)	**0.91**	1.04
Diluted earnings per share:		
Net profit after payment of Tier 1 capital notes (AED'000)	**8,751,559**	5,887,970
Add: Interest on convertible note (AED'000)	**25,683**	-
Net profit for the year for calculating diluted earnings per share (AED'000)	**8,777,242**	5,887,970
Weighted average number of ordinary shares ('000)	**9,570,093**	5,643,000
Effect of dilutive potential ordinary shares issued ('000)	**97,861**	-
Weighted average number of dilutive shares under share options scheme ('000)	**5,125**	-
Weighted average number of ordinary shares in issue for diluted earnings per share ('000)	**9,673,079**	5,643,000
Diluted earnings per share (AED)	**0.91**	1.04

Notes to the consolidated financial statements *(continued)*

41 Related parties

Parties are considered to be related if one party has the ability to control the other party or exercise significant influence over the other party in making financial or operational decisions. Related parties comprise major shareholder, directors and key management personnel of the Group. Key management personnel comprise those executive committee members "EXCO" of the Group who are involved in the strategic planning and decision making of the Group. The terms of these transactions are approved by the Group's management and are made on terms agreed by the Board of Directors or management.

	2017			2016
	Senior management and related entities AED'000	**Major shareholders AED'000**	**Total AED'000**	Total AED'000
Balances with related parties at the reporting date are shown below:				
Financial assets	**1,481,279**	**11,394,596**	**12,875,875**	3,740,172
Financial liabilities	**8,116,999**	**8,547,073**	**16,664,072**	7,632,844
Contingent liabilities	**1,558,212**	**11,834,686**	**13,392,898**	1,828,369

Transactions carried out during the year ended with related parties are shown below:

	2017			2016
Interest income	**67,968**	**226,179**	**294,147**	82,222
Interest expense	**132,511**	**2,035**	**134,546**	120,408

No allowances for impairment have been recognised against loans and advances extended to related parties or contingent liabilities issued in favour of related parties during the year *(2016: AED nil)*.

42 Business Combination

On 7 December 2016, the shareholders of First Gulf Bank ("FGB") and National Bank of Abu Dhabi ("NBAD") approved the merger of FGB and NBAD. The merger was effected through a share-swap transaction at an exchange ratio of 1.254 NBAD shares for every one share of FGB. The merger is accounted for as a reverse acquisition.

FGB shares were delisted from the Abu Dhabi Securities Exchange and NBAD issued 5,643 million new shares to the shareholders of FGB. Following the completion of the merger, FGB shareholders owned approximately 52 percent of the combined bank and NBAD shareholders owned approximately 48 percent.

The merger transaction is accounted for in accordance with IFRS 3 - Business Combinations. IFRS 3 requires that an acquirer be identified in any business combination and acquisition accounting principles be applied. FGB was identified as the "accounting acquirer" in this transaction. The principles of reverse acquisition were used to reflect the acquisition of NBAD by FGB, effective 1 April 2017.

The merger was effected to create a new Bank with the financial strength, expertise and global network to accelerate growth in the UAE economy and drive the country's international business relationships.

Notes to the consolidated financial statements *(continued)*

42 Business Combination *(continued)*

a. Purchase consideration

The purchase consideration is determined to be AED 53,572 million, calculated on the basis of FGB's closing share price of AED12.90 per share on Abu Dhabi Securities Exchange on 30 March 2017.

The consideration is computed as follows:

Outstanding shares of FGB (units'000)	**4,500,000**
Divided by: FGB shareholder's percentage ownership in the Group	**52.01%**
Total number of shares of the Group (units'000)	**8,652,881**
Multiplied by: NBAD shareholder's percentage ownership in the Group	**47.99%**
Number of shares issued by FGB to NBAD's shareholders (units'000)	**4,152,881**
Multiplied by: Share price of FGB on transaction date	**12.90**
Total consideration (AED'000)	**53,572,167**

b. Integration related costs

The Group incurred Integration-related costs of AED 463 million relating to consultant and external legal fees and due diligence costs. These costs have been included in 'General, administrative and other operating expenses' in the consolidated statement of profit or loss.

c. Valuation approach and methodologies :

Customer relationship

- The income approach has been used in estimating the fair value of NBAD's customer relationships as an intangible asset as at the Transaction Date. The income approach values the customer relationship as the present value of the future earnings that it is expected to generate over its remaining useful economic life.
- Under the income approach, the Multi-period excess earnings method ("MEEM") has been utilized which is a commonly accepted method for valuing customer relationships.
- MEEM is a specific application of the discounted cash flow method where the value of an intangible asset is taken as the present value of the incremental (after-tax) cash flows attributable only to the subject intangible asset after deducting contributory asset charges ("CAC").
- The principle behind CAC is that an intangible asset "rents" or "leases" from a hypothetical third party all the assets it requires to produce the cash flows resulting from its development, that each project rents only those assets it needs (including element of goodwill) and not the ones that it does not need, and that each project pays the owner of the assets a fair return on (and of, when appropriate) the fair value of the rented assets.
- Thus, any net cash flows remaining after the CAC are attributable to the subject intangible asset being valued. The incremental after-tax cash flows attributable to the subject intangible asset are then discounted to their present value.

Core deposits

- The income approach to valuation has been used in estimating the fair value of the core deposits as an intangible asset as at the Transaction Date. The income approach values the core deposits as the present value of the future savings that are expected to be generated over its remaining useful economic life. Within the income approach, the MEEM method was utilized which is a commonly accepted method for valuing core deposits.

Notes to the consolidated financial statements *(continued)*

42 Business Combination *(continued)*

d. Identifiable assets acquired and liabilities assumed

The following table summarises the fair value of assets acquired and liabilities assumed on the date of acquisition.

	31 Mar 2017 AED'000
Assets	
Cash and balances with central banks	112,819,619
Investments at fair value through profit or loss	16,077,659
Due from banks and financial institutions	9,356,896
Reverse repurchase agreements	17,876,372
Derivative financial instruments	9,290,077
Loans and advances	207,807,269
Non-trading investments	47,105,716
Other assets	8,917,134
Investment properties	45,106
Property and equipment	1,841,308
Intangible assets – Customer relationships	1,643,517
Intangible assets – Core deposits	966,038
Total assets	433,746,711
Liabilities	
Due to banks and financial institutions	40,983,859
Repurchase agreements	6,600,187
Commercial paper	11,976,634
Derivative financial instruments	11,727,613
Customer accounts and other deposits	272,994,885
Term borrowings	31,308,591
Other liabilities	14,399,305
	389,991,074
Subordinated notes	365,234
Tier 1 capital notes	6,754,750
Share option scheme	235,798
Convertible notes - equity component	108,265
Total liabilities	397,455,121
NBAD net assets as at acquisition date attributable to its common equity holders	36,291,590

Notes to the consolidated financial statements *(continued)*

42 Business Combination *(continued)*

e. Goodwill and Intangibles

The Group has assumed the carrying value of NBAD's financial assets and liabilities as at 31 March 2017 to be equal to their fair value for the purpose of calculating goodwill:

	AED'000
Total consideration	**53,572,167**
NBAD net assets value	**(36,291,590)**
Goodwill	**17,280,577**

The Group has twelve months from the date of acquisition to complete a Purchase Price Allocation (PPA) exercise which sets out in detail the way in which the fair value of the acquired NBAD financial assets and liabilities has been determined. A comprehensive PPA exercise has been undertaken and the results of this exercise are reflected in these Financial Statements. The PPA exercise is substantially complete and we do not expect any changes to the fair value of the acquired NBAD financial assets and liabilities between now and 31 March 2018 to be significant.

f. Impact on Group's results

From the date of acquisition until 31 Dec 2017, NBAD contributed revenue and operating income of AED 7,257 million and a profit of AED 4,030 million to the Group's results. If the acquisition had occurred on 1 January 2017, management estimate that consolidated operating income and profit for the period would be AED 19,533 million and AED 10,915 million respectively, on a similar basis the comparative figure for 2016 would have been AED 20,302 million & AED 11,322 million. In determining these amounts, the Group has assumed that the fair value adjustments, determined provisionally, that arose on the date of acquisition would have been the same if the acquisition had occurred on 1 January 2017.

43 Change in accounting policy

Prior to the merger between FGB and NBAD, both banks maintained accounting records and prepared financial statements in accordance with IFRS and complied with the regulations of the UAE Central Bank ("UAE CB"). In order to facilitate compliance each bank had in place their own set of accounting policies.

Following the merger, FAB's management embarked on a journey to harmonise these accounting policies in order to determine a common set of accounting policies to be adopted by FAB. Following were the three key accounting policies which were harmonised:

- ***Harmonisation of the rating scales -*** the Customer Risk Rating ('CRR') scales of NBAD and FGB have been harmonised to create one set of CRR scales to be followed by FAB. Key driver for the harmonisation of the policy is to provide the users of the financial statements with more reliable and consistent financial information. No new information was used in determining the revised rating scales and for the adjustment calculated as result of the harmonisation of this policy.

Notes to the consolidated financial statements *(continued)*

43 Change in accounting policy *(continued)*

- ***Fair valuation adjustments –*** accounting policies in relation to fair valuation adjustments, for instance bid-offer reserves, were harmonised for the combined bank. Accounting standards permits entities to use a choice of pricing conventions or practical expedients in order to determine fair value of instruments. The Group has harmonised fair valuation adjustments to ensure the pricing conventions used by the Group provide more reliable approximation of the exit price for the securities held.

- ***Recognition of fees income –*** the Group has harmonised the combined Bank's accounting policies in order to consistently determine the fees which are recognised upfront or amortised over the life of the Loans and Advances and other financial products provided by the Bank.

Changes in accounting policies have been accounted for retrospectively through an adjustment of opening retained earnings.

44 Fiduciary activities

The Group held assets under management in trust or in a fiduciary capacity for its customers at 31 December 2017 amounting to AED 7,782.85 million *(2016: nil)*. Furthermore, the Group provides custodian services for some of its customers.

The underlying assets held in a custodial or fiduciary capacity are excluded from these consolidated financial statements of the Group.

45 Special Purpose Entities

The Group has created Special Purpose Entities (SPEs) with defined objectives to carry on fund management and investment activities on behalf of customers. The equity and investments managed by the SPEs are not controlled by the Group and the Group does not obtain benefits from the SPEs' operations, apart from commissions and fee income. In addition, the Group does not provide any guarantees or assume any liabilities of these entities. Consequently, the SPEs' assets, liabilities and results of operations are not included in these consolidated financial statements of the Group. The SPEs are as follows:

Legal name	Activities	Country of incorporation	Holding 2017
One share PLC	Investment Company	Republic of Ireland	100%
NBAD Private Equity 1	Fund Management	Cayman Island	58%
NBAD (Cayman) Limited	Fund Management	Cayman Island	100%

46 Comparative figures

In addition to the changes in the accounting policy impact highlighted in Note 43, certain comparative figures have been reclassified where appropriate to conform to the presentation adopted in these consolidated financial statements.