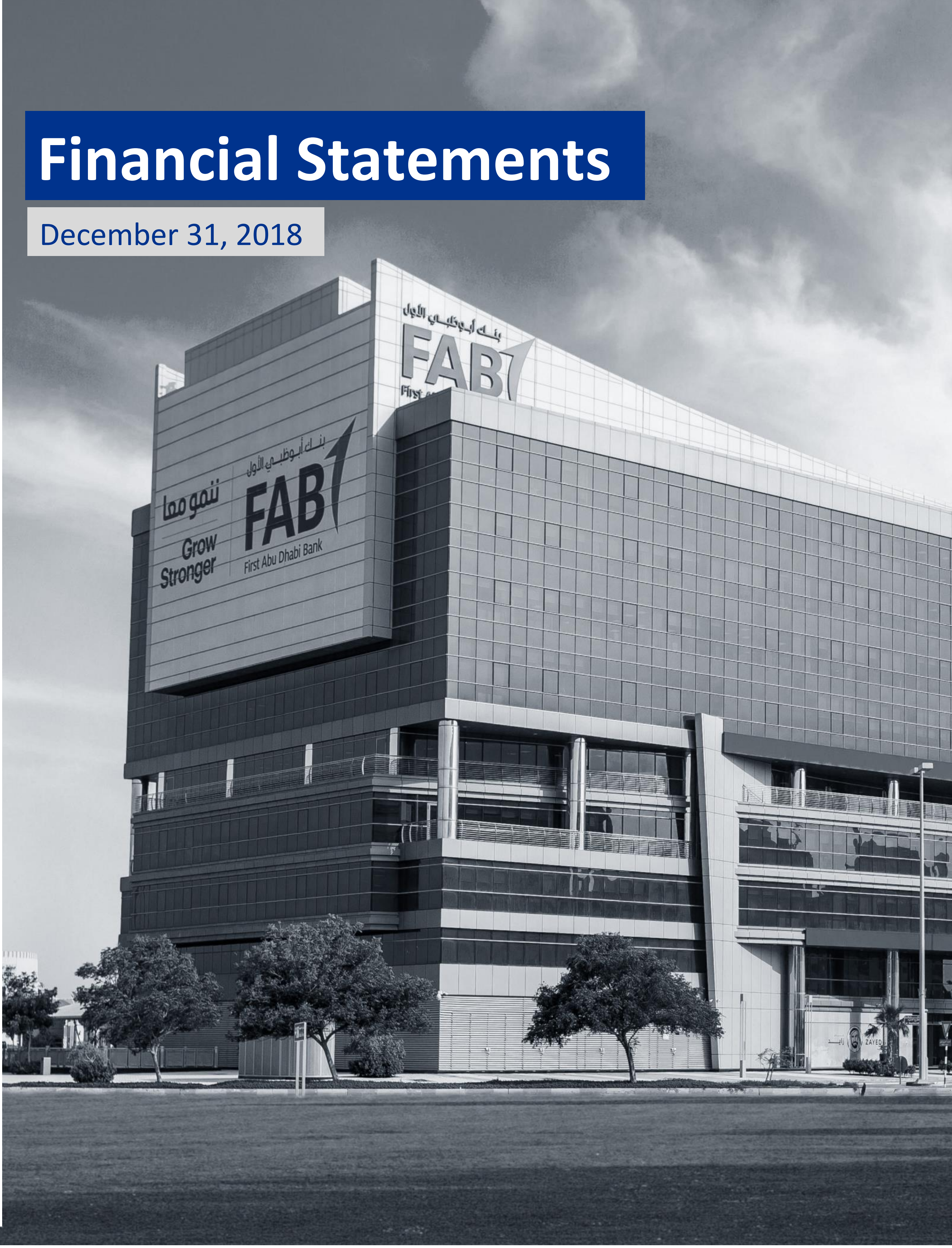
Financial Statements

December 31, 2018



FAB الإسلامي ISLAMIC

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FAB ISLAMIC الإسلامي

Board of Director's report

The Board of Directors are pleased to present their report and audited financial statements for First Abu Dhabi Islamic Finance Pvt.JSC ("the Company") for year ended 31 December 2018.

Principal Activities
The principal activities of the Company consist of Islamic financing, investments and other services in accordance with Islamic Sharia'a.

Results
During the year, the Company has recorded total assets of AED 900,988 thousand (2017: *AED 877,868 thousand*). The net profit for the year amounted to AED 24,669 thousand (2017: *AED 13,648 thousand*).

Chairman

KPMG

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Independent Auditors' Report

To the Board of Directors of First Abu Dhabi Islamic Finance Pvt. JSC

Report on the Audit of the Financial Statements

Opinion

We have audited the financial statements of First Abu Dhabi Islamic Finance Pvt. JSC ("the Company"), which comprise the statement of financial position as at 31 December 2018, the 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 financial statements present fairly, in all material respects, the financial position of the Company as at 31 December 2018, and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards (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 Financial Statements* section of our report. We are independent of the Company 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 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.

Other Information

Management is responsible for the other information. The other information comprises the Board of Directors' report, but does not include the financial statements and our auditors' report thereon.

Our opinion on the 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 financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated. If, based on the work we have performed, 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 Financial Statements

Management is responsible for the preparation and fair presentation of the 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 financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, management is responsible for assessing the Company'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 Company or to cease operations, or has no realistic alternative but to do so.

Those charged with Governance are responsible for overseeing the Company's financial reporting process.

Auditors' Responsibilities for the Audit of the Financial Statements

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

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

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.

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

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

- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Company's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditors' report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditors' report. However, future events or conditions may cause the Company to cease to continue as a going concern.

Auditors' Responsibilities for the Audit of the Financial Statements (continued)

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

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

Report on Other Legal and Regulatory Requirements

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

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

ii) the 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 Company has maintained proper books of account;

iv) the financial information included in the Board of Directors' report, in so far as it relates to these financial statements, is consistent with the books of account of the Company;

v) the Company has not purchased any shares during the year ended 31 December 2018;

vi) note 25 to the 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 Company has contravened during the financial year ended 31 December 2018 any of the applicable provisions of the UAE Federal Law No.(2) of 2015 or in respect of the Company, its Articles of Association, which would materially affect its activities or its financial position as at 31 December 2018; and

viii) there were no social contributions made during the year.

Further, as required by the Decretal Federal Law No. (14) of 2018, we report that we have obtained all the information and clarifications deemed necessary for the purposes of our audit.

KPMG Lower Gulf Limited

Emilio Pera

Registration number: 1146

Abu Dhabi, United Arab Emirates

28 March 2018

Statement of financial position

As at 31 December

Assets	Note	2018 AED'000	2017 AED'000
Cash and balances with banks	8	**295,791**	30,426
Investments at fair value through profit or loss	9	**69,835**	106,606
Due from banks and financial institutions	10	**85,000**	50,000
Islamic financing	11	**356,279**	593,057
Non-trading investments	12	**-**	10,858
Property and equipment	13	**2,442**	2,994
Other assets	14	**91,641**	83,927
Total assets		**900,988**	877,868
Liabilities			
Other liabilities	15	**27,367**	26,234
Total liabilities		**27,367**	26,234
Equity			
Share capital	16	**500,000**	500,000
Statutory and special reserves	16	**75,922**	70,988
Fair value reserve	16	**-**	(3,305)
Retained earnings		**297,699**	283,951
Total equity		**873,621**	851,634
Total liabilities and equity		**900,988**	877,868

Chairman

Chief Executive Officer

Rita Dugar

Head of Finance

The notes 1 to 27 are an integral part of these financial statements.
The independent auditor's report on audit of financial statements is set out on pages 2 to 4.

Statement of profit or loss and other comprehensive income

For the year ended 31 December

	Note	2018 AED'000	2017 AED'000
Profit income	*17*	**40,564**	59,066
Depositors' share of profit	*18*	**(4,451)**	(7,077)
Net profit income		**36,113**	51,989
Fee and commission income		**577**	2,055
Fee and commission expense		**(8,110)**	(5,735)
Net fee and commission expense	*19*	**(7,533)**	(3,680)
Net (loss)/ gain on investments and derivatives	*20*	**(1,520)**	518
Management fee income		**78,370**	102,881
Operating income		**105,430**	151,708
General, administration and other operating expenses	*21*	**(83,933)**	(114,643)
Profit before net impairment charge		**21,497**	37,065
Net impairment charge	*22*	**3,172**	(23,417)
Profit for the year		**24,669**	13,648
Other comprehensive income			
Items that will not be subsequently be reclassified to statement of profit or loss			
Net change in fair value of investments in equity instruments designated at fair value through other comprehensive income		**5,628**	360
Total comprehensive income for the year		**30,297**	14,008

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Statement of cash flows

For the year ended 31 December

	Note	2018 AED'000	2017 AED'000
Cash flows from operating activities			
Profit for the year		**24,669**	13,648
Adjustments for:			
Depreciation and amortisation	*13*	**739**	1,098
Net impairment charges	*22*	**(3,172)**	23,417
Property and Equipment written off		**-**	8,942
		22,236	47,105
Changes in:			
Investments at fair value through profit or loss		**36,771**	1,454
Islamic financing		**231,640**	483,319
Other assets		**(7,714)**	(11,080)
Due to banks and financial institutions		**-**	(457,044)
Other liabilities		**1,133**	(4,509)
Net cash from operating activities		**284,066**	59,245
Cash flows from investing activities			
Placements with Banks		**(35,000)**	(50,000)
Sale proceeds of Non Trading investments		**16,486**	-
Purchase of property and equipment, net of disposals		**(187)**	(591)
Net cash (used) investing activities		**(18,701)**	(50,591)
Net increase in cash and cash equivalents		**265,365**	8,654
Cash and cash equivalents at 1 January		**30,426**	21,772
Cash and cash equivalents at 31 December	*23*	**295,791**	30,426

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Statement of changes in equity

	Share capital AED '000	Statutory reserve AED '000	Special reserve AED '000	Fair value reserve AED '000	Retained earnings AED '000	Total AED '000
Balance at 1 January 2017	500,000	34,129	34,129	(3,665)	273,033	837,626
Profit for the year	-	-	-	-	13,648	13,648
Other comprehensive income for the year	-	-	-	360	-	360
Transfer to statutory reserve	-	1,365	-	-	(1,365)	-
Transfer to special reserve	-	-	1,365	-	(1,365)	-
Balance at 31 December 2017	500,000	35,494	35,494	(3,305)	283,951	851,634
Balance at 1 January 2018	**500,000**	**35,494**	**35,494**	**(3,305)**	**283,951**	**851,634**
Impact of adopting IFRS 9 at 1 January 2018 (note 4)	**-**	**-**	**-**	**-**	**(8,310)**	**(8,310)**
Restated balance at 1 January 2018	**500,000**	**35,494**	**35,494**	**(3,305)**	**275,641**	**843,324**
Profit for the year	**-**	**-**	**-**	**-**	**24,669**	**24,669**
Other comprehensive income for the year	**-**	**-**	**-**	**3,305**	**2,323**	**5,628**
Transfer to statutory reserve	**-**	**2,467**	**-**	**-**	**(2,467)**	**-**
Transfer to special reserve	**-**	**-**	**2,467**	**-**	**(2,467)**	**-**
Balance at 31 December 2018	**500,000**	**37,961**	**37,961**	-	**297,699**	**873,621**

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Notes to the financial statements

1 Legal status and principal activities

On 24th June 2018, Abu Dhabi National Islamic Finance PVT.JSC (ADNIF) board of directors approved the proposal to change the name of the company to 'First Abu Dhabi Islamic Finance Pvt.JSC" (FAB ISLAMIC). The registered office of the Company is Golden Beach Tower, Corniche Street, P.O. Box 40057, Abu Dhabi, United Arab Emirates.

First Abu Dhabi Islamic Finance Pvt.JSC (the "Company") is a private joint stock Company incorporated in the Emirate of Abu Dhabi on 14 November 2007 in accordance with the provisions of the UAE Federal Law No. 2 of 2015 Commercial Companies Law .The Company operates through its branches in Abu Dhabi, Dubai, Al Ain, Sharjah and Ras Al Khaimah.

The Company is primarily engaged in financing and investing activities that are conducted in accordance with Islamic Sharia'a principles approved by the Company's Sharia'a Supervisory Board.

The Company is a wholly owned subsidiary of First Abu Dhabi Bank (formerly a subsidiary of National Bank of Abu Dhabi PJSC, the "Parent").

On 7th 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.

2 Basis of Preparation

(a) Statement of Compliance

These 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, UAE Federal Law No 2 for Commercial Companies ("UAE Companies Law of 2015") was issued with effective date 1 July 2015. The Company is in compliance with applicable sections of the UAE Companies Law No 2 of 2015 as at the date of these financial statements.

These financial statements were authorised for issue by the Board of Directors on 28 March 2019.

(b) Basis of measurement

These 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 at fair value through other comprehensive income (FVOCI) are measured at fair value;

(c) Functional and presentation currency

These financial statements are presented in United Arab Emirates Dirhams ("AED"), which is the Company's functional currency. All amounts have been rounded to the nearest thousand, unless otherwise indicated.

Notes to the financial statements *(continued)*

2 Basis of Preparation *(continued)*

(d) Use of estimates and judgments

The preparation of financial statements requires management to make judgments, 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 judgments in applying accounting policies that have the most significant effect on the amounts recognised in these financial statements are described in note 6.

3 Significant accounting policies

(a) New and Amended standards and interpretations adopted

The Company has adopted IFRS 9 and IFRS 15 from 1 January 2018. A number of other new standards are also effective from 1 January 2018 but they do not have a material effect on the Company's financial statements.

Due to the transition method chosen by the Company in applying IFRS 9, comparative information throughout these financial statements has not been restated to reflect its requirements.

The adoption of IFRS 15 did not impact the timing or amount of fee and commission income from contracts with customers and the related assets and liabilities recognised by the Company. Accordingly, the impact on the comparative information is limited to new disclosure requirements.

The effect of initially applying these standards is mainly attributed to the following:

- an increase in impairment losses recognised on financial assets (see Note 4); and
- additional disclosures related to IFRS 9 (see Notes 5(a)).

Except for the changes below, the Company has consistently applied the accounting policies as to all periods presented in these financial statements.

(i) IFRS 9 – Financial Instruments

IFRS 9 sets out requirements for recognizing and measuring financial assets, financial liabilities and some contracts to buy or sell non-financial items. This standard replaces IAS 39 Financial Instruments: Recognition and Measurement. The requirements of IFRS 9 represent a significant change from IAS 39. The new standard brings fundamental changes to the accounting for financial assets and to certain aspects of the accounting for financial liabilities.

As permitted by IFRS 9, the Company has elected to continue to apply the hedge accounting requirements of IAS 39. As a result of the adoption of IFRS 9, the Company has adopted consequential amendments to IAS 1 Presentation of financial statements, which require separate presentation in the statement of profit or loss and statement of other comprehensive income of profit income revenue calculated using the effective profit rate method.

Additionally, the Company has adopted consequential amendments to IFRS 7 Financial Instruments: Disclosures that are applied to disclosures about 2018, but have not been applied to the comparative information.

The key changes to the Company's accounting policies resulting from its adoption of IFRS 9 are summarised below. The full impact of adopting the standard is set out in Note 4.

Notes to the financial statements *(continued)*

3 Significant accounting policies *(continued)*

(a) New and Amended standards and interpretations adopted *(continued)*

(i) IFRS 9 – Financial Instruments *(continued)*

Classification of financial assets and financial liabilities

IFRS 9 contains three principal classification categories for financial assets: measured at amortised cost, fair value through other comprehensive income ("FVOCI") and fair value through profit or loss ("FVTPL"). IFRS 9 classification is generally based on the business model in which a financial asset is managed and its contractual cash flows. The standard eliminates the previous IAS 39 categories of held-to-maturity, loans and receivables and available-for-sale. Under IFRS 9, derivatives embedded in contracts where the host is a financial asset in the scope of the standard are never bifurcated. Instead, the whole hybrid instrument is assessed for classification.

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

- the amount of change in the fair value that is attributable to changes in the credit risk of the liability is presented in OCI; and
- the remaining amount of change in the fair value is presented in profit or loss.

For an explanation of how the Company classifies financial liabilities under IFRS 9, see Note 3(b)(ii).

Impairment of financial assets

IFRS 9 replaces the 'incurred loss' model in IAS 39 with an 'expected credit loss' ("ECL") model. The new impairment model also applies to certain islamic financing commitments and financial guarantee contracts but not to equity investments. Under IFRS 9, credit losses are recognized earlier than under IAS 39. For an explanation of how the Company applies the impairment requirements of IFRS 9, see Note 3(b)(vii).

Transition

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

- Comparative periods generally have not been restated. Differences in the carrying amounts of financial assets and financial liabilities resulting from the adoption of IFRS 9 are recognised in retained earnings and reserves as at 1 January 2018. Accordingly, the information presented for 2017 does not reflect the requirements of IFRS 9 and therefore is not comparable to the information presented for 2018 under IFRS 9.

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

    - The determination of the business model within which a financial asset is held.
    - The designation and revocation of previous designations of certain financial assets and financial liabilities as measured at FVTPL.
    - The designation of certain investments in equity instruments not held for trading as at FVOCI.
    - For financial liabilities designated as at FVTPL, the determination of whether presenting the effects of changes in the financial liability's credit risk in OCI would create or enlarge an accounting mismatch in profit or loss.

- If a debt security had low credit risk at the date of initial application of IFRS 9, then the Company has assumed that credit risk on the asset had not increased significantly since its initial recognition.

For more information and details on the changes and implications resulting from the adoption of IFRS 9, see Note 4.

Notes to the financial statements *(continued)*

3 Significant accounting policies *(continued)*

(a) New and Amended standards and interpretations adopted *(continued)*

(ii) IFRS 15 - Revenue from contracts with customers

IFRS 15 establishes a comprehensive framework for determining whether, how much and when revenue is recognised. It replaced IAS 18 Revenue, IAS 11 Construction Contracts and related interpretations.

The Company applied IFRS 15 on 1 January 2018 retrospectively in accordance with IAS 8 without any practical expedients. The timing or amount of the Company's fee and commission income from contracts with customers was not impacted by the adoption of IFRS 15. The impact of IFRS 15 was limited to the new disclosure requirements.

(b) Financial assets and liabilities

(i) Recognition and initial measurement

The Company initially recognizes Islamic financing and customers' deposits on the date on which they are originated. All other financial instruments (including regular way purchases and sales of financial assets) are recognized on the trade date, which is the date on which the Company becomes a party to the contractual provisions of the instrument.

All regular way purchases and sales of financial assets are recognized 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.

(ii) Classification

Financial assets – Policy applicable from 1 January 2018

On initial recognition, a financial asset is classified as measured at: amortised cost, FVOCI or FVTPL. A financial asset is measured at amortised cost if it meets both of the following conditions and is not designated as at FVTPL:

- the asset is held within a business model whose objective is to hold assets to collect contractual cash flows; and
- the contractual terms of the financial asset give rise on specified dates to cash flows that are Solely Payment of Principal and Profit "SPPP".

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

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

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

All other financial assets are classified as measured at FVTPL.

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

Notes to the financial statements *(continued)*

3 Significant accounting policies *(continued)*

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

(ii) Classification *(continued)*

Business model assessment

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

- the stated policies and objectives for the portfolio and the operation of those policies in practice. In particular, whether management's strategy focuses on earning contractual profit revenue, maintaining a particular profit rate profile, matching the duration of the financial assets to the duration of the liabilities that are funding those assets or realising cash flows through the sale of the assets;
- how the performance of the portfolio is evaluated and reported to the Company's management;
- the risks that affect the performance of the business model (and the financial assets held within that business model) and its strategy for how those risks are managed;
- how managers of the business are compensated (e.g. whether compensation is based on the fair value of the assets managed or the contractual cash flows collected); and
- the frequency, volume and timing of sales in prior periods, the reasons for such sales and its expectations about future sales activity. However, information about sales activity is not considered in isolation, but as part of an overall assessment of how the Company's stated objective for managing the financial assets is achieved and how much cash flows are realised.

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

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

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

In assessing whether the contractual cash flows are SPPP, the Company considers the contractual terms of the instrument. This includes assessing whether the financial asset contains a contractual term that could change the timing or amount of contractual cash flows such that it would not meet this condition. In making the assessment, the company considers:

- contingent events that would change the amount and timing of cash flows;
- leverage features;
- prepayment and extension terms;
- terms that limit the Company's claim to cash flows from specified assets (e.g.non-recourse islamic financing); and
- features that modify consideration of the time value of money (e.g. periodical reset of profit rates).

Notes to the financial statements *(continued)*

3 Significant accounting policies *(continued)*

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

(ii) Classification (continued)

Financial assets – Policy applicable from 1 January 2018 *(continued)*

Non-recourse Islamic Facilities

In some cases, islamic facilities made by the Company that are secured by collateral of the borrower limit the Company's claim to cash flows of the underlying collateral (non-recourse finances). The company applies judgment in assessing whether the non-recourse facilities meet the SPPP criterion. The Company typically considers the following information when making this judgement:

- whether the contractual arrangement specifically defines the amounts and dates of the cash payments of the facility;
- the fair value of the collateral relative to the amount of the secured financial asset;
- the ability and willingness of the borrower to make contractual payments, notwithstanding a decline in the value of collateral;
- whether the borrower is an individual or a substantive operating entity or is a special-purpose entity;
- the Company's risk of loss on the asset relative to a full-recourse facility;
- the extent to which the collateral represents all or a substantial portion of the borrower's assets; and
- whether the company will benefit from any upside from the underlying assets.

Reclassifications

Financial assets are not reclassified subsequent to their initial recognition, except in the period after the Company changes its business model for managing financial assets.

Financial assets – Policy applicable prior to 1 January 2018

The Company 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 Company 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 Company 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.

Notes to the financial statements *(continued)*

3 Significant accounting policies *(continued)*

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

(ii) Classification (continued)

Financial assets – Policy applicable prior to 1 January 2018 *(continued)*

(b) Finances and receivables

Finances and receivables include cash and balances with banks, due from bank and financial institutions, finance lease receivables, and islamic financing assets. These are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market and that the Company 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 Company has the positive intent and ability to hold to maturity.

(d) Available-for-sale

The Company has classified non-derivative financial assets designated as available-for-sale when these are not classified as islamic finances 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 profit rates or pricing of the financial assets.

(iii) De-recognition

Financial assets

The Company derecognises a financial asset when the contractual rights to the cash flows from the financial asset expire (see also 3b(iv)), or it transfers the rights to receive the contractual cash flows in a transaction in which substantially all of the risks and rewards of ownership of the financial asset are transferred or in which the Company neither transfers nor retains substantially all of the risks and rewards of ownership and it does not retain control of the financial asset.

On derecognition of a financial asset, the difference between the carrying amount of the asset (or the carrying amount allocated to the portion of the asset derecognised) and the sum of (i) the consideration received (including any new asset obtained less any new liability assumed) and (ii) any cumulative gain or loss that had been recognised in OCI is recognised in profit or loss.

From 1 January 2018 any cumulative gain/loss recognised in OCI in respect of equity investment securities designated as at FVOCI is not recognised in profit or loss on derecognition of such securities. Any profit in transferred financial assets that qualify for derecognition that is created or retained by the Company is recognised as a separate asset or liability.

In transactions in which the Company neither retains nor transfers substantially all of the risks and rewards of ownership of a financial asset and it retains control over the asset, the Company continues to recognise the asset to the extent of its continuing involvement, determined by the extent to which it is exposed to changes in the value of the transferred asset.

In certain transactions, the Company retains the obligation to service the transferred financial asset for a fee. The transferred asset is derecognised if it meets the derecognition criteria. An asset or liability is recognised for the servicing contract if the servicing fee is more than adequate (asset) or is less than adequate (liability) for performing the servicing.

3 Significant accounting policies *(continued)*

(iii) Derecognition *(continued)*

Financial liabilities

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

(iv) Modifications of financial assets and financial liabilities

Policy applicable from 1 January 2018

Financial assets

If the terms of a financial asset are modified, then the Company evaluates whether the cash flows of the modified asset are substantially different. If the cash flows are substantially different, then the contractual rights to cash flows from the original financial asset are deemed to have expired. In this case, the original financial asset is derecognised and a new financial asset is recognised at fair value plus any eligible transaction costs. Any fees received as part of the modification are accounted for as follows:

- fees that are considered in determining the fair value of the new asset and fees that represent reimbursement of eligible transaction costs are included in the initial measurement of the asset; and
- other fees are included in profit or loss as part of the gain or loss on derecognition.

If cash flows are modified when the borrower is in financial difficulties, then the objective of the modification is usually to maximise recovery of the original contractual terms rather than to originate a new asset with substantially different terms. If the Company plans to modify a financial asset in a way that would result in forgiveness of cash flows, then it first considers whether a portion of the asset should be written off before the modification takes place. This approach impacts the result of the quantitative evaluation and means that the derecognition criteria are not usually met in such cases.

If the modification of a financial asset measured at amortised cost or FVOCI does not result in derecognition of the financial asset, then the Company first recalculates the gross carrying amount of the financial asset using the original effective profit rate of the asset and recognises the resulting adjustment as a modification gain or loss in profit or loss. For floating-rate financial assets, the original effective profit rate used to calculate the modification gain or loss is adjusted to reflect current market terms at the time of the modification. Any costs or fees incurred and fees receivable as part of the modification adjust the gross carrying amount of the modified financial asset and are amortised over the remaining term of the modified financial asset.

If such a modification is carried out because of financial difficulties of the borrower, then the gain or loss is presented together with impairment losses. In other cases, it is presented as profit income calculated using the effective profit rate method.

Financial liabilities

The Company derecognises a financial liability when its terms are modified and the cash flows of the modified liability are substantially different. In this case, a new financial liability based on the modified terms is recognised at fair value. The difference between the carrying amount of the financial liability derecognised and consideration paid is recognised in profit or loss. Consideration paid includes non-financial assets transferred, if any, and the assumption of liabilities, including the new modified financial liability.

If the modification of a financial liability is not accounted for as derecognition, then the amortised cost of the liability is recalculated by discounting the modified cash flows at the original effective profit rate and the resulting gain or loss is recognised in profit or loss. For floating-rate financial liabilities, the original effective profit rate used to calculate the modification gain or loss is adjusted to reflect current market terms at the time of the modification. Any costs and fees incurred are recognised as an adjustment to the carrying amount of the liability and amortised over the remaining term of the modified financial liability by re-computing the effective profit rate on the instrument.

Notes to the financial statements *(continued)*

3 Significant accounting policies *(continued)*

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

(iv) Modifications of financial assets and financial liabilities *(continued)*

Policy applicable prior to 1 January 2018

Financial assets

If the terms of a financial asset were modified, then the Company evaluated whether the cash flows of the modified asset were substantially different. If the cash flows were substantially different, then the contractual rights to cash flows from the original financial asset were deemed to have expired. In this case, the original financial asset was derecognised (see 3b(iii)) and a new financial asset was recognised at fair value.

If the terms of a financial asset were modified because of financial difficulties of the borrower and the asset was not derecognised, then impairment of the asset was measured using the premodification profit rate (see 3b(vii)).

Financial liabilities

The Company derecognised a financial liability when its terms were modified and the cash flows of the modified liability were substantially different. In this case, a new financial liability based on the modified terms was recognised at fair value. The difference between the carrying amount of the financial liability extinguished and consideration paid was recognised in profit or loss. Consideration paid included non-financial assets transferred, if any, and the assumption of liabilities, including the new modified financial liability.

If the modification of a financial liability was not accounted for as derecognition, then any costs and fees incurred were recognised as an adjustment to the carrying amount of the liability and amortised over the remaining term of the modified financial liability by re-computing the effective profit rate on the instrument.

(v) Offsetting

As per IAS 32, financial assets and liabilities are offset and the net amount presented in the statement of financial position when, and only when, the Company 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 Company's trading activity.

(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 Company's has access at that date. The fair value of a liability reflects its non-performance risk. When available, the Company 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 Company 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 Company 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 recognised in the 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.

Notes to the financial statements *(continued)*

3 Significant accounting policies *(continued)*

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

(vi) Fair value measurement *(continued)*

If an asset or a liability measured at fair value has a bid price and an ask price, the Company 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 Company 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.

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

(vii) Impairment

Policy applicable from 1 January 2018

Financial instruments carried at amortised cost

The Company recognises loss allowances for ECL on the following financial instruments that are not measured at FVTPL:

- Cash and balances with Banks
- Islamic financing assets;
- Due from banks; and
- Islamic financing commitments issued.

No impairment loss is recognised on equity investments.

The Company measures loss allowances at an amount equal to lifetime ECL, except for the following, for which they are measured as 12-month ECL:

- debt investment securities that are determined to have low credit risk at the reporting date; and
- other financial instruments (other than lease receivables) on which credit risk has not increased significantly since their initial recognition (see Note 5(a)).

Loss allowances for lease receivables are always measured at an amount equal to lifetime ECL.

Notes to the financial statements *(continued)*

3 Significant accounting policies *(continued)*

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

(vii) Impairment *(continued)*

Policy applicable from 1 January 2018 *(continued)*

Measurement of ECL

Credit loss allowances are measured using a three-stage approach based on the extent of credit deterioration since origination:

- Stage 1 – Where there has not been a significant increase in credit risk (SICR) since initial recognition of a financial instrument, an amount equal to 12 months expected credit loss is recorded. The expected credit loss is computed using a probability of default occurring over the next 12 months. For those instruments with a remaining maturity of less than 12 months, a probability of default corresponding to remaining term to maturity is used.
- Stage 2 – When a financial instrument experiences a SICR subsequent to origination but is not considered to be impaired, it is included in Stage 2. This requires the computation of expected credit loss based on the probability of default over the remaining estimated life of the financial instrument.
- Stage 3 – Financial instruments that are considered to be impaired are included in this stage. Similar to Stage 2, the allowance for credit losses captures the lifetime expected credit losses.

The key inputs into the measurement of ECL are:

- Probability of default (PD);
- Loss given default (LGD);
- Exposure at default (EAD)

These parameters are generally derived from statistical models and other historical data. They are adjusted to reflect forward-looking information. Additionally, the company has elaborate review process to adjust ECL for factors not available in the model.

Details of these statistical parameters/inputs are as follows:

- PD – The probability of default is an estimate of the likelihood of default over a given time horizon.
- EAD – The exposure at default is an estimate of the exposure at a future default date, taking into account expected changes in the exposure after the reporting date
- LGD – The loss given default is an estimate of the loss arising in the case where a default occurs at a given time. It is based on the difference between the contractual cash flows due and those that the lender would expect to receive, including from the realization of any collateral. It is usually expressed as a percentage of the EAD.

ECL are a probability-weighted estimate of credit losses. They are measured as follows:

- financial assets that are not credit-impaired at the reporting date: as the present value of all cash shortfalls (i.e. the difference between the cash flows due to the entity in accordance with the contract and the cash flows that the Company expects to receive);
- financial assets that are credit-impaired at the reporting date: as the difference between the gross carrying amount and the present value of estimated future cash flows;
- undrawn finance commitments: as the present value of the difference between the contractual cash flows that are due to the Company if the commitment is drawn down and the cash flows that the Company expects to receive; and
- financial guarantee contracts: the expected payments to reimburse the holder less any amounts that the Company expects to recover.

Notes to the financial statements *(continued)*

3 Significant accounting policies *(continued)*

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

(vii) Impairment *(continued)*

Policy applicable from 1 January 2018 *(continued)*

Measurement of ECL *(continued)*

- undrawn finance commitments: as the present value of the difference between the contractual cash flows that are due to the Company if the commitment is drawn down and the cash flows that the Company expects to receive; and
- financial guarantee contracts: the expected payments to reimburse the holder less any amounts that the Company expects to recover.

Restructured financial assets

If the terms of a financial asset are renegotiated or modified or an existing financial asset is replaced with a new one due to financial difficulties of the borrower, then an assessment is made of whether the financial asset should be derecognised and ECL are measured as follows.

- If the expected restructuring will not result in derecognition of the existing asset, then the expected cash flows arising from the modified financial asset are included in calculating the cash shortfalls from the existing asset. If the expected restructuring will result in derecognition of the existing asset, then the expected fair value of the new asset is treated as the final cash flow from the existing financial asset at the time of its derecognition.
- This amount is included in calculating the cash shortfalls from the existing financial asset that are discounted from the expected date of derecognition to the reporting date using the original effective profit rate of the existing financial asset.

Credit-impaired financial assets

At each reporting date, the Company assesses whether financial assets carried at amortised cost and debt financial assets carried at FVOCI, and finance lease receivables are credit‑impaired (referred to as 'Stage 3 financial assets'). A financial asset is 'credit‑impaired' when one or more events that have a detrimental impact on the estimated future cash flows of the financial asset have occurred. Evidence that a financial asset is credit-impaired includes the following observable data:

- significant financial difficulty of the borrower or issuer;
- a breach of contract such as a default or past due event;
- the restructuring of a Islamic financing facility by the Company on terms that the Company would not consider otherwise;
- it is becoming probable that the borrower will enter bankruptcy or other financial reorganisation; or
- the disappearance of an active market for a security because of financial difficulties.

A financing facility that has been renegotiated due to a deterioration in the borrower's condition is usually considered to be credit-impaired unless there is evidence that the risk of not receiving contractual cash flows has reduced significantly and there are no other indicators of impairment.

In making an assessment of whether an exposure to sovereign is credit-impaired, the Company considers the following factors.

- The market's assessment of creditworthiness as reflected in the sukuk yields.
- The rating agencies' assessments of creditworthiness.
- The country's ability to access the capital markets for new debt issuance.
- The probability of debt being restructured, resulting in holders suffering losses through voluntary or mandatory debt forgiveness.

Notes to the financial statements *(continued)*

3 Significant accounting policies *(continued)*

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

(vii) Impairment *(continued)*

Policy applicable from 1 January 2018 *(continued)*

Presentation of allowance for ECL in the statement of financial position

Loss allowances for ECL are presented in the statement of financial position as follows:

- financial assets measured at amortised cost: as a deduction from the gross carrying amount of the assets;
- finance facility commitments and financial guarantee contracts: generally, as a provision; where a financial instrument includes both a drawn and an undrawn component, and the Company cannot identify the ECL on the financing commitment component separately from those on the drawn component: the Company presents a combined loss allowance for both components. The combined amount is presented as a deduction from the gross carrying amount of the drawn component. Any excess of the loss allowance over the gross amount of the drawn component is presented as a provision; and
- debt instruments measured at FVOCI: no loss allowance is recognised in the statement of financial position because the carrying amount of these assets is their fair value. However, the loss allowance is disclosed and is recognised in the fair value reserve.

Write-off

Islamic financing facilities and debt securities are written off (either partially or in full) when there is no reasonable expectation of recovering a financial asset in its entirety or a portion thereof. This is generally the case when the Company determines that the borrower does not have assets or sources of income that could generate sufficient cash flows to repay the amounts subject to the write-off. This assessment is carried out at the individual asset level.

Recoveries of amounts previously written off are included in net impairment charge in the statement of profit or loss. Financial assets that are written off could still be subject to enforcement activities in order to comply with the Company's procedures for recovery of amounts due.

Central Bank of UAE ("CBUAE") provision requirements

As per the CBUAE notice no. CBUAE/BSD/2018/458 dated 30 April 2018, if the specific provision and general/collective provision cumulatively is higher than the impairment allowance computed under IFRS 9, the differential should be transferred to an "Impairment Reserve" as an appropriation from the Retained earnings. This Impairment Reserve should be split to that which relates to difference in specific provision and general/collective provision.

Since impairment allowance computed under IFRS 9 is higher than IAS 39, there is no requirement to create an impairment reserve.

Policy prior to 1 January 2018

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 facility or an advance by the Company on terms that the Company 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 company, or economic conditions that correlate with defaults in the Company. 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.

Notes to the financial statements *(continued)*

3 Significant accounting policies *(continued)*

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

(vii) Impairment *(continued)*

Policy prior to 1 January 2018 *(continued)*

The Company considers evidence of impairment for financing facilities 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 Company 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 profit rate. Impairment losses are recognised in the 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 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 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 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 Company in the management of its short-term commitments.

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

Notes to the financial statements *(continued)*

3 Significant accounting policies *(continued)*

(d) Due from banks and financial institutions

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

(e) Investments at fair value through profit or loss

These are securities that the Company acquire principally for the purpose of selling in the near term or holding as a part of portfolio that is managed together for short-term profit or position taking. These assets are initially recognised and subsequently measured at fair value in the statement of financial position. All changes in fair values are recognised as part of profit or loss.

(f) Islamic financing

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

Definitions

Ijara

Ijara consists of Ijara muntahia bitamleek. Ijara financing is an agreement whereby the Company's (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 Company's 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 Company sells to a customer commodities and other assets at an agreed upon profit mark up on cost. The Company 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.

Wakala

An agreement between the Company 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 Company 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.

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.

Notes to the financial statements *(continued)*

3 Significant accounting policies *(continued)*

(f) Islamic financing *(continued)*

Revenue recognition *(continued)*

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.

(g) Non-trading investments

Policy applicable from 1 January 2018

The 'non-trading investments' caption in the statement of financial position includes:

- debt investment securities measured at amortised cost; these are initially measured at fair value plus incremental direct transaction costs, and subsequently at their amortised cost using the effective profit method;
- debt securities measured at FVOCI; and
- equity investment securities designated as at FVOCI.

When a debt securities measured at FVOCI, gains and losses are recognised in OCI, except for the following, which are recognised in profit or loss in the same manner as for financial assets measured at amortised cost:

- proift revenue using the effective profit method;
- ECL and reversals; and
- foreign exchange gains and losses.

When debt security measured at FVOCI is derecognised, the cumulative gain or loss previously recognised in OCI is reclassified from equity to profit or loss.

The Company elects to present in OCI changes in the fair value of certain investments in equity instruments that are not held for trading. The election is made on an instrument-by-instrument basis on initial recognition and is irrevocable. Gains and losses on such equity instruments are never reclassified to profit or loss and no impairment is recognised in profit or loss. Dividends are recognised in profit or loss unless they clearly represent a recovery of part of the cost of the investment, in which case they are recognised in OCI. Cumulative gains and losses recognised in OCI are transferred to retained earnings on disposal of an investment.

Policy prior to 1 January 2018

Included in non-trading investments are FVOCI (both equity and debt) which are initially recognised at fair value plus incremental transaction costs directly attributable to the acquisition. Prior to 1 January 2018, non-trading investments includes 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 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 statement of profit or loss to the extent of the changes in fair value being hedged.

Notes to the financial statements *(continued)*

3 Significant accounting policies *(continued)*

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

Policy applicable prior to 1 January 2018 *(continued)*

Profit income is recognised on FVOCI debt securities using the effective profit 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 profit 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 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 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 Company has the positive intent and ability to hold them until maturity. These are initially recorded at fair value plus any directly attributable transaction costs, and are subsequently measured at amortised cost using the effective profit 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 Company 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:

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

(h) 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.

Notes to the financial statements *(continued)*

3 Significant accounting policies *(continued)*

(h) Property and equipment *(continued)*

(i) Recognition and measurement *(continued)*

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 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 Company. On-going expenses are charged to statement of profit or loss as incurred.

(ii) Depreciation

Depreciation is recognised in the 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.

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

During the year, the estimated useful lives of property and equipment was revised. The estimated useful lives of property and equipment for the current and comparative period are as follows:

	Estimated useful life as at 31 December 2017	Reassessed estimated useful life as at 31 December 2018
Office furniture and equipment	1 to 5 years	5 to 7 years
Fit-out leased premises	10 years	10 years
Safes	10 to 20 years	10 years
Computer systems and equipment	3 to 7 years	3 to 7 years
Vehicles	3 years	3 years

The revision of useful lives of property and equipment resulted in additional depreciation charge of AED 57 thousand.

(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 Company'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 Company's policies.

(iv) Impairment of non-financial assets

At each reporting date, the Company 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.

An impairment loss is recognised if the carrying amount of an asset or cash generation unit exceeds its recoverable amount.

Notes to the financial statements *(continued)*

3 Significant accounting policies *(continued)*

(h) Property and equipment *(continued)*

(iv) Impairment of non-financial assets

Impairment losses are recognised in profit or loss. 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 recognised.

(i) Profit income and expense

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

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 Company is the Rab Al Mal the losses are charged to the Company's income statement when incurred.

(j) 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 statement of profit or loss. The amounts are calculated in accordance with agreed terms and conditions of the wakala deposits and Sharia'a principles.

(k) Fee and commission income

The Company 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 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 profit rate of a financial instrument is recognised as an adjustment to the effective profit rate and recorded in "profit income".

A contract with a customer that results in a recognised financial instrument in the Company's financial statements may be partially in the scope of IFRS 9 and partially in the scope of IFRS 15. If this is the case, then the Company first applies IFRS 9 to separate and measure the part of the contract that is in the scope of IFRS 9 and then applies IFRS 15 to the residual.

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

(l) Zakat

Zakat is the responsibility of shareholders and is payable by them.

Notes to the financial statements *(continued)*

3 Significant accounting policies *(continued)*

(m) 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 designated at fair value.

Gains and losses arising from changes in fair value of FVOCI assets are recognised in the statement of other comprehensive income and recorded in fair value reserve with the exception of ECL, profit calculated using the effective profit rate method and foreign exchange gains and losses on monetary assets which are recognised directly in the 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 statement of profit or loss in case of debt instruments.

Non-trading investment includes FVOCI and amortised cost instruments.

(n) Derivative financial instruments and hedging

Derivatives are initially recognised, and subsequently measured at fair value with transaction costs taken directly to the 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 statement of profit or loss. When derivatives are designated as hedges, the Company 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

Policy applicable from 1 January 2018

Derivatives may be embedded in another contractual arrangement (a host contract). The Company accounts for an embedded derivative separately from the host contract when:

- the host contract is not an asset in the scope of IFRS 9;
- the host contract is not itself carried at FVTPL;
- the terms of the embedded derivative would meet the definition of a derivative if they were contained in a separate contract; and
- the economic characteristics and risks of the embedded derivative are not closely related to the economic characteristics and risks 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. Separated embedded derivatives are presented in the statement of financial position together with the host contract.

Notes to the financial statements *(continued)*

3 Significant accounting policies *(continued)*

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

Embedded derivatives *(continued)*

Policy applicable prior to 1 January 2018

Derivatives may be embedded in another contractual arrangement (a host contract). The Company 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 statement of financial position.

Hedge accounting

It is the Company'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 Company 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 Company 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.

(o) Foreign currency

Transactions in foreign currencies are translated into the respective functional currencies of the company 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 profit and payments during the period

Foreign currency differences arising on transaction are generally recognised in profit or loss. However, foreign currency differences arising from the transaction arising from the translation of the following item are recognised in OCI.

- available for sale equity instruments / FVOCI equity instruments
- qualifying cash flow hedges to the extent that the hedge is effective.

(p) Provisions

A provision is recognised if, as a result of a past event, the Company 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.

Notes to the financial statements *(continued)*

3 Significant accounting policies *(continued)*

(q) Employees' end of service benefit

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

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 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 Company 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 profit 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 profit) and the effect of the asset ceiling (if any, excluding profit), are recognised immediately in OCI. Net expenses related to defined benefit plans are recognised in Staff cost in 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 Company recognises gains and losses on the settlement of a defined benefit plan when the settlement occurs.

(r) Directors' remuneration

Pursuant to Article 118 of the Commercial Companies Law No. 2 of 2015 and in accordance with the Company'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.

Notes to the financial statements *(continued)*

3 Significant accounting policies *(continued)*

(s) New standards and interpretations not yet adopted

A number of new standards and amendments to standards are effective for annual periods beginning after 1 January 2018 and earlier application is permitted; however, the Company has not early adopted them in preparing these financial statements.

A. IFRS 16 Leases

The IASB issued a new standard for accounting for leases in January 2018.

a) The new standard does not significantly change the accounting for leases for lessors. However, it does require lessees to recognise most leases on their balance sheets as lease liabilities, with the corresponding right-of-use assets.
b) Lessees must apply a single model for all recognised leases, but will have the option not to recognise 'short-term' leases and leases of 'low-value' assets.
c) Generally, the profit or loss recognition pattern for recognised leases will be similar to today's finance lease accounting, with interest and depreciation expense recognised separately in the statement of profit or loss.

Early application is permitted provided the new revenue standard, IFRS 15, is applied on the same date.

The Company is still in the process of assessing the impact of above standard on the financial statements of the Company.

B. Other standards

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

- Annual Improvements to IFRS Standards 2015–2017 Cycle – various standards
- Plan Amendment, Curtailment or Settlement (Amendments to IAS 19)
- Amendments to References to Conceptual Framework in IFRS Standards

4 Transitional impact

The impact from the adoption of IFRS 9 as at 1 January 2018 on the retained earnings and fair value reserve is as follows:

	Retained earnings AED'000	Fair value reserve AED'000	Total AED'000
Balance as at 31 December 2017 under IAS 39	**283,951**	**(3,305)**	**280,646**
Impact on recognition of Expected Credit Losses			
On financial assets and unfunded exposures *(net of tax)*	**(8,310)**	**-**	**(8,310)**
Opening balance under IFRS 9 on date of initial application of 1 January 2018	**275,641**	**(3,305)**	**272,336**

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Notes to the financial statements *(continued)*

4 Transitional impact *(continued)*

The following tables reconciles the original measurement categories and carrying amounts in accordance with IAS 39 and the new measurement categories with those under IFRS 9 for the Company's financial assets and financial liabilities as at 1 January 2018

	IAS 39 classification	IFRS 9 classification	IAS 39 carrying amount AED'000	Reclassification to other category AED'000	Re-measurements AED'000	Impact of ECL AED'000	IFRS 9 carrying amount AED'000
Financial assets							
Cash and balances with bank	Loans and receivables	Amortised cost	30,426	-	-	-	30,426
Investments at fair value through profit or loss	FVTPL	FVTPL	106,606	-	-	-	106,606
Due from banks and financial institutions	Loans and receivables	Amortised cost	50,000	-	-	-	50,000
Islamic financing	Loans and receivables	Amortised cost	593,057	764	-	(8,286)	585,535
Non-trading investments	Available for sale - equity	FVOCI Equity	10,858	-	-	-	10,858
Other assets	Loans and receivables	Amortised cost	83,927	(764)	-	(7)	83,156
Total Financial Assets			874,874	-	-	(8,293)	866,581

	IAS 39 classification	IFRS 9 classification	IAS 39 carrying amount AED'000	Reclassification to other category AED'000	Re-measurements AED'000	Impact of ECL AED'000	IFRS 9 carrying amount AED'000
Financial liability							
Other liabilities[1]	Amortised cost	Amortised cost	26,234	-	-	(17)	26,217
Total Financial liabilities			26,234	-	-	(17)	26,217

[1] Includes ECL for unfunded exposures

Notes to the financial statements *(continued)*

5 Financial risk management

Introduction and overview

Risk management framework

The primary objective of the Company 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 Company gets exposed to multiple risks notably credit risk, market risk, liquidity and funding risk, profit 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 Company. 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") is responsible for the overall direction, supervision and control of the Company. The day-to-day management of the Company is conducted by the BOD committees, and the Chief Executive Officer ("CEO"). The BOD has overall responsibility for the Company 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.

Corporate Governance Framework

The Company has a comprehensive corporate governance framework that puts in place rules, processes and policies through which BOD and Senior Management manages the Company. The BOD drives the implementation of the corporate governance standards and in accordance with its charter had oversight responsibility for the Company's corporate governance framework. The Company's corporate governance standards bind its signatories to the highest standards of professionalism and due diligence in the performance of their duties. The Parent' Chief Risk Officer ("GCRO") is the custodian of the Corporate Framework document.

Risk Management Structure

The Parent BOD approves risk management plans for the Company. Under authority delegated by the BOD, the 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 Parent CRO functionally reports to this committee.

Board Level Committees within the Parent

Board Management Committee ("BMC")

BMC comprises three members of the BOD and the CEO. BMC oversees execution of the Parent's business plan as per the strategy approved by the Board and oversees and reviews material aspects of the business of the Parent. 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.

Board Risk and Compliance Committee ("BRCC")

The BRCC provides oversight and advice to the Parent Board in relation to current and potential future risk and compliance exposures of the FAB Group. It also considers and helps direct future risk strategy, including determination of risk appetite and tolerance as well as promote a risk and compliance awareness culture among 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 BRCC's charter.

Notes to the financial statements *(continued)*

5 Financial risk management *(continued)*

Risk management framework *(continued)*

Board Level Committees within the Parent *(continued)*

Board Audit Committee ("BAC")

BAC comprises three members of the BOD and the GCEO. BAC ensures oversight of the effectiveness of the internal control systems and the quality and integrity of financial statements and financial reporting. In addition, it reviews, approves and oversees the internal and external audit programs and ensures coordination between internal and external auditors. The Parent Chief Audit Officer ("GCAO") provides reports to the Committee on Internal controls. 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.

Management Level Committees within the Parent

Group Risk Committee ("GRC"):
Oversees the Group-wide risk strategy and exposures to enable integrated risk management in an effective manner. Defines, develops and periodically monitors the Parent's risk appetite along with its related methodology, parameters, targets, and tolerances taking into account the Bank's strategy and business planning. The GRC will report relevant matters to the Group EXCO, and as appropriate the BRCC, advising and informing them as required on the Parent's risk appetite and framework.

Group Compliance Committee ("GCC"):
Assists the Board Risk & Compliance Committee ("BRCC") in fulfilling its objective of overseeing the Bank's regulatory responsibilities as well as ensuring the Bank's compliance with the applicable laws and regulations issued by various regulatory authorities across the Group. The Committee also oversees that the relevant policies and procedures, including, but not limited to the Group Code of Ethics are complied with across the Group.

Group Operational Risk Committee ("GORC")
Assists the Parent's Risk Committee in fulfilling its objective of overseeing the Bank's operational risk management, business continuity and information security responsibilities. Responsibility areas of the GORC include identifying, measuring, managing, reporting of the Bank's operational risk profile, ratifying information security policy and procedures, integrated business continuity management policy and business recovery strategy of the Bank.

Information Security Committee ("ISC")

Assists the Board Risk and Compliance Committee and the Parent's Risk Committee in overseeing, reviewing and taking decisions on the implementation of FAB's security controls to ensure that information assets of the Bank are adequately protected. It also serves as an independent and objective governance forum which ensures the adequacy and effectiveness of the Bank's information security framework.

Parent Risk Management and Compliance Function

The Parent 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 and also includes the Parent's corporate governance function.

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.

Notes to the financial statements *(continued)*

5 Financial risk management *(continued)*

Risk Management Framework *(continued)*

Enterprise Risk Management Policy Framework *(continued)*

Core objective of ERMP is to provide a reasonable degree of assurance to the BOD that the risks threatening FAB's 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, profit 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 Parent 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 Parent's risk appetite and are in compliance with all relevant internal policies and processes. Parent Credit, Parent 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 Parent Chief Risk Officer ("GCRO") has a direct reporting line to the BRCC to ensure the independence of Parent 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 Parent's 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 Company to incur a financial loss. It arises principally from the Company's Islamic financing assets, cash and balances with banks, non-trading, due from banks and financial institutions, derivative financial instruments and certain other assets.

Management of credit risk

Credit risk identification and assessment at Company 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 Parent's Credit Unit that assesses the risk on a customer & facility level and ensures proper documentation of customer, facility and security documents along with Parent 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 Parent. 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.

Credit quality analysis

The following table sets out information about the credit quality of financial assets measured at amortised cost, FVOCI debt investments (2018) and available-for-sale debt assets (2017). Unless specifically indicated, for financial assets, the amounts in the table represent gross carrying amounts. For islamic financing commitments and financial guarantee contracts, the amounts in the table represent the amounts committed or guaranteed, respectively.

Notes to the financial statements *(continued)*

5 Financial risk management *(continued)*

(a) Credit risk *(continued)*

Credit quality analysis *(continued)*

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

As of 31 December 2018	Stage 1		Stage 2		Stage 3		Total	
	AED'000 Exposure	AED'000 Provision	AED'000 Exposure	AED'000 Provision	AED'000 Exposure	AED'000 Provision	AED'000 Exposure	AED'000 Provision
Cash and balances with bank	295,791	-	-	-	-	-	295,791	-
Investments at fair value through profit or loss	69,835	-	-	-	-	-	69,835	-
Due from banks and financial institutions	85,000	-	-	-	-	-	85,000	-
Islamic financing[1]	320,406	(973)	25,682	(4,641)	48,018	(32,213)	394,106	(37,827)
Non-trading investments	-	-	-	-	-	-	-	-
Other assets[2]	91,658	(17)	-	-	-	-	91,658	(17)
Unfunded exposure	-	-	-	-	-	-	-	-
	862,690	(990)	25,682	(4,641)	48,018	(32,213)	936,390	(37,844)

[1]The exposure represents gross islamic financing facilities.
[2]On certain assets included as part of other assets, ECL is computed based on simplified approach and reported as part of stage 1.

Notes to the financial statements *(continued)*

5 Financial risk management *(continued)*

(a) Credit risk *(continued)*

Credit quality analysis *(continued)*

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

Opening balance as at 1 January 2018	Stage 1		Stage 2		Stage 3		Total	
	AED'000 Exposure	AED'000 Provision	AED'000 Exposure	AED'000 Provision	AED'000 Exposure	AED'000 Provision	AED'000 Exposure	AED'000 Provision
Cash and balances with bank	30,426	-	-	-	-	-	30,426	-
Investments at fair value through profit or loss	106,606	-	-	-	-	-	106,606	-
Due from banks and financial institutions	50,000	-	-	-	-	-	50,000	-
Islamic financing[1]	540,100	(2,828)	25,153	(3,996)	95,153	(68,811)	660,406	(75,635)
Non-trading investments	10,858	-	-	-	-	-	10,858	-
Other assets[2]	83,927	(7)	-	-	-	-	83,927	(7)
Unfunded exposure	3,600	(17)	-	-	-	-	3,600	(17)
	825,517	(2,852)	25,153	(3,996)	95,153	(68,811)	945,823	(75,659)

[1]The exposure represents gross finances and advances.
[2]On certain assets included as part of other assets, ECL is computed based on simplified approach and reported as part of stage 1.

Notes to the financial statements *(continued)*

5 Financial risk management *(continued)*

(a) Credit risk *(continued)*

Credit quality analysis *(continued)*

Classification of investments as per their external ratings:

	Non-trading investments		Investments at fair value through profit or loss	
	2018 AED'000	2017 AED'000	**2018 AED'000**	2017 AED'000
AAA	**-**	-	**-**	-
AA to A	**-**	-	**33,747**	68,669
BBB to B	**-**	-	**-**	-
CCC and below	**-**	-	**-**	-
Unrated	**-**	10,858	**36,088**	37,937
	-	10,858	**69,835**	106,606

Investments at fair value through profit or loss are neither past due nor impaired.

Collateral held and other credit enhancements

The Company 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 collaterals. The Company ensures that all documentation used in collateralized transactions and for documenting on and off-balance sheet netting and collateral is binding on all parties and is legally enforceable in all relevant jurisdictions.

The Company 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 Company may also close out transactions or assign them to other counterparties to mitigate credit risk.

An estimate of the carrying value of collateral and other security enhancements held against Islamic financing are shown below:

	2018 AED'000	2017 AED'000
Collateral value cover		
Unsecured facilities	**226,808**	466,533
0 – 50%	**-**	-
50 – 100%	**31,039**	37,032
Above 100%	**141,582**	163,618
Total Gross islamic financing	**399,429**	667,183

During the year 2018 and 2017, the Company did not repossess collateral that was held as security against Islamic financing.

Notes to the financial statements *(continued)*

5 Financial risk management *(continued)*

Risk Management Framework *(continued)*

(a) Credit risk *(continued)*

Amounts arising from ECL

Inputs, assumptions and techniques used for estimating impairment

See accounting policy 3(b)(vii).

Significant increase in credit risk

When determining whether the risk of default on a financial instrument has increased significantly since initial recognition, the Company considers reasonable and supportable information that is relevant and available without undue cost or effort. This includes both quantitative and qualitative information and analysis, based on the Company's historical experience and expert credit assessment and including forward-looking information.

The objective of the assessment is to identify whether a significant increase in credit risk has occurred for an exposure by comparing:

- the remaining lifetime probability of default (PD) as at the reporting date; with
- the remaining lifetime PD for this point in time that was estimated at the time of initial recognition of the exposure (adjusted where relevant for changes in prepayment expectations).

For retail portfolio historical payment behavior of the exposure is evaluated to determine significant increase in credit risk.

In addition to the quantitative test based on movement of PD, the Company also applies experienced credit judgment to incorporate the estimated impact of factors not captured in the modelled ECL results.

Credit risk grades

The Company allocates each corporate exposure to a credit risk grade based on a variety of data that is determined to be predictive of the risk of default and applying experienced credit judgment. Credit risk grades are defined using qualitative and quantitative factors that are indicative of risk of default. These factors vary depending on the nature of the exposure and the type of borrower.

Credit risk grades are defined and calibrated such that the risk of default occurring increases exponentially as the credit risk deteriorates so, for example, the difference in risk of default between credit risk grades 1 and 2 is smaller than the difference between credit risk grades 2 and 3.

Each exposure is allocated to a credit risk grade on initial recognition based on available information about the borrower. Exposures are subject to ongoing monitoring, which may result in an exposure being moved to a different credit risk grade.

Notes to the financial statements *(continued)*

5 Financial risk management *(continued)*

Risk management framework *(continued)*

(a) Credit risk *(continued)*

Amounts arising from ECL *(continued)*

Determining whether credit risk has increased significantly

The Company assesses whether credit risk has increased significantly since initial recognition at each reporting date. Determining whether an increase in credit risk is significant depends on the characteristics of the financial instrument and the borrower, and the geographical region. What is considered significant differs for different types of lending, in particular between corporate and retail.

The credit risk may also be deemed to have increased significantly since initial recognition based on qualitative factors linked to the Company's credit risk management processes that may not otherwise be fully reflected in its quantitative analysis on a timely basis. This will be the case for exposures that meet certain heightened risk criteria, such as placement on a watch list. Such qualitative factors are based on expert judgment and relevant historical experiences.

If there is evidence that there is no longer a significant increase in credit risk relative to initial recognition, then the loss allowance on an instrument returns to being measured as 12-month ECL. Some qualitative indicators of an increase in credit risk, such as delinquency or forbearance, may be indicative of an increased risk of default that persists after the indicator itself has ceased to exist. In these cases, the Company determines a probation period during which the financial asset is required to demonstrate good behaviour to provide evidence that its credit risk has declined sufficiently. When contractual terms of a financing facility have been modified, evidence that the criteria for recognising lifetime ECL are no longer met includes a history of up-to-date payment performance against the modified contractual terms.

Definition of default

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

- The borrower is unlikely to pay its credit obligations to the Company in full, without recourse by the Company to actions such as realising security (if any is held);
- For retail, a facility or any material credit obligation to the Company is more than 90 days past due;

Inputs into the assessment of whether a financial instrument is in default and their significance may vary over time to reflect changes in circumstances.

Notes to the financial statements *(continued)*

5 Financial risk management *(continued)*

Risk management framework *(continued)*

(a) Credit risk *(continued)*

Amounts arising from ECL *(continued)*

Incorporation of forward-looking information

The Company incorporates forward-looking information into both the assessment of whether the credit risk of an instrument has increased significantly since its initial recognition and the measurement of ECL.

The Company formulates three economic scenarios: a base case, which is the median scenario assigned a 40% probability of occurring, and two less likely scenarios, one upside and one downside, each assigned a 30% probability of occurring. External information considered includes economic data and forecasts published by governmental bodies and monetary authorities.

The Company has identified and documented key drivers of credit risk and credit losses for each portfolio of financial instruments and, using an analysis of historical data, has estimated relationships between macro-economic variables and credit risk and credit losses.

The economic scenarios used as at 31 December 2018 included the following key indicators for the years ending 31 December 2019 to 2023.

Region	Macro Variable[1,2]	Scenario	2019	2020	2021	2022	2023
Gulf	Oil Price	Base	-2.16%	-7.01%	-2.74%	0.88%	1.23%
		Upside	20.34%	-2.20%	-3.88%	-1.03%	-0.41%
		Downside	-28.69%	-12.55%	4.47%	10.23%	6.98%
	UAE Equity Index	Base	22.77%	8.80%	6.80%	6.55%	7.56%
		Upside	28.97%	10.47%	15.35%	8.85%	8.48%
		Downside	6.58%	13.33%	1.52%	1.27%	3.75%

(1) Represents the average annualized increase / decrease over the period.
(2) There are additional macro variables factors used of other regions relevant to their market.

Modified financial assets

The contractual terms of a islamic financing facility may be modified for a number of reasons, including changing market conditions, customer retention and other factors not related to a current or potential credit deterioration of the customer. An existing facility whose terms have been modified may be derecognised and the renegotiated finances recognised as a new financing facility at fair value in accordance with the accounting policy set out in Note 3(b)(iv).

When the terms of a financial asset are modified and the modification does not result in derecognition, the determination of whether the asset's credit risk has increased significantly reflects comparison of:

- its remaining lifetime PD at the reporting date based on the modified terms; with
- the remaining lifetime PD estimated based on data on initial recognition and the original contractual terms.

The Company renegotiates financing facilities to customers in financial difficulties (referred to as 'forbearance activities') to maximise collection opportunities and minimise the risk of default. Under the Company's forbearance policy, finance forbearance is granted on a selective basis if the debtor is currently in default on its debt or if there is a high risk of default, there is evidence that the debtor made all reasonable efforts to pay under the original contractual terms and the debtor is expected to be able to meet the revised terms.

Notes to the financial statements *(continued)*

5 Financial risk management *(continued)*

Risk management framework *(continued)*

(a) Credit risk *(continued)*

Modified financial assets *(continued)*

The revised terms usually include extending the maturity, changing the timing of profit payments and amending the terms of facility covenants. Both retail and corporate facilities are subject to the forbearance policy. The Company Credit Committee regularly reviews reports on forbearance activities. For financial assets modified as part of the Company's forbearance policy, the estimate of PD reflects whether the modification has improved or restored the Company's ability to collect profit and principal and the Company's previous experience of similar forbearance action.

As part of this process, the Company evaluates the borrower's payment performance against the modified contractual terms and considers various behavioral indicators. Generally, forbearance is a qualitative indicator of a significant increase in credit risk and an expectation of forbearance may constitute evidence that an exposure is credit-impaired (see Note 3(b) (vii)). A customer needs to demonstrate consistently good payment behaviour over a period of time before the exposure is no longer considered to be credit-impaired/in default or the PD is considered to have decreased such that the loss allowance reverts to being measured at an amount equal to Stage 1.

Measurement of ECL

The key inputs into the measurement of ECL are the term structure of the following variables:

- probability of default (PD);
- loss given default (LGD); and
- exposure at default (EAD).

ECL for exposures in Stage 1 is calculated by multiplying the 12-month PD by LGD and EAD. Lifetime ECL is calculated by multiplying the lifetime PD by LGD and EAD. The Lifetime PDs are determined based on maturity profile. The maturity profile looks at how defaults develop on a portfolio throughout the remaining life of the facility. The maturity profile is based on historical observed data .LGD is the magnitude of the likely loss if there is a default. The Company estimates LGD parameters based on the history of recovery rates of claims against defaulted counterparties.

The LGD models consider the structure, collateral, seniority of the claim, counterparty industry and recovery costs of any collateral that is integral to the financial asset. For financing facility secured by retail property, LTV ratios are a key parameter in determining LGD. LGD estimates are recalibrated for different economic scenarios and, for real estate lending, to reflect possible changes in property prices. They are calculated on a discounted cash flow basis using the effective profit rate as the discounting factor.

EAD represents the expected exposure in the event of a default. The Company derives the EAD from the current exposure to the counterparty and potential changes to the current amount allowed under the contract and arising from amortisation. The EAD of a financial asset is its gross carrying amount at the time of default. For lending commitments, the EADs are potential future amounts that may be drawn under the contract, which are estimated based on historical observations and forward-looking forecasts. For financial guarantees, the EAD represents the amount of the guaranteed exposure when the financial guarantee becomes payable. For some financial assets, EAD is determined by modelling the range of possible exposure outcomes at various points in time using scenario and statistical techniques.

Notes to the financial statements *(continued)*

5 Financial risk management *(continued)*

Risk management framework *(continued)*

(a) Credit risk *(continued)*

Amounts arising from ECL *(continued)*

Measurement of ECL *(continued)*

As described above, and subject to using a maximum of a 12-month PD for Stage 1 financial assets, the Company measures ECL considering the risk of default over the maximum contractual period (including any borrower's extension options) over which it is exposed to credit risk, even if, for credit risk management purposes, the Company considers a longer period. The maximum contractual period extends to the date at which the Company has the right to require repayment of an advance or terminate a facility commitment.

However, for facilities that include both Finances and an undrawn commitment component, the Company measures ECL over a period longer than the maximum contractual period if the Company's contractual ability to demand repayment and cancel the undrawn commitment does not limit the Company's exposure to credit losses to the contractual notice period. These facilities do not have a fixed term or repayment structure and are managed on a collective basis. The Company can cancel them with immediate effect but this contractual right is not enforced in the normal day-to-day management, but only when the Company becomes aware of an increase in credit risk at the facility level. This longer period is estimated taking into account the credit risk management actions that the Company expects to take, and that serve to mitigate ECL. These include a reduction in limits, cancellation of the facility and/or turning the outstanding balance into a facility with fixed repayment terms.

Where modelling of a parameter is carried out on a collective basis, the financial instruments are grouped on the basis of shared risk characteristics that include:

- instrument type;
- collateral type;
- LTV ratio for retail mortgages;
- date of initial recognition;
- remaining term to maturity;
- industry; and
- geographic location of the borrower.

Notes to the financial statements *(continued)*

5 Financial risk management *(continued)*

Risk management framework *(continued)*

(a) Credit risk *(continued)*

Amounts arising from ECL *(continued)*

Loss allowance

The following tables show reconciliations from the opening to the closing balance of the loss allowance. Comparative amounts for 2017 represent the allowance account for credit losses and reflect the measurement basis under IAS 39.

	Stage 1 AED'000	Stage 2 AED'000	Stage 3 AED'000	2018 Total AED'000	2017 AED'000
Beginning of the period	9,088	-	58,261	**67,349**	83,029
Impact due to IFRS 9 adoption	(6,236)	3,996	10,550	**8,310**	-
	2,852	3,996	68,811	**75,659**	83,029
Transfer from Stage 1 to Stage 2	(47)	47	-	-	-
Transfer from Stage 1 to Stage 3	(83)	-	83	-	-
Transfer from Stage 2 to Stage 1	84	(84)	-	-	-
Transfer from Stage 2 to Stage 3	-	(254)	254	-	-
Transfer from Stage 3 to Stage 1	1,235	-	(1,235)	-	-
Transfer from Stage 3 to Stage 2	-	5,461	(5,461)	-	-
	1,189	5,170	(6,359)	-	-
Impact of change in provision	(3,051)	(4,525)	111	**(7,465)**	13,738
Write-offs and other adjustments	-	-	(30,350)	**(30,350)**	(29,418)
	990	4,641	32,213	**37,844**	67,349

Notes to the financial statements *(continued)*

5 Financial risk management *(continued)*

(a) Credit risk *(continued)*

The Company 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:

Concentrations by industry sector

	Islamic financing		**Investments at fair value through profit or loss**		**Fair Value through other comprehensive income**		**Undrawn Commitments**	
	2018 AED'000	2017 AED'000	**2018 AED'000**	2017 AED'000	**2018 AED'000**	2017 AED'000	**2018 AED'000**	2017 AED'000
Real estate	**-**	-	**33,747**	34,949	**-**	-	**-**	-
Trading	**395**	464						
Banks	**-**	-	**-**	33,720	**-**	-	**-**	-
Other financial institutions	**-**	-	**-**	-	**-**	10,858	**-**	-
Government	**-**	-	**36,088**	37,937	**-**	-	**-**	-
Personal – Islamic financing	**257,452**	503,101	**-**	-	**-**	-	**-**	3,600
Personal Islamic financing for business and others	**141,582**	163,618	**-**	-	**-**	-	**-**	-
	399,429	667,183	**69,835**	106,606	**-**	10,858	**-**	3,600

The above numbers are presented on a gross basis and are not adjusted for provisions or profit in suspense if any.

Notes to the financial statements *(continued)*

5 Financial risk management *(continued)*

(a) Credit risk *(continued)*

Classification of investments as per their counterparties:

	Non-trading investments		Investments at fair value through profit or loss	
	2018 AED'000	2017 AED'000	**2018 AED'000**	2017 AED'000
Government sector	**-**	-	**36,088**	37,937
Supranational	**-**	-	**-**	-
Public Sector	**-**	-	**-**	-
Banking sector	**-**	-	**-**	33,720
Corporate / private sector	**-**	10,858	**33,747**	34,949
	-	10,858	**69,835**	106,606

Settlement risk

The Company 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 Company. 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 Company's derivative contracts are entered into with the Parent.

(b) Liquidity risk

Liquidity risk is defined as the risk that the Company 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. Company 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 Company has defined the liquidity risk appetite at a level so as to ensure that the Company 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 Company 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 company's external credit rating objectives.

Notes to the financial statements *(continued)*

5 Financial risk management *(continued)*

(b) Liquidity risk *(continued)*

Liquidity limits are defined at the Parent level and are cascaded down throughout the organization to ensure that the Company complies with the defined Parent's Liquidity Risk appetite.

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

Exposure to liquidity risk

Details of the Company's assets and liabilities is summarized in the table below by the maturity profile of the Company's assets and liabilities based on the contractual repayment arrangements and does not take account of the effective maturities as indicated by the Company's deposit retention history. The contractual maturities of assets and liabilities have been determined on the basis of the remaining period at the reporting date to the contractual maturity date. The maturity profile is monitored by management to ensure adequate liquidity is maintained.

Exposure to liquidity risk

The contractual asset and liability maturity mismatch report without considering the Company's retention history is detailed below.

Notes to the financial statements *(continued)*

5 Financial risk management *(continued)*

(b) Liquidity risk *(continued)*

The maturity profile of the assets and liabilities as at 31 December 2018;

	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 bank	295,791	-	-	-	-	-	295,791
Investments at fair value through profit or loss	69,835	-	-	-	69,835	-	-
Due from banks and financial institutions	85,000	-	85,000	-	-	-	-
Islamic financing	356,279	15,859	20,484	66,903	46,701	206,332	-
Property and equipment	2,442	-	-	-	-	-	2,442
Other assets	91,641	89,542	1,694	405	-	-	-
	900,988	105,401	107,178	67,308	116,536	206,332	298,233
Liabilities and equity							
Other liabilities	27,367	17,036	1,609	1,014	-	-	7,708
Equity	873,621	-	-	-	-	-	873,621
	900,988	17,036	1,609	1,014	-	-	881,329
Undrawn commitments to extend credit	-	-	-	-	-	-	-

Notes to the financial statements *(continued)*

5 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 bank	30,426	30,426	-	-	-	-	-
Investments at fair value through profit or loss	106,606	-	33,720	-	72,886	-	-
Due from banks and financial institutions	50,000	-	50,000	-	-	-	-
Islamic financing	593,057	23,632	144,111	198,375	79,419	147,520	-
Non-trading investments	10,858	-	-	-	-	-	10,858
Property and equipment	2,994	-	-	-	-	-	2,994
Other assets	83,927	1,485	82,442	-	-	-	-
	877,868	55,543	310,273	198,375	152,305	147,520	13,852
Liabilities and equity							
Other liabilities	26,234	18,000	-	-	-	-	8,234
Equity	851,634	-	-	-	-	-	851,634
	877,868	18,000	-	-	-	-	859,868
Undrawn commitments to extend credit	3,600	-	-	-	1,050	2,550	-

Notes to the financial statements *(continued)*

5 Financial risk management *(continued)*

(b) Liquidity risk *(continued)*

The table below summarizes the maturity profile of the Company'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 2018							
Due to banks and financial institutions	-	-	-	-	-	-	-
Customers' deposits	-	-	-	-	-	-	-
	-	-	-	-	-	-	-
Undrawn finance commitments to extend credit[1]	-	-	-	-	-	-	-
As at 31 December 2017							
Due to banks and financial institutions	-	-	-	-	-	-	-
Customers' deposits	-	-	-	-	-	-	-
	-	-	-	-	-	-	-
Undrawn finance commitments to extend credit[1]	3,600	-	-	-	-	1,050	2,550

[1]Calculated as per the contractual maturity profile.

Notes to the financial statements *(continued)*

5 Financial risk management *(continued)*

(c) Market risk

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

Management of market risk

The Company has set risk limits based on sensitivities and other risk parameters which are closely monitored by the Risk Management Division of the Parent and reported regularly to Senior Management and discussed by the Assets and Liabilities Committee.

Profit rate risk

Profit rate risk arises from profit bearing financial instruments and reflects the possibility that changes in profit rates will adversely affect the value of the financial instruments and the related income. The Company manages this risk principally through monitoring profit rate gaps and by matching the re-pricing profile of assets and liabilities.

The substantial portion of the Company's assets and liabilities are re-priced within one year. The Company considers market profit rates and future trends prior to offering fixed price Islamic financing.

The effective profit rate is the rate that exactly discounts the estimated future cash flows through the expected life of the financial asset or liability to the carrying amount of the financial asset or liability. The rate is an original effective profit rate for a fixed rate instrument carried at amortised cost and a current market rate for a floating instrument or an instrument carried at fair value.

Profit rate risk is also assessed by measuring the impact of reasonable possible change in profit rate movements. The Company assumes a fluctuation in profit rates of 50 basis points (2017: 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	
	2018	2017
	AED'000	AED'000
Fluctuation in yield	**633**	1,121

The profit rate sensitivities set out above are illustrative only and employ simplified scenarios. They are based on AED 213,728 thousand *(2017: AED 418,769 thousand)* profit bearing assets and AED Nil *(2017: AED 4,883 thousand)* profit bearing liabilities with profit 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 profit rate sensitivity on the fair value through other comprehensive income portfolio. The sensitivity does not incorporate actions that could be taken by management to mitigate the effect of profit rate movements.

Notes to the financial statements *(continued)*

5 Financial risk management *(continued)*

(c) Market risk *(continued)*

The Company's profit rate gap and sensitivity position based on contractual re-pricing arrangements at 31 December 2018 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-profit bearing AED'000
Assets							
Cash and balances with banks	295,791	-	-	-	-	-	295,791
Investments at fair value through profit or loss	69,835	-	-	-	69,835	-	-
Due from banks and financial institutions	85,000		85,000	-	-	-	-
Islamic financing	356,279	53,050	75,678	33,066	95,268	99,217	-
Property and equipment	2,442	-	-	-	-	-	2,442
Other assets	91,641	-	-	-	-	-	91,641
	900,988	53,050	160,678	33,066	165,103	99,217	389,874
Liabilities and equity							
Other liabilities	27,367	-	-	-	-	-	27,367
Equity	873,621	-	-	-	-	-	873,621
	900,988	-	-	-	-	-	900,988
On statement of financial position gap		53,050	160,678	33,066	165,103	99,217	(511,114)
Cumulative profit rate sensitivity		53,050	213,728	246,794	411,897	511,114	-

Notes to the financial statements *(continued)*

5 Financial risk management *(continued)*

(c) Market risk *(continued)*

The Company's profit 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-profit bearing AED'000
Assets							
Cash and balances with banks	30,426	-	-	-	-	-	30,426
Investments at fair value through profit or loss	106,606	-	33,720	72,886	-	-	-
Due from banks and financial institutions	50,000	-	50,000	-	-	-	-
Islamic financing	593,057	114,307	192,628	208,995	-	77,127	-
Non-trading investments	10,858	-	-	-	-	-	10,858
Property and equipment	2,994	-	-	-	-	-	2,994
Other assets	83,927	-	-	-	-	-	83,927
	877,868	114,307	276,348	281,881	-	77,127	128,205
Liabilities and equity							
Other liabilities	26,234	-	-	-	-	-	26,234
Equity	851,634	-	-	-	-	-	851,634
	877,868	-	-	-	-	-	877,868
On statement of financial position gap		114,307	276,348	281,881	-	77,127	(749,663)
Cumulative profit rate sensitivity		114,307	390,655	672,536	672,536	749,663	-

Notes to the financial statements *(continued)*

5 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 Company's functional currency is the UAE Dirham. The Parent 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 Company had the following significant net exposures denominated in foreign currencies:

	Total 2018 (short)/long AED'000	Total 2017 (short)/long AED'000
Currency		
US Dollar	**69,835**	106,606

As AED is pegged against US Dollar, the Company's risk exposure to this currency is limited to that extent. Exposure to other foreign currencies is insignificant.

Notes to the financial statements *(continued)*

5 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 Company. The primary responsibility to ensure that risks are managed and monitored resides with the businesses within the Company. Company's business are supported by embedded risk functions and Parent operational Risk Management as 'second line of defense' to ensure robust risk management.

Further, there are reviews conducted by Parent 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 Audit Committee.

The Company 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 Company;
- Damage to physical assets: Risk of impact to the Company 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 Company. These responsibilities are delegated and exercised through the Parent Risk & Compliance Committee, which is the senior management forum responsible for the oversight of Operational Risk.

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

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

Notes to the financial statements *(continued)*

5 Financial risk management *(continued)*

(e) Capital management

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

The Company's objectives when managing capital are:

• safeguard the Company's ability to continue as a going concern and increase the returns for the shareholders, and
• comply with regulatory capital requirements set by the Central Bank of the UAE.

(f) Strategic risk

Strategic risk refers to the risk of current or prospective impact on the Company's earnings, capital, reputation or standing arising from changes in the environment the Company 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 Company's strategic goals, strategies developed to achieve those goals, resources deployed to meet those goals and the quality of implementation.

The Company 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 Company.

Strategic risks are monitored and controlled as part of the strategic planning process wherein the Company 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.

(g) 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 Company, 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 Parent's Risk Management function has a company-wide compliance unit that develops internal controls to manage such risks and it is supported by the Parent's Internal Audit and Legal functions.

In order to monitor compliance and anti-money laundering risks, the Company has set in place the due diligence processes, reviews of policies and procedures across the Company, 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.

Notes to the financial statements *(continued)*

5 Financial risk management *(continued)*

(h) 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 Company 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 Company also refers to other relevant information for risk identification purposes. Such information may be sourced from media reports, stakeholder analysis reports, Parent's 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 Company 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 Company 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.

6 Use of estimates and judgements

In the process of applying the Company's accounting policies, IFRS require the management to select suitable accounting policies, apply them consistently and make judgments 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 judgments. Listed below are those estimates and judgment which could have the most significant effect on the amounts recognised in the financial statements.

Key sources of estimation uncertainty

(a) Going concern

The Company's management has made an assessment of the Company's ability to continue as a going concern and is satisfied that the Company 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 Company's ability to continue as a going concern. Therefore, the financial statements continue to be prepared on the going concern basis.

(b) Impairment charge on financing facilities and non-trading investments

Applicable from 1 January 2018

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

The measurement of impairment losses both under IFRS 9 and IAS 39 across all categories of financial assets requires judgment, in particular, the estimation of the amount and timing of future cash flows and collateral values when determining impairment losses and the assessment of a significant increase in credit risk. These estimates are driven by a number of factors, changes in which can result in different levels of allowances.

The Company's ECL calculations are outputs of complex models with a number of underlying assumptions regarding the choice of variable inputs and their interdependencies. Elements of the ECL models that are considered accounting judgments and estimates include:

Notes to the financial statements *(continued)*

6 Use of estimates and judgments *(continued)*

(b) Impairment charge on financial assets *(continued)*

Applicable from 1 January 2018 *(continued)*

- The Company's internal credit grading model, which assigns PDs to the individual grades
- The Company's criteria for assessing if there has been a significant increase in credit risk and so allowances for financial assets should be measured on a lifetime ECL basis and the qualitative assessment
- The segmentation of financial assets when their ECL is assessed on a collective basis
- Development of ECL models, including the various formulas and the choice of inputs
  Determination of associations between macroeconomic scenarios and, economic inputs, such as unemployment levels and collateral values, and the effect on PDs, EADs and LGDs
- Selection of forward-looking macroeconomic scenarios and their probability weightings, to derive the economic inputs into the ECL models

Prior to 1 January 2018

The Company evaluates impairment on financing facilities 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 statement of profit or loss. In particular, considerable judgment 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 judgments 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 judgment and uncertainty, and actual results may differ resulting in future changes to such impairment charges.

It is the Company's policy to regularly review its models in the context of actual loss experience and adjust when necessary.

(c) Collective impairment charge

Prior to 1 January 2018

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

In addition to specific impairment charge against individually impaired assets, the Company also maintains a collective impairment allowance against portfolios of financing facilities 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 note 3(l)(iv).

In determining the net realisable value, the Company 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.

Notes to the financial statements *(continued)*

6 Use of estimates and judgments *(continued)*

(e) Contingent liability arising from litigations

Due to the nature of its operations, the Company 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) 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 7.

(g) 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 Company determines the appropriate discount rate at the end of each year. This is the profit 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 company considers profit 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 15.

(h) Financial asset and liability classification

The Company'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 Company has determined it meets the description as set out in policy 3(b) (ii).

(i) Qualifying hedge relationships

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

(j) Determination of fair value hierarchy of financial instruments

The Company's determination of fair value hierarchy of financial instruments is discussed in note 7.

Notes to the financial statements *(continued)*

7 Financial assets and liabilities

(a) Valuation control framework

The Company has an established control framework with respect to the measurement of fair value. This framework includes a Valuation Committee that reports to the Parent Risk Committee. The parent also has control functions to support this framework (Product Control, Independent Price Verification, Model Validation and Parent's 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, due to banks and financial institutions 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 Company estimates that the fair value of its islamic financing portfolio is not materially different from its carrying value since the majority of financing facilities carry floating market rates of profit and are frequently re-priced.

(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 Company 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 Company 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 Company 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 (Prior to 1 January 2019) 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.

7 Financial assets and liabilities *(continued)*

(c) Valuation techniques *(continued)*

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 Company 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 profit 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 Company uses widely recognised valuation models for determining the fair value of common financial instruments, such as profit 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 profit rate swaps. Availability of observable market prices and model inputs reduces the need for management judgment 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 Company uses third party valuation models, which are developed from recognised valuation models. These valuation models require expert judgment 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 financial statements *(continued)*

7 Financial assets and liabilities *(continued)*

(c) Fair value of financial instruments

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

	Designated at fair value through profit or loss AED'000	Amortised cost AED'000
Financial Assets		
Cash and balances with banks	-	295,791
Investments at fair value through profit or loss	69,835	-
Due from banks and financial institutions	-	85,000
Loans and receivables	-	356,279
Other assets	566	91,075
	70,401	828,145
Financial Liabilities		
Other liabilities[1]	2,842	24,525
	2,842	24,525

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

7 Financial assets and liabilities *(continued)*

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

The table below sets out the Company'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	Available for sale AED'000	Loans and Receivables AED'000	Other Amortised cost AED'000
Financial Assets				
Cash and balances with central banks	-	-	-	30,426
Investments at fair value through profit or loss	106,606	-	-	-
Due from banks and financial institutions	-	-	-	50,000
Loans and receivables	-	-	593,057	-
Non-trading investments	-	10,858	-	-
Other assets	573	-	-	83,354
	107,179	10,858	593,057	163,780
Financial Liabilities				
Other liabilities[1]	4,883	-	-	21,351
	4,883	-	-	21,351

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

Notes to the financial statements *(continued)*

7 Financial assets and liabilities *(continued)*

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

The Company's financial assets and financial liabilities that are classified as financing facilities 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 Company considers these to have a fair value approximately equivalent to their net carrying value as the majority of such financial instrument carries variable profit 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 2018				
Investments designated at fair value through profit and loss	**69,835**	**-**	**-**	**69,835**
	69,835	**-**	**-**	**69,835**
As at 31 December 2017				
Non-trading investments	10,858	-	-	10,858
Investments designated at fair value through profit and loss	106,606	-	-	106,606
	117,464	-	-	117,464

Financial assets also consist of cash and balances with banks, due from banks and financial institutions, Islamic financing and receivables carried at amortised costs. Financial liabilities consist of payables carried at amortised cost.

The fair value of these financial instruments are not materially different from their carrying value. These are classified under Level 3 of the fair value hierarchy.

Notes to the financial statements *(continued)*

8 Cash and balances with bank

	2018 AED'000	2017 AED'000
Current account	**295,791**	30,426
Less: **expected credit losses**	**-**	-
	295,791	30,426

9 Investments at fair value through profit or loss

	2018 AED'000	2017 AED'000
Investments in Sukuk	**69,835**	106,606
	69,835	106,606

10 Due from banks and financial institutions

	2018 AED'000	2017 AED'000
Wakala placements	**85,000**	50,000
	85,000	50,000

Notes to the financial statements *(continued)*

11 Islamic financing

	2018 **AED'000**	2017 AED'000
Murabaha financing	**257,847**	503,565
Ijara financing	**141,582**	163,618
Less: profit suspended	**(5,323)**	(6,777)
***Less:* expected credit losses**	**(37,827)**	(67,349)
Net Islamic financing	**356,279**	593,057

	2018 **AED'000**	2017 AED'000
By counterparty:		
Corporate / private sector	**394**	464
Personal / retail sector	**399,035**	666,719
Gross Islamic financing	**399,429**	667,183

	2018 **AED'000**	2017 AED'000
By product:		
Real estate	**141,582**	163,618
Personal financing	**130,743**	337,812
Vehicle financing	**31,039**	37,040
Others	**96,065**	128,713
Gross Islamic financing	**399,429**	667,183

The movement in the allowance for expected credit losses for Islamic financing facilities during the year is shown below:

	2018 **AED'000**	2017 AED'000
Beginning of the year	**67,349**	83,029
Initial application of IFRS 9	**8,286**	-
Net provision charge for the year	**(7,458)**	13,738
Amounts written off and other adjustments	**(30,350)**	(29,418)
As of 31 December 2018	**37,827**	67,349

Notes to the financial statements *(continued)*

12 Non-trading Investments

	2018 AED'000	2017 AED'000
Available-for-sale investments	-	10,858
Less: **expected credit losses**	-	-
	-	10,858

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

	2018 AED'000			2017 AED'000		
	Quoted	**Unquoted**	**Total**	Quoted	Unquoted	Total
Equity investments	-	-	-	10,858	-	10,858
	-	-	-	10,858	-	10,858

During the year, investments at fair value through other comprehensive income were sold off for AED 16,486 thousand with a realized gain of AED1, 851 thousand realized in other comprehensive income.

Notes to the financial statements *(continued)*

13 Property and equipment

	Alteration to premises AED'000	Computer systems and equipment AED'000	Furniture, equipment, fixtures, safes and vehicles AED'000	Capital work in progress AED'000	Total AED'000
Cost					
At 1 January 2017	17,437	2,928	9,366	3,391	33,122
Additions	-	-	-	-	-
Disposals, transfers and write offs	(4,577)	(1,207)	(2,494)	(3,391)	(11,669)
At 31 December 2017	12,860	1,721	6,872	-	21,453
Additions	**9**	**46**	**132**	**-**	**187**
Allocations from CWIP	**-**	**-**	**-**	**-**	**-**
Disposals, transfers and write offs	**-**	**(9)**	**(120)**	**-**	**(129)**
At 31 December 2018	**12,869**	**1,758**	**6,884**	**-**	**21,511**
Accumulated depreciation and impairment losses					
At 1 January 2017	11,303	2,507	6,869	-	20,679
Charge for the year	524	133	441	-	1,098
Disposals, transfers and write offs	(1,086)	(974)	(1,258)	-	(3,318)
At 31 December 2017	10,741	1,666	6,052	-	18,459
Charge for the year	**381**	**26**	**332**	**-**	**739**
Disposals, transfers and write offs	**-**	**(8)**	**(121)**	**-**	**(129)**
At 31 December 2018	**11,122**	**1,684**	**6,263**	**-**	**19,069**
Carrying amounts					
At 31 December 2017	2,119	55	820	-	2,994
At 31 December 2018	**1,747**	**74**	**621**	**-**	**2,442**

Notes to the financial statements *(continued)*

14 Other assets

	2018 AED'000	2017 AED'000
Profit receivable	**2,754**	1,492
Prepayments	**1,434**	1,704
Due from Parent	**87,065**	80,264
Other receivables	**388**	467
	91,641	83,927

The Company does not perceive any significant credit risk on profit receivable.

15 Other liabilities

	2018 AED'000	2017 AED'000
Provision employees' end of service benefits	**7,708**	8,235
Provision for expenses	**16,816**	13,117
Other liabilities	**2,843**	4,882
	27,367	26,234

Notes to the financial statements *(continued)*

15 Other liabilities *(continued)*

Employees' end of service benefits

Defined benefit obligations
The Company provides for end of service benefits for its eligible employees. An actuarial valuation has been carried out as at December 31, 2018 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:

	2018
Discount rate	**3.85 % per annum**
Salary increase rate	**2.00 % per annum**

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 152 thousand and AED 159 thousand respectively. Similarly, a shift in the salary increment assumption by +/- 50 basis points would impact the liability by AED 162 thousand and AED 155 thousand respectively.

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

	2018 **AED'000**	2017 AED'000
Balance at 1 January	**8,235**	10,013
Net charge during the year	**714**	1,530
Paid during the year	**(1,241)**	(3,308)
Balance at 31 December	**7,708**	8,235

Defined contribution plan
The Company 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 1,002 thousand *(2017: AED 1,637 thousand)*.

Notes to the financial statements *(continued)*

16 Capital and reserves

Share Capital

Authorized and paid up share capital	**2018 AED'000**	2017 AED'000
5,000,000 ordinary shares of AED 100 each	**500,000**	500,000
	500,000	500,000

Statutory and special reserves

In accordance with the Company'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.

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.

	2018 AED'000	2017 AED'000
Revaluation reserve – Non- trading investments		
At 1 January	**(3,305)**	(3,665)
Net change in fair value reserve	**3,777**	360
Realised gains recognised during the year	**1,851**	
Transfer from fair value reserve and realised gain to retained earnings	**(5,628)**	-
	-	(3,305)

Notes to the financial statements *(continued)*

17 Profit income

	2018 AED'000	2017 AED'000
Profit from:		
Banks and financial institutions	**2,326**	43
Investments at fair value through profit or loss	**4,451**	4,665
Islamic financing	**30,300**	51,632
Profit rate swap income	**3,487**	2,726
	40,564	59,066

18 Depositors' share profit

	2018 AED'000	2017 AED'000
Profit to:		
Banks and financial institutions	**-**	2,412
Profit rate swap expense	**4,451**	4,665
	4,451	7,077

19 Net fee and commission income

	2018 AED'000	2017 AED'000
Fee and commission income		
Islamic Financing	**577**	2,055
Total fee and commission income	**577**	2,055
Fee and commission expense		
Sales Incentive	**6,845**	3,966
Insurance Premium	**1,099**	1,490
Other Fees expense	**166**	279
Total fee and commission expense	**8,110**	5,735
Net fee and commission income	**(7,533)**	(3,680)

20 Net gain on investments and derivatives

	2018 AED'000	2017 AED'000
Net realised and unrealised gain on investments at fair value through profit or loss and derivatives	**(1,520)**	518
	(1,520)	518

Notes to the financial statements *(continued)*

21 General, administration and other operating expenses

	2018 AED'000	2017 AED'000
Staff costs	**67,451**	81,976
IT expense	**7,207**	6,406
Depreciation (note 13)	**739**	1,098
Rent expense	**6,906**	8,568
Other general and administration expenses	**1,630**	16,595
	83,933	114,643

22 Net impairment charge

	2018 AED'000	2017 AED'000
Impairment (release)/ charge on		
Islamic financing assets	**(7,458)**	13,737
other assets	**(7)**	9,470
Recoveries	**(200)**	-
Write-off of impaired financial assets	**4,493**	210
	(3,172)	23,417

23 Cash and cash equivalents

	2018 AED'000	2017 AED'000
Cash and balances with Banks	**295,791**	30,426
	295,791	30,426

Cash and cash equivalents included in the statement of cash flows comprise amounts with original contractual maturities of less than three months from the transaction date.

Notes to the financial statements *(continued)*

24 Commitments and contingencies

The Company, 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 financing facility 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.

	2018 **AED'000**	2017 AED'000
Undrawn commitment to extend credit	-	3,600
Total commitments and contingencies	-	3,600

Credit risk characteristics of these unfunded facilities closely resemble the funded facilities as described in note 5 are neither past due nor impaired.

Commitments to extend credit represent contractual commitments to extend facilities 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.

As of 31 December 2018, all Company operating lease commitments are less than one year.

Notes to the financial statements *(continued)*

25 Derivative financial instruments

In the ordinary course of business the Company 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 Sukuk derivatives enable users to increase, reduce or alter exposure to credit or market risks. Derivative financial instruments include swaps. These transactions are primarily entered with parent.

Swaps

Profit rate swaps are commitments to exchange one set of cash flows for another. Swaps result in an economic exchange of profit rates (for example, fixed rate for floating rate) or a combination of all these. No exchange of principal takes place, except for certain cross currency swaps. The Company'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 Company assesses counterparties using the same techniques as for its lending activities.

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 fair values of derivative financial instruments, which are equivalent to their fair values, together with the notional amounts analyzed 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.

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 investments.

	2018 **AED'000**	2017 AED'000
Negative fair value of profit rate swaps	**2,144**	3,971

26 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 shareholders, directors and key management personnel of the Company. Key management personnel comprise of Chief Executive Officer of the Company who is involved in the strategic planning and decision making of the Company. The terms of these transactions are approved by the Company's management and are made on terms agreed by the Board of Directors or management.

Parent and ultimate controlling party

First Abu Dhabi Bank PJSC holds 99.99% of the issued and fully paid up share capital of the Company.

The Parent has issued a letter of guarantee amounting to AED200 million on behalf of the company. No commission is charged by the Parent for the letter of guarantee issued.

Notes to the financial statements *(continued)*

26 Related parties *(continued)*

Significant transactions and balances with Related parties
The significant transactions and balances with related parties included in these financial statements are as follows:

Balances with related parties at the reporting date are shown below:

	2018 AED'000	2017 AED'000
Cash and balances with bank	**295,791**	30,426
Due from bank	**85,000**	50,000
Management fees receivable	**87,065**	80,264
Receivable on floating rate derivative	**566**	573
Payable on floating rate derivative	**697**	912
Receivable on Wakala placements	**1,491**	8
Payable to the Parent	**7,708**	8,235
Negative fair value profit rate swaps	**2,144**	3,971

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

	2018 AED'000	2017 AED'000
Income from Murabaha placements	**1,603**	43
Wakala deposit profit expense	**-**	(2,412)
Management Fee Income	**78,370**	102,881
Fee and Commission expense	**-**	(284)
Profit rate swaps income	**3,487**	2,726
Profit rate swaps expense	**(4,451)**	(4,665)
Gain on profit rate swaps	**1,827**	2,726

Management Fee income is management and administrative fees income which relates to services provided to the Parent's Islamic Banking Division (ISD) as per the agreement between the Company and the Parent.

	2018 AED'000	2017 AED'000
Key Management Compensation		
Short term employment benefits	**1,589**	1,442
Post-employment benefits	**162**	162

27 Comparative figures

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