Habib Bank AG Zurich

(Incorporated in Switzerland 1967)

Habib Bank AG Zurich

United Arab Emirates

Annual Report 2020

Habib Bank AG Zurich UAE Branches

FINANCIAL STATEMENTS

31 DECEMBER 2020

Habib Bank AG Zurich - UAE Branches

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REPORT OF THE MANAGEMENT

We are pleased to submit this report and the audited financial statements of Habib Bank AG Zurich, United Arab Emirates ("UAE") branches (the "Branches" or the "Bank") for the year ended 31 December 2020.

Incorporation and registered offices
The Bank has been operating in the United Arab Emirates since 1974. The Bank has eight branches across the country in the emirates of Dubai, Abu Dhabi and Sharjah. The registered address of the Bank is PO Box 3306, Dubai, United Arab Emirates.

The Head Office of the Bank is Habib Bank AG Zurich ("Head Office") incorporated in Switzerland.

Internal Shari'ah Supervision Committee of Habib Bank AG Zurich- UAE Branches
Subsequent to year end, the Internal Shari'ah Supervision Committee of Habib Bank AG Zurich, UAE Branches, has concluded with reasonable level of confidence, that the institution's activities are in compliance with Islamic Shari'ah, except for few observations with directions to take appropriate measure in regard to those observation. The management has initiated the plan on those measures for implementation.

Financial position and results
The financial position and results of the Branches for the year ended 31 December 2020 are set out in the accompanying financial statements.

During the year ended 31 December 2020, the Branches recorded total operating income and net profit of AED 373,939 thousand (2019: AED 444,814 thousand) and AED 94,679 thousand (2019: AED 142,300 thousand) respectively.

Signed on behalf of the Management

Jamaluddin Alvi
Chief Executive Officer

Date: 29 March 2021

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INDEPENDENT AUDITORS' REPORT TO THE BOARD OF DIRECOTRS OF HABIB BANK AG ZURICH, UNITED ARAB EMIRATES BRANCHES

Report on the audit of the financial statements

Opinion

We have audited the financial statements of Habib Bank AG Zurich, United Arab Emirates Branches (the "Bank" or the "Branches"), which comprise the statement of financial position as at 31 December 2020, and the statement of profit or loss and other comprehensive income, statement of changes in head office capital and reserves and statement of cash flows for the year then ended, and notes to the financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying financial statements present fairly, in all material respects, the financial position of the Branches as at 31 December 2020 and their financial performance and their cash flows for the year then ended in accordance with International Financial Reporting Standards ("IFRS").

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing ("ISAs"). Our responsibilities under those standards are further described in the *Auditor's responsibilities for the audit of the financial statements section* of our report. We are independent of the Branches in accordance with the International *Code of Ethics for Professional Accountants (including International Independence Standards) (the "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

The other information obtained at the date of the auditor's report is the Branches' 2020 Management Report. Those charged with governance are responsible for the other information.

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.

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INDEPENDENT AUDITORS' REPORT TO THE BOARD OF DIRECTORS OF HABIB BANK AG ZURICH, UNITED ARAB EMIRATES BRANCHES (continued)

Report on the audit of the financial statements (continued)

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 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 Branches' ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Branches or to cease operations, or has no realistic alternative but to do so.

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

Auditor's responsibilities for the audit of the financial statements

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

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

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than 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 Branches' internal control.

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

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INDEPENDENT AUDITORS' REPORT TO THE BOARD OF DIRECTORS OF HABIB BANK AG ZURICH, UNITED ARAB EMIRATES BRANCHES (continued)

Report on the audit of the financial statements (continued)

Auditor's responsibilities for the audit of the financial statements (continued)

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

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

We communicate with 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 Decretal Federal Law No. (14) of 2018, we report that we have obtained all the information and explanations we considered necessary for the purposes of our audit.

For Ernst & Young

Signed by:
Anthony O'Sullivan
Partner
Registration No. 687

Date: 29 March 2021

Dubai, United Arab Emirates

STATEMENT OF FINANCIAL POSITION

As at 31 December 2020

	Notes	*2020* *AED 000*	*2019* *AED 000*
ASSETS			
Cash and balances with the Central Bank of UAE	6	**3,668,854**	3,256,115
Due from banks, net	7	**3,939,817**	3,420,062
Due from related parties	28	**37,527**	99,598
Loans and Islamic financing receivables, net	8	**2,836,713**	3,203,850
Investments, net	9	**2,174,203**	1,508,918
Property and equipment	10	**53,995**	61,116
Right-of-use assets	11	**124,160**	126,044
Customers' indebtedness for acceptances		**44,387**	75,706
Deferred tax assets	12	**83,347**	81,493
Other assets	13	**62,920**	69,076
Total assets		**13,025,923**	11,901,978
LIABILITIES			
Deposits from customers	14	**10,883,342**	9,784,097
Due to banks	15	**43,501**	141,245
Due to related parties	28	**52,163**	8,798
Liabilities under acceptances		**44,387**	75,706
Other liabilities	16	**175,500**	205,194
Lease liabilities	11	**101,505**	90,609
Deferred tax liability	12	**15,239**	8,336
Total liabilities		**11,315,637**	10,313,985
CAPITAL AND RESERVES			
Allocated capital	17	**100,000**	100,000
Legal reserve	18	**50,000**	50,000
Retained earnings		**1,498,202**	1,402,676
Revaluation reserve		**60,957**	33,343
Impairment reserve	32	**1,127**	1,974
Total capital and reserves		**1,710,286**	1,587,993
Total liabilities, capital and reserves		**13,025,923**	11,901,978
CONTINGENT LIABILITIES AND OTHER COMMITMENTS	19	**618,326**	528,113

These financial statements were approved and authorized for issue on March 29, 2021 by

Chief Executive Officer

The attached notes 1 to 37 form part of these financial statements.

STATEMENT OF PROFIT OR LOSS AND OTHER COMPREHENSIVE INCOME

For the year ended 31 December 2020

	Notes	***2020 AED 000***	*2019 AED 000*
Interest income and income from Islamic financing	20	**269,442**	351,397
Interest expense and distribution to Islamic depositors	21	**(26,885)**	(36,627)
Net interest income and income from Islamic financing		**242,557**	314,770
Fee and commission income (net)	22	**62,317**	62,146
Other income	23	**69,065**	67,898
Operating income		**373,939**	444,814
Credit loss expense on financial assets (net)	25	**(11,021)**	(18,149)
Net operating income		**362,918**	426,665
General and administrative expenses	24	**(241,914)**	(248,170)
Profit for the year before taxation		**121,004**	178,495
Taxation	26	**(26,325)**	(36,195)
Net profit for the year after taxation		**94,679**	142,300
Other comprehensive income			
Items that will be subsequently reclassified to profit or loss:			
Net changes in fair values of debt investments classified as FVOCI		**37,282**	45,716
Changes in allowance for expected credit losses on debt investments classified as FVOCI	9 (a)	**(2,765)**	11,128
Income tax related to the above	12 (b)	**(6,903)**	(8,336)
Other comprehensive income for the year, net of tax		**27,614**	48,508
TOTAL COMPREHENSIVE INCOME FOR THE YEAR		**122,293**	190,808

The attached notes 1 to 37 form part of these financial statements.

STATEMENT OF CHANGES IN HEAD OFFICE CAPITAL AND RESERVES

For the year ended 31 December 2020

	Allocated capital AED 000	*Legal reserve AED 000*	*Retained earnings AED 000*	*Impairment reserve AED 000*	*Fair value reserve AED 000*	*Total AED 000*
As at 1 January 2019	100,000	50,000	1,319,446	2,404	(15,165)	1,456,685
Repatriation to Head Office	-	-	(59,500)	-	-	(59,500)
Transfer from impairment reserve (Note 32)	-	-	430	(430)	-	-
Profit for the year	-	-	142,300	-	-	142,300
Other comprehensive income	-	-	-	-	48,508	48,508
Total comprehensive income	-	-	142,300	-	48,508	190,808
As at 31 December 2019	100,000	50,000	1,402,676	1,974	33,343	1,587,993
Transfer from impairment reserve (Note 32)	-	-	847	(847)	-	-
Profit for the year	-	-	94,679	-	-	94,679
Other comprehensive income	-	-	-	-	27,614	27,614
Total comprehensive income	-	-	94,679	-	27,614	122,293
As at 31 December 2020	**100,000**	**50,000**	**1,498,202**	**1,127**	**60,957**	**1,710,286**

The attached notes 1 to 37 form part of these financial statements.

STATEMENT OF CASH FLOWS

For the year ended 31 December 2020

	Notes	*2020* *AED 000*	*2019* *AED 000*
OPERATING ACTIVITIES			
Profit for the year before taxation		**121,004**	178,495
Adjustments for:			
Impairment allowance on loans and Islamic financing receivables	25	**4,385**	5,293
(Reversal)/Impairment allowance on other assets	25	**(41)**	3,028
(Reversal)/impairment allowance on investments	25	**(2,593)**	11,416
Impairment allowance/(reversal) on due from banks	25	**3,040**	(1,588)
Impairment allowance on off balance-sheet	25	**6,230**	-
Depreciation on right-of-use assets	11	**16,278**	14,809
Finance cost on lease liabilities	11	**2,711**	2,725
Depreciation on property and equipment	10	**9,225**	9,129
Realized gain on sale of investments (net)	9	**(432)**	(823)
Amortization of premium on Investments (net)	9	**14,091**	10,662
(Gain)/loss on disposal/write off of property and equipment (net)	10	**(168)**	13
Operating profit before changes in net operating assets		**173,730**	233,159
Change in UAE Central Bank certificates of deposit with maturity over three months	33	**480,000**	(115,000)
Change in statutory reserve with UAE Central Bank	33	**185,321**	(72,407)
Change in bank placements with maturity over three months		**(1,004,317)**	377,853
Change in loans and receivables		**362,752**	249,200
Change in other assets		**6,197**	4,509
Change in deposits from customers		**1,099,245**	397,044
Change in other liabilities		**(24,749)**	5,746
Net cash generated from operations		**1,278,179**	1,080,104
Income tax paid		**(39,355)**	(37,088)
Net cash generated from operating activities		**1,238,824**	1,043,016
Investing activities			
Purchase of property and equipment	10	**(3,185)**	(6,427)
Sale proceeds from disposal of property and equipment		**1,249**	45
Net proceeds from sale/redemption of investments		**227,550**	327,272
Purchase of investments		**(869,384)**	(703,473)
Net cash used in investing activities		**(643,770)**	(382,583)
Financing activities			
Profits remitted to Head Office		**-**	(59,500)
Repayment of lease liabilities	11	**(6,208)**	(12,217)
Net cash used in financing activities		**(6,208)**	(71,717)
INCREASE IN CASH AND CASH EQUIVALENTS		**588,846**	588,716
Balance at 1 January		**4,399,419**	3,810,703
BALANCE AT 31 DECEMBER	33	**4,988,265**	4,399,419

The attached notes 1 to 37 form part of these financial statements.

1 LEGAL STATUS AND ACTIVITIES

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

These financial statements represent the combined financial position and results of the eight branches of the Bank in the United Arab Emirates. The Bank is not a separate legal entity but meets the definition of a reporting entity under IFRS under the Conceptual Framework for IFRS. IFRS defines a reporting entity as an entity that is required, or chooses, to prepare financial statements.

The Bank is owned by the Head Office and is in the business of providing retail, commercial and Islamic banking services in United Arab Emirates, which represent its economic activities. All the operating activities of the Bank are clearly defined and separately managed from the other businesses of the Head Office and accounting records are maintained on this basis. The assets of the Bank are used solely by the Bank and are registered in the name of the Bank. The liabilities relate to the activities of the Bank.

It is important to note whilst the reporting boundary is defined above, the assets and liabilities presented within the reporting boundary remain the assets and liabilities of the Head Office and are not legally separable from the Head Offices' other assets and liabilities. As such legally, the assets of the reporting entity may be available to the other claims of the Head Office.

Federal Decree Law No. 26 of 2020 which amends certain provisions of Federal Law No. 2 of 2015 on Commercial Companies was issued on 27 September 2020 and the amendments came into effect on 2 January 2021. The Bank is in the process of reviewing the new provisions and will apply the requirements thereof no later than one year from the date on which the amendments came into effect.

2 BASIS OF PREPARATION

2.1 Statement of compliance

The financial statements of the Branches have been prepared in accordance with International Financial Reporting Standards ("IFRS") issued by the International Accounting Standards Board ("IASB"), the UAE Federal Law No. (2) of 2015 and applicable regulations of the Central Bank of the UAE.

The financial statements have been prepared on the historical cost basis except for the following:

- Derivative financial instruments measured at fair value; and
- Financial instruments classified as fair value through other comprehensive income.

The Bank presents its statement of financial position in order of liquidity based on the Bank's intention and perceived ability to recover/settle the majority of assets/liabilities of the corresponding financial statement line item. An analysis regarding the recovery or settlement within 12 months after the reporting date (current) and more than 12 months after the reporting date (non-current) is presented in Note 32 (c).

The Covid 19 pandemic has resulted in significant volatility in the financial markets worldwide. Numerous governments, including UAE, have announced measures to provide both financial and non-financial assistance to the affected entities. The pandemic affects the assumptions and estimation uncertainty associated with the measurements of assets and liabilities with details covered in Note 32 (a) of these financial statements.

2.2 Functional and presentation currency

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

3 SIGNIFICANT ACCOUNTING POLICIES

Foreign currency translation
Foreign currency transactions are translated into the UAE Dirham at the rate ruling on the transaction date. Monetary assets and liabilities denominated in foreign currencies are translated into UAE Dirhams at the rates ruling at the reporting date. Any resultant gains or losses are accounted for in the statement of profit or loss and other comprehensive income.

Non-monetary assets and liabilities denominated in foreign currencies, which are stated at historical cost, are translated at the foreign exchange rate ruling at the date of the transaction. Non-monetary assets and liabilities denominated in foreign currencies that are stated at fair value are translated to AED at the foreign exchange rates ruling at the dates that the fair values were determined.

Forward foreign exchange contracts are translated into AED at market rates of exchange ruling at the reporting date. Foreign exchange differences arising on translation are recognised in the statement of profit or loss and other comprehensive income.

Fair value measurement
For those assets and liabilities carried at fair value, the Branches measure fair value at each reporting date. 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.

The fair value measurement of financial instruments is based on the presumption that the transaction to sell the asset or transfer the liability takes place either:

- In the principal market for the asset or liability, or
- In the absence of a principal market, in the most advantageous market for the asset or liability

The principal or the most advantageous market must be accessible to the Branches. The fair value of an asset or a liability is measured using the assumptions that market participants would use when pricing the asset or liability, assuming that market participants act in their economic best interest. A fair value measurement of non-financial instruments (instruments other than financial instruments) takes into account a market participant's ability to generate economic benefits by using the asset in its highest and best use or by selling it to another market participant that would use the asset in its highest and best use.

The Branches use valuation techniques that are appropriate in the circumstances and for which sufficient data are available to measure fair value, maximising the use of relevant observable inputs and minimising the use of unobservable inputs.

Fair values for financial instruments traded in active markets are based on closing bid prices. For all other financial instruments including instruments for which the market has become inactive, the fair value is determined by using appropriate valuation techniques. Valuation techniques include the fair value derived from recent arm’s length transaction, comparison to similar instruments for which market observable prices exist, discounted cash flow method or other relevant valuation techniques commonly used by market participants.

Fair values of non-financial instruments are measured based on valuation provided by independent valuators.

The fair value of a derivative financial instrument is the equivalent of the unrealised gain or loss from marking to market the derivative financial instrument, using relevant market rates or internal pricing models.

All assets and liabilities for which fair value is measured or disclosed in the financial statements are categorised within the fair value hierarchy, described as follows, based on the lowest level input that is significant to the fair value measurement as a whole:

Level 1: Quoted market price (unadjusted) in an active market for an identical instrument. A financial instrument is regarded as quoted in an active market if quoted prices are readily and regularly available from an exchange, dealer, broker, industry, branch, pricing service or regulatory agency, and those prices represent actual and regularly recurring market transactions on an arm’s length basis.

3 SIGNIFICANT ACCOUNTING POLICIES (continued)

Fair value measurement (continued)
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; quoted prices for identical or similar instruments; or other valuation techniques where all significant inputs are directly or indirectly observable from market data.

Level 3: Valuation techniques using significant unobservable inputs. This category includes all instruments where the valuation technique includes inputs based on unobservable data and the unobservable inputs have a significant effect on the instrument's valuation. This category includes instruments that are valued based on quoted prices for similar instruments where significant unobservable adjustments or assumptions are required to reflect differences between the instruments.

For assets and liabilities that are recognised in the financial statements on a recurring basis, the Branches determine whether transfers have occurred between Levels in the hierarchy by re-assessing categorisation (based on the lowest level input that is significant to the fair value measurement as a whole) at the end of each reporting period.

The Bank's Valuation Committee determines the policies and procedures for both recurring fair value measurement and unquoted financial assets. External valuers are involved for valuation of significant assets, such as unquoted financial assets, and significant liabilities, such as contingent consideration. At each reporting date, the Valuation Committee analyses the movements in the values of assets and liabilities which are required to be remeasured or reassessed as per the Bank's accounting policies. For this analysis, the Valuation Committee verifies the major inputs applied in the latest valuation by agreeing the information in the valuation computation to contracts and other relevant documents.

For the purpose of fair value disclosures, the Bank has determined classes of assets and liabilities on the basis of the nature, characteristics and risks of the asset or liability and the level of the fair value hierarchy, as explained above.

Fair-value related disclosures for financial instruments and non-financial assets that are measured at fair value or where fair values are disclosed, are summarised in the following notes:

- Disclosures for valuation methods, significant estimates and assumptions notes
- Quantitative disclosures of fair value measurement hierarchy
- Investment in non-listed equity shares (discontinued operations)
- Financial instruments (including those carried at amortised cost)
- Contingent consideration

Financial instruments
A financial instrument is any contract that gives rise to both a financial asset for the Branches and a financial liability or equity instrument for another party or vice versa.

Date of recognition
All financial assets and liabilities are initially recognised on the trade date, i.e., the date that the Branches become a party to the contractual provisions of the instrument. This includes regular way trades: purchases or sales of financial assets that require delivery of assets within the time frame generally established by regulation or convention in the market place.

Initial measurement of financial instruments
The classification of financial instruments at initial recognition depends on their purpose and characteristics and the management's intention in acquiring them. All financial instruments are measured initially at their fair value plus transaction costs, except in the case of financial assets and financial liabilities recorded at fair value through profit or loss where transaction costs are charged off to the statement of profit or loss and other comprehensive income.

If the transaction price differs from fair value at initial recognition, the bank will account for such difference as follows:

- if fair value is evidenced by a quoted price in an active market for an identical asset or liability or based on a valuation technique that uses only data from observable markets, then the difference is recognised in statement of profit or loss on initial recognition (i.e. day 1 profit or loss); and
- in all other cases, the fair value will be adjusted to bring it in line with the transaction price (i.e. day 1 profit or loss will be deferred by including it in the initial carrying amount of the asset or liability). After initial recognition, the deferred gain or loss will be released to statement of profit or loss on a rational basis, only to the extent that it arises from a change in a factor (including time) that market participants would take into account when pricing the asset or liability.

3 SIGNIFICANT ACCOUNTING POLICIES (continued)

Financial instruments (continued)

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

All recognised financial assets are subsequently measured in their entirety at either amortised cost or fair value, depending on the classification of the financial assets.

Classification of financial assets
For the purposes of classifying financial assets, an instrument is an 'equity instrument' if it is a non-derivative and meets the definition of 'equity' for the issuer except for certain non-derivative puttable instruments presented as equity by the issuer. All other non-derivative financial assets are 'debt instruments'.

Debt instruments, including loans and advances and investments products, are measured at amortised cost if both of the following conditions are met:

- the asset is held within a business model whose objective is to hold assets in order to collect contractual cash flows; and
- the contractual terms of the instrument give rise on specified dates to cash flows that are solely payments of principal and interest/profit (SPPI) on the principal amount outstanding.

All other financial assets are subsequently measured at fair value.

Business model assessment
The Bank makes an assessment of the objective of a business model in which a financial asset is held at portfolio level, because this reflects the way the business is managed and information is provided to the management. The assessment is not determined by a single factor or activity. Instead, the entity considers all relevant information available at the date of the assessment. The information considered includes:

- The stated policies and objectives for the business and the operation of those policies in practice. In particular, whether management's strategy focuses on earning contractual interest revenue, maintaining a particular interest 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 and the financial asset held within the portfolio is evaluated and reported to the management;

- The risks that affect the performance of the portfolio and, in particular, the way in which those risks are managed;

- How the managers of the business are compensated;

- 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 Bank's stated objective for managing the financial assets is achieved and how cash flows are realised; and

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.

3 SIGNIFICANT ACCOUNTING POLICIES (continued)

Financial instruments (continued)

Financial assets (continued)

Classification of financial assets (continued)

Assessment whether contractual cash flows is solely payments of principal and interest
In assessing whether the contractual cash flows are solely payments of principal and interest (SPPI), the Bank considers the contractual terms of the instrument.

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

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 Bank considers:

- Contingent events that would change the amount and timing of cash flows;
- Leverage features;
- Prepayment and extension terms;
- Terms that limit the Bank's claim to cash from specified assets; and
- Features that modify consideration of the time value of money (e.g. periodical reset of interest rates).

The Bank holds a portfolio of long-term fixed-rate loans for which the Bank has the option to propose to revise the interest rate at periodic reset dates. These reset rights are limited to the market rate at the time of revision. The Bank has determined that the contractual cash flows of these loans are SPPI because the interest rate varies in a way that is consideration for the time value of money, credit risk, other basic lending risks and costs associated with the principal amount outstanding.

Financial assets at amortised cost
Debt instruments meeting above criteria are measured initially at fair value plus transaction costs (except if they are designated as at fair value through profit or loss - see below). They are subsequently measured at amortised cost using the effective interest method less any impairment (see below), with interest revenue recognised on an effective yield basis in interest income.

Subsequent to initial recognition, the Branches are required to reclassify debt instruments from amortised cost to fair value through profit or loss, if the objective of the business model changes so that the amortised cost criteria are no longer met.

The effective interest method is a method of calculating the amortised cost of a debt instrument and of allocating interest income over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash receipts through the expected life of the debt instrument, or, where appropriate, a shorter period, to the net carrying amount on initial recognition.

The Branches may irrevocably elect at initial recognition to classify a debt instrument that meets the amortised cost criteria above as at fair value through profit or loss, if that designation eliminates or significantly reduces an accounting mismatch had the financial asset been measured at amortised cost.

Financial assets at FVTOCI
At initial recognition, the Branches can make an irrevocable election (on an instrument-by-instrument basis) to designate investments in equity instruments as at FVTOCI. Designation at FVTOCI is not permitted if the equity investment is held for trading.

A financial asset is held for trading if:

- it has been acquired principally for the purpose of selling it in the near term;
- on initial recognition it is part of a portfolio of identified financial instruments that the Branches manage together and has evidence of a recent actual pattern of short-term profit-taking; or
- it is a derivative that is not designated and effective as a hedging instrument or a financial guarantee.

3 SIGNIFICANT ACCOUNTING POLICIES (continued)

Financial instruments (continued)

Financial assets (continued)

Classification of financial assets (continued)

Financial assets at FVTOCI (continued)
Investments in equity instruments at FVTOCI are initially measured at fair value plus transaction costs. Subsequently, they are measured at fair value with gains and losses arising from changes in fair value recognised in other comprehensive income and accumulated in the investment revaluation reserve. Where the asset is disposed of, the cumulative gain or loss previously accumulated in the investment revaluation reserve is not transferred to income statement, but is reclassified to retained earnings.

Dividends on these investments in equity instruments are recognised in income statement when the Branches' right to receive the dividends is established, unless the dividends clearly represent a recovery of part of the cost of the investment.

Financial assets at fair value through profit or loss (FVTPL)
Debt instruments that do not meet the amortised cost criteria (as described above) are measured at FVTPL. In addition, debt instruments that meet the amortised cost criteria but are designated as at FVTPL are measured at FVTPL. A debt instrument may be designated as at FVTPL upon initial recognition if such designation eliminates or significantly reduces a measurement or recognition inconsistency that would arise from measuring assets or liabilities or recognising the gains and losses on them on different bases.

Debt instruments are reclassified from amortised cost to FVTPL when the business model is changed such that the amortised cost criteria are no longer met. Reclassification of debt instruments that are designated as at FVTPL on initial recognition is not allowed.

Financial assets at FVTPL are measured at fair value at the end of each reporting period, with any gains or losses arising on remeasurement recognised in the income statement. The net gain or loss is recognised in the income statement.

Interest income on debt instruments as at FVTPL is included in the net gain or loss described above and is included in the income statement.

Dividend income on investments in equity instruments at FVTPL is recognised in the income statement when the Branches' right to receive the dividends is established.

Reclassification of financial assets
The financial assets are required to be reclassified if the objective of the Branches' business model for managing those financial assets changes. Such changes are expected to be very infrequent. The Branches' management determine these changes as a result of external or internal changes and must be significant to the Branches' operations and demonstrable to external parties.

If the Branches reclassify financial assets, it shall apply the reclassification prospectively from the reclassification date. Any previously recognised gains, losses or interest are not required to be restated.

If the Branches reclassify a financial asset so that it is measured at fair value, its fair value is determined at the reclassification date. Any gain or loss arising from a difference between the previous carrying amount and fair value is recognised in the income statement.

If the Branches reclassify a financial asset so that it is measured at amortised cost, its fair value at the reclassification date becomes its new carrying amount. The reclassification day is the first day of the first reporting period following the change in business model that results in an entity reclassifying financial assets.

3 SIGNIFICANT ACCOUNTING POLICIES (continued)

Financial instruments (continued)

Financial assets (continued)

Expected credit losses

(i) Overview of expected credit losses
IFRS 9 requires the Bank to record an allowance for ECLs for all loans and other debt financial assets not held at FVTPL, together with loan commitments and financial guarantee contracts. The allowance is based on the ECLs associated with the probability of default in the next twelve months unless there has been a significant increase in credit risk since origination.

The Bank recognizes loss allowances for Expected Credit Losses (ECL) on the following financial instruments that are not measured at FVTPL:

- balances with central banks;
- due from banks and financial institutions;
- financial assets that are debt instruments;
- loans and advances;
- loan commitments issued; and
- financial guarantees contracts issued.

Equity instruments are not subject to impairment testing under IFRS 9.

The provision for credit losses is based on expected credit losses over the lifetime of the asset. If there is no significant change in credit risk from inception, the provision is based on the expected 12-month credit loss.

The expected credit loss weighted by the probability of default on credit exposure within 12 months is part of the expected credit loss on the lifetime of the asset arising from financial instrument deteriorations that may occur within 12 months of the reporting date.

The expected credit losses are calculated by the probability of default for the entire lifetime of the credit exposure or within 12 months of the credit exposure either on an individual or collective basis based on the nature of the portfolio of financial instruments.

The Bank has established a policy to periodically assess whether the credit risk of the financial instrument has increased significantly from the date of initial recognition, taking into account the change in the risk of default on the remaining life of the financial instruments.

Based on the above, the Bank classifies the financial instruments into three stages, stage (1), stage (2) and stage (3), as described below:

- Stage 1 – Upon initial recognition of financial instruments, the Bank records an allowance based on credit losses expected over the next 12 months. Stage 1 also includes financial assets which have been reclassified from Stage 2.
- Stage 2 – When a financial instrument experiences a significant increase in credit risk subsequent to origination, the Bank recognizes an allowance for expected credit losses for the entire lifetime of the credit exposure. Stage 2 includes financial instruments which have seen an improvement in credit risk and have been reclassified from Stage 3.
- 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)

For financial assets where the Bank has no reasonable expectation of recovery, either for the full amount of the outstanding amount or part of it, the carrying amount of the financial asset is reduced. It is considered as a (partial) cancellation of the financial assets.

3 SIGNIFICANT ACCOUNTING POLICIES (continued)

Financial instruments (continued)

Financial assets (continued)

Expected credit losses (continued)

(i) Overview of expected credit losses (continued)

The Bank's internal credit rating system:
The Bank's credit review and evaluation process is governed by the credit rules and policies set out in the Credit Facility Policies. The credit rating of the borrower is a key element in the credit review and evaluation. Consequently, the Bank has developed an internal rating methodology whereby the customer is evaluated according to the customer's financial and non-financial criteria.

(ii) Measurement of ECL
The Bank calculates expected credit losses based on the weighted average estimate of the expected cash deficit, discounted at an effective interest rate. The cash deficit is the difference between the cash flows due to the Bank in accordance with the contract and the expected cash flows.

The mechanism for calculating expected credit losses and key components is as follows:

- **Probability of default (PD):** The probability of default is an estimate of the probability of default over a certain period of time. Impairment may occur in a specified period during the valuation period.

- **Exposure at default (EAD):** The credit exposure at default is the estimate of the amount outstanding at a future date, taking into account expected changes to the amount after the reporting date, principal and interest, whether scheduled with a contract, expected withdrawals from facilities, or interest payable due to delayed payments.

- **Loss given default (LGD):** The loss given default is an estimate of the loss arising in a situation where the default occurs at a particular time. It represents the difference between the contractual cash flows due and the amount that the lender expects to collect from the existence of collateral. It is usually expressed as a percentage of credit exposure upon default.

In estimating the expected credit losses, the Bank takes into account three scenarios (the base scenario, the upside scenario, the downside scenario), each with different probabilities of default, credit exposure at default, and loss given default.

The multi-scenario assessment also includes how to recover non-performing loans, including the possibility of recovering non-performing loans and the amount of collaterals or amounts expected to be collected from the sale of collateral.

Except for credit cards and other revolving loans, the maximum period for which credit losses are determined is the contractual life of the financial instruments unless the Bank has the legal right to purchase them in advance.

The mechanisms for calculating expected credit losses are summarized as follows:

- **Stage 1** – The expected credit losses are calculated as the probability of default on the credit exposure within 12 months as part of the expected credit losses on the lifetime of the asset. Accordingly, the Bank calculates the provision for the probability of default of the financial instruments within 12 months after the reporting date. These 12-month defaults are applied to the amount of credit exposure at default multiplied by the loss rate given default, discounted at the effective interest rate.

- **Stage 2** – In the event of a significant increase in credit risk from the date of initial recognition, the Bank calculates an allowance for expected credit loss for the entire lifetime of the credit exposure. The calculation mechanism is similar to the method described above, including the use of different scenarios, but the probability of default and credit exposure at default are used for the entire lifetime of the financial instrument and the expected cash deficit amount is deducted at the effective interest rate.

3 SIGNIFICANT ACCOUNTING POLICIES (continued)

Financial instruments (continued)

Financial assets (continued)

Expected credit losses (continued)

(ii) Measurement of ECL (continued)

- **Stage 3** – Financial instruments to which the concept of default applies, the Bank calculates the expected credit loss for the entire lifetime of the credit exposure. The calculation mechanism is similar to that used in stage 2. The probability of default is 100% and the loss rate is assumed to be greater than that applied in stages 1 and 2.
- **Loan commitment and letter of credit** – The ECL related to loan commitments and letters of credit are included in expected credit losses relating to loans and advances. When estimating ECLs for undrawn loan commitments, the Branch estimates the expected portion of the loan commitment that will be drawn down over its expected life. The ECL is then based on the present value of the expected shortfalls in cash flows if the loan is drawn down, based on a probability-weighting of the three scenarios. The expected cash shortfalls are discounted at an approximation to the expected EIR on the loan.
- **Financial guarantee contract** - The Branches' liability under each guarantee is measured at the higher of the amount initially recognized less cumulative amortization recognized in the statement of profit or loss and other comprehensive income, and the ECL provision. For this purpose, the Branch estimates ECLs based on the present value of the expected payments to reimburse the holder for a credit loss that it incurs. The shortfalls are discounted by the risk-adjusted interest rate relevant to the exposure. The calculation is made using a probability-weighting of the three scenarios. The ECLs related to financial guarantee contracts are recognized within other liabilities.

(iii) Forward-looking Expected Credit Losses approach

In the expected credit loss calculation model, the Bank relies on a wide range of future information used as inputs, for example:

- International oil prices
- Gross domestic products

The inputs and models used to calculate expected credit losses may not include all market characteristics as at the date of the financial statements. As a result, qualitative adjustments are sometimes made as temporary modifications in case of significant differences.

(iv) Scenarios

Weighted average ECL is calculated considering base case, upside and downside scenarios multiplied by the associated scenario weightings, at the input stage for reflection of the ECL impact in the books of accounts. The management has assessed the impact of recent development and the abnormal situation that resulted from COVID-19, on the scenarios considered and based on its portfolio assessment concluded that the given scenarios remain appropriate. The most significant period-end assumptions used for ECL estimate as at 31 December 2020 are Gross Domestic Product (GDP) of United Arab Emirates (UAE) and international oil prices. The scenarios base case, upside and downside were used for all portfolios keeping in view the following principal macroeconomic variables

Macroeconomic variables	*Scenario*	*Assigned probabilities*	*2020*	*2021*	*2022*	*2023*	*Subsequent years*
GDP of UAE	Base case	67%	1,388.7	1,407.4	1,438.4	1,475.2	1,513.1
	Upside	17.1%	1,402.9	1,448.8	1,503.1	1,549.8	1,598.0
	Downside	15.9%	1,331.6	1,340.6	1,349.6	1,371.7	1,392.2
Oil pri (USD per barr	Base case	67%	42.3	48.0	52.0	54.0	60.8
	Upside	17.1%	46.2	56.6	60.0	61.2	65.0
	Downside	15.9%	39.0	42.0	37.4	44.5	51.0

(v) Sensitivity analysis

If the macroeconomic variables (defined above) were to change by the base case, upside and downside scenarios, the ECL under stages 1 and 2 will change between -10% to +15% among 3 scenarios.

There has been no significant sensitivity impact on stage 3 ECL.

3 SIGNIFICANT ACCOUNTING POLICIES (continued)

Financial instruments (continued)

Financial assets (continued)

Credit-impaired financial assets / definition of default:
At each reporting date, the Bank assesses whether financial assets carried at amortised cost and debt securities carried at FVOCI are credit-impaired.

Assets classified under this category are obligors which are unlikely to repay their contractual obligations, on a timely basis and are considered as defaulted obligors. The default definition used by the Bank is captured by the 'For Adjustment Purpose ("FAP")' tagging which in turn is triggered by the qualitative and quantitative criteria listed below:

- **Days Past Due (DPD):** Corporate / SME / Retail accounts is identified as default if the contractual payment is more than or equal to 90 days past due. For Investments & FI portfolios account is identified as default if the contractual coupon payment is more than 30 days past due. Additionally, for overdraft exposures, any excess over limit or forced debit will be treated similar to days past due i.e., an overdraft account showing excess over limit for 90 days will become a Stage 3 exposure. The days past due will be calculated and applied in line with the credit risk policy as applicable to the bank (and will be reflected in FAP tagging).

- **Non-Performing Loans ('For Adjustment Purpose (FAP)' Tagging):** The tagging of exposures to the Non-performing Loans ("NPL") category or Default FAP (2 or worse) based on the overdue status or qualitative information available with the Bank will trigger transfer of credit exposures to Stage 3.

- **Credit Rating Downgrade:** Under Investments & FI portfolios for Investment Grade ("IG") exposures, a downgrade of more than 2 notches from IG to Non-Investment Grade ("NIG") will trigger transfer to Stage 3. Whereas for exposures within the NIG, a 3 notch downgrade will trigger transfer to Stage 3.

- **Cross-Product Default:** For Corporate / SME or Retail portfolio whenever a credit exposure is marked NPL or Default FAP (2 or worse), all related exposures within the same entity / counterparty (all facilities and credit exposure from all product areas) are marked NPL or Overdue / Default FAP. The tagging of credit exposures as NPL or Default FAP (2 or worse) will trigger transfer to stage 3.

Collateral valuation
To mitigate its credit risks on financial assets, the Branches seek to use collateral, where possible. The collateral comes in various forms, such as cash, securities, letters of credit/guarantees, real estate, receivables, inventories and other non-financial assets and credit enhancements such as netting agreements. The Branches' accounting policy for collateral assigned to it through its lending arrangements under IFRS 9 is the same it was under IAS 39. Collateral, unless foreclosed, is not recorded on the Branches' statement of financial position. However, the fair value of collateral is re-assessed periodically. However, some collateral, for example, cash or securities relating to margining requirements, is valued daily.

To the extent possible, the Branches uses active market data for valuing financial assets held as collateral. Other financial assets which do not have readily determinable market values are valued using models. Non-financial collateral, such as real estate, is valued based on data provided by third parties such as mortgage brokers or independent valuers.

Write-offs
Financial assets are written off either partially or in their entirety only when the Branches has no reasonable expectation of recovering a financial asset in its entirety or a portion thereof. If the amount to be written off is greater than the accumulated loss allowance, the difference is first treated as an addition to the allowance that is then applied against the gross carrying amount. Any subsequent recoveries are credited to credit loss expense.

Renegotiated loans and advances
Where possible, the Branches seek to restructure loans rather than to take possession of collateral. This may involve extending the payment arrangements and the agreement on new loan conditions. Once the terms have been renegotiated, any impairment is measured using the original effective interest rate as calculated before the modification of terms and the loan is no longer considered past due. Management continuously reviews renegotiated loans to ensure that all criteria are met and that future payments are likely to occur. The loans continue to be subject to an individual or collective impairment assessment, calculated using the loan's original effective interest rate.

3 SIGNIFICANT ACCOUNTING POLICIES (continued)

Financial instruments (continued)

Financial assets (continued)

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

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

On derecognition of a financial asset (equity instrument) that is classified as FVTOCI, the cumulative gain or loss previously accumulated in the investment revaluation reserve is not reclassified to the income statement, but is reclassified to retained earnings.

On derecognition of a financial asset (debt instrument) that is classified as FVTOCI, the cumulative gain or loss previously accumulated in the investment revaluation reserve is reclassified to the income statement.

Purchased or originated credit-impaired (POCI) financial assets
The Bank, as a policy, does not purchase credit impaired assets. However, a significant modification of a financial asset can result in de-recognition of the existing financial asset and the subsequent recognition of the modified financial asset, the modified asset is considered a 'New' financial asset, assuming that the level of modification exceeds the internal thresholds set by the management.

The effective interest rate (EIR) for a POCI asset is estimated using expected cash-flows (i.e. its credit adjusted) rather than contractual cash-flows. For a POCI, interest accrual is not done on a gross basis, even if the credit quality of the asset improves. Since, the Bank utilizes the expected cash-flows to compute the credit adjusted EIR, these assets already incorporate life time expected credit losses and hence a separate loss allowance is not required. Any changes (whether a loss or a gain), however in the lifetime expected losses for these assets would require that a loss allowance is accrued to reflect the same.

Modification of financial assets
Restructuring a credit facility, based on urgent request from the client, enables the client to continue servicing interest and amortization payments. Without restructuring the client would not be able anymore to meet the conditions of the contract. A restructuring therefore can be defined as the inability of the borrower to continue servicing the debt without any relief in the terms and conditions.

Restructuring is not referring to a normal - business as usual – rescheduling request by the client to amend credit facilities according to the changing economic environment. This could be due to expansion of the business or reallocation of resources and therefore changing financing needs in view of a different expectation of the future economic environment.

In certain cases, there might be a subtle line between the two above described cases. However, whenever all credit facilities of various banks need to be re-negotiated or a syndicated loan needs re-negotiation, this is most likely due to a breach of contract. If a private client is asking for re-negotiation, the Bank's judgment should be dependent on the financial flexibility of the client. An over-leveraged home loan where the Loan-to-value (LTV) is over 100% and the client asks for re-negotiation but has no additional financial resources (which he possibly could bring in) is also to be treated as a breach of contract.

Restructured cases need to be flagged as "restructured" from the start. This flagging is an additional earmark besides the classification. The ECL numbers for stage 2 exposures will be computed over the lifetime of the facility based on residual maturity / tenor of the facility.

3 SIGNIFICANT ACCOUNTING POLICIES (continued)

Financial instruments (continued)

Financial liabilities
Financial liabilities are classified as either financial liabilities 'at FVTPL' or 'other financial liabilities'.

Financial liabilities at FVTPL
Financial liabilities are classified as at FVTPL when the financial liability is either held for trading or it is designated as at FVTPL.

A financial liability is classified as held for trading if:

- it has been acquired principally for the purpose of repurchasing it in the near term; or
- on initial recognition it is part of a portfolio of identified financial instruments that the Branches manage together and has a recent actual pattern of short-term profit-taking; or
- it is a derivative that is not designated and effective as a hedging instrument.

A financial liability other than a financial liability held for trading may be designated as at FVTPL upon initial recognition if:

- such designation eliminates or significantly reduces a measurement or recognition inconsistency that would otherwise arise; or
- the financial liability forms part of a group of financial assets or financial liabilities or both, which is managed and its performance is evaluated on a fair value basis, in accordance with the Branches' documented risk management or investment strategy, and information about the grouping is provided internally on that basis; or
- it forms part of a contract containing one or more embedded derivatives, and IAS 39 *Financial Instruments: Recognition and Measurement* permits the entire combined contract (asset or liability) to be designated as at FVTPL.
- Financial liabilities at FVTPL are stated at fair value, with any gains or losses arising on remeasurement recognised in profit or loss. The net gain or loss recognised in profit or loss incorporates any interest paid on the financial liability and is included in the 'other gains and losses' line item in the statement of income.

Other financial liabilities
Other financial liabilities, include deposits and balances due to Head Office and its branches abroad, borrowings, are initially measured at fair value, net of transaction costs.

Other financial liabilities are subsequently measured at amortised cost using the effective interest method, with interest expense recognised on an effective interest rate.

The effective interest method is a method of calculating the amortised cost of a financial liability and of allocating interest expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments through the expected life of the financial liability, or (where appropriate) a shorter period, to the net carrying amount on initial recognition.

Derecognition of financial liabilities
A financial liability is derecognised when the obligation under the liability is discharged or cancelled or expires. Where an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is treated as a derecognition of the original liability and the recognition of a new liability. The difference between the carrying value of the original financial liability and the consideration paid is recognised in the statement of profit or loss and other comprehensive income.

3 SIGNIFICANT ACCOUNTING POLICIES (continued)

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

Financial guarantee contracts issued by the Bank are initially measured at their fair values and, if not designated as at FVPL and not arising from a transfer of a financial asset, are subsequently measured at the higher of:

The amount of the loss allowance determined in accordance with IFRS 9 and the amount initially recognised less, where appropriate, the cumulative amount of income recognised in accordance with the Bank's revenue recognition policies.

Loan commitments
Loan commitments are firm commitments to provide credit under pre-specified terms and conditions. Commitments to provide a loan at a below-market interest rate are initially measured at their fair values and, if not designated as at FVPL, are subsequently measured as follows:

At the higher of the amount of the loss allowance determined in accordance with IFRS 9 and the amount initially recognised less, where appropriate, the cumulative amount of income recognised in accordance with the Bank's revenue recognition policies.

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

Investments
The '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 interest method;
- Debt and equity investment securities measured at FVPL or designated as at FVPL: These are at fair value with changes recognised immediately in profit or loss;
- Debt securities measured at FVOCI; and
- Equity investment securities designated as FVOCI.

For 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.

- Interest revenue using the effective interest 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 Bank 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 on equity instruments recognised in OCI are transferred to retained earnings on disposal of an investment.

3 SIGNIFICANT ACCOUNTING POLICIES (continued)

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

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

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

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

Buildings	25 years
Furniture and office equipment	4 to 7 years
Computer systems	4 years
Motor vehicles	5 years

Right-of-use assets
The Bank recognises right-of-use assets at the commencement date of the lease (i.e. the date the underlying asset is available for use). Subsequent to initial recognition, Right-of-use assets are measured at cost, less any accumulated depreciation and impairment losses, and adjusted for any re-measurement of lease liabilities. The cost of right-of-use assets includes the amount of lease liabilities recognised, initial direct costs incurred, and lease payments made at or before the commencement date less any lease incentives received. Unless the Bank is reasonably certain to obtain ownership of the leased asset at the end of the lease term, the recognised right-of-use assets are depreciated on a straight-line basis over the shorter of its estimated useful life and the lease term. Right-of-use assets are subject to impairment.

Lease liabilities
At the commencement date of the lease, the Bank recognises lease liabilities measured at the present value of lease payments to be made over the lease term. The lease payments include fixed payments (including in substance fixed payments) less any lease incentives receivable, variable lease payments that depend on an index or a rate, and amounts expected to be paid under residual value guarantees. The lease payments also include the exercise price of a purchase option reasonably certain to be exercised by the Bank and payments of penalties for terminating a lease, if the lease term reflects the Bank exercising the option to terminate. Variable lease payments that do not depend on an index or a rate are recognised as expense in the period in which the event or condition that triggers the payment occurs.

In calculating the present value of lease payments, the Branch uses the incremental borrowing rate, as applicable, at the lease commencement date since the interest rate implicit in the lease is not readily determinable. After the commencement date, the amount of lease liabilities is increased to reflect the accretion of interest and reduced for the lease payments made. In addition, the carrying amount of lease liabilities is re-measured if there is a modification, a change in the lease term, a change in the in-substance fixed lease payments or a change in the assessment to purchase the underlying asset.

Short-term leases and leases of low-value assets
The Bank applies the short-term lease recognition exemption to its short-term leases of property and equipment (i.e. those leases that have a lease term of 12 months or less from the commencement date and do not contain a purchase option). It also applies the lease of low-value assets recognition exemption to leases of property and equipment that are considered of low value. Payments on short-term leases and leases of low-value assets are recognised as an expense on a straight-line basis over the lease term.

The Bank has the option, under some of its leases to lease the assets for an additional term. The Bank applies judgement in evaluating whether it is reasonably certain to exercise the option to renew. That is, it considers all relevant factors that create an economic incentive for it to exercise the renewal. After the commencement date, the Bank reassesses the lease term if there is a significant event or change in circumstances that is within its control and affects its ability to exercise (or not to exercise) the option to renew (e.g. a change in business strategy).

3 SIGNIFICANT ACCOUNTING POLICIES (continued)

Impairment of non-financial assets
At the end of each reporting period, the Branches review the carrying amounts of their non-financial assets to determine whether there is any indication that those assets have suffered an impairment loss. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss (if any). Where it is not possible to estimate the recoverable amount of an individual asset, the Branches estimate the recoverable amount of the cash-generating unit to which the asset belongs. Where a reasonable and consistent basis of allocation can be identified, corporate assets are also allocated to individual cash-generating units, or otherwise they are allocated to the smallest Bank of cash-generating units for which a reasonable and consistent allocation basis can be identified.

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

If the recoverable amount of an asset (or cash-generating unit) is estimated to be less than its carrying amount, the carrying amount of the asset (or cash-generating unit) is reduced to its recoverable amount. An impairment loss is recognised immediately in statement of profit or loss and other comprehensive income.

Where an impairment loss subsequently reverses, the carrying amount of the asset (or cash-generating unit) is increased to the revised estimate of its recoverable amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognised for the asset (or cash-generating unit) in prior years. A reversal of an impairment loss is recognised immediately in statement of comprehensive income.

Customer deposits and Islamic customer deposits
Customer deposits are initially recognised at fair value, being the fair value of the consideration received.

After initial recognition, all deposits are subsequently measured at amortised cost using the effective interest method. Amortised cost is calculated by taking into account any transaction costs that are directly attributable to the acquisition or receipt of customer deposit.

The Islamic customer deposits are received by entering into following kinds of agreements:

Mudaraba
An agreement between the Bank and a third party whereby one party would provide a certain amount of funds (Rab ul Mal) which the other party (Mudarib) would then invest in a specific enterprise or activity against a specific share in the profit. The Mudarib would bear the loss in case of default, negligence or violation of any of the terms and conditions of the Mudaraba. In principle Mudaraba profit is distributed on declaration/distribution by the Mudarib.

Wakala
An agreement between Bank and third party whereby one party (Muwakil) provides certain amount of funds which the other party (Wakil) would invest according to the terms and conditions of Wakala in return for a certain fee. The Wakil is obliged to return the invested amount in case of default, negligence or violation of any of the terms and conditions of the Wakala. The Wakeel may be granted any excess over and above a certain pre-agreed rate of return as a performance incentive. In principle, wakala profit is distributed on declaration/distribution by the Wakil.

Islamic customer deposits are initially measured at fair value plus transaction costs, and subsequently measured at their amortised cost using the effective profit method.

Staff terminal benefits
With respect to the Bank’s national employees, the Bank contribute to the pension scheme for UAE nationals under the UAE pension and social security law. This is a defined contribution pension plan and the Bank contributions are charged to the statement of profit or loss in the period to which they relate. In respect of this scheme, the Bank have an obligation to pay the fixed contributions as they fall due and no obligations exist to pay the future benefits.

The Bank provide for end of services benefits to other employees based on applicable laws and regulations which is based on period of service and basic salaries.

3 SIGNIFICANT ACCOUNTING POLICIES (continued)

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

Cash and cash equivalents are carried at amortised cost.

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

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

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

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

Revenue recognition and expense
Revenue is recognised to the extent that it is probable that the economic benefits will flow to the Branches and the revenue can be reliably measured. The following specific recognition criteria must also be met before revenue is recognised:

Interest income and expense
Interest income and expense for all interest-bearing financial instruments are recognised using the effective interest rate, which is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument or a shorter period, where appropriate, to the net carrying amount of the financial asset or financial liability on initial recognition. When there is doubt in the collection of the principal or the interest, the recognition of interest income ceases.

When calculating the effective interest rate for financial instruments other than credit-impaired assets, the Bank estimates future cash flows considering all contractual terms of the financial instrument, but not ECL. For credit-impaired financial assets, a credit-adjusted effective interest rate is calculated using estimated future cash flows including ECL.

The calculation of the effective interest rate includes transaction costs and fees that are an integral part of the effective interest rate. Transaction costs include incremental costs that are directly attributable to the acquisition or issue of a financial asset or financial liability.

Fee and commission income
Fee and commission income is recognised at point in time when customer obtain controls over the related services as performed.

Fees and commission that are an integral part of the effective interest rate of a financial instrument are treated as an adjustment to the effective interest rate. Other fees and commissions are recognised over the period of service.

Income from recoveries
Recoveries in respect of defaulted loans are accounted for when recovery is virtually certain and amount can be measured reliably.

3 SIGNIFICANT ACCOUNTING POLICIES (continued)

Revenue recognition and expense (continued)

Income from Islamic financing and distributions to depositors
Income from Islamic financing is recognised in the statement of profit or loss using the effective profit method.

The calculation of the effective profit rate includes all fees paid or received, transaction costs, and discounts or premiums that are an integral part of the effective profit rate. Transaction costs are incremental costs that are directly attributable to the acquisition, issue or disposal of a financial asset.

Distribution to depositors (Islamic products) is calculated according to the Bank's standard procedures and is approved by the Bank's Sharia's Supervisory Board.

Fees for custodian services
The Bank provides custodian services to various clients. Fees for custodian services are calculated based on a fixed percentage of the value of assets managed and deducted from the customer's account balance on a monthly basis.

Amortised cost and gross carrying amount
The 'amortised cost' of a financial asset or financial liability is the amount at which the financial asset or financial liability is measured on initial recognition minus the principal repayments, plus or minus the cumulative amortisation using the effective interest method of any difference between that initial amount and the maturity amount and, for financial assets, adjusted for any expected credit loss allowance.

The 'gross carrying amount of a financial asset' is the amortised cost of a financial asset before adjusting for any expected credit loss allowance.

Contract balances
The following is recognised in the statement of financial position arising from revenue from contracts with customers:

'Commission received in advance' included under 'Other liabilities', which represent the Bank's obligation to transfer services to a customer for which the Bank has received consideration (or an amount of consideration is due) from the customer. A liability for unearned fees and commissions is recognised when the payment is made, or the payment is due (whichever is earlier). Unearned fees and commissions are recognised as revenue when (or as) the Bank performs.

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

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

Deferred tax
Deferred tax is provided on temporary differences at the statement of financial position date between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes. Deferred tax liabilities are recognised for all taxable temporary differences, except:

- Where the deferred tax liability arises from the initial recognition of goodwill or of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss.
- In respect of taxable temporary differences associated with investments in subsidiaries, where the timing of the reversal of the temporary differences can be controlled and it is probable that the temporary differences will not reverse in the foreseeable future.

Deferred tax assets are recognised for all deductible temporary differences, carry forward of unused tax credits and unused tax losses, to the extent that it is probable that taxable profit will be available against which the deductible temporary differences, and the carry forward of unused tax credits and unused tax losses can be utilised except:

- Where the deferred tax asset relating to the deductible temporary difference arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss.
- In respect of deductible temporary differences associated with investments in subsidiaries, deferred tax assets are recognised only to the extent that it is probable that the temporary differences will reverse in the foreseeable future and taxable profit will be available against which the temporary differences can be utilised.

3 SIGNIFICANT ACCOUNTING POLICIES (continued)

Deferred tax (continued)
The carrying amount of deferred tax assets is reviewed at each statement of financial position date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred tax asset to be utilised. Unrecognised deferred tax assets are reassessed at each statement of financial position date and are recognised to the extent that it has become probable that future taxable profit will allow the deferred tax asset to be recovered.

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply in the year when the asset is realised or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted at mthe statement of financial position date. Deferred taxes relating to items recognised directly in equity are also recognised in equity and not in the statement of profit or loss and other comprehensive income.

Deferred tax assets and deferred tax liabilities are offset if a legally enforceable right exists to set off current tax assets against current tax liabilities and the deferred taxes relate to the same taxable entity and the same taxation authority.

The Bank have consistently applied the accounting policies same as prior year except for the changes in accounting policies resulting from adoption of new standards and interpretation.

(a) *New/amended standards and interpretations effective from annual periods beginning on or after 1 January 2020.*

Interest Rate Benchmark Reform: Amendments to IFRS 9, IAS 39 and IFRS 7
The amendments to IFRS 9 and IAS 39 Financial Instruments: Recognition and Measurement provide a number of reliefs, which apply to all hedging relationships that are directly affected by interest rate benchmark reform. A hedging relationship is affected if the reform gives rise to uncertainty about the timing and/or amount of benchmark-based cash flows of the hedged item or the hedging instrument.

These amendments have no impact on the financial statements of the Bank as it does not have any interest rate hedge relationships.

Amendments to IFRS 3: Definition of a Business
The amendment to IFRS 3 Business Combinations clarifies that to be considered a business, an integrated set of activities and assets must include, at a minimum, an input and a substantive process that, together, significantly contribute to the ability to create output. Furthermore, it clarifies that a business can exist without including all of the inputs and processes needed to create outputs.

These amendments had no impact on the financial statements of the Bank, but may impact future periods should the Bank enter into any business combinations.

Amendments to IAS 1 and IAS 8 Definition of Material
The amendments provide a new definition of material that states, "information is material if omitting, misstating or obscuring it could reasonably be expected to influence decisions that the primary users of general purpose financial statements make on the basis of those financial statements, which provide financial information about a specific reporting entity." The amendments clarify that materiality will depend on the nature or magnitude of information, either individually or in combination with other information, in the context of the financial statements. A misstatement of information is material if it could reasonably be expected to influence decisions made by the primary users.

These amendments had no impact on the financial statements of, nor is there expected to be any future impact to the Bank.

Amendments to IFRS 16 Covid-19 Related Rent Concessions
On 28 May 2020, the IASB issued Covid-19-Related Rent Concessions - amendment to IFRS 16 Leases The amendments provide relief to lessees from applying IFRS 16 guidance on lease modification accounting for rent concessions arising as a direct consequence of the Covid-19 pandemic. As a practical expedient, a lessee may elect not to assess whether a Covid-19 related rent concession from a lessor is a lease modification. A lessee that makes this election accounts for any change in lease payments resulting from the Covid-19 related rent concession the same way it would account for the change under IFRS 16, if the change were not a lease modification. The Bank has elected not to apply the practical expedient.

3 SIGNIFICANT ACCOUNTING POLICIES (continued)

(b) New/amended standards and interpretations issued but not yet effective

The standards and interpretations that are issued, but not yet effective, up to the date of issuance of the Branches' financial statements are disclosed below. The Branches intends to adopt these standards, if applicable, when they become effective.

Amendments to IAS 1: Classification of Liabilities as Current or Non-current
In January 2020, the IASB issued amendments to paragraphs 69 to 76 of IAS 1 to specify the requirements for classifying liabilities as current or non-current. The amendments clarify:

- What is meant by a right to defer settlement?
- That a right to defer must exist at the end of the reporting period
- That classification is unaffected by the likelihood that an entity will exercise its deferral right. That only if an embedded derivative in a convertible liability is itself an equity instrument would the terms of a liability does not impact its classification

The amendments are effective for annual reporting periods beginning on or after 1 January 2023 and must be applied retrospectively. These amendments are not applicable to the Bank.

Reference to the Conceptual Framework – Amendments to IFRS 3
In May 2020, the IASB issued Amendments to IFRS 3 Business Combinations - Reference to the Conceptual Framework. The amendments are intended to replace a reference to the Framework for the Preparation and Presentation of Financial Statements, issued in 1989, with a reference to the Conceptual Framework for Financial Reporting issued in March 2018 without significantly changing its requirements.

The Board also added an exception to the recognition principle of IFRS 3 to avoid the issue of potential 'day 2' gains or losses arising for liabilities and contingent liabilities that would be within the scope of IAS 37 or IFRIC 21 Levies, if incurred separately.

At the same time, the Board decided to clarify existing guidance in IFRS 3 for contingent assets that would not be affected by replacing the reference to the Framework for the Preparation and Presentation of Financial Statements.

The amendments are effective for annual reporting periods beginning on or after 1 January 2022 and apply prospectively. The amendments are not expected to have a material impact on the Bank.

Onerous Contracts – Costs of Fulfilling a Contract – Amendments to IAS 37
In May 2020, the IASB issued amendments to IAS 37 to specify which costs an entity needs to include when assessing whether a contract is onerous or loss-making.

The amendments apply a "directly related cost approach". The costs that relate directly to a contract to provide goods or services include both incremental costs and an allocation of costs directly related to contract activities. General and administrative costs do not relate directly to a contract and are excluded unless they are explicitly chargeable to the counterparty under the contract.

The amendments are effective for annual reporting periods beginning on or after 1 January 2022. The amendments are not expected to have a material impact on the Bank.

IFRS 9 Financial Instruments – Fees in the '10 per cent' test for derecognition of financial liabilities
As part of its 2018-2020 annual improvements to IFRS standards process the IASB issued amendment to IFRS 9. The amendment clarifies the fees that an entity includes when assessing whether the terms of a new or modified financial liability are substantially different from the terms of the original financial liability. These fees include only those paid or received between the borrower and the lender, including fees paid or received by either the borrower or lender on the other's behalf. An entity applies the amendment to financial liabilities that are modified or exchanged on or after the beginning of the annual reporting period in which the entity first applies the amendment.

The amendment is effective for annual reporting periods beginning on or after 1 January 2022 with earlier adoption permitted. The Company will apply the amendments to financial liabilities that are modified or exchanged on or after the beginning of the annual reporting period in which the entity first applies the amendment. The amendments are not expected to have a material impact on the Company.

4 STANDARDS, AMENDMENTS AND INTERPRETATIONS (continued)

(b) New/amended standards and interpretations issued but not yet effective (continued)

IBOR reform Phase 2
IBOR reform Phase 2 includes a number of reliefs and additional disclosures. The reliefs apply upon the transition of a financial instrument from an IBOR to a risk-free-rate (RFR). Changes to the basis for determining contractual cash flows as a result of interest rate benchmark reform are required as a practical expedient to be treated as changes to a floating interest rate, provided that, for the financial instrument, the transition from the IBOR benchmark rate to RFR takes place on an economically equivalent basis.

As indicated in the accounting policies, the Bank elected, as a policy choice permitted under IFRS 9, to continue to apply hedge accounting in accordance with IAS 39. IBOR reform Phase 2 provides temporary reliefs that allow the Bank's hedging relationships to continue upon the replacement of an existing interest rate benchmark with an RFR. The reliefs require the Bank to amend hedge designations and hedge documentation. This includes redefining the hedged risk to reference an RFR, redefining the description of the hedging instrument and / or the hedged item to reference the RFR and amending the method for assessing hedge effectiveness. Updates to the hedging documentation must be made by the end of the reporting period in which a replacement takes place. For the retrospective assessment of hedge effectiveness, the Bank may elect on a hedge by hedge basis to reset the cumulative fair value change to zero. The Bank may designate an interest rate as a non-contractually specified, hedged risk component of changes in the fair value or cash flows of a hedged item, provided the interest rate risk component is separately identifiable, e.g., it is an established benchmark that is widely used in the market to price loans and derivatives. For new RFRs that are not yet an established benchmark, relief is provided from this requirement provided the Bank reasonably expects the RFR to become separately identifiable within 24 months. For hedges of groups of items, the Bank is required to transfer to subgroups those instruments that reference RFRs. Any hedging relationships that prior to application of IBOR reform Phase 2, have been discontinued solely due to IBOR reform and meet the qualifying criteria for hedge accounting when IBOR reform Phase 2 is applied, must be reinstated upon initial application.

The Bank has not early adopted the requirements of 'Interest Rate Benchmark Reform – Phase 2 Amendments to IFRS 9, IAS 39, IFRS 7, IFRS 4 and IFRS 16' (IBOR reform Phase 2), hence the same had no impact on the financial statements of the Bank.

5 SIGNIFICANT ACCOUNTING JUDGEMENTS, ESTIMATES AND ASSUMPTIONS

In the process of applying the Branches' accounting policies, which are described in Note 3, management is required to use certain critical accounting estimates and assumptions that affect the reported amounts of assets and liabilities. It also requires management to exercise its judgment. Such estimates, assumptions and judgments are continually evaluated and are based on historical experience and other factors, including obtaining professional advices and expectations of future events that are believed to be reasonable under the circumstances.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised if the revision affects only that period, or in the period of the revision and future periods if the revision affects both current and future periods.

Significant areas where management has used estimates, assumptions or exercised judgments are as follows:

a) Fair value of financial instruments not quoted in active markets
Where the fair values of financial assets and financial liabilities recorded on the statement of financial position cannot be derived from active markets, they are determined using a variety of valuation techniques that include the use of mathematical models. The inputs to these models are derived from observable market data where possible, but where observable market data are not available, judgment is required to establish fair values. The judgments include considerations of liquidity and model inputs such as volatility for longer dated derivatives and discount rates, prepayment rates and default rate assumptions for asset backed securities. The management believes that the chosen valuation techniques and assumptions used are appropriate in determining the fair value of unquoted financial instruments.

5 SIGNIFICANT ACCOUNTING JUDGEMENTS, ESTIMATES AND ASSUMPTIONS (continued)

b) Classification and measurement of financial assets
The classification and measurement of the financial assets depend on the management's business model for managing its financial assets and on the contractual cash flow characteristics of the financial asset assessed. Management is satisfied that the Branches' investments in securities are appropriately classified and measured.

c) Impairment of financial assets
Key concepts in IFRS 9 that have the most significant impact and require a high level of judgment, as considered by the Branches, are:

Assessment of Significant Increase in Credit Risk (SICR)
As per IFRS 9, SICR can be assessed at a collective/portfolio level if common risk characteristics are shared. Any instruments that are assessed collectively must possess shared credit risk characteristics. The Branches has followed the following criteria to determine the ECL calculation at collective basis vs on individual basis:

- Retail Portfolio: on collective basis based on the product level (Loans, Housing Loans, Car Loans, and Credit Cards).
- Corporate Portfolio: individual basis at customer/ facility level.
- Financial Institutions: individual basis at Bank/ facility level.
- Debt instruments measured at amortized cost: individual level at instrument level.
- Debt instruments measured at fair value through other comprehensive income: individual level at instrument level.

To assess whether the credit risk of a financial asset has increased significantly since origination, the Branches compares the risk of default occurring over the expected life of the financial asset at the reporting date to the corresponding risk of default at origination, using key risk indicators that are used in the Branches' existing risk management processes.

The Branches' assessment of significant increase in credit risk is performed periodically for each individual exposure based on three factors. If any of the following factors indicates that a significant increase in credit risk has occurred, the instrument will be moved from Stage 1 to Stage 2:

1. Significant increases in credit risk based on movement in the customer's internal credit grade and the related PDs relative to initial recognition against established thresholds.
2. Restructuring and/or Rescheduling on the customers' accounts/ facilities during the assessment period is considered as indicator for SICR.
3. Instruments which are 90 days past due have experienced a significant increase in credit risk as per the Branches' policies. Central Bank of UAE in its instructions requested to apply 90 days past due for significant increase in credit risk.

The Branches also consider other qualitative and quantitative reasonable and supportable forward-looking information to firm its assessment of significant increase in credit risk.

Movements between Stage 2 and Stage 3 are based on whether financial assets are credit-impaired as at the reporting date. The determination of credit-impairment under IFRS 9 will be similar to the individual assessment of financial assets for objective evidence of impairment under IAS 39, as mentioned in the "Definition of default" below.

Curing criteria – upward ECL stage movement
The curing criteria is in line with UAE Central Bank IFRS 9 guidelines and is considered based on the combination of the following qualitative factors:

- DPD movement
- Probationary period
- Notches of ratings upward movement

From Stage 2 (Lifetime ECL) to Stage 1 (12-month ECL)
- Where there is an evidence of a significant reduction in credit risk, financial instruments are monitored for probationary period of 12 months to confirm if the risk of default has decreased sufficiently before upgrading such exposures from stage 2 to stage 1.
- DPD shall be ≤ 30 days over the last 12 months period; and / or
- Upward movement of risk ratings is reflected as per internally defined criteria.

5 SIGNIFICANT ACCOUNTING JUDGEMENTS, ESTIMATES AND ASSUMPTIONS (continued)

c) Impairment of financial assets (continued)

Curing criteria – upward ECL stage movement (continued)

From Stage 3 (Lifetime ECL – credit impaired) to Stage 2 (Lifetime ECL – not credit impaired)

- Where there is an evidence of a significant reduction in credit risk, financial instruments are monitored for a probationary period of 3 months or 3 installments, whichever is longer, to confirm if the risk of default has decreased sufficiently before upgrading such exposures from stage 3 to stage 2.
- DPD shall be <90 days over the last 3 months period; and/or
- Upward movement of risk ratings is reflected as per internally defined criteria.

An exposure cannot be upgraded from Stage 3 to Stage 1 directly and should be upgraded to Stage 2 initially before upgrading to Stage 1 based on the above-mentioned criteria.

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

The measurement of expected credit losses for each stage and the assessment of significant increases in credit risk considers information about past events and current conditions as well as reasonable and supportable forecasts of future events and economic conditions. The estimation and application of forward-looking information will require significant judgment.

PD, Loss Given Default (LGD) and Exposure At Default (EAD) inputs used to estimate Stage 1 and Stage 2 credit loss allowances are modelled based on the macroeconomic variables (or changes in macroeconomic variables) that are most closely correlated with credit losses in the relevant portfolio.

Each macroeconomic scenario used in expected credit loss calculation will have forecasts of the relevant macroeconomic variables.

The estimation of expected credit losses in Stage 1 and Stage 2 will be a discounted probability-weighted estimate that considers a minimum of three future macroeconomic scenarios.

The base case scenario will be based on macroeconomic forecasts (e.g.: GDP growth rate and international oil prices indices). Upside and downside scenarios will be set relative to base case scenario based on reasonably possible alternative macroeconomic conditions.

Scenarios will be probability-weighted according to the best estimate of their relative likelihood based on historical frequency and current trends and conditions. Probability weights will be updated on a quarterly basis. All scenarios considered will be applied to all portfolios subject to expected credit losses with the same probabilities.

Definition of default

The definition of default used in the measurement of expected credit losses and the assessment to determine movement between stages will be consistent with the definition of default used for internal credit risk management purposes. IFRS 9 does not define default but contains a rebuttable presumption that default has occurred when an exposure is greater than 90 days past due.

Notwithstanding the above, the classification of credit facilities is governed by the Central Bank of UAE regulations.

The Branches has set out the definition of default where a default is considered to have occurred when either or both of the two following events have taken place:

- The obligor is considered unlikely to pay its credit obligations in full; and
- The obligor is past due for 90 days or more on any material credit obligation.

Expected Life

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

5 SIGNIFICANT ACCOUNTING JUDGEMENTS, ESTIMATES AND ASSUMPTIONS (continued)

d) Derivative financial instruments
Subsequent to initial recognition, the fair values of derivative financial instruments measured at fair value are generally obtained by reference to quoted market prices, discounted cash flow models and recognised pricing models as appropriate. When prices are not available, fair values are determined by using valuation techniques which refer to observable market data. These include comparison with similar instruments where market observable prices exist, discounted cash flow analysis, option pricing models and other valuation techniques commonly used by market participants. The main factors which management considers when applying a model are:

- The likelihood and expected timing of future cash flows on the instrument. These cash flows are usually governed by the terms of the instrument, although management judgment may be required in situations where the ability of the counterparty to service the instrument in accordance with the contractual terms is in doubt; and
- An appropriate discount rate of the instrument. Management determines this rate, based on its assessment of the appropriate spread of the rate for the instrument over the risk-free rate. When valuing instruments by reference to comparable instruments, management takes into account the maturity, structure and rating of the instrument with which the position held is being compared. When valuing instruments on a model basis using the fair value of underlying components, management considers, in addition, the need for adjustments to take account of a number of factors such as bid-offer spread, credit profile, servicing costs of portfolios and model uncertainty.

e) Useful lives of property and equipment
The cost of property and equipment is depreciated over the estimated useful life, which is based on expected usage of the asset, expected physical wear and tear, which depends on operational factors. The management has not considered any residual value as it is deemed immaterial.

f) Tax liabilities and deferred tax assets
The deferred tax asset relating to the Branches' operations in the UAE primarily reflected the deductible temporary differences in respect of impairment allowances on loans and advances and interest in suspense and changes in fair value of investments carried at fair value through other comprehensive income.

Deductions for loan impairments for UAE tax purposes generally occur when the impaired loan is specifically approved for deduction by UAE tax authority, written off, or if earlier, when the impaired loan is sold. The tax deduction often occurs in periods subsequent to that in which the impairment is recognised for accounting purposes.

As a result, the amount of the associated deferred tax asset should generally move in line with the impairment allowance balance.

Deferred tax assets and liabilities are recorded using substantially enacted tax rates for the effect of temporary differences between book and tax bases of assets and liabilities. Based on available evidence, it is assessed whether it is probable that all or a portion of the deferred tax assets will be realized, or will not be realised. The main factors which are considered include future earnings potential; cumulative losses in recent years; tax-planning strategies that would, if necessary, be implemented, and the nature of the income that can be used to realize the deferred tax asset.

g) Employees end of service benefits
The Branches' carried provision for employees end of service benefits based on applicable laws and regulations. The management has determined that provision for employees end of service benefits using actuarial valuation would not be significantly different than carrying amount as the net impact of increase in salaries and discount rate would not be material.

h) Determination of the lease term for lease contracts with renewal and termination options (Bank as a lessee)
The Bank determines the lease term as the non-cancellable term of the lease, together with any periods covered by an option to extend the lease if it is reasonably certain to be exercised, or any periods covered by an option to terminate the lease, if it is reasonably certain not to be exercised.

The Bank has several lease contracts that include extension and termination options. The Bank applies judgement in evaluating whether it is reasonably certain whether or not to exercise the option to renew or terminate the lease. That is, it considers all relevant factors that create an economic incentive for it to exercise either the renewal or termination. After the commencement date, the Bank reassesses the lease term if there is a significant event or change in circumstances that is within its control that affects its ability to exercise or not to exercise the option to renew or to terminate (e.g., construction of significant leasehold improvements or significant customisation of the leased asset).

5 SIGNIFICANT ACCOUNTING JUDGEMENTS, ESTIMATES AND ASSUMPTIONS (continued)

i) Estimating the incremental borrowing rate

The Bank cannot readily determine the interest rate implicit in the lease, therefore, it uses its incremental borrowing rate (‘IBR’) to measure lease liabilities. The IBR is the rate of interest that the Bank would have to pay to borrow over a similar term, and with a similar security, the funds necessary to obtain an asset of a similar value to the right-of-use asset in a similar economic environment. The IBR therefore reflects what the Bank ‘would have to pay’, which requires estimation when no observable rates are available or when they need to be adjusted to reflect the terms and conditions of the lease. The Bank estimates the IBR using observable inputs (such as market interest rates) when available and is required to make certain entity-specific adjustments.

j) Effective Interest Rate (EIR) method

The Bank’s EIR method recognises interest income using a rate of return that represents the best estimate of a constant rate of return over the expected behavioural life of loans and deposits and recognises the effect of potentially different interest rates charged at various stages and other characteristics of the product life cycle (including prepayments and penalty interest and charges). This estimation, by nature, requires an element of judgement regarding the expected behaviour and life-cycle of the instruments, as well expected changes to base rate and other fee income/expense that are integral parts of the instrument.

k) Provisions and other contingent liabilities

The Bank operates in a regulatory and legal environment that, by nature, has a heightened element of litigation risk inherent to its operations. As a result, it is involved in various litigation, arbitration and regulatory investigations and proceedings both in Goodland and in other jurisdictions, arising in the ordinary course of the Bank’s business.

When the Bank can reliably measure the outflow of economic benefits in relation to a specific case and considers such outflows to be probable, the Bank records a provision against the case. Where the probability of outflow is considered to be remote, or probable, but a reliable estimate cannot be made, a contingent liability is disclosed. However, when the Bank is of the opinion that disclosing these estimates on a case-by-case basis would prejudice their outcome, then the Bank does not include detailed, case-specific disclosers in its financial statements.

Given the subjectivity and uncertainty of determining the probability and amount of losses, the Bank takes into account a number of factors including legal advice, the stage of the matter and historical evidence from similar incidents. Significant judgement is required to conclude on these estimates.

For further details on provisions and other contingencies see Notes 16 and 19.

6 CASH AND BALANCES WITH THE CENTRAL BANK OF UAE

	2020	*2019*
	AED 000	*AED 000*
Cash in hand	**62,704**	67,929
Balances with the Central Bank of UAE:		
- Certificates of deposit	**120,000**	1,660,000
- Overnight deposit facility	**2,575,000**	-
- Clearing account	**82,558**	359,273
- Statutory reserve	**773,592**	958,913
- Islamic commodity murabaha	**55,000**	210,000
	3,668,854	3,256,115

The statutory reserve represents mandatory interest free reserve deposits, which are not available to finance the Bank’s day to day operations and cannot be withdrawn without the prior approval of the Central Bank of UAE. The level of reserves required changes periodically in accordance with the directives of the Central Bank of UAE.

Cash and balances with the Central Bank of UAE were classified as Stage 1 financial assets throughout the period.

7 DUE FROM BANKS

	2020 AED 000	*2019 AED 000*
Time	**3,743,110**	3,280,093
Demand	**208,118**	148,340
	3,951,228	3,428,433
Less: Allowance for expected credit losses (see note a below)	**(11,411)**	(8,371)
	3,939,817	3,420,062

a) An analysis of change in the ECL allowance related to due from banks is as follows:

	Stage 1 AED 000	***Stage 2 AED 000***	***Stage 3 AED 000***	***Total AED 000***
ECL allowance at 1 January 2020	**8,362**	**9**	**-**	**8,371**
Net impairment charge (Note 25 (iii))	**2,757**	**283**	**-**	**3,040**
ECL allowance at 31 December 2020	**11,119**	**292**	**-**	**11,411**

	Stage 1 AED 000	*Stage 2 AED 000*	*Stage 3 AED 000*	*Total AED 000*
ECL allowance at 1 January 2019	8,808	1,151	-	9,959
Net reversals (Note 25 (iii))	(446)	(1,142)	-	(1,588)
ECL allowance at 31 December 2019	8,362	9	-	8,371

b) Following is the geographical distribution of due from banks:

	2020 AED'000	*2019 AED'000*
Banks in the U.A.E.	**2,466,246**	2,069,188
Banks abroad	**1,484,982**	1,359,245
Less: Allowance for expected credit losses	**(11,411)**	(8,371)
	3,939,817	3,420,062

c) As at 31 December 2020, there were time deposits with an original maturity of more than 3 months of AED 1,633.7 million (2019: AED 632.4 million)

d) The table below shows the credit quality and the maximum exposure to credit risk based on the Bank's internal credit rating system and year-end stage classification. The amounts presented are gross of allowance for ECL.

7 DUE FROM BANKS (continued)

In AED'000s
31 December 2020

Internal rating grade	***Stage 1***	***Stage 2***	***Stage 3***	***Total***
Performing				
High grade	**2,917,737**	**-**	**-**	**2,917,737**
Standard grade	**775,598**	**-**	**-**	**775,598**
Sub-standard grade	**99,034**	**39,924**	**-**	**138,958**
Low grade	**118,927**	**8**	**-**	**118,935**
Non-performing				
Individually impaired	**-**	**-**	**-**	**-**
Total	**3,911,296**	**39,932**	**-**	**3,951,228**

In AED'000s
31 December 2019

Internal rating grade	*Stage 1*	*Stage 2*	*Stage 3*	*Total*
Performing				
High grade	2,132,620	-	-	2,132,620
Standard grade	1,158,976	-	-	1,158,976
Sub-standard grade	97,597	-	-	97,597
Low grade	38,944	296	-	39,240
Non-performing				
Individually impaired	-	-	-	-
Total	3,428,137	296	-	3,428,433

There were no movements between stages during the years ended 31 December 2020 and 2019.

8 LOANS AND ISLAMIC FINANCING RECEIVABLES

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

		2020			*2019*	
	UAE AED 000	***Others AED 000***	***Total AED 000***	*UAE AED 000*	*Others AED 000*	*Total AED 000*
Trade	**1,061,440**	**-**	**1,061,440**	1,178,578	-	1,178,578
Other commercial & business sector	**1,412,329**	**200,671**	**1,613,000**	1,642,980	95,895	1,738,875
Personal	**534,260**	**11,979**	**546,239**	655,099	13,538	668,637
Gross receivables	**3,008,029**	**212,650**	**3,220,679**	3,476,657	109,433	3,586,090
Allowance for impairment						
- Stage 3			**(199,846)**			(180,760)
- Stage 1 & 2			**(184,120)**			(201,480)
Net receivables			**2,836,713**			3,203,850

8 LOANS AND ISLAMIC FINANCING RECEIVABLES (continued)

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

A reconciliation of changes in gross carrying amount and corresponding allowance for ECL by stage for corporate lending is, as follows:

In AED 000	***Stage 1***		***Stage 2***		***Stage 3***		***Total***	
	Gross carrying amount	***ECL***	***Gross carrying amount***	***ECL***	***Gross carrying amount***	***ECL***	***Gross carrying amount***	***Gross carrying ECL***
1 January 2020	**2,181,052**	**73,608**	**1,092,112**	**127,872**	**312,926**	**180,760**	**3,586,090**	**382,240**
Transfers to stage 1	**9,387**	**502**	**(9,387)**	**(502)**	**-**	**-**	**-**	**-**
Transfers to stage 2	**(229,243)**	**(2,488)**	**229,243**	**2,488**	**-**	**-**	**-**	**-**
Transfers to stage 3	**(1,097)**	**(50)**	**(13,778)**	**(5,979)**	**14,875**	**6,029**	**-**	**-**
Net additions /recoveries	**(162,477)**	**(14,231)**	**(185,041)**	**2,900**	**(6,811)**	**15,716**	**(354,329)**	**4,385**
Interest in suspense*	**-**	**-**	**-**	**-**	**(8,423)**	**-**	**(8,423)**	**-**
Amounts written off	**-**	**-**	**-**	**-**	**(2,659)**	**(2,659)**	**(2,659)**	**(2,659)**
At 31 December 2020	**1,797,622**	**57,341**	**1,113,149**	**126,779**	**309,908**	**199,846**	**3,220,679**	**383,966**

In AED 000	*Stage 1*		*Stage 2*		*Stage 3*		*Total*	
	Gross carrying amount	*ECL*	*Gross carrying amount*	*ECL*	*Gross carrying amount*	*ECL*	*Gross carrying amount*	*Gross carrying ECL*
1 January 2019	2,336,962	24,766	1,169,348	184,326	335,447	174,322	3,841,757	383,414
Transfers to stage 1	61,385	219	(61,385)	(219)	-	-	-	-
Transfers to stage 2	(136,369)	(12,943)	136,369	12,943	-	-	-	-
Transfers to stage 3	-	-	(13,599)	(12,943)	13,599	12,943	-	-
Net additions /recoveries	(80,926)	61,566	(138,621)	(56,235)	(17,185)	(38)	(236,732)	5,293
Interest in suspense*	-	-	-	-	(12,468)	-	(12,468)	-
Amounts written off	-	-	-	-	(6,467)	(6,467)	(6,467)	(6,467)
At 31 December 2019	2,181,052	73,608	1,092,112	127,872	312,926	180,760	3,586,090	382,240

8 LOANS AND ISLAMIC FINANCING RECEIVABLES (continued)

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

*The movement represents the charge of interest on loans and advance classified under stage 3 (previously reported as interest in suspense) and the balance as of 31 December 2020 of such interest (previously reported as interest in suspense) is AED 33,719 thousand (2019: AED 25,296 thousand)

An analysis of risk concentration in gross carrying amounts and corresponding ECL in the loans portfolio by type of lending, industry and geographical location is presented below:

31 December 2020 In AED '000	***Gross carrying amount***				***Allowance for ECL***				***ECL Coverage %***			
	Stage 1	***Stage 2***	***Stage 3***	***Total***	***Stage 1***	***Stage 2***	***Stage 3***	***Total***	***Stage 1***	***Stage 2***	***Stage 3***	***Total***
Loans and advances to customers												
Corporate lending	**1,219,572**	**471,410**	**108,998**	**1,799,980**	**46,867**	**37,868**	**70,783**	**155,518**	**3.8%**	**8.0%**	**64.9%**	**8.6%**
Small business lending	**411,998**	**362,915**	**99,546**	**874,459**	**8,148**	**53,548**	**78,448**	**140,144**	**2.0%**	**14.8%**	**78.8%**	**16.0%**
Consumer lending	**47,143**	**1,938**	**1,209**	**50,290**	**2,072**	**54**	**1,254**	**3,380**	**4.4%**	**2.8%**	**103.7%**	**6.7%**
Residential mortgages	**118,909**	**276,886**	**100,155**	**495,950**	**254**	**35,309**	**49,361**	**84,924**	**0.2%**	**12.8%**	**49.3%**	**17.1%**
Total	**1,797,622**	**1,113,149**	**309,908**	**3,220,679**	**57,341**	**126,779**	**199,846**	**383,966**	**3.2%**	**11.4%**	**64.5%**	**11.9%**

Loans and Islamic financing receivables include Mudaraba financing activities amounting to AED 59.45 million (*2019:* 5.97 *million*) provided through a Shari'a compliant Islamic window.

The provision for expected credit losses of AED 383,966 thousand (2019: AED 382,240 thousand) is after consideration of post-model adjustments (both positive and negative) and management overlays, in relation to data and model limitations as a result of the Covid-19 economic disruption, other early warning procedures of the Bank and the significant uncertainty as a consequence of the Covid-19 pandemic. The adjustments resulting in overlays of AED 71,892 thousand, are based on a combination of industry portfolio level credit risk analysis and an evaluation of ECL coverage at an exposure level after considering the potential severity and duration of the economic disruption and the heightened credit risk of specific sectors and loan classes / segments, such as energy, aviation and hospitality.

9 INVESTMENTS

	2020	*2019*
	AED 000	*AED 000*
At fair value through other comprehensive income		
Equities - unquoted	**1,197**	1,197
Bonds - quoted (refer note 9a) *	**1,788,281**	1,238,941
At amortized cost		
Bonds - quoted (refer note 9b) *	**384,725**	268,780
	2,174,203	1,508,918

* The above investments include bonds guaranteed by foreign governments, other corporates including international banks and financial institutions, denominated in USD and UAE Dirhams.

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

	2020	*2019*
	AED 000	*AED 000*
Interest income and income from Islamic financing (Note 20)	**48,565**	40,737
Realised gain on bonds designated at fair value through OCI	**432**	824

(a) Investments at fair value through OCI

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

Bonds – quoted

	2020	*2019*
	AED 000	*AED 000*
Opening balance	**1,257,393**	948,625
Acquired during the year	**691,027**	525,465
Sold / redeemed during the year	**(169,427)**	(264,832)
Amortisation of premium	**(9,974)**	(9,533)
Realized gain	**432**	824
Fair value movement *	**34,517**	56,844
	1,803,968	1,257,393
Allowances for expected credit losses	**(15,687)**	(18,452)
Closing balance	**1,788,281**	1,238,941

* Fair value movement is after netting reversal of expected credit losses of AED 2,765 thousand (2019: charge of expected credit losses of AED 11,128 thousand) during the year ended 31 December 2020.

9 INVESTMENTS (continued)

(b) Investments at amortised costs

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

Bonds – quoted

	2020 ***AED 000***	*2019* *AED 000*
Opening balance	**269,561**	155,122
Acquired during the year	**178,357**	178,008
Redeemed during the year	**(58,123)**	(62,440)
Amortisation of premium/discount, net	**(4,117)**	(1,129)
	385,678	269,561
Allowances for expected credit losses	**(953)**	(781)
Closing balance	**384,725**	268,780

(c) An analysis of change in the gross carrying amount and the corresponding ECL allowance is as follows:

	Stage 1 ***AED 000***	***Stage 2*** ***AED 000***	***Stage 3*** ***AED 000***	***Total*** ***AED 000***
Gross exposure at 1 January 2020	1,483,408	-	44,743	1,528,151
Net transfers between Stages	(12,249)	12,249	-	-
Net additions / (disposals)	660,908	12,314	(10,530)	662,692
At 31 December 2020	**2,132,067**	**24,563**	**34,213**	**2,190,843**

	Stage 1 ***AED 000***	***Stage 2*** ***AED 000***	***Stage 3*** ***AED 000***	***Total*** ***AED 000***
ECL allowance at 1 January 2020	2,997	-	16,236	19,233
Net transfers between Stages	(337)	337	-	-
Net charge / (reversals)	1,419	739	(4,751)	(2,593)
Total ECL on investments	**4,079**	**1,076**	**11,485**	**16,640**
Represented for:				
ECL on FVOCI bonds	**3,126**	**1,076**	**11,485**	**15,687**
ECL on amortised cost bonds	**953**	**-**	**-**	**953**
Total ECL on investments	**4,079**	**1,076**	**11,485**	**16,640**

9 INVESTMENTS (continued)

(c) An analysis of change in the gross carrying amount and the corresponding ECL allowance is as follows: (continued)

	Stage 1 AED 000	*Stage 2 AED 000*	*Stage 3 AED 000*	*Total AED 000*
Gross exposure at 1 January 2019	961,023	110,835	44,214	1,116,072
Net transfers between Stages	-	-	-	-
Net additions / (disposals)	522,385	(110,835)	529	412,079
At 31 December 2019	1,483,408	-	44,743	1,528,151

	Stage 1 AED 000	*Stage 2 AED 000*	*Stage 3 AED 000*	*Total AED 000*
ECL allowance at 1 January 2019	806	583	6,428	7,817
Net transfers between Stages	-	-	-	-
Net charge / (reversals)	2,191	(583)	9,808	11,416
Total ECL on investments	2,997	-	16,236	19,233
Less: ECL on FVOCI bonds	(2,216)	-	(16,236)	(18,452)
Closing Balance on 31 December 2019	781	-	-	781

By geographical area (Gross):

	2020 AED'000	*2019 AED'000*
Within UAE	**13,238**	12,750
Outside UAE	**2,177,605**	1,515,401
	2,190,843	1,528,151
Less: Expected credit losses	**(16,640)**	(19,233)
	2,174,203	1,508,918

d) By economic sector:

	2020 AED'000	*2019 AED'000*
Government and public sector	**50,512**	30,587
Governmental related enterprises - Commercial	**12,041**	11,553
Trade and business sector	**918,548**	740,858
Financial institutions	**1,209,742**	745,153
	2,190,843	1,528,151
Less: ECL collective provision	**(16,640)**	(19,233)
	2,174,203	1,508,918

9 INVESTMENTS (continued)

d) By economic sector: (continued)

By credit rating (for debt securities) (Net):

	2020 AED'000	*2019 AED'000*
Rated AAA to A-	**769,523**	493,596
Rated BBB+ to B-	**1,403,483**	1,014,125
Rated CCC+ to D	**-**	-
Unrated	**1,197**	1,197
	2,174,203	1,508,918

The above represents approved rating from External Credit Assessment Institutions (ECAI) as per Basel III Pillar 3 guidelines.

10 PROPERTY AND EQUIPMENT

	Buildings AED 000	*Furniture and office equipment AED 000*	*Computer system AED 000*	*Motor vehicles AED 000*	*Total AED 000*
Cost					
At 1 January 2019	52,184	40,567	13,986	7,761	114,498
Additions	-	5,656	771	-	6,427
Disposals and write-offs	-	(6,988)	(5,703)	-	(12,691)
At 31 December 2019	52,184	39,235	9,054	7,761	108,234
At 1 January 2020	52,184	39,235	9,054	7,761	108,234
Additions	-	1,589	1,046	550	3,185
Disposals and write-offs	(2,231)	(3,601)	(1,970)	(439)	(8,241)
At 31 December 2020	**49,953**	**37,223**	**8,130**	**7,872**	**103,178**
Accumulated Depreciation					
At 1 January 2019	14,863	18,010	12,119	5,630	50,622
Charge for the year	2,110	5,174	1,031	814	9,129
Disposals and write-offs	-	(6,943)	(5,690)	-	(12,633)
At 31 December 2019	16,973	16,241	7,460	6,444	47,118
At 1 January 2020	16,973	16,241	7,460	6,444	47,118
Charge for the year	2,046	5,231	1,266	682	9,225
Disposals and write-offs	(1,154)	(3,597)	(1,970)	(439)	(7,160)
At 31 December 2020	**17,865**	**17,875**	**6,756**	**6,687**	**49,183**
Net book value					
At 31 December 2020	**32,088**	**19,348**	**1,374**	**1,185**	**53,995**
At 31 December 2019	35,211	22,994	1,594	1,317	61,116

11 LEASES

The Bank has lease contracts for branches,ATM and CDM used in its operations. Leases of branches generally have lease terms between 5 and 30 years, CDM have lease term of 7 years while ATM locations generally have shorter lease terms between 1 and 2 years. The Bank's obligations under its leases are secured by the lessor's title to the leased assets. Generally, the Bank is restricted from assigning and subleasing the leased assets. There are several lease contracts that include extension and termination options, which are further discussed below.

Set out below are the carrying amounts of right-of-use assets recognised and the movements during the year ended 31 December 2020:

	2020	*2019*
	AED'000	*AED'000*
Right-of-use assets		
As at 1 January 2020	**126,044**	140,853
Less: Lease modification adjustments	**(732)**	-
Post modification balance	**125,312**	140,853
Additions	**15,126**	-
Depreciation expense	**(16,278)**	(14,809)
	124,160	126,044

Set out below are the carrying amounts of lease liabilities and the movements during the year ended 31 December 2020:

	2020	*2019*
	AED'000	*AED'000*
Lease Liabilities		
As at 1 January 2020	**90,609**	100,101
Lease modification adjustments:	**(732)**	-
Post modification balance	**89,877**	100,101
Accretion of interest (Note 21)	**2,711**	2,725
Additions	**15,126**	-
Payments during the year	**(6,208)**	(12,217)
As at 31 December	**101,505**	90,609

The maturity analysis of lease liabilities are disclosed under liquidity risk management note.

The following are the amounts recognised in profit or loss:

	2020	*2019*
	AED'000	*AED'000*
Depreciation expense of right-of-use assets	**16,278**	14,809
Interest expense on lease liabilities	**2,711**	2,725
Total amount recognised in profit or loss	**18,989**	17,534

The Bank had total cash outflows for leases of AED 6,208 thousand (2019: AED 12,217 thousand) in 2020.

The Bank has several lease contracts that include extension and termination options. These options are negotiated by management to provide flexibility in managing the leased-asset portfolio and align with the Bank's business needs. Management exercises significant judgement in determining whether these extension and termination options are reasonably certain to be exercised.

12 DEFERRED TAX

a) Deferred tax assets are attributable to the following:

	2020	*2019*
	AED 000	*AED 000*
Allowances for expected credit losses	**83,226**	81,387
Others	**121**	106
	83,347	81,493

Movements in temporary differences during the year are as follows:

	Opening balance AED 000	***Recognized in assets AED 000***	***Recognised in profit or loss AED 000***	***Recognised in OCI/ equity AED 000***	***Closing balance AED 000***
2020					
Allowances for loan losses	**81,387**	**153**	**1,686**	**-**	**83,226**
Others	**106**	**-**	**15**	**-**	**121**
	81,493	**153**	**1,701**	**-**	**83,347**

	Opening balance AED 000	*Recognized in assets AED 000*	*Recognised in profit or loss AED 000*	*Recognised in OCI/ equity AED 000*	*Closing balance AED 000*
2019					
Allowances for loan losses	78,133	-	3,254	-	81,387
Others	113	15	(22)	-	106
	78,246	15	3,232	-	81,493

b) Deferred tax liability of AED 15,239 thousand (2019: AED 8,336 thousand) is attributable to the fair value reserve relating to investments carried at fair value through other comprehensive income. The movement in deferred tax liability during the year ended 31 December 2020 represents addition of deferred tax liability of AED 6,903 thousand (2019: AED 8,336 thousand) relating to net changes in fair values of investment classified as FVOCI, net of related changes in allowance for expected credit losses during the year ended 31 December 2020.

13 OTHER ASSETS

	2020	*2019*
	AED 000	*AED 000*
Accrued interest receivable	**43,749**	43,518
Prepayments and deposits	**8,187**	8,717
Asset acquired in settlement of debt	**-**	344
Precious metal - Gold	**4,212**	3,454
Derivatives financial assets	**25**	-
Custodian collection	**4,198**	11,889
Others	**2,549**	1,154
	62,920	69,076

Assets acquired in settlement of debt includes certain assets at year ended 31 December 2020 of AED 5.4 million (2019: AED 16.1 million) which are fully impaired and the impairment allowance on these was AED 5.4 million (2019: AED 16.1 million).

14 DEPOSITS FROM CUSTOMERS

	2020	*2019*
	AED 000	*AED 000*
Business accounts		
Demand deposits	**4,553,994**	3,646,797
Time deposits	**942,810**	862,796
Call deposits	**784,517**	667,426
Savings deposits	**80,344**	48,758
Margin deposits	**126,113**	97,068
	6,487,778	5,322,845
Individual customers		
Demand	**1,629,654**	1,378,543
Time deposits	**1,586,599**	1,911,421
Call deposits	**308,488**	317,562
Savings deposits	**870,110**	846,027
Margin deposits	**713**	7,699
	4,395,564	4,461,252
Total	**10,883,342**	9,784,097

Deposits from customers include Islamic customer deposits amounting to AED 451.5 million (2019: 211.8 million) undertaken through a Sharia'a compliant Islamic window.

15 DUE TO BANKS

	2020	*2019*
	AED 000	*AED 000*
Demand deposits (current)	**43,501**	141,245

There are no interest paid on balances due to banks during the years ended 31 December 2020 and 2019.

16 OTHER LIABILTIES

	2020	*2019*
	AED 000	*AED 000*
Accrued interest payable	**10,918**	22,316
Staff terminal benefits	**37,400**	36,332
Accrued expenses payable	**4,024**	4,624
Commission received in advance	**1,962**	468
Tax payable	**27,927**	39,256
Bills payable	**22,041**	45,994
Provision – off balance sheet	**6,230**	-
Others	**64,998**	56,204
	175,500	205,194

Others included overdue bills and other payables of AED 59,462 thousand (2019: AED 47,023 thousand) remained unclaimed by the counterparties.

17 ALLOCATED CAPITAL

The allocated capital represents the deposit of AED 100 million contributed by the Head Office as assigned capital for the UAE branches.

18 LEGAL RESERVE

In accordance with Federal Law No. 2 of 2015, 10% of the net profit for the year should be transferred to a non-distributable legal reserve, until such time as this reserve equals 50% of the allocated capital. No such transfers were made during the years 2020 and 2019, as reserves already equals 50% of the allocated capital.

19 CONTINGENT LIABILITIES AND OTHER COMMITMENTS

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

		2020 ***AED 000***	*2019* *AED 000*
a)	Direct credit substitutes including general guarantees of indebtedness and standby letters of credit serving as financial guarantees for loans and securities	**190,691**	180,185
b)	Transaction-related contingencies including performance bonds, bid bonds and standby letters of credit related to particular transactions	**131,367**	177,131
c)	Short-term self-liquidating trade-related contingencies arising from the movement of goods, such as documentary credits where the underlying shipment is used as security	**296,268**	170,797
		618,326	528,113

19 CONTINGENT LIABILITIES AND OTHER COMMITMENTS (continued)

a) An analysis of changes in the gross balance of off-balance sheet exposures is as follows:

In AED '000

	Stage 1		***Stage 2***		***Stage 3***		***Total***	
	Outstanding exposure	***ECL***	***Outstanding exposure***	***ECL***	***Outstanding exposure***	***ECL***	***Outstanding exposure***	***ECL***
1 January 2020	**448,165**	**3,233**	**77,322**	**1,313**	**2,626**	**-**	**528,113**	**4,546**
Transfers to Stage 1	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**
Transfers to Stage 2	**(1,728)**	**(94)**	**1,728**	**94**	**-**	**-**	**-**	**-**
Transfers to Stage 3	**-**	**-**	**(3)**	**-**	**3**	**-**	**-**	**-**
Other movement	**91,590**	**(324)**	**(1,377)**	**58**	**-**	**1,950**	**90,213**	**1,684**
At 31 December 2020	**538,027**	**2,815**	**77,670**	**1,465**	**2,629**	**1,950**	**618,326**	**6,230**

In AED '000

	Stage 1		*Stage 2*		*Stage 3*		*Total*	
	Outstanding exposure	*ECL*	*Outstanding exposure*	*ECL*	*Outstanding exposure*	*ECL*	*Outstanding exposure*	*ECL*
1 January 2019	507,171	1,965	127,604	1,601	2,859	-	637,634	3,566
Transfers to Stage 1	17,291	258	(17,291)	(258)	-	-	-	-
Transfers to Stage 2	-	-	-	-	-	-	-	-
Transfers to Stage 3	-	-	-	-	-	-	-	-
Other movement	(76,297)	1,010	(32,991)	(30)	(233)	-	(109,521)	980
At 31 December 2019	448,165	3,233	77,322	1,313	2,626	-	528,113	4,546

20 INTEREST INCOME AND INCOME FROM ISLAMIC FINANCING

	2020	*2019*
	AED 000	*AED 000*
Interest income calculated using the effective interest method		
Loans and receivables	**166,526**	196,556
Certificates of deposits with U.A.E. Central Bank	**16,996**	38,827
Due from Head Office, branches abroad and associates	**108**	361
Due from Banks	**37,247**	74,916
Investment securities	**48,565**	40,737
	269,442	351,397

This includes income from Islamic financing amounting to AED 8.4 million (2019: 7.8 million) for the year ended 31 December 2020.

21 INTEREST EXPENSE AND DISTRIBUTION TO ISLAMIC DEPOSITORS

	2020	*2019*
	AED 000	*AED 000*
Interest expense calculated using the effective interest method		
Due to banks	**152**	115
Deposit from customers	**23,768**	33,367
Due to Head Office, branches abroad and associates	**254**	420
Finance cost on leased liabilities (Note 11)	**2,711**	2,725
	26,885	36,627

This includes distribution to Islamic depositors amounting to AED 0.651 million (2019: 1.039 million) for the year ended 31 December 2020.

22 FEE AND COMMISSION INCOME (NET)

	2020	*2019*
	AED’000	*AED’000*
Commission income	**65,659**	65,512
Commission expense	**(3,342)**	(3,366)
	62,317	62,146

23 OTHER INCOME

	2020	*2019*
	AED 000	*AED 000*
Foreign exchange income	**34,327**	31,365
Telex charges recovery	**19,245**	19,453
Courier charges recovery	**6,828**	6,374
Insurance charges recovery	**474**	570
Other miscellaneous income	**8,797**	10,851
Commission expense	**(606)**	(715)
	69,065	67,898

24 GENERAL AND ADMINISTRATIVE EXPENSES

	2020	*2019*
	AED 000	*AED 000*
Staff salaries and benefits	**133,272**	134,279
Depreciation	**9,225**	9,129
Telephone, telex and courier expenses	**6,824**	6,581
Head office charges	**17,007**	19,335
Depreciation of right-of-use assets	**16,278**	14,809
Operating leases	**2,312**	3,503
Repairs and maintenance	**5,496**	5,846
Printing and stationery	**822**	943
Insurance and travel	**1,943**	3,319
Operational losses	**24**	(5)
Other miscellaneous expenses	**48,711**	50,431
	241,914	248,170

The total numbers of employees as at 31 December 2020 were 451 (2019: 459) of which 109 (2019: 109) were UAE Nationals.

25 CREDIT LOSS EXPENSE ON FINANCIAL ASSETS

The charge for the net impairment allowances in the statement of comprehensive income comprises of the following:

	2020	*2019*
	AED'000	*AED'000*
Provision for expected credit losses:		
Specific (Stage 3) - see i below	**18,944**	22,713
12 moths ECL (Stage 1) and Lifetime ECL (Stage 2) - see ii and iii below	**(7,923)**	(4,564)
	11,021	18,149

i) *Provisions against impaired loans and advances, net (Stage 3)/Specific provision*

	2020	*2019*
	AED'000	*AED'000*
Charge for specific impairment allowance – loans and advances*	**15,716**	12,905
Charge for specific impairment allowance - investments	**(4,751)**	9,808
Charge for specific impairment allowance – indirect facilities	**1,950**	-
	12,915	22,713

ii) *Provisions against loans and advances, net (12 moths ECL (Stage 1) & Lifetime ECL (Stage 2))*

	2020	*2019*
	AED'000	*AED'000*
Charge for impairment allowance – loans and advances*	**(11,331)**	(7,612)

*The movement in impairment allowance also includes transfer of impairment allowance of AED 6,029 thousand (from Stage 1 to Stage 3 of AED 50 thousand, from Stage 2 to Stage 3 of AED 5,979 thousand).

25 CREDIT LOSS EXPENSE ON FINANCIAL ASSETS (continued)

iii) *Expected credit losses (Stage 1 and 2)*

	2020 AED'000	*2019 AED'000*
Investments	**2,158**	1,608
Due from banks (Note 7 (a))	**3,040**	(1,588)
Charge for specific impairment allowance - other assets	**(41)**	3,028
Indirect facilities	**4,280**	-
	9,437	3,048

The table below shows the ECL charges on financial instruments for the year recorded in the statement of profit or loss and other comprehensive income:

2020 **In AED '000s**	***Stage 1***	***Stage 2***	***Stage 3***	***Total***
Due from banks	**2,757**	**283**	**-**	**3,040**
Loans and advances to customers	**(14,231)**	**2,900**	**15,716**	**4,385**
Debt instruments measured at FVOCI	**1,247**	**739**	**(4,751)**	**(2,765)**
Debt instruments measured at amortised cost	**172**	**-**	**-**	**172**
Other assets	**(41)**	**-**	**-**	**(41)**
Indirect facilities	**2,815**	**1,465**	**1,950**	**6,230**
Total Impairment loss	**(7,281)**	**5,387**	**12,915**	**11,021**

2019 In AED '000s	*Stage 1*	*Stage 2*	*Stage 3*	*Total*
Due from banks	(446)	(1,142)	-	(1,588)
Loans and advances to customers	48,842	(56,454)	12,905	5,293
Debt instruments measured at FVOCI	1,498	(988)	9,808	10,318
Debt instruments measured at amortised cost	693	405	-	1,098
Other Assets	3,028	-	-	3,028
Indirect facilities	-	-	-	-
Total Impairment loss	53,615	(58,179)	22,713	18,149

26 TAXATION

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

	2020 AED 000	*2019 AED 000*
Current tax expense	**27,927**	39,256
Additional tax paid for prior year	**99**	186
Deferred tax expense		
- Reversal of temporary differences	**(1,701)**	(3,247)
Total tax expense for the year	**26,325**	36,195

26 TAXATION (continued)

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

Reconciliation of effective tax rate:

	2020 ***AED 000***	*2019* *AED 000*
Profit for the year before taxation	**121,004**	178,925
Tax calculated using UAE tax rates (20%)	**24,201**	35,785
Prior year tax	**99**	186
Tax exempt income	**(1,030)**	(2,668)
Non-deductible expenses	**3,055**	2,892
Total tax expense in statement of profit or loss and other comprehensive income	**26,325**	36,195
Effective tax rate	**21.76%**	20.23%

27 DERIVATIVES

In the ordinary course of business, the Branches enter into various types of transactions that involve derivative financial instruments. A derivative financial instrument is a financial contract between two parties where payments are dependent upon movements in price in one or more underlying financial instrument, reference rate or index. Derivative financial instruments include forwards, futures, swaps and options. During the year, the Branches entered into forward foreign exchange.

The table below shows the positive and negative fair values of derivative financial instruments, which are equivalent to the market values, together with the notional amounts. The notional amount is the amount of a derivative's underlying asset, 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.

At 31 December 2020			***Notional amounts by term to maturity***		
	Positive fair value AED'000 (Note 12)	***Notional amount AED'000***	***Within 3 months AED'000***	***3-12 months AED'000***	***1-5 years AED'000***
Foreign exchange forward contracts	**25**	**183,675**	**183,675**	**-**	**-**

At 31 December 2019			*Notional amounts by term to maturity*		
	Positive fair value AED'000 (Note 12)	*Notional amount AED'000*	*Within 3 months AED'000*	*3-12 months AED'000*	*1-5 years AED'000*
Foreign exchange forward contracts	-	493	493	-	-

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

28 RELATED PARTY TRANSACTIONS

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

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

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

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

	2020 ***AED 000***	*2019* *AED 000*
Due from		
- Head office	**11,692**	69,052
- Subsidiaries of Habib Group	**25,835**	30,546
	37,527	99,598
Due to		
- Head office	**45,043**	1,845
- Branches (other than UAE)	**681**	1,572
- Subsidiaries of Habib Group	**6,439**	5,381
	52,163	8,798
Loan to HBZ Services LLC	**24,778**	26,219
Deposit from HBZ Services LLC	**6,256**	14,001

Due from Head Office and its branches abroad are classified as Stage 1 financial assets. No allowance for impairment has been recognized in respect of due from related parties, including loans and Islamic financing receivables from related parties (2019: nil).

Transactions with Related Parties

	2020 ***AED 000***	*2019* *AED 000*
Interest income (including on loan to HBZ Services LLC)	**1,536**	1,899
Interest expense	**254**	420
Head office charges	**17,007**	19,335
Expenses reimbursed to HBZ Services LLC	**29,612**	27,626

28 RELATED PARTY TRANSACTIONS (continued)

Deposits from related parties

	2020 ***AED 000***	*2019* *AED 000*
Deposits at 1 January	**153,584**	146,283
Deposits received and interest rollover during the year	**183,403**	348,587
Deposits repaid during the year	**(173,444)**	(341,286)
Deposits at 31 December	**163,543**	153,584
Interest expense for the Bank during the year	**1,340**	2,429

Key management compensations

	2020 ***AED 000***	*2019* *AED 000*
Short term employment benefits	**3,287**	3,218
Post-employment benefits	**113**	19

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

Collateral given by related parties
Related parties have provided collaterals in form of guarantees against three loan facilities.

29 GEOGRAPHICAL CONCENTRATION OF ASSETS

	Loans AED 000	*Debt securities AED 000*	*OTC derivatives AED 000*	*Total funded AED 000*	*Other off balance sheet exposures AED 000*	*Total non funded AED 000*	*Total AED 000*
31 December 2020							
UAE	**2,624,244**	**13,238**	**77,148**	**9,130,228**	**581,060**	**658,208**	**9,788,436**
GCC excluding UAE	**8**	**-**	**-**	**19,151**	**-**	**-**	**19,151**
Arab League (Excluding GCC)	**10,442**	**-**	**-**	**10,442**	**-**	**-**	**10,442**
Asia	**155,277**	**569,752**	**-**	**1,345,864**	**26,502**	**26,502**	**1,372,366**
Africa	**5,887**	**-**	**-**	**44,925**	**3,587**	**3,587**	**48,512**
North America	**2,328**	**635,765**	**-**	**678,793**	**-**	**-**	**678,793**
Caribbean	**10**	**-**	**-**	**10**	**-**	**-**	**10**
Europe	**38,517**	**887,827**	**106,527**	**1,715,341**	**7,094**	**113,621**	**1,828,962**
Australia	**-**	**67,621**	**-**	**81,169**	**83**	**83**	**81,252**
Total	**2,836,713**	**2,174,203**	**183,675**	**13,025,923**	**618,326**	**802,001**	**13,827,924**

29 GEOGRAPHICAL CONCENTRATION OF ASSETS (continued)

	Loans	*Debt Securities AED 000*	*OTC Derivatives AED 000*	*Total funded AED 000*	*Other off balance sheet exposures AED 000*	*Total Non Funded AED 000*	*Total AED 000*
31 December 2019							
UAE	3,096,103	12,749	493	8,837,699	476,097	476,590	9,314,289
GCC excluding UAE	-	-	-	60,648	-	-	60,648
Arab League (Excluding GCC)	-	-	-	-	-	-	-
Asia	100,938	475,472	-	1,271,533	32,656	32,656	1,304,189
Africa	855	-	-	4,861	-	-	4,861
North America	-	566,323	-	600,885	-	-	600,885
Europe	5,954	454,374	-	1,121,450	19,360	19,360	1,140,810
Australia	-	-	-	4,902	-	-	4,902
Total	3,203,850	1,508,918	493	11,901,978	528,113	528,606	12,430,584

30 FINANCIAL ASSETS AND LIABILITIES

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

At 31 December 2020

	Fair value through profit or loss AED 000	***Fair value through other comprehensive income AED 000***	***Amortised cost AED 000***	***Total carrying amount AED 000***	***Fair value AED 000***
Cash and balances with UAE Central Bank	**-**	**-**	**3,668,854**	**3,668,854**	**3,688,854**
Due from banks	**-**	**-**	**3,939,817**	**3,939,817**	**3,939,817**
Due from Head office, Branches abroad and associates	**-**	**-**	**37,527**	**37,527**	**37,527**
Loans and receivables	**-**	**-**	**2,836,713**	**2,836,713**	**2,836,713**
Customers' indebtedness for acceptances	**-**	**-**	**44,387**	**44,387**	**44,387**
Investments	**-**	**1,789,478**	**384,725**	**2,174,203**	**2,206,916**
Other assets	**25**	**-**	**57,722**	**57,747**	**57,747**
	25	**1,789,478**	**10,969,745**	**12,759,248**	**12,791,961**
Liabilities, capital and reserves					
Deposits from customers	**-**	**-**	**10,883,342**	**10,883,342**	**10,883,342**
Due to banks	**-**	**-**	**43,501**	**43,501**	**43,501**
Due to Head office, Branches abroad and associates	**-**	**-**	**52,163**	**52,163**	**52,163**
Liabilities under acceptances	**-**	**-**	**44,387**	**44,387**	**44,387**
Lease liabilities	**-**	**-**	**101,505**	**101,505**	**101,505**
Other liabilities	**-**	**-**	**108,211**	**108,211**	**108,211**
	-	**-**	**11,233,109**	**11,233,109**	**11,233,109**

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

At 31 December 2019

	Fair value through profit or loss AED 000	*Fair value through other comprehensive income AED 000*	*Amortised cost AED 000*	*Total carrying amount AED 000*	*Fair value AED 000*
Assets					
Cash and balances with UAE Central Bank	-	-	3,256,115	3,256,115	3,256,115
Due from banks	-	-	3,420,062	3,420,062	3,420,062
Due from Head office, Branches abroad and associates	-		99,598	99,598	99,598
Loans and receivables	-	-	3,203,850	3,203,850	3,203,850
Customers' indebtedness for acceptances	-	-	75,706	75,706	75,706
Investments	-	1,240,138	268,780	1,508,918	1,511,284
Other assets	-	-	62,431	62,431	62,431
	-	1,240,138	10,386,542	11,626,680	11,629,046

30 FINANCIAL ASSETS AND LIABILITIES (continued)

At 31 December 2019

	Fair value through profit or loss AED 000	*Fair value through other comprehensive income AED 000*	*Amortised cost AED 000*	*Total carrying amount AED 000*	*Fair value AED 000*
Liabilities, capital and reserves					
Deposits from customers	-	-	9,784,097	9,784,097	9,784,097
Due to banks	-	-	141,245	141,245	141,245
Due to Head office, Branches abroad and associates	-	-	8,798	8,798	8,798
Liabilities under acceptances	-	-	75,706	75,706	75,706
Lease liabilities	-	-	90,609	90,609	90,609
Other liabilities	-	-	129,138	129,138	129,138
	-	-	10,229,593	10,229,593	10,229,593

31 FAIR VALUE HIERARCHY

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

	Level 1 AED 000	***Level 2 AED 000***	***Level 3 AED 000***	***Total AED 000***
At 31 December 2020				
Financial assets				
Investments	**1,788,281**	**-**	**1,197**	**1,789,478**
Derivatives financial assets (Forward foreign exchange contracts)	**-**	**25**	**-**	**25**
	1,788,281	**25**	**1,197**	**1,789,503**
At 31 December 2019				
Financial assets				
Investments	1,238,941	-	1,197	1,240,138
Derivatives financial assets (Forward foreign exchange contracts)	-	-	-	-
	1,238,941	-	1,197	1,240,138

The following table sets out the fair values of financial instruments measured at amortised cost and analyses them by the level in the fair value hierarchy into which each fair value measurement is categorized.

At 31 December 2020	***Level 1 AED'000***	***Level 2 AED'000***	***Level 3 AED'000***	***Fair value AED'000***	***Carrying amount AED'000***
Financial assets					
Investments	**417,438**	**-**	**-**	**417,438**	**384,725**

At 31 December 2019	*Level 1 AED'000*	*Level 2 AED'000*	*Level 3 AED'000*	*Fair value AED'000*	*Carrying amount AED'000*
Investments	271,147	-	-	271,147	268,780

31 FAIR VALUE HIERARCHY (continued)

Fair value hierarchy (continued)
Fair values of all others financial assets and liabilities approximates their carrying value based on the following:

- In respect of those financial assets and financial liabilities measured at amortised cost, which are of short term nature (up to 1 year), management believes that carrying amount is equivalent to its fair value.

- Financing to customers are fair valued based on DCF which takes into account original underlying cash borrower credit grading and expected prepayments. These features are used to estimate expected cash flows and discounted at risk-adjusted rates. However, this technique is subject to inherent limitations, such as estimation of the appropriate risk-adjusted discount rate, and different assumptions and inputs would yield different results.

- Fair values of customer deposits and due to banks is estimated using discounted cash flow techniques, applying the rates that are offered for deposits of similar maturities and terms. The fair value of deposits payable on demand is the amount payable at the reporting date.

32 RISK MANAGEMENT

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

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

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

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

(a) Credit risk

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

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

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

32 RISK MANAGEMENT (continued)

(a) Credit risk (continued)

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

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

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

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

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

<u>Exposure to credit risk</u>
The bank measures its exposure to credit risk by reference to gross carrying amount of financial assets less interest suspended and expected credit allowances, if any.

	Stage 1 ***AED'000***	***Stage 2*** ***AED'000***	***Stage 3*** ***AED'000***	***Total*** ***AED'000***
At 31 December 2020				
Due from banks				
Performing	**3,911,296**	**39,932**	**-**	**3,951,228**
Allowance for impairment losses	**(11,119)**	**(292)**	**-**	**(11,411)**
Net carrying amount	**3,900,177**	**39,640**	**-**	**3,939,817**

	Stage 1 ***AED'000***	***Stage 2*** ***AED'000***	***Stage 3*** ***AED'000***	***Total*** ***AED'000***
Loans and advances				
Performing	**1,797,622**	**1,113,149**	**-**	**2,910,771**
Non-performing	**-**	**-**	**309,908**	**309,908**
Allowance for impairment losses	**(57,341)**	**(126,779)**	**(199,846)**	**(383,966)**
Net carrying amount	**1,740,281**	**986,370**	**110,062**	**2,836,713**

	Stage 1 ***AED'000***	***Stage 2*** ***AED'000***	***Stage 3*** ***AED'000***	***Total*** ***AED'000***
Debt securities				
Performing	**2,135,193**	**25,639**	**-**	**2,160,832**
Non-performing	**-**	**-**	**30,011**	**30,011**
Allowance for impairment losses				
- Investment carried at amortised cost	**(953)**	**-**	**-**	**(953)**
- Investment carried at FVOCI	**(3,126)**	**(1,076)**	**(11,485)**	**(15,687)**
Net carrying amount	**2,131,114**	**24,563**	**18,526**	**2,174,203**

32 RISK MANAGEMENT (continued)

(a) Credit risk (continued)

Exposure to credit risk (continued)

	Stage 1 AED'000	*Stage 2 AED'000*	*Stage 3 AED'000*	*Total AED'000*
At 31 December 2019				
Due from banks				
Performing	3,428,137	296	-	3,428,433
Allowance for impairment losses	(8,362)	(9)	-	(8,371)
Net carrying amount	3,419,775	287	-	3,420,062

	Stage 1 AED'000	*Stage 2 AED'000*	*Stage 3 AED'000*	*Total AED'000*
Loans and advances				
Performing	2,181,052	1,092,112	-	3,273,164
Non-performing	-	-	312,926	312,926
Allowance for impairment losses	(73,608)	(127,872)	(180,760)	(382,240)
Net carrying amount	2,107,444	964,240	132,166	3,203,850

	Stage 1 AED'000	*Stage 2 AED'000*	*Stage 3 AED'000*	*Total AED'000*
Debt securities				
Performing	1,483,408	-	-	1,483,408
Non-performing	-	-	44,743	44,743
Allowance for impairment losses				
- Investment carried at amortised cost	(781)	-	-	(781)
- Investment carried at FVOCI	(2,997)	-	(16,236)	(19,233)
Net carrying amount	1,482,009	-	26,909	1,508,918

Based on internal processes, loans and advances are subject to FAP tagging based on their performance. Performing loans and advances are tagged as FAP '0' and classified under stage 1. Loans with increase in significant credit risks are tagged as FAP '1' and classed under Sage 2. Credit impaired loans and advances are tagged as FAP '2', '3' or '4' (corresponds to substandard, doubtful and loss respectively) and classified as stage 3.

Set out below is an analysis of the gross amounts of impaired loans and advances by FAP tagging:

	2020 AED'000	*2019 AED'000*
Substandard (FAP '2')	**277**	206,168
Doubtful (FAP '3)	**53,007**	44,236
Loss (FAP '4')	**256,624**	62,522
Total	**309,908**	312,926

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

	S&P equivalent rating	***2020 AED 000***	*2019 AED 000*
Low risk	AAA to A-	**769,523**	493,596
Fair risk	BBB+ to B-	**1,403,483**	1,014,125
High risk	CCC+ to D	**-**	-
	Unrated	**1,197**	1,197
		2,174,203	1,508,918

32 RISK MANAGEMENT (continued)

(a) Credit risk (continued)

Set out below is an analysis of the overall provision movement during the year

AED'000	***31 December 2020***				*31 December 2019*			
	Collective 12-month ECL	***Lifetime ECL not credit-impaired***	***Lifetime ECL credit-impaired***	***Total***	*Collective 12-month ECL*	*Lifetime ECL not credit-impaired*	*Lifetime ECL credit-impaired*	*Total*
As at 1 January	**101,019**	**127,881**	**196,996**	**425,896**	56,744	186,279	180,750	423,773
Allowances for impairment made during the year	**(7,281)**	**5,387**	**12,915**	**11,021**	53,615	(58,179)	22,713	18,149
Amounts written-off during the year	**(7,821)**	**-**	**(2,659)**	**(10,480)**	(9,559)	-	(6,467)	(16,026)
Transfers to Stage 1	**501**	**(501)**	**-**	**-**	219	(219)	-	-
Transfers to Stage 2	**(2,824)**	**2,824**	**-**	**-**	-	-	-	-
Transfers to Stage 3	**(50)**	**(5,979)**	**6,029**	**-**	-	-	-	-
As at 31 December	**83,544**	**129,612**	**213,281**	**426,437**	101,019	127,881	196,996	425,896

32 RISK MANAGEMENT (continued)

(a) Credit risk (continued)

Impact on modelled ECL allowance
The Bank's models have been constructed and calibrated using historical trends and correlations as well as forward looking economic scenarios. The severity of the current macro-economic projections and the added complexity caused by the various support schemes and regulatory guidance across the main regions in which the Bank operates could not be reliably modelled for the time being. As a consequence, the existing models may generate results that are either overly conservative or overly optimistic depending on the specific portfolio / segment. As a result, post-model adjustments are needed. Given model changes take a significant amount of time to develop and test and the data limitation issues noted above, the Bank expects that post-model adjustments will be applied for the foreseeable future.

Impairment reserve under the Central Bank of UAE (CBUAE) guidance
The CBUAE has issued its IFRS 9 guidance addressing various implementation challenges and practical implications for Banks adopting IFRS 9 in the UAE ("the guidance").

Since stage 1 and stage 2 ECL held by the bank is higher than the general provision as per the requirements of CBUAE, hence no general impairment reserve is created since 1 January 2019 (first adoption of IFRS 9) till 31 December 2020. Whereas, based on individual comparison of stage 3 ECL as per IFRS 9 and specific provision as required by the CBUAE, the Bank has maintained specific impairment reserve amounting to AED 1,127 thousand as of 31 December 2020 (2019: AED 1,974 thousand) and AED 847 thousand (2019: AED 430 thousand) of the impairment reserve transferred during the year ended 31 December 2020, to retained earnings since not required anymore.

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

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

- Loans and advances which bear normal banking risk, whereby information available to the bank assures repayment as agreed are classified as normal loans;
- Loans and advances which show some weaknesses in the borrower's financial condition and credit worthiness, requiring more than normal attention but not allocation of provisions are classified as Watch list loans;
- Those accounts where adverse factors may hinder repayment or weaken security or lead to some loss are classified as "Substandard accounts". In general these are credit exposures where agreed payments of principal and/or interest are more than 90 consecutive days in arrears;
- Those accounts where full recovery of interest and principal seems doubtful on the basis of information available, leading generally to a loss of part of these loans are classified as "Doubtful accounts"; and
- Those accounts where the bank has exhausted all courses of action available but failed to recover anything or where there is a possibility that nothing shall be recovered are classified as "Loss accounts".

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

During IFRS 9 implementation, the Bank formed a Steering Committee comprising of the appropriate Bank representatives to oversee the process of IFRS 9 implementation.

32 RISK MANAGEMENT (continued)

(a) Credit risk (continued)

Impairment assessment (continued)
Post implementation of IFRS 9, the Bank established principles for ongoing IFRS 9 governance to ensure effective oversight of IFRS 9 processes. An effective IFRS 9 governance structure incorporates Credit, Risk and Finance departments as central support functions for each component of IFRS 9, defines clear process owners and reviewing functions and utilizes the three lines of defense to ensure an effective framework.

Under the IFRS 9 Governance Structure of the Bank, below are the three lines of defense for the key IFRS 9 processes i.e. classification and measurement, staging, impairment and disclosures:

- The process owners i.e. Credit, Financial Control and Treasury form the first line of defense;
- The reviewing/approving functions i.e. Chief Executive Officer, Head of Financial Control, Country Credit Management Committee and Country Asset and Liability Committee form the second line of defense; and
- The independent review functions i.e. Internal Audit and the Audit Committee of the BOD form the third line of defense.

To develop an effective governance framework, roles and responsibilities of the relevant stakeholders are defined to ensure appropriate segregation of duties and accountability.

The CCMC and Head of Credit will be responsible for review of the directive. The directive is subject to amendments if necessary as the Bank's business practice changes, the IFRS 9 standard evolves, market practices develop and regulatory directives are updated / introduced. The roles and responsibilities are updated in the appropriate committee charters and policies of the Bank.

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

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

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

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

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

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

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

32 RISK MANAGEMENT (continued)

(a) Credit risk (continued)

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

	2020			*2019*		
	Loans and receivables AED 000	***Banks & investment AED 000***	***Other Off-balance Sheet exposures AED 000***	*Loans and receivables AED 000*	*Banks & investment AED 000*	*Other Off-balance Sheet exposures AED 000*
Manufacturing	**492,334**	**-**	**165,915**	516,376	-	158,370
Construction & Real Estate	**876,523**	**-**	**23,628**	1,030,679	-	35,617
Trade	**1,064,272**	**-**	**298,252**	1,179,874	-	150,511
Transport and communication	**24,924**	**-**	**7,781**	29,418	-	8,401
Other Services	**44,377**	**-**	**24,563**	83,488	-	54,120
Sovereign	**59,450**	**50,512**	**-**	5,915	30,586	-
Personal	**583,106**	**-**	**2,250**	698,456	-	9,845
Banks & other financial institutions	**109,412**	**5,145,284**	**95,937**	67,179	4,155,136	111,249
Others	**-**	**946,275**	**-**	-	770,862	-
Total gross assets	**3,254,398**	**6,142,071**	**618,326**	3,611,385	4,956,584	528,113

Impairment
The Bank's past due loans and advances (including interest in suspense) by industry segment and geographical location at 31 December 2019, as defined by the Central Bank of the UAE are as follows:

	Past Due but not impaired AED 000	***Individually impaired AED 000***	***Total AED 000***	***ECL AED 000***	***Net impaired assets AED 000***
As at 31 December 2020					
Industry Segment					
Manufacturing	-	48,522	48,522	(48,402)	120
Construction & Real Estate	34,801	123,409	158,210	(85,289)	72,921
Trade	4,905	46,097	51,002	(45,326)	5,676
Transport and Communication	-	479	479	(354)	125
Other Services	3,328	337	3,665	(264)	3,401
Sovereign	-	-	-	-	-
Personal	17,668	120,052	137,720	(50,574)	87,146
Banks & Other Financial Institutions	-	4,731	4,731	(3,356)	1,375
Total	**60,702**	**343,627**	**404,329**	**(233,565)**	**170,764**

	Past Due but not impaired AED 000	***Individually impaired AED 000***	***Total AED 000***	***ECL AED 000***	***Net impaired assets AED 000***
Concentration by Geography					
United Arab Emirates	60,702	343,453	404,155	(233,391)	170,764
Non UAE	-	174	174	(174)	-
Total	**60,702**	**343,627**	**404,329**	**(233,565)**	**170,764**
As at 31 December 2019	117,816	338,222	456,038	(206,056)	249,982

32 RISK MANAGEMENT (continued)

(a) Credit risk (continued)

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

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

	2020 AED'000	*2019 AED'000*
Against loans and advances - Stage 3		
Pledged deposits	**233**	233
Property	**105,948**	136,957
Vehicles	**4,503**	5,840
Total	**110,684**	143,029

	2020 AED'000	*2019 AED'000*
Against loans and advances - Stage 1 and 2		
Pledged deposits	**707,776**	764,063
Debt / Equity securities	**68,025**	64,406
Property	**990,845**	1,171,028
Vehicles	**54,574**	85,463
Bank guarantees	**2,287**	2,332
Total	**1,823,507**	2,087,292

The collateral value represents actual value as of the reporting date, irrespective of customer exposures/outstanding balances.

Analysis of the Bank's exposure at 31 December 2020 based on BASEL III standardised approach is as follows:

		Credit risk mitigation ("CRM")			***Risk weighted assets***
Assets classes	***On & Off Balance sheet gross outstanding AED 000***	***Exposure before CRM AED 000***	***CRM AED 000***	***After CRM AED 000***	***Total AED 000***
As at 31 December 2020					
Claims on sovereign	**3,684,127**	**3,672,642**	**-**	**3,672,642**	**96,216**
Claims on (PSEs)	**31,985**	**31,985**	**-**	**31,985**	**6,397**
Claims on banks	**5,286,393**	**5,286,393**	**(1,155)**	**5,266,253**	**2,289,789**
Claims on securities Firm	**-**	**-**	**-**	**-**	**-**
Claims on corporate	**4,023,585**	**4,023,585**	**(475,330)**	**2,811,769**	**2,094,084**
Claims included in retail portfolio	**261,835**	**261,835**	**(124,618)**	**252,524**	**104,661**
Claims secured by residential property	**650,753**	**650,753**	**(258)**	**650,753**	**527,227**
Claims secured by commercial real estate	**389,183**	**389,183**	**(11,000)**	**389,183**	**378,183**
Past due loans	**408,522**	**171,124**	**(2,024)**	**170,583**	**169,558**
High risk categories	**-**	**-**	**-**	**-**	**-**
Other assets	**393,255**	**387,880**	**-**	**387,880**	**445,985**
Total	**15,129,638**	**14,875,380**	**(614,385)**	**13,633,572**	**6,112,100**

32 RISK MANAGEMENT (continued)

(a) Credit risk (continued)

Collateral (continued)

Assets classes	*On & Off Balance sheet gross outstanding*	*Credit risk mitigation ("CRM")*			*Risk weighted assets*
		Exposure before CRM	*CRM*	*After CRM*	*Total*
	AED 000	*AED 000*	*AED 000*	*AED 000*	*AED 000*
As at 31 December 2019					
Claims on sovereign	3,213,031	3,201,371	-	3,201,371	16,142
Claims on (PSEs)	11,658	11,658	-	11,658	2,332
Claims on banks	4,302,876	4,302,876	-	4,275,229	1,467,538
Claims on securities Firm		-	-	-	-
Claims on corporate	3,720,283	3,715,707	(403,777)	2,771,010	2,271,969
Claims included in retail portfolio	494,641	494,641	(227,777)	450,944	196,704
Claims secured by residential property	520,653	520,653	-	520,653	335,007
Claims secured by commercial real estate	560,654	560,654	-	560,654	560,654
Past due loans	461,281	253,250	-	251,200	252,175
High risk categories	-	-	-	-	-
Other assets	418,510	405,658	-	405,658	456,515
Total	13,703,587	13,466,468	(631,554)	12,448,377	5,559,036

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

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

Funded exposure

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

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

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

Claims on banks
Claims on banks are risk weighted based on the ratings assigned to them by external rating agencies, however, short term claims denominated in local currency were assigned more favourable risk weighting.

No claim on an unrated bank would receive a risk weight lower than that applied to claims on its sovereign of incorporation.

32 RISK MANAGEMENT (continued)

(a) Credit risk (continued)

Risk weighted capital requirement (continued)

Funded exposure (continued)

Claims on corporate portfolio and government related entities portfolio
Claims on corporate and government related entities portfolio (entities with greater than 50% government ownership) are risk weighted in accordance with ratings from acceptable ECAIs. Risk weightings for unrated corporate and government related entities' claims are assigned at 100%.

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

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

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

Past due exposures
The unsecured portion of any loan (other than a qualifying residential mortgage loan) that is past due for more than 90 days, net of specific provisions (including partial write-offs), is risk weighted as follows:
– 150% risk weight when specific provisions are less than 20% of the outstanding amount of the loan; and
– 100% risk weight when specific provisions are greater than 20% of the outstanding amount of the loan.

Other exposures
These are risk weighted at 100%.

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

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

Unfunded exposure (continued)
The Bank's exposure and credit risk mitigation at 31 December 2020 is summarised as follows:

	2020 AED'000	*2019 AED'000*
Gross exposure prior to credit risk mitigation	**14,247,957**	13,079,931
Less: exposure covered by eligible financial collateral	**613,230**	630,303
Less: exposure covered by guarantees	**1,155**	1,251
Net exposure after credit risk mitigation	**13,633,572**	12,448,377
Risk Weighted Assets	**6,112,100**	5,559,036

32 RISK MANAGEMENT (continued)

(a) Credit risk (continued)

Covid-19 and Expected Credit Loss (ECL)
The existence of novel coronavirus (Covid-19) was confirmed in early 2020 and has spread globally, causing disruptions to businesses and economic activity. In response, governments and central banks have launched economic support and relief measures (including payment deferrals) to minimize the impact on individuals and corporates.

In determination of ECL, the Bank has considered potential impact caused by Covid-19 pandemic (based upon available information) and taken into account economic support and relief measures of governments and central banks. The Bank has also considered the notices issued by the Central Bank of UAE with regards to the 'Targeted Economic Support Scheme (TESS)' and 'Treatment of IFRS9 Expected Credit Loss in the context of Covid-19 crisis' as well as the guidance issued by the International Accounting Standards Board (IASB).

The Bank has a dedicated IFRS 9 governance process established to review and approve IFRS 9 Stage migrations, management overlays to ECL estimates, and macro-economic scenarios and weightings.

Significant Increase in Credit Risk (SICR)
Under IFRS 9, loans are required to be moved from Stage 1 to Stage 2 if and only if they have been the subject of SICR since origination. SICR occurs when there has been a significant increase in risk of default.

The Bank continues to assess borrowers for other indicators of unlikeliness to pay, taking into consideration the underlying cause of any financial difficulty and whether it is likely to be temporary as a result of Covid-19 or long term.

During 2020, the Bank has initiated a program of payment relief to support its impacted customers either by deferring interest/principal for a period or through adjustment of monthly installments. The Bank believes that the extension of payment reliefs does not automatically trigger SICR where the impact on customer's business is expected to be short term. For all other customers, the Bank continues to consider severity and extent of potential Covid-19 impact on economic sector and future outlook, cash flow and financial strength, agility and change in risk profile along with the past track record in determining SICR.

As per the disclosure requirements of the Central Bank of UAE in the context of Covid-19, for the UAE operations, the Bank has divided its customers benefitting from payment deferrals into two groups (Group 1 and Group 2). Customers not expected to face substantial changes in their creditworthiness, beyond liquidity issues caused by the Covid-19 crisis, have been retained in the same Stage categorized in Group 1.

Customers expected to be significantly impacted by Covid-19 in the long term and that are expected to face substantial deterioration in their creditworthiness have been migrated to Stage 2 and categorized in Group 2. In exceptional circumstances, Stage 3 migration may have also been triggered where a customer's business, income streams and interest servicing capacity were expected to be permanently impaired. Such customers have also been categorized in Group 2 with ECL overlay.

The accounting impact of the extension / restructuring of credit facilities due to Covid-19 has been assessed and has been treated as per the requirements of IFRS 9 for modification of terms of arrangement.

Forward Looking Information
In light of the current uncertain economic environment, the Bank has assessed a range of possible macro-economic scenarios and associated weights, and analyzed their impact on ECL estimates. Accordingly, the Bank used macro-economic forecasts in 2020 to reflect the impact of Covid-19, using baseline, upside and downside scenarios. The Bank has also applied portfolio-level ECL adjustments to wholesale exposures based upon affected geographies and sectors, as well as to retail customers availing deferrals or adjustments to monthly installments based upon employment status and level of salary inflows. The Bank continues to assess individually significant exposures for any adverse movements due to Covid-19.

As with any economic forecasts, the projections and likelihoods of the occurrence are subject to inherent uncertainty and therefore the actual outcomes may be significantly different to those projected.

32 RISK MANAGEMENT (continued)

(a) Credit risk (continued)

Analysis of customers benefiting from payment deferrals

Deferral amount and outstanding balances of UAE customers
The table below contains analysis of the deferral amount and outstanding balances of UAE customers benefiting from deferrals:

Clients benefiting from deferrals during 2020

As at 31 December 2020		*AED '000s*	*Number of clients deferred*	*Payment deferrals*	*Exposure*	*Impairment Allowance*
Segment	**Stage**	**Group**				
Retail banking	Stage 1	Group 1	10	1,607	15,425	32
		Group 2	-	-	-	-
			10	1,607	15,425	32
	Stage 2	Group 1	7	2,562	46,830	4,464
		Group 2	19	8,308	156,183	23,819
			26	10,870	203,013	28,283
Total retail banking			**36**	**12,474**	**218,438**	**28,315**
Wholesale banking	Stage 1	Group 1	78	169,701	214,706	8,627
		Group 2	1	935	-	-
			79	170,636	214,706	8,627
	Stage 2	Group 1	40	92,497	179,035	19,924
		Group 2	32	91,970	197,358	38,478
			72	184,467	376,393	58,402
Total wholesale banking			**151**	**355,103**	**591,099**	**67,029**

32 RISK MANAGEMENT (continued)

(a) Credit risk (continued)

Analysis of customers benefiting from payment deferrals (continued)

Deferral amount and outstanding balances of UAE customers (continued)
The Bank did not avail Zero Cost Funding under the CBUAE TESS program.

As per the requirements of the Central Bank of UAE, the Bank has divided its customers benefitting from payment deferrals into two groups as follows:

Group 1: includes those customers that are not expected to face substantial changes in their creditworthiness, beyond liquidity issues and are temporarily and mildly impacted by the Covid-19 crisis.

For these customers, the payment deferrals are believed to be effective and thus the economic value of the facilities is not expected to be materially affected. These customers are subject to ongoing monitoring for any changes in their creditworthiness for the appropriateness of their grouping and IFRS 9 staging.

Group 2: includes those customers that are expected to face substantial changes in their creditworthiness, in addition to liquidity issues that will be addressed by payment deferrals.

For these customers, there is sufficient deterioration in credit risk to trigger IFRS 9 stage migration. The Bank continues to monitor the creditworthiness of these customer, particularly indications of potential inability to pay any of their obligations as and when they become due.

The impact of Covid-19 crisis continues to filter through into the real economy. In view of this, the Bank has taken a proactive approach and on an ongoing basis for all customers, the Bank continues to consider the severity and extent of potential Covid-19 impact on economic sectors and outlook, cash flow, financial strength, agility and change in risk profile along with the past track record and ongoing adaptation. Accordingly, all staging and grouping decisions are subject to regular review to ensure these reflect an accurate view of the Bank's assessment of the customers' creditworthiness, staging and grouping as of the reporting date.

32 RISK MANAGEMENT (continued)

(a) Credit risk (continued)

Migration during the year

	Non-credit impaired				Credit Impaired					
	Stage 1		Stage 2		Stage 3		POCI		Total	
	Exposure	Impairment	Exposure	Impairment Allowance	Exposure	Impairment Allowance	Exposure	Impairment Allowance	Exposure	Impairment Allowance
Retail banking loans										
As at 1 Jan 2020	244,583	3,118	287,084	36,836	152,221	53,893	-	-	683,888	93,847
Transfers from stage 1 to stage 2	(44,918)	(99)	44,918	99	-	-	-	-	-	-
Transfers from stage 2 to stage 1	4,413	397	(4,413)	(397)	-	-	-	-	-	-
Transfers from 1&2 to stage 3	(63)	(5)	(1)	-	64	5	-	-	-	-
Transfers from stage 3 to stage 2	-	-	-	-	-	-	-	-	-	-
Other movements	(37,963)	(1,086)	(48,764)	(1,174)	(32,232)	(3,283)	-	-	(118,959)	(5,543)
As of 31 Dec 2020	166,052	2,325	278,824	35,364	120,053	50,615	-	-	564,929	88,304
Wholesale banking loans:										
As of 1 Jan 2020	1,936,469	70,490	805,028	91,036	186,001	126,867	-	-	2,927,498	288,393
Transfers from stage 1 to stage 2	(184,325)	(2,389)	184,325	2,389	-	-	-	-	-	-
Transfers from stage 2 to stage 1	4,974	105	(4,974)	(105)	-	-	-	-	-	-
Transfers from 1&2 to stage 3	(1,034)	(45)	(13,777)	(5,979)	14,811	6,024	-	-	-	-
Transfers from stage 3 to stage 2	-	-	-	-	-	-	-	-	-	-
Other movements	(124,514)	(13,145)	(136,277)	4,074	22,762	16,340	-	-	(238,029)	7,269
As of 31 Dec 2020	1,631,570	55,016	834,325	91,415	223,574	149,231	-	-	2,689,469	295,662

32 RISK MANAGEMENT (continued)

(a) Credit risk (continued)

Change in ECL allowance by industry sector for UAE Corporate and Institutional banking customers
Below is an analysis of change in ECL allowance by industry sector since 31 December 2019 on UAE Corporate and Institutional banking customers benefiting from payment deferrals:

	Non-credit impaired		*Credit Impaired*	
AED '000	***Stage 1***	***Stage 2***	***Stage 3***	***Total***
Retail banking loans:				
ECL allowance as of start of year	3,118	36,836	53,893	93,847
Credit Cards	(246)	6	(10)	(250)
Housing Loans	(148)	(1,470)	(1,965)	(3,583)
Personal Loans	1	-	(6)	(5)
Auto Loans	(32)	(9)	(83)	(124)
Others	(368)	1	(1,214)	(1,581)
ECL allowance as of end of year	2,325	35,364	50,615	88,304
Wholesale banking loans:				
ECL allowance as of start of year	70,490	91,036	126,867	288,393
Federal Government	-	-	-	-
Emirates Governments	-	-	-	-
GREs (Gov ownership >50%)	-	(8,548)	6,319	(2,229)
Corporate with Govt ownership <50%	-	-	-	-
Other Corporates	(17,574)	2,550	652	(14,372)
High Net Worth Individuals	105	-	-	105
SMEs	1,997	6,377	15,517	23,891
Banks	-	-	-	-
NBFI	(2)	-	(124)	(126)
Others	-	-	-	-
ECL allowance as of end of year	55,016	91,415	149,231	295,662

(b) Market risk

Market risk is the risk that changes in market prices, such as interest rate, equity prices, foreign exchange rates and credit spreads (not relating to changes in the obligor's/ issuer's credit standing) will affect the Bank's income or the value of its holdings of financial instruments. The objective of market risk management is to manage and control market risk exposures within acceptable parameters, while optimising the return on risk. The prohibition on speculative trading on the Bank's own behalf is designed to ensure that such risks are kept to a minimum.

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

32 RISK MANAGEMENT (continued)

(b) Market risk (continued)

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

	AED *AED 000*	*USD* *AED 000*	*GBP* *AED 000*	*Others* *AED 000*	*Total* *AED 000*
Assets					
Cash and balances with UAE Central Bank	3,668,444	410	-	-	3,668,854
Due from banks	2,448,640	1,055,582	273,972	161,623	3,939,817
Due from Head Office and branches	1,096	8,820	5,581	22,030	37,527
Loans and receivables	2,421,018	346,560	1,018	68,117	2,836,713
Investments	1,197	2,134,353	-	38,653	2,174,203
Property and equipment	53,995	-	-	-	53,995
Right-of-use assets	124,160	-	-	-	124,160
Customers' indebtedness for acceptances	5,360	36,678	-	2,349	44,387
Deferred tax assets	83,347	-	-	-	83,347
Other assets	50,426	7,716	166	4,612	62,920
Total assets	**8,857,683**	**3,590,119**	**280,737**	**297,384**	**13,025,923**

	AED *AED 000*	*USD* *AED 000*	*GBP* *AED 000*	*Others* *AED 000*	*Total* *AED 000*
Liabilities					
Deposits from customers	7,076,864	3,239,497	279,629	287,352	10,883,342
Due to banks	392	43,109	-	-	43,501
Due to Head Office and branches	52,026	113	24	-	52,163
Liabilities under acceptances	5,360	36,678	-	2,349	44,387
Lease liabilities	101,505	-	-	-	101,505
Deferred tax liabilities	15,239	-	-	-	15,239
Other liabilities	164,719	6,936	1,143	2,702	175,500
Total liabilities	**7,416,105**	**3,326,333**	**280,796**	**292,403**	**11,315,637**
Capital & Reserves					
Allocated Capital	100,000	-	-	-	100,000
Legal reserve	50,000	-	-	-	50,000
Retained earnings	1,498,202	-	-	-	1,498,202
Revaluation reserves	60,957	-	-	-	60,957
Impairment reserves	1,127	-	-	-	1,127
Total capital and reserves	**1,710,286**	**-**	**-**	**-**	**1,710,286**
Total liabilities, capital and reserves	**9,126,391**	**3,326,333**	**280,796**	**292,403**	**13,025,923**
Net balance sheet position	(268,708)	263,786	(59)	4,981	-

32 RISK MANAGEMENT (continued)

(b) Market risk (continued)

Foreign currency risk (continued)

	AED *AED 000*	*USD* *AED 000*	*GBP* *AED 000*	*Others* *AED 000*	*Total* *AED 000*
At 31 December 2019					
Total assets	8,274,857	2,939,905	277,341	409,875	11,901,978
Total liabilities, capital and reserves	8,296,417	2,922,322	277,328	405,911	11,901,978
Net balance sheet position	(21,560)	17,583	13	3,964	-

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

	Net spot position 2020 AED 000	***Forward position 2020 AED 000***	***Net exposure 2020 AED 000***	*Net exposure 2019 AED 000*
Currency				
US Dollar	**263,786**	**(183,675)**	**80,111**	18,075
GBP	**(59)**	**-**	**(59)**	13
Others	**4,981**	**-**	**4,981**	3,472

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

Shift in yield curve	***2020 AED 000***	*2019 AED 000*
+200 b.p.	**126,901**	105,662
-200 b.p.	**(126,901)**	(105,662)

A substantial portion of the Bank's assets and liabilities are re-priced within one year. Accordingly there is limited exposure to interest rate risk. The interest rate sensitivities set out above are illustrative only and employ simplified scenarios. They are based on AED 9.9 billion of monthly average interest bearing assets and AED 4.6 billion of monthly average interest bearing liabilities (31 Dec 2019: AED 9.8 billion average interest bearing assets and AED 5.0 billion average interest bearing liabilities.) The sensitivity does not incorporate actions that could be taken by the management to mitigate the effect of interest rate movements.

32 RISK MANAGEMENT (continued)

(b) Market risk (continued)

Interest rate risk (continued)

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

As at 31 December 2020	*Up to 3 months AED 000*	*3 – 12 months AED 000*	*1 – 5 year AED 000*	*Over 5 years AED 000*	*Non interest bearing AED 000*	*Carrying amount AED 000*
Assets						
Cash and balances with UAE Central Bank	2,750,000	-	-	-	918,854	3,668,854
Due from banks	2,649,569	1,082,130	-	-	208,118	3,939,817
Due from Head Office, branches abroad and Associates	7,101	-	-	-	30,426	37,527
Loans and receivables	2,561,999	120,832	79,860	19,659	54,363	2,836,713
Investments	76,815	120,018	1,687,279	290,091	-	2,174,203
Property and equipment	-	-	-	-	53,995	53,995
Right-of-use assets	-	-	-	-	124,160	124,160
Customers' indebtedness for acceptances	-	-	-	-	44,387	44,387
Deferred tax assets	-	-	-	-	83,347	83,347
Other assets	-	-	-	-	62,920	62,920
Total assets	**8,045,484**	**1,322,980**	**1,767,139**	**309,750**	**1,580,570**	**13,025,923**
Liabilities, capital and reserves						
Deposits from customers	2,231,489	1,124,525	161,015	-	7,366,313	10,883,342
Due to banks	-	-	-	-	43,501	43,501
Due to Head Office, branches abroad and Associates	-	-	-	-	52,163	52,163
Liabilities under acceptances	-	-	-	-	44,387	44,387
Lease liabilities	-	-	-	-	101,505	101,505
Other liabilities	-	-	-	-	175,500	175,500
Deferred tax liabilities	-	-	-	-	15,239	15,239
Capital and reserves	-	-	-	-	1,710,286	1,710,286
Total liabilities and capital and reserves	**2,231,489**	**1,124,525**	**161,015**	**-**	**9,508,894**	**13,025,923**
Interest rate sensitivity gap						
2020	**5,813,995**	**198,455**	**1,606,124**	**309,750**	**(7,928,324)**	**-**
2019	5,186,154	(405,611)	982,496	245,821	(6,008,860)	-
Cumulative interest rate sensitivity gap						
2020	**5,813,995**	**6,012,450**	**7,618,574**	**7,928,324**	**-**	**-**
2019	5,186,154	4,780,543	5,763,039	6,008,860	-	-

32 RISK MANAGEMENT (continued)

(b) Market risk (continued)

Interest rate risk (continued)
Repricing of assets and liabilities has been determined on the basis of contractual pricing or maturity dates, whichever is earlier.

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

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

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

IBOR Reforms
A fundamental reform of major interest rate benchmarks is being undertaken globally to replace or reform IBOR with alternative risk-free rates (referred to as 'IBOR reform'). The Bank has exposure to interbank offered rates (IBORs) on its financial instruments that will be replaced or reformed as part of this market-wide initiative.

Financial assets:
The Bank's IBOR exposures on floating-rate loans and advances are covered in the following table:

Currency	***2020*** ***AED '000***
USD	**251,308**
EUR	**452**
GBP	**391**
	252,151

The Bank expects that retail products will be amended in a uniform way. However, the Bank expects to participate in bilateral negotiations with the counterparties in its bespoke products, such as loans and advances issued to corporates. The Bank expects to begin amending the contractual terms of its existing floating-rate assets in 2021; however, the exact timing will vary depending on the extent to which standardized language can be applied across certain loan types and the extent of bilateral negotiations between the Bank and loan counterparties.

Financial liabilities:
The Bank does not have any floating-rate liabilities indexed to IBORs denominated in USD.

The following table shows the bank's assets linked to LIBOR whose maturity date is later than 31 December 2021, however, there were liabilities and derivatives of the Bank linked to LIBOR:

31 December 2020	***AED'000***
USD LIBOR (1 month)	**32,922**
USD LIBOR (3 month)	**60,974**
USD LIBOR (6 month)	**85,987**
USD LIBOR (12 month)	**59,450**
Others	**12,818**
Total	**252,151**

32 RISK MANAGEMENT (continued)

(c) Liquidity risk

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

	Carrying amount AED 000	*inflow / (outflow) AED 000*	*0 – 3 months AED 000*	*3 months to 1 year AED 000*	*1 year to 5 years AED 000*
At 31 December 2020					
Financial Liabilities					
Deposits from customers	**10,883,342**	**(10,900,871)**	**(9,606,569)**	**(1,131,725)**	**(162,577)**
Due to banks	**43,501**	**(43,501)**	**(43,501)**	**-**	**-**
Due to Head Office, branches abroad and Associates	**52,163**	**(52,163)**	**(52,163)**	**-**	**-**
Lease liabilities	**101,505**	**(101,505)**	**(7,041)**	**(28,166)**	**(66,298)**
Other liabilities	**96,637**	**(96,637)**	**-**	**-**	**(96,637)**
	11,177,148	**(11,194,677)**	**(9,709,274)**	**(1,159,891)**	**(325,512)**
Unrecognised loan commitments	**618,326**	**618,326**	**316,428**	**269,850**	**32,048**
At 31 December 2019					
Financial Liabilities					
Deposits from customers	9,784,097	(9,809,323)	(8,357,839)	(1,268,403)	(183,081)
Due to banks	141,245	(141,283)	(141,283)	-	-
Due to Head Office, branches abroad and Associates	8,798	(8,843)	(8,843)	-	-
Lease liabilities	90,609	(90,609)	(3,839)	(10,379)	(76,391)
Other liabilities	120,402	(120,402)	-	-	(120,402)
	10,145,151	(10,170,460)	(8,511,804)	(1,278,782)	(379,874)
Unrecognised loan commitments	528,113	528,113	284,778	186,900	56,435

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

32 RISK MANAGEMENT (continued)

(c) Liquidity risk (continued)

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

As at 31 December 2020	*Up to 3 months AED 000*	*3 – 12 months AED 000*	*1 – 5 year AED 000*	*Over 5 years AED 000*	*No maturity AED 000*	*Total amount AED 000*
Assets						
Cash and balances with UAE Central Bank	2,750,000	-	-	-	918,854	3,668,854
Due from banks	2,649,569	1,082,130	-	-	208,118	3,939,817
Due from related parties	7,101	-	-	-	30,426	37,527
Loans and receivables	811,790	596,489	1,182,316	19,659	226,459	2,836,713
Investments	17,573	120,018	1,746,521	290,091	-	2,174,203
Property and equipment	-	-	-	-	53,995	53,995
Right-of-use assets	-	-	-	-	124,160	124,160
Customers' indebtedness for acceptances	36,226	8,161	-	-	-	44,387
Deferred tax assets	-	-	-	-	83,347	83,347
Other assets	-	-	-	-	62,920	62,920
Total assets	6,272,259	1,806,798	2,928,837	309,750	1,708,279	13,025,923
Liabilities, capital and reserves						
Deposits from customers	2,463,700	1,124,525	161,015	-	7,134,102	10,883,342
Due to banks	-	-	-	-	43,501	43,501
Due to related parties	-	-	-	-	52,163	52,163
Liabilities under acceptances	36,226	8,161	-	-	-	44,387
Lease liabilities	7,041	281,66	63,912	2,386	-	101,505
Other liabilities	-	-	-	-	175,500	175,500
Deferred tax liabilities	-	-	-	-	15,239	15,239
Capital and reserves	-	-	-	-	1,710,286	1,710,286
Total liabilities and capital and reserves	2,506,967	1,132,686	224,927	2,386	9,130,791	13,025,923
Maturity gap 2020	3,765,292	674,112	2,703,910	307,364	(7,422,512)	-

32 RISK MANAGEMENT (continued)

(c) Liquidity risk (continued)

As at 31 December 2019	*Up to 3 months AED 000*	*3 – 12 months AED 000*	*1 – 5 year AED 000*	*Over 5 years AED 000*	*No maturity AED 000*	*Total amount AED 000*
Assets						
Cash and balances with UAE Central Bank	1,435,000	435,000	-	-	1,386,115	3,256,115
Due from banks	2,979,169	212,553	80,000	-	148,340	3,420,062
Due from related parties	7,491	-	-	-	92,107	99,598
Loans and receivables	1,266,828	809,702	785,715	32,475	309,130	3,203,850
Investments	15,299	142,217	1,126,146	224,059	1,197	1,508,918
Property and equipment	-	-	-	-	61,116	61,116
Right-of-use assets	-	-	-	-	126,044	126,044
Customers' indebtedness for acceptances	62,776	12,930	-	-	-	75,706
Deferred tax assets	-	-	-	-	81,493	81,493
Other assets	-	-	-	-	69,076	69,076
Total assets	5,766,563	1,612,402	1,991,861	256,534	2,274,618	11,901,978
Liabilities, capital and reserves						
Deposits from customers	2,419,155	1,263,180	181,637	-	5,920,125	9,784,097
Due to banks	-	-	-	-	141,245	141,245
Due to related parties	3,475	-	-	-	5,323	8,798
Liabilities under acceptances	62,776	12,930	-	-	-	75,706
Lease liabilities	3,839	10,379	65,678	10,713	-	90,609
Other liabilities	-	-	-	-	205,194	205,194
Deferred tax liabilities	-	-	-	-	8,336	8,336
Capital and reserves	-	-	-	-	1,587,993	1,587,993
Total liabilities and capital and reserves	2,489,245	1,286,489	247,315	10,713	7,868,216	11,901,978
Maturity gap 2019	3,277,318	325,913	1,744,546	245,821	(5,593,598)	-

(d) Operational Risk

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

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

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

32 RISK MANAGEMENT (continued)

(e) Capital risk management

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

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

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

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

The Bank also assesses its capital requirements internally taking into consideration growth requirements and business plans, and quantifies its Regulatory and Risk/ Economic Capital requirements within its integrated Internal Capital Adequacy Process ("ICAAP") Framework.

Risks such as Interest Rate Risk in the Banking Book, Concentration Risk, Strategic Risk, Legal and Compliance Risk, Stress Risk, Insurance Risk and Reputational Risk are all part of the ICAAP.

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

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

- CET1 capital is the highest quality form of capital, comprising share capital, legal, statutory and other reserves, fair value reserve, retained earnings, after deductions for intangibles and other regulatory adjustments relating to items that are included in equity but are treated differently for capital adequacy purposes under 'CBUAE' guidelines.
- Tier 2 capital comprises of collective provision which shall not exceed 1.25% of total credit risk weighted assets.

The CBUAE issued Basel III capital regulations, which came into effect from 1 February 2017 introducing minimum capital requirements at three levels, namely Common Equity Tier 1 ('CET1'), Additional Tier 1 ('AT1') and Total Capital.
The minimum capital adequacy requirements as set out by the Central Bank are as follows:
- Minimum common equity tier 1 (CET 1) ratio of 7% of risk weighted assets (RWAs).
- Minimum tier 1 ratio of 8.5% of RWAs.
- Total capital adequacy ratio of 10.5% of RWAs.

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

For 2020, CCB is effective in transition arrangement and is required to be kept at 2.5% of the Capital base. CCyB is not in effect and is not required to be kept for 2020.

The Bank has complied with all the externally imposed capital requirements.

32 RISK MANAGEMENT (continued)

(e) Capital risk management (continued)

Capital allocation (continued)
As at 31 December 2020 and 2019, the Bank's regulatory capital position is as follows:

	2020	*2019*
	AED'000	*AED'000*
Common Equity Tier 1 (CET 1) CAPITAL		
Share capital	**100,000**	100,000
Legal reserves	**50,000**	50,000
Retained earnings*	**1,427,202**	1,331,676
Fair value reserve	**27,229**	10,452
Total CET 1 capital	**1,604,431**	1,492,128
Regulatory adjustments	**-**	-
Total tier 1 capital	**1,604,431**	1,492,128
TIER 2 CAPITAL		
General provisions	**76,401**	69,488
Total tier 2 capital	**76,401**	69,488
Total regulatory capital (Sum of tier 1 and 2 capital)	**1,680,832**	1,561,616

	2020	*2019*
	AED'000	*AED'000*
RISK WEIGHTED ASSETS		
Credit risk	**6,112,100**	5,559,036
Market risk	**9,120**	7,341
Operational risk	**777,902**	777,298
Total risk weighted assets (RWA)	**6,899,122**	6,343,675
Total CET 1 capital expressed as % of RWA	**23.26%**	23.52%
Total tier 1 capital expressed as % of RWA	**23.26%**	23.52%
Total regulatory capital expressed as % of RWA	**24.36%**	24.62%

*Habib Bank AG Zurich Head Office had proposed the Bank for profit repatriation of AED 71 million. This amount is excluded from the retained earnings as at 31 December 2020 for calculation of CET 1 capital.

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

Risk weight for operation risk
Capital requirement for operation risk is calculated using basic indicator approach. This capital change was computed using basic indicator approach by multiplying the three years' average gross income by a predefined beta factor.

33 CASH AND CASH EQUIVALENTS

Analysis of the balances of cash and cash equivalent items:

	2020 ***AED 000***	*2019* *AED 000*	***Net change in year*** ***AED 000***
Cash and deposits with UAE Central Bank	**3,668,854**	3,256,115	412,739
Less: Certificates of deposit and Islamic commodity murabaha with maturity of over 3 months	**(155,000)**	(635,000)	480,000
Less: Statutory reserve	**(773,592)**	(958,913)	185,321
Due from banks	**3,939,817**	3,420,062	519,755
Less: Bank placements with maturity of over 3 months	**(1,633,677)**	(632,400)	(1,001,277)
Due from Head Office, branches abroad and associates	**37,527**	99,598	(62,071)
Due to banks including CB	**(43,501)**	(141,245)	97,744
Due to Head Office, branches abroad and associates	**(52,163)**	(8,798)	(43,365)
	4,988,265	4,399,419	588,846

34 LEGAL PROCEEDINGS

Litigation is a common occurrence in the banking industry due to the nature of the business undertaken. The Bank has been advised by its legal counsel that it is only possible, but not probable, that the action will succeed. Accordingly, no provision for any liability has been made in these financial statements.

35 CUSTODY ACCOUNTS

The Bank provides custody, trustee and administration services to third parties in relation to a wide range of financial instruments. Those assets that are held in a fiduciary capacity are not included in these financial statements. At the reporting date, the Bank has investment custody accounts aggregating to approximately AED 1,045 million (2019: AED 1,032 million). The income related to custody account of AED 4,560 thousand is included in the fee and commission income in the statement of profit or loss and other comprehensive income.

36 SUBSEQUENT EVENTS

Subsequent to year end, the Bank has closed down one of its two Branches in Emirate of Abu Dhabi and opened a new Brach in Emirate of Dubai. The overall number of Branches remained 8.

37 COMPARATIVE FIGURES

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