بنك دبي الإسلامي
Dubai Islamic Bank

Basel III – Pillar III Disclosures

2019

Table of Contents

PILLAR III DISCLOSURES
31 DECEMBER 2019

1. Overview and Introduction

This document presents Pillar III disclosures which complements the Basel III minimum capital requirements and the supervisory review process of Dubai Islamic Bank PJSC including its financial subsidiaries ("DIB" or the "Bank") and non-financial subsidiaries (collectively referred to as the "Group"). The disclosures include information on Group's reporting structure, regulatory capital structure, risk exposures, risk management objectives, policies and assessment process. The disclosures consist of both quantitative and qualitative information and are provided at the consolidated level.

The Bank is regulated by the Central Bank of the United Arab Emirates ("CBUAE") and follows the Pillar 3 disclosure requirement guidelines issued by the CBUAE. In February 2017, new Basel III capital regulations issued by CBUAE came into effect for all Banks in the UAE. Additional guidelines for Basel III were issued over the course of 2018/2019 in consultations with the UAE Banks.

The CBUAE Basel III framework addresses the importance of developing and implementing enhanced risk management techniques for monitoring and managing the risks and intends to strengthen the market discipline and risk management practices of UAE Banks.

The Pillar III disclosures provide both qualitative and quantitative information at Group level in order to meet the disclosure requirements. Some of the Pillar III requirements have been disclosed in the audited consolidated financial statements for the year ended 31
December 2019, which covers the risk and capital management processes of the Group and its compliance with the Basel Accords.

BASEL Regulatory Framework

The Basel Accord framework consists of following three main pillars:

- **Pillar I** - defines the regulatory minimum capital requirements by providing rules and regulations for measurement of credit risk, market risk and operational risk. The requirement of capital has to be covered by the banks' own regulatory fund;

- **Pillar II** - addresses a bank's Internal Capital Adequacy Assessment Process ("ICAAP") for assessing overall capital adequacy in relation to risks other than Pillar I. Pillar II also introduces the Supervisory Review and Evaluation Process ("SREP"), which is used as a tool to assess the internal capital adequacy of banks; and

- **Pillar III** - complements the other two pillars and focuses on enhanced transparency in information disclosure, covering risk and capital management, including capital adequacy which encourages market discipline that also allows market participants to assess specific information.

Differences between Financial Statements and Pillar III Reporting of Credit Risk Exposures

Credit risk exposures reported under Pillar III differ in respect of the following vis-à-vis financial statements:

- As per CBUAE Basel framework, off balance sheet exposures are converted, by applying a credit conversion factor (CCF), into equivalent credit exposures;
- Deferred Tax Assets and Intangible assets are deducted from Capital and not taken under credit risk assets;
- Commercial subsidiaries are completely deconsolidated and only the investments at cost in those entities are taken for risk weight purposes; reserves and retained earnings in these companies and deducted from the group capital. Any intra group loans to such entities are treated as third party loans for risk weighting purposes;
- Under the comprehensive credit risk mitigation approach under the standardized approach, eligible collaterals are considered subject to regulatory haircuts to estimate and report net exposure;
- General provisions are not netted off against loans but used as Tier 2 capital up to 1.25% of Credit RWA;
- Acceptances reported under other assets in financial statements are taken under off balance sheet exposures with 100% CCF for capital requirements calculations purpose;
- Private equity exposures reported under FVPL category for financial reporting are treated under banking book exposures for capital calculations purpose since they don't meet the Basel criteria for trading book exposures.

Future Regulatory Developments

The regulation and supervision of financial institutions has undergone a significant change since the global financial crisis. CBUAE Basel III capital regulations have been implemented and are compiled by the Bank.

PILLAR III DISCLOSURES
31 DECEMBER 2019

All revised capital standards for 2019 as per Basel III guidelines on capital standards for Common Equity Tier 1 (CET1), Additional Tier 1 (AT1) and Capital Buffers such as Capital Conservation Buffer (CCB) and Domestic Systemically Important Banks Buffer (DSIB) are implemented. There is close coordination between UAE Banks and CBUAE for the smooth implementation of any forthcoming new guidelines and disclosure requirements.

In October 2018, CBUAE issued draft Standards on the revised Pillar III disclosure requirements which is currently under consultation with the UAE Banks and will replace the existing Pillar III disclosure requirements that were issued in 2009. The revised requirements shall be implemented by the bank and will be disclosed in 2021.

Implementation and Compliance of Basel Framework Guidelines

The Bank has been in compliance with Basel Accord guidelines since December 2007, in accordance with CBUAE directives on Standardized Approach for Credit, Market and Operational Risk.

In compliance with the CBUAE guidelines and Basel accords, these disclosures include information on the Bank’s risk management objectives and policies, risk assessment processes and computation, capital management and capital adequacy.

Verification:

The Pillar III disclosures for the year ended 31 December 2019 have been appropriately verified internally, but are not subject to audit by the Bank’s external auditor.

PILLAR III DISCLOSURES
31 DECEMBER 2019

2. Group Structure - Information on Subsidiaries and Significant Investments

The Group consists of Dubai Islamic Bank P.J.S.C. and its subsidiaries. As of 31 December 2019, the Group's interest held directly or indirectly in its financial and non-financial subsidiaries are as follows:

	Name of Subsidiary	Principal Activity	Place of Incorporation and Operation	Ownership Interest and Voting Power	
				2019	2018
1.	Dubai Islamic Bank Pakistan Ltd.	Banking	Pakistan	**100.0%**	100.0%
2.	Tamweel P.S.C	Financing	U.A.E	**92.0%**	92.0%
3.	DIB Bank Kenya	Banking	Kenya	**100.0%**	100.0%
4.	Dubai Islamic Financial Services L.L.C.	Brokerage services	U.A.E.	**95.5%**	95.5%
5.	Deyaar Development P.J.S.C.	Real estate development	U.A.E	**44.9%**	44.9%
6.	Dar al Shariah Financial & Legal Consultancy L.L.C.	Financial and legal advisory	U.A.E.	**60.0%**	60.0%
7.	Al Tanmyah Services L.L.C.	Labour services	U.A.E.	**99.5%**	99.5%
8.	Al Tatweer Al Hadith Real Estate	Real estate development	Egypt	**100.0%**	100.0%
9.	Al Tameer Modern Real Estate Investment	Real estate development	Egypt	**100.0%**	100.0%
10.	Al Tanmia Modern Real Estate Investment	Real estate development	Egypt	**100.0%**	100.0%
11.	Naseej Private Property Management Services	Property management	U.A.E.	**99.0%**	99.0%
12.	DIB Printing Press L.L.C.	Printing	U.A.E.	**99.5%**	99.5%
13.	Al Islami Real Estate Investments Ltd.	Investments	U.A.E.	**100.0%**	100.0%
14.	Dubai Islamic Trading Center L.L.C.	Trading in vehicles	U.A.E.	**100.0%**	100.0%
15.	Creek Union Limited FZ LLC	Investments	U.A.E.	**100.0%**	100.0%
16.	Madinat Bader Properties Co. L.L.C.	Real Estate Development	U.A.E.	**100.0%**	100.0%

In addition to the registered ownership described above, the remaining equity in the entities 4, 7, 11 and 12 are also beneficially held by the Group through nominee arrangements.

Below is the list of Special Purpose Vehicles (SPV) which were formed to manage specific transactions including funds, and are expected to be closed upon completion of the related transactions:

	Name of SPV	Principal Activity	Place of Incorporation and Operation	Ownership Interest and Voting Power	
				2019	2018
17.	HoldInvest Real Estate Sarl	Investments	Luxembourg	**100.0%**	100.0%
18.	France Invest Real Estate SAS	Investments	France	**100.0%**	100.0%
19.	SARL Barbanniers	Investments	France	**100.0%**	100.0%
20.	SCI le Sevine	Investments	France	**100.0%**	100.0%
21.	Findi Real Estate SAS	Investments	France	**100.0%**	100.0%
22.	PASR Einudzwanzigste Beteiligunsverwaltung GMBH	Investments	Austria	**100.0%**	100.0%
23.	Al Islami German Holding Co. GMBH	Investments	Germany	**100.0%**	100.0%
24.	Rhein Logistics GMBH	Investments	Germany	**100.0%**	100.0%
25.	Jef Holdings BV	Investments	Netherlands	**100.0%**	100.0%
26.	Al Islami Trade Finance FZ L.L.C.	Investments	U.A.E.	**100.0%**	100.0%
27.	MESC Investment Company	Investments	Jordan	**40.0%**	40.0%
28.	Levant One Investment Limited	Investments	U.A.E.	**100.0%**	100.0%
29.	Petra Limited	Investments	Cayman Islands	**100.0%**	100.0%
30.	Deyaar Investments L.L.C.	Investments	U.A.E.	**Controlling Interest**	Controlling Interest
31.	Deyaar Funds L.L.C.	Investments	U.A.E.	**Controlling Interest**	Controlling Interest

2. Group Structure - Information on Subsidiaries and Significant Investments (continued)

32.	Sequia Investments L.L.C.	Investments	U.A.E.	**99.0%**	99.0%
33.	Blue Nile Investments L.L.C.	Investments	U.A.E.	**99.0%**	99.0%
34.	DIB FM Ltd	Investments	Cayman Islands	**100.0%**	100.0%
35.	Al Ameen	Investments	Cayman Islands	**100.0%**	100.0%

In addition to the registered ownership described above, the remaining equity in the entities 30, 31, 32 and 33 are also beneficially held by the Bank through nominee arrangements.

PILLAR III DISCLOSURES
31 DECEMBER 2019

3. Capital Management Structure and Policies

The capital management process of the Bank is aligned with the overall business strategy. The Bank conducts capital planning in conjunction with the strategic business and financial planning exercise. The Bank develops medium-term strategic plan on a rolling basis which is updated annually. Detailed business plan and budget for the year is prepared based on the medium-term plan. The overall strategic plan and budget are approved by the Board of Directors of the Bank. The business plan and budget for the year are cascaded down to the individual businesses. The detailed business plan and budget provides the foundation for financial risk management.

3.1. Capital Management Objectives

The Bank's key objectives in the capital management process are:

- To ensure that the bank has sufficient capital to cover the risks associated with its activities;
- To safeguard the Group's ability to continue as a going concern and increase the returns for the shareholders;
- To maintain a strong capital base to support the development of its business;
- To ensure smooth transition to Basel III compliance in terms of capital and liquidity ratios;
- To comply and maintain sufficient capital to meet minimum capital requirement set by the CBUAE;
- Maintain sufficient capital to support bank's risk appetite in line with the strategic objectives as per the medium term strategic plan.

The primary objective of the Bank's capital management policies is to ensure that it has sufficient capital to cover the risks associated with its activities. The assessment of the various risks across the Bank and their likely impact is carried out annually with ICAAP. As part of ICAAP, Risk Management identifies various risks the Bank is exposed to as part of its day-to-day operations. The Bank establishes policies and procedures, frameworks and methodologies; and contingency plans to measure, manage and mitigate the impact of such risks.

3.2. Regulatory Capital

The Bank's lead regulator, the CBUAE sets and monitors capital requirements for the Bank as a whole. The Bank and its individual banking operations are directly supervised by their respective local regulators.

The Bank's regulatory capital is composed of following tiers:

- Common Equity Tier 1 (CET1), which includes fully paid up capital, statutory reserve, general reserve, retained earnings, exchange translation reserve and investment fair value reserve. Regulatory adjustments under Basel III include deductions of deferred tax assets, investments in banking and financial entities, and the shortfall of provisions to expected losses, if any;
- Tier 1 capital, which includes CET1, with additional items that consist of Tier 1 capital instruments and certain non-controlling interests in subsidiaries; and
- Tier 2 capital, which includes collective impairment allowance and qualifying subordinated liabilities

CBUAE has put in regulatory thresholds for Common Equity Tier 1, Tier 1 and overall regulatory Capital.

- CET1 must be at least 7.0% of risk weighted assets (RWA);
- Tier 1 Capital must be at least 8.5% of RWA; and
- Total Capital, calculated as the sum of Tier 1 Capital and Tier 2 Capital, must be at least 10.5% of RWA.

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

The Bank is following the standardised approach for credit, market and operational risk, as permitted by CBUAE. Under Standardised Approach, all credit exposures are assessed according to the counterparty classifications and against the External Credit Assessment Institutions ("ECAI") ratings.

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

PILLAR III DISCLOSURES
31 DECEMBER 2019

3 Capital Management Structure and Policies (continued)

3.2. Regulatory Capital (continued)

No changes have been made to the objectives, policies and processes from the previous year. However, they are under constant review by the management.

During the years ended 31 December 2019, the Bank complied in full with all its externally imposed capital requirements. The Bank was recognized as Domestic Systemically Important Bank (D-SIB) during the year ended 31 December 2018 and is accordingly required to keep an additional D-SIB buffer of 0.5% for year ended 31 December 2019. Additional capital buffers Capital Conservation Buffer (CCB), Bank is required to be kept at 2.5%.

During the years ended 31 December 2019 and 2018, all banks operating in the U.A.E. were required to maintain a capital adequacy ratio at 13.00% and 12.375% respectively excluding the D-SIB buffer.

Capital Adequacy Ratio (CAR) under Basel III in accordance with regulations of the CBUAE is as follows:

	2019 AED'000	2018 AED'000
Common Equity Tier 1 (CET1)		
Share capital	**6,589,585**	6,589,585
Other reserves	**10,860,963**	10,860,963
Retained earnings	**7,602,471**	6,267,023
Cumulative deferred exchange losses	**(1,094,745)**	(1,051,515)
Investment fair value reserve	**(1,174,698)**	(850,362)
Deferred tax assets	**(36,224)**	-
Total CET 1 Capital	**22,747,352**	21,815,694
Additional Tier 1 Capital (AT1)		
Tier 1 Sukuk	**6,427,750**	6,978,700
Total AT1 Capital	**6,427,750**	6,978,700
Total Tier 1 Capital	**29,175,102**	28,794,394
Tier 2 Capital		
Collective impairment allowance	**2,155,925**	2,021,725
Total Tier 2 Capital	**2,155,925**	2,021,725
Total Capital Base	**31,331,027**	30,816,119

3 Capital Management Structure and Policies (continued)

3.2 Regulatory Capital (continued)

The Bank is computing and reporting risk weighted assets (RWA) in accordance with guidelines of the CBUAE.

	2019 AED'000	2018 AED'000
Risk weighted assets		
Credit risk	**172,474,010**	161,737,978
Market risk	**2,158,934**	1,520,866
Operational risk	**14,922,142**	13,266,610
Total risk weighted assets	**189,555,086**	176,525,454
	=========	=========

The Bank's capital adequacy ratios as of 31 December 2019 were as follows:

Capital Ratios	2019 AED'000	2018 AED'000
Capital adequacy ratio	**16.5%**	17.5%
Tier 1 Capital ratio	**15.4%**	16.3%
Common Equity Tier 1 ratio	**12.0%**	12.4%
Total capital adequacy ratios for each significant banking subsidiary :		
DIB Pakistan ("Basel III Total capital adequacy ratio")	**14.0%**	14.0%

The capital adequacy ratio for the year ended 31 December 2019 has been calculated after considering the impact of the proposed dividend as required by the Capital Supply Standard and the related guidance issued by the CBUAE.

The financial subsidiaries of the Bank are regulated by their local supervisors who set and monitor their capital adequacy requirements. CBUAE monitors the capital adequacy requirements of the Bank at a financial group level.

3.3 Tier 1 Sukuk

SPV ("the Issuer") Profit rate risk	Date of issuance	Discretionary profit rate	Callable period	Issuance amount Equivalent AED '000 2019	2018
DIB Tier 1 Sukuk Limited	March 2013	6.25% per annum paid semi-annually	On or after March 2019	-	3,673,000
DIB Tier 1 Sukuk (2) Limited	January 2015	6.75% per annum paid semi-annually	On or after January 2021	3,673,000	3,673,000
DIB Tier 1 Sukuk (3) Limited	January 2019	6.25% per annum paid semi-annually	On or after January 2025	2,754,750	-
				6,427,750	7,346,000
				========	========

3 Capital Management Structure and Policies (continued)

3.3 Tier 1 Sukuks (continued)

During 2013, the Bank issued Shari'a compliant Tier 1 Sukuk through an SPV, DIB Tier 1 Sukuk Ltd, ("the Issuer") amounting to USD 1,000 million (AED 3,673 million) at a par value of USD 1,000 (AED 3,673) per Sukuk. In January 2015, the Bank issued second series of Sharia compliant Tier 1 Sukuk through an SPV, DIB Tier 1 Sukuk II Ltd, ("the issuer") amounting to USD 1,000 million (AED 3,673 million) at a par value of USD 1,000 (AED 3,673) per Sukuk. In January 2019, the Bank issued third series of Sharia compliant Tier 1 Sukuk through an SPV, DIB Tier 1 Sukuk III Ltd, ("the issuer") amounting to USD 750 million (AED 2,755 million) at a par value of USD 1,000 (AED 3,673) per Sukuk.

Tier 1 Sukuk is a perpetual security in respect of which there is no fixed redemption date and constitutes direct, unsecured, subordinated obligations (senior only to share capital) of the Bank subject to the terms and conditions of the Mudaraba Agreement. The Tier 1 Sukuk are listed on the Irish Stock Exchange and Dubai Financial Market / Nasdaq Dubai callable by the Bank after the "First Call Date" or any profit payment date thereafter subject to certain redemption conditions.

The net proceeds of Tier 1 Sukuk are invested by way of Mudaraba with the Bank (as Mudareb) on an unrestricted co-mingling basis, by the Bank in its general business activities carried out through the Mudaraba Common pool.

At the Issuer's sole discretion, it may elect not to make any Mudaraba profit distributions expected and the event is not considered an event of default. In such event, the Mudaraba profit will not be accumulated but forfeited to the issuer. If the Issuer makes a non-payment election or a non-payment event occurs, then the Bank will not (a) declare or pay any distribution or dividend or make any other payment on, and will procure that no distribution or dividend or other payment is made on ordinary shares issued by the Bank, or (b) directly or indirectly redeem, purchase, cancel, reduce or otherwise acquire ordinary shares issued by the Bank.

3.4. Risk Weighted Assets

3.4.1 Credit Risk Weighted Assets

The details of Credit Risk Weighted Assets as of 31 December 2019 are as follows:

	Gross Exposure AED'000	Risk Weighted Assets AED'000
Claims on sovereigns	**47,834,224**	**10,010,869**
Claims on non-commercial public sector enterprises (PSEs)	**2,322,837**	**-**
Claims on multilateral development banks	**156,142**	**-**
Claims on banks	**48,561,218**	**4,234,539**
Claims on corporate and government related entities (GRE)	**163,214,189**	**104,153,535**
Claims included in the regulatory retail portfolio	**26,016,259**	**18,856,457**
Claims secured by residential property	**13,944,194**	**7,738,447**
Claims secured by commercial real estate	**10,149,136**	**9,925,709**
Past due financing assets	**8,758,447**	**5,308,521**
Higher-risk categories	**704,178**	**615,889**
Other assets	**13,016,841**	**11,630,045**
Total	**334,677,665**	**172,474,010**

3 Capital Management Structure and Policies (continued)

3.4. Risk Weighted Assets (continued)

3.4.1 Credit Risk Weighted Assets (continued)

The details of Credit Risk Weighted Assets as of 31 December 2018 are as follows:

	Gross Exposure AED'000	Risk Weighted Assets AED'000
Claims on sovereigns	45,000,457	7,746,833
Claims on non-commercial public sector enterprises (PSEs)	2,497,595	-
Claims on multilateral development banks	155,694	-
Claims on banks	41,682,408	4,183,427
Claims on corporate and government related entities (GRE)	156,079,933	99,967,366
Claims included in the regulatory retail portfolio	24,197,035	18,021,764
Claims secured by residential property	12,868,488	6,928,586
Claims secured by commercial real estate	10,116,868	9,640,128
Past due financing assets	7,438,094	3,621,307
Higher-risk categories	838,933	818,022
Other assets	10,590,073	10,810,544
Total	311,465,578	161,737,978

3.4.2 Market Risk Weighted Assets

Market risk weighted assets subject to capital charge are based on the following risks:

- Profit rate risk;
- Foreign exchange risk; and
- Equity risk.

The scope of capital charges on market risk weighted assets is restricted to 'trading book' only for the profit rate risk and equity positions. Foreign exchange risk is applicable to the Bank's overall positions.

As of 31 December 2019, the capital requirement for Market Risk as per standardized approach was as follows:

	2019 AED'000	2018 AED'000
Profit rate risk	**108,651**	24,442
Foreign exchange risk	**182,800**	135,249
Equity	**5**	-
Total capital requirement for market risk	**291,456**	159,691

3 Capital Management Structure and Policies (continued)

3.4. Risk Weighted Assets (continued)

3.4.3 Operational Risk Weighted Assets

In accordance with Basel III guidelines operational risk charge is computed by multiplying the beta factors of respective banking business activities as required by the Standardised Approach. The total capital requirement for Operational Risk as at 31 December 2019 is AED 1,567 million (31 December 2018 was AED 1,393 million).

3.5. Qualitative Risk Disclosures

For each separate risk area (credit, market, operational and equity risk) banks are required to describe their risk management objectives and policies, which primarily include strategies, processes, organization framework, reporting and measurement systems. These disclosures are discussed and are set out in the "Risk Management" section of the DIB 2019 Annual Report and Notes 48 of the audited consolidated financial statements. Also, refer to section 4 of this report for cross-referencing information.

4. Risk Management Objectives and Policies

4.1. Introduction

Risk is inherent in the Group's activities and is managed through a process of ongoing identification, measurement and monitoring, subject to risk limits and other controls. This process of risk management is critical to the Group's continuing profitability and each individual within the Group is accountable for the risk exposures relating to his responsibilities.

The Group is exposed to various risks including:

- Credit risk;
- Liquidity risk;
- Market risk; and
- Operational risk.

The independent risk control process does not include business risks such as changes in the environment, technology and industry. These risks are monitored through strategic planning process.

4.1.1 Risk Management Structure

The Board of Directors, supported by the Board Risk Management Committee, Risk Management Committee of the management and Risk Management Department, is ultimately responsible for identifying, monitoring and controlling risks; additionally there are other independent bodies / functions also responsible for managing and monitoring risks.

Board of Directors

The Board of Directors is responsible for the overall risk management approach and for approving the risk strategies and policies

Board Risk Management Committees

The Board Risk Management Committee has the overall responsibility for the development of the risk strategies, frameworks, policies and limits, and for recommending these strategies and policies to the Board of Directors. It is responsible for the fundamental risk issues, and manages and monitors relevant risk decisions.

Risk Management Committee

The day-to-day monitoring of risk has been delegated to Risk Management Committee.

The Risk Management Committee has the overall responsibility to support the Board Risk Management Committee for the development and formulation of the risk strategies, frameworks, policies and limits. It is responsible for ensuring the compliance with all risk limits, monitoring risk exposures and implementing the regulatory guidelines issued by the regulatory bodies (e.g. The Central Bank of the U.A.E.).

Risk Management Department

The Risk Management Department is responsible for implementing and maintaining risk related procedures to ensure risk remains within the acceptable range as approved by the Board Risk Management Committee and the Board of Directors. The department is responsible for credit administration, portfolio management, credit risk, market risk, operational risk and overall risk control.

Asset and Liability Management Committee

Asset and Liability Management Committee ("ALCO") is responsible for managing the Group's assets and liabilities and the overall financial structure. It is also primarily responsible for the funding and liquidity risks of the Group.

Internal Audit Department

Risk management processes throughout the Group are audited periodically by the Internal Audit Department which examines both the adequacy of the procedures and the Group's compliance with the procedures. Internal Audit Department comments on the results of their assessments with management, and reports its findings and recommendations to the Board Audit Committee.

4. Risk Management Objectives and Policies (continued)

4.1. Introduction (continued)

4.1.2 Risk Measurement and Reporting Systems

The Group measures risks using qualitative as well as quantitative methods for credit, market, liquidity and operational risks. Further, the Group also uses quantitative analysis and methods to support revisions in business and risk strategies as and when required. These analysis and methods reflect both the expected loss likely to arise in normal course of business or unexpected losses in an unforeseen event based on simple statistical techniques and probabilities derived from historical experience. The Group also runs stress scenarios that would arise in the event that extreme events which are unlikely to occur do, in fact, occur.

Monitoring and controlling risks is primarily performed based on limits established by the Board of Directors and management. These limits reflect the business strategy and market environment of the Group as well as the level of risk that the Group is willing to accept, with additional emphasis on selected industries.

Information compiled from all the businesses is examined and processed in order to analyze the risk profile and identify early risks. This information is presented and explained to the management, management committees, the Risk Management Committee, and Board Risk Management Committee. Specialized reports are presented to the pertinent heads of business and are delivered with a frequency suited to the volatility of the risk. The report includes aggregate credit exposure, limit exceptions, liquidity, operational loss incidents and other risk profile changes. On a monthly basis, detailed reporting of industry, customer and geographic risks takes place. Senior management assesses the appropriateness of the provision for impairment losses on a quarterly basis.

4.1.3 Model Risk Management

The Bank uses a number of quantitative models in many of its financial and business activities from underwriting a credit facility to reporting expected credit losses under IFRS 9.

To manage the model risks, the Bank has developed and implemented Model Governance Framework which contains Bank wide development, implementation and validation policies and practices. According to the framework, all internally or externally developed risk quantification models that directly affect the financial reporting on expected credit losses require validation periodically (internally or externally). Model Risk Management Committee (MRMC) is responsible for overseeing all model related development, implementation of framework and performance of the models. MRMC reports to Risk Management Committee of the Bank.

The Framework establishes a systematic approach to manage the development, implementation, approval, validation and ongoing use of models. It sets out an effective governance and management structure with clearly defined roles and responsibilities, policies and controls for managing model risk. The Framework is reviewed on a regular basis to ensure it meets regulatory standards and international practices. Any major change to the Framework is approved by the Risk Management Committee upon recommendation of MRMC.

The Bank has an independent validation function that performs independent model validation. It provides Fit-for Purpose, Conditional Approval or Not Fit-for-Purpose recommendation to MRMC to approve the use of the new risk quantification / valuation models. In addition to new model validation, the validation function also evaluates the performance of existing models through an annual validation process.

4.1.4 Risk Mitigation

As part of its overall risk management, the Group uses various methods to manage exposures resulting from changes in credit risks, liquidity risks, market risks (including profit rate risk, foreign exchange risk, and equity price risk), and operational risks.

The Group seeks to manage its credit risk exposures through diversification of financing and investing activities to avoid undue concentration of risk with individuals and groups of customers in specific locations or businesses. The Group actively uses collateral to reduce its credit risks.

In order to guard against liquidity risk, management has diversified funding sources and assets are managed with overall liquidity in consideration maintaining a healthy balance of liquid assets (i.e. cash and cash equivalents).

The market risks are managed on the basis of predetermined asset allocation across various asset categories and continuous appraisal of market conditions for movement and expectation of foreign currencies rate, bench mark profit rates and equity prices.

4. Risk Management Objectives and Policies (continued)

4.1. Introduction (continued)

4.1.4 Risk Mitigation (continued)

To manage all other risks, the Group has developed a detailed risk management framework to identify and apply resources to mitigate the risks.

4.1.5 Risk Concentration

Concentrations arise when a number of counterparties are engaged in similar business activities, or activities in the same geographic region, or have similar economic features that would cause their ability to meet contractual obligations to be similarly affected by changes in economic, political or other conditions. Concentrations indicate the relative sensitivity of the Bank performance to developments affecting a particular industry or geographical location.

4.2 Credit Risk

In order to avoid excessive concentrations of risk, the Group's policies and procedures include specific guidelines to focus on maintaining a diversified portfolio. Identified concentrations of credit risks are controlled and managed accordingly.

Credit Risk Measurement

The Group assesses the probability of default of individual counterparties using internal rating tools tailored to the various categories of counterparties. Whilst some of the models for assessment of Real Estate projects are internally developed, others for the Corporate, Contracting and SME businesses have been acquired from Moody's and subsequently optimized and calibrated to the Group's internal rating scale. The models are housed with the Moody's Risk Analyst rating tool.

The rating tools are kept under review and upgraded as necessary. The Group regularly validates the performance of the rating and their predictive power with regard to default events.

Collateral

The Group employs a range of policies and practices to mitigate credit risk. The most traditional of these is the taking of securities for facilities provided, which is a common practice. The Group implements guidelines on the acceptability of specific classes of collateral or credit risk mitigation. The principal collateral types for Islamic financing and investing assets are:

- Mortgages over residential and commercial properties;
- Corporate guarantees;
- Charges over business assets such as premises, machinery, vehicles and inventory; and
- Charges over financial instruments such as deposits and equity investments.

Islamic derivative financial instruments

Credit risk arising from Islamic derivative financial instruments is, at any time, limited to those with positive fair values, as recorded in the consolidated financial position.

Credit – Related Commitments Risks

The Bank makes available to its customers guarantees and letters of credit which require that the Bank makes payments in the event that the customer fails to fulfil certain obligations to other parties. This exposes the Group to a similar risk to Islamic financing and investing assets and these are mitigated by the same control processes and policies.

4.2.1 Maximum exposure to credit risk without taking account of any collateral and other credit mitigation

The table below shows the maximum exposure to credit risk by class of financial asset, including Islamic derivatives. The maximum exposure is shown gross, before the effect of mitigation through the use of risk mitigation and collateral agreements.

4. Risk Management Objectives and Policies (continued)

4.2 Credit Risk (continued)

4.2.1 Maximum exposure to credit risk without taking account of any collateral and other credit mitigation (continued)

	Gross maximum exposure 2019 AED'000	Gross maximum exposure 2018 AED'000
Balances with central banks	**19,598,494**	20,878,794
Due from banks and financial institutions	**6,251,739**	8,297,032
Islamic financing and investing assets	**156,994,111**	150,465,957
Investment in Islamic Sukuk measured at amortised cost	**33,343,437**	31,268,322
Other investments measured at fair value	**1,266,235**	1,687,824
Receivables and other assets	**9,406,206**	6,646,455
	226,860,222	219,244,384
Contingent liabilities	**14,454,548**	15,432,639
Commitments	**19,440,465**	18,686,154
Total	**260,755,235**	253,363,177

4.2.2 Risk concentrations of the maximum exposure to credit risk

Concentration of risk is managed by client/counterparty, by geographical region and by industry sector. The Bank's financial assets, before taking into account any collateral held or other credit enhancement can be analysed by the following geographical regions:

	2019 AED'000	2018 AED'000
The U.A.E.	**228,699,898**	224,421,279
Other Gulf Cooperation Council (GCC) countries	**10,364,264**	9,647,147
Asia	**14,595,349**	13,405,831
Europe	**5,804,403**	4,416,400
Africa	**543,349**	467,606
Others	**747,972**	1,004,914
Total	**260,755,235**	253,363,177

4. Risk Management Objectives and Policies (continued)

4.2 Credit Risk (continued)

4.2.2 Risk concentrations of the maximum exposure to credit risk (continued)

An industry sector analysis of the Bank's financial assets, before taking into account collateral held or other credit enhancement, is as follows:

	Gross Maximum Exposure 2019 AED'000	Gross Maximum Exposure 2018 AED'000
Government	**27,589,909**	23,494,616
Financial Institutions	**44,856,620**	46,141,576
Real estate	**51,764,791**	48,386,477
Contracting	**13,831,768**	14,233,003
Trade	**12,440,448**	11,136,355
Aviation	**19,808,739**	21,852,705
Services and manufacturing	**44,778,960**	44,742,199
Consumer financing	**30,874,518**	29,498,112
Consumer home finance	**14,809,482**	13,878,134
Total	**260,755,235**	253,363,177

4. Risk Management Objectives and Policies (continued)

4.2 Credit Risk (continued)

4.2.3 Gross credit risk exposures as per Basel III standardized approach

The gross credit exposure as per standardized approach with the effect of CRM as of 31 December 2019 is detailed below:

December 2019 AED'000	On & Off Balance Sheet Gross Outstanding	Credit Risk Mitigation (CRM) Exposure Before Credit Risk Mitigation (CRM)	Credit Risk Mitigation (CRM)	Net exposure after CCF	Risk Weighted Assets
Claims on sovereigns	47,834,224	47,834,224	–	47,110,334	10,010,869
Claims on non-commercial public sector enterprises (PSEs)	2,322,837	2,322,837	–	2,322,837	–
Claims On Multi-Lateral Development Banks	156,142	156,142	–	156,142	–
Claims on banks	48,561,218	48,561,218	16,713	9,955,814	4,234,539
Claims on corporate and government related enterprises	163,214,189	163,208,719	9,434,215	105,115,608	104,153,535
Claims included in the regulatory retail portfolio	26,016,259	26,014,098	1,025,682	24,985,765	18,856,457
Claims secured by residential property	13,944,194	13,802,754	–	13,802,754	7,738,447
Claims secured by commercial real estate	10,149,136	10,051,183	132,774	9,934,034	9,925,709
Past due financing assets	8,758,447	4,339,072	1,801	4,302,801	5,308,521
Higher-risk categories	704,178	704,178	293,585	410,593	615,889
Other assets	13,016,841	13,016,841	62,113	12,954,728	11,630,045
Total	334,677,665	330,011,266	10,966,882	231,051,411	172,474,010

4. Risk Management Objectives and Policies (continued)

4.2 Credit Risk (continued)

4.2.3 Gross credit risk exposures as per Basel III standardized approach (continued)

The gross credit exposure as per standardized approach with the effect of CRM as of 31 December 2018 is detailed below:

December 2018 AED'000	On & Off Balance Sheet Gross Outstanding	Credit Risk Mitigation (CRM) Exposure Before Credit Risk Mitigation (CRM)	Credit Risk Mitigation (CRM)	Net exposure after CCF	Risk Weighted Assets
Claims on sovereigns	45,000,457	45,000,457	–	45,000,148	7,746,833
Claims on non-commercial public sector enterprises (PSEs)	2,497,595	2,497,595	–	2,497,595	–
Claims On Multi-Lateral Development Banks	155,694	155,694	–	155,694	–
Claims on banks	41,682,408	41,682,408	9,750	11,921,017	4,183,427
Claims on corporates and government related enterprises	156,079,933	156,061,955	10,958,600	101,738,528	99,967,366
Claims included in the regulatory retail portfolio	24,197,035	24,195,571	371,581	23,817,905	18,021,764
Claims secured by residential property	12,868,488	12,725,878	10,658	12,715,221	6,928,586
Claims secured by commercial real estate	10,116,868	10,102,730	575,810	9,754,471	9,640,128
Past due financing assets	7,438,094	3,577,525	586,463	2,921,168	3,621,307
Higher-risk categories	838,933	838,933	293,585	545,348	818,022
Other assets	10,590,073	10,325,380	124,221	10,201,160	10,810,544
Total	311,465,578	307,164,126	12,930,669	221,268,255	161,737,978

4. Risk Management Objectives and Policies (continued)

4.2 Credit Risk (continued)

4.2.4 Gross credit risk exposures as per standardised approach

The gross credit exposures as per standardized approach in terms of rated/unrated assets as of 31 December 2019 is detailed below:

AED'000	Ra	Unrated	Total Gross Outstanding	Exposure Before CRM	Credit Risk Mitigation	Net exposure after CCF	Risk Weighted Assets
Claims on sovereigns	20,447,'	27,386,440	47,834,224	47,834,224	–	47,110,334	10,010,869
Claims on non-commercial public sector enterprises (PSEs)		2,322,837	2,322,837	2,322,837	–	2,322,837	–
Claims On Multi-Lateral Development Banks	156,:	–	156,142	156,142	–	156,142	–
Claims on banks	42,030,4	6,530,783	48,561,218	48,561,218	16,713	9,955,814	4,234,539
Claims on corporates and government related enterprises (GREs)	10,559,:	152,654,937	163,214,189	163,208,719	9,434,215	105,115,608	104,153,535
Claims included in the regulatory retail portfolio		26,016,259	26,016,259	26,014,098	1,025,682	24,985,765	18,856,457
Claims secured by residential property		13,944,194	13,944,194	13,802,754	–	13,802,754	7,738,447
Claims secured by commercial real estate		10,149,136	10,149,136	10,051,183	132,774	9,934,034	9,925,709
Past due financing assets		8,758,447	8,758,447	4,339,072	1,801	4,302,801	5,308,521
Higher-risk categories		704,178	704,178	704,178	293,585	410,593	615,889
Other assets		13,016,841	13,016,841	13,016,841	62,113	12,954,728	11,630,045
Total	73,193,613	261,484,052	334,677,665	330,011,266	10,966,882	231,051,411	172,474,010

4. Risk Management Objectives and Policies (continued)

4.2 Credit Risk (continued)

4.2.4 Gross credit risk exposures as per standardised approach (continued)

The gross credit exposures as per standardized approach in terms of rated/unrated assets as of 31 December 2018 is detailed below:

AED'000	Rated	Unrated	Total Gross Outstanding	Exposure Before CRM	Credit Risk Mitigation	Net exposure after CCF	Risk Weighted Assets
Claims on sovereigns	34,642,978	10,357,479	45,000,457	45,000,457	–	45,000,148	7,746,833
Claims on non-commercial public sector enterprises (PSEs)	–	2,497,595	2,497,595	2,497,595	–	2,497,595	–
Claims On Multi-Lateral Development Banks	155,694	–	155,694	155,694	–	155,694	–
Claims on banks	37,465,446	4,216,962	41,682,408	41,682,408	9,750	11,921,017	4,183,427
Claims on corporates and government related enterprises (GREs)	10,226,789	145,853,144	156,079,933	156,061,955	10,958,600	101,738,528	99,967,366
Claims included in the regulatory retail portfolio	–	24,197,035	24,197,035	24,195,571	371,581	23,817,905	18,021,764
Claims secured by residential property	–	12,868,488	12,868,488	12,725,878	10,658	12,715,221	6,928,586
Claims secured by commercial real estate	–	10,116,868	10,116,868	10,102,730	575,810	9,754,471	9,640,128
Past due financing assets	–	7,438,094	7,438,094	3,577,525	586,463	2,921,168	3,621,307
Higher-risk categories	–	838,933	838,933	838,933	293,585	545,348	818,022
Other assets	–	10,590,073	10,590,073	10,325,380	124,221	10,201,160	10,810,544
Total	82,490,907	228,974,671	311,465,578	307,164,126	12,930,669	221,268,255	161,737,978

4. Risk Management Objectives and Policies (continued)

4.2 Credit Risk (continued)

4.2.5 Analysis of credit quality

2019	Balances with central banks and due from banks and financial institutions	Islamic financing and investing assets	Investments in Islamic Sukuk and other investments at fair value	Receivables and other assets	Contingent liabilities and commitments	Total
	AED'000	AED'000	AED'000	AED'000	AED'000	AED'000
Individually impaired	-	6,225,171	-	707,057	-	6,932,228
Non-impaired exposures						
Neither past due nor impaired	25,850,233	147,221,209	34,609,672	8,358,167	33,895,013	249,934,294
Past due by less than 30 days	-	2,046,910	-	-	-	2,046,910
Past due by more than 30 days but less than 90 days	-	1,416,096	-	-	-	1,416,096
Past due by more than 90 days	-	84,725	-	340,982	-	425,707
Gross amount	25,850,233	150,768,940	34,609,672	8,699,149	33,895,013	253,823,007
Total gross maximum exposure	25,850,233	156,994,111	34,609,672	9,406,206	33,895,013	260,755,235
Provisions for impairment	(3,566)	(6,080,683)	(99,579)	(356,531)	-	(6,540,359)
Net carrying amount	25,846,667	150,913,428	34,510,093	9,049,675	33,895,013	254,214,876

4. Risk Management Objectives and Policies (continued)

4.2 Credit Risk (continued)

4.2.5 Analysis of credit quality (continued)

2018

	Balances with central banks and due from banks and financial institutions	Islamic financing and investing assets	Investments in Islamic Sukuk and other investments at fair value	Receivables and other assets	Contingent liabilities and commitments	Total
Individually impaired	-	5,030,370	-	1,069,895	-	6,100,265
Non-impaired exposures						
Neither past due nor impaired	29,175,826	142,005,402	32,956,146	5,576,560	34,118,793	243,832,727
Past due by less than 30 days	-	1,899,731	-	-	-	1,899,731
Past due by more than 30 days but less than 90 days	-	1,310,317	-	-	-	1,310,317
Past due by more than 90 days	-	220,137	-	-	-	220,137
Gross amount	29,175,826	145,435,587	32,956,146	5,576,560	34,118,793	247,262,912
Total gross maximum exposure	29,175,826	150,465,957	32,956,146	6,646,455	34,118,793	253,363,177
	========	========	========	========	========	=========
Provisions for impairment	-	(5,727,372)	(89,797)	(660,224)	-	(6,477,393)
Net carrying amount	29,175,826	144,738,585	32,866,349	5,986,231	34,118,793	246,885,784
	========	=========	=========	========	========	=========

4. Risk Management Objectives and Policies (continued)

4.2 Credit Risk (continued)

4.2.6 Credit risk exposure of the Banks's financial assets for each internal risk rating

	Moody's equivalent grades	Total 2019 AED'000	Total 2018 AED'000
Low risk			
Risk rating classes 1 to 3	Aaa – A3	**105,962,274**	107,497,972
Moderate risk			
Risk rating classes 4 to 5	Baa1 – Ba3	**117,632,360**	109,157,850
Fair risk			
Risk rating classes 6 to 7	B1 - Caa3	**29,933,278**	30,459,297
Default			
Risk rating classes 8 to11	Ca - C	**7,227,323**	6,248,058
		260,755,235	253,363,177

It is the Bank's policy to maintain accurate and consistent risk ratings across the credit portfolio. This facilitates focused management of the applicable risks and the comparison of financing exposures across all lines of business, geographic regions and products. All internal risk ratings are tailored to the various categories and are derived in accordance with the Bank rating policy. The attributable risk ratings are assessed and updated regularly.

4.2.7 Analysis by Economic Sector and Geography

The details of financing and investing assets by economic activity and geography are as below:

	Within the U.A.E. AED'000	Outside the U.A.E. AED'000	Total AED'000
2019			
Government	**6,277,755**	**2,852,836**	**9,130,591**
Financial institutions	**5,816,744**	**944,382**	**6,761,126**
Real estate	**32,289,495**	**511,083**	**32,800,578**
Contracting	**5,073,452**	**944,228**	**6,017,680**
Trade	**7,514,410**	**713,249**	**8,227,659**
Aviation	**17,488,595**	**-**	**17,488,595**
Services and others	**31,840,318**	**3,540,207**	**35,380,525**
Consumer home finance	**26,134,291**	**501,520**	**26,635,811**
Consumer financing	**14,283,393**	**268,153**	**14,551,546**
	146,718,453	**10,275,658**	**156,994,111**
Less: provision for impairment			**(6,080,683)**
Total			**150,913,428**

4. Risk Management Objectives and Policies (continued)

4.2 Credit Risk (continued)

4.2.7 Analysis by Economic Sector and Geography (continued)

2018	Within the U.A.E. AED'000	Outside the U.A.E. AED'000	Total AED'000
Government	5,745,492	1,521,827	7,267,319
Financial institutions	5,830,020	644,686	6,474,706
Real estate	28,581,368	261,913	28,843,281
Contracting	5,799,483	964,868	6,764,351
Trade	7,564,031	682,717	8,246,748
Aviation	18,770,762	113,493	18,884,255
Services and others	31,220,294	3,178,972	34,399,266
Consumer home finance	13,357,669	290,197	13,647,866
Consumer financing	25,396,744	541,421	25,938,165
	142,265,863	8,200,094	150,465,957
Less: provision for impairment			(5,727,372)
Total			144,738,585

4.2.8 Provision for impairment

2019	**Stage 1 AED'000**	**Stage 2 AED'000**	**Stage 3 AED'000**	**Total AED'000**
Balance at 1 January	**1,014,083**	**1,006,837**	**3,706,452**	**5,727,372**
Impairment charge during the year	**61,123**	**(40,646)**	**2,074,820**	**2,095,297**
Write back/recoveries during the year	**-**	**-**	**(434,522)**	**(434,522)**
Write off	**-**	**-**	**(1,311,317)**	**(1,311,317)**
Exchange and other adjustments	**789**	**(246)**	**3,310**	**3,853**
Balance at 31 December	**1,075,995**	**965,945**	**4,038,743**	**6,080,683**

2018	Stage 1 AED'000	Stage 2 AED'000	Stage 3 AED'000	Total AED'000
Balance at 1 January	1,810,964	-	3,921,704	5,732,668
Reversal on transition to IFRS 9	(1,810,964)	-	-	(1,810,964)
ECL recognized on adoption of IFRS 9	1,380,253	696,072	-	2,076,325
Balance at 1 January - restated	1,380,253	696,072	3,921,704	5,998,029
Impairment charge during the year	(348,732)	311,109	1,827,006	1,789,383
Write back/recoveries during the year	-	-	(869,492)	(869,492)
Write off	-	-	(1,165,634)	(1,165,634)
Exchange and other adjustments	(17,438)	(344)	(7,132)	(24,914)
Balance at 31 December	1,014,083	1,006,837	3,706,452	5,727,372

5. Impairment Assessment

5.1 Impairment of Financial Assets

Financial assets that are measured at amortized cost are assessed for impairment at each reporting date.

The Bank applies a three-stage approach to measure allowance for credit losses, using an expected credit loss approach as required under IFRS 9, for the following categories of financial instruments that are measured at amortized cost:

- Islamic financing and investing assets and investment in Islamic Sukuks;
- Off-balance sheet instruments issued;
- Financial guarantee contracts issued;
- Due from banks and financial institutions;
- Balances with Central Banks; and
- Other financial assets

Financial assets migrate through three stages based on the change in credit risk since initial recognition.

No impairment loss is recognized on equity investments.

Excepted credit loss impairment model

The Expected Credit Loss (ECL) model contains a three stage approach which is based on the change in credit quality of financial assets since initial recognition. Expected credit losses reflect the present value of all cash shortfalls related to default events either (i) over the following twelve months or (ii) over the expected life of a financial instrument depending on credit deterioration from inception.

- Under Stage 1, where there has not been a significant increase in credit risk since initial recognition, an amount equal to 12 months ECL will be recorded. The 12 months ECL is calculated as the portion of life time ECL that represents the ECL that result from default events on a financial instrument that are possible within the 12 months after the reporting date. The Bank calculates the 12 months ECL allowance based on the expectation of a default occurring in the 12 months following the reporting date. These expected 12 month default probabilities are applied to a forecast EAD and multiplied by the expected LGD and discounted by an approximation to the original effective profit rate.
- Under Stage 2, where there has been a significant increase in credit risk since initial recognition but the financial instruments are not considered credit impaired, an amount equal to the default probability weighted lifetime ECL will be recorded. The PD and LGD are estimated over the lifetime of the instrument and the expected cash shortfalls are discounted by an approximation to the original effective profit rate.
- Under the Stage 3, where there is objective evidence of impairment at the reporting date these financial instruments will be classified as credit impaired and an amount equal to the lifetime ECL will be recorded for the financial assets, with the PD set at 100%.

When estimating ECL for undrawn commitments, the Bank estimates the expected portion of the 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 financing is drawn down. The expected cash shortfalls are discounted at an approximation to the expected effective profit rate on the financing.

The Bank's liability under each guarantee is measured at the higher of the amount initially recognized less cumulative amortization recognized in the income statement, and the ECL provision. For this purpose, the Bank 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 rate relevant to the exposure.

The ECL model is forward looking and requires the use of reasonable and supportable forecasts of future economic conditions in the determination of significant increases in credit risk and measurement of ECL.

Measurement of ECL

The Bank calculates ECLs based on probability-weighted scenarios to measure the expected cash shortfalls, discounted at an approximation to the effective profit rate. A cash shortfall is the difference between the cash flows that are due to the Bank in accordance with the contract and the cash flows that the Bank expects to receive. IFRS 9 considers the calculation of ECL by multiplying the Probability of default (PD), Loss Given Default (LGD) and Exposure at Default (EAD). The Bank has developed methodologies and models taking into account the relative size, quality and complexity of the portfolios.

5. Impairment Assessment (continued)

5.1 Impairment of Financial Assets (continued)

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

Details of these statistical parameters/inputs are as follows:

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

Macroeconomic factors, forward looking information and multiple scenarios

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

When estimating the ECLs, the Bank considers three scenarios (a base case, an upside and a downside). Each of these is associated with different PDs, EADs and LGDs. When relevant, the assessment of multiple scenarios also incorporates how defaulted financing are expected to be recovered, including the probability that the financing will cure and the value of collateral or the amount that might be received for selling the asset.

In its ECL models, the Bank relies on a broad range of forward looking information as economic inputs, such as:

- Average oil prices
- Non-oil Economic Composite Index (ECI) of UAE
- Economic composite index of UAE
- Real estate prices of Dubai and Abu Dhabi
- Dubai hotel room occupancy

Macroeconomic factors and forward looking information are required to be incorporated into the measurement of ECL as well as the determination of whether there has been a significant increase in credit risk since origination. Measurement of ECLs at each reporting period should reflect reasonable and supportable information at the reporting date about past events, current conditions and forecasts of future economic conditions. The inputs and models used for calculating ECLs may not always capture all characteristics of the market at the date of the financial statements. To reflect this, qualitative adjustments or overlays are occasionally made as temporary adjustments when such differences are significantly material.

Assessment of significant increase in credit risk

The assessment of a significant increase in credit risk is done on a relative basis. To assess whether the credit risk on a financial asset has increased significantly since origination, the Bank compares the risk of default occurring over the expected life of the financial assets at the reporting date to the corresponding risk of default at origination, using key risk indicators that are used in the Bank's existing risk management processes. At each reporting date, the assessment of a change in credit risk will be individually assessed for those considered individually significant and at the segment level for retail exposures.

The group of assets are moved from stage 1 to stage 2 if:

- the probability of default changes beyond the Bank's established threshold related to the initial recognition;
- an instrument is past due beyond 30 days; and
- an instrument's credit risk is considered higher based on qualitative criteria of the Bank.

The instruments moved to stage 2 from stage 1 remain in the stage until they perform for a sustained period as per Bank's policy.

Movement from stage 2 to stage 3 are based on whether the financial assets are credit impaired at the reporting date. The determination of the credit impairment remains unchanged in IFRS 9 consistent with IAS 39.

5. Impairment Assessment (continued)

5.1 Impairment of Financial Assets (continued)

Experienced credit judgement

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

When measuring ECL, the Bank considers the maximum contractual period over which the Bank is exposed to credit risk. All contractual terms are considered when determining the expected life, including prepayment options and extension and rollover options.

Default definition followed by the Bank for impairment assessment remains in line with the guidelines of IFRS 9, without any recourse to the assumptions, and consistent with regulatory requirements.

Expected life

When measuring expected credit loss, the Bank considers the maximum contractual period over which the Bank is exposed to credit risk. All contractual terms are considered when determining the expected life, including prepayment, and extension and rollover options.

Renegotiated financing facilities

The Bank sometimes makes concessions or modifications to the original terms of financing as a response to the customer's financial difficulties, rather than taking possession or to otherwise enforce collection of collateral. The Bank considers a financing forborne when such concessions or modifications are provided as a result of the customer's present or expected financial difficulties and the Bank would not have agreed to them if the customer had been financially healthy. Indicators of financial difficulties include defaults on covenants or that a customer may not be in a position to honour contractual commitments. Forbearance may involve extending the payment arrangements and the agreement of new financing conditions. Once the terms have been renegotiated, any impairment is measured using the original effective profit rate as calculated before the modification of terms. It is the Bank's policy to monitor forborne financing to help ensure that future payments continue to be likely to occur. Classification between Stage 2 and Stage 3 are determined on a case-by-case basis. If these procedures identify a loss in relation to a financing, it is disclosed and managed as an impaired Stage 3 forborne asset until it is collected or written off.

When the financing has been renegotiated or modified but not derecognized, the Bank also reassesses whether there has been a significant increase in credit risk. The Bank also considers whether the assets should be classified as Stage 3. Once an asset has been classified as forborne, it will remain forborne for a minimum 12-month probation period. In order for the financing to be reclassified out of the forborne category, the customer has to meet all of the following criteria:

- All of its facilities has to be considered performing;
- The probation period of one year has passed from the date the forborne contract was considered performing; and
- Regular payments of more than an insignificant amount of principal or profit have been made during the probation period.

Definition of default

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

- it is established that due to financial or non-financial reasons the customer is unlikely to pay its credit obligations to the Bank in full without recourse by the Bank to actions such as realizing security (if any is held); or
- the customer is past due 90 days or more on any material credit obligation to the Bank.

In assessing whether a customer is in default, the Bank considers indicators that are:

(i) qualitative - e.g. material breaches of covenant;
(ii) quantitative - e.g. overdue status and non-payment on another obligation of the same customer / customer group to the banks; and
(iii) based on data developed internally and obtained from external sources.

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

5. Impairment Assessment (continued)

5.2 Carrying value of gross exposure by internal risk rating category and by ECL stage

As at 31 December 2019

	Gross exposure (AED'000)				Expected credit loss (ECL) (AED'000)			
	Stage 1	**Stage 2**	**Stage 3**	**Total**	**Stage 1**	**Stage 2**	**Stage 3**	**Total**
Low	**43,764,785**	**-**	**-**	**43,764,785**	**9,668**	**-**	**-**	**9,668**
Moderate	**81,014,810**	**5,793,870**	**-**	**86,808,680**	**850,024**	**330,841**	**-**	**1,180,865**
Fair	**13,887,833**	**6,307,642**	**-**	**20,195,475**	**216,303**	**635,104**	**-**	**851,407**
Default	**-**	**-**	**6,225,171**	**6,225,171**	**-**	**-**	**4,038,743**	**4,038,743**
Total	**138,667,428**	**12,101,512**	**6,225,171**	**156,994,111**	**1,075,995**	**965,945**	**4,038,743**	**6,080,683**

As at 31 December 2018

	Gross exposure (AED'000)				Expected credit loss (ECL) (AED'000)			
	Stage 1	Stage 2	Stage 3	Total	Stage 1	Stage 2	Stage 3	Total
Low	43,505,321	-	-	43,505,321	7,338	-	-	7,338
Moderate	77,090,046	4,576,803	-	81,666,849	871,351	294,077	-	1,165,428
Fair	11,653,006	8,610,411	-	20,263,417	135,394	712,760	-	848,154
Default	-	-	5,030,370	5,030,370	-	-	3,706,452	3,706,452
Total	132,248,373	13,187,214	5,030,370	150,465,957	1,014,083	1,006,837	3,706,452	5,727,372

6. Liquidity Risk

6.1 Liquidity Risk and Funding Management

Liquidity risk is the risk that the Group will be unable to meet its payment obligations when they fall due under normal and stress circumstances. To limit this risk, management has arranged diversified funding sources in addition to its core deposit base, manages assets with liquidity in mind, and monitors future cash flows and liquidity on a daily basis. This incorporates an assessment of expected cash flows and the availability of high grade collateral which could be used to secure additional funding if required.

The Bank maintains a portfolio of highly marketable and diverse assets that can be easily liquidated in the event of an unforeseen interruption of cash flow. The Group also has committed lines of credit that it can access to meet liquidity needs. In addition, the Group maintains statutory deposits with the central banks. The liquidity position is assessed and managed under a variety of scenarios, giving due consideration to stress factors relating to both the market in general and specifically to the Group.

The high quality of the asset portfolio ensures its liquidity and coupled with the Group's own funds and stable customer deposits help form a stable funding source. Even under adverse conditions, the Group has access to the funds necessary to cover customer needs and meet its funding requirements.

The primary tool (in addition to other tools) for monitoring liquidity is the maturity mismatch analysis, which is monitored over successive time bands and across functional currencies. Guidelines are established for the cumulative negative cash flow over successive time bands.

6.1.1 Liquidity risk management process

The Group liquidity risk management process, as carried out within the Group and monitored by a separate team in Group Treasury department, includes:

- Monitoring future cash flows to ensure that requirements can be met. This includes replenishment of funds as they mature or are financed by customers;
- Maintaining a portfolio of highly marketable assets that can easily be liquidated as protection against any unforeseen interruption to cash flow;
- Monitoring financial position liquidity ratios against internal and regulatory requirements;
- Managing the concentration and profile of Islamic financing and investing exposures maturities; and
- Monitoring liquidity ratios

6.2 Funding Approach

Sources of liquidity are regularly reviewed by management to maintain a wide diversification by currency, geography, provider, product and term.

The Bank issued Tier 1 Sukuk of AED 3,673 million (USD 1,000 million) each during the year ended 31 December 2013 and 31 December 2015 and AED 2,755 million (USD 750 million) during the year ended 31 December 2019 to diversify sources of funding to support business growth.

6.2.1 Non-derivative cash flows

The table below summarises the maturity profile of the gross cash flows of the Group financial assets and liabilities as at 31 December 2019 and 2018. The amounts disclosed in the table are the contractual gross cash flows, whereas the Group manages the inherent liquidity risk based on expected gross cash flows.

Repayments which are subject to notice are treated as if notice were to be given immediately. However, the management expects that many customers will not request repayment on the earliest date the Group could be required to pay and the table does not reflect the expected cash flows indicated by the Group's deposit retention history.

6. Liquidity Risk (continued)

6.2 Funding Approach (continued)

6.2.2 Non-derivative cash flows

2019	Less than 3 months AED'000	3 months to 1 year AED'000	1 to 5 years AED'000	Over 5 Years AED'000	Total AED'000
Customers' deposits	**79,007,795**	**69,490,524**	**18,784,535**	**5,968**	**167,288,822**
Due to banks and other financial institutions	**3,643,219**	**2,995,802**	**2,573,263**	**-**	**9,212,284**
Sukuk issued	**-**	**2,788,266**	**13,231,779**	**179,243**	**16,199,288**
Payables and other liabilities	**3,365,945**	**3,562,161**	**1,164,799**	**15,706**	**8,108,611**
Zakat payable	**-**	**326,895**	**-**	**-**	**326,895**
Total liabilities	**86,016,959**	**79,163,648**	**35,754,376**	**200,917**	**201,135,900**

2018	Less than 3 months AED'000	3 months to 1 year AED'000	1 to 5 years AED'000	Over 5 Years AED'000	Total AED'000
Customers' deposits	68,569,499	79,407,021	9,557,776	159,677	157,693,973
Due to banks and other financial institutions	5,484,613	5,672,249	2,154,680	-	13,311,542
Sukuk issued	-	260,752	13,546,483	286,057	14,093,292
Payables and other liabilities	4,348,863	2,146,949	1,232,898	-	7,728,709
Zakat payable	-	305,202	-	-	305,202
Total liabilities	78,402,975	87,792,173	26,491,837	445,734	193,132,718

Assets available to meet all of the liabilities and to cover outstanding commitments include cash and balances with central banks, Islamic financing and investing assets, other investments at fair value and items in the course of collection.

6.2.3 Islamic derivatives financial instruments

Fair values of Islamic derivative financial instruments:

The table below shows the positive and negative fair values of Islamic derivative financial instruments, which are equivalent to the market values, together with the notional amounts analysed by the term to maturity. The notional amount is the amount of an Islamic derivative's underlying asset, reference rate or index and is the basis upon which changes in the value of Islamic derivatives are measured. The notional amounts indicate the volume of transactions outstanding at year end.

6. Liquidity Risk (continued)

6.2 Funding Approach (continued)

6.2.3 Islamic derivatives financial instruments (continued)

	Positive fair value	Negative fair value	Notional amount total	Notional amounts by term to maturity: Within 3 months	Over 3 months to 1 year	Over 1 year to 3 years	Over 3 to 5 years	Over 5 years
	AED'000	AED'000	AED'000	AED'000	AED'000	AED'000	AED'000	AED'000
2019								
Islamic Derivatives held for trading:								
Unilateral promise to buy/sell currencies	**92,966**	**93,242**	**11,145,753**	**4,789,269**	**6,356,484**	**-**	**-**	**-**
Islamic profit rate swaps	**762,551**	**649,060**	**58,353,599**	**1,406,305**	**3,601,355**	**10,877,838**	**16,747,950**	**25,720,151**
Islamic currency (Call/Put) options	**629**	**629**	**5,498**	**-**	**5,498**	**-**	**-**	**-**
Total	**856,146**	**742,931**	**69,504,850**	**6,195,574**	**9,963,337**	**10,877,838**	**16,747,950**	**25,720,151**
2018								
Islamic Derivatives held for trading:								
Unilateral promise to buy/sell currencies	73,860	67,990	7,038,180	4,896,909	2,141,271	-	-	-
Islamic profit rate swaps	436,988	379,819	45,851,853	1,365,978	5,000,624	10,531,327	9,448,963	9,504,961
Islamic currency (Call/Put) options	4,654	4,655	557,652	-	557,652	-	-	-
Total	515,502	452,464	53,447,685	6,262,887	7,699,547	10,531,327	9,448,963	9,504,961

Unilateral promise to buy/sell currencies

Unilateral promises to buy/sell currencies are promises to either buy or sell a specified currency at a specific price and date in the future. The actual transactions are executed on the value dates, by exchanging the purchase/sale offers and acceptances between the relevant parties and delivering (exchanging) the relevant currencies on spot basis.

Islamic Swaps

Islamic Swaps are based on a Waa'd (promise) structure between two parties to buy a specified Sharia compliant asset at an agreed price on the relevant date in future. It is a conditional promise to purchase an asset through a unilateral purchase undertaking. Islamic swap structure comprises profit rate swap and currency swap. For Islamic profit rate swaps, counterparties generally exchange fixed and floating rate profit payments by executing the purchase/sale of asset under "Murabaha Sale Agreement" in a single currency. For Islamic currency swaps, fixed or floating profit payments as well as cost of underlying asset are exchanged in different currencies, by executing the purchase/sale of asset under "Murabaha Sale Agreement".

6.2.4 Contingent liabilities and commitments

The table below shows the contractual expiry by maturity of the Bank's contingent liabilities and commitments:

6. Liquidity Risk (continued)

6.2 Funding Approach (continued)

6.2.4 Contingent liabilities and commitments (continued)

	Less than 3 months AED'000	**3 months to 1 year AED'000**	**1 to 5 years AED'000**	**Over 5 years AED'000**	**Total AED'000**
2019					
Contingent liabilities:					
Letters of guarantee	**11,286,923**	**1,228,202**	**371,727**	**50,270**	**12,937,122**
Letters of credit	**1,142,972**	**366,407**	**4,841**	**-**	**1,514,220**
	12,429,895	**1,594,609**	**376,568**	**50,270**	**14,451,342**
Capital expenditure commitments	**9,730**	**-**	**705,463**		**715,193**
Total	**12,439,625**	**1,594,609**	**1,082,031**	**50,270**	**15,166,535**

	Less than 3 months AED'000	3 months to 1 year AED'000	1 to 5 years AED'000	Over 5 years AED'000	Total AED'000
2018					
Contingent liabilities:					
Letters of guarantee	11,434,751	1,484,130	654,260	7,587	13,580,728
Letters of credit	724,993	1,027,808	99,110	-	1,851,911
	12,159,744	2,511,938	753,370	7,587	15,432,639
Capital expenditure commitments	-	-	867,525	-	867,525
Total	12,159,744	2,511,938	1,620,895	7,587	16,300,164

7. Market Risk

7.1 Market Risk

Market risk arises from changes in market rates such as profit rates, foreign exchange rates and equity prices, as well as in their correlation and implied volatilities. Market risk management is designed to limit the amount of potential losses on open positions which may arise due to unforeseen changes in profit rates, foreign exchange rates or equity prices. The Group is exposed to diverse financial instruments including securities, foreign currencies, equities and commodities.

The Group pays considerable attention to market risk. The Group uses appropriate models, as per standard market practice, for the valuation of its positions and receives regular market information in order to regulate market risk.

The trading market risk framework comprises the following elements:

- Limits to ensure that risk-takers do not exceed aggregate risk and concentration parameters set by senior management; and
- Independent mark-to-market valuation, reconciliation of positions and tracking of stop-losses for trading positions on a timely basis.

The policies and procedures and the trading limits are set to ensure the implementation of the market risk policy in day-to-day operations. These are reviewed periodically to ensure they remain in line with the Group's general market risk policy. The Chief Risk Officer of the Bank ensures that the market risk management process is always adequately and appropriately staffed. In addition to its internal procedures and systems, the Bank is required to comply with the guidelines and regulations of the Central Bank of the U.A.E.

7.1.1 Profit margin risk

The Group is not significantly exposed to risk in terms of repricing of its customer deposits since, in accordance with Islamic Sharia'a, the Group does not provide contractual rates of return to its depositors or investment account holders. The return payable to depositors and investment account holders is based on the principle of the Mudaraba by which the depositors and investment account holders agree to share the profit or loss made by the Group's common and wakala asset pool over a given period.

7.1.2 Profit rate risk

Profit rate risk arises from the possibility that changes in profit rates will affect future profitability or the fair values of financial instruments. The Group is exposed to profit rate risk as a result of mismatches or gaps in the amounts of assets and liabilities and off-balance sheet instruments that mature or re-price in a given period. The Group manages this risk through risk management strategies.

The effective profit rate (effective yield) of a monetary financial instrument is the rate that, when used in a present value calculation, results in the carrying amount of the instrument. The rate is a historical rate for a fixed rate instrument carried at amortised cost and a current rate for a floating rate instrument or an instrument carried at fair value.

The following table demonstrates the sensitivity to a reasonable possible change in profit rates, with all other variables held constant, of the Group's consolidated statement of profit or loss.

The sensitivity of the consolidated statement of profit or loss is the effect of the assumed changes in profit rates on the net income for one year, based on the variable profit rate non-trading financial assets and financial liabilities held at 31 December 2019 and 2018.

Currency	**Increase in basis points**	**2019 AED'000**	2018 AED'000
Sensitivity of net profit income	**50**	**76,602**	103,051

7.1.3 Foreign exchange risk

The Group has significant income recorded in its overseas subsidiaries and is therefore exposed to movements in the foreign currency rates used to convert income into the Group presentation currency, the U.A.E. Dirham.

The table below summarises the Bank's exposure to foreign currency exchange rate risk at 31 December 2019 and 2018. Included in the table are the Bank's financial instruments at their carrying amounts, categorised by currency.

7. Market Risk (continued)

7.1 Market Risk (continued)

7.1.3 Foreign exchange risk (continued)

2019	AED AED'000	USD AED'000	Other G.C.C. AED'000	GBP AED'000	Euro AED'000	Other AED'000	Total AED'000
Financial Assets:							
Cash and balances with the central banks	20,171,339	613,433	74	135	260	483,254	21,268,495
Due from banks and financial institutions	1,635,462	3,732,142	474,845	38,301	51,017	316,406	6,248,173
Islamic financing and investing assets, net	108,789,637	36,420,858	1,267,118	-	-	4,435,815	150,913,428
Investment in Islamic Sukuk measured at amortised cost	-	32,101,855	-	-	-	1,142,003	33,243,858
Other investments at fair value	542,996	594,831	109,905	-	-	18,503	1,266,235
Receivables and other assets	5,226,550	2,975,841	80,568	-	32,695	355,365	8,671,019
Total	136,365,984	76,438,960	1,932,510	38,436	83,972	6,751,346	221,611,208
Financial Liabilities:							
Customers' deposits	124,187,496	25,834,875	8,826,331	79,557	248,616	5,241,542	164,418,417
Due to banks and other financial institutions	3,697,530	5,200,135	3	8	27	249,044	9,146,747
Sukuk issued	-	14,675,936	-	-	-	176,009	14,851,945
Payables and other liabilities	6,139,106	1,828,861	189,452	1,614	66,512	280,595	8,506,140
Total	134,024,132	47,539,807	9,015,786	81,179	315,155	5,947,190	196,923,249
Net on balance sheet	2,341,852	28,899,153	(7,083,276)	(42,743)	(231,183)	804,156	24,687,959
Unilateral promise to buy/sell currencies	6,327,692	(9,901,210)	3,399,984	41,856	148,383	(12,666)	4,039
Currency position - long/(short)	8,669,544	18,997,943	(3,683,292)	(887)	(82,800)	791,490	24,691,998

7. Market Risk (continued)

7.1 Market Risk (continued)

7.1.3 Foreign exchange risk (continued)

2018	AED AED'000	USD AED'000	Other G.C.C. AED'000	GBP AED'000	Euro AED'000	Other AED'000	Total AED'000
Financial Assets:							
Cash and balances with the central banks	21,394,566	677,421	-	-	-	473,539	22,545,526
Due from banks and financial institutions	6,646,321	1,230,936	107,023	6,670	45,572	260,510	8,297,032
Islamic financing and investing assets, net	105,553,606	33,875,485	1,190,589	-	-	4,118,905	144,738,585
Investment in Islamic Sukuk measured at amortised cost	-	29,920,263	-	-	-	1,258,262	31,178,525
Other investments at fair value	725,103	816,957	129,257	-	-	16,507	1,687,824
Receivables and other assets	4,280,643	1,218,948	24,294	-	59,170	321,737	5,904,792
Total	138,600,239	67,740,010	1,451,163	6,670	104,742	6,449,460	214,352,284
Financial Liabilities:							
Customers' deposits	119,322,369	24,347,270	5,193,372	1,613,694	200,413	4,980,198	155,657,316
Due to banks and other financial institutions	5,202,653	7,646,502	-	11,706	28	342,339	13,203,228
Sukuk issued	-	12,181,831	-	-	-	189,137	12,370,968
Payables and other liabilities	5,888,914	1,671,641	153,064	39,802	18,055	273,436	8,044,912
Total	130,413,936	45,847,244	5,346,436	1,665,202	218,496	5,785,110	189,276,424
Net on balance sheet	8,186,303	21,892,766	(3,895,273)	(1,658,532)	(113,754)	664,350	25,075,860
Unilateral promise to buy/sell currencies	3,978,294	(6,205,769)	449,841	1,752,604	116,116	(93,867)	(2,781)
Currency position - long/(short)	12,164,597	15,686,997	(3,445,432)	94,072	2,362	570,483	25,073,079

7. Market Risk (continued)

7.1 Market Risk (continued)

7.1.3 Foreign exchange risk (continued)

Sensitivity analysis - impact of fluctuation of various currencies on net income and equity

The tables below indicate the extent to which the Group was exposed to currency risk at 31 December 2019 and 2018 on its non-trading monetary assets and liabilities, and forecast cash flows. The analysis is performed for a reasonable possible movement of the currency rate against the AED with all other variables held constant on the consolidated statement of profit or loss (due to the changes in the fair values of currency sensitive non-trading monetary assets and liabilities) and equity (due to the change in fair value of foreign currency denominated available-for-sale equity instruments). A negative amount in the table reflects a potential net reduction in consolidated statement of profit or loss and equity, while a positive amount reflects a net potential increase. The sensitivity analysis does not take account of actions by the Group that might be taken to mitigate the effect of such changes.

Currency	Increase in currency rate in %	Effect on profit or loss 2019 AED'000	Effect on profit or loss 2018 AED'000
US Dollar	+2	379,959	315,424
GBP	+2	(18)	1,881
EURO	+2	(1,656)	2,099

Currency	Decrease in currency rate in %	Effect on profit or loss 2019 AED'000	Effect on profit or loss 2018 AED '000
US Dollar	-2	(379,959)	(315,424)
GBP	-2	18	(1,881)
EURO	-2	1,656	(2,099)

7.2 Foreign Investment

The Group has income recorded in its overseas subsidiaries and is therefore exposed to movements in the foreign currency rates used to convert income into the Group presentation currency, the U.A.E. Dirham.

The table below indicates the change in profit before tax and equity had the result for the year ended 31 December 2019 and 2018 been translated at exchange rates against the AED adjusted, with all other variables held constant, by the assumed changes below. The sensitivity analyses do not take account of actions by the Group that might be taken to mitigate the effect of such changes.

Currency	Increase in currency rate in %	Effect on profit or loss 2019 AED'000	Effect on equity 2019 AED'000	Effect on profit or loss 2018 AED'000	Effect on equity 2018 AED'000
Pak Rupees	+5	4,303	26,645	4,013	25,113
Egypt Sterling	+5	309	5,502	396	4,588

Currency	Decrease in currency rate in %	Effect on profit or loss 2019 AED'000	Effect on equity 2019 AED'000	Effect on profit or loss 2018 AED'000	Effect on equity 2018 AED'000
Pak Rupees	-5	(3,894)	(23,067)	(3,631)	(21,685)
Egypt Sterling	-5	(280)	(4,978)	(358)	(4,151)

7. Market Risk (continued)

7.3 Equity Price Risk

Equity price risk is the risk that the fair values of equities decrease as the result of changes in the levels of equity indices and the value of individual stocks. The non-trading equity price risk exposure arises from the Bank's investment portfolio.

The effect on equity (as a result of a change in the fair value of equity instruments held as fair value through other comprehensive income (FVTOCI) at 31 December 2019 and 2018) due to a reasonably possible change in equity indices, with all other variables held constant, is as follows:

Market indices	**Change in market Indices**	**Effect on other comprehensive income**	Effect on other comprehensive income
	%	**2019 AED'000**	2018 AED'000
Dubai Financial Market	**± 5%**	**14,943**	8,737
Abu Dhabi Exchange	**± 5%**	**1,210**	509
Bahrain Stock Exchange	**± 5%**	**1,293**	1,212
Other	**± 5%**	**3,816**	3,301

An increase of 5% in fair value of Level 3 financial instruments due to change in unquoted market price / valuation of financial instruments as at the reporting date would have increased the net assets attributable to the Bank by AED 35.6 million (2018: AED 48.5 million).

8. Operational Risk

8.1 Operational Risk

Operational risk is the potential exposure to financial or other damage arising from inadequate or failed internal processes, people or systems.

The Group has developed a detailed operational risk framework. The framework clearly defines roles and responsibilities of individuals/units across different functions of the Group that are involved in performing various operational risk management tasks. Operational Risk Management Framework will ensure that operational risks within the Group are properly identified, monitored, managed and reported. Key elements of the framework include process mapping, setting up loss data base, setting up of KRIs, risk analysis and risk management reporting.

The Group is currently using operational risk tracking system, i.e. ORMS to track operational risk events across the Group. The system houses five years of operational loss data. The subject system is also capable to record KRI, RCSA and scenario based fraud risk self-assessment.

In addition to ORMS, the Bank is also implementing eGRC system (centralized governance framework) for all control activities.

Each new product introduced is subject to a risk review and signoff process where all relevant risks are identified and assessed by departments independent of the risk-taking unit proposing the product. Variations of existing products are also subject to a similar process. Business and support units are responsible for managing operations risk in their respective functional areas. They operate within the Group’s operational risk management framework and ensure that risk is being managed within their respective business units. The day-to-day management of operations risk is through the maintenance of a comprehensive system of internal controls, supported by robust systems and procedure to monitor transaction positions and documentation, as well as maintenance of key backup procedures and business contingency planning.

9. Regulatory Compliance

9.1 Regulatory / Compliance Risk

Regulatory/Compliance risk is the risk of reputational and/or financial losses due to the failure to comply with applicable laws, regulations or sanctions. The Bank has an independent Compliance function, with the necessary mandate and authority to enforce and monitor compliance.

Compliance policies covering key areas such as Sanctions, Anti Money Laundering (AML), Counter Terrorist Financing (CTF), Foreign Account Tax Compliance Act (FATCA) and Common Reporting Standards (CRS) are applicable Group wide and are supplemented where necessary to address any unique local requirements. These policies are supported by automated screening and monitoring systems and associated investigation teams to help comply with the Sanctions, AML, CTF, FATCA and CRS requirements. Independent Compliance Monitoring is undertaken to provide assurance over the effectiveness of controls. Mandatory Compliance Training is provided to all relevant staff both at onboarding and periodically thereafter to help ensure that key requirements are complied with.

9.2 Reputational Risk

Reputational risk is the risk of potential loss of earnings and future revenue, loss in market value or lack of liquidity supply due to deterioration of reputation. It also includes the threat to the brand value of a financial institution.

Reputational risk can arise as a consequence of failures with a strong negative perception amongst clients, shareholders, creditors or the public. The Group has measures to ensure a positive perception of the Group and that overall risk management ensures appropriate management of reputational risk.