**Finance House P.J.S.C.**

**Consolidated financial statements for the year ended 31 December 2018**

## Finance House P.J.S.C.

## Consolidated financial statements for the year ended 31 December 2018


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## Chairman's Report for the year ended 31 December 2018

On behalf of the Board of Directors, I am pleased to present the consolidated financial statements of Finance House P.J.S.C. and its subsidiaries (FH Group) for the financial year ended 31 December 2018.

From a reformist perspective 2018 was a landmark year for the UAE with the Government announcing and/or introducing a series of sweeping changes that are intended to have a positive impact on the country's economy, fiscal policies, visa system and even the gender make-up of the Federal National Council, in the medium to long term. The UAE Government aims to prepare the country for a more prosperous future in a post-oil world, by creating a dynamic economic environment that will stimulate public & private sector investment, create jobs, spur innovation & technological advances across all key economic sectors and improve the overall quality of life of UAE residents at large.

The flipside of "anticipated long term gain" is invariably "agonising short term pain" and this is what most economic sectors in the UAE (including the financial services sector) experienced in 2018. With a business strategy that is almost entirely focused on the UAE, the FH Group is no exception to this rule. For the year ended 31 December 2018, the FH Group posted a Consolidated Net Profit of AED 17.84 million compared to AED 32.61 million in the previous year. Despite a lower bottom-line in comparison to the earlier years, we are still proud to maintain our profitable track record for the fourteenth successive year since inception.

Net Interest Income, Income from Islamic Financing & Investing Assets and Net Income from Perpetual Instruments were marginally lower at AED 194.95 million in 2018 compared to AED 196.64 million in the previous year. This is mainly due to increased cost of funding that was not entirely passed on to our corporate customers. Net Fee and Commission income earned in 2018 was also marginally lower at AED 46.75 million compared to AED 47.48 million in the previous year. Poor trading volumes in domestic equity markets during 2018 translated to significantly lower brokerage fees at our local stock broking subsidiary. Net Insurance Income catapulted to AED 38.77 million in 2018 compared to AED 12.68 million in the previous year, aided by a sustained turnaround in the core operations of our insurance subsidiary. Aggregate investment & other operating income was substantially lower at AED 19.32 million in 2018 compared to AED 42.77 million in the previous year primarily on account of the disappointing performance of domestic equity markets in 2018 and consequential marked to market losses of circa AED 31.50 million from our domestic equities trading portfolio. The anticipated resurgence in domestic equity valuations during 2019 could potentially reverse the negative P&L impact of 2018.

Net Loans & Advances including Islamic Financing & Investing Assets as of 31 December 2018 were also marginally lower at AED 2.44 billion compared to AED 2.51 billion as at the end of the previous year. This is primarily attributable to weak demand for credit from our target customer segments, who in turn were negatively impacted by subdued economic conditions that prevailed throughout 2018. Customers' Deposits & Margin Accounts as of 31 December 2018 stood at AED 2.75 billion translating into a healthy Loans to Deposits ratio of 88.9% as of 31 December 2018.

## Chairman's Report for the year ended 31 December 2018 (continued)

Our loan loss provisioning policy continues to be conservative. With the implementation of the expected credit losses model (ECL) for loan impairment provisioning under IFRS 9 with effect from 1 Jan 2018, net impairment charge to the P&L A/C for the year 2018 has increased to AED 79.50 million compared to AED 55.96 million in the previous year. With gradual improvement in economic conditions anticipated over the coming 12 months, net impairment charge to the P&L A/C is expected to moderate in the near future.

Bearing in mind the subdued macro-economic conditions, we took decisive steps during 2018, to reduce Salaries & employees related expenses. As a result, employee costs for the year ended 31 December 2018 were lower by 9.3% at AED 145 million compared to AED 159.87 million in the previous year. However in 2018, General and administrative expenses increased by AED 6.33 million to AED 57.46 million compared to AED 51.12 million in the previous year. Bulk of this increase ie. AED 5.7 million out of AED 6.33 million is on account of input VAT that is not recoverable from customers pursuant to the Federal VAT Law that came into force with effect from 1 Jan 2018.

FH Group continues to manage its liquidity in a prudent and conservative manner. Since the onset of the financial crisis in October 2008, we have remained net lenders to the UAE inter-bank market and continue to maintain this position until date. Net cash and cash equivalents as at 31 December 2018 stood at AED 509.15 million, representing a healthy 12.43% of Total Assets.

At the consolidated level, Shareholders' equity as at 31 December 2018 stood at AED 768.17 million. This is after distributing a cash dividend of 5% for 2017, amounting to AED 15.14 million and 7.5% coupon on the Tier 1 Sukuk amounting to AED 22.50 million. Capital adequacy ratio at the consolidated level as of 31 December 2018 stood at a robust 20.3%, providing a solid footing for sustained future growth in assets.

Subject to the approval of the Central Bank of the UAE, the Board has recommended a cash dividend payout not exceeding 50% of the Net Profit for the year ended 31 December 2018.

In December 2018, the investment grade Corporate Credit Ratings of Finance House were reaffirmed by Capital Intelligence, at "A3" Short Term and "BBB-" Long Term, both with a stable outlook. The reaffirmation of our investment grade credit ratings is a fitting testament to the soundness of our growth strategies, the resilience of our business model and the robustness of our liquidity management & strategy execution capabilities.

We look forward to 2019 with measured optimism for profitable growth, in line with anticipated improvement in overall market conditions. We continue to recalibrate our strategies and strategy execution capabilities on a regular basis in response to dynamic changes in market conditions. We are convinced that our corporate and business strategies are sound and we have the necessary mechanisms and execution capabilities in place to exploit profitable opportunities, to adapt quickly to changing market conditions, to continue managing risks well and to maximize returns for our shareholders.

On behalf of the Board of Directors,

**Mohammed Abdulla Alqubaisi**
**Chairman**

Abu Dhabi
13 February 2019

# *Independent auditor's report to the shareholders of Finance House P.J.S.C.*

## *Report on the audit of the consolidated financial statements*

### *Our opinion*

In our opinion, the consolidated financial statements present fairly, in all material respects, the consolidated financial position of Finance House P.J.S.C. ("the Company") and its subsidiaries (together, "the Group") as at 31 December 2018, and its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with International Financial Reporting Standards.

**What we have audited**

The Group's consolidated financial statements comprise:

- the consolidated statement of financial position as at 31 December 2018;
- the consolidated income statement for the year then ended;
- the consolidated statement of comprehensive income for the year then ended;
- the consolidated statement of changes in equity for the year then ended;
- the consolidated statement of cash flows for the year then ended; and
- the notes to the consolidated financial statements, which include a summary of significant accounting policies.

### *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 Consolidated Financial Statements* section of our report.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

**Independence**

We are independent of the Group in accordance with the International Ethics Standards Board for Accountants' Code of Ethics for Professional Accountants (IESBA Code) and the ethical requirements that are relevant to our audit of the consolidated financial statements in the United Arab Emirates. We have fulfilled our other ethical responsibilities in accordance with those requirements and the IESBA Code.

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Douglas O'Mahony, Rami Sarhan, Jacques Fakhoury and Mohamed ElBorno are registered as practising auditors with the UAE Ministry of Economy

# Independent auditor's report to the shareholders of Finance House P.J.S.C. (continued)

## Our audit approach

### Overview

| Key audit matter | • Measurement of Expected Credit Losses ("ECL") and related disclosures |
|---|---|

As part of designing our audit, we determined materiality and assessed the risks of material misstatement in the consolidated financial statements. In particular, we considered where the directors made subjective judgments; for example, in respect of significant accounting estimates that involved making assumptions and considering future events that are inherently uncertain. As in all of our audits, we also addressed the risk of management override of internal controls, including among other matters, consideration of whether there was evidence of bias that represented a risk of material misstatement due to fraud.

We tailored the scope of our audit in order to perform sufficient work to enable us to provide an opinion on the consolidated financial statements as a whole, taking into account the structure of the Group, the accounting processes and controls, and the industry in which the Group operates.

## Key audit matters

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

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## *Independent auditor's report to the shareholders of Finance House P.J.S.C.* (continued)

### *Key audit matters (continued)*

| Key audit matter | How our audit addressed the Key audit matter |
|---|---|
| ***Measurement of Expected Credit Losses and related disclosures***<br><br>IFRS 9 'Financial instruments' became effective from 1 January 2018 and replaced most of the guidance in IAS 39 – 'Financial instruments'. In particular, the incurred loss impairment model under IAS 39 has been replaced with the Expected Credit Losses model ("ECL"). The Group has in previous years adopted the first phase of the IFRS 9 with regards to classification and measurement of financial instruments. The Group adopted the final phase of IFRS 9 with respect to impairment of financial assets with effect from 1 January 2018. The adoption of the ECL model under IFRS 9 has resulted in an increase in the impairment provision of AED 66.3 million which, has been recognised as an adjustment to retained earnings at 1 January 2018. The impairment charge for the year was AED 79.5 million.<br><br>The Group applies ECL on all the financial instruments measured at amortised cost, and debt instruments measured at fair value through other comprehensive income, and financial guarantee contracts including financing commitments.<br><br>The Group exercises significant judgements and makes a number of assumptions in developing its ECL models, which includes probability of default computation separately for retail and corporate portfolios, determining Loss Given Default ("LGD") and Exposure at Default ("EAD") for both funded and unfunded exposures, forward looking adjustments and staging criteria. | We performed the following audit procedures on the computation of the ECL included in the Group's consolidated financial statements for the year ended 31 December 2018:<br><br>➢ We involved our internal impairment modelling specialists to assess and review the following areas:<br>• Conceptual framework used for developing the Group's impairment policy in the context of it's consistency with the requirements of IFRS 9.<br>• ECL modelling methodology and calculations used to compute the Probability of Default ("PD"), Loss Given Default ("LGD"), and Exposure at Default ("EAD") for the Group's classes of financial instruments.<br>• Reasonableness of the assumptions made in developing the modelling framework including assumptions used for estimating forward looking scenarios and significant increase in credit risk.<br>• For a sample of exposures, we checked the appropriateness of determining EAD, including the consideration of repayments and the resultant arithmetical calculations.<br><br>➢ We tested the completeness and accuracy of the data used in calculation of ECL.<br><br>➢ For a sample of exposures, we checked the appropriateness of the Group's staging of financial instruments. |

## *Key audit matters (continued)*

| Key audit matter | How our audit addressed the key audit matter |
|---|---|
| ***Measurement of Expected Credit Losses and related disclosures*** (continued)<br><br>Measurement of ECL is considered as a key audit matter as the Group applies significant judgments and makes a number of assumptions in the staging criteria applied to the financial instruments as well as in developing ECL models for calculating its impairment provisions and judgments are involved in determining the disclosures under IFRS 7 and IFRS 9.<br><br>The Group's impairment policy as per IFRS 9 is presented in *Note 2.4 (f)* to the consolidated financial statements. | ➢ In addition, for the Stage 3 corporate portfolio, the appropriateness of provisioning assumptions were independently assessed for a sample of exposures selected on the basis of risk and the significance of individual exposures. An independent view was formed on the levels of provisions recognised, based on the detailed loan and counterparty information available in the credit file. For the Stage 3 retail portfolio, assumptions were independently assessed for each product category and an independent view was formed on the levels of provisions recognised at each category level.<br><br>➢ We assessed the consolidated financial statement disclosures to ensure compliance with IFRS 7 and IFRS 9. |

# *Independent auditor's report to the shareholders of Finance House P.J.S.C.* (continued)

## *Other information*

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

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

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

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

When we read the Group's Annual Report, if we conclude that there is a material misstatement therein, we are required to communicate the matter to those charged with governance.

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

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

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

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

## *Auditor's responsibilities for the audit of the consolidated financial statements*

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an 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 consolidated financial statements.

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

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

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

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

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

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

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

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

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

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

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

# *Independent auditor's report to the shareholders of Finance House P.J.S.C.* (continued)

## *Report on other legal and regulatory requirements*

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

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

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

(iii) the Group has maintained proper books of account;

(iv) the financial information included in the report of the Chairman is consistent with the books of account of the Group;

(v) as disclosed in note 5 to the consolidated financial statements the Group has purchased shares during the year ended 31 December 2018;

(vi) note 27 to the consolidated financial statements discloses material related party transactions, and the terms under which they were conducted;

(vii) based on the information that has been made available to us, nothing has come to our attention which causes us to believe that the Group has contravened during the year ended 31 December 2018 any of the applicable provisions of the UAE Federal Law No. (2) of 2015 or in respect of the Company, its Articles of Association which would materially affect its activities or its financial position as at 31 December 2018; and

(viii) as disclosed in note 1 to the consolidated financial statements, the Group did not make any social contributions during the year ended 31 December 2018.

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

Jacques E. Fakhoury
Registered Auditor Number 379
Abu Dhabi, United Arab Emirates

13 February 2019

**Finance House P.J.S.C.**

## Consolidated statement of financial position

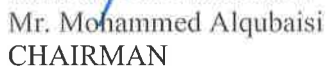
| | Note | As at 31 December 2018 AED'000 | 2017 AED'000 |
|---|---|---|---|
| **ASSETS** | | | |
| Cash balances | 4 | 17,599 | 17,437 |
| Due from banks | 4 | 512,563 | 701,032 |
| Investments carried at fair value through other comprehensive income | 5 | 560,578 | 716,341 |
| Investments carried at fair value through profit or loss | 5 | 161,384 | 176,358 |
| Investments carried at amortised cost | 5 | 1,837 | 81,654 |
| Loans and advances | 6 | 2,300,504 | 2,335,801 |
| Islamic financing and investing assets | 7 | 142,614 | 173,370 |
| Investment in an associate | 8 | 50,485 | 51,720 |
| Interest receivable and other assets | 12 | 236,489 | 208,200 |
| Property, fixtures and equipment | 10 | 24,532 | 13,890 |
| Intangibles | 11 | 6,705 | 6,966 |
| Investment properties | 28 | 79,478 | 82,070 |
| **Total assets** | | **4,094,768** | **4,564,839** |
| **EQUITY AND LIABILITIES** | | | |
| **EQUITY** | | | |
| Share capital | 16 | 310,050 | 310,050 |
| Treasury shares | 20 | (21,402) | (21,402) |
| Employees' share-based payment scheme | 17 | (1,750) | (1,750) |
| Statutory reserve | 18 | 147,367 | 146,185 |
| Cumulative changes in fair value of investments carried at fair value through other comprehensive income | | (44,690) | (6,305) |
| Retained earnings | | 20,146 | 117,349 |
| Tier 1 Sukuk | 9 | 281,500 | 283,550 |
| Proposed directors' remuneration | | 1,064 | 3,090 |
| | | 692,285 | 830,767 |
| Non-controlling interests | 3 | 75,888 | 72,432 |
| **Net equity** | | **768,173** | **903,199** |

The notes on pages 17 to 95 form an integral part of these consolidated financial statements. 

## Consolidated statement of financial position (continued)

| | Note | As at 31 December 2018 AED'000 | 2017 AED'000 |
|---|---|---|---|
| **LIABILITIES** | | | |
| Customers' deposits and margin accounts | 13 | 2,747,275 | 2,950,544 |
| Due to banks and other financial institutions | 4 | 15,014 | 23,831 |
| Short term borrowings | 14 | 27,600 | 266,410 |
| Medium term loans | 14 | 183,335 | 120,834 |
| Interest payable and other liabilities | 15 | 339,291 | 286,397 |
| Provision for employees' end of service benefits | | 14,080 | 13,624 |
| **Total liabilities** | | **3,326,595** | **3,661,640** |
| **Total equity and liabilities** | | **4,094,768** | **4,564,839** |
| **Commitments and contingent liabilities** | 21 | **1,544,002** | **1,950,461** |

These consolidated financial statements were approved and authorised for issue by the Board of Directors on 13 February 2019 and were signed on its behalf by:



Mr. Mohammed Alqubaisi
CHAIRMAN

Mr. Hamid Taylor
GENERAL MANAGER

**Finance House P.J.S.C.**

## Consolidated income statement

| | Note | Year ended 31 December 2018 AED'000 | 2017 AED'000 |
|---|---|---|---|
| Interest income and income from Islamic financing and investing assets | 22 | 261,543 | 244,899 |
| Interest expense and profit distributable to depositors | 22 | (85,608) | (74,034) |
| **Net interest income and income from Islamic financing and investing assets** | 22 | **175,935** | **170,865** |
| Income from Tier 1 Capital Instruments | 5 | 19,017 | 25,773 |
| Net fee and commission income | 23 | 46,748 | 47,480 |
| Net insurance income | 24 | 38,773 | 12,681 |
| Net loss from investments | 25 | (407) | (1,159) |
| Gain on disposal of a subsidiary | | - | 15,001 |
| Share of (loss)/profit of associate | 8 | (1,235) | 1,243 |
| Other operating income | 34 | 20,962 | 27,683 |
| Salaries and employees related expenses | 29 | (145,001) | (159,870) |
| Net impairment charges on loans and advances and Islamic financing and investing assets | 6, 7 | (79,496) | (55,959) |
| General and administrative expenses | 35 | (57,456) | (51,124) |
| **Profit for the year** | | **17,840** | **32,614** |
| **Attributable to:** | | | |
| Equity holders of the parent | | 11,825 | 34,330 |
| Non-controlling interests | 3 | 6,015 | (1,716) |
| | | **17,840** | **32,614** |
| **Basic and diluted earnings per share attributable to ordinary shares (AED)** | 26 | **(0.04)** | **0.03** |

The notes on pages 17 to 95 form an integral part of these consolidated financial statements.

**Finance House P.J.S.C.**

## Consolidated statement of comprehensive income

| | Note | Year ended 31 December 2018 AED'000 | 2017 AED'000 |
|---|---|---|---|
| Profit for the year | | 17,840 | 32,614 |
| **Other comprehensive income** | | | |
| ***Items that will not be reclassified to consolidated income statement:*** | | | |
| Change in fair value of investments carried at fair value through other comprehensive income | | (42,336) | (26,556) |
| Directors' remuneration paid | | (3,090) | (1,976) |
| **Other comprehensive loss for the year** | | **(45,426)** | **(28,532)** |
| **Total comprehensive (loss)/income for the year** | | (27,586) | 4,082 |
| **Attributable to:** | | | |
| Equity holders of the parent | | (32,430) | 5,441 |
| Non-controlling interests | | 4,844 | (1,359) |
| | | **(27,586)** | **4,082** |

## Consolidated statement of changes in equity

| | Note | Share capital AED'000 | Treasury shares AED'000 | Employees' share-based payment scheme AED'000 | Statutory reserve AED'000 | Cumulative changes in fair value AED'000 | Retained earnings AED'000 | Proposed directors' remuneration AED'000 | Tier 1 Sukuk AED'000 | Attributable to shareholders of the parent company AED'000 | Non controlling interests AED'000 | Total AED'000 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| **2018** | | | | | | | | | | | | |
| **Balance at 1 January 2018** | | 310,050 | (21,402) | (1,750) | 146,185 | (6,305) | 117,349 | 3,090 | 283,550 | 830,767 | 72,432 | **903,199** |
| Change on Initial application of IFRS9 *(Note 2.3)* | | - | - | - | - | - | (66,361) | - | - | (66,361) | - | **(66,361)** |
| Restated balance at 1st January 2018 | | 310,050 | (21,402) | (1,750) | 146,185 | (6,305) | 50,988 | 3,090 | 283,550 | 764,406 | 72,432 | 836,838 |
| Profit for the year | | - | - | - | - | - | 11,825 | - | - | 11,825 | 6,015 | **17,840** |
| Change in fair value of investments carried at fair value through other comprehensive income | | - | - | - | - | (41,165) | - | - | - | (41,165) | (1,264) | **(42,429)** |
| Loss on disposal of investments carried at fair value through other comprehensive income | | - | - | - | - | 2,780 | (2,780) | - | - | - | 93 | **93** |
| Directors' remuneration paid | | - | - | - | - | - | - | (3,090) | - | (3,090) | - | **(3,090)** |
| Proposed directors' remuneration | | - | - | - | - | - | (1,064) | 1,064 | - | - | - | - |
| Cash dividends paid | 19 | - | - | - | - | - | (15,141) | - | - | (15,141) | - | **(15,141)** |
| Transfer to statutory reserve | | - | - | - | 1,182 | - | (1,182) | - | - | - | - | - |
| Purchase of treasury shares | 20 | - | - | - | - | - | - | - | - | - | - | - |
| Elimination of Tier I Sukuk held by subsidiaries | 9 | - | - | - | - | - | - | - | (2,050) | (2,050) | - | **(2,050)** |
| Increase (decrease) in non- Treasury shares | | - | - | - | - | - | - | - | - | - | (1,388) | **(1,388)** |
| Tier I Sukuk coupon paid | | - | - | - | - | - | (22,500) | - | - | (22,500) | - | **(22,500)** |
| **Balance at 31 December 2018** | | **310,050** | **(21,402)** | **(1,750)** | **147,367** | **(44,690)** | **20,146** | **1,064** | **281,500** | **692,285** | **75,888** | **768,173** |

The notes on pages 17 to 95 form an integral part of these consolidated financial statements.

## Consolidated statement of changes in equity (continued)

| | Note | Share capital AED'000 | Treasury shares AED'000 | Employees' share-based payment scheme AED'000 | Statutory reserve AED'000 | Cumulative changes in fair value AED'000 | Retained earnings AED'000 | Proposed directors' remuneration AED'000 | Tier 1 Sukuk AED'000 | Attributable to shareholders of the parent company AED'000 | Non controlling interests AED'000 | Total AED'000 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| **2017** | | | | | | | | | | | | |
| **Balance at 1 January 2017** | | 310,050 | (12,587) | (1,750) | 142,752 | 17,493 | 133,327 | 1,976 | 288,700 | 879,961 | 73,791 | **953,752** |
| Profit for the year | | - | - | - | - | - | 34,330 | - | - | 34,330 | (1,716) | **32,614** |
| Change in fair value of investments carried at fair value through other comprehensive income | | - | - | - | - | (26,913) | - | - | - | (26,913) | (334) | **(27,247)** |
| Loss on disposal of investments carried at fair value through other comprehensive income | | - | - | - | - | 3,115 | (3,115) | - | - | - | 691 | **691** |
| Directors' remuneration paid | | - | - | - | - | - | - | (1,976) | - | (1,976) | - | **(1,976)** |
| Proposed directors' remuneration | | - | - | - | - | - | (3,090) | 3,090 | - | - | - | **-** |
| Cash dividends paid | 19 | - | - | - | - | - | (18,170) | - | - | (18,170) | - | **(18,170)** |
| Transfer to statutory reserve | | - | - | - | 3,433 | - | (3,433) | - | - | - | - | **-** |
| Purchase of treasury shares | 20 | - | (8,815) | - | - | - | - | - | - | (8,815) | - | **(8,815)** |
| Elimination of Tier I Sukuk held by subsidiaries | 9 | - | - | - | - | - | - | - | (5,150) | (5,150) | - | **(5,150)** |
| Tier I Sukuk coupon paid | | - | - | - | - | - | (22,500) | - | - | (22,500) | - | **(22,500)** |
| **Balance at 31 December 2017** | | **310,050** | **(21,402)** | **(1,750)** | **146,185** | **(6,305)** | **117,349** | **3,090** | **283,550** | **830,767** | **72,432** | **903,199** |

The notes on pages 17 to 95 form an integral part of these consolidated financial statements.

## Finance House P.J.S.C.

## Consolidated statement of cash flows

| | Note | Year ended 31 December 2018 AED'000 | 2017 AED'000 |
|---|---|---|---|
| **Cash flows from operating activities** | | | |
| Profit for the year | | 17,840 | 32,614 |
| **Adjustments for:** | | | |
| Depreciation of property, fixtures and equipment | 10 | 8,701 | 7,170 |
| Amortisation of intangibles | 11 | 261 | 784 |
| Change in fair valuation of investment properties | | 2,592 | 6,000 |
| Share of results of an associate | | 1,235 | (1,243) |
| Dividend income from investments | 25 | (27,560) | (27,501) |
| (Gain)loss on disposal of investments carried at fair value through profit or loss | 25 | (3,531) | 5,925 |
| Change in fair value of investments carried at fair value through profit or loss | 25 | 31,498 | 22,735 |
| Net impairment charges on loans and advances and Islamic financing and investing assets | 6,7 | 79,496 | 55,959 |
| Net movement in provision for employees' end of service benefits | | 456 | 1,568 |
| **Operating cash flows before changes in working capital** | | **110,988** | **104,011** |
| **Changes in working capital** | | | |
| Loans and advances | | (101,764) | (325,708) |
| Islamic financing and investing assets | | 21,959 | (5,877) |
| Interest receivable and other assets | | (28,289) | (64,063) |
| Assets held for sale | | - | 12,313 |
| Customers' deposits and margin accounts | | (203,269) | 108,562 |
| Interest payable and other liabilities | | 52,894 | 38,921 |
| **Net cash outflow from operating activities** | | **(147,481)** | **(131,841)** |
| **Cash flow from investing activities** | | | |
| Purchase of investments carried at fair value through other comprehensive income | | (78,603) | (69,367) |
| Proceeds from sale of investments carried at fair value through other comprehensive income | | 192,031 | 38,895 |
| Purchase of investments carried at fair value through profit or loss | | (123,303) | (226,471) |
| Proceeds from sale of investments carried at fair value through profit or loss | | 110,310 | 226,219 |
| Purchase of investments carried at amortised cost | | (1,837) | (41,334) |
| Proceeds from sale of investments carried at amortised cost | | 81,654 | 88,249 |
| Addition to property, fixtures and equipment | | (19,343) | (6,591) |
| Proceeds from disposal of property, fixtures and equipment | | - | 207 |
| Acquisition of investment properties in respect of settlement of a loan | 28 | - | (5,070) |
| Dividend income received | | 27,560 | 27,501 |
| **Net cash inflow from investing activities** | | **188,469** | **32,238** |
| **Cash flow from financing activities** | | | |
| Proceeds from short term borrowings and medium term loans | 14 | 150,000 | 223,910 |
| Repayment of short term borrowings and medium term loans | 14 | (326,309) | (116,666) |
| Directors' remuneration paid | | (3,090) | (1,976) |
| Movement inTier I Sukuk | | (2,050) | (5,150) |
| Tier 1 Sukuk coupon paid | | (22,500) | (22,500) |
| Purchase of treasury shares | | - | (8,815) |
| Change in non-controlling interest | | (1,388) | - |
| Cash dividend paid | | (15,141) | (18,170) |
| **Net cash (outflow) inflow from financing activities** | | **(220,478)** | **50,633** |
| **Net decrease in cash and cash equivalents** | | **(179,490)** | **(48,970)** |
| Cash and cash equivalents, beginning of the year | | 688,638 | 737,608 |
| Cash and cash equivalents, end of the year | 4 | **509,148** | **688,638** |

The notes on pages 17 to 95 form an integral part of these consolidated financial statements. 

## 1 Activities

Finance House P.J.S.C. (the "Company") is a Public Joint Stock Company incorporated in Abu Dhabi, United Arab Emirates (U.A.E.) in accordance with the provisions of the U.A.E. Federal Commercial Companies Law No. (2) of 2015 and decretal Federal law No 14 of 2018 regarding the Central Bank & organisation of federal institution and activities.

The Company was established on 13 March 2004 and commenced its operations on 18 July 2004. The Company performs its activities through its head office in Abu Dhabi and its Abu Dhabi, Dubai, Sharjah and Musaffah branches. The principal activities of the Company consist of investments, consumer and commercial financing and other related services.

The registered head office of the Company is at P.O. Box 7878, Abu Dhabi, U.A.E.

The consolidated financial statements of the Group were authorised for issue by the Board of Directors on 13 February 2019.

The Group has not made any social contributions during the financial year ended 31 December 2018.

## 2.1 Basis of preparation

The consolidated financial statements of the Group have been prepared in accordance with International Financial Reporting Standards, and interpretations issued by the IFRS Interpretations Committee (IFRIC) applicable to companies reporting under IFRS and the applicable requirements of the laws in the U.A.E. The consolidated financial statements comply with IFRS as issued by the International Accounting Standards Board (IASB).

The consolidated financial statements of the Group are prepared in U.A.E. Dirham (AED) which is the functional currency of the Group. All values are rounded to the nearest thousand (AED '000), except otherwise indicated.

The consolidated financial statements of the Group have been prepared on the historical cost basis except for debt securities, equity shares that are classified as either fair value through profit and loss (FVTPL) or fair value through other comprehensive income (FVTOCI) and investment properties that are measured at their fair values at the end of each reporting period.

## 2.2 Application of new and revised International Financial Reporting Standards (IFRSs)

### 2.2.1 New standards and amendments – applicable 1 January 2018

The following new and revised IFRSs, which became effective for annual periods beginning on or after 1 January 2018, have been adopted in these consolidated financial statements. The application of these revised IFRSs, except where stated, have not had any material impact on the amounts reported for the current and prior years.

- IFRS 9, 'Financial instruments' - The complete version of IFRS 9 replaces most of the guidance in IAS 39. IFRS 9 retains but simplifies the mixed measurement model and establishes three primary measurement categories for financial assets: amortised cost, fair value through other comprehensive income (FVTOCI) and fair value through profit and loss (FVTPL). The basis of classification depends on the entity's business model and the contractual cash flow characteristics of the financial asset. Investments in equity instruments are required to be measured at fair value through profit or loss with the irrevocable option at inception to present changes in fair value in OCI. There is now a new expected credit losses model that replaces the incurred loss impairment model used in IAS 39. For financial liabilities, there were no changes to classification and measurement except for the recognition of changes in own credit risk in other comprehensive income, for liabilities designated at fair value, through profit or loss. IFRS 9 relaxes the requirements for hedge effectiveness by replacing the bright line hedge effectiveness tests. It requires an economic relationship between the hedged item and hedging instrument and for the 'hedged ratio' to be the same as the one management actually uses for risk management purposes. Contemporaneous documentation is still required but is different to that currently prepared under IAS 39. The Company has in previous years adopted the first phase of the IFRS 9 with regards to classification and measurement of financial instruments. The Group adopted the final phase of IFRS 9 with respect to impairment of financial assets with effect from 1 January 2018. The impact of IFRS 9 on the consolidated financial statements of the Group has been disclosed in Note 2.3.

- IFRS 15, 'Revenue from contracts with customers' - The standard replaces IAS 11, 'Construction contracts', IAS 18, 'Revenue' and related interpretations. Revenue is recognised when a customer obtains control of a good or service and thus has the ability to direct the use of and obtain the benefits from the good or service. The core principle of IFRS 15 is that an entity recognises revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. IFRS 15 also includes a cohesive set of disclosure requirements that will result in an entity providing users of consolidated financial statements with comprehensive information about the nature, amount, timing and uncertainty of revenue and cash flows arising from the entity's contracts with customers.

## 2.2 Application of new and revised International Financial Reporting Standards (IFRSs) (continued)

### 2.2.1 New standards and amendments – applicable 1 January 2018 (continued)

- **Amendment to IFRS 15, 'Revenue from contracts with customers'** - The amendments comprise clarifications on identifying performance obligations, accounting for licenses of intellectual property and the principal versus agent assessment (gross versus net revenue presentation). The IASB has also included additional practical expedients related to transition to the new revenue standard.

- **Amendment to IAS 40, 'Investment Property'** - The amendment clarified that to transfer to, or from, investment properties there must be a change in use. To conclude if a property has changed use there should be an assessment of whether the property meets the definition of an investment property. The change must be supported by evidence. It was confirmed that a change in intention, in isolation, is not enough to support a transfer to or from the investment property.

- **Amendment to IFRS 2, 'Share-Based Payment'** - The amendment clarifies the measurement basis for cash-settled, share-based payments and the accounting for modifications that change an award from cash – settled to equity settled. It also introduces an exception to the principles in IFRS 2 that will require an award to be treated if it was wholly owned equity – settled, where an employer is obliged to withhold an amount for the employee's tax obligation associated with a share based payment and pay that amount to the tax authority.

- **Amendments to IFRS 4, 'Insurance contracts'** - The amendment address the concerns about the effective dates of IFRS 9, 'Financial Instruments' and the forth-coming new insurance contracts standard. The amendment introduces two approaches for insurance companies: a temporary exemption from IFRS 9 for entities that meet specific requirement, and the 'overlay approach'. Under overlay approach, an insurer is permitted to reclassify in respect of certain financial assets – from profit or loss to other comprehensive the difference between the amount that is reported in profit or loss account under IFRS 9 and the amount that would have been reported in profit or loss under IAS 39. The Group has elected to apply neither temporary exemption nor the overlay approach.

- **IFRIC 22, 'Foreign currency transactions and advance consideration'** - The interpretation considers how to determine the date of transaction when applying the standard on applying the date of transactions, IAS 21. The date of transaction determines the exchange rate to be used on initial recognition to be used on an initial recognition of a related asset, expense or income. The interpretation provides guidance for when a single payment / receipt is made, as well as for situations where multiple payments / receipts are made.

## 2.2 Application of new and revised International Financial Reporting Standards (IFRSs) (continued)

### 2.2.2 New standards and amendments – applicable 1 January 2019

| New standards, amendments and interpretations | Effective for annual periods beginning on or after |
|---|---|
| **Amendment to IFRS 9, 'Financial instrument'** - The amendment permits more assets to be measured at amortised cost than under the previous version of IFRS 9, in particular some prepayable financial assets. The amendment also confirms that modifications in financial liabilities will result in the immediate recognition of a gain or loss.<br><br>It is unlikely that there will be any material impact on the consolidated financial statements of the Group from the adoption of above amendment on 1 January 2019. | 1 January 2019 |
| **IFRS 16, 'Leases'** - This standard replaces the current guidance in IAS 17 and is a far reaching change in accounting by lessees in particular. Under IAS 17, lessees were required to make a distinction between a finance lease (on balance sheet) and an operating lease (off balance sheet). IFRS 16 now requires lessees to recognise a lease liability reflecting future lease payments and a 'right-of-use asset' for virtually all lease contracts. The IASB has included an optional exemption for certain short-term leases and leases of low-value assets; however, this exemption can only be applied by lessees.<br><br>For lessors, the accounting stays remains mainly unchanged. However, as the IASB has updated the guidance on the definition of a lease (as well as the guidance on the combination and separation of contracts), lessors will also be affected by the new standard. At the very least, the new accounting model for lessees is expected to impact negotiations between lessors and lessees. Under IFRS 16, a contract is, or contains, a lease if the contract conveys the right to control the use of an identified asset for a period of time in exchange for consideration.<br><br>It is unlikely that there will be any material impact on the consolidated financial statements of the Group from the adoption of above new standards on 1 January 2019. | 1 January 2019 |

## 2.2 Application of new and revised International Financial Reporting Standards (IFRSs) (continued)

### 2.2.2 New standards and amendments –applicable 1 January 2019 (continued)

| **New standards, amendments and interpretations** (continued) | **Effective for annual periods beginning on or after** |
|---|---|
| **IFRS 17, 'Insurance contracts'** - On 18 May 2017, the IASB finished its long-standing project to develop an accounting standard on insurance contracts and published IFRS 17, 'Insurance Contracts'. IFRS 17 replaces IFRS 4, which currently permits a wide variety of practices. IFRS 17 will fundamentally change the accounting by all entities that issue insurance contracts and investment contracts with discretionary participation features. | 1 January 2022 |
| The standard applies to annual periods beginning on or after 1 January 2022, with earlier application permitted if IFRS 15, 'Revenue from contracts with customers' and IFRS 9, 'Financial instruments' are also applied. | |
| IFRS 17 requires a current measurement model, where estimates are remeasured in each reporting period. The measurement is based on the building blocks of discounted, probability-weighted cash flows, a risk adjustment and a contractual service margin ("CSM") representing the unearned profit of the contract. A simplified premium allocation approach is permitted for the liability for the remaining coverage if it provides a measurement that is not materially different from the general model or if the coverage period is one year or less. However, claims incurred will need to be measured based on the building blocks of discounted, risk-adjusted, probability weighted cash flows. | |
| The Group is currently assessing the impact of the above new standard on the consolidated financial statements. | |

There are no other relevant applicable new standards and amendments to published standards or IFRIC interpretations that have been issued but are not effective for the first time for the Group's financial year beginning on 1 January 2019 that would be expected to have a material impact on the consolidated financial statements of the Group.

## 2.3 Changes in accounting policies

The Group has adopted the impairment requirements of IFRS 9 as issued by the IASB in July 2014 with a date of transition of 1 January 2018, which resulted in changes in accounting policies and adjustments to the amounts previously recognised in the consolidated financial statements.

As permitted by the transitional provisions of IFRS 9, the Group elected not to restate comparative figures. Any adjustments to the carrying amounts of financial assets and financial liabilities at the date of transition have been recognised in the opening retained earnings and other reserves of the current period. Consequently, for note disclosures, the consequential amendments to IFRS 7 disclosures have also only been applied to the current period. The comparative period notes disclosures reflect those disclosures made in the prior period.

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

Reconciliation of impairment allowance balance from IAS 39 / IAS 37 to IFRS 9

The following table reconciles the prior period's closing impairment allowance measured in accordance with the IAS 39 incurred loss model and IAS 37 provision to the new impairment allowance measured in accordance with the IFRS 9 expected credit loss model at 1 January 2018:

| | **Loan loss allowance under IAS 39** | **Re-measurements** | **Loan loss allowance under IFRS 9** |
|---|---|---|---|
| | AED'000 | AED'000 | AED'000 |
| **Financial assets** | | | |
| Loans and advances | 214,584 | 47,553 | 262,137 |
| Letters of credit and letters of guarantee | - | 14,324 | 14,324 |
| | **214,584** | **61,877** | **276,461** |
| Islamic Financing and Investing assets | 50,944 | 4,484 | 55,428 |
| Total | **265,528** | **66,361** | **331,889** |

The net effect of ECL measured under IFRS 9 for the other financial assets are insignificant to the consolidated financial statements as all of such financial assets are classified as stage 1 exposures.

## 2.4 Significant accounting policies

### (a) Subsidiaries

Control is achieved when the Group:

- has power over an investee,
- is exposed, or has rights, to variable returns from its involvement with the investee, and
- has the ability to use its power over the investee to affect the amount of the investor's returns.

The Group reassesses whether or not it controls an investee if facts and circumstances indicate that there are changes to one or more of the three elements of control listed above.

When the Group has less than a majority of the voting rights of an investee, it has power over the investee when the voting rights are sufficient to give it the practical ability to direct the relevant activities of the investee unilaterally. The Group considers all relevant facts and circumstances in assessing whether or not the Group's voting rights in an investee are sufficient to give it power, including:

- the size of the Group's holding of voting rights relative to the size and dispersion of holdings of the other vote holders;
- potential voting rights held by the Group, other vote holders and other parties;
- rights raising from other contractual arrangements; and
- any additional facts and circumstances that indicate that the Group has, or does not have, the current ability to direct the relevant activities at the time that decisions need to be made, including voting patterns and previous shareholders' meetings.

Consolidation of a subsidiary begins when the Company obtains control over the subsidiary and/or ceases when the Company loses control over the subsidiary. Specifically, income and expenses of a subsidiary acquired or disposed of during the year are included in the consolidated statement of profit or loss from the date the Company gains control until the date when the Company ceases to control the subsidiary.

Profit or loss of each component of other comprehensive income is attributable to the owners of the Group and to the non-controlling interests. Total comprehensive income of subsidiaries is attributable to the owners of the Company and to the non-controlling interest even if this results in the non-controlling interests having a deficit balance.

When necessary, adjustments are made to the financial statements of subsidiaries to bring their accounting policies into line with the Group's accounting policies. All intragroup assets, liabilities, equity, income, expenses and cash flows relating to transactions between members of the Group are eliminated in full on consolidation.

*Changes in the Group's ownership interest in existing subsidiaries*

Changes in the Group's ownership interests in subsidiaries that do not result in the Group losing control over the subsidiaries are accounted for as equity transactions. The carrying amounts of the Group's interests and the non-controlling interests are adjusted to reflect the changes in their relative interests in the subsidiaries. Any difference between the amount by which the non-controlling interests are adjusted and the fair value of the consideration paid or received is recognised directly in equity and attributed to shareholders of the Parent.

## 2.4 Significant accounting policies (continued)

### (a) Subsidiaries (continued)

When a change in the Group's ownership interest in a subsidiary results in a loss of control over the subsidiary, the assets and liabilities of the subsidiary including any goodwill are derecognised. Amounts previously recognised in other comprehensive income in respect of that entity are also reclassified to the consolidated income statement or transferred directly to retained earnings.

Any retained equity interest in the entity is remeasured at fair value. The difference between the carrying amount of the retained interest at the date when control is lost and its fair value is recognised in the consolidated income statement.

The fair value of any investment retained in the former subsidiary at the date when control is lost is regarded as the fair value on initial recognition for subsequent accounting under IFRS 9 'Financial Instruments' or, when applicable, the cost on initial recognition of an investment in an associate or a joint venture.

### (b) Associates

Associates are all entities over which the Group has significant influence but not control or joint control. This is generally the case where the Group holds between 20% and 50% of the voting rights. Investments in associates are accounted for using the equity method of accounting, after initially being recognised at cost.

### (c) Equity method

Under the equity method of accounting, the investments are initially recognised at cost and adjusted thereafter to recognise the Group's share of the post-acquisition profits or losses of the investee in profit or loss, and the Group's share of movements in other comprehensive income of the investee in other comprehensive income. Dividends received or receivable from associates are recognised as a reduction in the carrying amount of the investment. When the Group's share of losses in an equity-accounted investment equals or exceeds its interest in the entity, including any other unsecured long-term receivables, the Group does not recognise further losses, unless it has incurred obligations or made payments on behalf of the other entity. Unrealised gains on transactions between the group and its associates are eliminated to the extent of the group's interest in these entities. Unrealised losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred. Accounting policies of equity accounted investees have been changed where necessary to ensure consistency with the policies adopted by the Group.

The carrying amount of equity-accounted investments is tested for impairment in accordance with the policy described in *Note 2.4(m)*.

If the ownership interest in an associate is reduced but significant influence is retained, only a proportionate share of the amounts previously recognised in other comprehensive income are reclassified to profit or loss where appropriate.

## 2.4 Significant accounting policies (continued)

### (d) Business combinations

Acquisitions of businesses are accounted for using the acquisition method. The consideration transferred in a business combination is measured at fair value, which is calculated as the sum of the acquisition-date fair values of the assets transferred by the Group, liabilities incurred by the Group to the former owners of the acquiree and the equity interests issued by the Group in exchange for control of the acquiree. Acquisition-related costs are generally recognised in profit or loss as incurred.

Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are, with limited exceptions, measured initially at their fair values at the acquisition date. The Group recognises any non-controlling interest in the acquired entity on an acquisition-by-acquisition basis either at fair value or at the non-controlling interest's proportionate share of the acquired entity's net identifiable assets.

Acquisition-related costs are expensed as incurred.

The excess of the

- consideration transferred;
- amount of any non-controlling interest in the acquired entity; and
- acquisition date fair value of any previous equity interest in the acquired entity

Over the fair value of the net identifiable assets acquired is recorded as goodwill. If those amounts are less than the fair value of the net identifiable assets of the business acquired, the difference is recognised directly in the consolidated statement profit or loss as a bargain purchase.

Where settlement of any part of cash consideration is deferred, the amounts payable in the future are discounted to their present value as at the date of exchange. The discount rate used is the entity's incremental borrowing rate, being the rate at which a similar borrowing could be obtained from an independent financier under comparable terms and conditions.

Contingent consideration is classified either as equity or a financial liability. Amounts classified as a financial liability are subsequently re-measured to fair value with changes in fair value recognised in profit or loss.

If the business combination is achieved in stages, the acquisition date carrying value of the acquirer's previously held equity interest in the acquire is re-measured to fair value at the acquisition date. Any gains or losses arising from such re-measurement are recognised in profit or loss.

## 2.4 Significant accounting policies (continued)

### (e) Cash and cash equivalents

Cash and cash equivalents comprise of 'cash in hand' and 'due from banks', which mature within three months from the date of placement, net of balances 'due to banks' maturing within three months from the date of acceptance and 'restricted balances'. Cash and cash equivalents are carried in the consolidated statement of financial position at amortised cost using the effective interest rate less any amounts written off and provision for impairment.

### (f) Financial assets

Classification

The Group has elected to apply IFRS 9 Financial Instruments as issued in July 2015, because the new accounting policies provide more reliable and relevant information for users to assess the amounts, timing and uncertainty of future cash flows in accordance with the transitional provisions in IFRS 9.

The Group classifies its financial assets in the following measurement categories:

i. those to be measured subsequently at fair value (either through other comprehensive income, or through profit or loss); and
ii. those to be measured at amortised cost. The classification depends on the entity's business model for managing the financial assets and the contractual terms of the cash flows.

For assets measured at fair value, gains and losses will either be recorded in profit or loss or consolidated statement of other comprehensive income. For investments in debt instruments, this will depend on the business model for which the investment is held. For investments in equity instruments, this will depend on whether the Group has made an irrevocable election at the time of initial recognition to account for the equity investment at fair value through other comprehensive income.

The Group reclassifies debt investments when and only when its business model for managing those assets changes.

Measurement

At initial recognition, the Group measures a financial asset at its fair value plus, in the case of a financial asset not at fair value through profit or loss, transaction costs that are directly attributable to the acquisition of the financial asset. Transaction costs of financial assets carried at fair value through profit or loss are expensed in the consolidated income statement.

Debt instruments

Subsequent measurement of debt instruments depends on the Group's business model for managing the asset and the cash flow characteristics of the asset. There are three measurement categories into which the Group classifies its debt instruments:

## 2.4 Significant accounting policies (continued)

### (f) Financial assets (continued)

Debt instruments (continued)

i. Amortised cost: financial assets that are held for collection of contractual cash flows where those cash flows represent solely payments of principal and profit are measured at amortised cost. A gain or loss on a debt investment that is subsequently measured at amortised cost and is not part of a hedging relationship is recognised in profit or loss when the asset is derecognised or impaired. Interest income from these financial assets is included in the profit and loss within the interest income using the effective interest rate method.

ii. Fair value through other comprehensive income (FVOCI): financial assets that are held for collection of contractual cash flows and for selling the financial assets, where the assets' cash flows represent solely payments of principal and profit are measured at fair value through other comprehensive income (FVOCI). Movements in the carrying amount are taken through OCI, except for the recognition of impairment gains or losses, interest income and foreign exchange gains and losses, which are recognised in the profit and loss. When the financial asset is derecognised, the cumulative gain or loss previously recognised in OCI is reclassified from equity to profit or loss.

iii. Fair value through profit or loss: financial assets that do not meet the criteria for amortised cost or FVOCI are measured at fair value through profit or loss. A gain or loss on a debt investment that is subsequently measured at fair value through profit or loss and is not part of a hedging relationship is recognised in the profit and loss and presented net in the profit and loss within other gains/(losses) in the period in which it arises. Interest income from these financial assets is included in 'Interest income' using the effective interest rate method.

Business model: the business model reflects how the Group manages the assets in order to generate cash flows. That is, whether the Group's objective is solely to collect the contractual cash flows from the assets or is to collect both the contractual cash flows and cash flows arising from the sale of assets. If neither of these is applicable (e.g. financial assets are held for trading purposes), then the financial assets are classified as part of 'other' business model and measured at FVTPL. Factors considered by the Group in determining the business model for a group of assets include past experience on how the cash flows for these assets were collected, how the asset's performance is evaluated and reported to key management personnel, how risks are assessed and managed and how managers are compensated.

SPPI: Where the business model is to hold assets to collect contractual cash flows or to collect contractual cash flows and sell, the Group assesses whether financial instruments' cash flows represent solely payments of principal and interest (the 'SPPI test').

In making this assessment, the Group considers whether contractual cash flows are consistent with a basic lending arrangement, i.e. interest includes only consideration for the time value of money, credit risk, other basic lending risks and an interest rate that is consistent with basic lending arrangement. Where the contractual terms introduce exposure to risk or volatility that are inconsistent with a basic lending arrangement, the related financial asset is classified and measured at fair value through profit or loss.

## 2.4 Significant accounting policies (continued)

### (f) Financial assets (continued)

Debt instruments (continued)

Financial assets with embedded derivatives are considered in their entirely when determining whether their cash flows are solely payment of principal and interest.

The Group reclassifies debt investments when and only when its business model for managing those assets changes. The reclassification takes place from the start of the first reporting period following the change. Such changes are expected to be very infrequent and there were no material reclassification during the year.

Equity instruments

Equity instruments are instruments that meet the definition of equity from the issuer's perspective; that is, instruments that do not contain a contractual obligation to pay and that evidence a residual interest in the issuer's net assets. Examples of equity instruments include basic ordinary shares.

The Group subsequently measures all equity investments at fair value through profit or loss, except where the Group's management has *elected, at initial recognition, to irrevocably designate an equity investment* at fair value through other comprehensive income. The Group's policy is to designate equity investments as FVTOCI when those investments are held for purposes other than to generate investment returns. When this election is used, fair value gains and losses are recognised in OCI and are not subsequently reclassified to profit or loss, including on disposal. Impairment losses (and reversal of impairment losses) are not reported separately from other changes in fair value.

Dividends from such investments continue to be recognised in Profit and loss and when the Group's right to receive payments is established. Changes in the fair value of financial assets at fair value through profit or loss are recognised in net income from investment in the profit and loss. Impairment losses (and reversal of impairment losses) on equity investments measured at FVOCI are not reported separately from other changes in fair value.

Amortised cost and effective interest method

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

The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial asset or financial liability to the gross carrying amount of a financial asset (i.e. its amortised cost before any impairment allowance) or to the amortised cost of a financial liability. The calculation does not consider expected credit losses and includes transaction costs, premiums or discounts and fees paid or received that are integral to the effective interest rate, such as origination fees.

## 2.4 Significant accounting policies (continued)

### (f) Financial assets (continued)

Amortised cost and effective interest method (continued)

When the Group revises the estimates of future cash flows, the carrying amount of the respective financial asset or financial liability is adjusted to reflect the new estimate discounted using original effective interest rate. Any changes are recognised profit and loss.

Interest income is calculated by applying the effective interest rate to the gross carrying amount of financial assets, except for financial assets that have subsequently become credit-impaired (or stage 3), for which interest income is calculated by applying the effective interest rate to their amortised cost (i.e. net of the expected credit loss provision).

Derecognition

Financial assets are derecognised when the contractual rights to receive the cash flows from these assets have ceased to exist or the assets have been transferred and substantially all the risks and rewards of ownership of the assets are also transferred (that is, if substantially all the risks and rewards have not been transferred, the Group tests control to ensure that continuing involvement on the basis of any retained powers of control does not prevent derecognition).

Impairment of financial assets

The Group assesses on a forward-looking basis the expected credit losses ('ECL') associated with its debt instrument assets carried at amortised cost and FVTOCI and with the exposure arising from loan commitments and financial guarantee contracts. The Group recognises a loss allowance for such losses at each reporting date. The measurement of ECL reflects:

- An unbiased and probability-weighted amount that is determined by evaluating a range of possible outcomes;
- The time value of money; and
- Reasonable and supportable information that is available without undue cost or effort at the reporting date about past events, current conditions and forecasts of future economic conditions.

*Note 31.3.2* provides more detail of how the expected credit loss allowance is measured.

Modification of loans

The Group sometimes renegotiates or otherwise modifies the contractual cash flows of loans to customers. Where this happens, the Group assesses whether or not the new terms are substantially different to the original terms. The Group does this by considering, among others, the following factors:

Modification of loans

- If the borrower is in financial difficulty, whether the modification merely reduces the contractual cash flows to amounts the borrower is expected to be able to pay.
- Whether any substantial new terms are introduced, such as a profit share / equity based return that substantially affects the risk profile of the loan.
- Significant extension of the loan term when the borrower is not in financial difficulty.
- Significant change in the interest rate.
- Change in the currency the loan is denominated in.
- Insertion of collateral, other security or credit enhancements that significantly affect the credit risk associated with the loan.

If the terms are substantially different, the Group derecognises the original financial asset and recognises a 'new' asset at fair value and recalculates a new effective interest rate for the asset. The date of renegotiation is consequently considered to be the date of initial recognition for impairment calculation purposes, including for the purpose of determining whether a significant increase in credit risk has occurred. However, the Group also assesses whether the new financial asset recognised is deemed to be credit-impaired at initial recognition, especially in circumstances where the renegotiation was driven by the debtor being unable to make the originally agreed payments. Differences in the carrying amount are also recognised in profit and loss as a gain or loss on derecognition.

If the terms are not substantially different, the renegotiation or modification does not result in the derecogntion, and the Group recalculates the gross carrying amount based on the revised cash flows of the financial asset and recognises a modification gain or loss in profit and loss. The new gross carrying amount is recalculated by discounting the modified cash flows at the original effective interest rate.

Derecognition other than on a modification

Financial assets, or a portion thereof, are derecognised when the contractual rights to receive the cash flows from the assets have expired, or when they have been transferred and either (i) the Group transfers substantially all the risks and rewards of ownerships, or (ii) the Group neither transfers nor retains substantially all the risks and rewards of ownership and the Group has not retained control.

## 2.4 Significant accounting policies (continued)

### (f) Financial assets (continued)

Derecognition other than on a modification (continued)

The Group enters into transactions where it retains the contractual rights to receive cash flows from assets but assumes a contractual obligation to pay those cash flows to other entities and transfers substantially all of the risks and rewards.

These transactions are accounted for as 'pass through' transfers that result in derecognition if the Group:

- Has no obligation to make payments unless it collects equivalent amounts from the assets;
- Is prohibited from selling or pledging the assets; and
- Has an obligation to remit any cash it collects from the assets without material delay.

Collateral (shares and bonds) furnished by the Group under standard repurchase agreements and securities lending and borrowing transactions are not derecognised because the Group retains substantially all the risks and rewards on the basis of predetermined repurchase price, and the criteria for derecognition are therefore not met. This also applies to certain securitisation transactions in which the Group retain a subordinated residual interest.

### (g) Financial liabilities

Classification and subsequent measurement

Financial liabilities (including customers' 'deposits and margin accounts' and 'due to bank – short term borrowings and medium term loans') are initially recognised as fair value and subsequently measured at amortised cost, except for:

- Financial liabilities at fair value through profit or loss: this classification is applied to derivatives, financial liabilities held for trading and other financial liabilities designated as such on initial recognition. Gains or losses on financial liabilities designated at fair value through profit or loss are presented partially in other comprehensive income (the change in fair value due to credit risk) and partially profit or loss (the remaining amount of change in the fair value of the liability). This is unless such a presentation would create, or enlarge, an accounting mismatch, in which case the gains and losses attributable to changes in the credit risk of the liability are also presented in profit or loss;
- Financial liabilities arising from the transfer of financial assets which did not qualify for derecognition whereby for financial liability is recognised for the consideration received for the transfer. In subsequent periods, the Group recognises any expense incurred on the financial liability; and
- Financial guarantee contracts and loan commitments.

## 2.4 Significant accounting policies (continued)

### (g) Financial liabilities (continued)

Derecognition

Financial liabilities are derecognised when they are extinguished (i.e. when the obligation specified in the contract is discharged, cancelled or expires).

When replacing an existing debt with a new debt from a new lender, the existing debt would be de-recognized in the consolidated statement of financial position, with the difference between the carrying amount and the fair value of the consideration paid recognised in profit or loss. However, when modifying or exchanging a debt while keeping the original lender, the International Financial Reporting Standards (IFRS) have specific guidance on whether the transaction results in a de-recognition or is accounted for differently. This analysis is driven by the question whether the modification is "substantial" or whether the original debt has been replaced by another debt with "substantially" different terms.

### (h) Financial guarantee contracts and loan commitments

Financial guarantees are contracts that require the Group to make specified payments to reimburse the holders for a loss they incur because a specified debtor fails to make payment when due, in accordance with the terms of a debt instrument. Loan commitments are irrevocable commitments to provide credit under pre-specified terms and conditions.

Financial guarantee contracts are initially measured at fair value and subsequently measured at the higher of:

- The amount of the loss allowance; and
- The premium received on initial recognition less income recognized in accordance with the principles of IFRS 15.

Loan commitments provided by the Group are measured as the amount of the loss allowance calculated as described in *Note 31*.

### (i) Receivables and other assets

Receivables and other assets that have fixed or determinable payments that are not quoted in an active market are classified as receivables. Receivables are measured at amortised cost using the effective interest method, less any impairment. Income is recognised by applying the effective interest rate, except for short-term receivables when the recognition of interest would be immaterial.

## 2.4 Significant accounting policies (continued)

### (j) Islamic financing and investing assets

Islamic financing assets are financial assets with fixed or expected profit payments. These assets are not quoted in an active market. They arise when the Group provides funds directly to a customer with no intention of trading the receivable.

i. Murabaha is stated at amortised cost less any provisions for impairment and deferred income.

ii. Ijara's cost is measured and reported in the consolidated financial statements at a value not exceeding the cash equivalent value. The Ijara and purchase and leaseback are classified as a finance lease, when the Group undertakes to sell the leased assets to the lessee using an independent agreement upon the maturity of the lease and the sale results in transferring all the risks and rewards incident to an ownership of the leased assets to the lessee. Leased assets represents finance lease of assets for periods, which either approximate or cover a major part of the estimated useful lives of such assets. Leased assets are stated at amounts equal to the net investment outstanding in the leases including the income earned thereon less impairment provisions.

### (k) Property, fixtures and equipment

Property, fixtures and equipment are stated at cost less accumulated depreciation and any impairment in value. The carrying amounts are reviewed at each reporting date to assess whether they are recorded in excess of their recoverable amount and, where carrying values exceed the recoverable amount, assets are written down.

Depreciation is provided on a straight-line basis on all property and equipment, other than freehold land, which is determined to have an indefinite life.

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

| | **Years** |
|---|---|
| Motor vehicles | 4 |
| Furniture, fixtures and equipment | 3-5 |
| Computer hardware | 3-4 |

Capital work-in progress is initially recorded at cost, and upon completion is transferred to the appropriate category of property and equipment and thereafter depreciated.

## 2.4 Significant accounting policies (continued)

### (l) Intangible assets

Intangible assets acquired separately are measured on initial recognition at cost. The cost of intangible assets acquired in a business combination is its fair value as at the date of acquisition. Following initial recognition, intangible assets are carried at cost less any accumulated amortisation and any accumulated impairment losses. Internally generated intangible assets, excluding capitalised development costs, are not capitalised and expenditure is reflected in the Profit and loss in the year in which the expenditure is incurred. The useful lives of intangible assets are assessed as either finite or indefinite.

Intangible assets with finite lives are amortised over the useful economic life and assessed for impairment whenever there is an indication that the intangible asset may be impaired. The amortisation period and the amortisation method for an intangible asset with a finite useful life are reviewed at least at each financial year end. Changes in the expected useful life or the expected pattern of consumption of future economic benefits embodied in the asset is accounted for by changing the amortisation period or method, as appropriate, and are treated as changes in accounting estimates. The estimated useful economic life of the intangible asset for the calculation of amortisation is as 5 years.

Intangible assets with indefinite useful lives are not amortised, but are tested for impairment annually, either individually or at the cash-generating unit level. The assessment of indefinite life is reviewed annually to determine whether the indefinite life continues to be supportable. If not, the change in useful life from indefinite to finite is made on a prospective basis.

Gains or losses arising from derecognition of an intangible asset are measured as the difference between the net disposal proceeds and the carrying amount of the asset and are recognised in the profit and loss when the asset is derecognised.

### (m) Impairment of non-financial assets

Non financial assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash inflows (cash-generating units).

The impairment test also can be performed on a single asset when the fair value less cost to sell or the value in use can be determined reliably. Non-financial assets that suffered impairment are reviewed for possible reversal of the impairment at each reporting date.

## 2.4 Significant accounting policies (continued)

### (n) Investment properties

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

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

Transfer is made to or from investment property only when there is a change in use evidenced by the end of owner-occupation or commencement of an operating lease to another party. For a transfer from investment property to owner occupied property, the deemed cost for subsequent accounting is the fair value at the date of change in use. If owner occupied property becomes an investment property, the Group accounts for such property in accordance with the policy stated under property and equipment up to the date of the change in use. Fair value is determined by open market values based on valuations performed by independent surveyors and consultants or broker's quotes.

### (o) Insurance receivables

Insurance receivables are recognised when due and measured on initial recognition at the fair value of the consideration received or receivable. Subsequent to initial recognition, insurance receivables are measured at amortised cost, using the effective interest rate method. The carrying value of insurance receivables is reviewed for impairment whenever events or circumstances indicate that the carrying amount may not be recoverable, with the impairment loss recorded in the consolidated income statement.

### (p) Reinsurance contracts held

In order to minimise financial exposure from large claims, the Group enters into agreements with other parties for reinsurance purposes. Claims receivable from reinsurers are estimated in a manner consistent with the claim liability and in accordance with the reinsurance contract. Once the claim is paid the amount due from the reinsurer in connection with the paid claim is transferred to receivables arising from insurance and reinsurance companies.

At each reporting date, the Group assesses whether there is any indication that a reinsurance asset may be impaired. Where an indicator of impairment exists, the Group makes a formal estimate of recoverable amount. Where the carrying amount of a reinsurance asset exceeds its recoverable amount the asset is considered impaired and is written down to its recoverable amount.

Ceded reinsurance arrangements do not relieve the Group from its obligations to policy holders.

Reinsurance assets or liabilities are derecognised when the contractual rights are extinguished or expire when the contract is transferred to another party.

## 2.4 Significant accounting policies (continued)

### (q) Repurchase agreements

Assets sold with a simultaneous commitment to repurchase at a specified future date ("Repo") are not derecognised. The counterparty liability for amounts received under these agreements is included in term loans in the consolidated statement of financial position, as appropriate. The difference between the sale and repurchase price is treated as interest expense, which is accrued over the life of the repo agreement using the effective interest rate.

### (r) Operating segment reporting

An operating segment is a distinguishable component of the Group that is engaged either in providing products or services (business segment) which is subject to risks and rewards that are different from those of other segments and whose operating results are regularly reviewed by the Group's Chief Operating decision maker to make decisions about allocation of resources and assess its performance.

### (s) Provisions

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

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

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

### (t) Accounts payable and accruals

Liabilities are recognised for amounts to be paid in the future for goods or services received, whether billed by the party or not.

### (u) Employees' end of service benefits

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

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

## 2.4 Significant accounting policies (continued)

### (v) Foreign currencies

Foreign currency transactions are recorded at rates of exchange ruling at the value dates of the transactions. Monetary assets and liabilities denominated in foreign currencies are translated into AED at the rates of exchange ruling at the consolidated statement of financial position date. Any resultant gains and losses are recognised in the consolidated statement of income statement.

Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rates as at the dates of the initial transactions. Non-monetary items measured at fair value in a foreign currency are translated using the exchange rates at the date when the fair value was determined.

### (w) Offsetting financial instruments

Financial assets and financial liabilities are offset and the net amount reported in the consolidated statement of financial position when there is a legally enforceable right to offset the recognised amounts and there is an intention to settle on a net basis or realise the asset and settle the liability simultaneously.

### (x) Earnings per share

(i) Basic earnings per share

Basic earnings per share is calculated by dividing:

- the profit attributable to owners of the Group, deducting any costs of servicing equity other than ordinary shares
- by the weighted average number of ordinary shares outstanding during the financial year, adjusted for bonus elements in ordinary shares issued during the year and excluding treasury shares (note 26).

(ii) Diluted earnings per share

Diluted earnings per share adjusts the figures used in the determination of basic earnings per share to take into account:

- the after income tax effect of interest and other financing costs associated with dilutive potential ordinary shares, and
- the weighted average number of additional ordinary shares that would have been outstanding assuming the conversion of all dilutive potential ordinary shares.

## 2.4 Significant accounting policies (continued)

### (y) Fair values measurements

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date, regardless of whether that price is directly observable or estimated using another valuation technique. In estimating the fair value of an asset or a liability, the Company takes into account the characteristics of the asset or liability if market participants would take those characteristics into account when pricing the asset or liability at the measurement date.

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

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

The fair value measurement 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.

A fair value measurement of a non-financial asset 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 Company uses 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.

For assets and liabilities that are recognised in the financial statements on a recurring basis, the Company determines 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.

## 2.4 Significant accounting policies (continued)

### (y) Fair values measurements (continued)

For the purpose of fair value disclosures, the Group 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. An analysis of fair values of financial instruments and further details as to how they are measured are provided in Note 32.

Management determines the policies and procedures for both recurring fair value measurement and for non-recurring measurement. External valuers are involved for valuation of significant assets, such as investment property. Selection criteria for valuers include market knowledge, reputation, independence and whether professional standards are maintained. Management decides, after discussions with the Group's external valuers, which valuation techniques and inputs to use for each case.

Management, in conjunction with the Group's external valuers, also compares changes in the fair value of each asset and liability with relevant external sources to determine whether the change is reasonable.

### (z) Recognition of income and expenses

(i) Interest

For all financial instruments measured at amortised cost and interest bearing financial instruments, interest income or expense is recorded at 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. The calculation takes into account all contractual terms of the financial instrument and includes any fees or incremental costs that are directly attributable to the instrument and are an integral part of the effective interest rate, but not future credit losses. The carrying amount of the financial asset or financial liability is adjusted if the Group revises its estimates of payments or receipts. The adjusted carrying amount is calculated based on the original effective interest rate and the change in carrying amount is recorded as interest income or expense.

(ii) Fee and commission

The Group earns fee and commission income from a diverse range of services it provides to its customers. Fee income can be divided into the following two categories:

- Fees earned for the provision of services over a period of time are accrued over that period. These fees include commission income and other management and advisory fees. Loan commitment fees for loans that are likely to be drawn down and other credit-related fees are deferred (together with any incremental costs) and recognised as an adjustment to the effective interest rate on the loan. When it is unlikely that a loan will be drawn down, the loan commitment fees are recognised over the commitment period on a straight-line basis.

## 2.4 Significant accounting policies (continued)

### (z) Recognition of income and expenses (continued)

(ii) Fee and commission (continued)

- Fees or components of fees that are linked to a certain performance are recognised after fulfilling the corresponding criteria.

(iii) Murabaha

Murabaha income is recognised on a time apportioned basis over the period of the contract based on the principal amounts outstanding.

(iv) Ijara

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

(v) Income on balances with financial institutions

Income on balances with financial institutions is calculated, on account, based on the expected/anticipated profit rates net of relevant fees and expenses.

(vi) Dividend income

Income is recognised when the Group's right to receive the payment is established.

*(a) Insurance income*

(i) Insurance contracts

Insurance contracts are those contracts where the Group has accepted significant insurance risk from another party (the "policyholders") by agreeing to compensate the policyholders if a specified uncertain future event (the "insured event") adversely affects the policyholders.

Once a contract has been classified as an insurance contract, it remains an insurance contract for the remainder of its lifetime, even if the insurance risk reduces significantly during this period, unless all rights and obligations are extinguished or expire.

(ii) Premiums earned

Premiums written are taken into income over the terms of the policies to which they relate on a pro-rata basis. Unearned premiums represent the portion of premiums written relating to the unexpired periods of coverage.

(iii) Commissions earned

Profit commission is accounted for as and when received while other commissions are accounted for when earned.

## 2.4 Significant accounting policies (continued)

### (z) Recognition of income and expenses (continued)

(iv) Claims

Claims comprising amounts payable to contract holders and third parties and related loss adjustment expenses, net of salvage and other recoveries, are charged to income as incurred. Claims comprise the estimated amounts payable, in respect of claims reported to the Group.

The Group generally estimates its claims based on previous experience. Claims requiring court or arbitration decisions are estimated individually. Independent loss adjusters normally estimate property claims.

The Group does not discount its liability for unpaid claims as these are expected to be settled within one year of reporting date.

## 2.5 Significant accounting judgements and estimates

The preparation of the Group's consolidated financial statements requires management to make judgements, estimates and assumptions that affect the reported amounts of revenues, expenses, assets and liabilities and the accompanying disclosures, and the disclosure of contingent liabilities. 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. Uncertainty about these assumptions and estimates could result in outcomes that could require a material adjustment to the carrying amount of the asset or liability affected in the future periods.

*(a) Judgments*

In the process of applying the Group's accounting policies, management has made the following judgements, apart from those involving estimations, which have the most significant effect on the amounts recognised in the consolidated financial statements:

(i) Consolidation of entities in which the Group holds less than majority of voting rights

The Group considers that it controls Insurance House P.S.C. even though it owns less than 50% of the voting rights. The Company is the largest shareholder of Insurance House P.S.C. with 45.15% equity interest. Furthermore, the Company has substantial and material board presence and control over key financial and operational decisions.

## 2.5 Significant accounting judgements and estimates (continued)

*(a) Judgments* (continued)

(ii) Classification of properties

Management decides, on acquisition of a property, whether it should be classified as investment property, property and equipment or as property held for sale. Properties acquired by the Group are recorded as investment properties if these were acquired for rental purposes or capital appreciation. Properties held for own use are recorded as property, fixtures and equipment. Properties are recorded as held for sale if their carrying amounts will be recovered through a sale transaction.

*(b) Estimates and assumptions*

The key assumptions concerning the future and other key sources of estimation uncertainty at the reporting date, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are discussed below. The Group based its assumptions and estimates on parameters available when the consolidated financial statements were prepared. Existing circumstances and assumptions about future developments, however, may change due to market changes or circumstances arising beyond the control of the Group. Such changes are reflected in the consolidated financial statements when they occur.

(i) Fair value of investment properties

The Group engaged an independent valuation specialist to assess fair value for its investment properties using a valuation methodology based on the 'income method'. The key assumptions used to determine the fair value of investment properties and sensitivity analyses are disclosed *Notes 28 and 32*.

(ii) Fair value of unquoted investments

As described in *Note 32*, management uses their judgment in selecting an appropriate valuation technique for financial instruments not quoted in an active market. Valuation techniques commonly used by market practitioners are applied. Such financial instruments are valued using discounted cash flow and capitalisation of sustainable earnings analysis based on assumptions supported, where possible, by observable market prices or rates. The estimation of fair value of unquoted shares includes some assumptions not supported by observable market prices or rates. Details of assumptions used and of the results of sensitivity analyses regarding these assumptions are provided in *Note 32*.

(iii) Measurement of the expected credit loss allowance

The measurement of the expected credit loss allowance for financial assets measured at amortised cost and FVTOCI is an area that requires the use of complex models and significant assumptions about future economic conditions and credit behavior (e.g. the likelihood of customers defaulting and the resulting losses). Explanation of the inputs, assumptions and estimation techniques used in measuring ECL is further detailed in *Note 31.3.2 (c)*.

## 2.5 Significant accounting judgements and estimates (continued)

*(b) Estimates and assumptions* (continued)

(iii) Measurement of the expected credit loss allowance (continued)

A number of significant judgements are also required in applying the accounting requirements for measuring ECL, such as:

- Determining the criteria for significant increase in credit risk;
- Determining the criteria and definition of default;
- Choosing appropriate models and assumptions for the measurement of ECL;
- Establishing the number and relative weightings of forward-looking scenarios for each type of product/market and the associated ECL; and
- Establishing groups of similar financial assets for the purposes of measuring ECL

(iv) Provision for outstanding claims

Considerable judgement by management is required in the estimation of amounts due to contract holders arising from claims made under insurance contracts. Such estimates are necessarily based on significant assumptions about several factors involving varying, and possible significant, degrees of judgement and uncertainty and actual results may differ from management's estimates resulting in future changes in estimated liabilities. The Group generally estimates its claims based on previous experience. Claims requiring court or arbitration decisions are estimated individually. Independent loss adjusters along with the Group's internal legal counsel normally estimate such claims. Management reviews its provisions for claims incurred on a quarterly basis.

## 2.6 Definitions

The following terms are used in the consolidated financial statements with the meaning specified:

*(a) Commodities Murabaha*

A selling contract for commodities at the purchase price with a defined and agreed profit mark-up. The mark-up may be a percentage of the purchase price or a fixed amount.

*(b) Istisna'a*

A sale contract, in which the Group (Al Saanee) sells an asset to be developed using its own materials to a customer (Al Mustasnee) according to pre-agreed upon precise specification, at a specific price, installments dates and to be delivered on a specific date. This developed asset can be either developed directly by the Group or through a subcontractor and then it is handed over to the customer on the pre-agreed upon date.

## 2.6 Definitions (continued)

*(c) Ijara*

A lease agreement whereby the Group (as lessor) leases an asset to the Customer (as lessee), after purchasing/acquiring the specified asset according to the customer's request and promise to lease, either from a third party seller or from the customer itself, against certain rental payments for specified lease term/periods. Whereas, upon fulfillment of all the obligations by the customer (lessee) under the lease agreement, the ownership of the subject asset is transferred from the Group (lessor) to the customer (lessee).

*(d) Sukuk*

These comprise Sharia'a compliant financial instruments representing debt under Murabaha contracts.

*(e) Wakala*

An agreement between the Group and a customer whereby one party (the principal: the Muwakkil) appoints the other party (the agent: Wakil) to invest certain funds according to the terms and conditions of the Wakala for a fixed fee in addition to any profit exceeding the expected profit as an incentive for the Wakil for the good performance. Any losses as a result of the misconduct or negligence or violation of the terms and conditions of the Wakala are borne by the Wakil; otherwise, they are borne by the principal.

## 3 Subsidiaries and partly owned subsidiaries

The consolidated financial statements comprise the financial statements of the Company and the following subsidiaries:

| Name of subsidiary | Country of incorporation | Ownership interest % | | Principal activity |
|---|---|---|---|---|
| | | **2018** | 2017 | |
| Islamic Finance House P.J.S.C. | U.A.E. | 100 | 100 | Islamic financing services |
| Insurance House P.S.C. | U.A.E. | 45.15 | 44.83 | Insurance |
| Finance House Securities Co L.L.C. | U.A.E. | 70 | 70 | Brokerage |
| CAPM Investment P.J.S | U.A.E. | 100 | 100 | Investment and asset management |

## 3 Subsidiaries and partly owned subsidiaries (continued)

The following table illustrates the summarised financial information of subsidiaries with material non-controlling interests. This information is based on amounts before inter-company eliminations:

| | **Insurance House P.S.C.** | | **Finance House Securities Co. LLC** | | **Total** | |
|---|---|---|---|---|---|---|
| | **2018 AED'000** | 2017 AED'000 | **2018 AED'000** | 2017 AED'000 | **2018 AED'000** | 2017 AED'000 |
| Non-controlling interests % | **54.85** | 55.17 | **30** | 30 | | |
| **Accumulated balance of material non-controlling interests** | 52,312 | 49,033 | 23,576 | 23,399 | 75,888 | 72,432 |
| **Subsidiaries' statement of financial position** | | | | | | |
| Total assets | 304,468 | 254,000 | 175,117 | 205,221 | 479,585 | 459,221 |
| Total liabilities | (204,640) | (162,505) | (93,916) | (124,608) | (298,556) | (287,113) |
| Total equity | **99,828** | **91,495** | **81,201** | **80,613** | **181,029** | **172,108** |
| **Subsidiaries' income statement** | | | | | | |
| Net revenue | 50,112 | 26,410 | 8,964 | 12,687 | 59,076 | 39,097 |
| **Net profit/(loss) for the year** | 10,643 | (5,208) | 589 | 3,935 | 11,232 | (1,273) |
| **Net profit/(loss) for the year allocated to non-controlling interest** | 5,838 | (2,897) | 177 | 1,181 | 6,015 | (1,716) |
| **Total comprehensive income/(loss) for the year** | **7,433** | **(4,260)** | **589** | **3,935** | **8,022** | **(325)** |
| **Total comprehensive income/(loss) allocated to non- controlling interest** | **4,077** | **(2,370)** | **177** | **1,181** | **4,254** | **(1,189)** |
| **Subsidiaries' cash flows** | | | | | | |
| Operating | 23,157 | 24,476 | 37,773 | 20,832 | 60,930 | 45,308 |
| Investing | (73,250) | 5,420 | (65) | (90) | (73,315) | 5,330 |
| Financing | - | - | (37,727) | 3,566 | (37,727) | 3,566 |
| **Net (decrease)/increase in cash and cash equivalents** | **(50,093)** | **29,896** | **(19)** | **24,308** | **(50,112)** | **54,204** |

## 4 Cash and cash equivalents

| | 2018 AED'000 | 2017 AED'000 |
|---|---|---|
| **Cash balances** | | |
| Cash in hand | 11,599 | 11,437 |
| Restricted cash balances* | 6,000 | 6,000 |
| | **17,599** | **17,437** |
| **Due from banks with original maturities of less than three months** | | |
| Placements with banks | 201,001 | 331,309 |
| Call accounts | 167,264 | 234,777 |
| Current and demand accounts | 132,553 | 110,761 |
| Balance with UAE Central Bank | 11,745 | 24,185 |
| | **512,563** | **701,032** |
| | **530,162** | **718,469** |
| Due to banks and other financial institutions with original maturity of less than three months | (15,014) | (23,831) |
| Restricted cash balances* | (6,000) | (6,000) |
| Cash and cash equivalents | **509,148** | **688,638** |

*Restricted cash represents deposits with insurance authority amounting to AED 6,000 thousand (2017: AED 6,000 thousand).

Reconciliations to liquidity risk and funding management *(Note 31.8)*

| | 2018 AED'000 | 2017 AED'000 |
|---|---|---|
| Cash in hand | 11,599 | 11,437 |
| Restricted cash balances* | 6,000 | 6,000 |
| Balance with UAE Central Bank | 11,745 | 24,185 |
| Cash and balances with U.A.E. Central Bank *(Note 31.8)* | **29,344** | **41,622** |

| | 2018 AED'000 | 2017 AED'000 |
|---|---|---|
| Due from banks | 512,563 | 701,032 |
| Less: Balance with UAE Central bank | (11,745) | (24,185) |
| Due from banks and financial institutions *(Note 31.8)* | **500,818** | **676,847** |

## 5 Investments

| | At fair value through other comprehensive income AED'000 | At fair value through profit or loss AED'000 | At amortised cost AED'000 | Total AED'000 |
|---|---|---|---|---|
| **31 December 2018** | | | | |
| Equity instruments: | | | | |
| - Quoted | 454,925 | 161,384 | - | 616,309 |
| - Unquoted | 99,317 | - | - | 99,317 |
| Debt instruments: | | | | |
| - Unquoted investments | - | - | 1,837 | 1,837 |
| Investment in managed funds | 6,336 | - | - | 6,336 |
| | **560,578** | **161,384** | **1,837** | **723,799** |
| Within UAE | 360,354 | 161,384 | - | 521,738 |
| Outside UAE | 200,224 | - | 1,837 | 202,061 |
| | **560,578** | **161,384** | **1,837** | **723,799** |
| **31 December 2017** | | | | |
| Equity instruments: | | | | |
| - Quoted | 616,102 | 174,858 | - | 790,960 |
| - Unquoted | 92,917 | - | - | 92,917 |
| Debt instruments: | | | | |
| - Quoted - fixed rate | - | 1,500 | - | 1,500 |
| - Unquoted investments | - | - | 81,654 | 81,654 |
| Investment in managed funds | 7,322 | - | - | 7,322 |
| | **716,341** | **176,358** | **81,654** | **974,353** |
| Within UAE | 450,133 | 176,358 | - | 626,491 |
| Outside UAE | 266,208 | - | 81,654 | 347,862 |
| | **716,341** | **176,358** | **81,654** | **974,353** |

The Group holds investments in Tier 1 perpetual instruments which are classified under quoted equity instruments and unquoted equity instruments amounting to AED 220,853 thousand (2017: AED 336,390 thousand) and AED 20,000 thousand (2017: AED 39,882 thousand), respectively. These instruments carry an average coupon interest/profit rate between 5.5% p.a - 8.25% p.a.

During the year, the Group has redeemed investments on maturity carried at amortised cost of AED 81,654 thousand (2017: AED 88,249 thousand).

## 6 Loans and advances

| | 2018<br>AED'000 | 2017<br>AED'000 |
|---|---|---|
| Commercial loans | 2,102,120 | 2,052,177 |
| Retail finance | 550,029 | 498,208 |
| Gross loans and advances | **2,652,149** | **2,550,385** |
| Less: assessed allowance for impairment | (351,645) | (214,584) |
| Net loans and advances | **2,300,504** | **2,335,801** |

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

| | 2018<br>AED'000 | 2017<br>AED'000 |
|---|---|---|
| At 1 January 2018 | 214,584 | 219,801 |
| Change on initial application of IFRS 9 *(Note 2.3)* * | 61,877 | - |
| Restated balance at 1 January 2018 | **276,461** | **219,801** |
| Impairment charges for the year | 75,848 | 48,736 |
| Reversal of no longer required impairment charges | (664) | (5,300) |
| Written off | - | (48,653) |
| Balance at 31 December | **351,645** | **214,584** |

In determining the recoverability of loans and advances, the Company considers any change in the credit quality of the loans and advances measured at amortised cost from the date credit was initially granted up to the end of the reporting period. The concentration of credit risk is limited due to the fact that the customer base is large and unrelated.

* Include amount of AED 14,324 thousand relating to unfunded balances as disclosed in *Note 2.3*.

## 7 Islamic financing and investing assets

| | 2018 AED'000 | 2017 AED'000 |
|---|---|---|
| Commodity Murabaha | 115,530 | 134,942 |
| Covered card and drawings | 67,503 | 62,894 |
| Purchase and lease back | 2,094 | 5,346 |
| Ijarah | 14,284 | 18,211 |
| Others | 2,944 | 2,921 |
| Gross Islamic financing and investing assets | **202,355** | **224,314** |
| Less: assessed allowance for impairment | (59,741) | (50,944) |
| Net Islamic financing and investing assets | **142,614** | **173,370** |

The movement in the allowance during the year is as follows:

| | 2018 AED'000 | 2017 AED'000 |
|---|---|---|
| At 1 January | 50,944 | 38,421 |
| Changes on initial application of IFRS 9 | 4,484 | - |
| Restated balance at 1 January 2018 *(Note 2.3)* | **55,428** | **38,421** |
| Impairment charges for the year | 4,313 | 12,523 |
| At 31 December | **59,741** | **50,944** |

The gross Ijara and purchase and leaseback and the related present value of minimum Ijara and purchase and leaseback payments are as follows:

| | 2018 AED'000 | 2017 AED'000 |
|---|---|---|
| **Gross Ijara and purchase and lease-back** | | |
| Less than one year | 6,538 | 7,156 |
| Between one and three years | 8,019 | 11,878 |
| Between three and five years | 4,252 | 6,796 |
| More than five years | 263 | 2,157 |
| | **19,072** | **27,987** |
| Less: deferred income | (2,694) | (4,430) |
| Net Ijara and purchase and lease-back | **16,378** | **23,557** |

Present value of minimum Ijara and purchase and leaseback payments

| | 2018 AED'000 | 2017 AED'000 |
|---|---|---|
| Less than one year | 5,441 | 5,690 |
| Between one and three years | 6,734 | 9,860 |
| Between three and five years | 3,958 | 5,978 |
| More than five years | 245 | 2,029 |
| | **16,378** | **23,557** |

## 8 Investment in an associate

The Group has the following investment in an associate

| | Country of incorporation | Percentage of holding | | Principal activity |
|---|---|---|---|---|
| | | 2018 | 2017 | |
| Mainland Management L.L.C. | U.A.E | 33.33% | 33.33% | Hospitality management services |

Movement in investment in an associate is as follows:

| | 2018 AED'000 | 2017 AED'000 |
|---|---|---|
| At 1 January | 51,720 | 50,477 |
| Share of results for the year | (1,235) | 1,243 |
| At 31 December | **50,485** | **51,720** |

Summarised financial information of the associate is set out below:

| | 2018 AED'000 | 2017 AED'000 |
|---|---|---|
| Associate's statement of financial position | | |
| Assets | 202,433 | 208,047 |
| Liabilities | (50,928) | (52,888) |
| Net assets | **151,505** | **155,159** |
| Group's share of net assets | 50,502 | 51,720 |
| Carrying amount of investment in an associate | 50,485 | 51,720 |
| Income statement | | |
| Revenue | 27,699 | 33,281 |
| (Loss)/profit for the year | (3,705) | 3,729 |
| Group's share of results for the year | **(1,235)** | **1,243** |

## 9 Tier 1 Sukuk

In July 2015, the Company raised financing by way of Shari'a compliant Tier 1 Capital Certificates amounting to AED 300 million (Tier 1 Sukuk). Issuance of these Capital Certificates was approved by the Company's Extra Ordinary General Meeting (EGM) in April 2015. The UAE Central Bank has also approved the facility to be considered as Tier 1 capital for regulatory purposes. These Capital Certificates bear profit at a fixed rate payable semi-annually in arrears. The Capital Certificates are non-cumulative perpetual securities for which there is no fixed redemption date, and are callable by the Company subject to certain conditions. Tier 1 Sukuk amounting to AED 18,500 thousand (2017: AED 16,450 thousand) are held by subsidiaries of the Group and, accordingly, eliminated in the consolidated statement of financial position. The payment of the coupon amounts on those instruments is solely at the discretion of the issuer at a coupon profit rate of 7.5% p.a.

## 10 Property, fixtures and equipment

| | Furniture fixtures and equipment AED'000 | Motor vehicles AED'000 | Computer hardware and software AED'000 | Total AED'000 |
|---|---|---|---|---|
| **Cost:** | | | | |
| At 1 January 2017 | 33,187 | 3,600 | 31,990 | **68,777** |
| Additions during the year | 2,905 | 386 | 3,300 | **6,591** |
| Disposals | (2,069) | (458) | - | **(2,527)** |
| **At 31 December 2017** | 34,023 | 3,528 | 35,290 | **72,841** |
| Additions during the year | 3,266 | 697 | 15,380 | **19,343** |
| Disposals | (308) | - | (7) | **(315)** |
| **At 31 December 2018** | **36,981** | **4,225** | **50,663** | **91,869** |
| **Accumulated depreciation** | | | | |
| At 1 January 2017 | 27,026 | 1,469 | 25,606 | 54,101 |
| Charge for the year | 3,600 | 507 | 3,063 | 7,170 |
| Release on disposals | (1,901) | (419) | - | (2,320) |
| **At 31 December 2017** | 28,725 | 1,557 | 28,669 | 58,951 |
| Charge for the year | 3,896 | 399 | 4,406 | 8,701 |
| Release on disposal | (308) | - | (7) | (315) |
| **At 31 December 2018** | **32,313** | **1,956** | **33,068** | **67,337** |
| **Net book value:** | | | | |
| **At 31 December 2018** | **4,668** | **2,269** | **17,595** | **24,532** |
| **At 31 December 2017** | **5,298** | **1,971** | **6,621** | **13,890** |

## 11 Intangibles

| | License AED'000 | Goodwill AED'000 | Total AED'000 |
|---|---|---|---|
| **2018** | | | |
| **Carrying value:** | | | |
| At 1 January | 261 | 6,705 | **6,966** |
| Amortisation charges during the year | (261) | - | **(261)** |
| At 31 December | - | **6,705** | **6,705** |
| **2017** | | | |
| **Carrying value:** | | | |
| At 1 January | 1,045 | 6,705 | **7,750** |
| Amortisation charges during the year | (784) | - | **(784)** |
| At 31 December | **261** | **6,705** | **6,966** |

### License

License represents the amount paid by the Group to acquire an existing investment banking license issued by the Central Bank of UAE.

### Goodwill

Goodwill acquired through business combinations relates to Islamic Finance House P.J.S.C.

### Impairment test of goodwill

The Group performs impairment testing of the goodwill annually on 31 December.

Goodwill has been allocated to the subsidiary as a cash-generating unit. This represents the lowest level within the Group at which the goodwill is monitored for internal management purposes.

During the year, the Group has performed a goodwill impairment review based on a forecast of the subsidiary's cash flows. The recoverable amount of the cash-generating unit was estimated on the basis of its value in use, which is determined by discounting future cash flows from the continuing operation of the cash generating unit. The discount rate applied to the cash flow projections is 12% and the growth rate used to extrapolate the cash flows beyond the five-year period is 3%. Based on the results of the goodwill impairment assessment the Group has concluded that the recoverable amount of the cash-generating unit is higher than its carrying value.

## 12 Interest receivable and other assets

| | 2018<br>AED'000 | 2017<br>AED'000 |
|---|---|---|
| Accounts receivable * | 40,381 | 44,400 |
| Less: impairment | (5,712) | (6,194) |
| | **34,669** | **38,206** |
| Insurance receivables | 52,028 | 55,609 |
| Re-insurance contract assets | 42,434 | 11,727 |
| Prepayments | 39,773 | 27,871 |
| Interest receivable and profit receivable | 20,786 | 33,167 |
| Advance for investments | 5,352 | 4,302 |
| Other assets | 41,447 | 37,318 |
| | **236,489** | **208,200** |

* In 2017, the Company has entered into a sale and purchase agreement with Infosec Ventures INC (Infosec) and Paramount Computer Systems FZ LLC in respect of the sale of the Company's share in Paramount Computer System. Accounts receivable includes an amount of AED 19,500 thousand (2017: AED 19,500 thousand) receivable from Infosec. It was agreed that payments will be made over 5 years in equal instalments commencing one year after the date of signing the agreement (i.e. AED 3,900 thousand each year).

(i) No impairment charge or impairment reversals recognised at the end of the reporting periods ended 31 December 2018 and 2017, respectively.

## 13 Customers' deposits and margin accounts

| | 2018<br>AED'000 | 2017<br>AED'000 |
|---|---|---|
| Call and demand deposits | 219,765 | 222,281 |
| Time deposits | 1,785,555 | 1,870,287 |
| Wakala deposits | 35,045 | 60,834 |
| | **2,040,365** | **2,153,402** |
| Margin accounts (i) | 706,910 | 797,142 |
| | **2,747,275** | **2,950,544** |
| Analysis of customers' deposits by sector is as follows: | | |
| Government | 976,732 | 720,414 |
| Corporate | 1,770,543 | 2,230,130 |
| | **2,747,275** | **2,950,544** |

Margin accounts represent cash margins collected from corporate customers against unfunded and funded credit facilities extended to them in the normal course of business.

Customers' deposits and margin accounts carry interest/profit rates ranging from Nil to 4.50% p.a (2017: Nil to 3.5% p.a).

## 14 Short term borrowings and medium term loans

*Short-term borrowings*

| | 2018<br>AED'000 | 2017<br>AED'000 |
|---|---|---|
| At 1 January | 266,410 | 192,500 |
| Proceeds received | - | 123,910 |
| Repayments | (238,810) | (50,000) |
| At 31 December | **27,600** | **266,410** |

These short-term borrowings carry variable interest rates ranging from 4.25% p.a to 6.34% p.a (2017: 3.37% p.a to 5.31% p.a).

*Medium term loans*

| | 2018<br>AED'000 | 2017<br>AED'000 |
|---|---|---|
| At 1 January | 120,834 | 87,500 |
| Proceeds received | 150,000 | 100,000 |
| Repayments | (87,499) | (66,666) |
| At 31 December | **183,335** | **120,834** |

| Obtained in | Matures in | Approved facility line AED '000 | Repayment schedule | Interest rate |
|---|---|---|---|---|
| 24 May 2017 | 2020 | 100,000 | 11 equal instalments of AED 8,333 thousand plus interest and one final instalment (12th) covering the residual utilisation amount plus interest. | 3 months EIBOR + 2.10% p.a. |
| 21 June 2018 | 2021 | 150,000 | 5 equal instalments of AED 25,000 thousand plus interest and one final instalment (6th) covering the residual utilisation amount plus interest. | 3 months EIBOR + 2.10% p.a. |

No financial covenants attached to short-term borrowings or medium term loans.

## 15 Interest payable and other liabilities

| | 2018<br>AED'000 | 2017<br>AED'000 |
|---|---|---|
| Unearned premiums | 88,938 | 125,342 |
| Gross claims outstanding | 63,352 | 19,118 |
| Trade payables | 44,560 | 38,529 |
| Interest payable and profit payable | 30,369 | 32,532 |
| Accrued expenses | 12,801 | 25,903 |
| Unclaimed checks and dividends | - | 13,748 |
| Transit account for payday accounts | 24,529 | - |
| Unclaimed cheques | 15,661 | 11,886 |
| Other liabilities | 59,081 | 19,339 |
| | **339,291** | **286,397** |

## 16 Share capital

| | 2018<br>AED'000 | 2017<br>AED'000 |
|---|---|---|
| **Authorised, issued and fully paid** | | |
| 310.1 million shares (2017: 310.1 million shares) of AED 1 each (2017: AED 1 each) | **310,050** | **310,050** |

## 17 Employees' share-based payment scheme

The share-based payment scheme is administered by a trustee and gives the Board of Directors the authority to determine which employees of the Group will be granted the shares. The values of shares granted to employees are expensed in the period in which they are granted, and that of the remaining shares are included within shareholders' equity. During the period, no shares were granted to employees and the value of outstanding shares not yet granted to employees as of 31 December 2018 was AED 1,750 thousand (2017: AED 1,750 thousand).

## 18 Statutory reserve

In line with the provisions of the UAE Federal Commercial Companies Law No. 2 of 2015, and the Company's Articles of Association, the Company is required to transfer annually to a statutory reserve account an amount equivalent to 10% of its profit, until such reserve reaches 50% of the share capital of the Company. During the year the Group has transferred AED 1,182 thousand to the reserve (2017: AED 3,433 thousand). The statutory reserve is not available for distribution.

## 19 Dividends

The Company's General Assembly in their annual meeting held on 22 March 2018 approved a cash dividend of AED 5 fils per share (2017: AED 6 fils per share) amounting to AED 15,141 thousand (2017: AED 18,170 thousand) in total. The dividend was approved by the U.A.E Central Bank and paid during the year.

## 20 Treasury shares

Treasury shares represent the cost of 9,400 thousand shares of the Company held by the Company and a subsidiary as at 31 December 2018 (2017: 9,400 thousand shares).

| | 2018 | | 2017 | |
|---|---|---|---|---|
| | Number of shares '000 | AED'000 | Number of shares '000 | AED'000 |
| Share held by Finance House PJSC | 7,212 | 13,842 | 7,212 | 13,842 |
| Share held by Insurance House PJSC | 2,188 | 7,560 | 2,188 | 7,560 |
| | **9,400** | **21,402** | **9,400** | **21,402** |

During 2014, the Company has obtained the necessary regulatory approvals to undertake a share-buy program whereby the Company buys and sells its own shares in the normal course of its equity trading and marketing activities. These shares are treated as a deduction from shareholders' equity. Any gain or loss on sales or redemption of own shares are credited or charged to reserves. During 2018, a total of Nil shares (2017: 4,948 thousand) were purchased back from the market at an average price of AED Nil (2017: AED 1.78) per share amounting to AED Nil (2017: AED 8,791 thousand).

## 21 Commitments and contingent liabilities

The Group has contractual amounts in respect of letters of credit and letters of guarantees that commits to extend credit to customers. These agreements have fixed limits and are generally for a certain period of time.

Capital commitments represent future capital expenditures that the Group has committed to spend on assets over a period of time.

Irrevocable commitments to extend credit represent contractual irrevocable commitments to make loans and revolving credits.

## 21 Commitments and contingent liabilities (continued)

The Group had the following commitments and contingent liabilities outstanding at year end:

| | 2018 AED'000 | 2017 AED'000 |
|---|---|---|
| Letters of credit | 169,522 | 218,437 |
| Letters of guarantee | 1,370,280 | 1,509,750 |
| Capital commitments | 4,200 | 4,200 |
| Irrevocable commitments to extend credit | - | 218,074 |
| | **1,544,002** | **1,950,461** |

All financial guarantees issued are in the ordinary course of business.

## 22 Net interest income and income from Islamic financing and investing assets

| | 2018 AED'000 | 2017 AED'000 |
|---|---|---|
| Loans and advances | 227,440 | 210,579 |
| Due from banks | 15,085 | 8,617 |
| Income from Islamic financing and investing assets | 17,267 | 18,787 |
| Others | 1,751 | 6,916 |
| **Interest income and income from Islamic financing and investing assets** | **261,543** | **244,899** |
| Customers' deposits and margin accounts | (66,638) | (55,723) |
| Profit distributable to depositors | (1,994) | (2,839) |
| Due to banks and other financial institutions | (16,976) | (15,472) |
| **Interest expense and profit distributable to depositors** | **(85,608)** | **(74,034)** |
| **Net interest income and income from Islamic financing and investing assets** | **175,935** | **170,865** |

No interest or profit income is recognised on impaired loans and advances or on impaired Islamic financing and investing assets.

## 23 Net fee and commission income

| | 2018<br>AED'000 | 2017<br>AED'000 |
|---|---|---|
| **Fee and commission income from** | | |
| Credit cards related fees | 29,828 | 30,222 |
| Corporate finance fees | 16,902 | 15,576 |
| Letters of credit and letters of guarantees | 12,199 | 12,399 |
| Other commission income | 9,224 | 10,736 |
| | **68,153** | **68,933** |
| **Fee expense on** | | |
| Credit cards related expenses | (18,432) | (15,829) |
| Others | (2,973) | (5,624) |
| **Net fee and commission income** | **46,748** | **47,480** |

## 24 Net insurance income

| | 2018<br>AED'000 | 2017<br>AED'000 |
|---|---|---|
| **Net insurance premiums earned** | | |
| Gross premiums written | 203,907 | 211,088 |
| Release/(charge) in unearned premium provision | 14,646 | (16,203) |
| Premium income earned | **218,553** | **194,885** |
| Re-insurance premiums ceded | (58,259) | (52,954) |
| Change in re-insurance portion of unearned premium provision | - | 7,568 |
| Re-insurance premium ceded | **(58,259)** | **(45,386)** |
| | **160,294** | **149,499** |
| **Net insurance claims incurred** | | |
| Claims paid | (134,365) | (112,669) |
| Outstanding claims expenses | (6,639) | (13,267) |
| Movements in reserves | (4,249) | (29,674) |
| Claims recovered from re-insurers | 41,914 | 35,608 |
| | **(103,339)** | **(120,002)** |
| **Net insurance commission** | | |
| Insurance commission income | 7,860 | 7,760 |
| Insurance commission expense | (26,042) | (24,576) |
| | (18,182) | (16,816) |
| **Net insurance income** | **38,773** | **12,681** |

## 25 Net income from investments

| | For the year ended 31 December | |
|---|---|---|
| | 2018 | 2017 |
| | AED'000 | AED'000 |
| Investments carried at fair value through profit or loss | | |
| Gain/(loss) on disposal | 3,531 | (5,925) |
| Change in fair value | (31,498) | (22,735) |
| Dividend income | 8,113 | 11,948 |
| Net loss | **(19,854)** | **(16,712)** |
| Investments carried at fair value through other comprehensive income | | |
| Dividend income | 19,447 | 15,553 |
| **Net loss from investments** | **(407)** | **(1,159)** |

## 26 Basic and diluted earnings per share

Earnings per share is calculated by dividing the profit for the year by the weighted average number of shares outstanding during the year. Diluted earnings per share is determined by adjusting the profit and the weighted average number of shares outstanding, adjusted for the effects of all dilutive potential ordinary shares. As of 31 December 2018, the Company has not issued any instruments which would have a dilutive impact on earnings per share when converted or exercised.

The calculation of basic and diluted earnings per share is based on the following data:

| | 2018 | 2017 |
|---|---|---|
| | AED'000 | AED'000 |
| Profit for the year attributable to equity holders of the parent (AED '000) | 11,825 | 34,330 |
| Less: Tier 1 Sukuk paid | (22,500) | (22,500) |
| Less: Proposed directors remuneration | (1,064) | (3,090) |
| | **(11,739)** | **8,740** |
| Number of ordinary shares in issue ('000) | 310,050 | 310,050 |
| Less: Treasury shares ('000) | (9,400) | (9,400) |
| Less: Employees' share-based payment scheme ('000) | (1,750) | (1,750) |
| | **298,900** | **298,900** |
| **Earnings per share (AED)** | **(0.04)** | **0.03** |

## 27 Related party balances and transactions

In the ordinary course of business, the Group enters into transactions with associates, major shareholders, directors, senior management and their related concerns at commercial interest and commission rates.

The year-end balances in respect of related parties included in the statement of financial position are as follows:

| | 2018<br>AED'000 | 2017<br>AED'000 |
|---|---|---|
| **Loans and advances** | | |
| To key management staff | 973 | 775 |
| To members of Board of Directors | 38,103 | 9,277 |
| To others | | - |
| **Customers' deposits** | | |
| From others | 11,527 | 11,084 |

Significant transactions with related parties during the year were as follows:

| | For the year ended 31 December | |
|---|---|---|
| | 2018<br>AED'000 | 2017<br>AED'000 |
| **Interest income** | | |
| From key management | 32 | 16 |
| From Board of Directors | 1,605 | 312 |
| **Interest expense** | | |
| To others | 161 | 80 |
| **Key management remuneration** | | |
| Short term benefits (salaries, benefits and bonuses) | 19,418 | 21,941 |

Balances with related parties include loans granted to Directors and their related parties in the normal course of business amounting to AED 38,103 thousand as at 31 December 2018 (2017: AED 9,277 thousand). These loans carry fixed interest rates of 6.0% p.a to 6.5% p.a (2017: fixed interest rates of 6.5% p.a).

## 28 Investment properties

| | 2018 AED'000 | 2017 AED'000 |
|---|---|---|
| At 1 January | 82,070 | - |
| Acquisition of investment properties in respect of settlement of a loan | - | 5,070 |
| Reclassified from assets classified as held for sale | - | 83,000 |
| Change in fair value | (2,592) | (6,000) |
| | **79,478** | **82,070** |

Investment properties comprise: 3 apartments located in Dubai Business Bay with a fair market value of AED 4,478 thousand which were held as a collateral in respect of loan whereas the Group has acquired these apartments in respect of settlement of loan; and a commercial building in Al Nahyan area in Abu Dhabi with a fair market value of AED 75,000 thousand.

*Commercial Building Al Nahyan Abu Dhabi*

An independent valuer for the valuation of this investment property adopts the income method in valuing the investment properties. This method calculates the value of the property by taking the estimated net income of property and capitalising it with an appropriate yield, which reflects market sentiment and situation. To value the property, the independent valuer has used the current rental income and adjusted for outgoings such as void period and maintenance towards the property. The prime location, maintenance and occupancy levels are also considered.

| | Valuation technique | Significant unobservable input | Range |
|---|---|---|---|
| Investment property | Income method | Estimated annual market rent income | AED 7.6 – 8.7 million |
| | | Yield | 8.5% - 9.5% |
| | | Occupancy level | 95% - 100% |

The rental income recognised is AED 6,554 thousand (2017: 6,344 thousand) and is recognised in the consolidated income statement under 'other operating income'.

## 29 Salaries and employees related expenses

| | 2018 AED'000 | 2017 AED'000 |
|---|---|---|
| Basic salaries | 39,812 | 40,637 |
| Cost of living allowance | 29,040 | 30,807 |
| Employees outsourced | 20,102 | 34,702 |
| Housing allowance | 15,453 | 16,521 |
| Gratuity | 2,830 | 2,790 |
| Others | 37,764 | 34,413 |
| | **145,001** | **159,870** |

## 30 Segmental information

For management purposes, the Group is organised into six major business segments:

(i) Commercial and retail financing, which principally provides loans and other credit facilities for institutional and individual customers.

(ii) Investment, which involves the management of the Group's investment portfolio and its treasury activities.

(iii) Islamic financing and investing, which involves one of the Group's subsidiaries principally providing investment, consumer and commercial financing and other related services based on Islamic Sharia's rules and principles.

(iv) Insurance, which involves one of the Group's subsidiaries providing non-life insurance services.

(v) Construction, which involves the Group's subsidiaries performing real estate construction related activities.

(vi) Brokerage, which involves one of the Group's subsidiaries providing brokerage services.

These segments are the basis on which the Group reports its primary segment information. Transactions between segments are conducted at rates determined by management taking into consideration the cost of funds.

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

## 30 Segmental information (continued)

### 30.1 Products and services from which reportable segments derive their revenues

Information regarding the Group's reportable segments is presented below:

| 31 December 2018 | Commercial and retail financing AED'000 | Investment AED'000 | Islamic financing and investing AED'000 | Brokerage AED'000 | Insurance AED'000 | Unallocated AED'000 | Total AED'000 |
|---|---|---|---|---|---|---|---|
| Interest income and income from Islamic financing and investing assets | 213,290 | 16,097 | 21,163 | 9,597 | 1,396 | - | **261,543** |
| Interest expense and profit distributable to depositors | (66,638) | (13,633) | (1,994) | (3,343) | - | - | **(85,608)** |
| Net income from perpetual instruments | - | 19,017 | - | - | - | - | **19,017** |
| Net fee and commission income | 40,856 | - | 3,676 | 2,216 | - | - | **46,748** |
| Net insurance income | - | - | - | - | 38,773 | - | **38,773** |
| Net investment income | - | (407) | - | - | - | - | **(407)** |
| Share of results of an associate | - | (1,235) | - | - | - | - | **(1,235)** |
| Other operating income | 20,064 | (1,968) | - | 494 | 3,037 | - | **21,627** |
| **Total operating income** | **207,572** | **17,871** | **22,845** | **8,964** | **43,206** | - | **300,458** |
| Depreciation of property, fixtures and equipment | - | (124) | (752) | (516) | (1,161) | (6,148) | **(8,701)** |
| Other expenses and charges | (62,758) | (9,926) | (11,500) | (7,859) | (38,308) | (63,405) | **(193,756)** |
| **Total expenses and other charges** | **(62,758)** | **(10,050)** | **(12,252)** | **(8,375)** | **(39,469)** | **(69,553)** | **(202,457)** |
| **Profit for the year before impairment** | **144,814** | **7,821** | **10,593** | **589** | **3,737** | **(69,553)** | **98,001** |
| Net impairment charges on loans and advances | (75,848) | - | - | - | - | - | **(75,848)** |
| Net impairment charges on Islamic financing and investing assets | - | - | **(4,313)** | - | - | - | **(4,313)** |
| **Net profit for the year** | **68,966** | **7,821** | **6,280** | **589** | **3,737** | **(69,553)** | **17,840** |
| Segmental assets | 2,317,670 | 1,114,750 | 182,763 | 175,117 | 304,468 | - | **4,094,768** |
| Segmental liabilities | 2,288,655 | 640,593 | 98,791 | 93,916 | 204,640 | - | **3,326,595** |
| Additions to non-current assets during the year | - | 80 | 62 | 14 | 1,233 | 17,954 | **19,343** |

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

## 30 Segmental information (continued)

### 30.1 Products and services from which reportable segments derive their revenues (continued)

| 31 December 2017 | Commercial and retail financing AED'000 | Investment AED'000 | Islamic financing and investing AED'000 | Brokerage AED'000 | Insurance AED'000 | Unallocated AED'000 | Total AED'000 |
|---|---|---|---|---|---|---|---|
| Interest income and income from Islamic financing and investing assets | 202,122 | 6,467 | 21,515 | 12,043 | 2,752 | - | **244,899** |
| Interest expense and profit distributable to depositors | (55,723) | (10,392) | (2,839) | (5,080) | - | - | **(74,034)** |
| Net income from perpetual instruments | - | 25,773 | - | - | - | - | **25,773** |
| Net fee and commission income | 38,123 | - | 3,633 | 5,724 | - | - | **47,480** |
| Net insurance income | - | - | - | - | 12,681 | - | **12,681** |
| Loss on fair valuation of investment property | - | (6,000) | - | - | - | - | **(6,000)** |
| Gain in disposal of subsidiary | - | 15,001 | - | - | - | - | **15,001** |
| Reversal of impairment charges on loans and advance | 5,300 | - | - | - | - | - | **5,300** |
| Net investment income | - | (1,159) | - | - | - | - | **(1,159)** |
| Share of results of an associate | - | 1,243 | - | - | - | - | **1,243** |
| Other operating income | 8,065 | 23,125 | - | - | 2,493 | - | **33,683** |
| **Total operating income** | **197,887** | **38,427** | **22,309** | **12,687** | **17,926** | **-** | **289,236** |
| Depreciation of property, fixtures and equipment | - | (178) | (776) | (571) | (950) | (4,695) | **(7,170)** |
| Other expenses and charges | (75,784) | (10,364) | (14,930) | (8,181) | (30,668) | (63,897) | **(203,824)** |
| **Total expenses and other charges** | (75,784) | (10,542) | (15,706) | (8,752) | (31,618) | (68,592) | **(210,994)** |
| **Profit for the year before impairment** | **122,103** | **43,516** | **6,603** | **3,935** | **(13,692)** | **(68,592)** | **93,873** |
| Net impairment charges on loans and advances | (48,736) | - | - | - | - | - | **(48,736)** |
| Net impairment charges on Islamic financing and investing assets | - | - | (12,523) | - | - | - | **(12,523)** |
| **Net profit/(loss) for the year** | **73,367** | **43,516** | **(5,920)** | **3,935** | **(13,692)** | **(68,592)** | **32,614** |
| Segmental assets | 2,266,402 | 1,612,188 | 227,028 | 205,221 | 254,000 | - | **4,564,839** |
| Segmental liabilities | 2,225,109 | 1,005,166 | 144,252 | 124,608 | 162,505 | - | **3,661,640** |
| Additions to non-current assets during the year | - | 2 | 18 | 45 | 1,299 | 5,227 | **6,591** |

## 30 Segmental information (continued)

### 30.1 Products and services from which reportable segments derive their revenues (continued)

Revenue reported above represents revenue generated from external customers. The inter-segment revenues and expenses have been eliminated in full.

For the purposes of monitoring segment performance and allocating resources between segments:

- all assets are allocated to reportable segments. Assets used jointly by reportable segments are allocated on the basis of the revenues earned by individual reportable segments; and
- all liabilities are allocated to reportable segments. Liabilities for which reportable segments are jointly liable are allocated in proportion to segment assets.

### 30.2 Geographical information

The Group primarily operates in the U.A.E. (country of domicile).

### 30.3 Information about major customers

There is no single customer accounting for more than 10% of the Group's revenues from external customers.

## 31 Risk management

### 31.1 Introduction

Risk is inherent in the Group's activities but it 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 or her responsibilities. The Group is exposed to credit risk, liquidity risk and market risk, the latter being subdivided into trading and non-trading risks. It is also subject to operational risks.

*(a) Risk management structure*

In line with the best practice followed in world class financial institutions the overall risk management responsibility lies with the Board of Directors of the Group, under which there is a Board Investment and Credit Committee (BICC) comprising of six board members and the Group Chief Risk Officer who take responsibility for identifying and controlling the risks.

(i) Board of Directors

The overall risk management responsibility lies with the Board of Directors of the Group. It provides the direction, strategy and oversight of all the activities through various committees.

## 31 Risk management (continued)

### 31.1 Introduction (continued)

*(a) Risk management structure* (continued)

(ii) Audit Committee

The Audit Committee comprises three members who are also part of the Board of Directors of the Group. The Audit Committee has the overall responsibility of assessing the internal audit findings, directing implementation of audit recommendations and overseeing the internal audit activities undertaken within the internal control environment and regulatory compliance framework of the Group. Duties and responsibilities of the Audit Committee are governed by a formally approved Audit Committee Charter which is in line with best practice and control governance.

(iii) Asset Liability Committee

The asset liability management process is an act of planning, acquiring, and directing the flow of funds through an organization. The ultimate objective of this process is to generate adequate and stable earnings and to steadily build an organization's equity over time, while taking measured business risks. The Group has a well-defined asset liability management policy duly describing the objective, role and function of the Asset Liability Committee, which is the body within the Group that holds the responsibility to make strategic decisions to manage balance sheet related risks. The Asset Liability Committee, consisting of the Group's senior management, meets at least once a month.

(iv) Investment and Credit Committee (ICC)

All major business proposals of clients are approved through the ICC. The ICC is a sub-committee of the Board of Directors. The approval process and the authorities vested with the ICC members are well defined in a credit policy manual. The policy manual enumerates various procedures to be followed by relationship managers in bringing relationships to the Group. Various aspects of the credit approval process have been defined in the policy which enables efficient approval of the proposals.

(v) Risk Management Department (RMD)

The RMD is an independent unit reporting to the Group Chief Risk Officer. The RMD is responsible for identifying, measuring, monitoring and controlling the risks arising out of various activities in the Group by the different business units. The process is through partnering with the units in identifying and addressing the risks by setting limits and reporting on the utilization thereof.

The RMD also monitors compliance with the regulatory procedures and anti-money laundering monitoring procedures of the Group.

## 31 Risk management (continued)

### 31.1 Introduction (continued)

*(a) Risk management structure* (continued)

(vi) Treasury

Group Treasury is responsible for managing the Group's assets and liabilities and the overall financial structure. It is also primarily responsible for managing the funding and liquidity risks of the Group.

(vii) Internal Audit

Risk management processes throughout the Group are audited annually by the internal audit function that examines both the adequacy of the procedures and the Group's compliance with the procedures. Internal Audit discusses the results of all assessments with management, and reports its findings and recommendations to the Audit Committee. The Head of Internal Audit has direct reporting lines to the Audit Committee in order to secure independence and objectivity in all audit engagements undertaken within the Group.

*(b) Risk measurement and reporting systems*

Monitoring and controlling risks is primarily performed based on limits established by the Group. 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. In addition, the Group monitors and measures the overall risk bearing capacity in relation to the aggregate risk exposure across all risk types and activities.

Information compiled from all the businesses is examined and processed in order to analyse, control and identify early risks. This information is presented and explained to the RMD, and the head of each business division. The report includes aggregate credit exposure, limit exceptions and 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 credit losses on a quarterly basis. RMD receives a comprehensive risk report once a quarter, which is designed to provide all the necessary information to assess and conclude on the risks of the Group.

For all levels throughout the Group, specifically tailored risk reports are prepared and distributed in order to ensure that all business divisions have access to extensive, necessary and up-to-date information.

*(c) Risk mitigation*

As part of its overall risk management, the Group uses certain instruments to manage exposures resulting from changes in interest rates and foreign currencies. The Group actively uses collateral to reduce its credit risks.

## 31 Risk management (continued)

### 31.1 Introduction (continued)

*(d) Risk concentration*

Concentrations of credit risk arise when a number of counter parties 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 of credit risk indicate the relative sensitivity of the Group's performance to developments affecting a particular industry or geographic location.

The Group seeks to manage its credit risk exposure through diversification of lending activities to avoid undue concentrations of risks with individuals or groups of customers in specific industries or businesses.

Details of the composition of the loans, advances and Islamic financing and investing portfolio are provided in notes 5, 6 and 7. Information on credit risk relating to investments is provided in note 32.3.

### 31.2 Market risk

Market risk is the risk that the fair value and future cash flows of financial instruments will fluctuate due to changes in market variables such as interest rates, foreign exchange rates, and prices of equity and fixed income securities.

*(a) Interest rate risk*

Interest rate risk arises from the possibility that changes in interest rates will affect future cash flows or the fair values of financial instruments.

The Group is exposed to interest rate risk on its interest bearing assets and liabilities.

The following table demonstrates the sensitivity of the income statement to reasonably possible changes in interest rates, with all other variables held constant, of the Group's result for the year.

The sensitivity of the income statement is the effect of the assumed changes in interest rates on the Group's profit for one year, based on the floating rate financial assets and financial liabilities held at 31 December 2018.

| | **Effect on profit and equity**<br>AED'000 |
|---|---|
| **2018** | |
| +100 increase in basis points | **17,021** |
| -100 decrease in basis points | **(14,868)** |
| **2017** | |
| +100 increase in basis points | 10,100 |
| -100 decrease in basis points | (10,100) |

## 31 Risk management (continued)

### 31.2 Market risk (continued)

*(b) Currency risk*

Currency risk is the risk that the value of a financial instrument will fluctuate due to changes in foreign exchange rates. The Board of Directors has set limits on positions by currency. Positions are monitored on a daily basis and it is ensured these are maintained within established limits.

Foreign currency risk is limited since a significant proportion of the Group's transactions, monetary assets and liabilities are denominated in U.A.E. Dirham and U.S. Dollar. As the U.A.E. Dirham is pegged to the U.S. Dollar, balances in U.S. Dollar are not considered to represent significant currency risk. Exposure to other currencies is insignificant to the overall Group.

*(c) Price risk*

Price risk is the risk that the fair values of equities and fixed income securities decrease as the result of changes in the levels of equity and fixed income indices and the value of individual instruments. The price risk exposure arises from the Group's investment portfolio.

The following table estimates the sensitivity to a possible change in equity and fixed income markets on the Group's consolidated income statement. The sensitivity of the consolidated income statement is the effect of the assumed changes in the reference equity and fixed income benchmarks on the fair value of investments carried at fair value through profit or loss.

| | **Assumed level of change** | **Impact on net income and equity 2018 AED'000** | **Impact on net income and equity** 2017 AED'000 |
|---|---|---|---|
| **Investments carried at fair value through profit or loss** | | | |
| Abu Dhabi Securities Market Index | 2% | 1,333 | 1,791 |
| Dubai Financial Market Index | 2% | 1,868 | 1,706 |
| Fixed income securities | 2% | 26 | 30 |

## 31 Risk management (continued)

### 31.2 Market risk (continued)

*(c) Price risk* (continued)

The effect on equity (as a result of a change in the fair value of equity instruments carried at fair value through other comprehensive income) due to a reasonably possible change in equity indices, with all other variables held constant, is as follows.

| | **Assumed level of change** | **Impact on equity 2018 AED'000** | **Impact on equity 2017 AED'000** |
|---|---|---|---|
| **Investments carried at fair value through other comprehensive income** | | | |
| Abu Dhabi Securities Market Index | 2% | 3,677 | 3,519 |
| Dubai Financial Market Index | 2% | 872 | 803 |
| Kuwait Stock Exchange | 2% | - | 371 |
| Unquoted investments | 2% | 1,555 | 1,858 |

The effect of decreases in prices of equity and fixed income securities is expected to be equal and opposite to the effect of the increases shown above.

### 31.3 Credit risk

Credit risk is the risk of suffering financial loss, should any of the Group's customers, clients or market counterparties fail to fulfil their contractual obligations to the Group. Credit risk arises mainly from commercial and consumer loans and advances, and loan commitments arising from such lending activities, but can also arise from financial guarantees, letters of credit, endorsements and acceptances.

The Group is also exposed to other credit risks arising from investments in debt securities and other exposures arising from its trading activities ('trading exposures').

Credit risk is the single largest risk for the Group's business; management therefore carefully manages its exposure to credit risk. The credit risk management and control are centralised in a credit risk management team, which reports regularly to the Board of Directors and head of each business unit.

#### (a) Loans and advances (including loan commitments, LCs and LGs)

The estimation of credit exposure for risk management purposes is complex and requires the use of models, as the exposure varies with changes in market conditions, expected cash flows and the passage of time. The assessment of credit risk of a portfolio of assets entails further estimations as to the likelihood of defaults occurring, of the associated loss ratios and of default correlations between counterparties. The Group measures credit risk using the concept of Expected Loss which, requires the following parameters: Probability of Default (PD%), Loss Given Default (LGD%) and Exposure at Default (EAD Amount).

## 31 Risk management (continued)

### 31.3 Credit risk (continued)

#### 31.3.1 Credit risk measurement

**(a) Loans and advances (including loan commitments, LCs and LGs)** (continued)

Under IFRS 9 provision computation method incurred loss approach is replaced by expected Credit Loss (ECL) approach, which is based on macro-economic scenario adjusted forward looking PD%, LGD% and EAD measures. Additionally, it also captures deterioration of risk profile and lifetime likelihood of defaults.

**(b) Credit risk grading**

The Group uses internal credit risk grading that reflect its assessment of the probability of default of individual counterparties. The Group use specific internal risk rating models tailored to the various categories of industry/segments of counterparty. Borrower and loan specific information collected at the time of application (such as financial spread, management quality, Risk Bureau information, and account conduct, turnover and industry type for wholesale exposures) which is fed into this rating model. This is supplemented with external data input such as credit bureau scoring on individual borrowers into the model. In addition, the models enable expert judgement from the Credit Risk Officer to be fed into the final internal credit rating for each exposure. This allows for considerations, which may not be captured as part of the other data inputs into the model.

The credit grades are calibrated such that risk of default increases exponentially at each higher risk grade. For example, this means that the difference in the PD between a 6 and 8 rating grade is lower than the difference in the PD between a 18 and 20 rating grade.

The Risk Rating system for performing assets ranges from Obligor Risk Rating ("ORR") ORR 1 to ORR 7, each grade being associated with a Probability of Default ("PD"). Non-performing clients are rated ORR 8 to ORR 10, corresponding to substandard, doubtful and loss classifications.

These risk ratings have been mapped into 5 Grades which are defined below:

| Grade | Risk Rating | Definition |
|---|---|---|
| Grade 1 | 1-13 | Investment grade |
| Grade 2 | 14-15 | Substandard grade |
| Grade 3 | 16-17 | Speculative grade |
| Grade 4 | 18-19 | Very high speculative grade |
| Grade 5 | 20-22 | Non-investment grade |

*Retail*

After the date of initial recognition, for retail business, the payment behaviour of the borrower is monitored on a periodic basis to develop a behavioural score. Any other known information about the borrower which impacts their creditworthiness – such as unemployment and previous delinquency history – is also incorporated into the behavioural score. This score is mapped to a PD.

## 31 Risk management (continued)

### 31.3 Credit risk (continued)

### 31.3.1 Credit risk measurement (continued)

### (b) Credit risk grading (continued)

*Retail* (continued)

Retail risk parameters i.e. PD, LGD & CCF or EAD have been estimated using 'Segmentation Methodology' or 'Retail Pooling'; where following factors have been considered:

- Asset classification as Credit Card, Executive Finance (or Personal Loan) and SME (or small business loan);
- Days Past Due – 2 segment each for Stage 1 & Stage 2; and 1 for Stage 3

Risk parameters have been estimated with respect to above segments and used the same for ECL computation.

*Wholesale*

For wholesale business, the rating is determined at the borrower level. A relationship manager will incorporate any updated or new information/credit assessments into the credit system on an ongoing basis. In addition, the relationship manager will also update information about the creditworthiness of the borrower every year from sources such as financial statements. This will determine the updated internal credit rating and the mapped PD. The Group's Internal Risk Rating Scale and mapping of external ratings are set out below:

| Grade | Score Range | ORR | PD% | FH ORR Description | Moody's | S&P | Fitch |
|---|---|---|---|---|---|---|---|
| 1 | SCORE >= X22 | ORR 1 | 0.005% | Invest. Grade (Very High) / Almost Credit Risk Free | Aaa | AAA | AAA |
| 2 | X20 <= SCORE < X21 | ORR 2+ | 0.010% | Invest. Grade (Very High) / Very Low Credit Risk | Aa1 | AA+ | AA+ |
| 3 | X19 <= SCORE < X20 | ORR 2 | 0.020% | Invest. Grade (Very High) / Very Low Credit Risk | Aa2 | AA | AA |
| 4 | X18 <= SCORE < X19 | ORR 2- | 0.050% | Invest. Grade (Very High) / Very Low Credit Risk | Aa3 | AA- | AA- |
| 5 | X17 <= SCORE < X18 | ORR 3+ | 0.10% | Invest. Grade (High) / Very Low Credit Risk | A1 | A+ | A+ |
| 6 | X16 <= SCORE < X17 | ORR 3 | 0.20% | Invest. Grade (High) / Low Credit Risk | A2 | A | A |
| 7 | X15 <= SCORE < X16 | ORR 3- | 0.40% | Invest. Grade (High) / Low Credit Risk | A3 | A- | A- |
| 8 | X14 <= SCORE < X15 | ORR 4+ | 0.75% | Invest. Grade (Good) / Low Credit Risk | Baa1 | BBB+ | BBB+ |
| 9 | X13 <= SCORE < X14 | ORR 4 | 1.25% | Invest. Grade (Good) / Moderate Credit Risk | Baa2 | BBB | BBB |
| 10 | X12 <= SCORE < X13 | ORR 4- | 2.00% | Invest. Grade (Good) / Moderate Credit Risk | Baa3 | BBB- | BBB- |
| 11 | X11 <= SCORE < X12 | ORR 5+ | 2.75% | Invest. Grade (Acceptable) / Moderate Credit Risk | Ba1 | BB+ | BB+ |
| 12 | X10 <= SCORE < X11 | ORR 5 | 3.50% | Invest. Grade (Acceptable) / Substantial Credit Risk | Ba2 | BB | BB |
| 13 | X9 <= SCORE < X10 | ORR 5- | 4.50% | Invest. Grade (Acceptable) / Substantial Credit Risk | Ba3 | BB- | BB- |
| 14 | X8 <= SCORE < X9 | ORR 6+ | 6.00% | Sub-Invest. Grade / High Credit Risk | B1 | B+ | B+ |
| 15 | X7 <= SCORE < X8 | ORR 6 | 8.00% | Sub-Invest. Grade / High Credit Risk | B2 | B | B |
| 16 | X6 <= SCORE < X7 | ORR 6- | 12.00% | Speculative Grade / High Credit Risk | B3 | B- | B- |
| 17 | X5 <= SCORE < X6 | ORR 7+ | 18.00% | Speculative Grade / Very High Credit Risk / Borderline Credit Quality | Caa1 | CCC+ | |
| 18 | X4 <= SCORE < X5 | ORR 7 | 27.50% | Very High Speculative Grade / Very High Credit Risk | Caa2 | CCC | CCC |
| 19 | X3 <= SCORE < X4 | ORR 7- | 40.00% | Very High Speculative Grade / Very High Credit Risk / Watch List (O.L.E.M.) | Caa3 | CCC- | |
| 20 | X2 <= SCORE < X3 | ORR 8 | 75.00% | Non Investment / Sub Standard (Partial Loss) | Ca | CC | CC |
| 21 | X1 <= SCORE < X2 | ORR 9 | 100.00% | Non Investment / Doubtful (Substantial Loss) | C | C | C |
| 22 | SCORE < X1 | ORR 10 | 100.00% | Non Investment / Loss | | SD/D | SD/D |

## 31 Risk management (continued)

### 31.3 Credit risk (continued)

### 31.3.1 Credit risk measurement (continued)

### (b) Credit risk grading (continued)

*Treasury*

For debt securities in the Treasury portfolio, external rating agency credit grades are used. These published grades are continuously monitored and updated. The PD's associated with each grade are determined based on realised default rates over the prior 12 months, as published by the rating agency.

### 31.3.2 Expected credit loss measurement

IFRS 9 outlines a *'three-stage'* model for impairment based on changes in credit quality since initial recognition of a facility as summarised below:

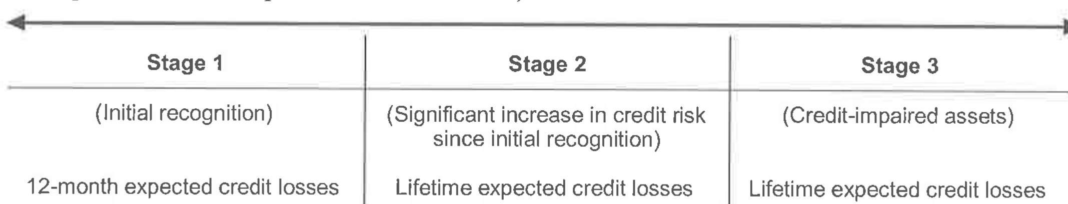
- A financial instrument that is not credit-impaired on initial recognition is classified in 'Stage 1' and has its credit risk continuously monitored by the Group.
- If a significant increase in credit risk ('SICR') since initial recognition is identified, the financial instrument is moved to 'Stage 2' but is not yet deemed to be credit-impaired. The identification of SICR is measured via Quantitative (Objective criteria) and Qualitative (Subjective criteria) and hence a change in one-year probability of default between the date of inception of facility and the date of IFRS 9 ECL run.
- If the financial instrument is credit-impaired, the financial instrument is then moved to 'Stage 3'. Refer to *Note 2.4 (f) and Refer to 31.3.2 (c)* for a description of how the Group defines credit-impaired and default.
- Financial assets in Stage 1 have their ECL measured at an amount equal to the portion of lifetime expected credit losses that result from default events possible within the next 12 months. Instruments in Stages 2 or 3 have their ECL measured based on expected credit losses on a lifetime basis. *Refer to 31.3.2 (c)* for a description of inputs, assumptions and estimation techniques used in measuring the ECL.
- A pervasive concept in measuring the ECL in accordance with IFRS 9 is that it should consider forward-looking information. *Refer to 31.3.2 (c)* includes an explanation of how the Group has incorporated this in its ECL models.
- Purchased or originated credit impaired financial assets are those financial assets that are credit impaired on initial recognition. Their ECL is always measured on a lifetime basis (Stage 3). However, Group does not have any such exposure in the book.

## 31 Risk management (continued)

### 31.3 Credit risk (continued)

#### 31.3.2 Expected credit loss measurement (continued)

The following diagram summarises the impairment requirements under IFRS 9 (other than purchased or originated credit-impaired financial assets):



| Stage 1 | Stage 2 | Stage 3 |
|---|---|---|
| (Initial recognition) | (Significant increase in credit risk since initial recognition) | (Credit-impaired assets) |
| 12-month expected credit losses | Lifetime expected credit losses | Lifetime expected credit losses |

**(a) Significant increase in credit risk (SICR)**

The Group considers a financial asset to have experienced a significant increase in credit risk when a significant change in one-year probability of default occurs between the origination date of a specific facility and the IFRS 9 ECL run date.

*Quantitative criteria*

*Corporate loans*

For corporate loans, if the borrower experiences a significant increase in probability of default, which can be triggered by the following quantitative factors:

- Operating performance
- Operating efficiency
- Liquidity assessment
- Capital structure
- Actual or expected forbearance or restructuring
- Accounts overdue between 30 and 90 days, however this criteria maybe rebutted with supporting evidence.

*Retail*

For Retail portfolio, if the borrowers meet one or more of the following criteria:

- Adverse findings for an account/ borrower as per credit bureau data;
- Loan rescheduling before 30 Days Past Due (DPD); and
- Accounts overdue between 30 and 90 days.

*Treasury*

- Significant increase in probability of default of the underlying treasury instrument;
- Significant change in the investments expected performance.

## 31 Risk management (continued)

### 31.3 Credit risk (continued)

#### 31.3.2 Expected credit loss measurement (continued)

#### (a) Significant increase in credit risk (SICR) (continued)

*Qualitative criteria:*

For Retail portfolios, if the borrower meets one or more of the following criteria:

- In short-term forbearance
- Direct debit cancellation
- Extension to the terms granted
- Previous arrears within the last 12 months

For Corporate loans and Treasury portfolios, if the borrower is on the Watch list and/or the instrument meets one or more of the following criteria:

- Significant increase in credit spread
- Significant adverse changes in business, financial and/or economic conditions in which the borrower operates
- Actual or expected forbearance or restructuring
- Actual or expected significant adverse change in operating results of the borrower
- Significant change in collateral value (secured facilities only) which is expected to increase risk of default
- Early signs of cash flow/liquidity problems such as delay in servicing of trade creditors/loans

The assessment of SICR incorporates forward-looking information and is performed on a quarterly basis at a portfolio level for all Retail financial instruments held by the Group. In relation to Wholesale and Treasury financial instruments, where a watch list is used to monitor credit risk, this assessment is performed at the counterparty level and on a periodic basis. The criteria used to identify SICR are monitored and reviewed periodically for appropriateness by the independent Credit Risk team.

*Backstop*

A backstop is applied and the financial instrument considered to have experienced a significant increase in credit risk if the borrower is more than 30 days past due on its contractual payments.

The Group has not used the low credit risk exemption for any financial instruments in the year ended 31 December 2018.

## 31 Risk management (continued)

### 31.3 Credit risk (continued)

### 31.3.2 Expected credit loss measurement (continued)

#### (b) Definition of default and credit-impaired assets

The Group defines a financial corporate, retail and investment instrument as in default, which is fully aligned with the definition of credit-impaired, when it meets one or more of the following criteria:

Quantitative criteria

The borrower is more than 90 days past due on its contractual payments.

Qualitative criteria:

The borrower meets unlikeliness to pay criteria, which indicates the borrower is in significant financial difficulty. These are instances where:

- The Group considers that the obligor is unlikely to pay its credit obligation to the Group in full without recourse by the Group to actions like realising security (if held).
- The borrower is in long-term forbearance
- The borrower is deceased
- The borrower is insolvent
- The borrower is in breach of financial covenants
- An active market for that financial asset has disappeared because of financial difficulties
- Concessions have been made by the lender relating to the borrower's financial difficulty
- It is becoming probable that the borrower will enter bankruptcy
- The obligor is past due more than 90 days on any material credit obligation to the Group.

The criteria above have been applied to all financial instruments held by the Group and are consistent with the definition of default used for internal credit risk management purposes. The default definition has been applied consistently to model the Probability of Default (PD), Exposure at Default (EAD), and Loss Given Default (LGD) throughout the Group's expected loss calculations.

An instrument is considered to no longer be in default (i.e. to have cured) when it no longer meets any of the default criteria for a consecutive period of six months. This period of six months has been determined based on an analysis, which considers the likelihood of a financial instrument returning to default status after cure using different cure definitions.

## 31 Risk management (continued)

### 31.3 Credit risk (continued)

### 31.3.2 Expected credit loss measurement (continued)

#### (c) Measuring ECL – Explanation of inputs, assumptions and estimation techniques

The Expected Credit Loss (ECL) is measured on either a 12-month (12M) or lifetime basis depending on whether a significant increase in credit risk has occurred since the initial recognition of a specific facility or whether an asset is considered credit-impaired. Expected credit losses are the discounted product of the Probability of Default (PD), Exposure at Default (EAD), and Loss Given Default (LGD), defined as follows:

- Probability of Default (PD) represents the likelihood of a borrower defaulting on its financial obligation (as per 'Definition of default and credit-impaired' above), either over the next 12 months (12M PD), or over the remaining lifetime (Lifetime PD) of the obligation.
- Exposure at Default (EAD) is based on the amounts the Group expected to be owed at the time of default, over the next 12 months (12M EAD) or over the remaining lifetime (Lifetime EAD). For example, for a revolving commitment, the Group includes the current drawn balance plus any further amount that is expected to be drawn up to the current contractual limit by the time of default, should it occur.
- Loss Given Default (LGD) represents the Group's expectation of the extent of loss on a defaulted exposure. LGD varies by type of counterparty, type and seniority of claim and availability of collateral or other credit support. LGD is expressed as a percentage loss per unit of exposure at the time of default (EAD). LGD is calculated on a 12-month or lifetime basis, where 12-month LGD is the percentage of loss expected to be made if the default occurs in the next 12 months and lifetime LGD is the percentage of loss expected to be made if the default occurs over the remaining expected lifetime of the loan.

The ECL is determined by projecting the PD, LGD and EAD for each future month and for each individual exposure or collective segment. These three components are multiplied together and adjusted for the likelihood of survival (i.e. the exposure has not prepaid or defaulted in an earlier month). This effectively calculates an ECL for each future month, which is then discounted back to the reporting date and summed. The discount rate used in the ECL calculation is the effective interest rate or an approximation thereof.

The Lifetime PD is developed by applying a maturity profile to the current 12M PD. The maturity profile looks at how defaults develop on a portfolio from the point of initial recognition throughout the lifetime of the loans. The maturity profile is based on historical observed data and is assumed to be the same across all assets within a portfolio and credit grade band. This is supported by historical analysis.

## 31 Risk management (continued)

### 31.3 Credit risk (continued)

#### 31.3.2 Expected credit loss measurement (continued)

**(c) Measuring ECL – Explanation of inputs, assumptions and estimation techniques** (continued)

The 12-month and lifetime EADs are determined based on the expected payment profile, which varies by product type.

- For amortising products and bullet repayments loans, this is based on the contractual repayments owed by the borrower over a 12-month period or lifetime basis. This will also be adjusted for any expected overpayments made by a borrower. Early repayment/refinance assumptions are also incorporated into the calculation.
- For revolving products, the exposure at default is predicted by taking current drawn balance and adding a "credit conversion factor" which allows for the expected drawdown of the remaining committed limit by the time of default. These assumptions vary by product type and current limit utilisation band, based on analysis of the Group's recent default data.

The 12-month and lifetime LGDs are determined based on the factors, which impact the recoveries made post default. These vary by product type.

- For secured products, this is primarily based on collateral type and projected collateral values, historical discounts to market/book values due to forced sales, time to repossession and recovery costs observed.
- For unsecured products, LGDs are typically set at product level due to the limited differentiation in recoveries achieved across different borrowers. These LGDs are influenced by recovery/collection strategies, including contracted debt sales and prices.

Forward-looking economic information is also included in determining the 12-month and lifetime PD, EAD and LGD. These assumptions vary by product type. Refer to *note 31.2.2 (d)* for an explanation of forward- looking information and its inclusion in ECL calculations.

The assumptions underlying the ECL calculation – such as how the maturity profile of the PDs and how collateral values change etc. – are monitored and reviewed on a quarterly basis.

There have been no significant changes in estimation techniques or significant assumptions made during the year.

## 31 Risk management (continued)

### 31.3 Credit risk (continued)

#### 31.3.2 Expected credit loss measurement (continued)

**(d) Forward looking information incorporated in the ECL models**

The assessment of SICR and the calculation of ECL both incorporate forward-looking information. The Group has performed historical analysis and identified the key economic variables impacting credit risk and expected credit losses for each portfolio. These economic variables and their associated impact on the PD, EAD and LGD vary by financial instrument. Expert judgement has also been applied in this process. Forecasts of these economic variables (the "base economic scenario") are computed on a quarterly basis and provide the best estimate view of the economy over the next ten years i.e. 'Macro Economy Scenario' for next ten years. The impact of these economic variables on the PD, EAD and LGD has been determined by performing statistical regression analysis to understand the impact changes in these variables have had historically on default rates and on the components of LGD and EAD.

**(e) Sensitivity analysis of forward looking factors**

The Group has calculated ECL for loans and advances on a segmented portfolio level, wholesale and retail.

*Wholesale*

The Group has used a scenario based analysis approach on macroeconomic status to arrive at a forward looking point-in-time PD, where management have assigned assumed probability weightage to the different scenarios on the state of economy. The Group has performed a sensitivity analysis on how ECL on the wholesale portfolio will change if the scenario probabilities used to calculate ECL change by a certain percentage. The impact on ECL due to a relative change in the assumed scenario by +10% / -10% in each of the base, upside and downside scenarios would result respectively in an ECL increase or decrease of AED 74 thousand. These changes are applied simultaneously to each probability-weighted scenario used to compute the expected credit losses. In reality, there will be interdependencies between the various economic inputs and the exposure to sensitivity will vary across the economic scenarios.

*Retail*

The most significant assumption affecting the ECL allowance in respect of the retail portfolio is Oil Price (% Change, Lag 0 months). The Group has performed a sensitivity analysis on how ECL on the retail portfolio will change if the key assumptions used to calculate ECL change by a certain percentage. The impact on ECL due to a relative change in the oil prices by +10% / -10% in each of the base, upside and downside scenarios would result respectively in an ECL increase or decrease of AED 2,712 thousand. These changes are applied simultaneously to each probability-weighted scenarios used to compute the expected credit losses. In reality, there will be interdependencies between the various economic inputs and the exposure to sensitivity will vary across the economic scenarios.

## 31 Risk management (continued)

### 31.4 Credit risk exposure

#### 31.4.1 Maximum exposure to credit risk – Financial instruments subject to impairment

The following table contains an analysis of the credit risk exposure of financial assets, which are subject to ECL. The gross carrying amount of financial assets below also represents the Group's maximum exposure to credit risk on these assets:

| | 2018 | | | |
|---|---|---|---|---|
| | ECL staging | | | |
| | Stage 1 12-month ECL AED'000 | Stage 2 Lifetime ECL AED'000 | Stage 3 Lifetime ECL AED'000 | Total AED'000 |
| ***Loans and advances*** | | | | |
| Grading 1 | 575,990 | 5,828 | - | **581,818** |
| Grading 2 | 483,649 | 17,646 | - | **501,295** |
| Grading 3 | 669,592 | 25,753 | - | **795,345** |
| Grading 4 | 160,568 | 138,813 | - | **299,381** |
| Grading 5 | - | - | 474,310 | **474,310** |
| | **1,889,799** | **288,040** | **474,310** | **2,652,149** |
| Loss allowance | (21,556) | (17,942) | (312,147) | **(351,645)** |
| Carrying amount | **1,868,242** | **270,098** | **162,163** | **2,300,504** |
| ***Islamic financing and investing assets*** | | | | |
| Grading 1 | 40,060 | | | **40,060** |
| Grading 2 | 37,077 | | | **37,077** |
| Grading 3 | 37,461 | 3,409 | | **40,870** |
| Grading 4 | 17,388 | 2,283 | 167 | **19,838** |
| Grading 5 | - | - | 64,510 | **64,510** |
| | **131,987** | **5,692** | **64,677** | **202,355** |
| Loss allowance | (1,975) | (1,164) | (56,603) | **(59,741)** |
| Carrying amount | **130,012** | **4,528** | **8,074** | **142,614** |
| ***Credit risk exposures relating to off-balance sheet items are as follows*** | | | | |
| Letters of credit | 169,522 | - | - | **169,522** |
| Guarantees | 1,301,264 | 10,533 | 58,483 | **1,370,280** |
| Loss allowance | (4,472) | (144) | (18,293) | **(22,909)** |
| Carrying amount | 1,466,314 | 10,389 | 40,190 | **1,516,893** |

## 31 Risk management (continued)

### 31.4 Credit risk exposure

#### 31.4.1 Maximum exposure to credit risk – Financial instruments not subject to impairment (continued)

| | 2018 | | | |
|---|---|---|---|---|
| | ECL staging | | | |
| | Stage 1 12-month ECL AED'000 | Stage 2 Lifetime ECL AED'000 | Stage 3 Lifetime ECL AED'000 | Total AED'000 |
| ***Credit risk exposures relating to on-balance sheet assets*** | | | | |
| Cash and balances with the UAE Central Bank | 29,344 | - | - | **29,344** |
| Due from banks at investment grade | 500,818 | - | - | **500,818** |
| Financial assets measured at amortised cost at investment grade | 1,837 | - | - | **1,837** |

***Credit quality per class of financial assets for the year ended 31 December 2017***

| | Neither past due nor impaired | | Past due or individually Impaired | |
|---|---|---|---|---|
| | **Pass grade** AED'000 | **Sub-standard grade** AED'000 | AED'000 | **Total** AED'000 |
| **2017** | | | | |
| Balances with U.A.E. Central Bank | 24,220 | - | - | 24,220 |
| Due from banks | 676,812 | - | - | 676,812 |
| Loans and advances | 2,102,554 | 54,218 | 179,029 | 2,335,801 |
| Islamic financing and investing assets | 168,493 | - | 4,877 | 173,370 |
| Investments carried at fair value through other comprehensive income | 376,269 | - | - | 376,269 |
| Investment carried at amortised cost | 81,654 | - | - | 81,654 |
| Statutory deposit | 6,000 | - | - | 6,000 |
| Other assets | 176,027 | - | - | 176,027 |
| **Total** | 3,612,029 | 54,218 | 183,906 | 3,850,153 |

An analysis of past due loans and Islamic financing and investing assets, by age, is provided below.

## 31 Risk management (continued)

### 31.4 Credit risk exposure

#### 31.4.1 Maximum exposure to credit risk – Financial instruments not subject to impairment (continued)

**Aging analysis of past due but not impaired and impaired loans and Islamic financing and investing assets**

| | Less than 30 days AED'000 | 31 to 60 Days AED'000 | 61 to 90 days AED'000 | More than 91 days AED'000 | Total AED'000 |
|---|---|---|---|---|---|
| **2017** | | | | | |
| Past due but not impaired | 31,365 | 12,896 | 19,149 | 16,378 | **79,788** |
| Impaired | - | - | - | 104,118 | **104,118** |
| Total past due or impaired | **31,365** | **12,896** | **19,149** | **120,496** | **183,906** |

#### 31.4.2 Collateral and other credit enhancements

The Group employs a range of policies and practices to mitigate credit risk. The most common of these is accepting collateral for funds advanced. The Group has internal policies on the acceptability of specific classes of collateral or credit risk mitigation. The Group prepares a valuation of the collateral obtained as part of the loan origination process. This assessment is reviewed periodically. Longer-term finance and lending to corporate entities are generally secured; revolving individual credit facilities are generally unsecured.

The Group's policies regarding obtaining collateral have not significantly changed during the reporting period and there has been no significant change in the overall quality of the collateral held by the Group since the prior period.

Collateral against loans and advances measured at amortised cost is generally held in the form of mortgage interests over property, other registered securities over assets and guarantees. Estimates of fair value are based on the value of the collateral assessed at the time of borrowing. Collateral generally is not held over amounts due from banks, except when securities are held as part of reverse repurchase and securities borrowing activity. Collateral usually is not held against financial assets.

The Group closely monitors collateral held for financial assets considered to be credit impaired, as it becomes more likely that the Group will take possession of the collateral to mitigate potential credit losses. Financial assets that are credit impaired and related collateral held in order to mitigate potential losses are shown below:

# 31 Risk management (continued)

## 31.4 Credit risk exposure (continued)

### 31.4.2 Collateral and other credit enhancements (continued)

The table below details the fair value of the collateral, which is updated regularly:

| | Loans and advances and Islamic financing and investment products | | Due from banks | |
|---|---|---|---|---|
| | 31 December | | 31 December | |
| | 2018 | 2017 | 2018 | 2017 |
| | AED'000 | AED'000 | AED'000 | AED'000 |
| **Against individually impaired loans and advances:** | | | | |
| Property | 53,488 | 28,302 | - | - |
| Equities | 1,872 | 9,855 | - | - |
| Cash | 5,319 | - | - | - |
| Others | 5,969 | 7,430 | - | - |
| **Total against Individually impaired** | **66,648** | **45,587** | | |
| **Against loans and advances not impaired:** | | | | |
| Property | 863,153 | 1,060,616 | - | - |
| Equities | 85,061 | 86,325 | - | - |
| Cash | 903,232 | 511,412 | - | - |
| Others | 130,678 | 106,776 | - | - |
| **Total against not impaired** | **1,982,124** | **1,765,129** | - | - |

## 31 Risk management (continued)

### 31.5 Loss allowance (continued)

The loss allowance recognised in the period is impacted by a variety of factors, as described below:

- Transfers between Stage 1 and Stages 2 or 3 due to financial instruments experiencing significant increases (or decreases) of credit risk or becoming credit-impaired in the period, and the consequent "step up" (or "step down") between 12-month and Lifetime ECL;
- Additional allowances for new financial instruments recognised during the period, as well as releases for financial instruments de-recognised in the period;
- Impact on the measurement of ECL due to changes in PDs, EADs and LGDs in the period, arising from regular refreshing of inputs to models;
- Impacts on the measurement of ECL due to changes made to models and assumptions;
- Discount unwind within ECL due to the passage of time, as ECL is measured on a present value basis; and
- Financial assets derecognised during the period and write-offs of allowances related to assets that were written off during the period

The following table explain the changes in the loss allowance between the beginning and the end of the annual period due to these factors:

| | 2018 | | | |
|---|---|---|---|---|
| | Stage 1 12-month ECL AED'000 | Stage 2 Lifetime ECL AED'000 | Stage 3 Lifetime ECL AED'000 | Total AED'000 |
| **Loans and advances** | | | | |
| Loss allowance as at 1 January | 32,791 | 18,092 | 225,578 | 276,461 |
| Transfers | | | | |
| Transfer from Stage 1 to Stage 2 | (2,872) | 2,872 | - | - |
| Transfer from Stage 1 to Stage 3 | - | - | - | - |
| Transfer from Stage 2 to Stage 1 | - | - | - | - |
| Transfer from Stage 2 to Stage 3 | - | (6,647) | 6,647 | - |
| Transfer from Stage 3 to Stage 1 | - | - | - | - |
| Transfer from Stage 3 to Stage 2 | - | - | - | - |
| New financial assets originated | 4,830 | 1,887 | - | 6,717 |
| Changes in PDs/LGDs/EADs | (13,195) | (1,739) | 80,586 | 69,131 |
| Write-offs | - | - | (664) | (664) |
| Loss allowance as at 31 December 2018 | **21,556** | **17,942** | **312,147** | **351,645** |

## 31 Risk management (continued)

### 31.5 Loss allowance (continued)

| | 2018 | | | |
|---|---|---|---|---|
| | Stage 1 12-month ECL AED'000 | Stage 2 Lifetime ECL AED'000 | Stage 3 Lifetime ECL AED'000 | Total AED'000 |
| **Islamic financing and investing assets** | | | | |
| Loss allowance as at 1 January | 5,129 | 2,674 | 47,625 | 55,428 |
| Transfers | | | | |
| Transfer from Stage 1 to Stage 2 | - | - | - | - |
| Transfer from Stage 1 to Stage 3 | (554) | - | 554 | - |
| Transfer from Stage 2 to Stage 1 | - | - | - | - |
| Transfer from Stage 2 to Stage 3 | - | - | - | - |
| Transfer from Stage 3 to Stage 1 | - | - | - | - |
| Transfer from Stage 3 to Stage 2 | - | - | - | - |
| New financial assets originated | - | - | - | - |
| Changes in PDs/LGDs/EADs | (2,600) | (1,511) | 8,424 | 4,313 |
| Write-offs | - | - | - | - |
| Loss allowance as at 31 December 2018 | **1,975** | **1,163** | **56,603** | **59,741** |

## Finance House P.J.S.C.

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

## 31 Risk management (continued)

### Gross carrying amount

The following table further explains the changes in the gross carrying amount from 1 January to 31 December 2018:

| | 2018 | | | |
|---|---|---|---|---|
| | Stage 1 | Stage 2 | Stage 3 | |
| | 12-month ECL AED'000 | Lifetime ECL AED'000 | Lifetime ECL AED'000 | Total AED'000 |
| ***Loans and advances*** | | | | |
| **Gross carrying amount as at 1 January 2018** | **2,084,866** | **129,275** | **336,243** | **2,550,385** |
| Transfers | | | | |
| Transfer from Stage 1 to Stage 2 | **(235,522)** | **235,522** | - | - |
| Transfer from Stage 1 to Stage 3 | - | - | - | - |
| Transfer from Stage 2 to Stage 3 | - | **(59,824)** | **59,824** | - |
| Transfer from Stage 3 to Stage 2 | - | - | - | - |
| Transfer from Stage 2 to Stage 1 | - | - | - | - |
| New financial assets originated | **317,239** | **52,948** | **77,566** | **447,753** |
| Repayments during the year | **(276,784)** | **(69,881)** | - | **(346,665)** |
| Other movements | - | - | - | - |
| Write-offs | - | - | **676** | **676** |
| **Gross carrying amount as at 31 December 2018** | **1,889,799** | **288,040** | **474,310** | **2,652,149** |
| ***Islamic financing and investing activities*** | | | | |
| **Gross carrying amount as at 1 January 2018** | **149,203** | **9,709** | **65,402** | **224,314** |
| Transfers | | | | |
| Transfer from Stage 1 to Stage 2 | - | - | - | - |
| Transfer from Stage 1 to Stage 3 | **(167)** | - | **167** | - |
| Transfer from Stage 2 to Stage 3 | - | **(489)** | **489** | - |
| Transfer from Stage 3 to Stage 2 | - | - | - | - |
| New financial assets originated | - | - | - | - |
| Repayments during the year | **5,507** | - | **402** | **5,909** |
| Write-offs | **(22,556)** | **(3,528)** | **(1,783)** | **(27,868)** |
| **Gross carrying amount as at 31 December 2018** | **131,987** | **5,692** | **64,677** | **202,355** |
| Cash and balances with the UAE Central Bank | **29,344** | - | - | **29,344** |
| Due from banks at investment grade | **500,818** | - | - | **500,818** |
| Financial assets measured at amortised cost at investment grade | **1,837** | - | - | **1,837** |
| | **531,999** | - | - | **531,999** |

## 31 Risk management (continued)

**Gross carrying amount** (continued)

| | 2018 | | | |
|---|---|---|---|---|
| | **Stage 1 12-month ECL AED'000** | **Stage 2 12-month ECL AED'000** | **Stage 3 12-month ECL AED'000** | **Total 12-month ECL AED'000** |
| ***Off-balance sheet items*** | | | | |
| **Gross carrying amount as at 1 January 2018** | **1,690,450** | **10,852** | **26,885** | **1,728,187** |
| Transfers | - | - | - | - |
| Transfer from Stage 1 to Stage 2 | **(8,044)** | **8,044** | - | - |
| Transfer from Stage 2 to Stage 3 | **(31,876)** | - | **31,876** | - |
| New financial assets originated | - | - | - | - |
| Repayments during the year | **(183,165)** | **(4,943)** | **(278)** | **(188,385)** |
| **Gross carrying amount as at 31 December 2018** | **1,467,365** | **13,954** | **58,483** | **1,539,802** |

### 31. 6 Write-off policy

The Group writes off financial assets, in a whole or in part, when it has exhausted all practical recovery efforts and has concluded there is no reasonable expectation of recovery. Indicators that there is no reasonable expectation of recovery include (i) ceasing enforcement activity and (ii) where the Group's recovery method is foreclosing on collateral and the value of the collateral is such that there is no reasonable expectation of recovering in full. The Group may write-off financial assets that are still subject to enforcement activity. The Group still seeks to recover amounts it is legally owned in full, but which have been partially or fully written off due to no reasonable expectation of recovery.

### 31.7 Modification of financial assets

The Group sometimes modifies the terms of loans provided to customers due to commercial renegotiations, or for distressed loans, with a view to maximising recovery. The risk of default of such assets after modification is assessed at the reporting date and compared with the risk under the original terms at initial recognition, when the modification is not substantial, it does not result in derecognition of the original asset. The Group may determine that credit risk has significantly improved after restructuring, and such assets are moved from Stage 3 to Stage 2 (Lifetime ECL) to Stage 1 (12 month ECL). This is only done when modified assets have performed in accordance with the new terms for twelve consecutive months or more. The gross carrying amounts of modified financial assets held at 31 December 2018 and 2017 was not material.

## 31 Risk management (continued)

### 31.8 Liquidity risk and funding management

Liquidity risk is the risk that an institution will be unable to meet its funding requirements. Liquidity risk can be caused by market disruptions or a credit downgrade, which may cause certain sources of funding to dry up immediately. To guard against this risk, management has diversified funding sources and assets are managed with liquidity in mind, maintaining a healthy balance of cash, cash equivalents, and readily marketable securities.

**Analysis of financial assets and financial liabilities by remaining contractual maturities**

The table below summarises the maturity profile of the Group's assets and liabilities at 31 December 2018 based on contractual maturities.

| | Less than 3 months AED'000 | 3 months to less than 1 year AED'000 | 1 year to 5 years AED'000 | Over 5 years AED'000 | Total AED'000 |
|---|---|---|---|---|---|
| **ASSETS** | | | | | |
| Cash and balances with U.A.E. Central Bank | 23,344 | - | 6,000 | - | 29,344 |
| Due from banks and financial institutions | 500,818 | - | - | - | 500,818 |
| Loans and advances | 489,335 | 800,660 | 959,003 | 51,506 | 2,300,504 |
| Islamic financing and investing assets | 91,407 | 24,935 | 26,010 | 262 | 142,614 |
| Investments and investment in associate | 269,775 | 136,106 | 153,396 | 215,007 | 774,284 |
| Other assets | 42,768 | 141,743 | 6,853 | - | 191,364 |
| Financial assets | 1,417,447 | 1,103,444 | 1,151,262 | 266,775 | 3,938,928 |
| Non-financial assets | 45,125 | - | 104,010 | 6,705 | 155,840 |
| **Total assets** | **1,457,572** | **1,108,444** | **1,255,272** | **273,480** | **4,094,768** |
| **LIABILITIES** | | | | | |
| Due to banks | 15,014 | - | - | - | 15,014 |
| Customers' deposits and margin accounts | 1,024,498 | 1,013,716 | 709,061 | - | 2,747,275 |
| Short term borrowings and medium term loans | 31,933 | 79,001 | 100,001 | - | 210,935 |
| Other liabilities | 323,173 | 3,317 | - | - | 326,490 |
| Financial liabilities | 1,394,618 | 1,096,034 | 809,062 | - | **3,299,714** |
| Non-financial liabilities | 12,801 | 95,763 | - | 14,080 | **122,644** |
| **Total liabilities** | **1,407,419** | **1,096,034** | **809,062** | **14,080** | **3,326,595** |
| **Net liquidity surplus** | **55,153** | **7,410** | **446,210** | **259,400** | **768,173** |
| **Off balance sheet** | | | | | |
| Contingent liabilities | 1,266,528 | 211,692 | 61,348 | 234 | **1,539,802** |
| Commitments | 4,200 | - | - | - | **4,200** |
| Total | **1,270,728** | **211,692** | **61,348** | **234** | **1,544,002** |

## 31 Risk management (continued)

### 31.8 Liquidity risk and funding management (continued)

The maturity profile of the Group's assets and liabilities at 31 December 2017 was as follows:

| | Less than 3 months AED'000 | 3 months to 1 year AED'000 | 1 year to 5 years AED'000 | Over 5 years AED'000 | Total AED'000 |
|---|---|---|---|---|---|
| **ASSETS** | | | | | |
| Cash and balances with U.A.E. Central Bank | 35,622 | - | 6,000 | - | 41,622 |
| Due from banks and financial institutions | 675,847 | 1,000 | - | - | 676,847 |
| Loans and advances | 710,254 | 657,841 | 588,046 | 379,660 | 2,335,801 |
| Islamic financing and investing assets | 66,672 | 48,454 | 56,215 | 2,029 | 173,370 |
| Investments, including associate | 289,803 | 152,296 | 202,105 | 381,869 | 1,026,073 |
| Other assets | 35,357 | 135,662 | 5,008 | - | 176,027 |
| Financial assets | 1,813,555 | 995,253 | 857,374 | 763,558 | 4,429,740 |
| Non-financial assets | 32,173 | - | 95,960 | 6,966 | 135,099 |
| **Total assets** | **1,845,728** | **995,253** | **953,334** | **770,524** | **4,564,839** |
| **LIABILITIES** | | | | | |
| Due to banks | - | 23,831 | - | - | 23,831 |
| Customers' deposits Margin accounts | 1,088,259 | 1,020,923 | 841,362 | - | 2,950,544 |
| Short term borrowings and medium term loans | 77,244 | 260,000 | 50,000 | - | 387,244 |
| Other liabilities | 82,374 | 52,778 | - | - | 135,152 |
| Financial liabilities | **1,247,877** | **1,357,532** | **891,362** | - | **3,496,771** |
| Non-financial liabilities | 25,903 | 125,342 | - | 13,624 | 164,869 |
| **Total liabilities** | **1,273,780** | **1,482,874** | **891,362** | **13,624** | **3,661,640** |
| **Net liquidity surplus (gap)** | **571,948** | **(487,621)** | **61,972** | **756,900** | **903,199** |
| **2017** | | | | | |
| Contingent liabilities | 1,341,523 | 314,189 | 72,227 | 248 | 1,728,187 |
| Commitments | 222,274 | - | - | - | 222,274 |
| Total | **1,563,797** | **314,189** | **72,227** | **248** | **1,950,461** |

## 31 Risk management (continued)

### 31.9 Operational risk

Operational risk is the risk of direct or indirect loss arising from inadequate or failed internal processes, systems failure, human error, fraud or external events. When required controls fail, operational risks can cause damage to reputation, have legal or regulatory implications, or lead to financial loss. While the Group cannot expect to eliminate all operational risks, through a control framework and by continuous monitoring and responding to potential risks, the Group is able to manage these risks. Controls include effective segregation of duties, appropriate access, authorisation and reconciliation procedures, staff training and robust assessment processes. The processes are reviewed by risk management and internal audit on an ongoing basis.

### 31.10 Insurance risk

The principal risk the Group faces under insurance contracts is that the actual claims and benefit payments or the timing thereof, differs from expectations. This is influenced by the frequency of claims, severity of claims, actual benefits paid and subsequent development of long–term claims. Therefore, the objective of the Group is to ensure that sufficient reserves are available to cover these liabilities.

The risk exposure is mitigated by diversification across a large portfolio of insurance contracts and geographical areas. The variability of risks is also improved by careful selection and implementation of underwriting strategy guidelines, as well as the use of reinsurance arrangements.

In common with other insurers, in order to minimize financial exposure arising from large insurance claims, the Group, in the normal course of business, enters into arrangements with other parties for reinsurance purposes. Such reinsurance arrangements provide for greater diversification of business, allow management to control exposure to potential losses arising from large risks, and provide additional capacity for growth. A significant portion of the reinsurance is effected under treaty, facultative and excess of loss reinsurance contracts.

To minimise its exposure to significant losses from reinsurer insolvencies, the Group evaluates the financial condition of its reinsurers and monitors concentrations of credit risk arising from similar geographic regions, activities or economic characteristics of the reinsurers.

## 32 Fair value measurement (continued)

While the Group prepares its financial statements under the historical cost convention modified for measurement to fair value of investments carried at fair value and investment properties, in the opinion of management, the estimated carrying values and fair values of financial assets and liabilities, that are not carried at fair value in the financial statements are not materially different, since assets and liabilities are either short term in nature or in the case of deposits and performing loans and advances, frequently repriced. For impaired loans and advances, expected cash flows, including anticipated realisation of collateral, were discounted using the original interest rates, considering the time of collection and a provision for the uncertainty of the cash flows.

*Fair value hierarchy:*

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

- **Level 1**: Quoted market price (unadjusted) in an active market for an identical instrument. Such instruments are valued by reference to unadjusted quoted prices for identical assets or liabilities in active markets where the quoted price is readily available, and the price represents actual and regularly occurring market transactions.
- **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 in markets that are considered less than active; 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 input not based on observable data and the unobservable input have a significant impact on the instrument's valuation. This category includes instruments that are valued based on quoted prices for similar instruments where significant unobservable adjustments or assumptions are required to reflect differences between the instruments.

Fair values of financial assets and financial liabilities that are traded in active markets are based on quoted market priced or dealer priced quotations. For all other financial instruments the Group determines fair values using valuation techniques.

Valuation techniques include net present value and discounted cash flow models. Assumptions and inputs used in valuation techniques include risk-free and benchmark interest rates, credit spreads and other inputs used in estimating discount rates. The objective of valuation techniques is to arrive at a fair value determination that reflects the price of the financial instrument at the reporting date that would have been determined by market participants acting at arm's length.

Observable prices and model inputs are usually available in the market for listed equity securities. Availability of observable market prices and model inputs reduces the need for management judgement and estimation and also reduces the uncertainty associated with determination of fair values. Availability of observable market prices and inputs varies depending on the products and markets and is prone to changes based on specific events and general conditions in the financial markets.

## 32 Fair value measurement (continued)

The following table shows the analysis of assets recorded at fair value by level of the fair value hierarchy for the year ended 31 December 2018:

| | Date of Valuation | Level 1 AED'000 | Level 2 AED'000 | Level 3 AED'000 | Total AED'000 |
|---|---|---|---|---|---|
| **Assets measured at fair value** | | | | | |
| Investment properties | 31 December 2018 | - | - | **79,478** | **79,478** |
| **At fair value through profit or loss** | | | | | |
| Quoted equities | 31 December 2018 | 161,384 | - | - | **161,384** |
| Quoted debt instruments | 31 December 2018 | - | - | - | - |
| | | **161,384** | - | - | **161,384** |
| **At fair value through other comprehensive income** | | | | | |
| Quoted equities | 31 December 2018 | 454,925 | - | - | **454,925** |
| Unquoted equities | 31 December 2018 | - | 12,036 | 87,281 | **99,317** |
| Investment in managed funds | 31 December 2018 | - | 6,336 | - | **6,336** |
| | | **454,925** | **18,372** | **87,281** | **560,578** |
| **Assets for which fair value is disclosed** | | | | | |
| Investment carried at amortised cost | | - | **1,837** | - | **1,837** |

The fair values of the Group's financial assets and liabilities that are carried at amortised cost approximate to their carrying amount as disclosed in these financial statements. For the long-term financial assets and liabilities, management does not expect to have a material difference between the carrying amount and the fair value.

## 32 Fair value measurement (continued)

The following table shows the analysis of assets recorded at fair value by level of the fair value hierarchy as at 31 December 2017:

| | Date of Valuation | Level 1 AED'000 | Level 2 AED'000 | Level 3 AED'000 | Total AED'000 |
|---|---|---|---|---|---|
| **Assets measured at fair value** | | | | | |
| Non-current assets classified as held for sale | 31December 2017 | - | - | 82,070 | 82,070 |
| **At fair value through profit or loss** | | | | | |
| Quoted equities | 31 December 2017 | 174,858 | - | - | 174,858 |
| Quoted debt instruments | 31 December 2017 | 1,500 | - | - | 1,500 |
| | | 176,358 | - | - | 176,358 |
| **At fair value through other comprehensive income** | | | | | |
| Quoted equities | 31 December 2017 | 616,102 | - | - | 616,102 |
| Unquoted equities | 31 December 2017 | - | 9,822 | 83,095 | 92,917 |
| Investment in managed funds | 31 December 2017 | - | 7,322 | - | 7,322 |
| | | **616,102** | **17,144** | **83,095** | **716,341** |
| **Assets for which fair value is disclosed** | | | | | |
| Investment carried at amortised cost | | - | 82,657 | - | 82,657 |

The following is a description of the determination of fair value for assets which are recorded at fair value using valuation techniques. These incorporate the Group's estimate of assumptions that a market participant would make when valuing the assets.

### Investments carried at fair value through profit or loss

Investments carried at fair value through profit and loss are listed equities and debt instruments in local as well as international exchanges. Valuations are based on market prices as quoted in the exchange.

### Investments carried at fair value through other comprehensive income

Investments carried at fair value through other comprehensive income, the revaluation gains/losses of which are recognized through equity, comprise long-term strategic investments in listed and unlisted equities, Tier 1 Capital instruments and private equity funds. Listed equity and Tier 1 Capital instruments valuations are based on market prices as quoted in the exchange while funds are valued on the basis of net asset value statements received from fund managers. For unquoted equities, the financial statements provide the valuations of these investments, which are arrived at primarily by using Price Earning Multiple basis valuation. The valuation requires management to make certain assumptions about the model inputs, including forecast cash flows, the discount rate, credit risk and volatility and price earnings multiples. The probabilities of the various estimates within the range can be reasonably assessed and are used in management's estimate of fair value for these unquoted equity investments.

## 32 Fair value measurement (continued)

Following is the description of the significant unobservable inputs used in the valuation of unquoted equities categorized under level 3 fair value measurement.

| | Valuation technique | Significant unobservable inputs to valuation | Range (Weighted average) | Sensitivity of the input to fair value |
|---|---|---|---|---|
| Unquoted equities | Price Earning Multiple Valuation Basis | PE Multiple | 9-11 | Increase (decrease) in the PE Multiples by 1 would result in increase (decrease) in fair value by AED 5 million |

**Transfers between categories**

During the period, there were no transfers between Level 1 and Level 2 fair value measurements, and no transfers into or out of Level 3 fair value measurements.

## 33 Capital adequacy

**Capital management**

The primary objective of the Group's capital management is to ensure that the Group maintains healthy capital ratios in order to support its business, to maximise shareholders' value and to ensure that the Group complies with externally imposed capital requirements.

The Group manages its capital structure and makes adjustments to it in the light of changes in economic conditions and the risk characteristics of its activities. In order to maintain or adjust the capital structure, the Group may adjust the amount of dividend payment to shareholders or issue capital securities. No changes were made in the objectives, policies and processes from the previous years.

The capital adequacy ratio calculated in accordance with the U.A.E. Central Bank's guidelines for commercial banks is as follows:

| | 2018 AED'000 | 2017 AED'000 |
|---|---|---|
| Total capital base | **761,468** | **941,909** |
| **Risk weighted assets:** | | |
| Statement of financial position items | 3,345,886 | 3,704,632 |
| Off statement financial position exposures | 399,786 | 492,477 |
| **Total risk weighted assets** | **3,745,672** | **4,197,109** |
| **Total assets ratio (%)** | **20.30%** | **22.4%** |

## 34 Other operating income, net

| | 2018<br>AED'000 | 2017<br>AED'000 |
|---|---|---|
| Rental income from investment property | 6,554 | 6,344 |
| Change in fair value of investment property | (2,592) | (6,000) |
| Collection from written off customers | 2,700 | 20,100 |
| Others | 14,300 | 7,239 |
| | **20,962** | **27,683** |

## 35 General and administrative expenses

| | 2018<br>AED'000 | 2017<br>AED'000 |
|---|---|---|
| Lease expense | 8,643 | 8,397 |
| Depreciation expense | 8,701 | 7,169 |
| Communication expenses | 5,568 | 4,728 |
| Management fees (Note 23) | - | - |
| Professional fees including legal, consultancy and others | 6,614 | 5,849 |
| Repair and maintenance | 2,833 | 2,885 |
| Advertising, maintenance and other expenses | 25,097 | 22,096 |
| | **57,456** | **51,124** |

## 36 Legal proceedings

The Group is involved in various legal proceedings and claims arising in the ordinary course of business. While the outcome of these matters cannot be predicted with certainty, management does not believe that these matters will have a material adverse effect on the Group's consolidated financial statements if disposed unfavourably.

## 37 Seasonality of results

No income of a seasonal nature was recorded in the consolidated income statement for the year ended 31 December 2018 and 2017.

## 38 Comparative figures

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