Bank Alfalah Limited

Dubai, United Arab Emirates

FINANCIAL STATEMENTS

for the year ended 31 December 2021

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KPMG

KPMG Lower Gulf Limited
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Independent auditors' report

To the Head Office of Bank Alfalah Limited – Dubai Branch

Report on the Audit of the Financial Statements

Opinion

We have audited the financial statements of Bank Alfalah Limited – Dubai Branch ("the Bank"), which comprise the statement of financial position as at 31 December 2021, the statements of profit or loss, other comprehensive income, changes in equity, and cash flows for the year then ended, and notes comprising significant accounting policies and other explanatory information.

In our opinion, the accompanying financial statements present fairly, in all material respects, the financial position of the Bank as at 31 December 2021, and its financial performance, and its cash flows for the year then ended in accordance with International Financial Reporting Standards (IFRS).

Basis for Opinion

We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the *Auditors' Responsibilities for the Audit of the Financial Statements* section of our report. We are independent of the Bank in accordance with International Ethics Standards Board for Accountants International Code of Ethics for Professional Accountants (including International Independence Standards) (IESBA Code) together with the ethical requirements that are relevant to our audit of the financial statements in the United Arab Emirates, and we have fulfilled our other ethical responsibilities in accordance with these requirements and the IESBA Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Responsibilities of Management and Those Charged with Governance for the Financial Statements

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

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

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

Auditors' Responsibilities for the Audit of the Financial Statements

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

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

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

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

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

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

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

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

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

Report on Other Legal and Regulatory Requirements

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

KPMG Lower Gulf Limited

Fawzi AbuRass
Registration No.: 968
Dubai, United Arab Emirates

Date: 7 April 2022

STATEMENT OF FINANCIAL POSITION
As at 31 December 2021

	Notes	***2021***	*2020*
		AED '000	*AED '000*
ASSETS			
Cash and balances with the UAE Central Bank	*5*	**124,423**	47,897
Balances with other banks	*6*	**42,471**	15,134
Loans and advances - net	*7*	**91,525**	57,026
Investment securities	*8*	**445,530**	342,414
Other assets	*9*	**6,542**	8,365
Property and equipment	*11*	**1,196**	615
TOTAL ASSETS		**711,687**	471,451
LIABILITIES AND EQUITY			
LIABILITIES			
Due to banks	*12*	**46,371**	68,419
Deposits and other accounts	*13*	**547,723**	282,144
Deferred tax liability	*27*	**279**	959
Other liabilities	*14*	**8,579**	10,396
TOTAL LIABILITIES		**602,952**	361,918
EQUITY			
Allocated capital	*15*	**100,000**	100,000
Regulatory credit risk reserve		**3,246**	1,722
Statutory reserve	*16*	**945**	529
Fair value reserve (OCI)	*17*	**1,849**	4,240
Retained earnings		**2,695**	3,042
TOTAL EQUITY		**108,735**	109,533
TOTAL LIABILITIES AND EQUITY		**711,687**	471,451

These financial statements were authorized for issue on April 6, 2022 by:

Manager Finance

Country Manager

The independent auditor's report is set out on pages 1 - 3
The notes 1 to 29 are an integral part of these financial statements.

STATEMENT OF PROFIT OR LOSS

for the year ended 31 December 2021

	Notes	***2021*** ***AED '000***	*2020* *AED '000*
Interest income	*21*	**13,952**	11,302
Interest expense	*22*	**(5,138)**	(3,515)
Net interest income		**8,814**	7,787
Fee, commission and brokerage income	*23*	**1,188**	1,064
Foreign exchange income		**783**	911
Other income	*24*	**2,617**	765
Total operating income		**4,588**	2,740
Expected credit loss		**(370)**	(237)
Net income		**13,032**	10,290
Non-interest expense			
Staff cost	*25*	**(5,345)**	(4,565)
Administrative and general expenses	*26*	**(1,752)**	(1,566)
Depreciation	*11*	**(631)**	(634)
Operating expense		**(7,728)**	(6,765)
Profit before tax		**5,304**	3,525
Taxation	*27.1*	**(1,143)**	(763)
Net profit for the year		**4,161**	2,762

The independent auditor's report is set out on pages 1 - 3
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STATEMENT OF OTHER COMPREHENSIVE INCOME

for the year ended 31 December 2021

	2021	2020
	AED '000	*AED '000*
Net profit for the year	**4,161**	2,762
Other comprehensive income		
Items that are or may be reclassified subsequently to income statement		
Net gains from change in fair value on financial assets measured at fair value through other comprehensive income	**(4,533)**	4,022
Deferred tax on financial assets measured at fair value through OCI	**1,811**	(1,755)
Expected credit loss on investments under IFRS 9	**377**	272
Actuarial gain / (loss)	**(46)**	-
Other comprehensive (loss)/income for the year	**(2,391)**	2,539
Total comprehensive income for the year	**1,770**	5,301

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STATEMENT OF CHANGES IN EQUITY

for the year ended 31 December 2021

	Share capital	***Regulatory credit risk reserve***	***Fair value reserve (OCI)***	***Statutory reserve***	***Retained earnings***	***Total***
	AED'000					
As at January 1, 2021	**100,000**	**1,722**	**4,240**	**529**	**3,042**	**109,533**
Net profit for the year	**-**	**-**	**-**	**-**	**4,161**	**4,161**
Other comprehensive (loss)/gain for the year	**-**	**-**	**(2,391)**	**-**	**-**	**(2,391)**
Total comprehensive profit for the year	**-**	**-**	**(2,391)**	**-**	**4,161**	**1,770**
Transfer from other reserve	**-**	**1,524**	**-**	**-**	**(1,524)**	**-**
Transfer to statutory reserve	**-**	**-**	**-**	**416**	**(416)**	**-**
Profit repatriated to Head Office	**-**	**-**	**-**	**-**	**(2,568)**	**(2,568)**
As at December 31, 2021	**100,000**	**3,246**	**1,849**	**945**	**2,695**	**108,735**

	Share capital	*Regulatory credit risk reserve*	*Fair value reserve (OCI)*	*Statutory reserve*	*Retained earnings*	*Total*
	AED'000					
As at January 1, 2020	100,000	1,389	1,701	253	889	104,232
Net profit for the year	-	-	-	-	2,762	2,762
Other comprehensive gain for the year	-	-	2,539	-	-	2,539
Total comprehensive profit for the year	-	-	2,539	-	2,762	5,301
Transfer from other reserve	-	333	-	-	(333)	-
Transfer to statutory reserve	-	-	-	276	(276)	-
As at December 31, 2020	100,000	1,722	4,240	529	3,042	109,533

The independent auditor's report is set out on pages 1 - 3
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STATEMENT OF CASH FLOWS

for the year ended 31 December 2021

	Notes	***2021*** ***AED '000***	*2020* *AED '000*
OPERATING ACTIVITIES			
Net profit before taxation		**5,304**	3,525
Adjustment for:			
Depreciation		**631**	634
Expected credit loss		**370**	237
Gain on sale of investments measured at FVOCI	*24*	**(491)**	(714)
Borrowing cost on lease liability		**6**	28
Provision for employees' end of service benefits	*14.1*	**65**	272
Cash generated from operations before changes in operating assets and liabilities		**5,885**	3,982
Changes in operating assets and liabilities:			
Loans and advances	*7*	**(34,568)**	(26,538)
Other assets	*9*	**1,823**	(4,867)
Due to banks	*12*	**7,336**	(2,438)
Customer deposits	*13*	**265,579**	114,494
Other liabilities		**(6,744)**	3,332
		233,426	83,983
Income tax paid		**747**	754
Net cash generated from operating activities		**240,058**	88,719
INVESTING ACTIVITIES			
Net investments in OCI		**(105,838)**	(131,116)
Purchase of property and equipment	*11*	**(353)**	(38)
Net cash (used in) from investing activities		**(106,192)**	(131,154)
FINANCING ACTIVITY			
Payment against lease liability		**(619)**	(514)
Net cash generated from financing activity		**(619)**	(514)
NET DECREASE IN CASH AND CASH EQUIVALENTS		**133,247**	(42,949)
Cash and cash equivalents at beginning of the year		**(3,083)**	39,866
CASH AND CASH EQUIVALENTS AT 31 DECEMBER		**130,164**	(3,083)
Cash and cash equivalents comprise of:			
Cash and balances with the UAE Central Bank	*5*	**124,423**	47,897
Balances with other banks	*6*	**42,471**	15,134
Less: Borrowings from banks with maturity of less than 3 months	*12*	**(36,730)**	(66,114)
CASH AND CASH EQUIVALENTS AT 31 DECEMBER 2021		**130,164**	(3,083)

The independent auditor's report is set out on pages 1 - 3
The notes 1 to 29 are an integral part of these financial statements.

NOTES TO THE FINANCIAL STATEMENTS

1. ESTABLISHMENT AND OPERATIONS

Bank Alfalah Limited - Dubai Branch operates as a branch of Bank Alfalah Limited with its Head Office ("Head Office") in Pakistan since 01 November, 2017. In the United Arab Emirates (“UAE”), it operates through its one branch located in the emirate of Dubai under license number 770308 issued by the Central Bank of the UAE ("UAE Central Bank"). Bank Alfalah Limited, is listed on the Pakistan Stock Exchange.

The principal activities of Bank Alfalah Limited - Dubai Branch (the “Bank” or “the Branch”). is to provide wholesale banking services in the UAE. The registered address of the Bank is Al-Khaleej Building, Zaabeel Street, Karama, P.O. Box No. 8456, Dubai, UAE.

2. ACCOUNTING POLICIES

2.1.1 Basis of preparation

These financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board (IASB) and comply with relevant laws of the U.A.E including UAE Federal Law No. 2 of 2015 ("Companies Law").

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

- derivative financial instruments are measured at fair value;
- financial assets at fair value through other comprehensive income ("FVOCI");

The preparation of financial statements in conformity with IFRS as issued by the IASB requires the use of certain critical accounting estimates. It also requires management to exercise its judgment in the process of applying the accounting policies. The areas involving a higher degree of judgment or complexity, or areas where assumptions and estimates are significant to the financial statements are disclosed in note 4.

2.1.2 Changes in accounting policies

Relevant new and revised IFRS applied with no material effect on the financial statements

The following new and revised IFRS have been adopted in these financial statements. The application of these new and revised IFRS has not had any material impact on the amounts reported for the current and prior periods.

	Effective for annual periods beginning on or after
a) Amendments to IFRS 9, IAS 39, IFRS 7, IFRS 4 and IFRS 16 relating to phase 2 of interest rate benchmark reforms	**1 January 2021**

Other than the above, there are no other significant IFRSs and amendments that were effective for the first time for the financial year beginning on or after 1 January 2021.

NOTES TO THE FINANCIAL STATEMENTS (continued)

2. ACCOUNTING POLICIES (continued)

2.2. Summary of significant accounting policies

a) Recognition and initial measurement

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

A financial asset or financial liability is measured initially at fair value plus, for an item not at Fair Value through the Statement of Profit or Loss (FVTPL), transaction costs that are directly attributable to its acquisition or issue. The fair value of a financial instrument at initial recognition is generally its transaction price.

Classification

The Bank classifies financial assets on initial recognition in the following categories:

i) Amortized cost;
ii) Fair value through other comprehensive income (FVOCI); and
iii) Fair value through profit or loss (FVTPL)

i) **Financial assets at amortized cost**

A financial asset is measured at amortized cost if it meets both of the following conditions and is not designated as at FVTPL:

- the asset is held within a business model whose objective is to hold financial assets in order to collect contractual cash flows; and
- the contractual terms of the financial asset give rise on specified dates to cash flows that are SPPI.

ii) **Financial assets at fair value through other comprehensive income (FVOCI)**

A debt instrument is classified as being measured at FVOCI if it meets the following two conditions and the debt instrument is not designated at FVTPL:

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

iii) **Fair value through profit or loss (FVTPL)**

All other financial assets are classified as measured at FVTPL.

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

All financial assets and liabilities are classified at amortised cost except for investment securities which are classified as fair value through OCI.

NOTES TO THE FINANCIAL STATEMENTS (continued)

2. ACCOUNTING POLICIES (continued)

2.2 Summary of significant accounting policies (continued)

b) Fair value measurement

'Fair value' is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date in the principal or, in its absence, the most advantageous market to which the Bank has access at that date. The fair value of a liability reflects its non-performance risk.

When one is available, the Bank measures the fair value of an instrument using the quoted price in an active market for that instrument. A market is regarded as 'active' if transactions for the asset or liability take place with sufficient frequency and volume to provide pricing information on an ongoing basis.

If there is no quoted price in an active market, then the Bank uses valuation techniques that maximise the use of relevant observable inputs and minimise the use of unobservable inputs. The chosen valuation technique incorporates all of the factors that market participants would take into account in pricing a transaction.

The best evidence of the fair value of a financial instrument on initial recognition is normally the transaction price – i.e. the fair value of the consideration given or received. If the Bank determines that the fair value on initial recognition differs from the transaction price and the fair value is evidenced neither by a quoted price in an active market for an identical asset or liability nor based on a valuation technique for which any unobservable inputs are judged to be insignificant in relation to the difference, then the financial instrument is initially measured at fair value, adjusted to defer the difference between the fair value on initial recognition and the transaction price. Subsequently, that difference is recognised in profit or loss on an appropriate basis over the life of the instrument but no later than when the valuation is wholly supported by observable market data or the transaction is closed out.

The Bank recognises transfers between levels of the fair value hierarchy as of the end of the reporting period during which the change has occurred.

Fair value hierarchy:

All assets and liabilities for which fair value is measured or disclosed in the financial statements are categorised within the fair value hierarchy, described as follows, which reflects the significance of inputs used in making the measurements:

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

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

NOTES TO THE FINANCIAL STATEMENTS (continued)

2. ACCOUNTING POLICIES (continued)

2.2 Summary of significant accounting policies (continued)

b) Fair value measurement (continued)

Fair value hierarchy (continued)

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

The Bank determines whether transfers have occurred between levels in the hierarchy by re-assessing categorization (based on the lowest level input that is significant to the fair value measurement as a whole) at the end of each reporting period.

At each reporting date, the Bank analyses the movements in the values of assets and liabilities which are required to be remeasured or re-assessed as per the Bank's accounting policies. For this analysis, the Bank verifies the major inputs applied in the latest valuation by agreeing the information in the valuation computation to contracts and other relevant documents.

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

Financial Assets

(a) Business model assessment

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

- The stated policies and objectives for the business and the operation of those policies in practice. In particular, whether management's strategy focuses on earning contractual interest revenue, maintaining a particular interest rate profile, matching the duration of the financial assets to the duration of the liabilities that are funding those assets or realizing cash flows through the sale of the assets;

- How the performance of the portfolio and the financial asset held within the portfolio is evaluated and reported to the management;
- The risks that affect the performance of the portfolio and, in particular, the way in which those risks are managed;
- How the managers of the business are compensated; and

The frequency, volume and timing of sales in prior periods, the reasons for such sales and its expectations about future sales activity. However, information about sales activity is not considered in isolation, but as part of an overall assessment of how the Bank's stated objective for managing the financial assets is achieved and how cash flows are realized.

NOTES TO THE FINANCIAL STATEMENTS (continued)

2. ACCOUNTING POLICIES (continued)

2.2. Summary of significant accounting policies (continued)

Financial Assets (continued)

Assessment whether contractual cash flows is solely payments of principal and interest

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

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

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

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

b) Subsequent measurement

The Bank measures financial instruments, such as derivatives and certain fixed income instruments, at fair value at each reporting date.

Financial asset classified as at FVOCI or FVTPL are subsequently measured at fair value. Financial assets not carried at fair value are subsequently measured at amortized cost using the effective interest method, less expected credit allowances.

c) Reclassifications

Financial assets are not reclassified subsequent to their initial recognition except in the period after the Bank changes its business model for managing financial assets. If the business model under which the Bank holds financial assets changes, the financial assets affected are reclassified. The classification and measurement requirements related to the new category apply prospectively from the first day of the first reporting period following the change in business model that results in reclassifying the Bank's financial assets. During the period there was no change in the business model under which the Bank holds financial assets and therefore no reclassifications were made. Changes in contractual cash flows are considered under the accounting policy on 'Modification of financial assets' and 'Derecognition of financial assets'.

d) Impairment

The Bank recognizes loss allowances for expected credit losses (ECLs) on the following financial instruments that are not measured at FVTPL:

- Loans and advances
- Debt investment securities
- Unfunded exposures

NOTES TO THE FINANCIAL STATEMENTS (continued)

2. ACCOUNTING POLICIES (continued)

2.2. Summary of significant accounting policies (continued)

Financial Assets (continued)

The Bank considers a debt investment security to have low credit risk when its credit risk rating is equivalent to the globally understood definition of 'investment grade'. The Bank has applied low credit risk exemption to cash and balances with the UAE Central Bank and balances with other banks.

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

Stage 1: When loans are first recognized, the Bank recognizes an allowance based on 12 months ECLs. 12-month ECL are the portion of ECL that result from default events on a financial instrument that are possible within the 12 months after the reporting date.

Stage 2: When a loan has shown a significant increase in credit risk since origination, the Bank records an allowance for the life time expected credit losses (LTECL). LTECL are the ECL that result from all possible default events over the expected life of the financial instrument.

Stage 3: Loans considered credit-impaired. The Bank records an allowance for the LTECLs.

ECLs are an unbiased probability-weighted estimate of the present value of credit losses that is determined by evaluating a range of possible outcomes. For funded exposures, ECL is measured as follows:

- for financial assets that are not credit-impaired at the reporting date: as the present value of all cash shortfalls (i.e. the difference between the cash flows due to the entity in accordance with the contract and the cash flows that the Bank expects to receive);

- financial assets that are credit-impaired at the reporting date: as the difference between the gross carrying amount and the present value of estimated future cash flows.

However, for unfunded exposures, ECL is measured as follows:

- for undrawn loan commitments, as the present value of the difference between the contractual cash flows that are due to the Bank if the holder of the commitment draws down the loan and the cash flows that the Bank expects to receive if the loan is drawn down; and
- for letter of credit and financial guarantee contracts, the expected payments to reimburse the holder of the guaranteed debt instrument less any amounts that the Bank expects to receive from the holder, the debtor or any other party.

The Bank measures ECL on an individual basis, or on a collective basis for portfolios of loans that share similar economic and credit risk characteristics. The measurement of the loss allowance is based on the present value of the asset's expected cash flows using the asset's original Effective Interest Rate (EIR), regardless of whether it is measured on an individual basis or a collective basis.

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

- Probability of Default (PD);
- Exposure at Default (EAD); and
- Loss Given Default (LGD)

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

NOTES TO THE FINANCIAL STATEMENTS (continued)

2. ACCOUNTING POLICIES (continued)

2.2. Summary of significant accounting policies (continued)

Financial Assets (continued)

d) Impairment (continued)

Details of these statistical parameters / inputs are as follows:

- PD – PD is the estimate of likelihood of default over a given time horizon, which is calculated based on statistical rating models currently used by the Bank and assessed using rating tools tailored to the various categories of counterparties and exposures.

EAD – EAD represents the expected exposure in the event of a default. The Bank derives the EAD from the current exposure to the counterparty and potential changes to the current amount allowed under the contract and arising from amortisation. The EAD of a financial asset is its gross carrying amount at the time of default. For lending commitments, the EADs are potential future amounts that may be drawn under the contract, which are estimated based on historical observations and forward-looking forecasts. For financial guarantees, the EAD represents the amount of the guaranteed exposure when the financial guarantee becomes payable. EAD is determined by the exposure at reporting date.

- LGD – LGD is an estimate of the loss arising on default. It is based on the difference between the contractual cash flows due and those that the lender would expect to receive, taking into account cash flows from any collateral.

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

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

Credit-impaired financial assets
At each reporting date, the Bank assesses whether financial assets carried at amortized cost and debt securities carried at FVOCI are credit-impaired.

A financial asset is 'credit-impaired' when one or more events that have a detrimental impact on the estimated future cash flows of the financial asset have occurred. Credit-impaired financial assets are referred to as Stage 3 assets. Evidence that a financial asset is credit-impaired includes the following observable data:

- significant financial difficulty of the borrower or issuer;
- a breach of contract such as a default or past due event;
- the lender of the borrower, for economic or contractual reasons relating to the borrower's financial difficulty, having granted to the borrower a concession that the lender would not otherwise consider;
- the disappearance of an active market for a security because of financial difficulties.

NOTES TO THE FINANCIAL STATEMENTS (continued)

2. ACCOUNTING POLICIES (continued)

2.2. Summary of significant accounting policies (continued)

Financial Assets (continued)

d) Impairment (continued)

It may not be possible to identify a single discrete event - instead, the combined effect of several events may have caused financial assets to become credit-impaired. The Bank assesses whether debt instruments that are financial assets measured at amortized cost or FVOCI are credit-impaired at each reporting date. To assess if sovereign and corporate debt instruments are credit impaired, the Bank considers the following factors:

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

A loan is considered credit-impaired when a concession is granted to the borrower due to a deterioration in the borrower’s financial condition, unless there is evidence that as a result of granting the concession the risk of not receiving the contractual cash flows has reduced significantly and there are no other indicators of impairment.

For financial assets where concessions are contemplated but not granted, the asset is deemed credit impaired when there is observable evidence of credit-impairment including meeting the definition of default. The definition of default includes unlikeliness to pay indicators and a backstop if amounts are overdue for 90 days or more.

Default definition

Critical to the determination of ECL is the definition of default. The definition of default is used in measuring the amount of ECL and in the determination of whether the loss allowance is based on 12-month or lifetime ECL, as default is a component of the probability of default (PD) which affects both the measurement of ECLs and the identification of a significant increase in credit risk.
The Bank considers a financial asset to be in default when:

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

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

- qualitative - e.g. breaches of covenant;
- quantitative - e.g. overdue status and non-payment on another obligation of the same issuer to the Bank and based on data developed internally and obtained from external sources.

NOTES TO THE FINANCIAL STATEMENTS (continued)

2. ACCOUNTING POLICIES (continued)

2.2. Summary of significant accounting policies (continued)

Financial Assets (continued)

d) Impairment (continued)

Wholesale portfolio

The wholesale portfolio comprises of loans which are managed individually by the Relationship Managers (RMs) with oversight from the Credit Risk team of the Bank. These loans are appraised at least annually based on the financial information, other qualitative information and account conduct of the customer.

A wholesale customer is identified as at default if the customer is materially delinquent for more than 90 days on any of its credit obligation.

Assessment of significant increase in credit risk

The Bank monitors all financial assets, issued loan commitments, letters of credit and financial guarantee contracts that are subject to the impairment requirements to assess whether there has been a significant increase in credit risk since initial recognition. If there has been a significant increase in credit risk, the Bank will measure the loss allowance based on lifetime rather than 12-month ECL. The assessment is performed at the reporting date for each individual exposure.

In assessing whether the credit risk on a financial instrument has increased significantly since initial recognition, the Bank compares the probability of a default occurring on the financial instrument at the reporting date based on the remaining maturity of the instrument with the probability of a default occurring that was anticipated for the remaining maturity at the current reporting date when the financial instrument was first recognized.

In making this assessment, the Bank considers both quantitative and qualitative information that is reasonable and supportable, including historical experience and forward-looking information that is available without undue cost or effort, based on the Bank's historical experience and expert credit assessment. The following indicators are incorporated:

- internal risk grade;
- external credit rating (as far as available);
- actual or expected significant adverse changes in business, financial or economic conditions that are expected to cause a significant change to the borrower's ability to meet its obligations;
- actual or expected significant changes in the operating results of the borrower;
- significant increases in credit risk on other financial instruments of the same borrower;
- significant changes in the value of the collateral supporting the obligation;
- significant changes in the actual or expected performance and behavior of the borrower, including changes in the payment status of borrowers in the group and changes in the operating results of the borrower; and
- macroeconomic information is incorporated as part of the internal rating model.

The quantitative factors that indicate significant increase in credit risk are reflected in PD models on a timely basis. However, the Bank still considers separately some qualitative factors to assess if credit risk has increased significantly.

NOTES TO THE FINANCIAL STATEMENTS (continued)

2. ACCOUNTING POLICIES (continued)

2.2. Summary of significant accounting policies (continued)

Financial Assets (continued)

d) Impairment (continued)

Assessment of significant increase in credit risk (continued)

For lending's there is particular focus on assets that are included on a 'watch list' given an exposure is on a watch list once there is a concern that the creditworthiness of the specific counterparty has deteriorated.

As a back stop, a significant increase in credit risk is presumed if a customer is more than 60 days past due in making a contractual payment. Days past due are determined by counting the number of days since the earliest elapsed due date in respect of which full payment has not been received. Due dates are determined without considering any grace period that might be available to the borrower.

Improvement in credit risk profile
If there is evidence that there is no longer a significant increase in credit risk relative to initial recognition, then the loss allowance on an instrument returns to being measured as 12-month ECL.

The Bank has defined below criteria in accordance with regulatory guidelines to assess any improvement in the credit risk profile which will result into upgrading of customers moving from Stage 3 to Stage 2 and from Stage 2 to Stage 1.

Significant decrease in credit risk will be upgraded stage-wise (one stage at a time) from Stage 3 to Stage 2 after 3 months or removal of condition that triggered movement to stage 3 (whichever is later) and from Stage 2 to Stage 1 after meeting the curing period of at least 12 months.

Restructured cases will be upgraded if repayments of 3 instalments (for quarterly instalments) have been made or 12 months (for instalments longer than quarterly) curing period is met.

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

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

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

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

NOTES TO THE FINANCIAL STATEMENTS (continued)

2. ACCOUNTING POLICIES (continued)

2.2. Summary of significant accounting policies (continued)

Financial Assets (continued)

e) Write-off

Loans and advances and debt securities are written-off when the Bank has no reasonable expectations of recovering the financial asset (either partially or in full). This is the case when the Bank determines that the borrower does not have assets or sources of income that could generate sufficient cash flows to repay the amounts subject to the write-off. This assessment is carried out at the individual asset level. A write-off constitutes a derecognition event. The Bank may apply enforcement activities to financial assets written-off.

f) Modification of financial assets

A modification of a financial asset occurs when the contractual terms governing the cash flows of a financial asset are renegotiated or otherwise modified between initial recognition and maturity of the financial asset. A modification affects the amount and / or timing of the contractual cash flows either immediately or at a future date.

When a financial asset is modified, the Bank assesses whether this modification results in derecognition. In accordance with the Bank's policy a modification results in derecognition when it gives rise to substantially different terms. To determine if the modified terms are substantially different from the original contractual terms the Bank considers the following:

- Qualitative factors, such as contractual cash flows after modification are no longer SPPI, change in currency or change of counterparty, the extent of change in interest rates, maturity, covenants. If these do not clearly indicate a substantial modification, then;
- A quantitative assessment is performed to compare the present value of the remaining contractual cash flows under the original terms with the contractual cash flows under the revised terms, both amounts discounted at the original effective interest. If the difference in present value is material, the Bank deems the arrangement is substantially different leading to derecognition.

When the contractual terms of a financial asset are modified and the modification does not result in derecognition, the Bank determines if the financial asset's credit risk has increased significantly since initial recognition by comparing:

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

If cash flows are modified when the borrower is in financial difficulties, then the objective of the modification is usually to maximize recovery of the original contractual terms rather than to originate a new asset with substantially different terms. The revised terms usually include extending the maturity, changing the timing of interest payments and amending the terms of loan covenants.

If the Bank plans to modify a financial asset in a way that would result in forgiveness of cash flows, then it first considers whether a portion of the asset should be written off before the modification takes place. This approach impacts the result of the quantitative evaluation and means that the derecognition criteria are not usually met in such cases.

NOTES TO THE FINANCIAL STATEMENTS (continued)

2. ACCOUNTING POLICIES (continued)

2.2. Summary of significant accounting policies (continued)

Financial Assets (continued)

f) Modification of financial assets (continued)

If the credit risk remains significantly higher than what was expected at initial recognition, the loss allowance will continue to be measured at an amount equal to lifetime ECL. The loss allowance on forborne loans will generally only be measured based on 12-month ECL when there is evidence of the borrower's improved repayment behavior following modification leading to a reversal of the previous significant increase in credit risk.

If the modification of a financial asset measured at amortized cost or FVOCI does not result in derecognition of the financial asset, then the Bank first recalculates the gross carrying amount of the financial asset using the original effective interest rate of the asset and recognizes the resulting adjustment as a modification gain or loss in the statement of profit or loss. Then the Bank measures ECL for the modified asset, where the expected cash flows arising from the modified financial asset are included in calculating the expected cash shortfalls from the original asset. For floating-rate financial assets, the original effective interest rate used to calculate the modification gain or loss is adjusted to reflect current market terms at the time of the modification. Any costs or fees incurred and fees received as part of the modification adjust the gross carrying amount of the modified financial asset and are amortized over the remaining term of the modified financial asset.

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

g) Derecognition of financial assets

The Bank derecognizes a financial asset only when the contractual rights to the asset's cash flows expire (including expiry arising from a modification with substantially different terms), or when the financial asset and substantially all the risks and rewards of ownership of the asset are transferred to another entity. If the Bank neither transfers nor retains substantially all the risks and rewards of ownership and continues to control the transferred asset, the Bank recognizes its retained interest in the asset and an associated liability for amounts it may have to pay. If the Bank retains substantially all the risks and rewards of ownership of a transferred financial asset, the Bank continues to recognize the financial asset and also recognizes a collateralized borrowing for the proceeds received.

In the case where the financial asset is derecognized, the loss allowance for ECL is premeasured at the date of derecognition to determine the net carrying amount of the asset at that date. The difference between this revised carrying amount and the fair value of the new financial asset with the new terms will lead to a gain or loss on derecognition. The new financial asset will have a loss allowance measured based on 12-month ECL except in the rare occasions where the new loan is considered to be originated credit impaired. This applies only in the case where the fair value of the new loan is recognized at a significant discount to its revised par amount because there remains a high risk of default which has not been reduced by the modification. The Bank monitors credit risk of modified financial assets by evaluating qualitative and quantitative information, such as if the borrower is in past due status under the new terms.

On derecognition of a financial asset in its entirety, the difference between the carrying amount allocated to the part that is no longer recognized and the sum of the consideration received for the part no longer recognized and any cumulative gain / loss allocated to it that had been recognized in OCI is recognized in the income statement.

NOTES TO THE FINANCIAL STATEMENTS (continued)

2. ACCOUNTING POLICIES (continued)

2.2. Summary of significant accounting policies (continued)

Financial liabilities

a) Classification

The Bank classifies its financial liabilities at amortized cost.

Financial liabilities at amortized cost

Financial liabilities, including deposits and borrowings, are initially measured at fair value, net of transaction costs. These financial liabilities are subsequently measured at amortized cost using the effective interest method.

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

b) Modification of financial liabilities

The Bank accounts for substantial modification of terms of an existing liability or part of it as an extinguishment of the original financial liability and the recognition of a new liability. It is assumed that the terms are substantially different if the discounted present value of the cash flows under the new terms, including any fees paid net of any fees received and discounted using the original effective rate is materially different from the discounted present value of the remaining cash flows of the original financial liability.

In this case, a new financial liability based on the modified terms is recognized at fair value. The difference between the carrying amount of the financial liability derecognized and consideration paid is recognized in the income statement. Consideration paid includes non-financial assets transferred, if any, and the assumption of liabilities, including the new modified financial liability.

If the modification of a financial liability is not accounted for as derecognition, then the amortized cost of the liability is recalculated by discounting the modified cash flows at the original effective interest rate and the resulting gain or loss is recognized in the income statement. For floating-rate financial liabilities, the original effective interest rate used to calculate the modification gain or loss is adjusted to reflect current market terms at the time of the modification.

Any costs and fees incurred are recognized as an adjustment to the carrying amount of the liability and amortized over the remaining term of the modified financial liability by re-computing the effective interest rate on the instrument.

c) Derecognition of financial liabilities

The Bank derecognizes financial liabilities when, and only when, the Bank’s obligations are discharged, cancelled or have expired. The difference between the carrying amount of the financial liability derecognized and the consideration paid and payable is recognized in the income statement.

When the Bank exchanges with the existing lender one debt instrument into another one with substantially different terms, such exchange is accounted for as an extinguishment of the original financial liability and the recognition of a new financial liability.

NOTES TO THE FINANCIAL STATEMENTS (continued)

2. ACCOUNTING POLICIES (continued)

2.2. Summary of significant accounting policies (continued)

Financial liabilities (continued)

Guarantees

In the ordinary course of business, the Bank gives financial guarantees, consisting of letters of credit, guarantees and acceptances. Financial guarantees represent irrevocable assurances to make payments in the event that a customer cannot meet its obligations to third parties, and carry the same credit risk as loans. Financial guarantees and commitments to provide a loan are initially recognized at their fair value, which is normally evidenced by the amount of fees received. This amount is amortized on a straight line basis over the life of the commitment.

Derivative financial instruments

a) Classification

The Bank enters into derivative financial instruments including forwards, futures and swaps in the foreign exchange and interest rate markets.

b) Initial and subsequent measurement

In the normal course of business, the fair value of a derivative on initial recognition is the transaction price. Subsequent to initial recognition, derivative financial instruments are stated at fair values. Fair values are generally obtained by reference to quoted market prices in active markets, or by using valuation techniques when an active market does not exist.

The positive mark to market values (unrealised gains) of derivative financial instruments is included in other assets. The negative mark to market values (unrealised losses) of derivative financial instruments is included in other liabilities.

Hedging instruments

As part of its asset and liability management, the Bank uses derivatives for hedging purpose.
When derivatives are designated as hedges, the Bank classifies them as fair value hedges which hedge the change in the fair value of recognized assets or liabilities.

Hedge accounting is applied to derivatives designated as hedging instruments in fair value.

<u>Hedge accounting:</u>

Hedge documentation
At the inception of the hedge, formal documentation of the hedge relationship must be established. The hedge documentation prepared at the inception of the hedge must include a description of the following:

- The Banks's risk management objective and strategy for undertaking the hedge;
- The nature of risk being hedged;
- Clear identification of the hedged item and the hedging instrument; and
- How the Bank will assess the effectiveness of the hedging relationship on an ongoing basis.

NOTES TO THE FINANCIAL STATEMENTS (continued)

2. ACCOUNTING POLICIES (continued)

2.2. Summary of significant accounting policies (continued)

Hedging instruments (continued)

Hedge accounting: *(continued)*

Hedge effectiveness testing

The hedge is regarded as highly effective if both of the following conditions are met:

- At the inception of the hedge and in subsequent periods, the hedge is expected to be highly effective in offsetting the changes in fair value of the hedging instruments with corresponding changes in the hedged risk and should be reliably measurable; and
- The actual results of the hedge effectiveness testing are within a range of 80 to 125 percent.

Fair value hedge

Fair value hedges modify exposure to changes in a fixed rate instrument's fair value caused by changes in interest rates. These hedges economically convert fixed rate assets and liabilities to floating rate. The interest rate swaps are being used to hedge interest rate risk.

Any fixed rate assets or liabilities that are part of a hedging relationship are adjusted for the change in value of the risk being hedged. To the extent that the change in the fair value of the derivative does not offset changes in the fair value of the hedged item for the risk being hedged, the net amount (hedge ineffectiveness) is recorded directly in non-interest revenue, other, in Income statement.

Discontinuance of hedge accounting

The hedge accounting is discontinued when a hedging instrument expires or is sold, or when a hedge no longer meets the criteria for hedge accounting. At that point of time, any cumulative gain or loss on the hedging instrument that has been recognized in OCI remains in other comprehensive income until the forecast transaction occurs. When a forecast transaction is no longer expected to occur, the cumulative gain or loss that was reported in other comprehensive income is immediately transferred to the income statement.

Hedges that do not qualify for hedge accounting

For hedges that do not qualify for hedge accounting, any gains or losses arising from changes in the fair value of the hedging instrument are taken directly to the income statement.

Due from banks

Amounts due from banks are initially recognized at fair value and subsequently measured at amortized cost less allowance for expected credit loss, if any.

Loans and advances

Loans and advances are initially measured at fair value plus incremental direct transaction costs less ECL, and subsequently measured at their amortized cost using the effective interest method.

The effective interest rate is the rate that exactly discounts estimated future cash flow through the expected life of the financial asset or liability.

Investment securities

The 'investment securities' caption in the statement of financial position includes debt securities measured at FVOCI. For debt securities measured at FVOCI, gains and losses are recognized in OCI.

NOTES TO THE FINANCIAL STATEMENTS (continued)

2. ACCOUNTING POLICIES (continued)

2.2. Summary of significant accounting policies (continued)

Acceptances

Acceptances arise when the Bank is under an obligation to make payments against documents drawn under letters of credit. Acceptances specify the amount of money, the date and the person to which the payment is due. After acceptance, the instrument becomes an unconditional liability (time draft) of the Bank and is therefore recognised as a financial liability in the statement of financial position with a corresponding contractual right of reimbursement from the customer recognized as a financial asset.

Acceptances have been considered within the scope of IFRS 9 - Financial Instruments for the purpose of calculation of expected credit loss and are valued at amortized cost and continued to be recognised as a financial liability in the statement of financial position with a contractual right of reimbursement from the customer as a financial asset.

Offsetting financial instruments

Financial assets and financial liabilities are offset and the net amount reported in the statement of financial position if, and only if, there is a legally enforceable right to set off the recognized amounts and there is an intention to settle on a net basis, or to realize the asset and settle the liability simultaneously. This is not generally the case with master netting agreements, therefore, the related assets and liabilities are presented gross in the statement of financial position.

Cash and cash equivalents

For the purpose of the statement of cash flows, cash and cash equivalents include cash on hand, balance in current and call accounts and placements with original maturity of less than three months and insignificant credit risk excluding the statutory deposit required to be maintained with the UAE Central Bank.

Taxation

Provision for taxation is made in respect of the Bank's operations in the Emirate of Dubai whereby tax is payable at the rate of 20% of the adjusted net profit generated during the year in accordance with the relevant legislation of the Emirate of Dubai.

Deferred tax

Deferred tax is provided on temporary differences at the statement of financial position date between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes.

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply in the year when the asset is realized or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted at the statement of financial position date

Deferred tax related to fair value re-measurement of financial instruments designated at FVOCI, which is recognised in other comprehensive income, is also recognised in the other comprehensive income.

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

NOTES TO THE FINANCIAL STATEMENTS (continued)

2. ACCOUNTING POLICIES (continued)

2.2. Summary of significant accounting policies (continued)

Revenue recognition

Interest income and expense

Interest income and expense for all interest bearing financial instruments except at FVTPL, are presented in 'interest income' and 'interest expense' in the income statement on an accrual basis using the effective interest rates of the financial assets or financial liabilities to which they relate.

Fee and commission

Fee income, which is not an integral part of the effective interest rate of a financial instrument, is earned from a diverse range of services provided by the Bank to its customers and are accounted for in accordance with IFRS 15 'Revenue from Contracts with Customers'. Under the IFRS 15, fee income is measured by the Bank based on the consideration specified in a contract with a customer and excludes amounts collected on behalf of third parties. The Bank recognizes revenue when it transfers control over a product or service to a customer.

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

Fee income is accounted for as follows:

- income earned on the execution of a significant act is recognized as revenue when the act is completed (for example, fees arising from negotiating, or participating in the negotiation of a transaction for a third-party, such as an arrangement for the acquisition of shares or other securities);
- income earned from the provision of services is recognized as revenue as the services are provided; and
- other fees and commission income and expense are recognized as the related services are performed or received.

Fee income which forms an integral part of the effective interest rate of a financial instrument is recognized as an adjustment to the effective interest rate and recorded in 'Interest income'.

Foreign currency translation

Functional and presentation currency

The financial statements are presented in United Arab Emirates Dirhams (AED), which is the Bank's functional and presentation currency, rounded to the nearest thousands, unless otherwise stated.

Foreign exchange gains and losses

The carrying amount of financial assets that are denominated in a foreign currency is determined in that foreign currency and translated at the spot rate at the end of each reporting period.

NOTES TO THE FINANCIAL STATEMENTS (continued)

2. ACCOUNTING POLICIES (continued)

2.2 Summary of significant accounting policies (continued)

Foreign currency translation (continued)

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

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

Borrowings, customer deposits and due to other banks
Borrowings are recognized initially at fair value, being their issue proceeds (fair value of consideration received), net of transaction costs incurred. Borrowings are subsequently stated at amortized cost; any difference between proceeds net of transaction costs and the redemption value is recognized in the income statement over the period of the borrowings using the EIR.

Employees' end of service benefits
With respect to its UAE national employees, the Bank makes contributions to a pension fund established by the General Pension and Social Security Authority calculated as a percentage of employees' salaries. The Bank's obligations are limited to these contributions, which are expensed when due.

The Bank provides end of service benefits to its expatriate employees. The entitlement to these benefits is usually based upon the employees' length of service and the completion of a minimum service period. The expected costs of these benefits are accrued over the period of employment and are not less than the liability arising under the UAE Labor Laws.

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

Property and equipment
Property and equipment are stated at cost less accumulated depreciation and impairment losses, if any. Cost includes expenditure that is directly attributable to the acquisition of the items plus their incidental costs. Depreciation is computed on the straight line method at rates calculated to reduce the cost of assets to their estimated residual values over their expected useful live.

	Years
Furniture and fixtures	10
Office Equipment	5
Computer and accessories	4
Motor vehicles	4
Right-of-use assets	3

NOTES TO THE FINANCIAL STATEMENTS (continued)

2. ACCOUNTING POLICIES (continued)

2.2. Summary of significant accounting policies (continued)

Property and equipment (continued)

Gains and losses on disposals are determined by comparing proceeds with the carrying amount. These are included in other income in the income statement.

Where the carrying amount of an asset is greater than its estimated recoverable amount, it is written down immediately to its recoverable amount being the higher of the net selling price and value in use.

The assets' residual values, useful lives and methods of depreciation are reviewed at each financial year end, and adjusted prospectively, if required.

Lease

At inception of a contract, the Bank assesses whether a contract is, or contains, a lease. 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. To assess whether a contract conveys the right to control the use of an identified asset, the Bank uses the definition of a lease in IFRS 16.

At commencement or on modification of a contract that contains a lease component, the Bank allocates consideration in the contract to each lease component on the basis of its relative standalone price.

The Bank recognises a right-of-use asset and a lease liability at the lease commencement date. The right-of-use asset is initially measured at cost, which comprises the initial amount of the lease liability adjusted for any lease payments made at or before the commencement date, plus any initial direct costs incurred and an estimate of costs to dismantle and remove any improvements made to branches or office premises.

The right-of-use asset is subsequently depreciated using the straight-line method from the commencement date to the end of the lease term. In addition, the right-of-use asset is periodically reduced by impairment losses, if any, and adjusted for certain remeasurements of the lease liability.

The lease liability is initially measured at the present value of the lease payments that are not paid at the commencement date, discounted using the interest rate implicit in the lease or, if that rate cannot be readily determined, the Bank's incremental borrowing rate. Generally, the Bank uses its incremental borrowing rate as the discount rate.

The Bank determines its incremental borrowing rate by analysing its borrowings from various external sources and makes certain adjustments to reflect the terms of the lease and type of asset leased.

Lease payments included in the measurement of the lease liability comprise the following:

- fixed payments, including in-substance fixed payments;
- variable lease payments that depend on an index or a rate, initially measured using the index or rate as at the commencement date;
- amounts expected to be payable under a residual value guarantee; and
- the exercise price under a purchase option that the Bank is reasonably certain to exercise, lease payments in an optional renewal period if the Bank is reasonably certain to exercise an extension option, and penalties for early termination of a lease unless the Bank is reasonably certain not to terminate early.

NOTES TO THE FINANCIAL STATEMENTS (continued)

2. ACCOUNTING POLICIES (continued)

2.2. Summary of significant accounting policies (continued)

Lease (continued)

The lease liability is measured at amortised cost using the effective interest method. It is remeasured when there is a change in future lease payments arising from a change in an index or rate, if there is a change in the Bank's estimate of the amount expected to be payable under a residual value guarantee, if the Bank changes its assessment of whether it will exercise a purchase, extension or termination option or if there is a revised in-substance fixed lease payment.

When the lease liability is remeasured in this way, a corresponding adjustment is made to the carrying amount of the right-of-use asset, or is recorded in income statement if the carrying amount of the right-of-use asset has been reduced to zero.

The Bank presents right-of-use assets in 'property and equipment' and lease liabilities in 'Other liabilities' in the statement of financial position.

The Bank has elected not to recognise right-of-use assets and lease liabilities for leases of low-value assets and short-term leases. The Bank recognises the lease payments associated with these leases as an expense on a straight-line basis over the lease term.

The Bank does not have any lease arrangements in which it acts as a lessor.

Impairment of non-financial assets

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

Recoverable amount is the higher of fair value less costs to sell and value in use. If the recoverable amount of an asset (or cash-generating unit) is estimated to be less than its carrying amount, the carrying amount of the asset (or cash-generating unit) is reduced to its recoverable amount. An impairment loss is recognized immediately in income statement.

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

Interest Rate Benchmark Reform

Interbank offered rates ("IBORs"), such as the London Interbank Offered Rate ("LIBOR"), plays a critical role in global financial markets, serving as reference rates for derivatives, loans and securities, and as parameters in the valuation of financial instruments.

NOTES TO THE FINANCIAL STATEMENTS (continued)

2. ACCOUNTING POLICIES (continued)

2.2. Summary of significant accounting policies (continued)

Interest Rate Benchmark Reform (continued)

Uncertainty surrounding the integrity of IBOR rates has in recent years, led regulators, central banks and market participants to work towards a transition to alternative risk-free benchmark reference rates ("RFRs") and market-led working groups in respective jurisdictions have recommended alternative risk-free reference rates, which are gradually being adopted.

The majority of market LIBOR and other IBOR rates were discontinued after 31 December 2021 and replaced with certain Alternative Reference Rates ("ARRs"), with the exception of certain USD LIBOR rates where cessation is delayed until 30 June 2023. The transition away from the IBORs covers most of the business units and support functions of the Bank.

The Bank monitors the progress of transition from IBORs to new benchmark rates by reviewing the amounts of contracts that have yet to transition to an alternative benchmark rate. The Bank considers that a contract is not yet transitioned to an alternative benchmark rate (and referred to as an 'unreformed contract') when interest under the contract is indexed to a benchmark rate that is still subject to IBOR reform, even if it includes a fallback clause that deals with the cessation of the existing IBOR.

The Bank holds derivatives in its trading book and as hedging instruments. The Bank's exposure to US Dollar LIBOR transactions designated in hedge accounting relationships as at 31 December 2021 represents a notional amount of USD 90 million. There were no items designated in hedging relationships with exposures to other LIBOR rates.

New standards and interpretations not yet adopted

A number of new standards and amendments to standards are effective for annual periods beginning after 1 January 2022 and earlier application is permitted; however, the Bank has not early adopted them in preparing these financial statements.
The following amended standards are not expected to have a significant impact on the Bank's financial statements.

- Amendments to IAS 16 Property, plant and equipment relating to proceeds before intended use
- Amendment to IAS 37 Provisions, Contingent Liabilities and Contingent Assets relating to onerous contracts.
- Annual improvements to IFRS standards 2018 - 2020 1 January 2022
- Amendments to IAS 8 Accounting policies, Changes in accounting estimates and errors
- Amendments to IAS 1 Presentation of Financial Statements relating to classification of Liabilities as Current or Non-Current

3. FINANCIAL RISK MANAGEMENT

The Bank's activities expose it to a variety of financial risks and those activities involve the analysis, evaluation, acceptance and management of some degree of risk or combination of risks. Taking risk is core to the financial business, and the operational risks are an inevitable consequence of being in business. The Bank's aim is therefore to achieve an appropriate balance between risk and return and minimize potential adverse effects on the Bank's financial performance.

The Bank's risk management policies as approved by the Head Office are designed to identify and analyze these risks, to set appropriate risk limits and controls, and to monitor the risks and adherence to limits by means of reliable and up-to-date information systems. The Bank regularly reviews its risk management policies and systems. These policies provide written principles for overall risk management, as well as

NOTES TO THE FINANCIAL STATEMENTS (continued)

3. FINANCIAL RISK MANAGEMENT (continued)

specific areas, such as foreign exchange risk, interest rate risk, credit risk, use of derivative financial instruments and non-derivative financial instruments. In addition, internal audit is responsible for the independent review of risk management and the control environment.

The most important types of risk are credit risk, market risk, liquidity risk, and other operational risk. Market risk includes currency risk, interest rate and other price risk.

3.1 Risks relating to the impact of COVID - 19

On 11 March 2020, the World Health Organisation ("WHO") officially declared COVID-19 a global pandemic. In light of the rapid spread of COVID-19 across the globe, various economies and sectors have faced significant disruptions and uncertainty as a result of measures taken by governments to contain or delay the spread of the virus.

The COVID-19 pandemic has had, and continues to have, a material impact on businesses around the world and the economic environments in which they operate. There are a number of factors associated with the pandemic and its impact on global economies that could have a material adverse effect on (among other things) the profitability, capital and liquidity of financial institutions such as Bank Alfalah Limited – Dubai Branch. As such, the COVID-19 has a potential impact on more than one principal risk.

In latest development UAE Central Bank extended banks' capital buffers and liquidity and stable funding requirements until June 30, 2022, under the Targeted Economic Support Scheme (TESS) to aid balance and sustained recovery in the banking sector and as well the overall economy of the country.

Although the Bank has identified the most vulnerable sectors to this stressed situation in response to the COVID-19 outbreak (real estate and others) but none of the borrowers of the Bank requested for any relief under TESS scheme of the Central Bank.

3.2. Credit risk

The Bank takes on exposure to credit risk, which is the risk that a counter party will cause financial loss to the Bank by failing to discharge an obligation. Significant changes in the economy, or in the health of a particular industry segment that represents a concentration in the Bank's portfolio, could result in losses that are different from those provided for at the reporting date. Management therefore carefully manages its exposure to credit risk. Credit exposures arise principally in loans and advances, due from other banks, investment securities and other receivables. There is also credit risk in financial arrangements not reflected on the statement of financial position such as credit commitments.

Internal credit risk ratings

In order to minimize credit risk, the Bank maintains the Bank's credit risk grading to categories exposures according to their degree of risk of default. The Bank's credit risk grading framework comprises various categories. The credit rating information is based on a range of data that is determined to be predictive of the risk of default and applying experienced credit judgement. The nature of the exposure and type of borrower are taken into account in the analysis. Credit risk grades are defined using qualitative and quantitative factors that are indicative of risk of default.

NOTES TO THE FINANCIAL STATEMENTS (continued)

3. FINANCIAL RISK MANAGEMENT (continued)

3.2. Credit risk (continued)

Internal credit risk ratings (continued)

The Bank measures credit risk of loans and advances to customers and to financial institutions at a counterparty level by using an internally developed technique named “Obligor Risk Rating” (ORR) considering various factors over a scale of 1 to 12 points. The better the customer credit strength the lower is the grade. This credit risk measurement technique is embedded in the Bank’s daily operational management.

Classification	Grades	Risk significance
Performing	1 – 9a	Exceptional
Performing	9b	Watchlist
Non-performing	10	Substandard
Non-performing	11	Doubtful
Non-performing	12	Loss

Measurement of ECL

The Bank measures ECL considering the risk of default over the maximum contractual period over which the entity is exposed to credit risk. However, for financial instruments such as overdraft facilities that include both a loan and an undrawn commitment component, the Bank's contractual ability to demand repayment and cancel the undrawn commitment does not limit the Bank’s exposure to credit losses to the contractual notice period. For such financial instruments the Bank measures ECL over the period that it is exposed to credit risk and ECL would not be mitigated by credit risk management actions. These financial instruments do not have a fixed term or repayment structure and have a short contractual cancellation period.

However, the Bank does not enforce in the normal day-to-day management the contractual right to cancel these financial instruments. This is because these financial instruments are managed on a collective basis and are canceled only when the Bank becomes aware of an increase in credit risk at the facility level. This longer period is estimated taking into account the credit risk management actions that the Bank expects to take to mitigate ECL, e.g. reduction in limits or cancellation of the loan commitment. The maximum contractual period extends to the date at which the Bank has the right to require repayment of an advance or terminate a loan commitment or guarantee.

Restructured and renegotiated loans

Loans with renegotiated terms are defined as loans that have been restructured due to a deterioration in the borrower's financial position, for which the Bank has made concessions by agreeing to terms and conditions that are more favorable for the borrower than the Bank had provided initially and that it would not otherwise consider. A loan continues to be presented as part of loans with renegotiated terms until maturity, early repayment or write-off. Management continuously monitors the progress on renegotiated loans (if any) to ensure compliance with the terms at all times.

NOTES TO THE FINANCIAL STATEMENTS (continued)

3. FINANCIAL RISK MANAGEMENT (continued)

3.2. Credit risk (continued)

Exposure to credit risk

The Bank measures its exposure to credit risk by reference to gross carrying amount of financial assets less interest suspended and expected credit allowances, if any.

As at 31 December 2021

	Stage 1	Stage 2	Stage 3	Total
Loans and advances	--------------- AED'000 ---------------			
Performing	**91,863**	**-**	**-**	**91,863**
Non-performing	**-**	**-**	**-**	**-**
Allowance for expected credit loss	**(338)**	**-**	**-**	**(338)**
Net carrying amount	**91,525**	**-**	**-**	**91,525**
Unfunded advances	**14,824**	**-**	**-**	**14,824**
Allowance for expected credit loss	**(10)**	**-**	**-**	**(10)**
Net carrying amount	**14,814**	**-**	**-**	**14,814**

	Stage 1	Stage 2	Stage 3	Total
Debt securities	--------------- AED'000 ---------------			
Measured at FVOCI	**445,530**	**-**	**-**	**445,530**
Allowance for expected credit loss	**(778)**	**-**	**-**	**(778)**
Net carrying amount	**444,752**	**-**	**-**	**444,752**

As at 31 December 2020

	Stage 1	Stage 2	Stage 3	Total
Loans and advances	--------------- AED'000 ---------------			
Performing	57,295	-	-	57,295
Non-performing	-	-	-	-
Allowance for expected credit loss	(269)	-	-	(269)
Net carrying amount	57,026	-	-	57,026
Unfunded advances	42,471	-	-	42,471
Allowance for expected credit loss	(86)	-	-	(86)
Net carrying amount	42,385	-	-	42,385

	Stage 1	Stage 2	Stage 3	Total
Debt securities	--------------- AED'000 ---------------			
Measured at FVOCI	342,414	-	-	342,414
Allowance for expected credit loss	(402)	-	-	(402)
Net carrying amount	342,012	-	-	342,012

Loans and advances, amounts due from other banks and amounts due from the Head Office and other branches are neither past due nor impaired.

NOTES TO THE FINANCIAL STATEMENTS (continued)

3. FINANCIAL RISK MANAGEMENT (continued)

3.2. Credit risk (continued)

Risk limit control and mitigation policies

The Bank manages limits and controls concentrations of credit risk wherever they are identified in particular, to individual counterparties and groups, and to industries and countries.

The credit risk is primarily managed by placing limits on the amount of risk accepted in relation to one borrower or groups of borrowers and to geographical and industry segments. Such risks are monitored on a revolving basis and subject to an annual or more frequent review.

Exposure to credit risk is also managed through regular analysis of the ability of borrowers and potential borrowers to meet interest and principal repayment obligations and by changing the lending limits where appropriate. Some other specific control and mitigation measures are outlined below.

(a) **Collateral**

As part of the Bank's credit risk management policies and practices, it obtains security where deemed necessary for loans and advances. The principal collateral types include:

- Mortgages over residential and commercial properties;
- Charges over business assets such as premises, inventory and accounts receivable;
- Charges over financial instruments such as debt securities and equities;
- Personal and corporate guarantees; and
- Cash held in margin accounts and liens.

Longer-term finance and lending to corporate entities are generally secured; revolving individual credit facilities are generally unsecured. In addition, in order to minimize the credit loss the Bank obtains additional collaterals from the counterparty as soon as impairment indicators are observed for the relevant loans and advances.

Collaterals held as security for financial assets other than loans and advances are determined by the nature of the instrument. Debt securities, treasury and other eligible bills are generally unsecured.

The Bank seeks to use collateral, where possible, to mitigate its risks on financial assets. The collateral comes in various forms such as cash, securities, letters of credit/guarantees, real estate, receivables, inventories, other non-financial assets and credit enhancements such as netting agreements. The fair value of collateral is generally assessed, at a minimum, at inception and based on the Bank's reporting schedule, however, some collateral, for example, cash or securities relating to margining requirements, is valued daily. To the extent possible, the Bank uses active market data for valuing financial assets, held as collateral. Other financial assets which do not have a readily determinable market value are valued using models. Non-financial collateral, such as real estate, is valued based on data provided by third parties such as mortgage brokers, housing price indices, audited financial statements, and other independent sources.

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

	2021	*2020*
	AED'000	*AED'000*
Cash Margin and Liens	**9,008**	23,388
Guarantee	**2,850**	16,747
Mortgage	**4,758**	8,020
	16,616	48,155

NOTES TO THE FINANCIAL STATEMENTS (continued)

3. FINANCIAL RISK MANAGEMENT (continued)

3.2. Credit risk (continued)

Risk limit control and mitigation policies (continued)

(b) **Derivatives**

At any one time, the amount subject to credit risk is limited to the current fair value of instruments that are favorable to the Bank, which in relation to derivatives is only a small fraction of the contract, or notional values used to express the volume of instruments outstanding. This credit risk exposure is managed as part of the overall lending limits with customers, together with potential exposures from market movements and entering into forward contracts with other banks, which forms as a back to back commitment to purchase and sell a contract, resulting in limited credit exposure to the Bank.

Collateral margin is also maintained with counter parties in accordance with the International Swaps & Derivatives Association (ISDA) Master Agreement, in line with the minimum requirements of the derivative contracts. Due to change in MTM revaluation, margin call payments are called to pay to bridge the market value with the agreed transaction deal.

Net exposure to credit risk before collateral held or other credit enhancements

	Maximum exposure	
	2021	*2020*
	AED '000	*AED '000*
Credit risk exposures relating to assets reflected on and off statement of financial position are as follows:		
Balances with the UAE Central Bank	**123,759**	46,846
Due from other banks	**42,471**	15,134
Loans and advances		
- Corporate loans	**91,525**	57,026
Investment securities	**445,530**	342,414
Other assets	**6,185**	7,977
Unfunded advances	**14,814**	42,385
At 31 December 2021	**724,284**	511,782

The above table represents a worst case scenario of credit risk exposure to the Bank, without taking account of any collateral held or other credit enhancements attached. For assets reflected on the statement of financial position, the exposures set out above are based on net amounts.

Management is confident in its ability to continue to control and sustain minimal exposure of credit risk to the Bank resulting from both its loans and advances portfolio and debt securities.

Repossessed assets

The Bank's policy is to determine whether a repossessed asset is best used for its internal operations or should be sold. Assets determined to be useful for the internal operations are transferred to their relevant asset category at the lower of their repossessed value or the carrying value of the original secured asset. Assets that are determined to be sold are immediately transferred to assets held for sale at their fair value at the repossession date in line with the Bank's policy.

NOTES TO THE FINANCIAL STATEMENTS (continued)

3. FINANCIAL RISK MANAGEMENT (continued)

3.2. Credit risk (continued)

Risk limit control and mitigation policies (continued)

Investment securities

Investment securities mainly comprise of debt securities issued by various governments and local / foreign reputable organizations.

The table below presents an analysis of investment securities by rating agency designation, based on Moody's ratings or equivalent:

	2021	*2020*
	AED '000	*AED '000*
AAA to A-	**263,991**	210,470
BBB to B-	**174,079**	124,495
Unrated – sovereign	**7,460**	7,449
Total	**445,530**	342,414

Impairment reserve under the Central Bank of UAE (CBUAE) guidance

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

Pursuant to clause 6.4 of the guidance, the reconciliation between general and specific provision under Circular 28/2010 of CBUAE and IFRS 9 is as follows:

	2021	*2020*
	AED '000	*AED '000*
Allowances for impairment losses: General		
General provisions under Circular 28/2010 of CBUAE	**4,373**	2,479
Less: Stage 1 and Stage 2 provisions under IFRS 9	**(1,126)**	(757)
General provision transferred to the regulatory credit risk reserve	**3,247**	1,722
Allowances for impairment losses: Specific		
Specific provisions under Circular 28/2010 of CBUAE	**-**	-
Less: Stage 3 provisions under IFRS 9	**-**	-
Specific provision transferred to the impairment reserve	**-**	-
Total provision retained in the regulatory credit risk reserve	**3,247**	1,722

Concentration of risks of financial assets with credit risk exposure

The following tables summaries the Bank's main credit exposure at their carrying amounts as categorized by the industry sectors of its counterparties.

NOTES TO THE FINANCIAL STATEMENTS (continued)

3. FINANCIAL RISK MANAGEMENT (continued)

3.2. Credit risk (continued)

Concentration of risks of financial assets with credit risk exposure (continued)

	Financial institutions	*Textile*	*Construction & real estate*	*Public sector*	*Wholesale & retail trade*	*Other industries*	**Individ-uals**	**Total**
	AED '000							
Balances with the Central Bank of UAE	123,759	-	-	-	-	-	-	123,759
Due from other banks	42,471	-	-	-	-	-	-	42,471
Lending to Financial Institutions	-	-	-	-	-	-	-	-
Loans and advances								
- Corporate loans	79,740	-	7,310	-	-	4,475	-	91,525
Investment securities	199,757	-	-	245,773	-	-	-	445,530
Other assets	4,638	-	35	1,237	-	632	-	6,542
As at 31 December 2021	450,365	-	7,345	247,010	-	5,107	-	709,827

	Financial institutions	*Textile*	*Construction & real estate*	*Public sector*	*Wholesale & retail trade*	*Other industries*	**Individ -uals**	**Total**
	AED '000							
Balances with the Central Bank of UAE	46,846	-	-	-	-	-	-	46,846
Due from other banks	15,134	-	-	-	-	-	-	15,134
Loans and advances								
- Corporate loans	39,000	-	10,962	-	-	7,064	-	57,026
Investment securities	154,363	-	-	188,051	-	-	-	342,414
Other assets	6,841	-	23	1,101	-	12	-	7,977
As at 31 December 2020	**262,184**	-	**10,985**	**189,152**	-	**7,076**	-	**469,397**

The following table breaks down the Bank's main credit exposure at their carrying amounts, as categorized by geographical region as of the year-end.

For this table, the Bank has allocated exposures to regions based on the country of domicile of its counterparties:

NOTES TO THE FINANCIAL STATEMENTS (continued)

3. FINANCIAL RISK MANAGEMENT (continued)

3.2. Credit risk (continued)

Concentration of risks of financial assets with credit risk exposure (continued)

	UAE	***OECD***	***Other Asian Countries***	***Others***	***Total***
			AED '000		
31 December 2021					
Balances with the UAE Central Bank	123,759	-	-	-	123,759
Due from other banks	50	42,421	-	-	42,471
Loans and advances:					
- Corporate loans	11,785	-	79,740	-	91,525
Investment securities	206,309	17,432	160,719	61,070	445,530
Other assets	4,578	66	1,479	419	6,542
	346,481	**59,919**	**241,938**	**61,489**	**709,827**

	UAE	*OECD*	*Other Asian Countries*	*Others*	*Total*
			AED '000		
31 December 2020					
Balances with the UAE Central Bank	46,846	-	-	-	46,846
Due from other banks	50	15,084	-	-	15,134
Loans and advances:					-
- Corporate loans	18,026	-	39,000	-	57,026
Investment securities	184,400	17,972	135,873	4,169	342,414
Other assets	6,874	66	1,010	27	7,977
	256,196	33,122	175,883	4,196	469,397

OECD represents Organization for Economic Corporation and Development. This includes United States, Canada, Australia, Japan, United Kingdom, Turkey and other European countries.

NOTES TO THE FINANCIAL STATEMENTS (continued)

3. FINANCIAL RISK MANAGEMENT (continued)

3.3 Market risk

The Bank takes exposure on market risks, which is the risk that the fair value of future cash flows of a financial instrument will fluctuate because of changes in market prices. Market risks arise from open positions in interest rate, currency and equity instruments, all of which are exposed to general and specific market movements and changes in the level of volatility of market rates or prices such as interest rates, credit spreads, foreign exchange rates and equity prices.

The Bank's Assets and Liability Committee (ALCO) is responsible for formalizing the key financial indicators and ratios, setting the thresholds to manage and monitor the market risk and also analyzing the sensitivity of the Bank's interest rate and maturity mis-matches. ALCO also guides the Bank's investment decisions and provides guidance in terms of interest rate and currency movements.

Foreign exchange risk

The Bank takes exposure on the effects of fluctuations in the prevailing foreign currency exchange rates on its financial position and cash flows. The Head Office sets limits on the level of exposure by currency and in aggregate for both overnight and intra-day positions, which are monitored regularly. The table below summarizes the Bank's exposure to foreign currency exchange rate risk. Included in the table are the Bank's assets and liabilities at carrying amounts, categorized by currency.

	AED	***USD***	***EURO***	***GBP***	***Total***
	AED'000	***AED'000***	***AED'000***	***AED'000***	***AED'000***
As at 31 December 2021					
Assets					
Cash and balances with the UAE Central Bank	**124,423**	**-**	**-**	**-**	**124,423**
Due from other banks	**50**	**40,499**	**1,872**	**50**	**42,471**
Loans and advances	**7,310**	**83,815**	**400**	**-**	**91,525**
Investment securities	**-**	**428,399**	**17,131**	**-**	**445,530**
Other assets *(excluding forward foreign exchange contracts)*	**44**	**6,113**	**28**	**-**	**6,185**
Forward foreign exchange contracts	**341,207**	**(328,734)**	**(12,933)**	**-**	**(460)**
	473,034	**230,092**	**6,498**	**50**	**709,674**
Liabilities					
Customer deposits	**294,880**	**246,462**	**6,344**	**37**	**547,723**
Borrowing	**9,641**	**36,730**	**-**	**-**	**46,371**
Other liabilities	**3,948**	**4,631**	**-**	**-**	**8,579**
	308,469	**287,823**	**6,344**	**37**	**602,673**
Net financial position	**164,565**	**(57,731)**	**154**	**13**	**107,001**

NOTES TO THE FINANCIAL STATEMENTS (continued)

3. FINANCIAL RISK MANAGEMENT (continued)

3.3. Market risk (continued)

Foreign exchange risk (continued)

	AED *AED'000*	*USD* *AED'000*	*EURO* *AED'000*	*GBP* *AED'000*	*Total* *AED'000*
As at 31 December 2020					
Assets					
Cash and balances with the UAE Central Bank	47,897	-	-	-	47,897
Due from other banks	50	4,249	10,794	41	15,134
Loans and advances	10,961	45,716	349	-	57,026
Investment securities	-	335,580	6,834	-	342,414
Other assets *(excluding forward foreign exchange contracts)*	392	7,575	10	-	7,977
Forward foreign exchange contracts	207,552	(207,552)	-	-	-
	266,852	185,568	17,987	41	470,448
Liabilities					
Customer deposits	158,384	105,842	17,879	39	282,144
Borrowing	2,305	66,114	-	-	68,419
Other liabilities	2,390	8,006	-	-	10,396
	163,079	179,962	17,879	39	360,959
Net financial position	103,773	5,606	108	2	109,498

Majority of Bank's assets and liabilities are in UAE Dirham or USD (which is pegged to the UAE Dirham), the Bank is not significantly exposed to currency risk as at 31 December 2021.

Price risk

The Bank mainly holds debt securities, issued by various governments and local / foreign reputable organizations, which are carried at fair value. The Bank's exposure to price risk is dependent on the economical and political factors of these respective countries. The Bank manages the price risk through diversification and placing limits on individual and total debt securities portfolio. Reports on the debt securities portfolio are submitted to the Bank's senior management on a regular basis.

The Bank's Investment Committee reviews and approves all debt securities investment decisions. A 10% increase / decrease in value of Bank's financial assets measured at fair value through OCI will result in an increase / decrease in the Bank's equity by AED 34.24 million (2019: AED 20.59 million). Such change will have no effect on the income statement of the Bank.

Interest rate risk

Cash flow interest rate risk is the risk that the future cash flows of a floating rate assets/liabilities will fluctuate because of changes in market interest rates. Fair value interest rate risk is the risk that the fair value of fixed rate assets/liabilities will fluctuate because of changes in market interest rates. The Bank takes on exposure to the effects of fluctuations in the prevailing levels of market interest rates on both its fair value and cash flow risks. Interest margins may increase as a result of such changes but may reduce losses in the event that unexpected movements arise. The ALCO sets limits on the level of mismatch of interest rate re-pricing that may be undertaken, which is monitored daily by Treasury.

The table below summarizes the Bank's exposure to interest rate risks. It includes the Bank's assets and liabilities at carrying amounts, categorized by the earlier of contractual repricing or maturity dates.

NOTES TO THE FINANCIAL STATEMENTS (continued)

3. FINANCIAL RISK MANAGEMENT (continued)

3.3. Market risk (continued)

Interest rate risk (continued)

	Upto 3 Months	***3 months to 1 year***	***1 year to 5 years***	***Over 5 years***	***Non-interest bearing***	***Total***	***Effective interest rate***
	AED'000						***(%)***
At 31 December 2021							
Assets							
Cash and balances with the UAE Central Bank	**75,000**	**-**	**-**	**-**	**49,423**	**124,423**	**0.15%**
Due from other banks	**-**	**-**	**-**	**-**	**42,471**	**42,471**	
Loans and advances	**29,583**	**57,265**	**4,677**	**-**	**-**	**91,525**	**2.47%**
Investment securities	**2,213**	**33,464**	**225,203**	**184,650**	**-**	**445,530**	**2.32%**
Other assets	**200**	**3,405**	**1,628**	**1,309**	**-**	**6,542**	
Unfunded advances	**7,952**	**2,250**	**4,612**	**-**	**-**	**14,814**	
Total financial assets	**114,948**	**96,384**	**236,120**	**185,959**	**91,894**	**725,305**	
Liabilities							
Borrowings	**36,730**	**-**	**-**	**-**	**9,641**	**46,371**	**0.34%**
Deposits and other account	**11,602**	**55,757**	**-**	**-**	**480,364**	**547,723**	**1.45%**
Other liabilities	**7,870**	**42**	**667**	**-**	**-**	**8,579**	
Total liabilities	**56,202**	**55,799**	**667**	**-**	**490,005**	**602,673**	
Interest sensitivity gap	**58,746**	**40,585**	**235,453**	**185,959**	**(398,111)**	**122,632**	

	Upto 3 Months	3 months to 1 year	1 year to 5 years	Over 5 years	Non-interest bearing	Total	Effective interest rate
	AED'000						(%)
At 31 December 2020							
Assets							
Cash and balances with the UAE Central Bank	30,000	-	-	-	17,897	47,897	
Due from other banks	-	-	-	-	15,134	15,134	
Loans and advances	22,586	26,556	7,884	-	-	57,026	3.54%
Investment securities	-	-	224,313	118,101	-	342,414	3.25%
Other assets	448	5,150	1,849	530	-	7,977	
Total financial assets	53,034	31,706	234,046	118,631	33,031	470,448	
Liabilities							
Borrowings	66,114	-	-	-	2,305	68,419	1.04%
Deposits and other account	44,131	14,500	-	-	223,513	282,144	1.78%
Other liabilities	8,216	1,624	556	-	-	10,396	
Total liabilities	118,461	16,124	556	-	225,818	360,959	
Interest sensitivity gap	(65,427)	15,582	233,490	118,631	(192,787)	109,489	

NOTES TO THE FINANCIAL STATEMENTS (continued)

3. FINANCIAL RISK MANAGEMENT (continued)

3.3. Market risk (continued)

Interest rate risk (continued)

Interest rate risk is also assessed by measuring the impact of a reasonably possible change in interest rate movements. The Bank assumes a fluctuation in interest rates of 25 basis points (bps) and estimates the following impact on the net profit for the year and net assets at that date:

	Interest Income AED '000	***Interest Expense AED '000***
As at 31 December 2021		
Fluctuation in yield by 25 bps	**1,243**	**1,181**

	Interest Income AED '000	*Interest Expense AED '000*
As at 31 December 2020		
Fluctuation in yield by 25 bps	841	679

3.4. Liquidity risk

The interest rate sensitivities set out above are illustrative only and employ simplified scenarios. The sensitivity does not incorporate actions that could be taken by management to mitigate the effect of interest rate movements.

Liquidity risk is the risk that the Bank is unable to meet its payment obligations associated with its financial liabilities when they fall due and to replace funds when they are withdrawn. The consequence may be the failure to meet obligations to repay depositors and fulfill commitments to lend.

The Bank manages its liquidity in accordance with UAE Central Bank requirements and the Bank's internal guidelines mandated by ALCO. The UAE Central Bank has prescribed reserve requirements on deposits at 1% and 7% on time and demand deposits respectively. The UAE Central Bank also imposes mandatory 1:1 lending to stable resources ratio whereby loans and advances (combined with financial guarantees and inter-bank placements having a remaining term of greater than three months) should not exceed stable funds as defined by the UAE Central Bank. ALCO of the Bank monitors liquidity ratios on a regular basis.
The table below presents the cash flows payable by the Bank under non-derivative financial liabilities by remaining contractual maturities at the reporting date. The amounts disclosed in the table are the contractual undiscounted cash outflows based on the current applicable interest rates.

	Upto 3 Months	***3 months to 1 year***	***1 year to 5 years***	***Over 5 years***	***Total***
	- - - - - - - - - - - - - - - - AED '000 - - - - - - - - - - - - - - - -				
At 31 December 2021					
Borrowings	**46,371**	**-**	**-**	**-**	**46,371**
Deposits and other accounts	**491,966**	**55,757**	**-**	**-**	**547,723**
Other liabilities	**7,870**	**42**	**667**	**-**	**8,579**
	546,207	**55,799**	**667**	**-**	**602,673**

NOTES TO THE FINANCIAL STATEMENTS (continued)

3. FINANCIAL RISK MANAGEMENT (continued)

3.4. Liquidity risk (continued)

	Upto 3 Months	*3 months to 1 year*	*1 year to 5 years*	*Over 5 years*	*Total*
	AED '000				
At 31 December 2020					
Borrowings	68,419	-	-	-	68,419
Deposits and other accounts	267,644	14,500	-	-	282,144
Other liabilities	8,216	1,624	556	-	10,396
	344,279	16,124	556	-	360,959

Operational risk is the risk of loss arising from system failure, human error, fraud or external events. When controls fail to perform, operational risks can cause damage to reputation, have legal or regulatory implications, or lead to financial loss. The Bank cannot expect to eliminate all operational risks, but through a control framework and by monitoring and responding to potential risks, the Bank is able to manage the risks. Controls include effective segregation of duties, access, authorization, and reconciliation procedures, staff education and assessment processes, including the use of internal audit.

3.5. Operational risk

3.6. Fair value of financial assets and liabilities

Financial assets consist of cash and balances with the UAE Central Bank, balances with other banks, lendings to financial institutions, loans and advances, investment securities, accrued interest and other receivables. Financial liabilities consist of borrowings, customer deposits, accrued interest and other payables.

Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at measurement date.

The fair values of financial instruments are not materially different from their carrying values.

Analysis of financial instruments recorded at fair value by level of the fair value hierarchy.

The Bank uses the following hierarchy for determining and disclosing the fair value of financial instruments which are carried at fair value by the following valuation techniques:

Level 1: quoted (unadjusted) prices in active markets for identical assets or liabilities.
Level 2: other techniques for which all inputs which have a significant effect on the recorded fair value are observable, either directly or indirectly.
Level 3: techniques which use inputs which have a significant effect on the recorded fair value that are not based on observable market data.

As at year end, investment securities classified as FVOCI amounted to **AED 445,530** thousand mentioned in note 8 of which **AED 80,648** thousand (2020: 82,974 thousand) were falling under level 1 category and investment securities amounting to **AED 364,882** thousand (2020: 259,440 thousand) were falling under level 2 category.

During the year, there was no movement between the level 1 and level 2 of the fair value hierarchy. During the current or prior year, bank has not classified any financial instrument in level 3 of the fair value hierarchy.

NOTES TO THE FINANCIAL STATEMENTS (continued)

3. FINANCIAL RISK MANAGEMENT (continued)

3.7. Capital management

The Bank's objectives when managing capital, which is a broader concept than the 'equity' on the face of statement of financial position, are:

- To comply with the capital requirements set by the UAE Central Bank;
- To safeguard the Bank's ability to continue as a going concern and increase the returns for the shareholders; and
- To maintain a strong capital base to support the development of its business.

Capital adequacy and the use of regulatory capital are monitored on a regular basis by the Bank's management, employing techniques based on the guidelines developed by the Basel Committee and the UAE Central Bank. The required information is filed with the regulators on a quarterly and annual basis.

The UAE Central Bank issued Basel III capital regulation which came into effect from December 31, 2017, introducing minimum capital requirement at three level: common equity tier 1 (CET1, Tier 1 (T1) and Total Capital.

Minimum transitional arrangements as per UAE Central Bank are as follows:

Capital element	***2021***	*2020*
Minimum common equity tier 1 ratio	**7.00%**	7.00%
Minimum tier 1 capital ratio	**8.50%**	8.50%
Minimum capital adequacy ratio	**10.50%**	10.50%
Capital conservation buffer	**2.50%**	2.50%

The capital adequacy ratio as per Basel III framework is given below:

	2021 ***AED '000***	*2020* *AED '000*
Tier 1 capital		
Allocated capital	**100,000**	100,000
Statutory reserves	**945**	529
Retained earnings	**2,695**	3,042
Fair value and other reserves	**832**	1,908
Total Tier 1 capital	**104,472**	105,479
Tier 2 capital		
Eligible general provision	**3,166**	2,066
Total Tier 2 capital	**3,166**	2,066
Total capital base	**107,638**	107,545
Risk Weighted Assets		
Credit risk	**253,302**	165,265
Market risk	**17,101**	11,407
Operational risk	**21,098**	17,738
Total risk weighted assets	**291,501**	194,410
Capital Adequacy Ratio (%)	**36.93**	55.32
Tier 1 capital to risk weighted assets ratio (%)	**35.84**	54.26

NOTES TO THE FINANCIAL STATEMENTS (continued)

3. FINANCIAL RISK MANAGEMENT (continued)

3.8. Credit Quality Analysis

As of 31 December 2021	***Stage 1***		***Total***	
	Exposure	***ECL***	***Exposure***	***ECL***
	AED '000			
Cash and balances with the UAE Central Bank	**124,423**	**-**	**124,423**	**-**
Balances with other banks	**42,471**	**-**	**42,471**	**-**
Loans and advances	**91,863**	**(338)**	**91,863**	**(338)**
Investment securities	**445,530**	**(778)**	**445,530**	**(778)**
Other assets	**6,542**	**-**	**6,542**	**-**
Unfunded exposure	**14,824**	**(10)**	**14,824**	**(10)**
	725,653	**(1,126)**	**725,653**	**(1,126)**

As of 31 December 2020	*Stage 1*		*Total*	
	Exposure	*ECL*	*Exposure*	*ECL*
	AED '000			
Cash and balances with the UAE Central Bank	47,897	-	47,897	-
Balances with other banks	15,134	-	15,134	-
Loans and advances	57,295	(269)	57,295	(269)
Investment securities	342,414	(402)	342,414	(402)
Other assets	7,977	-	7,977	-
Unfunded exposure	42,471	(86)	42,471	(86)
	513,188	(757)	513,188	(757)

The expected credit loss against financial instruments classified as FVOCI is routed through other comprehensive income and not deducted from carrying value in the statement of financial position.

NOTES TO THE FINANCIAL STATEMENTS (continued)

3. FINANCIAL RISK MANAGEMENT (continued)

3.9. Fair value of financial instruments

As of 31 December 2021	***FVOCI - Debt instruments***	***Amortised Cost***	***Carrying Value***
		AED '000	
Financial Assets			
Cash and balances with the UAE Central Bank	**-**	**124,423**	**124,423**
Balances with other banks	**-**	**42,471**	**42,471**
Loans and advances	**-**	**91,525**	**91,525**
Investment securities	**445,530**	**-**	**445,530**
Other assets	**-**	**6,542**	**6,542**
	445,530	**264,961**	**710,491**
Financial Assets			
Borrowings	**-**	**46,371**	**46,371**
Deposits and other account	**-**	**547,723**	**547,723**
Other liabilities	**-**	**8,579**	**8,579**
	-	**602,673**	**602,673**

As of 31 December 2020	*FVOCI - Debt instruments*	*Amortised Cost*	*Carrying Value*
		AED '000	
Financial Assets			
Cash and balances with the UAE Central Bank	-	47,897	47,897
Balances with other banks	-	15,134	15,134
Loans and advances	-	57,026	57,026
Investment securities	342,414	-	342,414
Other assets	-	7,977	7,977
	342,414	128,034	470,448
Financial Assets			
Borrowings	-	68,419	68,419
Deposits and other account	-	282,144	282,144
Other liabilities	-	10,396	10,396
	-	360,959	360,959

*The carrying values of the financial assets and liabilities (that are not stated at fair value) are not significantly different to their fair values due to several factors including short term nature of the portfolio, and also no increase in risk profile of the financial instruments and the respective market rates.

NOTES TO THE FINANCIAL STATEMENTS (continued)

4. CRITICAL ACCOUNTING ESTIMATES AND JUDGMENTS

The preparation of the financial statements requires management to make estimates and assumptions that affect the application of accounting policies and reported amounts of assets, liabilities, income and expenses. Such estimates are necessarily based on assumptions about several factors involving varying degrees of judgment and uncertainty and actual results may therefore differ, resulting in future changes in these estimates.

In particular, considerable management judgment is required in respect of the following issues:

Going concern

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

Impairment of non-financial assets

The Bank assesses at each reporting date whether there is an indication that an asset may be impaired. If any indication exists, or when annual impairment testing for an asset is required, the Bank estimates the asset's recoverable amount. An asset's recoverable amount is the higher of an asset's or CGU's fair value less costs to sell and its value in use.

In assessing value in use, the estimated future cash flows are discounted to their present value using a discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. In determining fair value less costs to sell, an appropriate valuation model is used. These calculations are corroborated by other available fair value indicators.

Financial asset classification

Financial asset classification requires management to make an assessment of the business model within which the assets are held and assessment of whether the contractual terms of the financial asset are solely payments of principal and interest on the principal amount outstanding.

Significant increase in credit risk

ECL are measured as an allowance equal to 12-month ECL for Stage 1 assets, or lifetime ECL assets for Stage 2 or Stage 3 assets. An asset moves to Stage 2 when its credit risk has increased significantly since initial recognition. IFRS 9 does not define what constitutes a significant increase in credit risk. In assessing whether the credit risk of an asset has significantly increased the Bank takes into account qualitative and quantitative reasonable and supportable forward looking information.

Models and assumptions used

The Bank uses various models and assumptions in measuring fair value of financial assets as well as in estimating ECL. Judgement is applied in identifying the most appropriate model for each type of asset, as well as for determining the assumptions used in these models, including assumptions that relate to key drivers of credit risk.

NOTES TO THE FINANCIAL STATEMENTS (continued)

4. CRITICAL ACCOUNTING ESTIMATES AND JUDGMENTS (continued)

Key sources of estimation uncertainty
The following are key estimations that have been used in the process of applying the Bank's accounting policies:

- Establishing the number and relative weightings of forward-looking scenarios for each type of product / market and determining the forward looking information relevant to each scenario: When measuring ECL the Bank uses reasonable and supportable forward looking information, which is based on assumptions for the future movement of different economic drivers and how these drivers will affect each other.

- Probability of default: PD constitutes a key input in measuring ECL. PD is an estimate of the likelihood of default over a given time horizon, the calculation of which includes historical data, assumptions and expectations of future conditions.

- Loss Given Default: LGD is an estimate of the loss arising on default. It is based on the difference between the contractual cash flows due and those that the lender would expect to receive, taking into account cash flows from collateral.

5. CASH AND BALANCES WITH THE UAE CENTRAL BANK

	2021	*2020*
	AED '000	*AED '000*
Cash in hand	**664**	1,051
With the UAE Central Bank in:		
Statutory deposits	**26,177**	12,265
Current accounts	**22,582**	4,581
Overnight placement	**75,000**	30,000
	124,423	47,897

The statutory deposits with the UAE Central Bank are not available to finance the day to day operations of the Bank.

6. BALANCES WITH OTHER BANKS

	2021	*2020*
	AED '000	*AED '000*
Current accounts	**42,471**	15,134

7. LOANS AND ADVANCES – NET

	2021	*2020*
	AED '000	*AED '000*
Corporate loans	**91,863**	57,295
Less: allowance for expected credit loss	**(338)**	(269)
Net loans and advances	**91,525**	57,026

NOTES TO THE FINANCIAL STATEMENTS (continued)

7.1. Analysis of gross loans and advances

	2021	*2020*
	AED '000	*AED '000*
Term loan	**4,758**	8,020
Current Finance	**2,633**	3,078
Loans against trust receipts	**-**	7,064
Bills discounted	**66,107**	24,562
Foreign bill purchased	**18,365**	14,571
Total	**91,863**	57,295

8. INVESTMENT SECURITIES

	2021	*2020*
	AED '000	*AED '000*
Debt securities - measured at fair value through other comprehensive income	**445,530**	342,414
Allowance for expected credit loss	**(778)**	(402)

9. OTHER ASSETS

	2021	*2020*
	AED '000	*AED '000*
Interest receivable	**3,611**	2,545
Receivable from Head office	**-**	369
Prepayments	**357**	388
Cash collateral receivables on derivative instruments	**2,574**	5,063
	6,542	8,365

10. RELATED PARTIES

Related parties include the Head Office, key management personnel and entities controlled, jointly controlled or significantly influenced by such parties. A number of banking transactions are entered into with the Head Office and other branches in the normal course of business. The terms and conditions of these transactions are agreed between the Bank and related parties.

	2021	*2020*
	AED '000	*AED '000*
Transactions during the year		
Advances		
Bills discounted outstanding from other branches	**18,271**	24,562
Due to banks		
Current account	**8,218**	2,305
Borrowings with original maturity equal to / less than 3 months	**-**	66,114
Interest income		
Bills discounted outstanding from other branches	**368**	185
Interest expense		
Due to banks (Borrowings / Repo)	**2**	98

NOTES TO THE FINANCIAL STATEMENTS (continued)

As at 31 December 2021, the Bank holds investment securities under fiduciary capacity on behalf of other overseas branches amounted to equivalent AED 633 million (2020: AED 641 million).

During the year, the Bank has not recorded any impairment of the amounts due from related parties.

The Bank's key decisions are taken at Head Office level by the key management personnel of the Head Office, therefore, key management compensation disclosure is not included in these financial statements.

11. PROPERTY AND EQUIPMENT

	2021	*2020*
	AED '000	*AED '000*
Property, Plant and Equipment	**1,027**	552
Capital work in process	**169**	63
	1,196	615

	Furniture, fixture and office equipment	***Computer and accessories***	***Motor vehicles***	***Right-of-use-assets***	***Total***
	- - - - - - - - - - - - - - - - - - -	*- - - - -*	*AED'000*	*- - - - -*	*- - - - - - - - - - - - - - - - - - -*
1 January 2021	145	36	224	1,506	**1,911**
Additions during the year	11	27	75	993	**1,106**
31 December 2021	**156**	**63**	**299**	**2,499**	**3,017**
Accumulated depreciation:					
1 January 2021	72	21	170	1,096	**1,359**
Charge for the period (Note 25)	26	11	59	535	**631**
31 December 2021	**98**	**32**	**229**	**1,631**	**1,990**
Net book value:					
31 December 2021	**58**	**31**	**70**	**868**	**1,027**

	Furniture, fixture and office equipment	*Computer and accessories*	*Motor vehicles*	*Right- of-use-assets*	*Total*
	- - - - - - - - - - - - - - - - - - -	*- - - - -*	*AED'000*	*- - - - -*	*- - - - - - - - - - - - - - - - - - -*
1 January 2020	117	26	224	1,506	1,873
Additions during the year	28	10	-	-	38
31 December 2020	145	36	224	1,506	1,911
Accumulated depreciation:					
1 January 2020	50	13	114	548	725
Charge for the period (Note 25)	22	8	56	548	634
31 December 2020	72	21	170	1,096	1,359
Net book value:					
31 December 2020	73	15	54	410	552

NOTES TO THE FINANCIAL STATEMENTS (continued)

12. DUE TO BANKS

	2021	2020
	AED '000	AED '000
Current account	**9,641**	2,305
Borrowings with original maturity equal to / less than 3 months	**36,730**	66,114
	46,371	68,419

During the year ended 31 December 2021, the Bank obtained borrowings at interest rates ranging between 0.050 % - 1.200% (2020: 0.050 % - 2.00%)

13. DEPOSITS AND OTHER ACCOUNTS

	2021	2020
	AED '000	AED '000
Current deposits	**474,206**	214,165
Time deposits	**67,359**	58,631
Others	**6,158**	9,348
	547,723	282,144

At 31 December 2021, 10 customers accounted for 48% (2020: 51%) of total customer deposits. At 31 December 2021, deposits amounting to AED 9.01 million (2020: AED 23.39 million) were held as cash collateral for loans and advances to customers.

14. OTHER LIABILITIES

	2021	2020
	AED '000	AED '000
Accrued interest payable	**1,150**	829
Mark to market value of derivatives	**1,002**	7,119
Provision for employees' end of service benefits (note 14.1)	**621**	556
VAT payable	**22**	21
Provision for expected credit loss on unfunded exposures	**10**	86
Provision for taxation	**1,139**	753
Others	**4,635**	1,032
	8,579	10,396

14.1 PROVISION FOR EMPLOYEES' END OF SERVICE BENEFITS

	2021	2020
	AED '000	AED '000
Balance as at 1 January 2021	**556**	284
Charge for the period (note 25)	**65**	272
At 31 December 2021	**621**	556

The Bank provides for staff terminal benefits based on an estimate of the amount of future benefit that the employees have earned in return of for their service until their retirement. The calculation is performed based on a projected unit credit method.

NOTES TO THE FINANCIAL STATEMENTS (continued)

14.1 PROVISION FOR EMPLOYEES' END OF SERVICE BENEFITS (continued)

UAE national employees in the United Arab Emirates are members of the Government-managed retirement pension and social security benefit scheme. As per Federal Labor Law No. 7 of 1999, the Bank is required to contribute between 12.5% - 15% of the "contribution calculation salary" of UAE payroll costs to the retirement benefit scheme to fund the benefits. The employees are also required to contribute 5% of the "contribution calculation salary" to the scheme. The only obligation of the Bank with respect to the retirement pension and social security scheme is to make the specified contributions. The contributions are charged to the income statement.

15. ALLOCATED CAPITAL

The assigned capital of the Bank is AED 100 million (2020: AED 100 million) and is provided by the Head Office.

Capital and reserves	***2021***	*2020*
	AED'000	*AED'000*
Allocated capital	**100,000**	100,000
Regulatory credit risk reserve	**3,246**	1,722
Fair value reserve (OCI)	**1,849**	4,240
Statutory reserve	**945**	529
Retained earnings / accumulated losses	**2,695**	3,042
Total	**108,735**	109,533

16. STATUTORY RESERVE

In accordance with Article 82 of the UAE Union Law Number 10 of 1980, as amended, 10% of the profit for the year is required to be transferred to a statutory reserve which is non-distributable. Allocations to this reserve are required to be made until such time as the balance in this reserve equals 50% of the allocated capital. During the current year 10% of profit for the year has been transferred to the statutory reserve.

17. FAIR VALUE AND OTHER RESERVES

	2021	*2020*
Fair value through OCI	***AED'000***	*AED'000*
At 1 January 2021	**4,240**	1,701
Net unrealized gain / (loss) on financial assets measured at FVOCI	**(4,533)**	4,022
Expected credit loss on investments under IFRS 9	**377**	272
Actuarial gain / (loss)	**(46)**	-
Change in related deferred tax liability	**38**	5,995
At 31 December 2021	**1,811**	(1,755)
	1,849	4,240

NOTES TO THE FINANCIAL STATEMENTS (continued)

18. DERIVATIVE FINANCIAL INSTRUMENTS

The table below shows the fair values of derivative financial instruments, recorded as assets or liabilities, together with their notional amounts. The notional amount, recorded gross, is the amount of a derivative's underlying asset, reference rate or index and is the basis upon which changes in the value of derivatives are measured. The notional amounts indicate the volume of transactions outstanding at the year end and are indicative of neither the market risk nor the credit risk. All such derivatives are due less than one year.

	Assets 2021	***Liabilities 2021***	***Notional amount 2021***
	AED '000		
Derivatives - liquidity management:			
Forward foreign exchange contracts	**(460)**	**-**	**341,207**
Futures	**-**	**-**	**-**
Interest rate swaps	**-**	**1,002**	**329,101**
	(460)	**1,002**	**670,308**

	Assets 2020	*Liabilities 2020*	*Notional amount 2020*
	AED '000		
Derivatives - liquidity management:			
Forward foreign exchange contracts	27	-	207,552
Futures	-	-	-
Interest rate swaps	-	7,119	161,979
	27	7,119	369,531

The following table outlines the notional amounts and average rates of derivatives:

	Remaining term to maturity					
	Within 1 year	***1 to 3 years***	***3 to 5 years***	***Over 5 years***	***2021 Total***	*2020 Total*
	AED '000					
Fair Value Hedges						
Interest rate risk – Interest rate swaps						
Notional amount	**11,019**	**58,768**	**95,865**	**163,449**	**329,101**	161,979
Average fixed interest rate	**0.63%**	**1.44%**	**1.58%**	**1.53%**	**1.29%**	1.72%

	Remaining term to maturity					
	Within 1 year	***1 to 3 years***	***3 to 5 years***	***Over 5 years***	***2021 Total***	*2020 Total*
	AED '000					
Forward foreign exchange contracts						
Notional amount	**341,207**	**-**	**-**	**-**	**341,207**	207,552

NOTES TO THE FINANCIAL STATEMENTS (continued)

19. CONTINGENCIES AND COMMITMENTS

	2021 ***AED '000***	*2020* *AED '000*
Letters of credit	**-**	14,443
Letters of guarantee	**14,824**	28,028
Undrawn credit commitments	**51,000**	21,130

ECL of AED 10,110 (2020: AED 85,879) against off balance sheet items has been recognized under other liabilities.

Guarantees and standby letters of credit, which represent irrevocable assurances that the Bank will make payments in the event that a customer cannot meet his obligations to third parties. Documentary and commercial letters of credit, which are written undertakings by the Bank on behalf of a customer authorizing a third party to draw drafts on the Bank up to a stipulated amount under specific terms and conditions, are collateralized by the underlying shipments of goods to which they relate and therefore have significantly less risk. Cash requirements under guarantees and standby letters of credit are considerably less than the amount of the commitment because the Bank does not generally expect the third party to draw funds under the agreement.

Forward foreign exchange contracts comprise commitments to purchase or sell foreign currencies on behalf of customers and in respect of the Bank's proprietary activity.

Undrawn credit commitments represent unused portions of authorizations to extend credit in the form of loans. With respect to credit risk on commitments to extend credit, the Bank is potentially exposed to loss for an amount equal to the total unused commitments. However, the likely amount of loss, though not easy to quantify, is considerably less than the total unused commitments since most commitments to extend credit are contingent upon customers' maintaining specific credit standards. While there is some credit risk associated with the remainder of commitments, the risk is viewed as low, since it results from the possibility of unused portions of loan authorizations being drawn by the customer and only if such drawings subsequently are not paid as due. The Bank monitors the term to maturity of the credit commitments because longer term commitments generally have a greater degree of credit risk than the shorter term commitments. The total outstanding contractual amount of the commitments to extend credit does not necessarily represent future cash requirements, since many of these commitments will expire or terminate without being funded.

NOTES TO THE FINANCIAL STATEMENTS (continued)

20. LEASES

The Bank leases office premises. The leases typically run for a period of three years.

Information about leases for which the Bank is a lessee is presented below.

Leases as lessee (IFRS 16)

i. Right-of-use assets

Right-of-use assets relate to leased office premises that are presented within property and equipment (note 11).

	2021	*2020*
	AED '000	*AED '000*
Balance at 1 January 2021	**1,506**	1,506
Additions	**993**	-
Depreciation charge for the year	**(1,631)**	(1,096)
Balance at 31 December	**868**	410

ii. Lease liability

	2021	*2020*
	AED '000	*AED '000*
As at 1 January 2021	**1,096**	548
Effects of changes in accounting policy	**535**	548
As at 31 December 2021	**1,631**	1,096
Profit expense	**-**	-
Cash payments	**-**	-
As at 31 December 2021	**1,631**	1,096

Maturity analysis as at 31 December 2021:

	2021	*2020*
	AED '000	*AED '000*
Not later than 1 year	**-**	-
Later than 1 year and not later than 5 years	**1,631**	1,096
Total lease liabilities at 31 December 2021	**1,631**	1,096

ii. Amounts recognised in consolidated statement of profit or loss and other comprehensive income

Leases under IFRS 16

	2021	*2020*
	AED '000	*AED '000*
Financing cost on lease liability	**1,096**	548
Depreciation expense	**535**	548

iii. Amounts recognised in consolidated statement of cash flows

	2021	*2020*
	AED '000	*AED '000*
Total cash outflow for leases	**(619)**	(514)

NOTES TO THE FINANCIAL STATEMENTS (continued)

21. INTEREST INCOME

	2021	*2020*
	AED'000	*AED'000*
Interest income:		
- investment securities	**11,410**	8,930
- loans and advances	**2,147**	1,551
- interest rate swaps	**395**	821
	13,952	11,302

22. INTEREST EXPENSE

	2021	*2020*
	AED '000	*AED '000*
Interest expense on:		
- due to banks	**(282)**	(388)
- customer deposits	**(1,148)**	(1,074)
- finance lease	**(6)**	(28)
- interest rate swaps	**(3,702)**	(2,025)
	(5,138)	(3,515)

23. FEE, COMMISSION AND BROKERAGE INCOME

	2021	*2020*
	AED '000	*AED '000*
Letters of credit / guarantees	**432**	465
Trade related fee	**592**	469
Remittance income	**164**	130
	1,188	1,064

24. OTHER INCOME

	2021	*2020*
	AED '000	*AED '000*
Gain on sale of investment	**491**	714
Miscellaneous income	**2,126**	124
	2,617	838

25. STAFF COSTS

	2021	*2020*
	AED '000	*AED '000*
Salaries and allowances	**5,063**	4,292
Charge for employees' end of service benefits (note 14.1)	**282**	272
	5,345	4,564

NOTES TO THE FINANCIAL STATEMENTS (continued)

26. OTHER ADMINISTRATIVE AND GENERAL EXPENSES

	2021	*2020*
	AED '000	*AED '000*
Legal & professional consultancy	**267**	206
Insurance	**303**	281
Communication costs	**379**	302
Branch license fee	**102**	144
Others	**701**	633
	1,752	1,566

27. TAXATION

The taxable income is calculated after making certain adjustments to the net profit before tax for the year and is based on management's best estimate. The components of income tax expense for the year are:

	2021	*2020*
	AED '000	*AED '000*
Current tax:		
- current income tax	**(1,139)**	(753)
Deferred tax:		
- Relating to origination and reversal of temporary differences	**(279)**	(959)
Prior year current tax	**(4)**	(10)

27.1. Reconciliation between taxation expense and accounting profit

	2021	*2020*
	AED '000	*AED '000*
Net profit for the year before taxation	**5,304**	3,525
Tax on income @ 20%	**(1,061)**	(705)
- Prior year current tax	**(4)**	(10)
- Disallowed provisions	**(78)**	(48)
Income tax expense for the year	**(1,143)**	(763)

NOTES TO THE FINANCIAL STATEMENTS (continued)

28. MATURITY PROFILE OF ASSETS AND LIABILITIES

The maturities of assets and liabilities and the ability to replace, at an acceptable cost, interest-bearing liabilities as they mature, are important factors in assessing the liquidity of the Bank and its exposure to changes in interest rates and exchange rates.

The table below analyses assets and liabilities of the Bank at the reporting date into relevant maturity groupings based on the remaining period to the contractual maturity date:

	Up to 3 months	*3 months to 1 year*	*Up to 1 year Subtotal*	*1 – 5 years*	*Over 5 years*	*More than 1 year Subtotal*	*No fixed maturity*	*Total*
				AED '000				
At 31 December 2021								
Assets								
Cash and balances with the UAE Central Bank	**124,423**	**-**	**124,423**	**-**	**-**	**-**	**-**	**124,423**
Balances with other banks	**42,471**	**-**	**42,471**	**-**	**-**	**-**	**-**	**42,471**
Loans and advances	**29,583**	**57,265**	**86,848**	**4,677**	**-**	**4,677**	**-**	**91,525**
Investment securities	**2,213**	**33,464**	**35,677**	**225,203**	**184,650**	**409,853**	**-**	**445,530**
Other assets	**200**	**3,405**	**3,605**	**1,628**	**1,309**	**2,937**	**-**	**6,542**
Property and equipment	**-**	**-**	**-**	**-**	**-**	**-**	**1,196**	**1,196**
Total Assets	**198,890**	**94,134**	**293,024**	**231,508**	**185,959**	**417,467**	**1,196**	**711,687**
Liabilities								
Borrowings	**46,371**	**-**	**46,371**	**-**	**-**	**-**	**-**	**46,371**
Deposits and other accounts	**11,602**	**55,757**	**67,359**	**-**	**-**	**-**	**480,364**	**547,723**
Deferred tax liability	**-**	**-**	**-**	**-**	**-**	**-**	**279**	**279**
Other liabilities	**7,870**	**42**	**7,912**	**667**	**-**	**667**	**-**	**8,579**
Total liabilities	**65,843**	**55,799**	**121,642**	**667**	**-**	**667**	**480,643**	**602,952**
Net liquidity gap	**133,047**	**38,335**	**171,382**	**230,841**	**185,959**	**416,800**	**(479,447)**	**108,735**

	Up to 3 months	*3 months to 1 year*	*Up to 1 year Subtotal*	*1 – 5 years*	*Over 5 years*	*More than 1 year Subtotal*	*No fixed maturity*	*Total*
				AED '000				
At 31 December 2020								
Assets								
Cash and balances with the UAE Central Bank	47,897	-	47,897	-	-	-	-	47,897
Balances with other banks	15,134	-	15,134	-	-	-	-	15,134
Loans and advances	22,586	26,556	49,142	7,884	-	7,884	-	57,026
Investment securities	-	-	-	224,313	118,101	342,414	-	342,414
Other assets	830	5,150	5,980	1,849	530	2,385	-	8,365
Property and equipment	-	-	-	-	-	-	615	615
Total Assets	86,447	31,706	118,153	234,046	118,631	352,683	615	471,451
Liabilities								
Borrowings	68,419	-	68,419	-	-	-	-	68,419
Deposits and other accounts	44,131	14,500	58,631	-	-	-	223,513	282,144
Deferred tax liability	-	-	-	-	-	-	959	959
Other liabilities	8,216	1,624	9,840	556	-	556	-	10,396
Total liabilities	120,766	16,124	136,890	556	-	556	224,472	361,918
Net liquidity gap	(34,319)	15,582	(18,737)	233,490	118,631	352,127	(223,857)	109,533

NOTES TO THE FINANCIAL STATEMENTS (continued)

28. MATURITY PROFILE OF ASSETS AND LIABILITIES (continued)

In the above table, all current account and saving account balances have been classified as maturing in upto 3 months' column. However, in normal course of events all of them are not withdrawn within three months.

29. SUBSEQUENT EVENTS

On 31 January 2022, the UAE Ministry of Finance announced the introduction of a federal corporate tax in the UAE that will be effective for financial years starting on or after 1 June 2023. At the date of reporting, the Ministry of Finance has yet to publish the full corporate tax legislation. Notwithstanding this, the corporate tax is likely to have an impact on the Bank's performance in future reporting.

A variety of sanctions have been imposed on Russia in response to the conflict in Ukraine by a number of jurisdictions, which may be broadened in the foreseeable future to include further individuals, additional entities, and a wider range of goods and services than currently targeted. The matter is considered as a non-adjusting event. However, management is currently analysing the financial impact of these events on the future operating and financial performance of the Bank.