Bank of Baroda - UAE Branches

Financial statements
for the year ended 31 December 2018

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KPMG

KPMG Lower Gulf Limited
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Independent Auditors' Report

To the Chief Executive of Bank of Baroda – UAE Branches

Report on the Audit of the Financial Statements

Opinion

We have audited the financial statements of Bank of Baroda – UAE Branches ("the Bank"), which comprise the statement of financial position as at 31 December 2018, 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 2018, and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards (IFRS).

Basis for Opinion

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

Other Matter

The financial statements for the year ended 31 December 2017 were audited by another auditor who expressed an unmodified audit opinion on the financial statements for the year ended 31 December 2017 on 29 March 2018.

Responsibilities of Management for the Financial Statements

Management is responsible for the preparation and fair presentation of the financial statements in accordance with IFRS, 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.

Responsibilities of Management for the Financial Statements (continued)

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.

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, we report that we have obtained all the information and explanations we considered necessary for the purposes of our audit.

KPMG Lower Gulf Limited

Emilio Pera
Registered Auditor Number: 1146
Dubai, United Arab Emirates
Date 31 MAR 2019

Statement of financial position

		As at 31 December	
		2018	2017
	Note	**AED'000**	AED'000
ASSETS			
Cash and balances with the UAE Central Bank	5	**2,991,272**	3,293,981
Due from banks	6	**884,373**	798,576
Due from Head Office and other branches	27	**3,610,584**	3,133,754
Loans and advances to customers	7	**13,209,688**	11,876,994
Investment securities	8	**142,880**	143,980
Derivatives	25	**4,727**	6,942
Customers' indebtedness under acceptances	26	**380,227**	622,486
Furniture and equipment	9	**7,458**	7,609
Deferred tax asset	22	**453,489**	511,614
Other assets	10	**69,858**	81,827
Total assets		**21,754,556**	20,477,763
LIABILITIESAND EQUITY			
LIABILITIES			
Due to banks	11	**2,399,371**	1,082,509
Due to Head Office and other branches	27	**2,075,967**	1,340,292
Deposits from customers	12	**14,207,838**	14,239,611
Derivatives	25	**360**	4,727
Liabilities under acceptances	26	**380,227**	622,486
Other liabilities	13	**316,429**	279,141
Total liabilities		**19,380,192**	17,568,766
EQUITY			
Head Office assigned capital	14	**760,000**	760,000
Statutory reserve	15	**65,289**	65,289
Fair value reserve		**(3,976)**	(2,876)
Retained earnings		**1,553,051**	2,086,584
Net equity		**2,374,364**	2,908,997
Total liabilities and equity		**21,754,556**	20,477,763

These financial statements were approved and authorised for issue on 31 MAR 2019 and signed by:

D Ananda Kumar
Chief Executive – GCC Operations

The notes on pages 9 to 80 are an integral part of these financial statements.

The independent auditors' report is set out on pages 1 to 3.

Statement of profit or loss

	Notes	Year ended 31 December 2018 AED'000	2017 AED'000
Interest income	16	**719,008**	688,853
Interest expense	17	**(278,378)**	(246,575)
Net interest income		**440,630**	442,278
Fee and commission income	18	**79,627**	75,597
Fee and commission expense	18	**(1,129)**	(183)
Net fee and commission income		**78,498**	75,414
Other operating income	19	**76,174**	76,831
Total income		**595,302**	594,523
Personnel expenses	20	**(51,190)**	(54,407)
Depreciation	9	**(2,399)**	1,547
General and administrative expenses	21	**(78,623)**	(51,025)
Total expenses		**(132,212)**	(103,885)
Profit before impairment losses and taxation		**463,090**	490,638
Impairment losses on loans and advances (net)	7	**(881,046)**	(400,424)
Impairment losses on unfunded exposures (net)		**(444)**	-
Impairment of investment securities	8	**-**	(64)
(Loss)/ profit for the year before taxation		**(418,400)**	90,150
Taxation	22	**(90,727)**	(19,165)
(Loss)/ profit for the year		**(509,127)**	70,985

The notes on pages 9 to 80 are an integral part of these financial statements.

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Statement of other comprehensive income

	Notes	Year ended 31 December 2018 AED'000	2017 AED'000
(Loss)/ profit for the year		**(509,127)**	70,985
Other comprehensive income			
Items that are or maybe reclassified subsequently to the statement of profit or loss:			
Loss from changes in investments held at fair value through other comprehensive income		**(1,100)**	(1,286)
Total other comprehensive loss		**(1,100)**	(1,286)
Total comprehensive (loss)/ profit for the year		**(510,227)**	69,699

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Statement of changes in equity

	Head Office assigned capital AED'000	Statutory reserve AED'000	Fair value reserve AED'000	Retained earnings AED'000	Total AED'000
At 1 January 2017	760,000	58,191	(1,590)	2,022,697	2,839,298
Profit for the year	-	-	-	70,985	70,985
Transfer to statutory reserve	-	7,098	-	(7,098)	-
Other comprehensive income					
Change in fair value of available for sale investments	-	-	(1,286)	-	(1,286)
At 31 December 2017	760,000	65,289	(2,876)	2,086,584	2,908,997
Transition impact of IFRS 9	-	-	-	**(24,406)**	**(24,406)**
Loss for the year	-	-	-	**(509,127)**	**(509,127)**
Other comprehensive income					
Changes in fair value of investments measured at fair value through other comprehensive income	-	-	**(1,100)**	-	**(1,100)**
At 31 December 2018	**760,000**	**65,289**	**(3,976)**	**1,553,051**	**2,374,364**

The notes on pages 9 to 80 are an integral part of these financial statements.

The independent auditors' report is set out on pages 1 to 3.

Statement of cash flows

	Notes	Year ended 31 December 2018 AED'000	2017 AED'000
Cash flows from operating activities			
(Loss)/ profit for the year before taxation		**(418,400)**	90,150
Adjustments for:			
Impairment losses on loans and advances		**881,046**	400,424
Impairment losses on unfunded exposures		**444**	-
Impairment of FVOCI / available for sale investments		**-**	64
Gain on sale of investments		**-**	(10,549)
Gain on disposal of furniture and equipment		**(32)**	
Depreciation		**2,399**	(1,547)
Write off		**-**	11
Fair value loss on derivatives		**(2,152)**	10,618
End of service benefit provision		**2,029**	4,077
Operating cash flows before changes in working capital and tax paid		**465,334**	493,248
Changes in working capital:			
End of service benefit paid		**(1,103)**	(1,047)
Change in due from Central Bank of the UAE maturing after three months		**782,182**	398,890
Change in due from banks maturing after three months		**259,272**	883,839
Change in due from Head Office and other branches maturing after three months		**(236,875)**	(3,359)
Change in loans and advances to customers		**(2,236,350)**	(347,478)
Change in other assets		**11,969**	(20)
Change in deposits from customers		**(31,773)**	(2,923,001)
Change in due to banks maturing after three months		**(81,096)**	(78,866)
Change in due to Head Office and other branches maturing after three months		**591,150**	(177,142)
Change in other liabilities		**29,738**	(92,495)
Taxes paid		**(28,218)**	(117,719)
Net cash used in operating activities		**(475,770)**	(1,965,150)
Cash flows from investing activities			
Proceeds on maturity of investment securities		**-**	19,914
Purchase of furniture and equipments		**(2,300)**	(1,215)
Proceeds from sale of furniture and equipments		**84**	-
Net cash (used in) / generated from investing activities		**(2,216)**	18,699
Cash flows from financing activities		**-**	-
Net increase in cash and cash equivalents		**(477,986)**	(1,946,451)
Cash and cash equivalents at 1 January		**5,250,549**	7,197,000
Cash and cash equivalents at 31 December	24	**4,772,563**	5,250,549

The notes on pages 9 to 80 are an integral part of these financial statements.
The independent auditors' report is set out on pages 1 to 3.

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

1 Incorporation and principal activities

Bank of Baroda - UAE Branches (the "Bank") operates in the United Arab Emirates (the "UAE") through its six branches located in the Emirates of Abu Dhabi, Dubai, Sharjah and Ras Al Khaimah under a banking license issued by the Central Bank of the UAE. The Head Office of the Bank is Bank of Baroda (the "Head Office"), which is incorporated in Baroda, India.

The principal address of the Bank is Zonal office, Sheikh Rashid Building, Dubai, United Arab Emirates and the registered address is P.O. Box 3162, Dubai, United Arab Emirates.

The principal activities of the Bank include accepting deposits, granting loans and advances and providing other banking services.

These financial statements represent the combined financial position and results of the six branches of the Bank in the United Arab Emirates.

2 Basis of preparation

(a) Statement of compliance

These financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") as issued by International Accounting Standards Board (IASB), interpretations as issued by the IFRS Interpretations Committee (IFRS IC), applicable requirements of the laws of the UAE, including the UAE Federal Law No 2 of 2015 ("UAE Companies Law of 2015") and the Decretal Federal Law No. (14) of 2018.

The financial statements include Basel III Pillar 3 disclosures in accordance with the guidelines issued by the Central Bank of the UAE.

(b) Basis of measurement

These financial statements have been prepared under the historical cost basis, except for the following:

- derivative financial instruments measured at fair value;
- financial assets at fair value through other comprehensive income (applicable from 1 January 2018); and
- available-for-sale ("AFS") financial instruments measured at fair value (applicable before 1 January 2018)

(c) Functional and presentation currency

These financial statements are presented in United Arab Emirates Dirham ("AED"), which is the functional and presentation currency of the Bank. Except as indicated, the financial statements have been rounded to the nearest thousand.

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

2 Basis of preparation (continued)

(d) Use of estimates and judgments

The preparation of financial statements in conformity with IFRS requires the management to make judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised and in any future periods affected.

Significant areas of estimation uncertainty and critical judgment in applying accounting policies that have the most significant effect on the amounts recognised in the financial statements are described in Note 4.

3 Summary of significant accounting policies

The principal accounting policies applied in the preparation of these financial statements are set out below. These policies have been consistently applied to the periods presented, unless otherwise stated.

3.1 Changes in accounting policies

The Bank has initially adopted IFRS 9 (refer 3.1.1) and IFRS 15 (refer 3.1.2) from 1 January 2018

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

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

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

- an increase in impairment losses recognized on financial assets (refer note 3)
- additional disclosures related to IFRS 9 (refer note 3.5)
- additional disclosures related to IFRS 15 (refer note 3.11)

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

3.1.1 IFRS 9 – Financial Instruments

The Bank has transitioned to IFRS 9 Financial Instruments issued in July 2014 with the date of initial application being 1 January 2018.

The requirements of IFRS 9 represent a significant change from IAS 39 Financial Instruments: Recognition and Measurement. The new standard brings fundamental changes to the accounting for financial assets, certain aspects of the accounting for financial liabilities and measurement of expected credit loss on financial assets included in off balance sheet items such as loan commitments and financial guarantees.

The key changes to the Bank's accounting policies resulting from its adoption of IFRS 9 are summarised below:

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

3 Summary of significant accounting policies (continued)

3.1 Changes in accounting policies (continued)

3.1.1 IFRS 9 – Financial Instruments (continued)

Classification of financial assets and liabilities

IFRS 9 contains three principal classification categories for financial assets: measured at amortised cost, fair value through other comprehensive income (FVOCI) and fair value through profit or loss (FVTPL). IFRS 9 classification is generally based on the business model in which a financial asset is managed and its contractual cash flows. The standard eliminates the existing IAS 39 categories of held-to-maturity, loans and receivables and available-for-sale.

As per IFRS 9, derivatives embedded in contracts where the host is a financial asset in the scope of the standard are never bifurcated. Instead, the whole hybrid instrument is assessed for classification. The classification of financial assets by the Bank under IFRS 9 has been explained in note 3.5.

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

- the amount of change in the fair value that is attributable to changes in the credit risk of the liability is presented in OCI; and
- the remaining amount of change in the fair value is presented in profit or loss
- How the Bank classifies financial liabilities under IFRS 9 has been explained in note 3.5.

Impairment of financial assets

IFRS 9 replaces the 'incurred loss' model in IAS 39 with 'expected credit loss' model. The new impairment model also applies to certain loan commitments and financial guarantee contracts but not to equity investments.

Under IFRS 9, credit losses are recognised earlier than under IAS 39.

Financial assets are assessed as credit impaired when one or more events that have a detrimental impact on the estimated future cash flows of that asset have occurred. As this uses the same criteria as under IAS 39, the Bank's methodology for specific provisions remains largely unchanged.

For an explanation of how the Bank apply the impairment requirements of IFRS 9 refer to note 3.5.

Transition

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

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

3 Summary of significant accounting policies (continued)

3.1 Changes in accounting policies (continued)

3.1.1 IFRS 9 – Financial Instruments (continued)

Transition (continued)

- Comparative periods have not been restated. Differences in the carrying amounts of financial assets and financial liabilities resulting from the adoption of IFRS 9 are recognised in retained earnings and appropriate components of other reserves as at 1 January 2018. Accordingly, the information presented for 2017 does not reflect the requirements of IFRS 9 and therefore is not comparable to the information presented for 2018 under IFRS 9.
- The following assessments have been made on the basis of the facts and circumstances that existed at the date of initial application:
    - The determination of the business model within which a financial asset is held.
    - The designation of certain investments in equity instruments not held for trading as at FVOCI.
    - If a debt security had low credit risk at the date of initial application of IFRS 9, then the Bank has assumed that credit risk on the financial asset had not increased significantly since its initial recognition.

Changes and implications resulting from the adoption of IFRS 9 has been explained in note 3.5.

3.1.2 IFRS 15 – Revenue from Contract with Customers

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

3.2 Foreign currencies

Foreign currency transactions are recorded at rates of exchange ruling at the dates of the transactions.

Monetary assets and liabilities denominated in foreign currencies, which are stated at historical cost, are translated at the foreign exchange rate ruling at the reporting date.

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.

Foreign exchange differences arising on translation are generally recognised in the statement of profit or loss and other comprehensive income.

3.3 Cash and cash equivalents

Cash and cash equivalents comprise cash on hand, unrestricted balances with the UAE Central Bank, due from and due to banks and the amounts due from and to the related parties including the Head Office and other branches with original maturities of three months or less from the date of acquisition that are subject to an insignificant risk of changes in their fair value and are used by the Bank for the purposes of meeting short term cash commitments.

Cash and cash equivalents are carried at amortised cost in the statement of financial position.

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

3 Summary of significant accounting policies (continued)

3.4 Due from banks

Amounts due from banks are initially recognised at fair value and subsequently measured at amortised cost less any amounts written off and expected credit losses, if any.

3.5 Financial instruments

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

a) Recognition and initial measurement

The Bank initially recognizes 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 recognized 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 FVTPL, transaction costs that are directly attributable to its acquisition or issue.

b) Classification

Financial Assets – Policy applicable from 1 January 2018

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

- The asset is held within a business model whose objective is to hold assets to collect contractual cash flows; and
- The contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

Financial investment is measured at FVOCI only if it meets both of the following conditions and is not designated as at FVTPL:

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

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

All other financial assets are classified as measured at FVTPL.

In addition, on initial recognition, the 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.

3 Summary of significant accounting policies (continued)

3.5 Financial Instruments (continued)

Financial Assets – Policy applicable from 1 January 2018 (continued)

b) Classification (continued)

Business model assessment

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

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

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

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

For the purposes 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.

In assessing whether the contractual cash flows are solely payments of principal and interest, the Bank considers the contractual terms of the instrument. This includes assessing whether the financial asset contains a contractual term that could change the timing or amount of contractual cash flows such that it would not meet this condition. In making the assessment, the branches considers:

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

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

3 Summary of significant accounting policies (continued)

3.5 Financial Instruments (continued)

b) Classification (continued)

Financial Assets – Policy applicable from 1 January 2018 (continued)

Non-recourse loans

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

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

Financial Assets – Policy applicable before 1 January 2018

The Bank classifies its financial assets in the following categories: Financial assets at fair value through profit or loss; loans and receivables; held to maturity financial assets; and available-for-sale financial assets. Management determines the classification of its investments at initial recognition.

a) Financial assets at fair value through profit or loss

This category includes: financial assets held for trading, and those designated at fair value through profit or loss at inception.

(i) Held for trading:

Financial assets held for trading are those that are acquired principally for the purpose of sale in the near term. They are recorded at fair value. Fair value changes are recognised in statement of profit or loss.

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

3 Summary of significant accounting policies (continued)

3.5 Financial Instruments (continued)

b) Classification (continued)

Financial Assets – Policy applicable before 1 January 2018 (continued)

a) Financial assets at fair value through profit or loss (continued)

(ii) Fair value through profit or loss

Financial assets are designated at fair value through profit or loss when:

- The assets are managed, evaluated and reported internally on a fair value basis.
- The designation eliminates or significantly reduces an accounting mismatch which would otherwise arise.
- The asset contains as embedded derivative that significantly modifies the cash flows that would otherwise be required under the contract.

b) Loans and receivables

Loans and receivables are non-derivative financial assets with fixed and determinable payments that are not quoted in an active market. These arise when the Bank provides money directly to the borrower with no intention of trading the receivable.

c) Held-to-maturity financial assets

Held-to-maturity investments are non-derivative financial assets with fixed or determinable payments and fixed maturities that the branches' management has the intention and ability to hold to maturity. If the bank was to sell other than an insignificant amount except for specific situations, the entire category would be reclassified as available for sale.

d) Available for sale financial assets

Available-for-sale investments are those non-derivative financial assets that are designated as available-for-sale or not classified as (i) financial assets at fair value through profit or loss, (ii) loans and receivables or (iii) held-to-maturity investments. These assets are carried at fair value, with fair value changes recognised in other comprehensive income.

Interest income is recognised in profit or loss using the effective interest method. Foreign exchange gains or losses on available-for-sale debt security investments are recognised in the statement of profit or loss. Impairment losses are recognised in the statement of profit or loss.

Other fair value changes, other than impairment losses, are recognised in OCI and presented in the fair value reserve within equity. When the investment is sold, the gain or loss accumulated in equity is reclassified to the statement of profit or loss.

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

3 Summary of significant accounting policies (continued)

3.5 Financial Instruments (continued)

b) Classification (continued)

Financial Liabilities

The Bank classifies its financial liabilities in the categories of fair value through profit or loss; and amortised cost. There has been no changes in the classification of financial liabilities from the application of IFRS 9 as compared to IAS 39.

i. Financial liabilities at fair value through profit or loss

Financial liabilities are classified as at FVPL when the financial liability is (i) held for trading, or (ii) it is designated as at FVPL. A financial liability is classified as held for trading if:

- it has been incurred principally for the purpose of repurchasing it in the near term; or
- on initial recognition it is part of a portfolio of identified financial instruments that the Bank manages together and has a recent actual pattern of short-term profit-taking.

A financial liability other than a financial liability held for trading or contingent consideration that may be paid by an acquirer as part of a business combination may be designated as at FVPL upon initial recognition if:

- such designation eliminates or significantly reduces a measurement or recognition inconsistency that would otherwise arise; or
- the financial liability forms part of a group of financial assets or financial liabilities or both, which is managed and its performance is evaluated on a fair value basis, in accordance with the Bank's documented risk management or investment strategy, and information about the grouping is provided internally on that basis; or
- it forms part of a contract containing one or more embedded derivatives, and IFRS 9 permits the entire hybrid (combined) contract to be designated as at fair value through profit or loss.

ii. Financial liabilities at amortised cost

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

The effective interest method is a method of calculating the amortised cost of a financial liability and of allocating interest expense over the relevant period. The 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.

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

3 Summary of significant accounting policies (continued)

3.5 Financial Instruments (continued)

c) Subsequent measurement

Financial Assets

Policy Applicable from 1 January 2018

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

Financial asset classified as at fair value through other comprehensive income or fair value through profit or loss 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.

Policy Applicable before 1 January 2018

Financial assets are initially measured at fair value. Transaction costs that are directly attributable to the acquisition or issue of financial assets and liabilities (other than financial assets and financial liabilities at fair value through profit or loss) are added to or deducted from the fair value of the financial assets or financial liabilities, as appropriate, on initial recognition. Transaction costs directly attributable to the acquisition of financial assets or financial liabilities at fair value through profit or loss are recognised immediately in the statement of profit or loss and other comprehensive income.

Financial Liabilities

Financial liabilities at FVPL are stated at fair value, with any gains / losses arising on remeasurement recognised in profit or loss to the extent that they are not part of a designated hedging relationship. The net gain / loss recognised in statement of profit or loss incorporates any interest paid on the financial liability.

However, for non-derivative financial liabilities that are designated as at fair value through profit or loss, the amount of change in the fair value of the financial liability that is attributable to changes in the credit risk of that liability is recognised in OCI, unless the recognition of the effects of changes in the liability's credit risk in OCI would create or enlarge an accounting mismatch in profit or loss. The remaining amount of change in the fair value of liability is recognised in profit or loss. Changes in fair value attributable to a financial liability's credit risk that are recognised in OCI are not subsequently reclassified to statement of profit or loss; instead, they are transferred to retained earnings upon derecognition of the financial liability.

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

3 Summary of significant accounting policies (continued)

3.5 Financial Instruments (continued)

d) Reclassification

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 current and previous financial year there was no change in the business model under which the Bank holds financial assets and therefore no reclassifications were made.

e) Impairment

Policy applicable from 1 January 2018

The Bank recognises loss allowances for expected credit losses (ECLs) on the following financial instruments that are not measured at fair value through profit or loss:

- due from banks;
- loans and advances to customers;
- investments measured at fair value through other comprehensive income;
- other financial assets;
- loan commitments; and
- financial guarantee contracts.

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

Under Stage 1, where there has not been a significant increase in credit risk since initial recognition, an amount equal to 12 months ECL will be recorded. The 12 months ECL is calculated as the portion of life time ECL that represents the ECL that result from default events on a financial instrument that are possible within the 12 months after the reporting date. The Bank calculates the 12 months ECL allowance based on the expectation of a default occurring in the 12 months following the reporting date. These expected 12 month default probabilities are applied to a forecast EAD and multiplied by the expected LGD and discounted by an approximation to the contractual interest rate.

Under Stage 2, where there has been a significant increase in credit risk since initial recognition but the financial instruments are not considered credit impaired, an amount equal to the default probability weighted lifetime ECL will be recorded. The PD and LGD are estimated over the lifetime of the instrument and the expected cash shortfalls are discounted by an approximation to the the contractual interest rate.

Under the Stage 3, where there is objective evidence of impairment at the reporting date these financial instruments will be classified as credit impaired and an amount equal to the lifetime ECL will be recorded for the financial assets, with the PD set at 100%.

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

3 Summary of significant accounting policies (continued)

3.5 Financial Instruments (continued)

e) Impairment (continued)

Policy applicable from 1 January 2018 (continued)

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 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 contractual interest rate, regardless of whether it is measured on an individual basis or a collective basis.

The key inputs into the measurement of ECL are described below:

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

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

Details of these statistical parameters / inputs are as follows:

- 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;

- EAD is an estimate of the exposure at a future default date, taking into account expected changes in the exposure after the reporting date; and

- LGD is determined as 100% for unsecured portfolio and for secured portfolio, LGD has been calculated after applying hair cut on collateral values as per CBUAE guidelines. It is usually expressed as a percentage of the EAD.

3 Summary of significant accounting policies (continued)

3.5 Financial Instruments (continued)

e) Impairment (continued)

Policy applicable from 1 January 2018 (continued)

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

- instrument type;
- credit risk ratings;
- collateral type;
- Loan to value ratio for retail exposure;
- date of initial recognition;
- remaining term of maturity;
- industry; and
- geographical location of the borrower.

The groupings are subject to regular review to ensure that exposure within a particular group remain appropriately homogenous.

Restructured financial assets

If the terms of a financial asset are renegotiated or modified or an existing financial asset is replaced with a new one due to financial difficulties of the borrower, then an assessment is made of whether the financial asset should be derecognised and ECLs 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 amortised cost and 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; or
- the purchase of a financial asset at a deep discount that reflects the incurred credit losses.

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

3 Summary of significant accounting policies (continued)

3.5 Financial Instruments (continued)

e) Impairment (continued)

Policy applicable from 1 January 2018 (continued)

Credit-impaired financial assets (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 amortised cost or FVOCI are credit-impaired at each reporting date. The Bank considers following factors, however not limited to:

- significant financial difficulty of the issuer or counterparty;
- breach of contract, such as a default or delinquency in profit or principal payments;
- it becoming probable that the customer will enter bankruptcy or financial re-organisation; or
- the disappearance of an active market for that financial asset because of financial difficulties.

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.

Purchased or originated credit-impaired (POCI) financial assets

For POCI financial assets, the Bank recognises all changes in lifetime ECL since initial recognition as a loss allowance with any changes recognised in statement of profit or loss. A favourable change for such assets creates an impairment gain.

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:

- Days Past Due: Exposures that have one or more instalment past due for more than 90 days.
- Rating: Customers with an internal rating of BOB-RAM 8 or 'D' or with an external default rating (not applicable in the case of retail facilities).
- Event driven defaults: This will be based on the customer specific factors such as breach of covenants which are deemed material, declaration of bankruptcy by the customer, death of borrower, loss of a significant contract significantly impacting the ability of the customer to repay and other customer specific factors. This will be applied on a case by case basis.

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

3 Summary of significant accounting policies (continued)

3.5 Financial Instruments (continued)

e) Impairment (continued)

Policy applicable from 1 January 2018 (continued)

Default Definition (continued)

- Regulatory default: If in future, the local regulator prescribes the criteria of default for IFRS 9 purposes, the Bank will choose the local regulatory criteria of defining default.

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.

Assessment of significant increase in credit risk

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

The movement from Stage 1 to Stage 2 is dependent upon a set of quantitative, qualitative and backstop indicators. The indicators are based on statistical models, delinquency movements and other qualitative criteria in place as required by the regulatory guidelines.

The determination of the credit impairment remains unchanged in IFRS 9 consistent with IAS 39.

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.

- Based on Bank's defined qualitative and quantitative criteria if there is significant decrease in credit risk, customers will be upgraded stage-wise (one stage at a time) from Stage 3 to Stage 2 after and from Stage 2 to Stage 1 after meeting the cooling off period of at least 12 months respectively.

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

3 Summary of significant accounting policies (continued)

3.5 Financial Instruments (continued)

e) Impairment (continued)

Policy applicable from 1 January 2018 (continued)

Incorporation of forward-looking information

IFRS 9 requires an unbiased and probability weighted estimate of credit losses by evaluating a range of possible outcomes that incorporates forecasts of future economic conditions. In its Expected Credit Life ("ECL") model, the Bank relies on GDP growth rates as a macroeconomic input

The Bank formulates three economic scenarios: a base case, which is the median scenario assigned a 80% probability of occurring, and two less likely scenarios, one upside and one downside, each assigned a 10% probability of occurring.

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 amortised cost: as a deduction from the gross carrying amount of the assets;
- for loan commitments and financial guarantee contracts: generally, as a provision; 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. Any excess of the loss allowance over the gross amount of the drawn component is presented as a provision.

Experienced credit judgement

The Bank's ECL allowance methodology requires the use of experienced credit judgement to incorporate the estimated impact of factors not captured in the modelled ECL results, in all reporting periods (refer note 4).

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

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

Expected life

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

3 Summary of significant accounting policies (continued)

3.5 Financial Instruments (continued)

e) Impairment (continued)

Policy applicable from 1 January 2018 (continued)

Rating methodology used by the Bank

Within the Corporate & Small Medium Enterprises (SME) Banking business, a Basel-II compliant Internal Rating Model is used for quantifying the risk associated with the counterparty. The model has been named as BOB Risk Assessment Model (BOB-RAM) ("the model"). Accounts having exposure of AED 3.673 million (US Dollar 1 million) and above are rated under the model. The model is a two dimensional rating model under which both the obligor and facility are rated. Obligor rating grades are defined from BOB 1 to BOB 10. BOB 1 is the highest safety grade while BOB 10 is the default grade. BOB 1 to BOB 6 are defined as the investment grade rating while BOB 7 to BOB 10 are defined as the non-investment grade. Similarly facility rating grades are from FR 1 to FR 8. Obligor rating matrix and facility rating matrix are combined to produce combined rating (CR) from CR 1 to CR 10.

Obligor Rating is the measure of Probability of Default ("PD") while Facility Rating is the measure of Loss Given Default ("LGD"). The combined rating will help the Bank measure expected loss. Pricing in corporate and SME exposures in AED currency are linked to the combined rating (CR). Exposures below AED 3.673 million (US Dollar 1 million) are rated under internal manual score based model. Based on the total score rating grades are defined as A+ to C with total 5 rating grades. A+ is the highest safety grade while C is the default grade.

Write off

Loans and debt securities are written off (either partially or in full) when there is no realistic prospect of recovery. This is generally 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. However, financial assets that are written off could still be subject to enforcement activities in order to comply with the branches' procedures for recovery of amounts due.

Policy applicable before 1 January 2018

The Bank assesses at each reporting date whether there is objective evidence that financial assets, not carried at fair value through profit or loss are impaired. Financial assets are impaired when objective evidence demonstrates that a loss event has occurred after the initial recognition of the asset, and that the loss event has an impact on the future cash flows relating to the asset that can be reliably estimated.

The Bank considers evidence of impairment at both individual asset and collective level. All individually significant financial assets are assessed for specific impairment. All significant assets found not to be specifically impaired are then collectively assessed for any impairment that has been incurred but not yet identified. Assets that are not individually significant are then collectively assessed for impairment by grouping together financial assets (carried at amortised cost) with similar risk characteristics.

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

3 Summary of significant accounting policies (continued)

3.5 Financial Instruments (continued)

e) Impairment (continued)

Policy applicable before 1 January 2018 (continued)

Objective evidence that financial assets (including equity securities) are impaired can include significant financial difficulty of the borrower or issuer, default or delinquency by a borrower, restructuring of a loan or advance by the Bank on terms that the Bank would not otherwise consider, in dications that a borrower or issuer will enter bankruptcy, the disappearance of an active market for a security, or other observable data relating to a Bank of assets such as adverse changes in the payment status of borrowers or issuers in the Bank, or economic conditions that correlate with defaults in the Bank. In addition, for an investment in equity security, a significant or prolonged decline in its fair value below its cost is an objective evidence of impairment.

In assessing collective impairment, the Bank uses statistical modelling of historical trends of the probability of default, timing of recoveries and the amount of loss incurred, adjusted for management's judgment as to whether current economic and credit conditions are such that the actual losses are likely to be greater or less than those suggested by historical modeling. Default rates, loss rates and the expected timing of future recoveries are regularly benchmarked against actual outcomes to ensure that they remain appropriate.

When a loan is uncollectible, it is written off against the related allowance for loan impairment. Such loans are written off after all the necessary procedures have been completed and the amount of the loss has been determined. Subsequent recoveries of amounts previously written off and / or any event resulting in a reduction in impairment loss, decreases the amount of loan impairment charge in the statement of income.

Impairment losses on assets carried at amortised cost are measured as the difference between the financial assets' carrying amount and the present value of estimated future cash flows discounted at the financial assets' original effective interest rate. Losses are recognised in the statement of income and reflected in an allowance account against loans and advances.

When a subsequent event causes the amount of impairment loss to decrease, the impairment loss is reversed through the statement of income.

If the terms of a financial asset are renegotiated or modified or an existing financial asset is replaced with a new one due to financial difficulties of the borrower, then an assessment is made of whether the financial asset should be derecognised. If the cash flows of the renegotiated asset are substantially different, then the contractual rights to cash flows from the original financial asset are deemed to have expired. In this case, the original financial asset is derecognised and the new financial asset is recognised at fair value. The impairment loss before an expected restructuring is measured as follows:

- if the expected restructuring will not result in derecognition of the existing asset, then the estimated cash flows arising from the modified financial asset are included in the measurement of the existing asset based on their expected timing and amounts discounted at the original effective interest rate of the existing financial asset.

- if the expected restructuring will result in derecognition of the existing financial asset, then the expected fair value of the new financial asset is treated as the final cash flow from the existing financial asset at the time of its derecognition. This amount is discounted from the expected date of derecognition to the reporting date using the original effective interest rate of the existing financial asset.

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

3 Summary of significant accounting policies (continued)

3.5 Financial Instruments (continued)

e) Impairment (continued)

Policy applicable before 1 January 2018 (continued)

Impairment losses on available for sale investment securities are recognised by transferring the difference between the amortised acquisition cost and cuffent fair value, less any impairment loss recognised previously in the statement of income, out of the statement of other comprehensive income to the statement of income. When a subsequent event causes the amount of impairment loss on an available for sale debt security to decrease, the impairment loss is reversed through the statement of income.

However, any subsequent recovery in the fair value of an impaired available for sale equity security is recognised in other comprehensive income. Changes in impairment provisions attributable to time value are reflected as a component of interest income.

f) Modifications

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.

3 Summary of significant accounting policies (continued)

3.5 Financial Instruments (continued)

f) Modification (continued)

Financial assets (continued)

If cash flows are modified when the borrower is in financial difficulties, then the objective of the modification is usually to maximise recovery of the original contractual terms rather than to originate a new asset with substantially different terms. 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.

If the modification of a financial asset measured at amortised 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 recognises 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 amortised over the remaining term of the modified financial asset.

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

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 recognised at fair value. The difference between the carrying amount of the financial liability derecognised and consideration paid is recognised in the statement of profit or loss. Consideration paid includes non-financial assets transferred, if any, and the assumption of liabilities, including the new modified financial liability.

If the modification of a financial liability is not accounted for as derecognition, then the amortised cost of the liability is recalculated by discounting the modified cash flows at the original effective interest rate and the resulting gain or loss is recognised in the statement of profit or loss. 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 recognised as an adjustment to the carrying amount of the liability and amortised over the remaining term of the modified financial liability by re-computing the effective interest rate on the instrument.

3 Summary of significant accounting policies (continued)

3.5 Financial Instruments (continued)

g) Derecognition

Financial assets

The Bank derecognises 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 recognises 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 recognise the financial asset and also recognises a collateralised borrowing for the proceeds received.

In the case where the financial asset is derecognised, the loss allowance for ECL is remeasured 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 recognised 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.

Financial liabilities

The Bank derecognises 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 derecognised and the consideration paid and payable is recognised in the statement of profit or loss.

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.

h) Offsetting

Financial assets and liabilities are offset when there is a legally enforceable right to offset the recognized amounts and there is an intention to settle on a net basis, or realize the asset and settle the liability simultaneously.

3 Summary of significant accounting policies (continued)

3.6 Furniture and equipment

(i) Recognition and measurement

Items of property and equipment are measured at historical cost less accumulated depreciation and impairment losses, if any. Historical cost includes expenditures that are directly attributable to the acquisition of the asset.

(ii) Subsequent cost

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

(iii) Depreciation

Depreciation is recognised in the statement of profit or loss on a straight-line basis over the estimated useful lives of items of furniture and equipment, principally between 3-10 years. Where the carrying value of an asset is greater than its estimated recoverable amount, it is written down immediately to its recoverable amount with a charge to the statement of profit or loss. The costs of the day-to-day servicing of furniture and equipment are recognised in the statement of profit or loss as incurred.

(iv) Derecognition / Disposal

An item of property, plant and equipment is derecognised upon disposal or when no future economic benefits are expected to arise from the continued use of the asset. Any gain or loss arising on the disposal or retirement of an item of furniture and equipment is determined as the difference between the sales proceeds and the carrying amount of the asset and is recognised in the statement of profit or loss.

3.7 Impairment of non financial assets

The carrying amount of the Bank's non-financial assets, other than deferred tax assets, is reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists then the asset's recoverable amount is estimated.

An impairment loss is recognised if the carrying amount of an asset or its cash-generating unit exceeds its recoverable amount. A cash generating unit is the smallest identifiable asset that generates cash flows and that largely is independent from other assets. Impairment losses are recognised in the statement of profit or loss.

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

Impairment losses recognised in prior periods are assessed at each reporting date for any indications that the loss has decreased or no longer exists. An impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised.

3.8 Deposits

Deposits are the Bank's sources of debt funding. Deposits are initially measured at fair value minus transaction costs, and subsequently measured at their amortised cost using the effective interest method.

3 Summary of significant accounting policies (continued)

3.9 Provisions

A provision is recognised in the statement of financial position when the Bank has a legal or constructive obligation as a result of a past event, when it is probable that an outflow of economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation. Provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and, where appropriate, the risks specific to the liability. The unwinding of the discount is recognised as finance cost.

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

3.10 Operating leases

Leases of assets under which the lessor effectively retains all the risks and rewards of ownership are classified as operating leases. Payments made under operating leases are recognised in the statement of profit or loss on a straight-line basis over the term of the lease.

3.11 Interest income and expense

Policy applicable from 1 January 2018

Effective interest rate

Interest income and expense for all interest-bearing financial instruments, except for those classified as FVTPL or designated at fair value through profit or loss, are recognized within 'interest income' and 'interest expense' in the income statement using the effective interest method.

Interest income and expense are recognized in profit or loss using the effective interest method. The 'effective interest rate' is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument to:

- the gross carrying amount of the financial asset; or
- the amortised cost of the financial liability.

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

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

Presentation

Interest income and expense presented in the statement of profit or loss and OCI include:

- Interest on financial assets and financial liabilities measured at amortised cost calculated on an effective interest basis;
- Interest on financial investment is measured at FVOCI calculated on an effective interest basis;

Interest income and expense on other financial assets and financial liabilities at FVTPL are presented in net income from other financial instruments at FVTPL.

3 Summary of significant accounting policies (continued)

3.11 Interest income and expense (continued)

Policy applicable from 1 January 2018 (continued)

Amortised cost and gross carrying amount

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

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

For financial assets that have become credit-impaired subsequent to initial recognition, interest income is calculated by applying the effective interest rate to the amortised cost of the financial asset. If the asset is no longer credit-impaired, then the calculation of interest income reverts to the gross basis.

For financial assets that were credit-impaired on initial recognition, interest income is calculated by applying the credit-adjusted effective interest rate to the amortised cost of the asset. The calculation of interest income does not revert to a gross basis, even if the credit risk of the asset improves.

In calculating interest income and expense, the effective interest rate is applied to the gross carrying amount of the asset (when the asset is not credit-impaired) or to the amortised cost of the liability.

Policy applicable before 1 January 2018

Interest income and expense for all interest-bearing financial instruments, except for those classified as held for trading or designated at fair value through profit or loss, are recognized within 'interest income' and 'interest expense' in the income statement using the effective interest method.

The effective interest method is a method of calculating the amortized cost of a financial asset or a financial liability and of allocating the interest income or interest expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument or, when appropriate, a shorter period to the net carrying amount of the financial asset or financial liability. When calculating the effective interest rate, the bank estimates cash flows considering all contractual terms of the financial instrument (for example, prepayment options) but does not consider future credit losses. The calculation includes all fees and points paid or received between parties to the contract that are an integral part of the effective interest rate, transaction costs and all other premiums or discounts.

3.12 Fee and commission income

Fee and commission income and expense that are integral to the effective interest rate of a financial asset or liability are included in the measurement of the effective interest rate.

Other fee and commission income, including account servicing fees, placement fees and syndication fees, are recognised as the related services are performed.

A contract with a customer that results in a recognised 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.

Other fees and commission expenses relates mainly to transaction and service fees, which are expensed in the statement of profit or loss as the services are received.

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

3 Summary of significant accounting policies (continued)

3.13 Taxation

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

Current tax comprises the expected tax payable or receivable on the taxable income or loss for the year and any adjustment to the tax payable or receivable in respect of previous years. It is measured using tax rates enacted or substantively enacted at the reporting date.

Deferred tax is recognised in respect of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred tax is not recognised for:

(1) temporary differences on the initial recognition of assets or liabilities in a transaction that is not a business combination and that affects neither accounting nor taxable profit and loss;
(2) temporary differences related to investments in subsidiaries to the extent that it is probable that they will not reverse in the foreseeable future; and
(3) taxable temporary differences arising on the initial recognition of goodwill.

Deferred tax assets are recognised for unused tax losses, unused tax credits and deductible temporary differences to the extent that it is probable that future taxable profits will be available against which they can be used. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

Deferred tax is measured at the tax rates that are expected to be applied to temporary differences when they reverse, using tax rates enacted or substantively enacted at the reporting date. The measurement of deferred tax reflects the tax consequences that would follow the manner in which the Bank expects, at the reporting date, to recover or settle the carrying amount of its assets and liabilities. Deferred tax assets and liabilities are offset if there is a legally enforceable right to offset current tax liabilities and assets, and they relate to taxes levied by the same tax authority on the same taxable entity, or on different tax entities, but they intend to settle current tax liabilities and assets on a net basis or their tax assets and liabilities will be realised simultaneously.

In determining the amount of current and deferred tax, the Bank considers the impact of tax exposures, including whether additional taxes and interest may be due. This assessment relies on estimates and assumptions and may involve a series of judgments about future events. New information may become available that causes the Bank to change its judgment regarding the adequacy of existing tax liabilities; such changes to tax liabilities would impact tax expense in the period in which such a determination is made.

3.14 Staff terminal benefits

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

The Bank contributes to the pension scheme for UAE nationals under the UAE pension and social security law. This is a defined contribution pension plan and the Bank's contributions are charged to the statement of profit or loss in the period to which they relate. In respect of this scheme, the Bank has a legal and constructive obligation to pay the fixed contributions as they fall due and no obligations exist to pay the future benefits.

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

3 Summary of significant accounting policies (continued)

3.15 Financial guarantees and loan commitments

Financial guarantees are contracts that require the Bank to make specified payments to reimburse the holder for a loss it incurs as a specified debtor fails to make payment when due in accordance with the terms of a debt instrument. Loan commitments are firm commitments to provide credit under pre-specified terms and conditions.

Financial guarantee liabilities are initially recognised at their fair value, and the initial fair value is amortised over the life of the financial guarantee. The guarantee liability is subsequently carried at the higher of this amortised amount and the present value of any expected future payment (when a payment under the guarantee has become probable).

Policy applicable from 1 January 2018

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

Policy applicable before 1 January 2018

The amount representing the initial fair value amortised over the life of the guarantee or the commitment and the present value of any expected payment to settle the liability when a payment under the contract has become probable.

3.16 New standards and interpretations not yet effective

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

The Bank anticipates that these IFRS and amendments will be adopted in the financial statements in the initial period when they become mandatorily effective. The impact of these standards and amendments are currently being assessed by the Bank. Based on the initial assessment, the Bank considers that there will not be a significant impact on the financial statements of the Bank.

a) IFRS 16 Leases

The IASB issued a new standard for accounting for leases effective from 1 January 2019

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

b) Other standards

- Annual Improvements to IFRS Standards 2015–2017 Cycle – various standards
- Long-term Interests in Associates and Joint Ventures (Amendments to IAS 28)
- Plan Amendment, Curtailment or Settlement (Amendments to IAS 19)
- IFRIC 23 Uncertainty over Income Tax Treatments
- Amendments to References to Conceptual Framework in IFRS Standards
- IFRS 17 Insurance Contracts.

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

3 Summary of significant accounting policies (continued)

3.17 Transitional impact of IFRS 9 application

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

	Retained earnings AED'000
Balance as at 31 December 2017 under IAS 39	**2,086,584**
Impact on recognition of Expected Credit Losses	
On loans and advances to customers	**(22,610)**
On unfunded exposures	**(1,796)**
	(24,406)
Opening balance under IFRS 9 on date of initial application of 1 January 2018	**2,062,178**

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

3 Summary of significant accounting policies (continued)

3.17 Transitional impact of IFRS 9 application (continued)

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

	IAS 39 classification	IFRS 9 classification	IAS 39 carrying amount AED'000	Impact of ECL AED'000	IFRS 9 carrying amount AED'000
Financial assets					
Cash and balances with the UAE Central Bank	Loans and receivables	Amortised cost	**3,293,981**	-	**3,293,981**
Due from banks	Loans and receivables	Amortised cost	**798,576**	-	**798,576**
Due from Head Office and other branches	Loans and receivables	Amortised cost	**3,133,754**	-	**3,133,754**
Loans and advances to customers	Loans and receivables	Amortised cost	**11,876,994**	**(22,610)**	**11,854,384**
Investment securities	AFS	FVOCI	**143,980**	-	**143,980**
Other financial assets (excluding prepayments)	Loans and receivables / FVTPL	Amortised cost / FVTPL	**75,963**	-	**75,963**
Total Financial Assets			**19,323,248**	**(22,610)**	**19,300,638**

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

3 Summary of significant accounting policies (continued)

3.17 Transitional impact of IFRS 9 application (continued)

	IAS 39 classification	IFRS 9 classification	IAS 39 carrying amount AED'000	Impact of ECL AED'000	IFRS 9 carrying amount AED'000
Financial Liabilities					
Deposits from customers	Amortised cost	Amortised cost	**14,239,611**	**-**	**14,239,611**
Due to banks	Amortised cost	Amortised cost	**1,082,509**	**-**	**1,082,509**
Due to Head Office and other branches	Amortised cost	Amortised cost	**1,340,292**	**-**	**1,340,292**
Other liabilities	Amortised cost / FVTPL	Amortised cost / FVTPL	**283,868**	**1,796**	**285,664**
Total Financial Liabilities			**16,946,280**	**1,796**	**16,948,076**

4 Significant management judgements and estimates

The preparation of the financial statements in conformity with IFRS requires management to make judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimates are revised and in any future periods affected.

Information about significant areas of estimation and uncertainty and critical judgements in applying accounting policies that have the most significant effect on the amounts recognised in the financial statements are described below:

(i) Impairment losses on loans and advances

Applicable from 1 January 2018

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

Applicable before 1 January 2018

The Bank evaluates impairment on loans and advances and investments on an ongoing basis and a comprehensive review on a quarterly basis to assess whether an impairment charge is recognised in the statement of profit or loss. In particular, considerable judgement by management is required in the estimation of the amount and timing of future cash flows when determining the level of impairment charge required. In estimating these cash flows, management makes judgements about the counterparty's financial situation and other means of settlement and the net realisable value of any underlying collateral. Such estimates are based on assumptions about several factors involving varying degrees of judgement and uncertainty, and actual results may differ resulting in future changes to such impairment charges.

(iii) Impairment losses on investment securities

The Bank evaluates its investments securities individually for impairment. Impairment provision on investment securities is based upon the management's best estimate of the present value of the cash flows that are expected to be received. In estimating these cash flows, the management makes judgments about a counterparty's financial situation. Judgment is also exercised while reviewing factors indicating and determining the objective evidence of impairment in respect of investment securities.

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

4 Significant management judgements and estimates (continued)

(iii) Fair value of derivatives

The fair value of derivatives that are not quoted in active markets are determined using valuation techniques. Valuation techniques include using arm's length transactions between knowledgeable, willing parties (if available), reference to the current market value of other instruments that are substantially the same and discounted cash flow analysis. To the extent it is practical, observable data is applied in the valuation techniques, however areas such as credit risk (both own and countcrparty), volatilities and correlation requires management to make assumptions. Changes in assumptions relating to these factors could affect the reported fair value of derivatives.

(iv) Income taxes

The Bank is subject to income tax in the UAE. Estimates are required in determining the provision for income taxes. There are several transactions and calculations for which the ultimate tax determination is uncertain during the ordinary course of business. The Bank recognises liabilities for anticipated tax audit issues based on estimates of whether additional taxes will be due. Where the final tax outcome of these matters is different from the amounts that were initially recorded, such differences will impact the income tax and deferred tax provisions in the period in which such determination is made.

(v) Recoverbility of deferred tax asset (DTA)

The Bank reviews the recoverbility of deferred tax asset on a periodic basis. DTA is relased to the statement of profit or loss as a result of decrease in loan loss provision or loan being written off from the statement of finacial postion. In determining the recoverbility of DTA, the management makes estimates and uses judgments as to whether there is any observable data indicating that DTA is not recoverable.

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

5 Cash and balances with the UAE Central Bank

	2018 AED'000	2017 AED'000
Cash on hand	**117,880**	203,423
Balances with UAE Central Bank:		
Certificate of deposits	**1,500,000**	1,600,000
Clearing accounts	**595,129**	658,376
Regulatory cash reserve deposits	**778,263**	832,182
	2,991,272	3,293,981

6 Due from banks

	2018 AED'000	2017 AED'000
Money market placements	**867,775**	664,813
Nostro balances	**16,598**	133,763
	884,373	798,576

7 Loans and advances to customers

The composition of the loans and advances is as follows:

	2018 AED'000	2017 AED'000
Overdrafts	**3,949,627**	4,155,415
Term loans	**7,148,281**	6,089,469
Loans against trust receipts	**1,775,159**	1,450,215
Bills discounted	**1,589,317**	1,501,410
Others	**1,725,106**	1,067,336
Gross loans and advances - net of interest suspense	**16,187,490**	14,263,845
Less: Allowances for impairment losses	**(2,977,802)**	(2,386,851)
Net loans and advances to customers	**13,209,688**	11,876,994

	2018 AED'000	2017 AED'000
Less:		
ECL on loans and advances - Performing (Stage 1 and 2)	**239,871**	-
ECL on loans and advances – non performing (Stage 3)	**2,737,931**	2,181,245
Collective impairment allowance	**-**	205,606
Less: Total impairment allowance	**2,977,802**	2,386,851

An analysis of changes in the carrying amount and the corresponding ECL allowances is as follows:

	Stage 1 AED'000	**Stage 2 AED'000**	**Stage 3 AED'000**	**Total AED'000**
Impairment allowance at 31 December 2017	-	**205,606**	**2,181,245**	**2,386,851**
Transition impact of IFRS 9	**88,751**	**(66,141)**	-	**22,610**
ECL allowance at 1 January 2018	**88,751**	**139,465**	**2,181,245**	**2,409,461**
Net (reversals) / impairment charge	**15,325**	**(3,670)**	**941,877**	**953,532**
Recoveries	-	-	**(72,486)**	**(72,486)**
Impairment losses - net	**15,325**	**(3,670)**	**869,391**	**881,046**
Amounts written off	-	-	**(312,705)**	**(312,705)**
At 31 December 2018	**104,076**	**135,795**	**2,737,931**	**2,977,802**

	Total AED'000
At 1 January 2017	2,291,469
Increase in provisions	553,023
Recoveries	(152,599)
Impairment losses – net	400,424
Amounts written off	(305,042)
At 31 December 2017	2,386,851

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

8 Investment securities

	2018 AED'000	2017 AED'000
Investments measured at fair value through other comprehensive income		
Opening balances as at 1 January	**143,980**	154,696
Fair value reserve movement	**(1,100)**	(1,286)
Disposal during the year	-	(9,366)
Impairment charged to statement of profit or loss	-	(64)
Balance at 31 December	**142,880**	143,980

9 Furniture and equipment

	Furniture fixtures and premises AED'000	Motor vehicles and other equipment AED'000	Total AED'000
Cost			
At 1 January 2017	25,845	7,140	32,985
Additions	1,178	37	1,215
Disposals and assets written off	(1,152)	(146)	(1,298)
At 31 December 2017	25,871	7,031	32,902
Additions	**1,924**	**376**	**2,300**
Transfers	**824**	**(824)**	**-**
Disposals and assets written off	**(198)**	**(298)**	**(496)**
At 31 December 2018	**28,421**	**6,285**	**34,706**
Accumulated depreciation			
At 1 January 2017	21,622	6,505	28,127
Charge for the year	(1,486)	(61)	(1,547)
Disposals and assets written off	(1,141)	(146)	(1,287)
At 31 December 2017	18,995	6,298	25,293
Charge for the year	**2,223**	**176**	**2,399**
Transfers	**383**	**(383)**	**-**
Disposals and assets written off	**(167)**	**(277)**	**(444)**
At 31 December 2018	**21,434**	**5,814**	**27,248**
Net book value			
At 31 December 2018	**6,987**	**471**	**7,458**
At 31 December 2017	6,876	733	7,609

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

10 Other assets

	2018 AED'000	2017 AED'000
Accrued interest receivable	**52,946**	62,567
Prepayments	**10,878**	12,806
Other receivables	**6,034**	6,454
	69,858	81,827

11 Due to banks

	2018 AED'000	2017 AED'000
Demand and call deposits	**44,460**	586
Term deposits	**2,354,911**	1,081,923
	2,399,371	1,082,509

12 Deposits from customers

	2018 AED'000	2017 AED'000
Demand deposits	**4,768,270**	5,360,681
Time deposits	**8,932,519**	8,305,448
Saving deposits	**495,418**	560,609
Other deposits	**11,631**	12,873
	14,207,838	14,239,611

13 Other liabilities

	2018 AED'000	2017 AED'000
Accrued interest payable	**116,105**	87,703
Staff terminal benefits	**18,608**	17,680
Provision for taxation (refer note 22)	**36,170**	31,786
Banker's cheque	**28,593**	27,436
ECL on unfunded exposures	**2,240**	-
Others	**114,713**	114,536
	316,429	279,141

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

14 Head Office assigned capital

This represents the amount received from the Head Office as Head Office assigned capital to the UAE branches of the Bank. On 21 December 2015, the Bank increased its Head Office assigned capital from AED 390,000 thousand to AED 760,000 thousand by additional funding provided by the Head Office.

15 Statutory reserve

In accordance with the Federal Law No. 2 of 2015, Bank needs to allocate a minimum of 10% of their annual net profits to non-distributable legal and statutory reserve until such reserve equals 50% of the assigned capital of the Bank. As the Bank had a net loss during the year, no transfer (2017: AED 7.1 million) has been made during the year.

16 Interest income

	2018 AED'000	2017 AED'000
On loans and advances to financial institutions / banks	**124,375**	126,325
On loans and advances to customers	**591,511**	558,543
On investment securities	**3,122**	3,985
	719,008	688,853

17 Interest expense

	2018 AED'000	2017 AED'000
On deposits from banks and financial institutions	**110,231**	89,108
On deposits from customers	**168,147**	157,467
	278,378	246,575

18 Fee and commission income and expense

	2018 AED'000	2017 AED'000
Personal Banking	**17,599**	8,316
Corporate Banking	**46,048**	52,918
Others	**15,980**	14,363
	79,627	75,597
Fee expense:		
Fee and commission expense	**(1,129)**	(183)

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

19 Other operating income

	2018 AED'000	2017 AED'000
Foreign exchange income	**31,431**	32,070
Others	**44,743**	44,761
	76,174	76,831

20 Personnel expenses

	2018 AED'000	2017 AED'000
Staff salaries and allowances	**46,065**	48,949
Pension and retirement benefits	**2,873**	4,076
Others	**2,252**	1,382
	51,190	54,407

21 General and administrative expenses

	2018 AED'000	2017 AED'000
Central management expense	**9,974**	9,350
Rent expense	**14,387**	14,305
Legal and professional charges	**34,262**	9,089
Other miscellaneous expenses	**20,000**	18,281
	78,623	51,025

22 Taxation

Provision for taxation is made in accordance with regulations enacted in the Emirates of Abu Dhabi, Dubai, Sharjah and Ras Al Khaimah relating to the computation of tax payable.

	2018 AED'000	2017 AED'000
Movement in tax provision		
Balance at 1 January	**31,786**	123,732
Current year tax expense	**26,927**	19,165
Prior year tax expense	**5,675**	-
Deferred tax- Origination of temporary differences	**-**	6,608
Taxes paid	**(28,218)**	(117,719)
Balance at 31 December	**36,170**	31,786

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

22 Taxation (continued)

	2018 AED'000	2017 AED'000
Current tax expense		
Provision for current year tax	**26,927**	31,786
Provision made for prior year tax	**5,675**	(6,013)
Total current tax expense	**32,602**	25,773
Deferred tax - origination of temporary differences	**58,125**	(6,608)
Total income tax expense	**90,727**	19,165

The tax charge is determined by applying the official tax rate of 20% to the taxable profit arising in the Emirates of Abu Dhabi, Dubai, Sharjah and Ras Al Khaimah.

	2018 AED'000	2017 AED'000
Profit before tax	**134,637**	88,766
Income tax at applicable tax rate – 20%	**26,927**	17,753
Deferred tax utilization	**58,125**	-
Tax for prior years	**5,675**	1,336
Unrecognised tax loss	**-**	76
Tax expense	**90,727**	19,165

The tax laws do not permit adjustment of a tax loss incurred in one Emirate with a tax profit of another Emirate. Therefore, the tax expense for the UAE branches of Bank of Baroda has been computed on taxable profit generated by the branches of the Bank in the Emirates of Abu Dhabi.

22.1 Deferred tax

Deferred taxation comprises of impairment provisions on loans and advances and interest in suspense. The movement in deferred tax during the year is as follows:

	2018 AED'000	2017 AED'000
Balance at 1 January	**511,614**	505,006
Additions during the year	**-**	158,703
Utilisation during the year	**(58,125)**	(152,095)
Balance at 31 December	**453,489**	511,614

23 Commitments and contingent liabilities

At any time the Bank has outstanding commitments to extend credit. These commitments take the form of approved loan facilities. Outstanding loan commitments have commitment periods that do not extend beyond the normal underwriting and settlement period.

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

23 Commitments and contingent liabilities (continued)

The Bank provides financial guarantees and letters of credit to guarantee the performance of customers to third parties.

The contractual amounts of commitments and contingent liabilities are set out in the following table by category. The amounts reflected in the table for commitments assume that amounts are fully advanced. The amounts reflected in the table for guarantees and letters of credit represent the maximum accounting loss that would be recognised at the reporting date if counterparties failed completely to perform as contracted.

At 31 December, the Bank's commitments and contingent liabilities were as follows:

	2018	2017
	AED'000	AED'000
Letters of credit	**561,680**	613,706
Guarantees	**1,121,830**	1,276,455
Undrawn loan commitments	**2,923,630**	5,284,849
Foreign exchange and forward commitments	**3,296,362**	5,442,558
	7,903,502	12,617,568

The commitments and contingent liabilities above may expire without being funded in whole or in part. Therefore, the amounts do not represent expected future cash flows.

Derivative financial instruments are disclosed under Note 25.7

23. 1 Contingencies

In the prior year, the Bank appointed a legal consulting firm for looking into historical transactions related to few customers, to assess the compliance with the relevant anti money laundering laws and regulations. The legal consulting firm is in the process of performing the due procedures required and has not yet concluded.

As on date there is no contingent liability against the Bank and also there has been no claim, proceeding or any regulatory action in UAE or in the home country against the Bank. No further disclosures regarding contingent liability arising from this is being made by the Bank, as the Bank believes that such disclosures may be prejudicial and detrimental to the Bank's position.

24 Cash and cash equivalents

	2018	2017
	AED'000	AED'000
Cash and balances with the UAE Central Bank (maturing within three months)	**2,741,272**	2,261,799
Due from banks (maturing within three months)	**884,373**	539,304
Due from the Head Office and branches (maturing within three months)	**3,318,692**	3,078,737
Due to banks (maturing within three months)	**(1,980,851)**	(582,893)
Due to the Head Office and branches (maturing within three months)	**(190,923)**	(46,398)
Cash and cash equivalents in the statement of cash flow	**4,772,563**	5,250,549

25 Financial risk management

25.1 Introduction and overview

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

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

The Bank has exposure to the following material risks from its use of financial instruments:

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

This note presents information about the Bank's exposure to each of the above risks, the Bank's objectives, risk management frameworks, policies and processes for measuring and managing risk and the management of the Bank's capital.

25.2 Risk management framework

The Bank through its Risk Management Framework (RMF):

- Establishes common principles and standards for the management and control of all risks and to inform behaviour across the organisation;
- Provides a shared framework and language to improve awareness of risk management processes; and
- Provides clear accountability and responsibility for risk management.

The core components of the RMF include risk classifications, risk principles and standards, definitions of roles, responsibilities and governance structure. It also includes a clear definition of key terms to ensure that we use them consistently.

25 Financial risk management (continued)

25.2 Risk management framework (continued)

Risk principles

Risk principles are adopted by the Risk Management Committee. The principles describe the risk culture that the Bank wishes to sustain and develop. They provide the foundation point of the revised Risk framework. All risk decisions and risk management activity should be in line with, and in the spirit of, the overall risk principles of the Bank. The principles are as follows:

(a) Balancing risk and reward

Risk is taken in support of the requirements of the Bank's stakeholders. Risk should be taken in support of strategy and within risk appetite responsibility.

(b) Responsibility

It is the Bank's responsibility to ensure that risk taking is both disciplined and focused. The Bank takes account of social responsibilities in taking risks to produce a return.

(c) Accountability

Risk is taken only within agreed authorities and where there is appropriate infrastructure and resources. All risk taking must be transparent, controlled and reported.

(d) Anticipation

The Bank looks to anticipate future risks and to ensure awareness of all risk.

(e) Risk management

The Bank has a specialist risk function, with strength in depth, experience across all risk types and economic scenarios.

The Bank's management has overall responsibility for the establishment and oversight of the Bank's risk management framework. The risk management department is responsible for implementing and maintaining risk related procedures to ensure an independent control process. It works closely with the commercial organisation to support their activities, while safe-guarding the risk profile of the Bank. It institutes prudent risk monitoring and control mechanisms (processes and systems) to ensure compliance of individual risk assets and portfolios to agreed terms and policy parameters. It reviews and presents all credit submissions, risk policy and portfolio management reports to the Corporate Head Office of the Bank situated in Mumbai.

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

25 Financial risk management (continued)

25.2 Risk management framework (continued)

Risk principles (continued)

(e) Risk management (continued)

The Bank continues to re-examine the entire process, inherent risk factors and controls and consider opportunities by rationalising regulatory risk management initiatives. Experiencing from the crisis, and to deliver value beyond mere adherence, one part of the framework is Internal Capital Adequacy Assessment Process (ICAAP), to assess capital to cover risks not covered under Pillar 1. This ICAAP exercise has demonstrated that the Bank has sufficient capital buffers to cushion any extreme circumstances or scenarios and the Bank has adequate risk bearing capacity at 99.9% confidence level.

The Bank has established polices, procedures, processes and controls and has provided the risk team with adequate support by way of risk systems and tools for measuring and reporting risk for monitoring, controlling, reviewing and managing risk.

25.3 Credit risk

Credit risk is the risk of financial loss to the Bank if a customer or counterparty will fail to meet a commitment / contractual obligation, resulting in financial loss to the Bank. Such risk arises from lending, trade finance, treasury and other activities undertaken by the Bank. Credit risk is actively monitored in accordance with the credit policies which clearly define delegated lending authorities, policies and procedures. The management of credit risk also involves the monitoring of risk concentrations by industrial sector as well as by geographic location.

(a) Credit risk management

Procedures for managing credit risk are determined at the business levels with specific policies and procedures being adapted to different risk environments and business goals. The Bank has established a credit quality review process to provide early identification of possible changes in the creditworthiness of counterparties, including regular collateral revisions. Credit analysis includes review of facility details, credit grade determination and financial spreading/ratio analysis. Counterparty limits are established by the use of a credit risk classification system, which assigns each counterparty a risk rating. Risk ratings are reviewed annually. The credit quality review process allows the Bank to assess the potential loss as a result of the risks to which it is exposed and take corrective action. The businesses work with the Head of Risk Management to take responsibility for managing pricing risk, portfolio diversification and overall asset quality within the requirements of the Bank's standards, policies and business strategy.

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

25 Financial risk management (continued)

25.3 Credit risk (continued)

(a) Credit risk management (continued)

The table below shows the maximum exposure to credit risk for the components of the statement of financial position, including contingent liabilities and commitments. The maximum exposure is shown, before the effect of mitigation through the use of credit enhancements, master netting and collateral agreements.

	Note	2018 AED'000	2017 AED'000
Cash and balances with the UAE Central Bank (excluding cash on hand)	5	**2,873,392**	3,090,558
Due from banks	6	**884,373**	741,318
Due from Head Office and other branches	27	**3,610,584**	3,133,754
Loans and advances to customers	7	**16,187,490**	14,230,344
Investment securities	8	**142,880**	143,980
Customers' indebtedness under acceptances	26	**380,227**	622,486
Derivative - net	25	**4,367**	2,215
Other assets (excluding prepayments)	10	**58,980**	69,020
		24,142,293	22,033,675
Letters of credit	23	**561,680**	613,706
Guarantees	23	**1,121,830**	1,276,455
Foreign Exchange forward commitments	23	**3,296,362**	5,442,558
Undrawn loan commitments	23	**2,923,630**	5,284,849
		7,903,502	12,617,568
Total credit risk exposure		**32,045,795**	34,651,243

Where financial instruments are recorded at fair value the amounts shown above represent the current credit risk exposure, but not the maximum risk exposure that could arise in the future as a result of changes in values.

For more detail on the maximum exposure to credit risk for each class of financial instrument, references have been made to the specific notes. The effect of collateral and other risk mitigation technique is discussed below.

25 Financial risk management (continued)

25.3 Credit risk (continued)

(b) Credit risk measurement

As explained in note 3.5 (e), 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.

Stage wise ECL impairment

Policies and the Bank's framework in relation to stage wise impairment have been explained in detail in note 3.5 (e).

Collateral and other credit enhancements

The amount and type of collateral required depends on an assessment of the credit risk of the counterparty. The Bank holds collateral against loans and advances to customers in the form of cash margins, pledges/liens over deposits, mortgage interests over property, other registered securities over assets and guarantees. The Bank accepts guarantees from parent companies for loans to their subsidiaries or other Bank companies. Bank monitors the market value of collateral, requests additional collateral in accordance with the underlying agreement, and monitor the market value of collateral obtained during its periodic review of credit facilities and of the adequacy of the allowance for impairment losses. It is the Bank's policy to dispose of repossessed properties in an orderly fashion. The proceeds are used to reduce or repay the outstanding claim. In general, the Bank does not occupy repossessed properties for business use.

It is the Bank's policy to ensure that loans are extended to customers within their capability to service interest and repay principal instead of relying excessively on collateral. Accordingly, depending on customers' credit worthiness and the type of product, facilities may be unsecured. Nevertheless, collateral is and can be an important credit risk mitigant.

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

25 Financial risk management (continued)

25.3 Credit risk (continued)

(b) Credit risk measurement (continued)

Credit quality analysis

The following table sets out information about the credit quality of financial assets. Unless specifically indicated, for financial assets, the amounts in the table represent gross carrying amounts. For loan commitments and financial guarantee contracts, the amounts in the table represent the amounts committed or guaranteed, respectively.

As of 31 December 2018	Stage 1		Stage 2		Stage 3		Total	
	AED'000 Exposure	AED'000 Provision	AED'000 Exposure	AED'000 Provision	AED'000 Exposure	AED'000 Provision	AED'000 Exposure	AED'000 Provision
Balances with the Central Bank of the UAE	2,991,272	-	-	-	-	-	2,991,272	-
Due from banks	884,373	-	-	-	-	-	884,373	-
Due from Head Office and other branches	3,610,584	-	-	-	-	-	3,610,584	-
Loans and advances to customers	11,427,351	104,076	1,799,998	135,795	2,960,141	2,737,931	16,187,490	2,977,802
Investment securities	142,880	-	-	-	-	-	142,880	-
Other financial assets (excluding prepayments)	63,707	-	-	-	-	-	63,707	-
Unfunded exposure	4,573,324	2,151	33,816	89	-	-	4,607,140	2,240
	23,693,491	106,227	1,833,814	135,884	2,960,141	2,737,931	28,487,446	2,980,042

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

25 Financial risk management (continued)

25.3 Credit risk (continued)

(b) Credit risk measurement (continued)

Credit quality analysis (continued)

The following table sets out information about the credit quality of financial assets. Unless specifically indicated, for financial assets, the amounts in the table represent gross carrying amounts. For loan commitments and financial guarantee contracts, the amounts in the table represent the amounts committed or guaranteed, respectively.

As of 1 January 2018	Stage 1		Stage 2		Stage 3		Total	
	AED'000 Exposure	AED'000 Provision	AED'000 Exposure	AED'000 Provision	AED'000 Exposure	AED'000 Provision	AED'000 Exposure	AED'000 Provision
Balances with the Central Bank of the UAE	3,293,981	-	-	-	-	-	3,293,981	-
Due from banks	798,576	-	-	-	-	-	798,576	-
Due from Head Office and other branches	3,133,754	-	-	-	-	-	3,133,754	-
Loans and advances to customers	9,817,458	88,751	2,152,832	139,465	2,292,960	2,181,245	14,263,250	2,409,461
Investment securities	143,980	-	-	-	-	-	143,980	-
Other financial assets (excluding prepayments)	75,963	-	-	-	-	-	75,963	-
Unfunded exposures	5,402,859	1,609	1,772,151	187	-	-	7,175,010	1,796
	22,666,571	90,360	3,924,983	139,652	2,292,960	2,181,245	28,884,514	2,411,257

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

25 Financial risk management (continued)

25.3 Credit risk (continued)

(b) Credit risk measurement (continued)

Credit quality per class of financial assets

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

31 December 2017

Individually impaired	**Loans and advances**	**Due from banks,Head Office and other branches**	**Investment securities**
	2017 AED'000	2017 AED'000	2017 AED'000
Carrying amount, net	11,876,994	3,875,073	143,980
Impaired portfolio			
Substandard	246,209	-	-
Doubtful	622,570	-	-
Legal and loss	1,775,166	-	-
Total impaired portfolio	2,643,945	-	-
Specific allowance on impairment	(2,177,184)	-	-
Carrying amount	466,761	-	-
Non Impaired portfolio			
Past due but not impaired (overdue till 90 days)	1,913,152	-	-
Neither past due nor impaired	9,706,748	3,875,073	143,980
Total non-impaired portfolio	11,619,900	3,875,073	143,980
Collective impairment provision	(205,512)	-	-
Provision on restructured accounts	(4,155)	-	-
Carrying amount	11,410,233	3,875,073	143,980
Net carrying amount	11,876,994	3,875,073	143,980

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

25 Financial risk management (continued)

25.3 Credit risk (continued)

(c) Risk mitigation

Collateral types which are eligible for risk mitigation include cash, residential, commercial and industrial properties, marketable securities, commodities, and plant and machinery in addition to bank guarantees and letters of credit. The valuation frequency of collateral is driven by the level of volatility in each class of collateral. Collateral held against impaired loans is maintained at fair value, which is the current market value of collateral under the assumption of 'normal' market conditions.

(d) Concentration risk

Credit concentration risk is managed via portfolio standards and within concentration caps set for counterparties or related parties and for industry sectors and credit grade bands.

Concentration of risk is managed by client/counterparty, by geographical region and by industry sector. The maximum credit exposure to any client or counterparty as of 31 December 2018 was AED 1,481 million (2017: AED 1,334 million) before taking account of collateral or other credit enhancements.

The Bank's maximum gross exposure to credit risk, before taking into account any collateral held or other credit enhancements can be analysed by the following geographical regions and sector wise:

Concentration by location	**Loans and advances**		**Due from banks,Head Office and other branches**		**Investment securities**	
	2018	2017	**2018**	2017	**2018**	2017
	AED'000	AED'000	**AED'000**	AED'000	**AED'000**	AED'000
Carrying amount	**16,187,490**	14,230,344	**4,412,220**	3,875,073	**142,880**	143,980
United Arab Emirates	**13,436,585**	11,260,869	**200,000**	34,427	**142,880**	143,980
Other Middle East Countries	**60,490**	32,868	**171,920**	-	-	-
India	**1,679,586**	1,323,804	**1,193,725**	1,965,097	-	-
Europe	**101,939**	320,379	**1,193,725**	641,730	-	-
USA	**15,436**	19,853	**550,950**	550,950	-	-
Others	**893,454**	1,272,571	**1,101,900**	682,869	-	-
	16,187,490	14,230,344	**4,412,220**	3,875,073	**142,880**	143,980

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

25 Financial risk management (continued)

25.3 Credit risk (continued)

(d) Concentration risk (continued)

Concentration by sector	Loans and advances		Due from banks,Head Office and other branches		Investment securities	
	2018	2017	**2018**	2017	**2018**	2017
	AED'000	AED'000	**AED'000**	AED'000	**AED'000**	AED'000
Agriculture	**-**	-	**-**	-	**-**	-
Mining and quarrying	**591,441**	1,130,273	**-**	-	**-**	-
Manufacturing	**2,645,028**	3,119,883	**-**	-	**-**	-
Electricity, gas and water	**185,176**	1,260	**-**	-	**-**	-
Real estate	**585,291**	-	**-**	-	**-**	-
Trade	**3,948,577**	4,788,850	**-**	-	**-**	-
Transport and communication	**365,955**	251,228	**-**	-	**-**	-
Banks and financial institutions	**893,906**	212,190	**4,412,220**	3,875,073	**-**	-
Government	**785,036**	785,036	**-**	-	**142,880**	143,980
Others	**6,187,080**	3,941,624	**-**	-	**-**	-
	16,187,490	14,230,344	**4,412,220**	3,875,073	**142,880**	143,980

Investment Securities

The Bank has investments in debt securities which are measured at fair value through other comprehensive income. Credit risk in these investments is managed within the overall credit risk appetite for corporates and financial institutions. The following table provide analysis of the debt securities. The standard credit ratings used by the Bank are those assessed by Standard & Poors or their equivalent.

Analysis of investment securities

	2018	2017
	AED'000	AED'000
Rating		
A- to A+	**142,880**	143,980
	142,880	143,980

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

25 Financial risk management (continued)

25.3 Credit risk (continued)

Aging analysis of past due but not impaired loans

The following table sets out the aging of loans and advances which are past due but not impaired and for which no individual impairment provision has been raised. A loan is considered to be past due when the counterparty has failed to make a principal or interest payment when contractually due. Past due status of a loan does not necessarily mean that the counterparty is impaired.

Particulars	**2018 Loans to customers**			2017 Loans to customers		
	Consumer AED'000	**Wholesale AED'000**	**Total AED'000**	Consumer AED'000	Wholesale AED'000	Total AED'000
Up to 30 days past due	**-**	**472,824**	**472,824**	-	1,628,870	1,628,870
Between 31-60 days past due	**1,450**	**312,115**	**313,565**	-	127,327	127,327
Between 61-90 days past due	**6,557**	**145,313**	**151,870**	-	156,955	156,955
	8,007	**930,252**	**938,259**	-	1,913,152	1,913,152

25.4 Market risk

Market risk is the risk that changes in market prices such as interest rates, equity prices and foreign exchange rates and credit spreads (not relating to change in the obligor's/issuer's credit standing) - will affect the Bank's profit or the value of its holdings of financial instruments. The objective of market risk management is to manage and control market risk exposures within acceptable parameters to ensure the Bank's solvency while optimising the return on risk. The Bank is exposed to market risk on its banking book as well as trading book. Market risk in the banking book is managed in accordance with the Bank's Asset and Liability Committee (ALCO), while market risk in the trading book is managed in accordance with the investment policy and treasury policy. The Bank has very limited trading portfolio, hence it is not exposed to any significant market risk in respect atrading portfolio.

(a) Management of market risk

Market risk is governed by the Bank's approved ALCO committee, investment policy and treasury policy which define levels of risk appetite in terms of Earning at Risk, forex positions and aggregate gap limit. The Asset Liability Management Committee provides market risk oversight and guidance on policy setting. The investment and treasury policies cover both trading and non-trading books of the Bank.

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

25 Financial risk management (continued)

25.4 Market risk (continued)

(b) Interest rate risk

The principal risk to which non-trading portfolios are exposed is the risk of loss from fluctuations in the future cash flows or fair values of financial instruments because of changes in market interest rates. The Bank is exposed to interest rate risk as a result of mismatches or gaps in the amounts of assets and liabilities and off-balance sheet instruments that mature or reprice in a given period. Interest rate risk is managed principally through monitoring interest rate gaps and establishing limits on the interest rate gaps for stipulated periods. The ALCO is the monitoring body for compliance with these limits. Interest rate risk is also assessed by measuring the impact of reasonable possible interest rate movements.

Sensitivity analysis - interest rate risk

	2018 **AED'000**	2017 AED'000
Shift in yield curve		
+100 bps	**9,190**	11,249
-100 bps	**(9,190)**	(11,249)

A substantial portion of the Bank's assets and liabilities are re-priced within 1-year. Accordingly there is limited exposure to interest rate 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 the management to mitigate the effect of interest rate movements.

The assets and liabilities repricing profile has been determined on the basis of the final maturity period or interest repricing periods at the reporting date, whichever is earlier.

The matching and controlled mismatching of the maturities and interest rates of assets and liabilities is fundamental to the management of the Bank. It is unusual for banks to be completely matched, as transacted business is often of uncertain term and of different types. An unmatched position potentially enhances profitability, but also increases the risk of losses. 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 Bank's interest rate gap position on assets and liabilities based on she contractual re-pricing dates is as follows:

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

25 Financial risk management (continued)

25.4 Market risk (continued)

(b) Interest rate risk (continued)

Particulars	Less than one month AED'000	1 to 3 months AED'000	3 to 6 months AED'000	6 months to year AED'000	Over 1 year AED'000	Non interest bearing AED'000	Total AED'000	Effective interest rate
2018								
Cash and balances with the Central Bank of the UAE	800,000	450,000	250,000	-	-	1,491,272	2,991,272	1.78 - 2 35%
Due from banks	720,855	146,920		-	-	16,598	884,373	2.45 – 3.4%
Due from the Head Office and other branches	2,626,195	642,775	183,650	91,825	-	66,139	3,610,584	0.85 - 3.7%
Loans and advances to customers	2,805,907	2,921,395	541,943	933,909	6,006,534	-	13,209,688	3.50 - 9.45%
Investment securities	-	-	-	-	142,880	-	142,880	2.15%
Customers indebtedness under acceptances	-	-	-	-	-	380,227	380,227	-
Furniture and equipments	-	-	-	-	-	7,458	7,458	-
Derivatives	-	-	-	-	-	4,367	4,367	-
Deferred tax asset	-	-	-	-	-	453,489	453,489	
Other assets	-	-	-	-	-	58,980	58,980	-
Total assets	6,952,957	4,161,090	975,593	1,025,734	6,149,414	2,478,530	21,743,318	
Due to banks	1,371,866	476,745	-	506,300	-	44,187	2,399,098	0.9 - 3.65%
Due to the Head Office and other branches	176,304	62,074	134,799	1,289,958	367,300	45,532	2,075,967	0.82 – 3.4%
Deposits from customers	1,115,579	2,002,917	2,017,488	3,680,471	622,839	4,768,544	14,207,838	0 - 4%
Liabilites under acceptances	-	-	-	-	-	380,227	380,227	-
Other liabilities	-	-	-	-	-	316,429	316,429	-
Total liabilities	2,663,749	2,541,736	2,152,287	5,476,729	990,139	5,554,919	19,379,559	
On balance sheet interest rate sensitivity gap – 2018	4,289,208	1,619,354	(1,176,694)	(4,450,995)	5,159,275	(3,076,389)	2,363,759	
Cumulative interest rate sensitivity gap -2018	4,289,208	5,908,562	4,731,868	280,873	5,440,148	2,363,759	-	

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

25 Financial risk management (continued)

25.4 Market risk (continued)

(b) Interest rate risk (continued)

Particulars 2017	**Less than one month** AED'000	**1 to 3 months** AED'000	**3 to 6 months** AED'000	**6 months to year** AED'000	**Over 1 year** AED'000	**Non interest bearing** AED'000	**Total** AED'000	**Effective interest rate**
Cash and balances with the Central Bank of the UAE	900,000	450,000	250,000	-	-	1,693,981	3,293,981	0.9 - 1.35%
Due from banks	57,729	462,798	110,190	91,825	-	76,034	798,576	1.9 - 2.3%
Due from the Head Office and other branches	2,747,404	330,570	7,346	13,201	-	35,233	3,133,754	0.15-2.55%
Loans and advances to customers	1,371,928	2,850,719	676,187	1,497,225	5,480,935	-	11,876,994	3.5-9.45%
Investment securities	-	-	-	-	143,980	-	143,980	1.5-2.5%
Customers indebtedness under acceptances	-	-	-	-	-	622,486	622,486	-
Furniture and equipments	-	-	-	-	-	7,609	7,609	-
Derivatives	-	-	-	-	-	2,215	2,215	-
Other assets	-	-	-	-	-	593,440	593,440	-
Total assets	5,077,061	4,094,087	1,043,723	1,602,251	5,624,915	3,030,998	20,473,035	
Due to banks	444,433	138,460	95,000	36,730	367,300	586	1,082,509	1.5-2.3%
Due to the Head Office and other branches	-	3,306	1,836	3,673	1,285,550	45,927	1,340,292	1.25-4.35%
Deposits from customers	1,377,877	2,519,379	1,526,996	3,236,701	217,977	5,360,681	14,239,611	0-4%
Liabilites under acceptances	-	-	-	-	-	622,486	622,486	-
Other liabilities	-	-	-	-	-	279,140	279,140	-
Total liabilities	1,822,310	2,661,145	1,623,832	3,277,104	1,870,827	6,308,820	17,564,038	
On balance sheet interest rate sensitivity gap – 2017	3,254,751	1,432,942	(580,109)	(1,674,853)	3,754,088	(3,277,822)	2,908,997	
Cumulative interest rate sensitivity gap -2017	3,254,751	4,687,693	4,107,584	2,432,731	6,186,819	2,908,997	-	

25 Financial risk management (continued)

25.4 Market risk (continued)

(c) Currency risk

Currency risk is the risk that the value of a financial instrument will fluctuate due to changes in foreign exchange rates. The Bank has set limits on positions by currency. Positions are monitored on a daily basis and hedging strategies used to ensure positions are maintained within established limits.

As the UAE Dirham and other GCC currencies, except Kuwait are currently pegged to the US Dollar, balances in US Dollars are not considered to represent significant currency risk.

(d) Equity price risk

Equity price risk is the possibility that equity prices will fluctuate, affecting the fair value of equity investments and other instruments that derive their value from a particular equity investment or index of equity prices. The Bank has no exposure to equity price risk as at 31 December 2018.

25.5 Liquidity risk

Liquidity risk is the risk that the Bank will encounter difficulty in meeting obligations associated with its financial liabilities that are settled by delivering cash or another financial asset. Liquidity risk can be segregated into two broad categories:

(1) Funding liquidity risk is the risk that the Bank will encounter difficulty in funding the increase in assets and meeting its obligations associated with financial liabilities that are settled by delivering cash or other financial assets, without incurring unacceptable losses.

(2) Market liquidity risk is the risk that the Bank cannot easily offset or eliminate a position at the market price because of market disruption or inadequate market depth.

(i) Management of liquidity risk

The Bank manages liquidity risk on a short term, medium term and long term basis. The Bank's approach to managing liquidity is to ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the Bank's reputation. ALCO is the responsible governing body that approves the Bank's liquidity management policies. Liquidity is managed by the ALCO within the predefined liquidity limits as set out in the Board approved Asset Liability Management Policy. ALCO is responsible for ensuring that the Bank is self-sufficient and is able to meet all its obligations to make payments as they fall due by operating within the liquidity limits set for the Bank.

25 Financial risk management (continued)

25.5 Liquidity risk (continued)

The key elements of the Bank's liquidity strategy are as follows :

(a) Maintaining a diversified funding base consisting of customer deposits (both retail and corporate) and wholesale market deposits and maintaining contingency facilities;

(b) Carrying a portfolio of highly liquid assets, diversified by currency and maturity;

(c) Monitoring liquidity ratios, maturity mismatches, behavioral characteristics of the Bank's financial assets and liabilities, and the extent to which the Bank's assets are encumbered and so not available as potential collateral for obtaining funding; and

(d) Carrying out stress testing of the Bank's liquidity position.

Liquidity requirements to support calls 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. The total outstanding contractual amount of commitments to extend credit does not necessarily represent future cash requirements, as many of these commitments will expire or terminate without being funded.

Exposure to liquidity risk

The key measure used by the Bank for managing liquidity risk is the ratio of net liquid assets (i.e. total assets by maturity against total liabilities by maturity) and its loans to deposit ratio.

	2018 **AED'000**	2017 AED'000
Loans and advances to customers, net	**13,209,688**	11,876,994
Deposits from customers	**14,207,838**	14,239,611
Loans to deposit ratio	**92.97%**	83.41%

Details of the Bank's net liquid assets are summarised in the table below by the maturity profile of the Bank's assets and liabilities based on the contractual repayments. The maturity profile is monitored by the management to ensure adequate liquidity is maintained.

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

25 Financial risk management (continued)

25.5 Liquidity risk (continued)

Maturity profile of asset and liabilities

Particulars	Less than one month AED'000	1 to 3 months AED'000	3 to 6 months AED'000	6 months to year AED'000	Over 1 year AED'000	Total AED'000
Cash and balances withthe Central Bank of the UAE	2,291,272	450,000	250,000	-	-	2,991,272
Due from banks	737,453	146,920			-	884,373
Due from the head office and other branches	2,675,916	642,775	200,068	91,825	-	3,610,584
Loans and advances to customers	2,805,907	2,921,395	541,943	933,909	6,006,534	13,209,688
Investment securities	-	-	-	-	142,880	142,880
Derivatives	4,367	-	-	-	-	4,367
Other assets	58,980	-	-	-	-	58,980
Total assets	8,573,895	4,161,090	992,011	1,025,734	6,149,414	20,902,144

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

25 Financial risk management (continued)

25.5 Liquidity risk (continued)

Maturity profile of asset and liabilities (continued)

Particulars	Less than one month AED'000	1 to 3 months AED'000	3 to 6 months AED'000	6 months to year AED'000	Over 1 year AED'000	Total AED'000
Due to banks	1,590,710	390,513	132,228	285,920	-	2,399,371
Due to the head office and other branches	192,452	3,306	2,571	1,510,338	367,300	2,075,967
Deposits from customers	5,884,123	2,002,971	2,017,488	3,680,471	622,785	14,207,838
Other liabilities	316,429	-	-	-	-	316,429
Total liabilities	7,983,714	2,396,790	2,152,287	5,476,729	990,085	18,999,605
Net on balance sheet liquidity gap 2018	590,181	1,764,300	(1,160,276)	(4,450,995)	5,159,329	1,902,539
At 31 December 2017:						
Total assets	10,106,523	3,078,014	1,724,906	974,720	3,447,163	19,331,326
Total liabilities	7,830,773	2,933,644	1,583,618	2,796,315	1,797,184	16,941,554
Net on balance sheet liquidity gap 2017	2,275,750	144,370	141,288	(1,821,595)	1,649,979	2,389,772

25 Financial risk management (continued)

25.6 Operational risk

Operational risk is the risk of loss arising from systems failure, human error, fraud or the impact of external events. Operational risks emanate from every segment of Bank's operation and are faced by all the business units. The Bank's objective is to manage operational risk so as to balance the avoidance of financial losses and damage to the Bank's reputation with overall cost effectiveness and innovation. In all cases, the Bank's policy requires compliance with all applicable legal and regulatory requirements.

The Bank has taken measures to put in place tools, firstly to identify all such operational risks. The Bank has also taken measures to implement processes and policies to mitigate the risk to an acceptable level and to avoid or minimise financial losses and damage to Bank's reputation. In order to ensure a structured and focused operational risk management process, the Bank has also an Operational Risk Management Committee ("ORMC") whose mandate is to oversee operational risk management process, consider each operational risk in order of "priority by significance", to develop policies, processes and procedures for managing operational risk in all of the Bank's material products, activities, processes and systems as well as recommend best way to integrate the operational risk management in the overall organisation wide risk management process. ORMC is to develop overall Bank standards for the management of operational risk in the following areas:

(a) requirements for appropriate segregation of duties, including the independent authorisation of transactions;
(b) requirements for the reconciliation and monitoring of transactions;
(c) compliance with regulatory and other legal requirements;
(d) documentation of controls and procedures;
(e) requirements for the periodic assessment of operational risks faced, and the adequacy of controls and procedures to address the risks identified;
(f) requirements for the reporting of operational losses and proposed remedial action;
(g) development of contingency plans;
(h) training and professional development;
(i) ethical and business standards; and
(j) risk mitigation, including insurance where this is cost effective.

Compliance with Head Office standards is supported by a programme of periodic reviews undertaken by internal audit. The results of internal audit reviews are shared with Audit Committee at Head Office level and Senior Management of the Bank.

In addition to the reviews by internal audit, the compliance with policies and procedures is strengthened by reviews of compliance and operational risk manager.

25 Financial risk management (continued)

25.7 Derivative financial instruments

The Bank enters into a variety of derivative financial instruments for hedging purposes. Derivative financial instruments used by the Bank include swaps and foreign exchange forward contracts. The Bank is not engaged in any trading in derivatives. Derivatives are used purely for the hedging purposes for the clients as well as the Bank's own balance sheet positions.

Swaps are agreements between the Bank and other parties to exchange future cash flows based upon agreed notional amounts. Swaps most commonly used by the Bank are interest rate swaps. Under interest rate swaps, the Bank agrees with other parties to exchange, at specified intervals, the difference between fixed-rate and floating-rate interest amounts calculated by reference to an agreed notional amount.

Foreign exchange forward contracts are commitments to either purchase or sell foreign currencies at a specified future date for a specified price.

The Bank is subject to credit risk arising from the respective counterparties' failure to perform. Market risk arises from the possibility of unfavourable movements in interest rates relative to the contractual rates. However, market risk in most of the cases is covered through back-to-back deals to square the Bank's position

25 Financial risk management (continued)

25.7 Derivative financial instruments (continued)

The table below shows the positive and negative fair values of derivative financial instruments, which are equivalent to the market values, together with the notional amounts analysed by the term to maturity.

				Notional amount by term of maturity			
	Positive fair value AED'000	Negative fair value AED'000	Notional amount AED'000	Within 3 months AED'000	3-12 months AED'000	1-5 years AED'000	Over 5 years AED'000
2018							
Foreign exchange contracts	**4,727**	**360**	**3,296,362**	**1,377,799**	**1,494,955**	**423,607**	**-**
	4,727	**360**	**3,296,362**	**1,377,799**	**1,494,955**	**423,607**	**-**
2017							
Foreign exchange contracts	6,942	4,727	5,442,558	2,673,342	2,617,546	151,670	-
	6,942	4,727	5,442,558	2,673,342	2,617,546	151,670	-

25 Financial risk management (continued)

25.8 Capital risk management

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

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

(1) Safeguarding the Bank's ability to continue as a going concern and increase return for stakeholders; and

(2) Comply with regulatory capital set by the Central Bank of the UAE.

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

The Bank also assesses its capital requirements internally taking into consideration growth requirements and business plans, and quantifies its regulatory and risk / economic capital requirements within its integrated ICAAP Framework. Risks such as interest rate risk in the banking book, concentration risk, strategic risk, legal and compliance risk, stress risk, insurance risk and reputational risk are all part of the ICAAP.

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

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

- CET1 capital is the highest quality form of capital, comprising share capital, legal, statutory and other reserves, fair value reserve, retained earnings, after deductions for intangibles and other regulatory adjustments relating to items that are included in equity but are treated differently for capital adequacy purposes under 'CBUAE' guidelines.

- Tier 2 capital comprises of collective provision which shall not exceed 1.25% of total credit risk weighted assets.

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

25 Financial risk management (continued)

25.8 Capital risk management (continued)

The CBUAE issued Basel III capital regulations, which came into effect from 1 February 2017 introducing minimum capital requirements at three levels, namely Common Equity Tier 1 ('CET1'), Additional Tier 1 ('AT1') and Total Capital. The minimum capital adequacy requirements as set out by the Central Bank are as follows:

- Minimum common equity tier 1 (CET 1) ratio of 7% of risk weighted assets (RWAs).
- Minimum tier 1 ratio of 8.5% of RWAs.
- Total capital adequacy ratio of 10.5% of RWAs.

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

For 2018, CCB is effective in transition arrangement and is required to be kept at 1.88% of the Capital base and from 2019 it will be required to be kept at 2.5% of the Capital base. CCyB is not in effect and is not required to be kept for 2018.

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

Following is the Bank's capital adequacy position under Basel III and Basel II as at 31 December 2018 and as at 31 December 2017 respectively:

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

25 Financial risk management (continued)

25.8 Capital risk management (continued)

	Under Basel III 2018 AED'000	Under Basel II 2017 AED'000
Tier 1 capital		
Head Office assigned capital	**760,000**	760,000
Statutory reserves	**65,289**	65,289
Retained earnings	**1,553,051**	2,086,584
Total tier 1 capital	**2,378,340**	2,911,873
Less: Regulatory Deductions	**(494,374)**	-
CET 1 Capital after deduction	**1,883,966**	2,911,873
Tier 2 capital		
Fair value reserve	**(3,976)**	(2,876)
General provisions/general loan loss reserves	**115,564**	117,884
Total tier 2 capital	**111,588**	115,008
Total regulatory capital (sum of tier 1 and 2 capital)	**1,995,554**	3,026,881
Risk weighted assets		
Credit risk	**9,245,111**	8,197,136
Market risk	**8,062**	1,670
Operational risk	**1,144,271**	1,231,946
Total risk weighted assets (RWA)	**10,397,444**	9,430,752
Total tier 1 capital expressed as % of RWA	**18.12%**	30.87%
Total tier 2 capital expressed as % of RWA	**1.07%**	1.22%
Capital adequacy ratio	**19.19%**	32.09%

26 Customers indebtedness and liabilities under acceptances

	2018 AED'000	2017 AED'000
Customers indebtedness and liabilities under acceptances	**380,227**	622,486

Customers' indebtedness under acceptances represent the accepted documented liability amount which is recoverable from the respective customers of the Bank at the reporting date. Liabilities under acceptances represent bills of exchange, letter of credits etc., where the Bank has accepted the liabilities under documentary credits at the reporting date. These assets and liabilities have been presented on a gross basis on the face of the statement of financial position as the Bank does not have a legal right of set-off.

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

27 Related party transactions

Parties are considered to be related if one party has the ability to control the other party or exercise significant influence over the other party in making financial or operational decisions. In the case of the Bank, related parties, as defined in International Accounting Standard 24: Related Parties (IAS 24), include key management personnel and other branches and fellow subsidiaries which are part of Bank of Baroda Group (which includes the Corporate Head Office of the Bank and the branches of the Group operating in different countires in the world), with whom banking transactions are carried out on mutually agreed terms. The management believes that the terms and transaction are comparable with those that could be obtained from third parties.

The significant transactions included in the financial statements with related parties are as follows:

	2018 AED'000	2017 AED'000
Interest income	**124,375**	126,354
Interest expenses	**168,147**	161,734
Head Office charges	**1,775**	1,093

The year-end balances in respect of related parties are disclosed as due from / to the Head Office and branches. The balances of amounts due from / to the Head Office and branches are as follows:

	2018 AED'000	2017 AED'000
Due from the Head Office and other branches		
Bank of Baroda - United Kingdom	**599,093**	318
Bank of Baroda - New York	**550,950**	550,950
Bank of Baroda - India (Mumbai)	**567,893**	1,869,599
Bank of Baroda - Brussels	**515,273**	439,715
Bank of Baroda - Oman	**550,950**	-
Bank of Baroda - Gift City	**91,825**	-
Bank of Baroda - Hong Kong	**183,650**	220,380
Bank of Baroda - Kenya	**-**	18,365
Bank of Baroda - Mauritius	**459,125**	-
Bank of Baroda - Singapore	**91,825**	-
Bank of Baroda - UAE Branches	**-**	34,427
	3,610,584	3,133,754

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

27 Related party transactions (continued)

	AED'000	AED'000
Due to Head Office and other branches		
Bank of Baroda - United Kingdom	**1,285,550**	1,285,550
Bank of Baroda - New York	**33,422**	43,093
Bank of Baroda - Oman	**12,411**	10,136
Bank of Baroda - India (Mumbai)	**372,448**	1,513
Bank of Baroda - Brussels	**146,920**	-
Bank of Baroda - UAE Branches	**4,836**	-
Bank of Baroda - Kenya	**179,977**	-
Bank of Baroda - Uganda	**29,384**	-
Bank of Baroda - Botswana	**11,019**	-
	2,075,967	1,340,292

27.1 The Bank's management has identified the Chief Executive Officer and Deputy Chief Executive Officer as key management personnel. The disclosure, as required under IAS 24 (revised) with respect to key management remuneration, would result in the disclosure of the compensation paid to both.

	2018 **AED'000**	2017 AED'000
Key management remuneration	**911**	1,002

28 Accounting classification and fair values

The table below shows a reconciliation between line items in the statement of financial position and categories of financial instruments:

Particulars	Carrying amount AED'000	Fair value through OCI AED'000	Amortised cost AED'000
As at 31 December 2018			
Financial assets			
Cash and balances with the UAE Central Bank	2,991,272	-	2,991,272
Due from banks	884,373	-	884,373
Due from the Head Office and other branches	3,610,584	-	3,610,584
Loans and advances to customers	13,209,688	-	13,209,688
Investment securities	142,880	142,880	-
Derivatives - net	4,367	4,367	-
Other assets (excluding prepayments)	58,980	-	58,980
	20,902,144	147,247	20,754,897
Financial liabilities			
Due to banks	2,399,371	-	2,399,371
Due to the Head Office and other branches	2,075,967	-	2,075,967
Deposits from customers	14,207,838	-	14,207,838
Other liabilities	316,429	-	316,429
	18,999,605	-	18,999,605

28 Accounting classification and fair values (continued)

Particulars	Carrying amount AED'000	Fair value through OCI AED'000	Amortised cost AED'000
As at 31 December 2017			
Financial assets			
Cash and balances with the UAE Central Bank	3,293,981	-	3,293,981
Due from banks	798,576	-	798,576
Due from the Head Office and other branches	3,133,754	-	3,133,754
Loans and advances to customers	11,876,994	-	11,876,994
Investment securities	143,980	143,980	-
Derivatives – net	2,215	2,215	-
Other assets (excluding prepayments)	69,021	-	69,021
	19,318,521	146,195	19,172,326
Financial liabilities			
Due to banks	1,082,509	-	1,082,509
Due to the Head Office and other branches	1,340,292	-	1,340,292
Deposits from customers	14,239,611	-	14,239,611
Other liabilities	279,141	-	279,141
	16,941,553	-	16,941,553

Management believes that the fair values of financial assets and liabilities measured at amortised cost are not significantly different from their carring values in these financial statements.

Fair value measurement - fair value hierarchy:

The fair values of financial assets and financial liabilities that are traded in active markets are based on quoted market prices or dealer price quotations. For all other financial instruments, the Bank determines fair values using other valuation techniques.

For financial instruments that trade infrequently and have little price transparency, fair value is less objective and requires varying degrees of judgment depending on liquidity, concentration, uncertainty of market factors, pricing assumptions and other risks affecting the specific instrument.

The Bank measures fair values using the following fair value hierarchy, which reflects the significance of the inputs used in making the measurements.

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

28 Accounting classification and fair values (continued)

Fair value measurement - fair value hierarchy (continued)

Level 1:
Inputs that are quoted market price (unadjusted) in active markets for an identical instruments.

Level 2:
Inputs other than quoted prices included within Level 1 that are observable either directly (i.e. as prices) or indirectly (i.e. derived from prices). This category includes instruments valued using: quoted market prices in active markets for similar instruments; quoted prices for identical or similar instruments in markets that are considered less than active; or other valuation techniques in which all significant inputs are directly or indirectly observable from market data.

Level 3:
Inputs that are unobservable. This category includes all instruments for which the valuation technique includes inputs that are not observable 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 for which significant unobservable adjustments or assumption are required to reflect differences between the instruments.

Valuation techniques include net present value and discounted cash flow models, comparison with similar instruments for which market observable prices exist. Assumptions and inputs used in valuation techniques include risk-free and benchmark profit rates, credit spreads and other premia used in estimating discount rates, bond and equity prices, foreign currency exchange rates, equity and equity index prices and expected price volatilities and correlations.

The objective of valuation techniques is to arrive at a fair value measurement that reflects the price that would be received to sell the asset or paid to transfer the liability in an orderly transaction between market participants at the measurement date.

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

28 Accounting classification and fair values (continued)

Fair value measurement - fair value hierarchy (continued)

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

	Level 1 AED 000	Level 2 AED 000	Level 3 AED 000	Total AED 000
2018				
Financial assets				
Investment securities	**142,880**	**-**	**-**	**142,880**
Derivatives	**-**	**4,727**	**-**	**4,727**
	142,880	**4,727**	**-**	**147,607**
Financial liabilities				
Derivatives	**-**	**360**	**-**	**360**
	-	**360**	**-**	**360**

	Level 1 AED 000	Level 2 AED 000	Level 3 AED 000	Total AED 000
2017				
Financial assets				
Investment securities	143,980	-	-	143,980
Derivatives	-	6,942	-	6,942
	143,980	6,942	-	150,922
Financial liabilities				
Derivatives	-	4,727	-	4,727
	-	4,727	-	4,727

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

28 Accounting classification and fair values (continued)

Fair value measurement - fair value hierarchy (continued)

The following table sets out the fair values of financial instruments not measured at fair value and analyses them by the level in the fair value hierarchy into which each fair value measurement is categorised.

At 31 December 2018	Level 1 AED'000	Level 2 AED'000	Level 3 AED'000	Fair value AED'000	Carrying amount AED'000
Assets					
Cash and balances with UAE Central Bank	-	2,991,272	-	-	2,991,272
Due from banks	-	16,598	867,775	-	884,373
Due from Head office and other branches	-	-	3,610,584	-	3,610,584
Loans and advances to customers	-	-	13,209,688	-	13,209,688
Customers' indebtedness under acceptances	-	-	380,227	-	380,227
Other assets	-	-	530,805	-	530,805
	-	3,007,870	18,599,079	-	21,606,949
Liabilities					
Deposits from customers	-	-	14,207,838	-	14,207,838
Due to banks	-	44,188	2,355,183	-	2,399,371
Due to Head office and other branches	-	-	2,075,967	-	2,075,967
Libilities under acceptances	-	-	380,227	-	380,227
Other liabilities	-	-	316,429	-	316,429
	-	44,188	19,335,644	-	19,379,832

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

28 Accounting classification and fair values (continued)

Fair value measurement - fair value hierarchy (continued)

	Level 1	Level 2	Level 3	Fair value	Carrying amount
	AED'000	AED'000	AED'000	AED'000	AED'000
At 31 December 2017					
Assets					
Cash and balances with UAE Central Bank	-	3,293,981	-	-	3,293,981
Due from banks	-	133,763	664,813	-	798,576
Due from head office and other branches	-	-	3,133,754	-	3,133,754
Loans and advances to customers	-	-	11,876,994	-	11,876,994
Customers' indebtedness under acceptance	-	-	622,486	-	622,486
Other assets	-	-	601,050	-	601,050
	-	3,427,744	16,899,097	-	20,326,841
Liabilities					
Due to banks	-	-	1,082,509	-	1,082,509
Due to Head Office and other brances	-	-	1,340,292	-	1,340,292
Deposits from customers	-	-	14,239,611	-	14,239,611
liabilities under acceptances	-	-	622,486	-	622,486
Other liabilities	-	-	279,141	-	279,141
	-	-	17,564,039	-	17,564,039

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

28 Accounting classification and fair values (continued)

Fair value measurement - fair value hierarchy (continued)

Movements in level 3 financial instruments measured at fair value

There was no movement between the levels of financial instruments during the year (2017: Nil)

Fair value of financial assets and liabilities not carried at fair value

The following describes the methodologies and assumptions used to determine fair values for those financial instruments which are not already recorded at fair value in the financial statements:

Asset for which fair value approximates carrying value

For financial assets and financial liabilities that have short term maturity (less than three months) it is assumed that the carrying amounts approximate to their fair value. This assumption is also applied to demand deposits and savings accounts without specific maturity.

Fixed rate financial instruments

The fair value of fixed rate financial assets and liabilities carried at amortised cost are estimated by comparing market interest rates when they were first recognised with current market rates for similar financial instruments. The estimated fair value of fixed interest bearing deposits is based on discounted cash flows using prevailing money-market interest rates for debts with similar credit and maturity. For other variable rate instruments, an adjustment is also made to reflect the change in required credit spread since the instrument was first recognised.

29 Comparative figures

Comparative figures are reclassified, where necessary, to conform with changes in the current period's presentation.

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