

CONSOLIDATED FINANCIAL STATEMENTS



FOR THE YEAR ENDED
31 DECEMBER 2021

Consolidated financial statements

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REPORT OF THE MANAGING DIRECTOR FOR THE YEAR ENDED 31 DECEMBER 2021

The Managing Director of Abu Dhabi National Leasing LLC (“the Company”) and its subsidiaries (together referred to as “the Group”) has pleasure in presenting his report and the audited consolidated financial statements for the year ended 31 December 2021.

Principal activities and review of business developments

The Group is principally set up for the purposes of carrying on and undertaking the business of asset leasing of all kinds including purchasing; owning, managing, selling, investing, renting and letting on hire all kinds of fixed and movable assets for commercial purposes.

Results for the year ended 31 December 2021

The results of the Group for the year ended 31 December 2021 are as follows:

	AED'000
Interest Income	12,586
Fees and commission income	398
Other income	342
Finance costs	(3,348)
Operating income	9,978
Depreciation and amortisation	(61)
Other costs	(16)
Operating expenses	(77)
Profit before net impairment	9,901
Net impairment charges	192
Profit for the year	9,709

Going concern basis

The management has reasonable expectation that the Company has adequate resources to continue its operational existence for the foreseeable future. For this reason, they continue to adopt the going concern basis in preparing the financial statements for the year ended 31 December 2021.

Transactions with related Parties

The Consolidated financial statements disclose related party transactions and balances in note 17. All transactions are carried out as part of our normal course of business and in compliance with applicable laws and regulations.



Fawaz Abusneineh
Acting Head of Global Corporate Finance



Bernar Kari
CFO, CCB, IB & International



KPMG Lower Gulf Limited
Level 19, Nation Tower 2
Corniche Road, P.O. Box 7613
Abu Dhabi, United Arab Emirates
Tel. +971 (2) 401 4800, www.kpmg.com/ae

Independent auditors' report

To the Shareholder of Abu Dhabi National Leasing LLC

Report on the Audit of the Consolidated Financial Statements

Opinion

We have audited the consolidated financial statements of Abu Dhabi National Leasing LLC ("the Company") and its subsidiaries ("the Group"), which comprise the consolidated statement of financial position as at 31 December 2021, the consolidated statements of profit or loss and 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 consolidated financial statements present fairly, in all material respects, the consolidated financial position of the Group as at 31 December 2021, and its consolidated financial performance and its consolidated 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 Consolidated Financial Statements* section of our report. We are independent of the Group in accordance with International Ethics Standards Board for Accountants International Code of Ethics for Professional Accountants (including International Independence Standards) (IESBA Code) together with the ethical requirements that are relevant to our audit of the consolidated 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 consolidated financial statements of the Group as at and for the year ended 31 December 2018 were unaudited.

Other Information

Management is responsible for the other information. The other information comprises the Managing Directors' report, but does not include the consolidated financial statements and our auditors' report thereon.

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

In connection with our audit of the consolidated financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the consolidated financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

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

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

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

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

Auditors' Responsibilities for the Audit of the Consolidated Financial Statements

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

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

- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Group's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by 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 Group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditors' report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditors' report. However, future events or conditions may cause the Group to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

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

Report on Other Legal and Regulatory Requirements

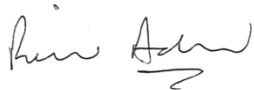
Further, as required by the UAE Federal Law No. (2) of 2015 (as amended), we report that for the year ended 31 December 2021:

- i) we have obtained all the information and explanations we considered necessary for the purposes of our audit;
- ii) the consolidated financial statements have been prepared and comply, in all material respects, with the applicable provisions of the UAE Federal Law No. (2) of 2015 (as amended); iii) the Group has maintained proper books of account;
- iv) the financial information included in the Directors' report is consistent with the books of account of the Group;
- v) as disclosed in note 1 to the consolidated financial statements, the Group has not purchased any shares during the year ended 31 December 2021;
- vi) note 17 to the consolidated financial statements discloses material related party transactions and the terms under which they were conducted; and

Report on Other Legal and Regulatory Requirements (continued)

- vii) based on the information that has been made available to us, nothing has come to our attention which causes us to believe that the Group has contravened during the financial year ended 31 December 2021 any of the applicable provisions of the UAE Federal Law No.(2) of 2015 (as amended) or its Articles of Association, which would materially affect its activities or its consolidated financial position as at 31 December 2021.

KPMG Lower Gulf Limited



Richard Ackland
Registration No.: 1015
Abu Dhabi, United Arab Emirates

Date

Consolidated statement of financial position
 As at 31 December

	Notes	2021 AED'000	2020 AED'000
Assets			
Due from banks	7	515,166	557,308
Loans and advances	8	481,567	628,731
Receivables and prepayments	9	7,669	6,941
Premises and equipment	11	407	468
Total assets		1,004,809	1,193,448
Liabilities			
Bank borrowings	12	413,267	608,152
Trade and other payables	13	18,915	22,378
Total liabilities		432,182	630,530
Equity			
Share capital	14	10,000	10,000
Statutory reserve	15	5,000	5,000
Retained earnings		557,627	547,918
Total equity		572,627	562,918
Total liabilities and equity		1,004,809	1,193,448

To the best of our knowledge, the financial statements present fairly in all material respects the financial condition, financial performance and cash flow of the Group as of and for, the periods presented there in.

These consolidated financial statements were approved and authorised for issue on _____ and signed by:



Fawaz Abusneineh
 Acting Head of Global Corporate Finance



Bernar Kari
 CFO, CCB, IB & International

The notes 1 to 18 are an integral part of these consolidated financial statements.

The Independent Auditors' report is set out on page 3 to 6.

Consolidated statement of profit or loss and other comprehensive income
For the year ended 31 December

	Notes	2021 AED'000	2020 AED'000
Interest Income		12,586	25,997
Fee and commission income		398	448
Other income		342	1
Finance costs	16	(3,348)	(11,553)
Net operating income		9,978	14,893
Depreciation and amortisation	11	(61)	(65)
Other costs		(16)	(91)
		(77)	(156)
Profit before net impairment charge		9,901	14,737
Net impairment (charges) / reversals	9	(192)	400
Profit for the year		9,709	15,137
Other comprehensive income		-	-
Total comprehensive income for the year		9,709	15,137

The notes 1 to 18 are an integral part of these consolidated financial statements.

The Independent Auditors' report is set out on page 3 to 6.

Consolidated statement of changes in equity
For the year ended 31 December

	Share Capital AED'000	Statutory reserve AED'000	Retained Earnings AED'000	Total AED'000
At 1 January 2020	10,000	5,000	532,781	547,781
Total comprehensive income for the year	-	-	15,137	15,137
At 31 December 2020	10,000	5,000	547,918	562,918
At 1 January 2021	10,000	5,000	547,918	562,918
Total comprehensive income for the year	-	-	9,709	9,709
At 31 December 2021	10,000	5,000	557,627	572,627

The notes 1 to 18 are an integral part of these consolidated financial statements.

The Independent Auditors' report is set out on page 3 to 6.

Consolidated statement of cash flows
For the year ended 31 December

	Notes	2021 AED'000	2020 AED'000
Cash flows from operating activities			
Profit for the year		9,709	15,137
<i>Adjustments for:</i>			
Depreciation of premises and equipment	11	61	65
Finance costs	16	3,348	11,553
Impairment charges / (reversals)	9	192	(400)
		13,310	26,355
Change in Loans and Advances		146,972	812,563
Change in receivables and prepayments		(728)	3,051
Change in trade and other payables		(3,463)	(5,189)
		156,091	836,780
Finance cost paid		(3,348)	(11,553)
Net cash from operating activities		152,743	825,227
Cash flows from financing activities			
Repayment of bank borrowings		(194,885)	(852,125)
Net cash used in financing activities		(194,885)	(852,125)
Decrease in cash and cash equivalents		(42,142)	(26,898)
Cash and cash equivalents at 1 January		557,308	584,206
Cash and cash equivalents at 31 December	7	515,166	557,308

The notes 1 to 18 are an integral part of these consolidated financial statements.

The Independent Auditors' report is set out on page 3 to 6.

Notes to the consolidated financial statements

1 Legal status and principal activities

Abu Dhabi National Leasing LLC (the “Company”) was established on 27 July 2003 as a limited liability company in accordance with UAE Federal Law No. 8 of 1984 (as amended). The Company is effectively a wholly owned subsidiary of First Abu Dhabi Bank PJSC (the “Parent”).

The Company and its subsidiaries (together referred to as the “Group”) set up primarily for the purpose of carry on and undertake the business of asset leasing and lease operations of all kinds including purchasing, owning, managing, selling, investing, renting and letting on hire all kinds of movable and immovable assets for commercial purposes. However, in compliance to Central Bank regulation the Group has stopped booking new leasing activity to meet the threshold set.

The registered office of the Group is P.O. Box 6316, Abu Dhabi, United Arab Emirates.

During the period ended 31 December 2021, the Group has not purchased in any shares.

These consolidated financial statements were authorised for issue on _____

2 Basis of preparation

(a) Statement of compliance

These consolidated financial statements have been prepared on an ongoing basis in accordance with the International Financial Reporting Standards (IFRSs) (which comprises accounting standards issued by international Accounting Standards Board (IASB) as well as Interpretations issued by the International Financial Reporting Interpretations Committee (IFRIC) and the requirements of applicable laws in the UAE.

On 1 April 2015, UAE Federal Law No 2 for Commercial Companies (“UAE Companies Law of 2015”) was issued with effective date 1 July 2015. The company is in compliance with applicable sections of the UAE Companies Law of 2015 (as amended) as at the date of these financial statements.

(b) Basis of measurement

The consolidated financial statements are prepared on the historical cost.

(c) Functional and presentation currency

These consolidated financial statements are presented in United Arab Emirates Dirhams (“AED”), which is the Company’s functional currency. Except as indicated, information presented in AED has been rounded to the nearest thousand.

Notes to the consolidated financial statements *(continued)*

2 Basis of preparation *(continued)*

(d) Use of estimates and judgements

The preparation of consolidated financial statements 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 assumption are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimates is revised and in any future periods affected.

Information about significant areas of estimation uncertainty and critical judgements in applying accounting policies that have the most significant effect on the amount recognised in the consolidated financial statements are described in note 5.

3 Significant accounting policies

(a) New and Amended standards and interpretations adopted

The following amendments to existing standards and framework have been applied by the Group in preparation of these consolidated financial statements. The adoption of the below did not result in changes to previously reported net profit or equity of the Group.

Description	Effective from
Interest Rate Benchmark Reform - Phase 2 (Amendments to IFRS 9, IAS 39, IFRS 7, IFRS 4 and IFRS 16)	1 January 2021

Interest Rate Benchmark Reform

On 27 August 2020 the International Accounting Standards Board (IASB or the Board) published 'Interest Rate Benchmark reform – Phase 2, Amendments to IFRS 9, IAS 39, IFRS 7, IFRS 4 and IFRS 16 (IBOR reform Phase 2). IBOR reform Phase 2 includes a number of reliefs and additional disclosures. The reliefs apply upon the transition of a financial instrument from an Interbank offered rate ("IBOR") to an alternative risk-free benchmark reference rate ("RFR").

Notes to the consolidated financial statements (continued)

3 Significant accounting policies (continued)

(a) New and Amended standards and interpretations adopted (continued)

Interest Rate Benchmark Reform (continued)

The first phase of amendments i.e. 'Interest Rate Benchmark Reform - Amendments to IFRS 9, IAS 39 and IFRS 7' (IBOR reform Phase 1), provided temporary reliefs to enable hedge accounting to continue during the period of uncertainty before the replacement of an IBOR with RFR. This has no impact on the Group as it does not have hedging instruments.

The effective date of the IBOR reform Phase 2 amendments is for periods beginning on or after 1 January 2021. The requirements must be applied retrospectively. The Group has adopted the IBOR reform Phase 2 amendments in its financial statements for the year ended 31 December 2021 and has provided the required disclosures in the notes to the financial statements (refer to Notes 3, 4(d) and 5(d)(e)). The Phase 2 amendments have been applied retrospectively. However, in accordance with exceptions provided in the Phase 2 amendments, the Group has elected not to restate the prior period to reflect the application of these amendments, including not providing additional disclosures for 2020. There is no impact on opening equity balances as a result of retrospective application.

The Phase 2 amendments provide practical relief from certain requirements in the standards. These reliefs relate to modifications of financial instruments, lease contracts or hedging relationships when a benchmark interest rate in a contract is replaced with a new alternative benchmark rate. The amendments also provide an exception to use a revised discount rate that reflects the change in interest rate when remeasuring a lease liability because of a lease modification that is required by interest rate benchmark reform.

As per the Phase 2 amendments, changes to the basis for determining contractual cash flows as a result of interest rate benchmark reform are required as a practical expedient to be treated as changes to a floating interest rate, provided that, for the financial instrument, the transition from the IBOR benchmark rate to RFR takes place on an economically equivalent basis. This may include the addition of a fixed spread to compensate for a basis difference between the existing IBOR benchmark and alternative RFR, changes to reset period, reset dates or number of days between coupon payment dates that are necessary to effect reform of an IBOR benchmark and the addition of any fallback provision to the contractual terms of a financial instrument that allow any of the above changes to be made. Any other change to contractual terms would be assessed under the Group's accounting policies for financial assets modifications, including an assessment of whether derecognition of the original instrument is required.

Notes to the consolidated financial statements (continued)

3 Significant accounting policies (continued)

(b) Basis of consolidation

IFRS 10 governs the basis for consolidation where it establishes a single control model that applies to all entities including special purpose entities or structured entities. The definition of control is such that an investor controls an investee when it is exposed to, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee. To meet the definition of control in IFRS 10, all three criteria must be met, including:

- (a) the investor has power over an investee;
- (b) the investor has exposure to, or rights, to variable returns from its involvement with the investee; and
- (c) the investor has the ability to use its power over the investee to affect the amount of the investor's returns.

(i) Subsidiaries

Subsidiaries are investees that are controlled by the Group. The Group controls the investee if it meets the control criteria discussed in note 3(a). The Group reassesses whether it has control if, there are changes to one or more of the elements of control. This includes circumstances in which protective rights held become substantive and lead to the Group having power over an investee. The financial statements of subsidiaries are included in these consolidated financial statements from the date that control commences until the date that control ceases.

Details of the Group's subsidiaries are as follows:

Company name	Country of Incorporation	Holding %
Asset Wonder Limited	Hong Kong	100%
FAS 1	Cayman Island	100%
FAS 2	Cayman Island	100%

These subsidiaries are wholly owned by the Group. These entities are established for the specific purposes of registration of title deeds for certain loans by the Group. The entities have no other operations of their own and accordingly no separate financial statements have been prepared for the subsidiaries.

Notes to the consolidated financial statements (continued)

3 Significant accounting policies (continued)

(c) Financial assets and liabilities

(i) Recognition and initial measurement

The Group initially recognised loans and advances, deposits, debt securities issued and subordinated liabilities on the date on which they are originated. All other financial instruments (excluding regular way purchases and sales of financial assets) are recognised on the trade date, which is the date on which the Group becomes a party to the contractual provisions of the instrument.

All regular way purchases and sales of financial assets are recognised on the settlement date, i.e. the date the asset is delivered to or received from the counterparty. Regular way purchases or sales of financial assets are those that require delivery of assets within the time frame generally established by regulation or convention in the market place.

(ii) Classification

Financial assets

On initial recognition, a financial asset is classified as measured at: amortised cost. A financial asset is measured at amortised cost if it meets both of the following conditions:

- 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 Payment of Principal and Interest ("SPPI").

A debt instrument 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 SPPI.

On initial recognition of an equity investment that is not held for trading, the Group 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 Group may irrevocably designate a financial asset that otherwise meets the requirements to be measured at amortised cost or at FVOCI as FVTPL if doing so eliminates or significantly reduces an accounting mismatch that would otherwise arise.

Notes to the consolidated financial statements (continued)

3 Significant accounting policies (continued)

(c) Financial assets and liabilities (continued)

(ii) Classification (continued)

Business model assessment

The Group 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, maintaining a particular interest rate profile, matching the duration of the financial assets to the duration of the liabilities that are funding those assets or realising cash flows through the sale of the assets;
- how the performance of the portfolio is evaluated and reported to the Group's management;
- the risks that affect the performance of the business model (and the financial assets held within that business model) and its strategy for how those risks are managed;
- 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 Group's stated objective for managing the financial assets is achieved and how much cash flows are realised.

Financial assets that are either 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 (SPPI)

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 SPPI, the Group 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 Group considers:

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

Notes to the consolidated financial statements (continued)

3 Significant accounting policies (continued)

(c) Financial assets and liabilities (continued)

The Group holds a portfolio of long-term fixed-rate loans for which the Group has the option to propose to revise the interest rate at periodic reset dates. These reset rights are limited to the market rate at the time of revision. The borrowers have an option to either accept the revised rate or redeem the loan at par without penalty. The Group has determined that the contractual cash flows of these loans are SPPI because the option varies the interest rate in a way that is consideration for the time value of money, credit risk, other basic lending risks and costs associated with the principal amount outstanding.

The Group classifies its financial liabilities, other than financial guarantees and loan commitments, as measured at amortised cost.

(iii) Derecognition

Financial assets

The Group derecognises a financial asset when the contractual rights to the cash flows from the financial asset expire (see also 3(iv)), or it transfers the rights to receive the contractual cash flows in a transaction in which substantially all of the risks and rewards of ownership of the financial asset are transferred or in which the Group neither transfers nor retains substantially all of the risks and rewards of ownership and it does not retain control of the financial asset.

On derecognition of a financial asset, the difference between the carrying amount of the asset (or the carrying amount allocated to the portion of the asset derecognised) and the sum of (i) the consideration received (including any new asset obtained less any new liability assumed) and (ii) any cumulative gain or loss that had been recognised in OCI is recognised in profit or loss.

Any cumulative gain/loss recognised in OCI in respect of equity investment securities designated as at FVOCI is not recognised in profit or loss on derecognition of such securities. Any interest in transferred financial assets that qualify for derecognition that is created or retained by the Group is recognised as a separate asset or liability.

The Group enters into transactions whereby it transfers assets recognised on its consolidated statement of financial position, but retains either all or substantially all of the risks and rewards of the transferred assets or a portion of them. In such cases, the transferred assets are not derecognised. Examples of such transactions are securities lending and sale-and-repurchase transactions.

When assets are sold to a third party with a concurrent total rate of return swap on the transferred assets, the transaction is accounted for as a secured financing transaction similar to sale-and-repurchase transactions, because the Group retains all or substantially all of the risks and rewards of ownership of such assets.

Notes to the consolidated financial statements *(continued)*

3 Significant accounting policies *(continued)*

(c) Financial assets and liabilities *(continued)*

(iii) Derecognition *(continued)*

In transactions in which the Group neither retains nor transfers substantially all of the risks and rewards of ownership of a financial asset and it retains control over the asset, the Group continues to recognise the asset to the extent of its continuing involvement, determined by the extent to which it is exposed to changes in the value of the transferred asset.

In certain transactions, the Group retains the obligation to service the transferred financial asset for a fee. The transferred asset is derecognised if it meets the derecognition criteria. An asset or liability is recognised for the servicing contract if the servicing fee is more than adequate (asset) or is less than adequate (liability) for performing the servicing.

Financial liabilities

The Group derecognises a financial liability when its contractual obligations are discharged or cancelled, or expire.

(iv) Modifications of financial assets and financial liabilities

Financial assets

If the terms of a financial asset are modified, then the Group evaluates whether the cash flows of the modified asset are substantially different.

If the cash flows 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 a new financial asset is recognised at fair value plus any eligible transaction costs. Any fees received as part of the modification are accounted for as follows:

- fees that are considered in determining the fair value of the new asset and fees that represent reimbursement of eligible transaction costs are included in the initial measurement of the asset; and
- other fees are included in profit or loss as part of the gain or loss on derecognition.

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. If the Group 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 Group 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 profit or loss.

Notes to the consolidated financial statements *(continued)*

- 3 **Significant accounting policies** *(continued)*
- (c) **Financial assets and liabilities** *(continued)*
- (iv) **Modifications of financial assets and financial liabilities** *(continued)*

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 receivable 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.

In the context of IBOR reform, the Group's assessment of whether a change to a financial asset is substantial, is made after applying the practical expedient introduced by IBOR reform Phase 2. This requires the transition from an IBOR to an RFR to be treated as a change to a floating interest rate as described in Note 3(d). Under the Phase 2 Interest Rate Benchmark Reform amendments to IFRS 9, changes to the basis for determining contractual cash flows as a direct result of interest rate benchmark reform are treated as changes to a floating interest rate to that instrument, provided that the transition from the IBOR benchmark rate to the alternative RFR takes place on an economically equivalent basis.

Where the instrument is measured at amortized cost or FVOCI, this results in a change in the instrument's effective interest rate, with no change in the amortized cost value of the instrument. If the change to the instrument does not meet these criteria, the Group applies judgement to assess whether the changes are substantial and if they are, the financial instrument is derecognized and a new financial instrument is recognized. If the changes are not substantial, the Group continues to carry the financial instrument at its current carrying value with the difference adjusted in revised effective interest rate on prospective basis, adjusts the gross carrying amount of the financial instrument by the present value of the changes not covered by the practical expedient, discounted using the revised effective interest rate.

Financial liabilities

The Group derecognises a financial liability when its terms are modified and the cash flows of the modified liability are substantially different. 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 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 profit or loss.

Notes to the consolidated financial statements *(continued)*

3 Significant accounting policies *(continued)*

(c) Financial assets and liabilities *(continued)*

(iv) Modifications of financial assets and financial liabilities *(continued)*

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.

In the context of IBOR reform, the Group's assessment of whether a change to a financial liability is substantial, is made after applying the practical expedient introduced by IBOR reform Phase 2. This requires the transition from an IBOR to an RFR to be treated as a change to a floating interest rate as described in Note 3(d). Under the Phase 2 Interest Rate Benchmark Reform amendments to IFRS 9, changes to the basis for determining contractual cash flows as a direct result of interest rate benchmark reform are treated as changes to a floating interest rate to that instrument, provided that the transition from the IBOR benchmark rate to the alternative RFR takes place on an economically equivalent basis.

Where the instrument is measured at amortized cost, this results in a change in the instrument's effective interest rate, with no change in the amortized cost value of the instrument. If the change to the instrument does not meet these criteria, the Group applies judgement to assess whether the changes are substantial and if they are, the financial instrument is derecognized and a new financial instrument is recognized. If the changes are not substantial, the Group adjusts the gross carrying amount of the financial instrument by the present value of the changes not covered by the practical expedient, discounted using the revised effective interest rate.

(v) Offsetting

Financial assets and liabilities are offset and the net amount presented in the consolidated statement of financial position when, and only when, the Group has a legal right to set off the amounts and intend either to settle on a net basis, or to realise the asset and settle the liability simultaneously.

Income and expenses are presented on a net basis only when permitted under IFRS, or for gains and losses arising from a group of similar transactions such as in the Group's trading activity.

(vi) Fair value measurement

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date in the principal, or in its absence, the most advantageous market to which the Group has access at that date. The fair value of a liability reflects its non-performance risk. When available, the Group measures the fair value of an instrument using the quoted price in an active market for that instrument. A market is regarded as active if transactions for the asset or liability take place with sufficient frequency and volume to provide pricing information on an on-going basis.

Notes to the consolidated financial statements (continued)

3 Significant accounting policies (continued)

(c) Financial assets and liabilities (continued)

(vi) Fair value measurement (continued)

If there is no quoted price in an active market, then the Group uses the valuation techniques that maximize the use of relevant observable inputs and minimize the use of unobservable inputs. The chosen valuation technique incorporates all the factors that market participants would take into account in pricing a transaction. The best evidence of the fair value of a financial instrument at initial recognition is normally the transaction price – i.e. the fair value of the consideration given or received. If the Group determines that the fair value at initial recognition differs from the transaction price and the fair value is evidenced neither by a quoted price in an active market for an identical

asset or liability nor based on a valuation technique that uses only data from observable markets, the financial instrument is initially measured at fair value, adjusted to defer the difference between the fair value at initial recognition and the transaction price. Subsequently, that difference is recognised in the consolidated statement of profit or loss on an appropriate basis over the life of the instrument but no later than when the valuation is supported wholly by observable market data or the transaction is closed out.

If an asset or a liability measured at fair value has a bid price and an ask price, the Group measures assets and long positions at a bid price and liabilities and short positions at an ask price.

Portfolios of financial assets and financial liabilities that are exposed to market risk and credit risk that are managed by the Group on the basis of the net exposure to either market or credit risk, are measured on the basis of a price that would be received to sell a net long position or paid to transfer a net short position for a particular risk exposure. These portfolio level adjustments are allocated to the individual assets and liabilities on the basis of the relative risk adjustment of each of the individual instruments in the portfolio.

For other investments, a reasonable estimate of the fair value is determined by reference to the price of recent market transactions involving similar investments, are based on the expected discounted cash flows.

The fair value of a demand deposit is not less than the amount payable on demand, discounted from the first date on which the amount could be required to be paid.

The Group recognizes transfers between levels of the fair value hierarchy as at the end of the reporting period during which the change has occurred.

(vii) Impairment

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

- due from banks and financial institutions;
- financial assets that are debt instruments;
- loans and advances;

Notes to the consolidated financial statements (continued)

3 Significant accounting policies (continued)

(c) Financial assets and liabilities (continued)

(vii) Impairment (continued)

No impairment loss is recognised on equity investments.

The Group measures loss allowances at an amount equal to lifetime ECL, except for the following, for which they are measured as 12-month ECL:

- debt investment securities that are determined to have low credit risk at the reporting date; and
- other financial instruments on which credit risk has not increased significantly since their initial recognition (see Note 5).

Measurement of ECL

Credit loss allowances are measured using a three-stage approach based on the extent of credit deterioration since origination:

- Stage 1 – Where there has not been a significant increase in credit risk (SICR) since initial recognition of a financial instrument, an amount equal to 12 months expected credit loss is recorded. The expected credit loss is computed using a probability of default occurring over the next 12 months. For those instruments with a remaining maturity of less than 12 months, a probability of default corresponding to remaining term to maturity is used.
- Stage 2 – When a financial instrument experiences a SICR subsequent to origination but is not considered to be impaired, it is included in Stage 2. This requires the computation of expected credit loss based on the probability of default over the remaining estimated life of the financial instrument.
- Stage 3 – Financial instruments that are considered to be impaired are included in this stage. Similar to Stage 2, the allowance for credit losses captures the lifetime expected credit losses.

The key inputs into the measurement of ECL are:

- Probability of default (PD);
- Loss given default (LGD);
- Exposure at default (EAD)

These parameters are generally derived from statistical models and other historical data. They are adjusted to reflect forward-looking information. Additionally, the Group has elaborate review process to adjust ECL for factors not available in the model.

Notes to the consolidated financial statements (continued)

3 Significant accounting policies (continued)

(c) Financial assets and liabilities (continued)

(vii) Impairment (continued)

Measurement of ECL (continued)

Details of these statistical parameters/inputs are as follows:

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

ECL are a probability-weighted estimate of credit losses. They are measured as follows:

- 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 Group 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;
- undrawn loan commitments: as the present value of the difference between the contractual cash flows that are due to the Group if the commitment is drawn down and the cash flows that the Group expects to receive; and
- financial guarantee contracts: the expected payments to reimburse the holder less any amounts that the Group expects to recover.

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 ECL are measured as follows.

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

Notes to the consolidated financial statements (continued)

3 Significant accounting policies (continued)

(c) Financial assets and liabilities (continued)

(vii) Impairment (continued)

Credit-impaired financial assets

At each reporting date, the Group assesses whether financial assets carried at amortised cost and debt financial assets carried at FVOCI, and finance lease receivables are credit-impaired (referred to as 'Stage 3 financial assets'). 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. 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 restructuring of a loan or advance by the Group on terms that the Group would not consider otherwise;
- it is becoming probable that the borrower will enter bankruptcy or other financial reorganisation; or
- the disappearance of an active market for a security because of financial difficulties.

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:

- financial assets measured at amortised cost: as a deduction from the gross carrying amount of the assets;
- loan commitments and financial guarantee contracts: generally, as a provision; and
- debt instruments measured at FVOCI: no loss allowance is recognised in the consolidated statement of financial position because the carrying amount of these assets is their fair value. However, the loss allowance is disclosed and is recognised in the fair value reserve.

Write-off

Loans and debt securities are written off (either partially or in full) when there is no reasonable expectation of recovering a financial asset in its entirety or a portion thereof. This is generally the case when the Group determines that the borrower does not have assets or sources of income that could generate sufficient cash flows to repay the amounts subject to the write-off. This assessment is carried out at the individual asset level.

Recoveries of amounts previously written off are included in 'net impairment charge' in the statement of profit or loss. Financial assets that are written off could still be subject to enforcement activities in order to comply with the Group's procedures for recovery of amounts due.

Notes to the consolidated financial statements (continued)

3 Significant accounting policies (continued)

(c) Financial assets and liabilities (continued)

(vii) Impairment (continued)

Central Bank of UAE (“CBUAE”) provision requirements

As per the CBUAE notice no. CBUAE/BSD/2020/458 dated 30 April 2020, clause 6.4, if the specific provision and general/collective provision cumulatively is higher than the impairment allowance computed under IFRS 9, the differential should be transferred to an “Impairment Reserve” as an appropriation from the Retained earnings. This Impairment Reserve should be split to that which relates to difference in specific provision and general/collective provision. The Impairment reserve will not be available for payment of dividend.

(d) Revenue Recognition

(i) Interest income and expense

Effective interest rate

Interest income and expense are recognised 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 purchased or originated credit-impaired assets, the Group estimates future cash flows considering all contractual terms of the financial instrument, but not ECL.

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.

The Group has adopted IBOR reform Phase 2 for its 2021 year end, which allows as a practical expedient for changes to the basis for determining contractual cash flows to be treated as changes to a floating rate of interest, provided certain conditions are met.

The conditions include that the change is necessary as a direct consequence of IBOR reform and that the transition takes place on an economically equivalent basis.

Amortised cost and gross carrying amount

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

Notes to the consolidated financial statements (continued)

3 Significant accounting policies (continued)

(d) Revenue Recognition (continued)

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

Calculation of interest income and expense

The effective interest rate of a financial asset or financial liability is calculated on initial recognition of a financial asset or a financial liability. 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. The effective interest rate is revised as a result of periodic re-estimation of cash flows of floating rate instruments to reflect movements in market rates of interest. The effective interest rate is also revised for fair value hedge adjustments at the date amortisation of the hedge adjustment begins.

For information on when financial assets are credit-impaired, see Note 3(c)(vii).

Presentation

Interest income calculated using the effective interest method presented in the statement of profit or loss and OCI includes:

- interest on financial assets and financial liabilities measured at amortised cost.

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

- financial liabilities measured at amortised cost.

Interest income and expense on financial assets and financial liabilities at FVTPL are presented as in interest income or interest expense from financial instruments at FVTPL.

(ii) Loan arrangement fees, other fees and commission income

Income is recognised in the profit or loss as and when the related services are rendered or significant act has been completed. In some circumstances these incomes form integral part of finance lease receivables through capitalisation.

(iii) Fees and commission

Fees and commission income that are integral to the effective interest rate on a financial asset are included in the measurement of the effective interest rate.

(iv) Interest income on advances against loans

Interest income on advances against loans is recognised in the profit or loss using, the effective interest method.

Notes to the consolidated financial statements *(continued)*

3 Significant accounting policies *(continued)*

(e) Finance cost

Finance cost comprises interest expense on borrowings which is recognised in the profit or loss using the effective interest method.

(f) Loans and Advances

'Loans and advances' captions in the statement of financial position include:

- loans and advances measured at amortised cost; they are initially measured at fair value plus incremental direct transaction costs, and subsequently at their amortised cost using the effective interest method;

(g) Premises and equipment

(i) Recognition and measurement

All items of premises and equipment are measured at cost less accumulated depreciation and impairment losses, if any. Cost includes expenditures that are directly attributable to the acquisition of the asset. Purchased software that is integral to the functionality of the related equipment is capitalised as part of that equipment.

Gains and losses on disposal of an item of premises and equipment are determined by comparing the proceeds from disposal with the carrying amount of premises and equipment, and are recognised net within "other income" in profit or loss.

(ii) Subsequent costs

Subsequent expenditures are only capitalised when it is probable that the future economic benefits of such expenditures will flow to the Group. On-going expenses are charged to the statement of profit or loss as incurred.

Notes to the consolidated financial statements (continued)

4 Significant accounting policies (continued)

(g) Premises and equipment (continued)

(iii) Depreciation

Depreciation is recognised in the statement of profit or loss on a straight-line basis over the estimated useful lives of all premises and equipment.

The estimated useful lives of assets for the current and comparative period are as follows:

Office furniture and equipment	1 to 5 years
Leasehold improvements	4 years
Safes	10 to 20 years
Computer equipment	3 to 7 years
Vehicles	3 years

Depreciation methods, useful lives and residual values are reassessed at each reporting date.

(iv) Impairment

The carrying amounts are reviewed at each reporting date for indication of impairment. If any such indication exists then the asset's recoverable amount is estimated. The recoverable amount of an asset 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 discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. An impairment loss is recognised in the statement of profit or loss if the carrying amount of an asset exceeds its recoverable amount.

(h) Cash and cash equivalents

Cash and cash equivalent comprise bank balances and term deposits, with original maturity of three months or less, which are subject to insignificant credit risk. Cash and cash equivalents are carried at amortised cost in the consolidated statement of financial position.

(i) Bank borrowings

Borrowings are initially recognised at fair value, net of transaction costs incurred. Borrowings are subsequently carried at amortised cost; any difference between the proceeds (net of transaction costs) and the redemption value is recognised in the profit or loss over the period of the borrowings using the effective interest rate method.

(j) Provisions

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

Notes to the consolidated financial statements (continued)

3 Significant accounting policies (continued)

(k) Foreign currency transactions

Transactions in foreign currencies are translated into the respective functional currencies of the Group entities at spot exchange rates at the dates of the transactions.

Monetary assets and liabilities denominated in foreign currencies at the reporting date are retranslated to the functional currency at the spot exchange rates at the reporting date. Non-monetary assets and liabilities that are measured in terms of historical cost in a foreign currency are translated using the exchange rate at the date of the transaction. The foreign currency gain or loss on monetary items is the difference between amortised cost in the functional currency at the beginning of the period, adjusted for effective interest and payments during the period, and the amortised cost in foreign currency translated at the exchange rate at the end of the period. Foreign currency differences arising on retranslation are recognised in the statement of profit or loss.

(l) Standards issued but not yet effective

A number of new standards and amendments to standards are effective for annual periods beginning after 1 January 2021 and earlier application is permitted; however, the Group has not early adopted them in preparing these consolidated financial statements.

The following amended standards are not expected to have a significant impact on the Group's consolidated financial statements.

- Onerous Contracts – Cost of Fulfilling a Contract (Amendments to IAS 37).
- Annual Improvements to IFRS Standards 2018–2020.
- Property, Plant and Equipment: Proceeds before Intended Use (Amendments to IAS 16)
- Reference to the Conceptual Framework (Amendments to IFRS 3)
- Classification of Liabilities as Current or Non-current (Amendments to IAS 1).
- IFRS 17 Insurance Contracts and amendments to IFRS 17 Insurance Contracts.
- Disclosure of Accounting Policies (Amendments to IAS 1 and IFRS Practice Statement 2).
- Definition of Accounting Estimates (Amendments to IAS 8).
- Financial Instruments: Fees in the '10 per cent' test for derecognition of financial liabilities (Annual improvements to IFRS 9)

Notes to the consolidated financial statements (continued)

4 Financial risk management

(a) Introduction and overview

The Group is exposed to a variety of risks inherent in carrying out its business activities. Principal risks include credit, market (traded and non-traded interest rate and foreign currency related risks), liquidity and funding, capital, operational, and business continuity. The Parent has institutionalized a risk management framework which seeks to effectively manage these risks.

The Group follows Parent's risk management policies and procedures for measurement and management of all risks. This note presents information about the Group's exposure to each of the above risks, along with an overview of relevant frameworks, policies and processes for measuring and managing these risks.

Risk management framework

The Board of Directors of the Parent (the "Board") has overall responsibility for the establishment and oversight of the Group's risk management framework and they are assisted by two board committees (Risk Management Committee and Audit Committee), and two management committees (Group Risk Committee ("GRC") and Parent Assets and Liabilities Committee ("G-ALCO")).

- The Risk Management Committee (RMC), comprising of members from the Board, is responsible for recommending and setting the Parent's and the Group's risk strategy and policy guidelines, and subsequently monitoring adherence. RMC takes credit decisions above management's discretionary powers, defines risk limits within which the Group's management operates and also monitors the overall risks for the Group.
- The Audit Committee, a board level committee, exercises oversight to monitor compliance with regulatory guidelines and the Parent's internal policies and procedures.

The management committees are responsible for implementing the risk management framework. The major functions of the two management committees are given below:

- The GRC is accountable to the Board RMC in respect of all Risk Management facets within the Group. The primary function of the committee is to ensure that the Bank's policies and procedures incorporate sound risk management practices and that the same are implemented. It also reviews, and recommends to the Board, the risk appetite, risk limits, risk aspects of business strategy and planning, and approves risk policies & analytical models to ensure effective risk management.
- The G-ALCO is the driving force and key decision maker behind the structure and quality of the balance sheet. The G-ALCO is directly accountable to the Board RMC for ensuring that the risks within the Group Asset and Liability position are prudently managed by way of strong Parent's policy and procedures and an appropriate risk framework. The G-ALCO must be constantly aware of and actively manage these risks and their potential impact on the Parent's business and strategic objectives.

Notes to the consolidated financial statements (continued)

4 Financial risk management (continued)

The Parent manages risk using three lines of defence comprising of business units, control units and Internal Audit. Business units, as the first line of defence, identify and manage risk in their day-to-day activities by ensuring that activities are within the Group's risk appetite and are in compliance with all relevant internal policies and processes. Risk Group (comprising head office risk and risk functions embedded in business divisions) and Legal & Compliance division of the Parent, as the second line of defence, establishes risk controls comprising of policies and processes while also providing oversight and independent challenge to the first line. The Parent's Group Chief Risk Officer ("GCRO") has a direct reporting line to Board RMC to ensure the independence of Risk Group from business. Internal audit, as the third line of defence, provides assurance to management and the Board of the effectiveness of risk management practices employed by the first two lines of defence. The Parent's Group Chief Audit Officer has a direct reporting line to the Board Audit Committee.

(b) Credit risk

Credit risk is the risk of a financial loss to the Group if a loan or counterparty to a financial asset fails to meet its contractual obligations, and arises principally from the Group's leasing activities.

Management of credit risk

Credit risk identification and assessment at Group is carried out through a comprehensive mechanism comprising three levels of defense. The first level of defense lies with the business units and is responsible for maintaining a sound credit quality of Assets in line with the approved business strategy and credit risk appetite. The second level of defense is with the Group Credit Unit that assesses the risk on a customer & facility level and ensures proper documentation of customer, facility and security documents along with Group Risk management unit that assesses credit risk on a portfolio basis and maintains credit risk policies and credit risk rating models up to date. Internal Audit acts as a third level of defense with regular reviews of credit analysis and the risk functions to check the compliance with policies and procedures of the Group. The unit also reviews the policy documents on a regular basis.

As a part of credit risk monitoring and control framework, regular risk monitoring at both individual and portfolio levels is carried out along several parameters which include credit quality, provisioning levels, exposure limits across several dimensions, financial and operating performance, account conduct, end use of funds, adequacy of credit risk mitigants, adherence to financial and non-financial covenants, recovery performance, rating system performance among others. The Group has set up a framework for credit risk mitigation as a means towards reducing credit risk in an exposure, at facility level, by a safety net of tangible and realizable securities including approved third-party guarantees/ insurance. The types of Credit Risk Mitigation (CRM) include netting agreements, collaterals, guarantees, credit derivatives, Stand by Letter of Credit (SBLC) and Comfort Letters. The Group ensures that all documentation used in collateralized transactions and for documenting on and off-balance sheet netting, guarantees, credit derivatives and collateral is binding on all parties and is legally enforceable in all relevant jurisdictions. The Group also ensures that all the documents are reviewed by appropriate authority and have appropriate legal opinions to verify and ensure its enforceability. In certain cases, the Group may also close out transactions or assign them to other counterparties to mitigate credit risk.

Notes to the consolidated financial statements (continued)

4 Financial risk management (continued)

Credit quality analysis

The following table sets out information about the credit quality of financial assets measured at amortised cost. 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 2021	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
Due from banks and financial institutions	515,166	-	-	-	-	-	515,166	-
Loans and advances ¹	468,741	638	3,679	920	89,752	34,506	562,172	36,064
Other assets ²	7,774	105	-	-	-	-	7,774	105
Unfunded exposure	20	-	-	-	-	-	20	-
	<u>991,701</u>	<u>743</u>	<u>3,679</u>	<u>920</u>	<u>89,752</u>	<u>34,506</u>	<u>1,085,132</u>	<u>36,169</u>

As of 31 December 2020	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
Due from banks and financial institutions	557,308	-	-	-	-	-	557,308	-
Loans and advances ¹	615,812	1,365	-	-	87,816	34,506	703,628	35,871
Other assets ²	7,047	106	-	-	-	-	7,047	106
Unfunded exposure	-	-	-	-	-	-	-	-
	<u>1,180,167</u>	<u>1,471</u>	<u>-</u>	<u>-</u>	<u>87,816</u>	<u>34,506</u>	<u>1,267,983</u>	<u>35,977</u>

¹The exposure represents gross loans and advances.

²On certain assets included as part of other assets, ECL is computed based on simplified approach and reported as part of stage 1.

Notes to the consolidated financial statements (continued)

4 Financial risk management (continued)

(b) Credit risk (continued)

Amounts arising from ECL

Inputs, assumptions and techniques used for estimating impairment

See accounting policy 3(c)(vii).

Significant increase in credit risk

When determining whether the risk of default on a financial instrument has increased significantly since initial recognition, the Group considers reasonable and supportable information that is relevant and available without undue cost or effort. This includes both quantitative and qualitative information and analysis, based on the Group's historical experience and expert credit assessment and including forward-looking information.

The objective of the assessment is to identify whether a significant increase in credit risk has occurred for an exposure by comparing:

- the remaining lifetime probability of default (PD) as at the reporting date; with
- the remaining lifetime PD for this point in time that was estimated at the time of initial recognition of the exposure.

In addition to the quantitative test based on movement of PD, the Group also applies experienced credit judgement to incorporate the estimated impact of factors not captured in the modelled ECL results.

Credit risk grades

The Group allocates each Corporate exposure to a credit risk grade based on a variety of data that is determined to be predictive of the risk of default and applying experienced credit judgement. Credit risk grades are defined using qualitative and quantitative factors that are indicative of risk of default. These factors vary depending on the nature of the exposure and the type of borrower.

Credit risk grades are defined and calibrated such that the risk of default occurring increases exponentially as the credit risk deteriorates so, for example, the difference in risk of default between credit risk grades 1 and 2 is smaller than the difference between credit risk grades 2 and 3.

Each exposure is allocated to a credit risk grade on initial recognition based on available information about the borrower. Exposures are subject to ongoing monitoring, which may result in an exposure being moved to a different credit risk grade.

Notes to the consolidated financial statements (continued)

4 Financial risk management (continued)

(b) Credit risk (continued)

Determining whether credit risk has increased significantly

The Group assesses whether credit risk has increased significantly since initial recognition at each reporting date. Determining whether an increase in credit risk is significant depends on the characteristics of the financial instrument and the borrower, and the geographical region.

The credit risk may also be deemed to have increased significantly since initial recognition based on qualitative factors linked to the Group's credit risk management processes that may not otherwise be fully reflected in its quantitative analysis on a timely basis. This will be the case for exposures that meet certain heightened risk criteria, such as placement on a watch list. Such qualitative factors are based on expert judgment and relevant historical experiences.

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. Some qualitative indicators of an increase in credit risk, such as delinquency or forbearance, may be indicative of an increased risk of default that persists after the indicator itself has ceased to exist. In these cases, the Group determines a probation period during which the financial asset is required to demonstrate good behaviour to provide evidence that its credit risk has improved sufficiently. When contractual terms of a loan have been modified, evidence that the criteria for recognising lifetime ECL are no longer met includes a history of up-to-date payment performance against the modified contractual terms.

Definition of default

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

- The borrower is unlikely to pay its credit obligations to the Group in full, without recourse by the Group to actions such as realising security (if any is held);
- For retail, a facility or any material credit obligation to the Group is more than 90 days past due;
- Overdrafts are considered as being past due once the customer has breached an advised limit or been advised of a limit smaller than the current amount outstanding.

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

Notes to the consolidated financial statements (continued)

4 Financial risk management (continued)

(b) Credit risk (continued)

Incorporation of forward-looking information

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

The Group formulates three economic scenarios: a base case, which is the median scenario assigned a 40% probability of occurring, and two less likely scenarios, one upside and one downside, each assigned a 30% probability of occurring. External information considered includes economic data and forecasts published by governmental bodies and monetary authorities in the countries where the Group operates, supranational organisations such as the OECD and the International Monetary Fund, and selected private-sector and academic forecasters.

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

The economic scenarios used as at 31 December 2021 included the following key indicators for the years ending 31 December 2022 to 2026.

Region	Macro Variable ^{1,2}	Scenario	2022	2023	2024	2025	2026	
MENA	Oil Price	Base	-11.15%	3.35%	1.47%	4.18%	3.11%	
		Upside	-7.25%	3.58%	1.44%	3.99%	3.02%	
		Downside	-36.77%	33.95%	6.08%	8.21%	4.56%	
	UAE GDP	Base	2.01%	2.59%	2.67%	2.75%	2.66%	
		Upside	5.63%	3.13%	2.02%	2.45%	2.28%	
		Downside	-6.00%	2.75%	5.46%	5.15%	4.53%	
	UAE Housing price Index	Base	-0.33%	0.69%	2.20%	2.97%	3.20%	
		Upside	2.41%	2.65%	0.95%	0.21%	0.92%	
			Downside	-9.50%	-3.54%	5.16%	7.67%	7.07%

(1) Represents the average annualized increase / decrease over the period.

(2) There are additional macro variables factors used for other regions which are relevant to their market.

Notes to the consolidated financial statements (continued)

4 Financial risk management (continued)

(b) Credit risk (continued)

Modified financial assets

The contractual terms of a loan may be modified for a number of reasons, including changing market conditions, customer retention and other factors not related to a current or potential credit deterioration of the customer. An existing loan whose terms have been modified may be derecognised and the renegotiated loan recognised as a new loan at fair value in accordance with the accounting policy set out in Note 3(c)(iv).

When the terms of a financial asset are modified and the modification does not result in derecognition, the determination of whether the asset's credit risk has increased significantly reflects comparison of:

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

The Group renegotiates loans to customers in financial difficulties (referred to as 'forbearance activities') to maximise collection opportunities and minimise the risk of default. Under the Group's forbearance policy, loan forbearance is granted on a selective basis if the debtor is currently in default on its debt or if there is a high risk of default, there is evidence that the debtor made all reasonable efforts to pay under the original contractual terms and the debtor is expected to be able to meet the revised terms.

The revised terms usually include extending the maturity, changing the timing of interest payments and amending the terms of loan covenants. Both retail and corporate loans are subject to the forbearance policy. The Group Credit Committee regularly reviews reports on forbearance activities.

For financial assets modified as part of the Group's forbearance policy, the estimate of PD reflects whether the modification has improved or restored the Group's ability to collect interest and principal and the Group's previous experience of similar forbearance action. As part of this process, the Group evaluates the borrower's payment performance against the modified contractual terms and considers various behavioural indicators.

Generally, forbearance is a qualitative indicator of a significant increase in credit risk and an expectation of forbearance may constitute evidence that an exposure is credit-impaired (see Note 3(c)(vii)). A customer needs to demonstrate consistently good payment behaviour over a period of time before the exposure is no longer considered to be credit-impaired/in default or the PD is considered to have decreased such that the loss allowance reverts to being measured at an amount equal to Stage 1.

Notes to the consolidated financial statements *(continued)*

4 Financial risk management *(continued)*

(b) Credit risk *(continued)*

Measurement of ECL

The key inputs into the measurement of ECL are:

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

The Lifetime PDs are determined based on maturity profile. The maturity profile looks at how defaults develop on a portfolio throughout the remaining life of the loans. The maturity profile is based on historical observed data.

LGD is the magnitude of the likely loss if there is a default. The Group estimates LGD term structure based on current collateral, counterparty industry, country of risk and recovery costs that is integral to the financial asset. LGD estimates are recalibrated for different economic scenarios incorporating the impact of change in oil prices, equity index and other parameters.

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

As described above, and subject to using a maximum of a 12-month for Stage 1 financial assets, the Group measures ECL considering the risk of default over the maximum contractual period (including any borrower's extension options) over which it is exposed to credit risk, even if, for credit risk management purposes, the Group considers a longer period. The maximum contractual period extends to the date at which the Group has the right to require repayment of an advance or terminate a loan commitment or guarantee.

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;
- LTV ratio for retail mortgages;
- remaining term to maturity;
- geographic location of the borrower
- collateral type;
- date of initial recognition;
- industry; and

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

Notes to the consolidated financial statements (continued)

4 Financial risk management (continued)

(b) Credit risk (continued)

Loss allowance

The following tables show reconciliations from the opening to the closing balance of the loss allowance by class of financial instrument.

	Stage 1 ¹	Stage 2	Stage 3	2021 Total
	AED'000	AED'000	AED'000	AED'000
Beginning of the period	1,471	-	34,506	35,977
	-----	-----	-----	-----
	1,471	-	34,506	35,977
Transfers:				
Transfer from Stage 1 to Stage 2	-	-	-	-
Transfer from Stage 1 to Stage 3	-	-	-	-
Transfer from Stage 2 to Stage 1	-	-	-	-
Transfer from Stage 2 to Stage 3	-	-	-	-
Transfer from Stage 3 to Stage 2	-	-	-	-
Transfer from Stage 3 to Stage 1	-	-	-	-
	-----	-----	-----	-----
	-	-	-	-
Impact of change in provision	(728)	920	-	192
Write-offs and other adjustments	-	-	-	-
	-----	-----	-----	-----
	743	920	34,506	36,169
	=====	=====	=====	=====

¹On certain assets included as part of other assets, ECL is computed based on simplified approach and reported as part of stage 1.

Notes to the consolidated financial statements (continued)

4 Financial risk management (continued)

(b) Credit risk (continued)

	Stage 1 AED'000	Stage 2 AED'000	Stage 3 AED'000	2020 Total AED'000
Beginning of the period	1,871	-	34,506	36,377
	<u>1,871</u>	<u>-</u>	<u>34,506</u>	<u>36,377</u>
Transfers:				
Transfer from Stage 1 to Stage 2	-	-	-	-
Transfer from Stage 1 to Stage 3	-	-	-	-
Transfer from Stage 2 to Stage 1	-	-	-	-
Transfer from Stage 2 to Stage 3	-	-	-	-
Transfer from Stage 3 to Stage 2	-	-	-	-
Transfer from Stage 3 to Stage 1	-	-	-	-
	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>
Impact of change in provision	(45)	-	-	(45)
Write-offs and other adjustments	(355)	-	-	(355)
	<u>1,471</u>	<u>-</u>	<u>34,506</u>	<u>35,977</u>

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

The table below shows the maximum exposure to credit risk for the components of the balance sheet. The maximum exposure is shown gross, before the effect of mitigation through the use of master netting and collateral agreements.

	Note	Gross Maximum exposure 2021 AED'000	Gross Maximum exposure 2020 AED'000
Due from banks	7	515,166	557,308
Loans and Advances	8	481,567	628,731
Receivables and prepayments	10	7,669	6,941
Total Credit risk exposure		<u>1,004,402</u>	<u>1,192,980</u>

Notes to the consolidated financial statements *(continued)*

4 Financial risk management *(continued)*

(b) Credit risk *(continued)*

Bank balances

The balances are held with banks with good credit standings.

Settlement risk

The Group's activities may give rise to risk at the time of settlement of transactions and trades. Settlement risk is the risk of loss due to the failure of a counter party to honour its obligations to deliver cash, securities or other assets as contractually agreed. Any delay in settlement is rare and monitored.

5 Liquidity risk

Liquidity risk arises from cash flows generated by assets and liabilities, including derivatives and other off-balance sheet commitments, not being matched in currency, size, and term, thereby creating financing needs which potentially cannot be met without incurring substantially higher costs or at any cost at all.

Liquidity risk is defined as the risk that the Group is unable to meet its financial obligations as and when they fall due or that it can only do so at an excessive cost.

Management of liquidity risk

The Parent has defined the liquidity risk appetite at consolidated level so as to ensure that there is controlled liquidity risk position with adequate cash or cash-equivalents to be able to meet its financial obligations, in all foreseeable circumstances and without incurring substantial additional costs, for a rolling period of three months.

The Parent or G-ALCO is responsible to ensure that the Group continues to have sufficient liquidity to support its operations and also to comply with current and proposed liquidity regulation (if any).

All liquidity policies and procedures are subject to review and approval by G-ALCO.

Notes to the consolidated financial statements (continued)

4 Financial risk management (continued)

(c) Liquidity risk (continued)

Exposure to liquidity risk

The contractual asset and liability maturity mismatch report without considering the Group's retention history as is detailed below.

	Total AED'000	Up to 3 months AED'000	3 months to 1 year AED'000	1 to 5 Years AED'000	Over 5 years AED'000	Unspecified maturity AED'000
At 31 December 2021						
Due from Banks	515,166	515,166	-	-	-	-
Loans and Advances	481,567	39,395	115,122	303,308	23,742	-
Receivables and prepayments	7,669	-	-	-	-	7,669
Premises and equipment	407	-	-	-	-	407
	-----	-----	-----	-----	-----	-----
Total assets	1,004,809	554,561	115,122	303,308	23,742	8,076
	=====	=====	=====	=====	=====	=====
Bank borrowings	413,267	413,267	-	-	-	-
Trade and other payables	18,915	-	-	-	-	18,915
Equity	572,627	-	-	-	-	557,627
	-----	-----	-----	-----	-----	-----
Total liabilities and equity	1,004,809	413,267	-	-	-	591,542
	=====	=====	=====	=====	=====	=====

Notes to the consolidated financial statements (continued)

4 Financial risk management (continued)

(c) Liquidity risk (continued)

Maturities of assets and liabilities (continued)

	Total AED'000	Up to 3 months AED'000	3 months to 1 year AED'000	1 to 5 years AED'000	Over 5 years AED'000	Unspecified maturity AED'000
At 31 December 2020						
Due from Banks	557,308	557,308	-	-	-	-
Loans and Advances	628,731	-	22,186	215,794	390,751	-
Receivables and prepayments	6,941	-	-	-	-	6,941
Premises and equipment	468	-	-	-	-	468
Total assets	1,193,448	557,308	22,186	215,794	390,751	7,409
Bank borrowings	608,152	608,152	-	-	-	-
Trade and other payables	22,378	-	-	-	-	22,378
Equity	562,918	-	-	-	-	562,918
Total liabilities and equity	1,193,448	608,152	-	-	-	585,296

Notes to the consolidated financial statements *(continued)*

4 Financial risk management *(continued)*

(d) Market risk

Market risk is the risk that the Group's income and / or value of a financial instrument will fluctuate due to changes in market prices such as interest rates, foreign exchange rates and market prices of equity.

Management of market risk

Overall authority for market risk is vested in the Group Risk Committee (GRC) and Group Asset & Liability Committee (G-ALCO), of the Parent, which sets limits for each type of risk in aggregate and for specific portfolios. Risk Group is responsible for the development of detailed risk management policies (subject to review and approval by the GRC).

Interest rate risk

Interest rate risk arises from interest bearing financial instruments and reflects the possibility that changes in interest rates will adversely affect the value of the financial instruments and the related income. The Group manages this risk principally through monitoring interest rate gaps and by matching the re-pricing profile of assets and liabilities.

The substantial portion of the Group's assets and liabilities are re-priced within one year. Accordingly there is a limited exposure to interest rate risk.

Notes to the consolidated financial statements (continued)

4 Financial risk management (continued)

(d) Market risk (continued)

Interest rate risk (continued)

The Group's interest rate sensitivity position based on contractual re-pricing arrangements at 31 December 2021 was as follows:

	Total AED'000	Up to 3 months AED'000	3 months to 1 year AED'000	1 year to 5 years AED'000	Over 5 years AED'000	Non-Interest bearing AED'000
Assets						
Due from Banks	515,166	515,166	-	-	-	-
Loans and Advances	481,567	367,590	18,962	95,015	-	-
Receivables and prepayments	7,669	-	-	-	-	7,669
Premises and equipment	407	-	-	-	-	407
Total assets	1,004,809	882,756	18,962	95,015	-	8,076
Liabilities						
Bank borrowings	413,267	413,267	-	-	-	-
Trade Payables	18,915	-	-	-	-	18,915
Equity	572,627	-	-	-	-	572,627
Total liabilities	1,004,809	413,267	-	-	-	591,542
Total interest rate sensitivity gap		469,489	18,962	95,015	-	(583,466)
Cumulative interest rate sensitivity		469,489	488,451	583,466	583,466	-

Notes to the consolidated financial statements (continued)

4 Financial risk management (continued)

(d) Market risk (continued)

Interest rate risk (continued)

The Group's interest rate sensitivity position based on contractual re-pricing arrangements at 31 December 2020 was as follows:

	Total AED'000	Up to 3 months AED'000	3 months to 1 year AED'000	1 year to 5 years AED'000	Over 5 years AED'000	Non-Interest bearing AED'000
Assets						
Due from Banks	557,308	557,308	-	-	-	-
Loans and Advances	628,731	477,170	-	-	151,561	-
Receivables and prepayments	6,941	-	-	-	-	6,941
Premises and equipment	468	-	-	-	-	468
Total assets	1,193,448	1,034,478	-	-	151,561	7,409
Liabilities						
Bank borrowings	608,152	608,152	-	-	-	-
Trade Payables	22,378	-	-	-	-	22,378
Equity	562,918	-	-	-	-	562,918
Total liabilities	1,193,448	608,152	-	-	-	585,296
Total interest rate sensitivity gap		426,326	-	-	151,561	(577,887)
Cumulative interest rate sensitivity		426,326	426,326	426,326	577,887	-

Notes to the consolidated financial statements (continued)

4 Financial risk management (continued)

(d) Market risk (continued)

Interest rate risk (continued)

Interest rate risk is also assessed by measuring the impact of reasonable possible change in interest rate movements. The Group assumes a fluctuation in interest rates of 50 basis points (2020: 50 basis points) and estimates the following impact on the net profit for the year and equity at that date:

	2021 Profit for the year AED'000	2020 Profit for the year AED'000
Fluctuation in yield	<u>± 2,101</u>	<u>± 1,868</u>

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

Interest Rate Benchmark Reform

A fundamental reform of major interest rate benchmarks is being undertaken globally, replacing some IBORs with ARRS. The Group has significant exposure to certain IBORs on its financial instruments that are being reformed as part of these market-wide initiatives.

IBORs, plays a critical role in global financial markets, serving as reference rates for derivatives, Loans, advances, and as parameters in the valuation of financial instruments.

The transition process away from IBORs, including the transition of legacy contracts that reference IBORs, exposes the Group to material execution risks, and increases some financial and non-financial risks which the project team is managing and monitoring closely. These risks include but are not limited to the following:

- Conduct risk arising from discussions with clients and market counterparties due to the amendments required to existing contracts necessary to effect IBOR reform.
- Financial risk to the Group and its clients that markets are disrupted due to IBOR reform giving rise to financial losses. Further, financial risks resulting from the discontinuation of IBORs and the development of market liquidity in RFRs will also affect the Group throughout transition.
- Pricing risk from the potential lack of market information if liquidity in IBORs reduces and RFRs are illiquid and unobservable.
- Operational risk arising from changes to the Group's IT systems and processes, also the risk of payments being disrupted if an IBOR ceases to be available; and

Notes to the consolidated financial statements *(continued)*

4 Financial risk management *(continued)*

(d) **Market risk** *(continued)*

Interest rate risk *(continued)*

Interest Rate Benchmark Reform *(continued)*

As the IBOR transition project progresses into the execution phase, resilience and operational risks are heightened. This is due to an expected transition of legacy IBOR contracts and the extensive systems and process changes required to facilitate the transition. Regulatory compliance, legal and conduct risks may also increase as a result of the co-existence of LIBORs and ARR for limited period.

Group's approach towards IBOR Transition

Loans and other On Balance Sheet related exposures

The Group, through its parent First Abu Dhabi Bank PJSC ("the Parent") initiated its IBOR transition project in 2019. The Project is sponsored by the Parent CFO and is being led by senior representatives from functions across the Group including the client facing teams, Legal, Finance, Operations and Technology. The Parent has maintained its momentum in tracking its exposure to IBORs, preparing its IT systems to accommodate the incoming Risk-Free Rates, amending, or preparing contractual templates and communicating its progress with both the Regulators and its clients. The Project provides monthly progress updates to the Project sponsors. The Group has successfully achieved the readiness to transition a significant portion of its IBOR exposure to RFRs and has in place detailed plans, processes, and procedures to support the transition of the IBOR exposures prior to the Benchmark cessation. Loans referencing USD LIBOR will be transitioned prior to the benchmark cessation date.

For contracts indexed to an IBOR that mature after the expected cessation of the IBOR rate, the Group has established policies to amend the contractual terms. These amendments include the addition of fallback clauses or replacement of the IBOR rate with an alternative benchmark rate.

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

Notes to the consolidated financial statements (continued)

4 Financial risk management (continued)

(d) Market risk (continued)

Interest rate risk (continued)

Interest Rate Benchmark Reform (continued)

Group's approach towards IBOR Transition (continued)

The table below sets out the IBOR rates that the Group had exposure to, the new benchmark rates to which these exposures have or are being transitioned, and the status of the transition.

Currency	Benchmark before reform	Benchmark after reform	31 Dec 2021	31 Dec 2020
USD	USD Libor	SOFR	In Progress	In Progress

Changes to the contractual terms of financial assets indexed to certain US dollar LIBOR to incorporate new benchmark rates are completed as of 31 December 2021. The Group has actively developed and implemented system and operational capabilities for alternative rates, such as base or prime rates and RFR products during 2021. The Group continues to have IBOR loan exposures maturing beyond the above mentioned cessation or non-representativeness dates but will cease the issuance of new IBOR linked products after 31 December 2021.

The Group has implemented commercial strategies that include active client engagement and communication. As at 31 December 2021, the Group

- amended existing contracts indexed to IBOR to incorporate new benchmark rates for contracts originally indexed to GBP LIBOR; and
- inserted fallback provisions into all remaining US dollar LIBOR indexed exposures.

The table below represents the exposures to interest rate benchmark reform by balance sheet account, which have yet to transition. The exposure disclosed is for positions with contractual maturities referencing: USD LIBOR (other than USD LIBOR 1W and 2M tenors) after 30 June 2023.

Balances reported at amortized cost are disclosed at their gross carrying value and do not include any expected credit losses that may be held against them.

	USD Libor	Total
Non Derivative financial assets		
Loans and advances	127,471	127,471
Non-derivative financial liabilities		
Bank Borrowing	141,018	141,018

Notes to the consolidated financial statements (continued)

4 Financial risk management (continued)

(d) Market risk (continued)

Interest rate risk (continued)

Interest Rate Benchmark Reform (continued)

Group's approach towards IBOR Transition (continued)

In the table below are exposures at 31 December 2021 that were not transitioned from IBORs to RFRs on 1 January 2022 and still present a risk arising from IBOR reform.

	USD Libor	Total
Non Derivative financial assets		
Loans and advances	127,471	127,471
Non-derivative financial liabilities		
Bank Borrowing	141,018	141,018

Foreign exchange risk

Foreign exchange risk is the risk that the value of a financial instrument will fluctuate due to changes in foreign exchange rates and arises from financial instruments denominated in a foreign currency. The Group's functional currency is the UAE Dirham.

The majority of the Group's transactions and balances are in AED, or in US Dollars to which the AED is pegged. Since the majority of the assets and liabilities are in AED or USD, the management estimates that any reasonable possible changes in exchange rates would not have a significant impact on the Group's consolidated financial statements.

(e) Operational risks

Operational risk is defined as the risk of losses resulting from inadequate or failed processes, people & systems or from external events, this includes legal and technology risk and excludes strategic and reputation risk.

Operational risks arise across all businesses in the Group. The primary responsibility to ensure that risks are managed and monitored resides with the businesses within the Group. Group's business are supported by Embedded risk functions and parent's Operational Risk Management as 'second line of defence' to ensure robust risk management.

Notes to the consolidated financial statements *(continued)*

4 Financial risk management *(continued)*

(e) Operational risks *(continued)*

Further, there are reviews conducted by Parent's Group Internal Audit as the 'third line of defence'. The results of internal audit reviews are discussed with the management of the respective divisions and summaries are submitted to the Audit Committee.

The Parent has an established Operational Risk framework consisting of policies and procedures to identify, assess, monitor, control, report and to manage risks and to notify, identify and rectify incidents. The Operational Risk framework also provides the interrelation with other risk categories. Where appropriate, risk is mitigated by way of insurance.

Typically, Operational Risk events are classified as:

- Internal fraud: Risk of unauthorized activity and fraud perpetrated by employees
- External fraud: Risk of fraud or breach of system security by an external party
- Employee practices & workplace safety: Risk of failures in employee relations, diversity and discrimination, and health and safety risks across the Group
- Damage to physical assets: Risk of impact to the Group due to natural disasters
- Clients, Products & Business Practices: Risk of failing in assessing client suitability, fiduciary responsibilities, improper business practices, flawed products and advisory activities.
- Business Disruption & System failures: Risk of not planning and testing business continuity and disaster recovery for systems
- Execution delivery and process management: Risk of failed transaction execution, customer intake and documentation, vendor management and monitoring and reporting.

The Board has oversight responsibilities for operational risk management across the Group. These responsibilities are delegated and exercised through the Group Risk Committee, which is the senior management forum responsible for the oversight of Operational Risk.

Key responsibilities of Group Risk Committee with regards to Operational risk include to ensure:

- Approval of the Group Operational Risk Management Framework and oversight over its implementation
- Approve large incidents as per the Operational Risk management approval matrix
- Approve the strategy and direction for Operational Risk across the group

(f) Capital management

The Group's policy is to maintain a strong capital base to maintain creditors and market confidence and to sustain future development of the business. The Group monitors the return on capital and the level of dividends to the shareholders.

As per Article 76 of the UAE Federal Law No. 2 of 2016, applicable to limited liability companies, the Cabinet may issue a decision determining the minimum limit of the capital of the company. There were no changes to the Group's approach to capital management during the year.

Notes to the consolidated financial statements *(continued)*

4 Financial risk management *(continued)*

(g) Compliance Risk

Compliance risk refers to the risk to earnings or capital or reputation or continued business existence arising from violations of, or non-conformance with, laws, rules, regulations, prescribed practices, or ethical standards. The Group, on a continuous basis, identifies and assesses such risks inherent in all new and existing “material” products, activities, processes and systems. This includes risk assessments on non-conformance with laws, rules, regulations, prescribed practices, or ethical standards. The Group Compliance function has a group-wide compliance unit that develops internal policies under which such risks are managed, and it is supported by the Risk Management, Internal Audit and Legal functions. In order to monitor compliance and financial crime risks, the Group has developed and implemented due diligence processes, reviews of policies and procedures across the Group, implementation of integrated compliance and financial crime systems which manage name clearance, transaction monitoring, payment monitoring activities, assessment through compliance checklists etc. Compliance risk is largely mitigated by way of focused policies and procedures, extensive checklist based and on-spot due diligence, annual risk assessments, monitoring and assurance, communications, and regular training sessions

(h) Reputational Risk

Reputational risk is the risk to earnings or capital arising from negative public opinion. This can be due to external or internal events. The Group identifies and assesses reputational risk by clearly defining types of risks to be captured, establishing key sources of reputational risk it may be exposed to, based on individual circumstances, describing the risks identified in terms of the nature of risk and the potential consequences that the risks may bring to its reputation. The Group also refers to other relevant information for risk identification purposes. Such information may be sourced from media reports, stakeholder analysis reports, internal audit and compliance reports, management exception reports or other early warning indicators. For reputational risks, apart from the regular monitoring of external and internal events that can result in possible reputational risks, the Group also has processes to track risks that may affect its reputation. These processes allow the BOD and senior management to take prompt corrective actions to address any anticipated reputational event in advance. In order to manage reputational risks, the Group has set in place a mechanism that entails drawing up action plans to identify reputational risk events and facilitate subsequent monitoring of the progress made; for those risks that may be very difficult or too costly to eliminate entirely the mechanism requires development of contingency plans as response actions.

5 Use of estimates and judgements

In the process of applying the Group’s accounting policies, IFRS require the management to select suitable accounting policies, apply them consistently and make judgements and estimates that are reasonable and prudent and would result in relevant and reliable information. The management, based on guidance in IFRS and the IASB’s Framework for the Preparation and Presentation of Financial Statements has made these estimates and judgements. Listed below are those estimates and judgement which could have the most significant effect on the amounts recognised in the consolidated financial statements.

Notes to the consolidated financial statements (continued)

5 Use of estimates and judgements (continued)

Key sources of estimation uncertainty

(a) Going concern

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

(b) Impairment charge on financial assets

Impairment losses are evaluated as described in accounting policy 3(c)(vii).

The measurement of impairment losses both under IFRS 9 and IAS 39 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 in which can result in different levels of allowances.

The Bank's ECL calculations are outputs of complex models with a number of underlying assumptions regarding the choice of variable inputs and their interdependencies. Elements of the ECL models that are considered accounting judgements and estimates include:

- The Group's internal credit grading model, which assigns PDs to the individual grades
- The Group's criteria for assessing if there has been a significant increase in credit risk and so allowances for financial assets should be measured on a lifetime ECL basis and the qualitative assessment
- The segmentation of financial assets when their ECL is assessed on a collective basis
- Development of ECL models, including the various formulas and the choice of inputs
- Determination of associations between macroeconomic scenarios and, economic inputs, such as unemployment levels and collateral values, and the effect on PDs, EADs and LGDs
- Selection of forward-looking macroeconomic scenarios and their probability weightings, to derive the economic inputs into the ECL models

(c) Contingent liability arising from litigations

Due to the nature of its operations, the Group may be involved in litigations arising in the ordinary course of business. Provision for contingent liabilities arising from litigations is based on the probability of outflow of economic resources and the reliability of estimating such outflow. Such matters are subject to many uncertainties and the outcome of individual matters is not predictable with assurance. The Group's accounting policies provide scope for financial assets and liabilities to be designated on inception into different accounting categories in certain circumstances. The classification criteria is mentioned in policy 3(c) (ii).

Notes to the consolidated financial statements *(continued)*

(d) **Effective Interest Rate (EIR) method**

The Group's EIR method, as explained in Note 3 (d), recognises interest income using a 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 along with recognising the impact of transaction costs and fees and points paid or received that are an integral part of the effective interest rate. This estimation, by nature, requires an element of judgement regarding the expected behaviour and life-cycle of the instruments, as well expected changes to the base rate and other fee income/expense that are integral parts of the instrument.

During the year, the Group has adopted IBOR reform Phase 2, which requires as a practical expedient for changes to the basis for determining contractual cash flows that are necessary as a direct consequence of IBOR reform, to be treated as a change to a floating rate of interest provided the transition from IBOR to RFR takes place on a basis that is economically equivalent. For changes that are not required by IBOR reform, the Group applies judgment to determine whether they result in the financial instrument being derecognised or adjust its carrying value as described below in 5(e). Therefore, as financial instruments transition from IBOR to RFRs, the Group applies judgment to assess whether the transition has taken place on an economically equivalent basis. In making this assessment, the Group considers the extent of any changes to the contractual cash flows as a result of the transition and the factors that have given rise to the changes, with consideration of both quantitative and qualitative factors.

(e) **Derecognition of financial instruments**

As explained in Note 3(c) (iv), the Group derecognises financial assets and financial liabilities if there has been a substantial modification of their terms and conditions. In the context of IBOR reform, many financial instruments have already been amended during 2021 as they transition from IBORs to RFRs. In addition to the interest rate of a financial instrument changing, there may be other changes made to the terms of the financial instrument at the time of transition. For financial instruments measured at amortized cost, the Group first applies the practical expedient as described in Note 5 (d) above, to reflect the change in the referenced interest rate from an IBOR to an RFR. Second, for any changes not covered by the practical expedient, the Group applies judgement to assess whether the changes are substantial and if they are, the financial instrument is derecognised and a new financial instrument is recognised. If the changes are not substantial, the Group adjusts the gross carrying amount of the financial instrument by the present value of the changes not covered by the practical expedient, discounted using the revised EIR.

Notes to the consolidated financial statements (continued)

6 Financial assets and liabilities

The table below sets out the Group's classification of each class of financial assets and liabilities and their carrying amounts as at 31 December 2021.

	Designated at fair value through profit or loss	Amortised Cost	Carrying Amount
	AED'000	AED'000	AED'000
Assets			
Due from banks	-	515,166	515,166
Loans and Advances	-	481,567	481,567
Receivables	-	7,669	7,669
	<u>-</u>	<u>1,004,402</u>	<u>1,004,402</u>
	<u><u>-</u></u>	<u><u>1,004,402</u></u>	<u><u>1,004,402</u></u>
Liabilities			
Bank borrowings	-	413,267	413,267
Trade and other payables	-	18,915	18,915
	<u>-</u>	<u>432,182</u>	<u>432,182</u>
	<u><u>-</u></u>	<u><u>432,182</u></u>	<u><u>432,182</u></u>

Assets and liabilities that are not measured at fair value, their carrying values are close approximates of their fair values. Financial assets and liabilities measured at amortised cost primarily fall under Level 3 (2020: Level 3) in the fair value hierarchy.

Notes to the consolidated financial statements (continued)

6 Financial assets and liabilities (continued)

The table below sets out the Group's classification of each class of financial assets and liabilities and their carrying amounts as at 31 December 2020.

	Designated at fair value through profit or loss		Carrying amount AED'000
	AED'000	Amortised cost AED'000	
Assets			
Due from banks	-	557,308	557,308
Loans and Advances	-	628,731	628,731
Receivables	-	6,941	6,941
	<u>-</u>	<u>1,192,980</u>	<u>1,192,980</u>
Liabilities			
Bank borrowings	-	608,152	608,152
Trade and other payables	-	22,378	22,378
	<u>-</u>	<u>630,530</u>	<u>630,530</u>

Valuation Models

All financial assets and liabilities are measured at amortised cost.

Notes to the consolidated financial statements (continued)

7 Due from banks

	2021 AED'000	2020 AED'000
Current account	515,166	557,308
	<u>515,166</u>	<u>557,308</u>

Current account balances are placed with the Parent.

8 Loans and advances

	2021 AED'000	2020 AED'000
Gross loans and advances	562,172	703,628
Less: interest suspended	(44,541)	(39,026)
Less: expected credit loss	(36,064)	(35,871)
Net loans and advances	<u>481,567</u>	<u>628,731</u>

	2021 AED'000	2020 AED'000
By counterparty:		
Public sector	352,352	477,170
Corporate / private sector	209,820	226,458
Gross loans and advances	<u>562,172</u>	<u>703,628</u>

Notes to the consolidated financial statements *(continued)*
8 Loans and advances *(continued)*

	2021 AED'000	2020 AED'000
By product:		
Asset Based Finance	562,172	703,628
Gross loans and advances	<u>562,172</u>	<u>703,628</u>

	2021 AED'000	2020 AED'000
By Industry:		
Transport & Communication Services	468,841	615,812
Manufacturing	89,652	87,816
	3,679	-
Gross loans and advances	<u>562,172</u>	<u>703,628</u>

9 Net impairment charge

	2021 AED'000	2020 AED'000
Impairment charge / (reversal) on loans and advances	192	(400)
	<u>192</u>	<u>(400)</u>

10 Receivables and prepayments

	2021 AED'000	2020 AED'000
Prepayments and others	7,669	6,941
	<u>7,669</u>	<u>6,941</u>

Notes to the consolidated financial statements (continued)

11 Premises and equipment

	Leasehold Improvements	Computer equipment	Furniture, Equipment, Fixtures, Safes and vehicles	Total
	AED'000	AED'000	AED'000	AED'000
Cost				
At 1 January 2020	922	45	639	1,606
Additions	-	-	-	-
Disposals, transfers and write offs.	-	-	-	-
At 31 December 2020	922	45	639	1,606
Additions	-	-	-	-
Asset reclassification	-	-	-	-
Disposals, transfers and write offs	-	(12)	(8)	(20)
At 31 December 2021	922	33	631	1,586
Accumulated depreciation				
At 1 January 2020	460	45	568	1,073
Charge for the year	42	-	23	65
Disposals, transfers and write offs	-	-	-	-
At 31 December 2020	502	45	591	1,138
Charge for the year	42	-	19	61
Disposals, transfers and write offs	-	(12)	(8)	(20)
At 31 December 2021	544	33	602	1,179
Carrying amounts				
At 31 December 2020	420	-	48	468
At 31 December 2021	378	-	29	407

Notes to the consolidated financial statements (continued)

12 Bank borrowings

	2021 AED'000	2020 AED'000
Unsecured loans	413,267	608,152

Unsecured loans are obtained from the Parent at market rates ranging from 0.16% to 2.62% (2020: 0.16% to 2.62%). Loans are obtained in US Dollars or AED and have maturities between 3 months to 9 years.

Bank overdrafts are variable rate facilities obtained from the Parent at market rates.

The Group has not had any default of principal, interest or other breaches with respect to its bank borrowings.

13 Trade and other payables

	2021 AED'000	2020 AED'000
Others	18,915	22,378

14 Share capital

	2021 AED'000	2020 AED'000
Authorised, issued and fully paid up: 1,000 shares of AED 10,000 each (2020: 1,000 shares of AED 10,000 each)	10,000	10,000

15 Statutory reserve

The Articles of Association of the Company require that 10% of the profit for the year is to be transferred to a statutory reserve until this reserve equals 50% of the paid-up share capital. The statutory reserve is not available for distribution to the shareholders. As the reserve is already at 50%, no transfers were made in current year (2020: nil).

Notes to the consolidated financial statements (continued)

16 Finance costs

	2021 AED'000	2020 AED'000
Interest on:		
Unsecured loans	3,348	11,553

17 Related parties

Parent and ultimate controlling party

The Company is effectively wholly owned subsidiary of the Parent.

Identity of related parties

Related parties comprise the Shareholders, directors and key management of the Company and their related concerns. The terms of these transactions are approved by the Company's management or the board.

Transactions with key management personnel

No remuneration was paid to the key management personnel during the current year (2020: AED nil).

Significant transactions and balances with related parties

The significant transactions and balances with related parties included in these consolidated financial statements are as follows:

		2021 AED'000	2020 AED'000
Transactions			
Finance cost	(note 16)	3,348	11,553
Interest income		12,586	25,997
Fee and commission income		342	1

Notes to the consolidated financial statements *(continued)*

17 Related parties *(continued)*

The Group's operational, administrative and managerial services are provided by the Parent for no consideration and the management service agreement for providing such services is in the process of being formalised.

Balances		2021 AED'000	2020 AED'000
Loans and Advances		257,137	164,418
Due from banks	<i>(note 7)</i>	515,166	557,308
Bank borrowings	<i>(note 12)</i>	413,267	608,152

18 Comparative figures

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