



بنك دبي الإسلامي  
Dubai Islamic Bank

## Basel III – Pillar III Disclosures

2019



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**PILLAR III DISCLOSURES**

31 DECEMBER 2019

**1. Overview and Introduction**

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

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

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

The Pillar III disclosures provide both qualitative and quantitative information at Group level in order to meet the disclosure requirements. Some of the Pillar III requirements have been disclosed in the audited consolidated financial statements for the year ended 31

December 2019, which covers the risk and capital management processes of the Group and its compliance with the Basel Accords.

**BASEL Regulatory Framework**

The Basel Accord framework consists of following three main pillars:

- **Pillar I** - defines the regulatory minimum capital requirements by providing rules and regulations for measurement of credit risk, market risk and operational risk. The requirement of capital has to be covered by the banks’ own regulatory fund;
- **Pillar II** - addresses a bank’s Internal Capital Adequacy Assessment Process (“ICAAP”) for assessing overall capital adequacy in relation to risks other than Pillar I. Pillar II also introduces the Supervisory Review and Evaluation Process (“SREP”), which is used as a tool to assess the internal capital adequacy of banks; and
- **Pillar III** - complements the other two pillars and focuses on enhanced transparency in information disclosure, covering risk and capital management, including capital adequacy which encourages market discipline that also allows market participants to assess specific information.

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

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

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

**Future Regulatory Developments**

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

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

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

#### **Implementation and Compliance of Basel Framework Guidelines**

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

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

#### **Verification:**

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



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**2. Group Structure - Information on Subsidiaries and Significant Investments**

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

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

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

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

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

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

|     |                              |             |                |               |        |
|-----|------------------------------|-------------|----------------|---------------|--------|
| 32. | Sequia Investments L.L.C.    | Investments | U.A.E.         | <b>99.0%</b>  | 99.0%  |
| 33. | Blue Nile Investments L.L.C. | Investments | U.A.E.         | <b>99.0%</b>  | 99.0%  |
| 34. | DIB FM Ltd                   | Investments | Cayman Islands | <b>100.0%</b> | 100.0% |
| 35. | Al Ameen                     | Investments | Cayman Islands | <b>100.0%</b> | 100.0% |

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



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**3. Capital Management Structure and Policies**

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

**3.1. Capital Management Objectives**

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

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

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

**3.2. Regulatory Capital**

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

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

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

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

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

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

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

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

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**3 Capital Management Structure and Policies (continued)**
**3.2. Regulatory Capital (continued)**

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

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

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

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

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



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**3 Capital Management Structure and Policies (continued)**
**3.2 Regulatory Capital (continued)**

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

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

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

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

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

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

**3.3 Tier 1 Sukuk**

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

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**3 Capital Management Structure and Policies (continued)**
**3.3 Tier 1 Sukuks (continued)**

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

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

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

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

**3.4. Risk Weighted Assets**
**3.4.1 Credit Risk Weighted Assets**

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

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

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**3 Capital Management Structure and Policies (continued)**
**3.4. Risk Weighted Assets (continued)**
**3.4.1 Credit Risk Weighted Assets (continued)**

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

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

**3.4.2 Market Risk Weighted Assets**

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

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

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

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

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

**3 Capital Management Structure and Policies (continued)****3.4. Risk Weighted Assets (continued)****3.4.3 Operational Risk Weighted Assets**

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

**3.5. Qualitative Risk Disclosures**

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



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## **4. Risk Management Objectives and Policies**

### **4.1. Introduction**

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

The Group is exposed to various risks including:

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

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

#### **4.1.1 Risk Management Structure**

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

##### **Board of Directors**

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

##### **Board Risk Management Committees**

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

##### **Risk Management Committee**

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

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

##### **Risk Management Department**

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

##### **Asset and Liability Management Committee**

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

##### **Internal Audit Department**

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

#### **4. Risk Management Objectives and Policies (continued)**

##### **4.1. Introduction (continued)**

##### **4.1.2 Risk Measurement and Reporting Systems**

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

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

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

##### **4.1.3 Model Risk Management**

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

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

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

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

##### **4.1.4 Risk Mitigation**

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

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

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

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

#### **4. Risk Management Objectives and Policies (continued)**

##### **4.1. Introduction (continued)**

##### **4.1.4 Risk Mitigation (continued)**

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

##### **4.1.5 Risk Concentration**

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

#### **4.2 Credit Risk**

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

##### **Credit Risk Measurement**

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

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

##### **Collateral**

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

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

##### **Islamic derivative financial instruments**

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

##### **Credit – Related Commitments Risks**

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

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

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

**DUBAI ISLAMIC BANK P.J.S.C.**
**PILLAR III DISCLOSURES**

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**4. Risk Management Objectives and Policies (continued)**
**4.2 Credit Risk (continued)**
**4.2.1 Maximum exposure to credit risk without taking account of any collateral and other credit mitigation (continued)**

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

**4.2.2 Risk concentrations of the maximum exposure to credit risk**

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

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



**DUBAI ISLAMIC BANK P.J.S.C.**
**PILLAR III DISCLOSURES**

31 DECEMBER 2019

**4. Risk Management Objectives and Policies (continued)**
**4.2 Credit Risk (continued)**
**4.2.2 Risk concentrations of the maximum exposure to credit risk (continued)**

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

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



بنك دبي الإسلامي  
 Dubai Islamic Bank

#### 4. Risk Management Objectives and Policies (continued)

##### 4.2 Credit Risk (continued)

##### 4.2.3 Gross credit risk exposures as per Basel III standardized approach

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

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

#### 4. Risk Management Objectives and Policies (continued)

##### 4.2 Credit Risk (continued)

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

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

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

#### 4. Risk Management Objectives and Policies (continued)

##### 4.2 Credit Risk (continued)

##### 4.2.4 Gross credit risk exposures as per standardised approach

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

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

#### 4. Risk Management Objectives and Policies (continued)

##### 4.2 Credit Risk (continued)

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

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

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

**4. Risk Management Objectives and Policies (continued)**
**4.2 Credit Risk (continued)**
**4.2.5 Analysis of credit quality**

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

**4. Risk Management Objectives and Policies (continued)**
**4.2 Credit Risk (continued)**
**4.2.5 Analysis of credit quality (continued)**

2018

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

**4. Risk Management Objectives and Policies (continued)**
**4.2 Credit Risk (continued)**
**4.2.6 Credit risk exposure of the Banks's financial assets for each internal risk rating**

|                             | Moody's<br>equivalent<br>grades | Total<br>2019<br>AED'000 | Total<br>2018<br>AED'000 |
|-----------------------------|---------------------------------|--------------------------|--------------------------|
| <b>Low risk</b>             |                                 |                          |                          |
| Risk rating classes 1 to 3  | Aaa – A3                        | 105,962,274              | 107,497,972              |
| <b>Moderate risk</b>        |                                 |                          |                          |
| Risk rating classes 4 to 5  | Baa1 – Ba3                      | 117,632,360              | 109,157,850              |
| <b>Fair risk</b>            |                                 |                          |                          |
| Risk rating classes 6 to 7  | B1 - Caa3                       | 29,933,278               | 30,459,297               |
| <b>Default</b>              |                                 |                          |                          |
| Risk rating classes 8 to 11 | Ca - C                          | 7,227,323                | 6,248,058                |
|                             |                                 | <b>260,755,235</b>       | <b>253,363,177</b>       |
|                             |                                 | =====                    | =====                    |

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

**4.2.7 Analysis by Economic Sector and Geography**

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

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



**4. Risk Management Objectives and Policies (continued)**
**4.2 Credit Risk (continued)**
**4.2.7 Analysis by Economic Sector and Geography (continued)**

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

**4.2.8 Provision for impairment**

| 2019                                  | Stage 1<br>AED'000 | Stage 2<br>AED'000 | Stage 3<br>AED'000 | Total<br>AED'000 |
|---------------------------------------|--------------------|--------------------|--------------------|------------------|
| <b>Balance at 1 January</b>           | <b>1,014,083</b>   | <b>1,006,837</b>   | <b>3,706,452</b>   | <b>5,727,372</b> |
| Impairment charge during the year     | 61,123             | (40,646)           | 2,074,820          | 2,095,297        |
| Write back/recoveries during the year | -                  | -                  | (434,522)          | (434,522)        |
| Write off                             | -                  | -                  | (1,311,317)        | (1,311,317)      |
| Exchange and other adjustments        | 789                | (246)              | 3,310              | 3,853            |
| <b>Balance at 31 December</b>         | <b>1,075,995</b>   | <b>965,945</b>     | <b>4,038,743</b>   | <b>6,080,683</b> |
|                                       | <u>=====</u>       | <u>=====</u>       | <u>=====</u>       | <u>=====</u>     |
| 2018                                  | Stage 1<br>AED'000 | Stage 2<br>AED'000 | Stage 3<br>AED'000 | Total<br>AED'000 |
| Balance at 1 January                  | 1,810,964          | -                  | 3,921,704          | 5,732,668        |
| Reversal on transition to IFRS 9      | (1,810,964)        | -                  | -                  | (1,810,964)      |
| ECL recognized on adoption of IFRS 9  | 1,380,253          | 696,072            | -                  | 2,076,325        |
| Balance at 1 January - restated       | 1,380,253          | 696,072            | 3,921,704          | 5,998,029        |
| Impairment charge during the year     | (348,732)          | 311,109            | 1,827,006          | 1,789,383        |
| Write back/recoveries during the year | -                  | -                  | (869,492)          | (869,492)        |
| Write off                             | -                  | -                  | (1,165,634)        | (1,165,634)      |
| Exchange and other adjustments        | (17,438)           | (344)              | (7,132)            | (24,914)         |
| Balance at 31 December                | 1,014,083          | 1,006,837          | 3,706,452          | 5,727,372        |
|                                       | <u>=====</u>       | <u>=====</u>       | <u>=====</u>       | <u>=====</u>     |

## 5. Impairment Assessment

### 5.1 Impairment of Financial Assets

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

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

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

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

No impairment loss is recognized on equity investments.

#### Excepted credit loss impairment model

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

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

When estimating ECL for undrawn commitments, the Bank estimates the expected portion of the commitment that will be drawn down over its expected life. The ECL is then based on the present value of the expected shortfalls in cash flows if the financing is drawn down. The expected cash shortfalls are discounted at an approximation to the expected effective profit rate on the financing.

The Bank's liability under each guarantee is measured at the higher of the amount initially recognized less cumulative amortization recognized in the income statement, and the ECL provision. For this purpose, the Bank estimates ECLs based on the present value of the expected payments to reimburse the holder for a credit loss that it incurs. The shortfalls are discounted by the risk-adjusted rate relevant to the exposure.

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

#### Measurement of ECL

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

## **5. Impairment Assessment (continued)**

### **5.1 Impairment of Financial Assets (continued)**

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

Details of these statistical parameters/inputs are as follows:

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

#### **Macroeconomic factors, forward looking information and multiple scenarios**

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

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

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

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

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

#### **Assessment of significant increase in credit risk**

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

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

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

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

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

## 5. Impairment Assessment (continued)

### 5.1 Impairment of Financial Assets (continued)

#### Experienced credit judgement

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

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

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

#### Expected life

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

#### Renegotiated financing facilities

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

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

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

#### Definition of default

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

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

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

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

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

**5. Impairment Assessment (continued)**
**5.2 Carrying value of gross exposure by internal risk rating category and by ECL stage**
**As at 31 December 2019**

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

**As at 31 December 2018**

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

## 6. Liquidity Risk

### 6.1 Liquidity Risk and Funding Management

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

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

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

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

#### 6.1.1 Liquidity risk management process

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

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

### 6.2 Funding Approach

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

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

#### 6.2.1 Non-derivative cash flows

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

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

**6. Liquidity Risk (continued)**
**6.2 Funding Approach (continued)**
**6.2.2 Non-derivative cash flows**

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

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

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

**6.2.3 Islamic derivatives financial instruments**
**Fair values of Islamic derivative financial instruments:**

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

**6. Liquidity Risk (continued)**
**6.2 Funding Approach (continued)**
**6.2.3 Islamic derivatives financial instruments (continued)**
**Notional amounts by term to maturity**

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

**Unilateral promise to buy/sell currencies**

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

**Islamic Swaps**

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

**6.2.4 Contingent liabilities and commitments**

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



**DUBAI ISLAMIC BANK P.J.S.C.**
**PILLAR III DISCLOSURES**
**31 DECEMBER 2019**
**6. Liquidity Risk (continued)**
**6.2 Funding Approach (continued)**
**6.2.4 Contingent liabilities and commitments (continued)**

|                                 | Less than<br>3 months<br>AED'000 | 3 months<br>to 1 year<br>AED'000 | 1 to 5<br>years<br>AED'000 | Over 5<br>years<br>AED'000 | Total<br>AED'000         |
|---------------------------------|----------------------------------|----------------------------------|----------------------------|----------------------------|--------------------------|
| <b>2019</b>                     |                                  |                                  |                            |                            |                          |
| <b>Contingent liabilities:</b>  |                                  |                                  |                            |                            |                          |
| Letters of guarantee            | 11,286,923                       | 1,228,202                        | 371,727                    | 50,270                     | 12,937,122               |
| Letters of credit               | 1,142,972                        | 366,407                          | 4,841                      | -                          | 1,514,220                |
|                                 | <u>12,429,895</u>                | <u>1,594,609</u>                 | <u>376,568</u>             | <u>50,270</u>              | <u>14,451,342</u>        |
| Capital expenditure commitments | 9,730                            | -                                | 705,463                    | -                          | 715,193                  |
| <b>Total</b>                    | <u><u>12,439,625</u></u>         | <u><u>1,594,609</u></u>          | <u><u>1,082,031</u></u>    | <u><u>50,270</u></u>       | <u><u>15,166,535</u></u> |
|                                 | Less than<br>3 months<br>AED'000 | 3 months<br>to 1 year<br>AED'000 | 1 to 5<br>years<br>AED'000 | Over 5<br>years<br>AED'000 | Total<br>AED'000         |
| <b>2018</b>                     |                                  |                                  |                            |                            |                          |
| <b>Contingent liabilities:</b>  |                                  |                                  |                            |                            |                          |
| Letters of guarantee            | 11,434,751                       | 1,484,130                        | 654,260                    | 7,587                      | 13,580,728               |
| Letters of credit               | 724,993                          | 1,027,808                        | 99,110                     | -                          | 1,851,911                |
|                                 | <u>12,159,744</u>                | <u>2,511,938</u>                 | <u>753,370</u>             | <u>7,587</u>               | <u>15,432,639</u>        |
| Capital expenditure commitments | -                                | -                                | 867,525                    | -                          | 867,525                  |
| <b>Total</b>                    | <u><u>12,159,744</u></u>         | <u><u>2,511,938</u></u>          | <u><u>1,620,895</u></u>    | <u><u>7,587</u></u>        | <u><u>16,300,164</u></u> |

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## 7. Market Risk

### 7.1 Market Risk

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

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

The trading market risk framework comprises the following elements:

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

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

#### 7.1.1 Profit margin risk

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

#### 7.1.2 Profit rate risk

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

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

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

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

| Currency                         | Increase in basis points | 2019<br>AED'000 | 2018<br>AED'000 |
|----------------------------------|--------------------------|-----------------|-----------------|
| Sensitivity of net profit income | 50                       | 76,602          | 103,051         |

#### 7.1.3 Foreign exchange risk

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

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

**7. Market Risk (continued)**
**7.1 Market Risk (continued)**
**7.1.3 Foreign exchange risk (continued)**

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

**7. Market Risk (continued)**
**7.1 Market Risk (continued)**
**7.1.3 Foreign exchange risk (continued)**

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

**7. Market Risk (continued)**
**7.1 Market Risk (continued)**
**7.1.3 Foreign exchange risk (continued)**
**Sensitivity analysis - impact of fluctuation of various currencies on net income and equity**

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

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

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

**7.2 Foreign Investment**

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

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

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

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

**7. Market Risk (continued)**
**7.3 Equity Price Risk**

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

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

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

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

## 8. Operational Risk

### 8.1 Operational Risk

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

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

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

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

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

## 9. Regulatory Compliance

### 9.1 Regulatory / Compliance Risk

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

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

### 9.2 Reputational Risk

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

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



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