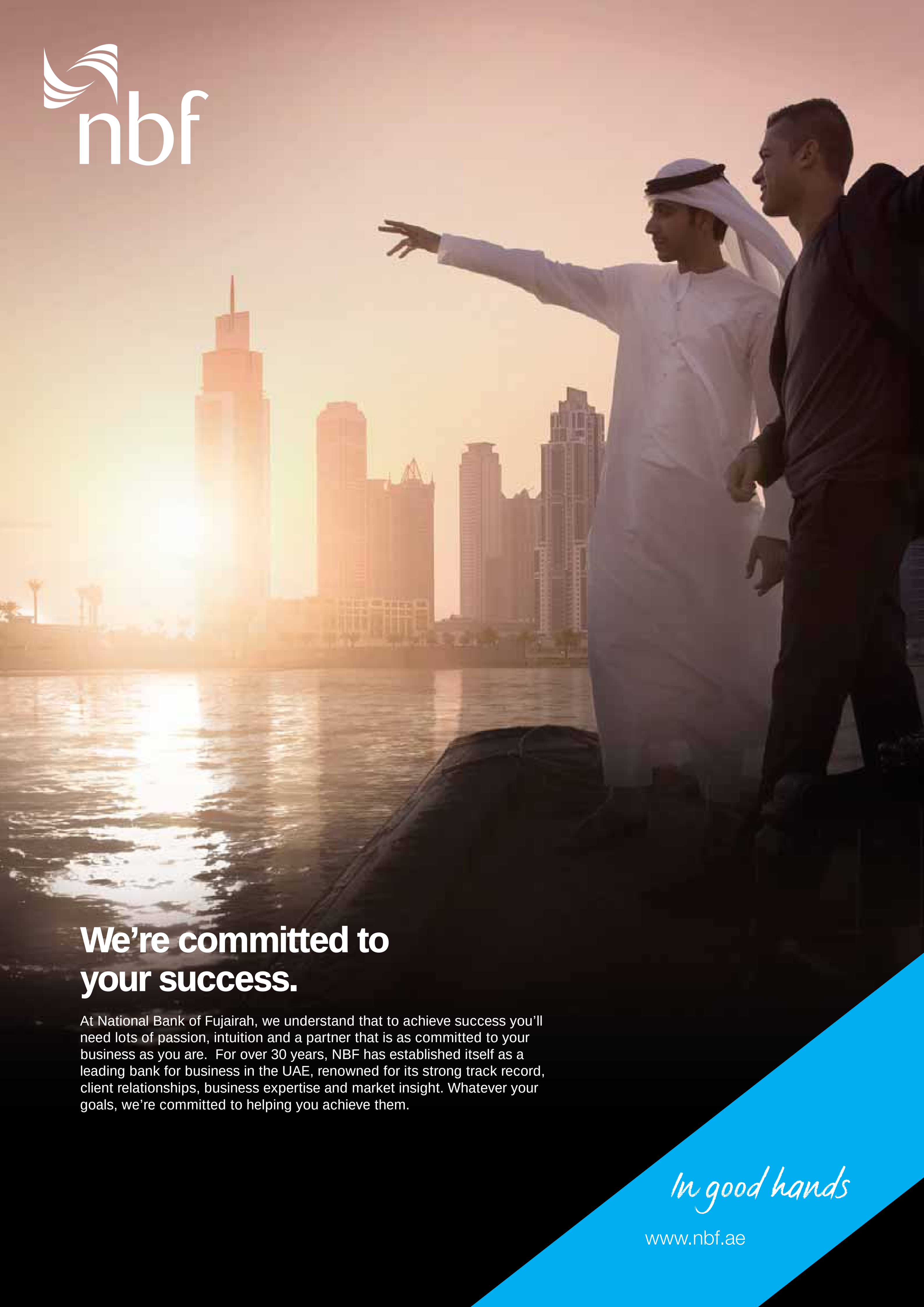
بنك الفجيرة الوطني
National Bank of Fujairah

# ANNUAL REPORT **2016**


nbf
We're committed to your success.
At National Bank of Fujairah, we understand that to achieve success you'll need lots of passion, intuition and a partner that is as committed to your business as you are.  For over 30 years, NBF has established itself as a leading bank for business in the UAE, renowned for its strong track record, client relationships, business expertise and market insight. Whatever your goals, we're committed to helping you achieve them.
In good hands
www.nbf.ae

HIS HIGHNESS SHEIKH KHALIFA BIN ZAYED AL NAHYAN

President of the UAE

HIS HIGHNESS SHEIKH MOHAMMED BIN RASHID AL MAKTOUM

Vice President and Prime Minister of the UAE and Ruler of Dubai

HIS HIGHNESS SHEIKH HAMAD BIN MOHAMMED AL SHARQI

Member of the Supreme Council and Ruler of Fujairah


**NBF**
AN INTRODUCTION

NBF has built a strong position by concentrating on its core business and deepening its focus on the customer.

## THE BANK FOR BUSINESS IN THE UAE, THE PRIDE OF FUJAIRAH

Incorporated in 1982, National Bank of Fujairah has a long established reputation for excellence in the areas of corporate and commercial banking, trade finance and treasury. More recently, we have expanded our range of products to include a comprehensive suite of personal banking options and Shari'a compliant services.

NBF's commitment to the economic development of the UAE and home emirate of Fujairah is evident through our support of industries ranging from oil and shipping to services, manufacturing, construction, education and healthcare.

With our solid track record, strong cultural heritage, deep market insight and unwavering focus on service and innovation, we seek to develop lasting relationships with our customers as we help them leverage growth opportunities in the ever-changing marketplace.

As a bank born and bred in the UAE, we at NBF celebrate our cultural heritage by playing a proactive role in the development of the local community.

We believe in cultivating rewarding relationships with our customers by providing them with the very best in financial services, innovation and service delivery.

Similarly, we continuously strive towards the creation of a stimulating environment that allows our people to pursue their own personal and professional development.

# OUR NETWORK

## Head Office

Hamad Bin Abdullah Street
PO Box 887, Fujairah

Tel +971 9 222 4518
Fax +971 9 222 4516

## NBF Branches and Offices

### Fujairah

**Fujairah Branch**
Hamad Bin Abdullah Street
PO Box 887, Fujairah
Tel +971 9 222 4513
Fax +971 9 222 9470

**Dibba Branch**
Sheikh Mohammed Bin Hamad Street
PO Box 11700, Fujairah
Tel +971 9 244 3788
Fax +971 9 244 3785

**Fujairah City Centre Branch**
G012A, Fujairah City Centre
PO Box 887, Fujairah
Tel +971 9 223 6392
Fax +971 9 223 7550

**Masafi Branch**
NBF Building, Masafi
PO Box 11208, Fujairah
Tel +971 9 202 9027
Fax +971 9 256 3339

**Qidfah Branch**
NBF Building, Qidfah
PO Box 12002, Fujairah
Tel +971 9 236 0449
Fax +971 9 236 0494

**Tawian Branch**
NBF Building, Dibba Road
PO Box 30098, Fujairah
Tel +971 7 258 4388
Fax +971 7 258 4355

**Fujairah Free Zone Branch**
NBF Building, Fujairah
Khorfakkan Road
PO Box 887, Fujairah
Tel +971 9 202 9500
Fax +971 9 224 1047

### Dubai

**Bur Dubai Branch**
Al Fujairah Building
Khalid Bin Waleed Street
PO Box 2979, Dubai
Tel +971 4 397 1700
Fax +971 4 397 9100

**Abu Hail Branch**
Al Zarouni Building
Opposite Abu Hail Centre
Abu Hail Main Road
PO Box 125841, Dubai
Tel +971 4 507 8100
Fax +971 4 221 6831

**Jebel Ali Branch**
NBF Building
Next to Etisalat, Jebel Ali
PO Box 17676, Dubai
Tel +971 4 515 7840
Fax +971 4 881 0939

**Al Quoz Branch**
Shop #14, The Curve Building
Next to Audi Showroom
Sheikh Zayed Road, Al Quoz
PO Box 126565, Dubai
Tel +971 4 515 7800
Fax +971 4 328 5494

**NBF Diamond Financing Office**
Almas Tower
Jumeirah Lake Towers
PO Box 340550, Dubai
Tel +971 4 507 8362
Fax +971 4 397 7515

### Sharjah

**Sharjah Branch**
Sparco Building, Sharjah College
Industrial Area
PO Box 1416, Sharjah
Tel +971 6 593 1111
Fax +971 6 525 5887

### Abu Dhabi

**Abu Dhabi Branch**
Al Ferdous Tower
Al Salam Street
PO Box 786, Abu Dhabi
Tel +971 2 612 5300/612 5400
Fax +971 2 672 8362/676 8503

**Mussafah Branch**
Rashid Al Mazroui Building
Bank Street, Mussafah Industrial Area
PO Box 786, Abu Dhabi
Tel +971 2 612 5700
Fax +971 2 555 1215

**NBF Corporate Banking Office**
Al Badie Building
Capital District
Near ADNEC Area
PO Box 786, Abu Dhabi
Tel +971 2 612 5320
Fax +971 2 445 9929

### Al Ain

**Al Ain Branch**
Sheikh Falah Bin Zayed
Al Nahyan Building
Near Clock Intersection
Opposite GPO, Main Road
PO Box 88108, Al Ain
Tel +971 3 764 8142
Fax +971 3 764 8156

## NBF Subsidiaries

### Dubai

**NBF Capital Ltd.**
(Regulated by the DFSA)
3rd Floor, Office No.303
Precinct Building 4, DIFC
PO Box 128217, Dubai
Tel +971 4 507 8517

### Fujairah

**NBF Financial Services FZC**
Fujairah Free Zone
PO Box 5230, Fujairah
Tel +971 9 202 9231
Fax +971 9 228 2979

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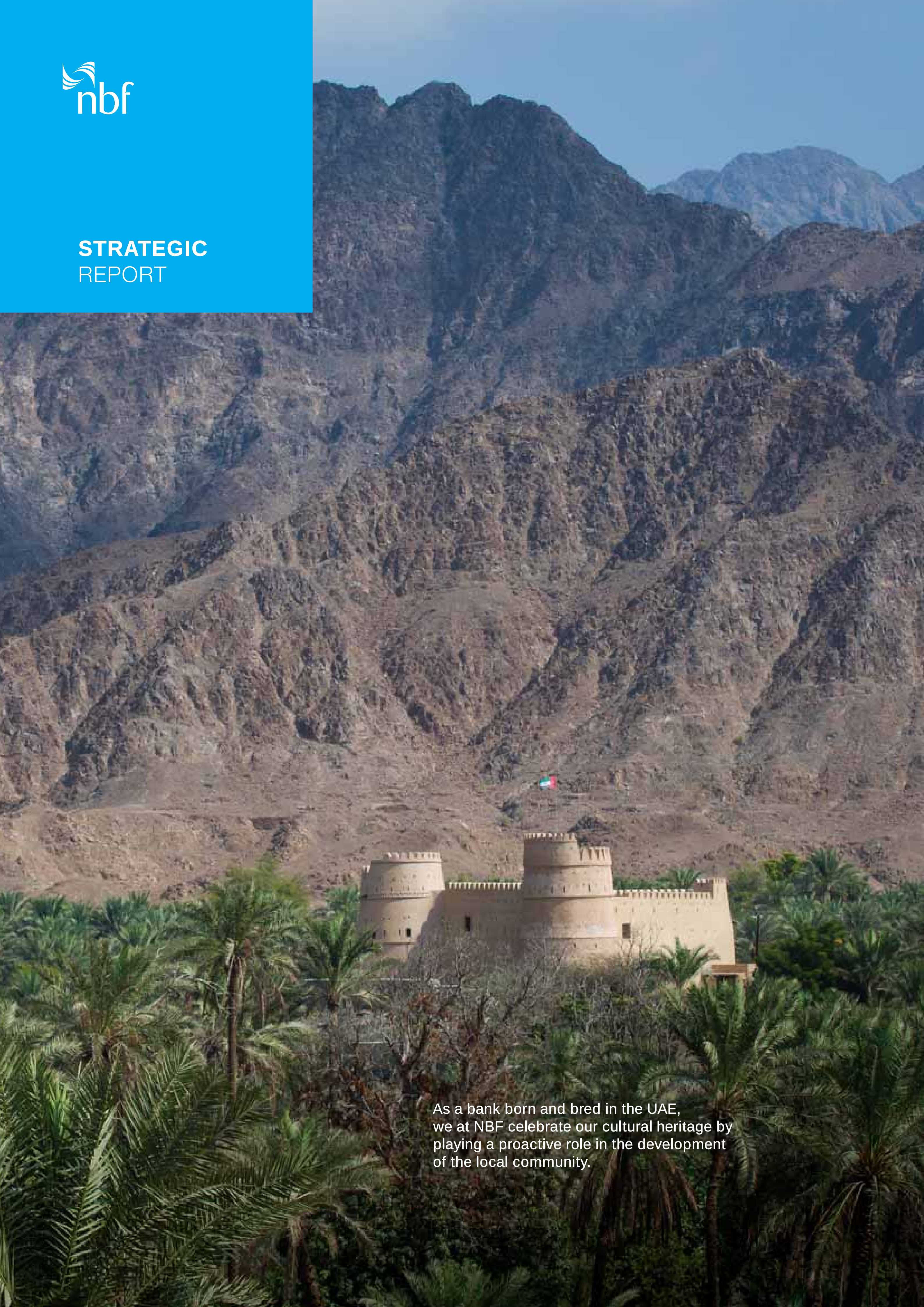
# **STRATEGIC** REPORT



As a bank born and bred in the UAE, we at NBF celebrate our cultural heritage by playing a proactive role in the development of the local community.

## NATIONAL BANK OF FUJAIRAH (NBF)
## WHO WE ARE

NBF is one of the fastest-growing financial institutions in the UAE with 34 years of exceptional customer service.

### Our Vision

We aspire to be the bank for business in the UAE and the pride of Fujairah.

### Our Mission

As a bank born and bred in the UAE, we celebrate our cultural heritage by playing a proactive role in the development of the local community.

With our solid track record, strong cultural heritage, deep market insight and unwavering focus on service and innovation, we believe in cultivating lasting relationships with our customers as we help them leverage growth opportunities in the ever-changing market place.

Similarly, we continuously strive towards the creation of a stimulating environment that allows people to pursue their own personal and professional development.

### Our Values

| | | |
|---|---|---|
| **P** | **Passion and Commitment** | Be ready to go the extra mile for the bank and for each other |
| **R** | **Respect** | Have mutual trust and understanding, appreciate and seek the views of others |
| **I** | **Integrity** | Be honest and transparent |
| **D** | **Dedication to team work** | Work toward shared, common goals. Build effective teams across organisational boundaries |
| **E** | **Excellence in service** | Make delivering an exceptional customer service the heart of everything we do |

## NBF AT A GLANCE

NBF is a full services corporate bank with strong corporate and commercial banking, treasury and trade finance expertise, as well as an expanding suite of personal banking options and Shari'a compliant services.

1982
Established

16
Branches

3
Subsidiaries

730
Employees

30,000
Customers

BBB+/A-
Rating

More than
5
Regulatory relationships

More than
35
Nationalities

| Operating income | Operating profit | Net profit |
|---|---|---|
| AED 1.3bn | AED 866.0m | AED 460.4m |
| (2015: AED 1.2bn) | (2015: AED 766.9m) | (2015: AED 558.8m) |

**Key Financial Performance Metrics**

10.4%
Return on average equity

1.4%
Return on average assets

15%
Dividend pay-out

## YEAR-ON-YEAR INDUSTRY ACCOLADES

### 2016

- **Best Corporate Bank UAE -** Banker Middle East UAE Industry Awards
- **Best Commercial Bank UAE -** Banker Middle East UAE Industry Awards
- **Bankers' Choice Award -** The Asian Banker, Middle East and Africa
- **Best New Islamic Window UAE -** Islamic Business and Finance Awards
- **Best Customer Service-Corporate and Investment Banking -** Banker Middle East UAE Product Awards
- **Best Corporate Advisory Service -** Banker Middle East UAE Product Awards
- **Best Cash Management -** Banker Middle East UAE Product Awards
- **Best Treasury Management -** Banker Middle East UAE Product Awards
- **Best Innovation in Employee Engagement -** HR Excellence Awards 2016
- **Mark of Excellence for Nationalisation Initiatives -** Middle East HR Excellence Awards
- **Best Employer Brand on LinkedIn -** LinkedIn MENA Talent Awards

### 2015

- **Best Corporate Bank UAE -** Banker Middle East UAE Industry Awards
- **Best Commercial Bank UAE -** Banker Middle East UAE Industry Awards
- **Best Customer Experience Team (NBF Capital) -** Gulf Customer Experience Awards
- **Best Local Bank UAE -** EMEA Finance Middle East Banking Awards
- **Best Corporate Advisory Service -** Banker Middle East UAE Product Awards
- **Best SME Customer Service -** Banker Middle East UAE Product Awards
- **Best SME Trade Finance Offering -** Banker Middle East UAE Product Awards
- **Best SME Internet Banking Service -** Banker Middle East UAE Product Awards
- **Best Treasury Management -** Banker Middle East UAE Product Awards
- **2015 CIO 100 Awards -** Computer News Middle East (CNME)
- **Upholding the Highest Standards of Transparency and Governance -** Hawkamah Institute of Corporate Governance

### 2014

- **Best Trade Finance Bank -** Trade and Export Excellence Awards
- **Best Domestic Commercial Bank -** Banker Middle East UAE Industry Awards
- **Best Treasury Management -** Banker Middle East UAE Product Awards
- **Best SME Trade Finance Offering -** Banker Middle East UAE Product Awards
- **Best Customer Service Corporate and Investment Banking -** Banker Middle East UAE Product Awards

### 2013

- **Best Domestic Commercial Bank -** Banker Middle East UAE Industry Awards
- **Best Treasury Management -** Banker Middle East UAE Product Awards
- **Best SME Trade Finance Offering -** Banker Middle East UAE Product Awards
- **Best Foreign Exchange Service -** Banker Middle East UAE Product Awards

### 2012

- **Best Commercial Bank -** Banker Middle East UAE Industry Awards
- **Best Trade Finance -** Banker Middle East UAE Product Awards
- **Best Treasury Management -** Banker Middle East UAE Product Awards

## CHAIRMAN'S STATEMENT

During this particularly unpredictable period, the bank has made great strides in growing its market recognition and protecting the long term interests of the shareholders. A persistent focus on quality operations and exceptional customer service have built a strong foundation for the future.

**"The Board is pleased with the resilient operating performance, robust liquidity, solid capital adequacy and healthy returns achieved this year. These all help to sustain the Group's competitive position in the face of a difficult credit environment. Our core business, balance sheet strength and agile operating platform secure the foundation for our future progress, and place NBF well to deal with the rapidly changing economic and regulatory environment. The Board is confident of the Group's opportunities as we move into 2017 with a clear strategy to reliably support businesses and corporations to achieve success by providing them with the very best in financial services, innovation and service delivery."**

2016 saw a number of developments that resulted in continued uncertainty in global and regional economic and financial markets; not least the on-going low level of commodity/oil prices and interest rates, the mixed outlook on global growth, the absence of credible improvements in the Eurozone, the planned exit of Britain from the European Union, the Republican's win in the US elections as well as rising geopolitical tensions. The budgetary deficits faced by the GCC countries caused governments to prioritise fiscal measures in the form of controlled spending, slowdown in new investment and projects and the introduction of new fees and taxes to generate additional sources of revenue. Similar trends are also observed in the private sector as weak revenue growth persisted in many industries. In addition, new regulatory and accounting changes are being introduced which put pressure on banking sector profitability in the short to medium term further reducing the capacity to support significant fiscal stimulus.

Against this backdrop, we remained close to our customers while managing risks and resources to deliver a net profit attributable to shareholders of AED 460.4 million and average return on equity of 10.4%. NBF was able to navigate the rapidly-changing market conditions with prudent liquidity management and by proactively absorbing an elevated level of provisions on the back of a very encouraging operating profit of AED 866.0 million. The current environment provides both an opportunity, and a need, for structural changes to the traditional banking models in the industry in order to respond to the new operating environment whilst continuing to produce attractive returns to our stakeholders. NBF is striving to adapt to these new challenges whilst maintaining its core customer proposition of being a dependable, transparent and consistent partner.

## AWARDS AND ACCOLADES

We were honoured with a number of prestigious awards and endorsements through-out 2016 *(covered on page 4)*, underscoring NBF's long outstanding culture of service excellence and client partnership. We are particularly proud that NBF bagged the "Best Corporate Bank Award" for the second year in a row and even more impressively, retained the "Best Commercial Bank" and "Best Treasury Management" title for five consecutive years at the Banker ME Awards. In addition, amongst a series of other accolades, the bank was awarded the winner of the "Bankers' Choice Awards 2016" by "The Asian Banker" and "Best New Islamic Window – UAE" at the Islamic Business & Finance Awards 2016.

Apart from the business awards, NBF was also recognised for its superior human resources management practices by a number of external players. NBF won the "Best Employer Brand on LinkedIn" by LinkedIn MENA and was the winner of the "Innovation in Employee Engagement" title, awarded at the annual HR Excellence Awards.

NBF staff form one of the most motivated and engaged groups of people in the local banking sector and across the region. In a research study conducted by the Korn Ferry Hay Group, the bank was ranked amongst the top banks in the region in terms of staff satisfaction and placed NBF in their Global High Performing Organisations (HPO) peer group.

The bank's sound fundamentals are further reaffirmed by its investment grade ratings of Baa1/Prime - 2 for deposits and A3 for counterparty risk assessment by Moody's, and BBB+/A-2 by Standard & Poor's, both with a stable outlook. Capital Intelligence also re-affirmed NBF's financial strength outlook as 'stable'. The bank's Long Term Foreign Currency Rating (FCR) has been maintained at 'A-' since 2008, reflecting its prudent and proactive risk management practices and sound business model.

These external recognitions are all testament of our commitment to deliver our Vision, Mission and Values.

## FINANCIAL PERFORMANCE

NBF posted an operating profit of AED 866.0 million (growth of 12.9%) compared to AED 766.9 million in 2015, demonstrating its continued focus on quality core business growth despite the lower level of general economic activity. Operating income growth of 8.7% was achieved by maintaining our focus on core businesses and broadening our services in order to offset the impact of the low interest rate environment.

The strong operating performance helped the Group respond well to the ongoing credit stress being experienced in the market; NBF's prudent loan loss provisioning policy resulted in net impairment losses of AED 405.5 million compared to AED 208.1 million in 2015. The bank's NPL ratio was 4.95% compared to 4.72% as at 31 December 2015 and total provision coverage ratio stood at 101.3%.

The Group recorded a net profit of AED 460.4 million compared to AED 558.8 million in 2015, depicting a decline of 17.6% after absorbing this exceptional level of provisions.

The cost-to-income ratio improved from 36.8% to 34.4% reflecting the Group's ongoing efforts to achieve operational efficiencies, creating capacity for investment to enhance our compliance systems and processes, and to provide a better experience for our clients. Return on average assets was 1.4% compared to 2.1% in 2015. Financial stability was underpinned by maintaining strong levels of capital adequacy and liquidity. Capital adequacy ratio stood at 17.6% with a tier 1 ratio of 15.2%. Pure advances to deposits ratio improved to 88.0% from 91.1% and eligible liquid assets ratio improved to 23.3% from 18.2%. Basel III LCR and NSFR stood at 182% and 103% respectively.

These measures, combined with our resolute focus on the core business, enhanced risk management, strong capital and liquidity positions and prudent provision coverage, ensure that NBF is in a good position to set itself apart from the competition pursuing long term sustainable growth without being overly distracted by near term economic cycles.

## SHAREHOLDERS' RETURNS

The Board recognises the importance of dividends to shareholders, and believes in balancing returns with investment in the brand to support future growth, while preserving strong capital ratios. Return on average equity stood at 10.4% compared to 14.6% in 2015. The book value per share stood at AED 2.82 (2015: AED 2.77) and earnings per share at AED 0.31 (2015: AED 0.40).

Taking into account the 2016 performance and the current market conditions, I, on behalf of the Board of Directors, am pleased to recommend a distribution of profits of 15.0% (2015: 15.0%) in the form of cash dividends of 7.5% (2015: 7.5%) and bonus shares of 7.5% (2015: 7.5%) of paid-up capital.

## PROGRESS ON STRATEGIC INITIATIVES

The Board is determined that the Group continues to adapt to the changing external environment and to realise fully the opportunities that are present in our markets. Enhancing the NBF brand, launching a new priority banking and investment propositions and digitising various offerings continue to be among the principal priorities for sustainable growth and healthy returns for shareholders.

NBF Islamic, the bank's recently formed full-fledged Shari'a banking proposition, recorded an operating income of AED 60.4 million and total assets worth AED 3.0 billion. During the year, the Group has extended its product suite to include Treasury offerings and Modaraba products are planned for launch in 2017 to offer a complete spectrum of Shari'a compliant products to its customers.

Social media presence is being strengthened to enhance the bank's visibility and improve customer reach. While we continue to manage our presence on LinkedIn, NBF also launched its Facebook page, which will be followed by a presence on Instagram in 2017.

NBF's 16th branch is now open for business in the Fujairah Free Zone and will play a significant role in supporting Fujairah's ongoing growth as a regional oil trading hub. In our constant endeavour to provide better customer service, we have also relocated our Deira branch to a new facility in Abu Hail.

Further, the bank secured a very good location for its long sought-after branch in the Al Ras area and the retail business will establish its first community-based branch in the Al Reef area in Abu Dhabi. These branches will commence operations in 2017.

Notwithstanding the challenging environment, we believe there will be good opportunities for the bank's focused approach that will bring future growth. We remain committed to achieving our ambition of delivering a sustainable return on average equity in the range of 10 to 15% per annum together with maintaining the highest level of compliance to all the existing and emerging statutory and regulatory requirements.

## STAKEHOLDER ENGAGEMENT AND CORPORATE GOVERNANCE

Stakeholder engagement and corporate governance continue to be of the utmost significance for NBF. The appointment of a new Board Member, namely Mr. Ahmed Saeed Al Raqbani, and amendment of the Memorandum and Articles of Association during the course of the year ensure that the bank is fully aligned with the latest laws and governance practices crucial for its ongoing success.

During the year, the Board engaged the services of Tripod Partners Management Consultants to further enhance its awareness of the latest world class corporate governance principles and various aspects of liquidity and market risk management. Such work enhances our internal processes and helps with our strategic planning priorities, further strengthening us as a bank allowing us to continue delivering the best-in-class solutions we are known for in the industry.

The bank has re-positioned its popular Corporate Days with the NBF Knowledge Series, a broader networking event seeking to apprise the bank's clients with the latest market developments. The 2016 Knowledge Series brought together 500 UAE business leaders and analysts to a series of one-day networking sessions in Fujairah, Abu Dhabi and Dubai to identify and discuss trends, opportunities and challenges affecting companies in the UAE. The event invited industry experts from PricewaterhouseCoopers (PwC) covering Value Added Tax (VAT) and New Company Law requirements, Forcepoint covering cyber security and fraud prevention, and the International Chamber of Commerce covering global trends in trade and its impact on corporates.

## ASSURING OUR ON-GOING COMMITMENT TOWARDS THE SUCCESS OF OUR COUNTRY AND ITS PEOPLE

With over three decades of operation in the UAE, we recognise the importance of our long-time customers, and further re-affirm our commitment to continue providing best-in-class service in support of their long-term goals. To be the bank for business in the UAE and the pride of Fujairah, NBF strives to develop services which are of direct relevance to its chosen segments and continues to enhance the value our customers gain from banking with us.

The UAE's economy is expected to maintain real GDP growth rates in the range of 2.8% to 3.3% for next 3 years up from 2.2% in 2016. The country benefits from diversified sources of growth and the substantial private and public sector investment plans in place. The UAE currently ranks 15th globally among top 20 competitive economies, first regionally and 28th globally in the World Happiness Report 2016, leads the GCC in smart building solutions and ranks first among the Arab World and 41st globally in the 2016 Global Innovation Index.

The bank's home emirate of Fujairah has experienced unprecedented investment and development, increased multi-national corporate presence with a major new highway, new hotels and beach resorts, entertainment and shopping complexes. 'Dubai to Fujairah in 10 minutes' through the Hyperloop solution was recently showcased as part of "Build Earth Live". This project aims to convert 25 per cent of the total commuting trips to autonomous mode (driverless) as one of the world's most important initiatives, turning Dubai into a global laboratory for next generation technologies in the field of transportation.

NBF has demonstrable financial strength, outstanding client relationships and a strong team of people focused on playing a significant role in the development of Fujairah and the UAE as a whole and playing its part in the growth of the UAE economy under the visionary and dynamic leadership of our President, His Highness Sheikh Khalifa Bin Zayed Al Nahyan, and our Vice President and Prime Minister of the UAE and Ruler of Dubai, His Highness Sheikh Mohammed Bin Rashid Al Maktoum.

I would like to extend my gratitude to His Highness Sheikh Hamad Bin Mohammed Al Sharqi, member of the Supreme Council and Ruler of Fujairah, for his unwavering support and for being an inspiration to the Group. I want to place on the record the Board's appreciation of that commitment and acknowledge the real achievements of the Group.

On behalf of the Board, I want to appreciate all the people within the bank for their ongoing hard work and commitment in taking the bank to greater heights year on year.

Finally, I would like to thank our customers and shareholders for their trust in us and support over the years, without whom the bank would not be where it is today.

**Saleh Bin Mohamed Bin Hamad Al Sharqi**
Chairman
25 January 2017

# DIRECTORS' REPORT AND SUSTAINABILITY REPORT

We continue to focus on true value creation, connecting customers to opportunities and ensuring the long-term sustainability of their business models.

## DEPUTY CHAIRMAN’S STATEMENT

NBF is in good shape to tap exciting opportunities and strengthen client relationships.

> **“Our 2016 results demonstrate NBF’s underlying strength and resilience to develop its core business through an unwavering customer focus. Our segmented approach and comprehensive set of products and service channels coupled with a long-term sustainable business model helped us achieve consistent business and revenue growth even in a subdued operating environment.”**

## FINANCIAL RESULTS

### The Group

**Equity**
AED 4.6bn
(2015: AED 4.3bn)

**Loans & advances**
AED 22.8bn
(2015: AED 19.7bn)

**Deposits**
AED 25.9bn
(2015: AED 21.6bn)

**Key financial performance metrics**

34.4%
Cost to income

17.6%
Capital adequacy

23.3%
Eligible liquid asset

## FINANCIAL PERFORMANCE

The Group posted an operating profit of AED 866.0 million (growth of 12.9%) compared to AED 766.9 million in 2015.

Operating income grew by 8.7% to AED 1,319.1 million, compared to AED 1,213.1 million in 2015, reflecting the Group's diversification strategy and growth in the underlying volume of core business. Net interest income grew by 5.9% to AED 848.2 million, compared to AED 801.3 million in 2015 due to robust asset and liability management after absorbing the impact of margin compression. Non-interest income rose to AED 470.9 million, 14.4% higher than the AED 411.8 million in 2015, primarily reflecting an increase in the bank's trade business and credit growth. Exchange income, including derivative income, saw a fine growth of 12.5% to AED 102.3 million. A gain in investment income of AED 11.1 million was recorded in 2016 compared to AED 2.7 million for the corresponding period in 2015.

Total operating expenses increased by a mere 1.5% reflecting tighter control on costs in view of the low growth environment and the negative pressure on margins and provisions. Total operating expenses amounted to AED 453.1 million. Cost-to-income ratio improved to 34.4% from 36.8% in the corresponding period of 2015 mainly due to higher growth in operating income and this disciplined cost control.

The strength of the underlying core businesses and operating performance enabled NBF to attain a prudent level of provisions in response to the credit stress and relative downturn in the market. Loan loss charges for the year stood at AED 405.5 million, up from AED 208.1 million in 2015. NBF's non-performing loans and advances (NPL) ratio was 4.95% compared to 4.72% in 2015. During the year, recoveries from NPLs *(including recovery from written-off cases)* stood at AED 87.8 million compared to AED 226.5 million in 2015, and write-offs amounted to AED 254.8 million compared to AED 78.7 million in the previous year. Total provision coverage was maintained at a healthy level of 101.3% compared to 107.7% over the same period in 2015.

The higher level of impairment charges and the resulting coverage ratios reflects the bank's prudent provisioning based on its Basel Internal Rating Based (IRB) approach and the UAE Central Bank regulations. The bank maintains total provisions based on a combination of through-the-life probability of default matrices, the regulatory requirements, and the developing accounting standards to ensure overall compliance and appropriate prudential coverage is achieved. Collective provisions are made in respect of the performing portfolio where impairment loss might occur but cannot yet be measured reliably. The credit stress and the current market conditions have crystalised many of these potential losses and part of the historic collective provision has become specifically allocated, whilst ensuring overall levels are managed to remain in compliance with the bank's medium term prudential model. Our prudent IRB approach followed in recent years also provided a strong foundation for the imminent IFRS 9 adoption and implementation.

The Group recorded a net profit of AED 460.4 million compared to AED 558.8 million in 2015, depicting a decline of 17.6% as a result of the elevated level of provisions. NBF's return on average equity was 10.4%, compared to 14.6% in 2015, and return on average assets was 1.4% compared to 2.1% in 2015.

The NBF Group remains highly disciplined in its focus on maintaining a strong balance sheet, which continues to be highly liquid, well diversified, and conservatively positioned. Growth in lending and deposits of 15.9% and 20.0% respectively in 2016 reflects the strength of the Group's customer relationship and its commitment to supporting the ongoing development of the UAE. The Group's growth is predicated on the availability of appropriate funding and despite tightening market conditions this has not proved a real constraint in 2016. Furthermore, total assets grew 18.8% to AED 35.7 billion during this period, up from AED 30.0 billion at the end of 2015.

The Group has always maintained strong capital adequacy and liquidity levels relative to its risk profile and growth strategy. Our focus on quality has contributed to the strength of our capital adequacy and liquidity and areas of relative concentration have all improved during this year as the Group's position becomes appreciated by more and more counterparties.

The Group's management takes into consideration the changing operating environment based on a real time and proactive assessment of the prevailing situation and the imminent changes expected in order to assess the appropriateness of its business strategy and risk management. Notwithstanding the trials ahead, we are confident that by maintaining an unwavering focus on risk management, financial prudence and sustainability, effective execution and transparency, the Group will continue to make worthy progress over the coming years.

## RISK MANAGEMENT

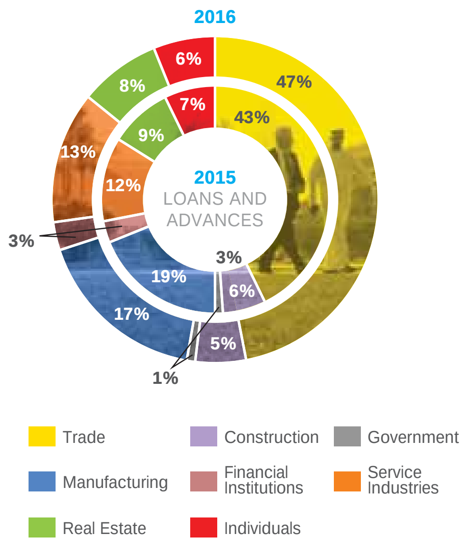
NBF has established a robust risk management and governance framework for effective enterprise-wide management of risks in line with the Board approved risk appetite to build a sustainable franchise in the interest of all our stakeholders.

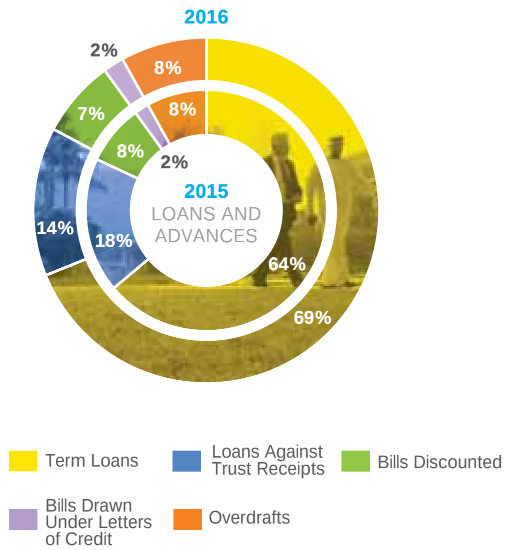
Effective risk management is fundamental to generate profits consistently and sustainably and is thus a central part of the financial and operational management of the Group. Risk policies and strategies adapt to the market conditions and operating environment dynamically to ensure that they remain within the Group's overall risk appetite and are balanced with returns.

The bank manages various risk elements in line with the Basel II methodologies including managing credit risk based on the Internal Rating Based (IRB) Approach. Further, the default predictive methodologies allow NBF to use risk management tools and best practices for assessing and managing its risks and capital adequacy effectively and efficiently.

NBF has consistently looked to expand its customer base and reduce any systemic credit concentrations that exist. Exposure to its top 20 customers (funded) stood at 29.5% in 2011 which reduced to 26.0% in 2016 and after taking into account cash collateral, top 20 customers' exposure concentration (funded) stood at 20.6% in 2016. During the year, lending mix (by pledged deposits) stood at 30.2% compared to 32.9% in 2015; and lending mix (by property mortgage) increased to 27.8% in 2016 compared to 22.1% in 2015, which reflects the bank's continued focus on enhancing risk quality and mitigants.

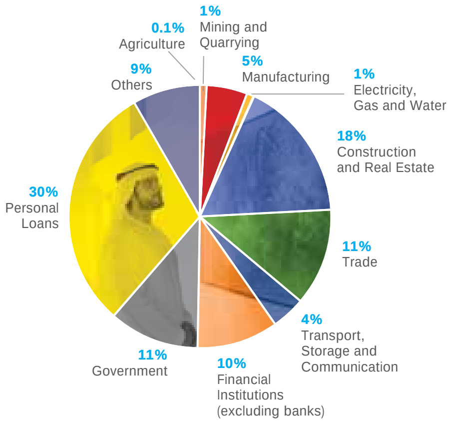
The bank also continuously monitors and manages its concentration risk from multiple perspectives through breadth of products, customer segments and sectors:



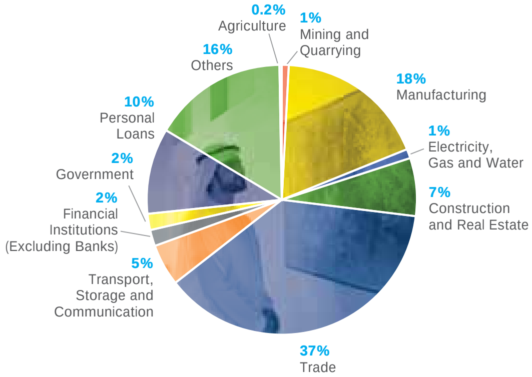



NBF's segmented focus compared to the industry continues to set it apart and reflects its prudent approach towards high risk sectors and focus on long term, sustainable results:

**INDUSTRY** (31 December 2016)




**NBF** (31 December 2016)




The current incurred loss approach is being adapted for compliance with the new accounting requirements set out by International Financial Reporting Standard (IFRS) 9 - 'Financial Instruments', with a mandatory effective date of 01 January 2018. The standard reflects the classification and measurement, impairment and hedge accounting phases of the IASB's project to replace IAS 39 - Financial Instruments: Recognition and Measurement. The standard includes the introduction of a forward-looking Expected Credit Loss (ECL) approach, replacing the incurred loss impairment approach for financial instruments in IAS 39, and the loss provisioning approach for financial guarantees and lending commitments in IAS 37, Provisions, contingent liabilities and contingent assets.

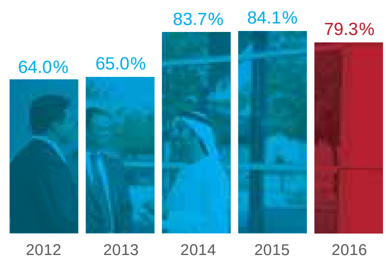
IFRS 9 is a key initiative for NBF and is currently being implemented under the joint sponsorship of the Chief Financial Officer (CFO) and Chief Risk Officer (CRO). The project structure has been defined to address the critical requirements of the standard and to manage the appropriate involvement of key stakeholders, including Finance, Risk, Credit, Information Systems and Technology and the business divisions. A Project Steering Committee and various work-streams have been created to ensure smooth implementation with appropriate controls and governance over all decisions. We have finalised key technical accounting, risk methodology decisions and a system for IFRS 9 ECL calculation and are currently focusing on model development, data and IT architecture, and consequential implementation work. We have planned to perform a parallel run in 2017 to achieve smooth transition and reflection of IFRS 9 requirements in the Group's risk and performance management.

NBF has significantly improved its liquidity risk profile in recent years and it continues to remain strong. Matching our lending with the growth in our deposits continues to be a principal focus, and the Group was able to achieve a growth in deposits in 2016 of AED 4.3 billion compared to lending growth of AED 3.1 billion. The Group is predominantly deposit funded and its deposits to total assets ratio was 72.7% compared to 72.0% in 2015. The bank's advances to deposits ratio improved to 87.8% from 2015 level of 91.1%. The bank's balance sheet is well-diversified and its eligible liquid assets ratio remains one of the highest at the industry level at 23.3% compared to 18.2% in 2015, while at the same time, the bank has improved the duration of its liabilities. The bank continues to monitor liquidity coverage ratio (LCR) and net stable funding ratio (NSFR) daily and qualitative aspects for the compliance of Basel III requirements are being progressively implemented. At 31 December 2016, the bank's NSFR and LCR stood at 103% and 182% respectively.

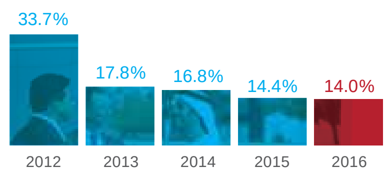
NBF maintains prudent market risk limits and its trades are executed predominantly to support customer activities. The Group improved its investments to 5.0% of assets from 4.7% in 2015 and is further widening its investment activities following the establishment of its new investment unit. Fixed income fund investment was undertaken with net asset value (NAV) of AED 200.1 million and equity fund investments undertaken with NAV of AED 16.8 million. Funds/equities residual value is AED 13.2 million which includes NBF Capital Limited investment of AED 5.0 million. NBF's debt investment portfolio is held with the principal objective of liquidity management in mind and comprises with 84.8% of the debt securities portfolio rated "BBB+" and above, compared to 80.8% in 2015. NBF's equity investment portfolio is being developed as part of its revenue and risk diversification strategy. Investment income of AED 11.1 million included realised income from equity investments of AED 3.6 million.

During the year, the bank has progressed well on the implementation of a treasury front end system which is targeted to go live in Q1 2017. Asset and liability management module of the new system is already operational and went live in 2016. The bank monitors its foreign exchange and derivative products based on credit equivalent exposure (CEE) which is supported by the new system. Central Bank's draft Basel III guidelines for capital requirements increase minimum capital requirements. This increase includes countercyclical and capital conservation buffers of 2.5% each and the emphasis is on Tier 1 and common equity capital and Tier 2 capital will no longer be considered for regulatory purposes. NBF is well poised to remain compliant with the increased requirements on the back of its strong current capital ratios and prudent dividend policy.

**Profit Retention Ratio**




**Tier 2 Capital/Capital Base**




NBF has always been committed to the highest compliance and anti-money laundering standards and the protection of the UAE financial system. The Group has decided to segregate the compliance function from operational risk management for enhancing the dedicated focus in view of growing demands and increasing regulations. Our anti-money laundering policies, procedures and systems are in line with the latest recommendations from the Financial Action Task Force (FATF), the international anti-money laundering regulatory body, UAE Federal Laws and guidelines from Central Bank of the UAE. The bank has also done the needful with regard to the requirements of National Electronic Security Agency (NESA).

NBF continues to complement its compliance efforts with annual learning programs to help staff to stay abreast of current developments and better fulfil their responsibilities.

## SEGMENT PERFORMANCE

NBF is widely recognised for its exceptional relationship management and delivery of the highest quality service to the customers and industry alike, as evidenced from the customer satisfaction survey recently concluded and a number of consistent awards won year on year. We aim to continue concentrating more on our client relationships by delivering excellent service to them, offering customised products and solutions proactively anticipating their needs. To this end, a dedicated product and channels team continues to work hand-in-hand with the individual business segments to enhance customer experience.

## CORPORATE AND INSTITUTIONAL BANKING

The operating income from corporate and institutional banking customers for the year was AED 1,071.9 million (2015: AED 1,017.6 million). This includes income from foreign exchange and derivatives AED 88.6 million (2015: AED 79.0 million) and advisory services AED 6.4 million (2015: AED 23.0 million) provided to these customers, which are reported under Treasury, ALM and Others segment.

### Corporate and Institutional (C&IB) Segments

NBF is highly regarded in the UAE as a trusted banking partner, and it received further acclaim by being awarded the winner of the "Bankers' Choice Awards 2016" by "The Asian Banker" and "The Best Corporate Bank UAE" at the Banker ME industry awards 2016. NBF's corporate and institutional banking segments represent 54.7% of the Group's operating income, compared to 53.6% in 2015. The segment's operating income stood at AED 721.3 million compared to AED 650.4 million in 2015. Additionally, assets reached AED 20.9 billion, rising 22.0% from AED 17.2 billion in 2015, while liabilities increased by 24.7% to AED 24.0 billion compared to AED 19.2 billion in 2015. The growth in these segments reflects the Group's strategy of reliably supporting its quality customers and at the same time diversifying its sources of business. A number of initiatives were undertaken which contributed to good results during this year:

- Global Transaction Services established in 2016, contributed to the growth in current and saving account (CASA) balances to 30.3% of total deposits.
- C&IB segments contributed to NBF Islamic with AED 33.5 million in operating income, AED 2.8 billion in deposits and AED 1.5 billion in financing.

- The bank continues to do well in the precious metals and jewellery sector by expanding its expertise in the diamond space. During the year, customers in this segment contributed AED 91.3 million in operating income depicting a growth of 35.5%, AED 2.5 billion in assets and AED 0.9 billion in deposits.

The segment's net profit, however, decreased by 21.4% to AED 230.2 million from AED 292.9 million in 2015 after absorbing the increase in loan losses of 97.6%.

### Business Banking Segment

NBF continues to raise its profile as a bank for business in the UAE, once again winning "Best Commercial Bank UAE" at the Banker Middle East Awards, further re-affirming the strong client focus and business partnerships the bank has cultivated over the years. NBF's business banking segment is closely aligned with a significant part of the UAE's economy. Whilst the bank remains committed to supporting this segment of the UAE economy, it has enhanced controls and underwriting standards to better protect it from the weakness currently seen in the market.

The segment has prudently provided for the impacted portfolio from the credit downturn resulting in credit losses increase by 90.8% to AED 106.0 million in 2016 from AED 55.5 million in 2015. Consequently, its net profit saw a decline of 72.7% to AED 23.1 million. The bank continues to follow a proactive and transparent approach in recognising and managing problem accounts, whilst it continues to support credit worthy customers. NBF's business banking segment represents 19.4% of the Group's operating income, down from 21.9% in 2015. Operating income decline of 3.6% to AED 255.7 million was recorded. The segment's assets totaled AED 2.94 billion in 2016 rising 0.2% from 2015. The segment's liabilities rose to AED 2.9 billion up 9.1% from AED 2.7 billion in 2015, a reflection of the enhanced focus on cash management and improvement in the cross-selling of products. The segment has cash collaterals/pledged deposits amounting to AED 784.6 million, which represents 27.5% of its credit portfolio.

## RETAIL BANKING

The Group's continued focus in the measured expansion of its retail business across the UAE has allowed the segment to achieve double digit operating growth, reflecting the ongoing success of NBF's diversified business strategy. Shari'a compliant retail banking products and services have also helped to grow the Group's customer base.

The segment's assets grew by 4.3% to AED 1.9 billion and liabilities went up by 17.0% to AED 2.1 billion in 2016. Operating income grew by 12.7% to AED 100.7 million. An enhanced sales focus aimed at building a stronger business has helped improve service and coverage, whilst managing the impact of the interest spread in a low interest rate environment. The segment's costs increased by 2.3% to AED 72.0 million, reflecting an enhanced focus on automation, a fine tuning of its operating model and improvements in allocation of costs around NBF's branch network to its broader segments. The segment reported a net loss of AED 5.0 million compared to a profit of AED 0.9 million in 2015, on account of a substantial increase in impairment losses, predominantly in the retail SME portfolio. The tighter credit standards now prevailing in this small business portfolio and the rebalanced focus on the priority personal banking segment will start showing an improvement in operating growth and net results in the months ahead.

## TREASURY, INVESTMENTS AND ASSET, LIABILITY MANAGEMENT (ALM) AND OTHERS

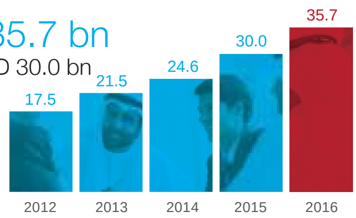
Our award-winning treasury business continues to be highly regarded in the market and offers a wide range of products to customers across diverse segments. Treasury has had another successful year, ranked "Best Treasury Management" at the Banker Middle East UAE Product Awards 2016. We have seen a robust growth in foreign exchange and derivatives income of 12.5% to AED 102.3 million, compared to AED 91.0 million in 2015. Sophisticated derivative transactions undertaken by the bank also highlighted the technical competence of NBF's treasury and its ability to offer a wide range of products in the market to help customers manage their financial risks. A new treasury front end system is due to go live in early 2017, broadening the spectrum of products offered, allowing greater efficiency and control to the business teams.

NBF's enhanced focus on asset and liability management during the year also resulted in strong net interest and net income from Islamic financing and investment activities growth of 5.9%. The combined share of the bank's income from Treasury and ALM improved to 18.3% from 17.2% in 2015. The investments portfolio, principally representing investment grade debt securities, increased by 26.9% to AED 1.8 billion.

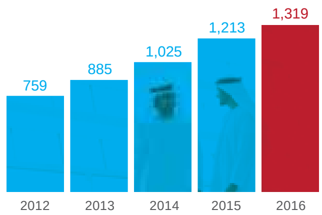
## NBF'S FIVE-YEAR PERFORMANCE SCORECARD

### **Assets** (AED Billion)

AED 35.7 bn
2015: AED 30.0 bn



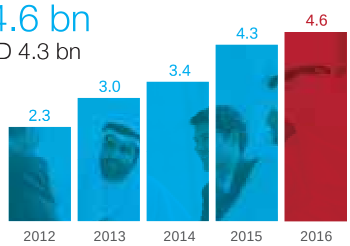

### **Operating Income** (AED Million)



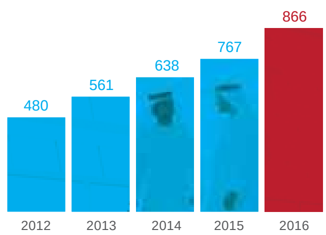

Operating income exceeded AED 1.3 billion – an all-time high in NBF's 34-year operating history.

### **Shareholders' Equity** (AED Billion)

AED 4.6 bn
2015: AED 4.3 bn



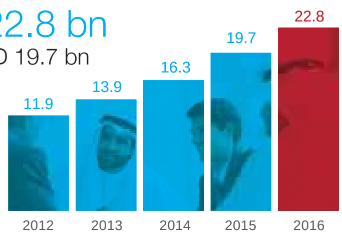

### **Operating Profit** (AED Million)



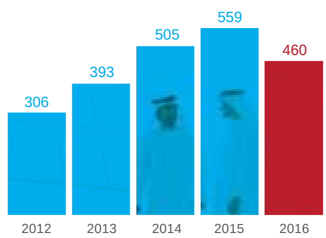

NBF's operating profit saw an impressive double digit growth on the back of business performance and improved efficiencies.

### **Loans and Advances** (AED Billion)

AED 22.8 bn
2015: AED 19.7 bn



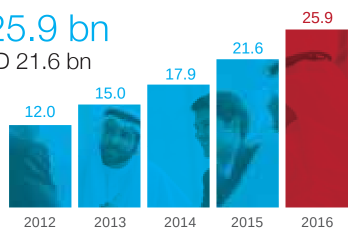

### **Net Profit** (AED Million)



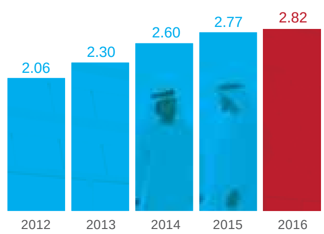

NBF's net profit has seen year-on-year double digit growth rate since 2011. ROAE of 10.4% achieved in 2016.

### **Customer Deposits** (AED Billion)

AED 25.9 bn
2015: AED 21.6 bn




### **Book Value Per Share** (AED)




Book value per share improved to AED 2.82.

## NBF ISLAMIC

The Global Islamic Economy Indicator (GIEI) ranks UAE at the second place in the overall GIEI rankings, second place in the Islamic Finance Indicator and first place in all other indicators (Halal Food, Modest Fashion, Halal Travel, Halal Media and Recreation and pharmaceuticals/ cosmetics). Indeed, relative to its size, the UAE has established a very healthy ecosystem for Islamic Economy Companies. The strong government led Islamic Economy Development initiatives has given the UAE a strong platform for the development of all Islamic Economy sectors.

The Central Bank of UAE announced setting up a Central Shari'a Board in early 2016 to provide unified supervision and guidance to financial institutions on Islamic Finance which will enhance transparency and harmonisation.

NBF Islamic has capitalised well on the positive developments in the Islamic financing space. NBF Islamic has outperformed new entrants in the industry and won the award for "Best New Islamic Window UAE" at the Islamic Business & Finance Awards 2016 in just two years of operation.

This accolade positions NBF Islamic as one of the leading providers of comprehensive suite of Shari'a compliant banking solutions.

During this year, NBF Islamic has grown at a phenomenal pace and in a short span of time has achieved an asset base of AED 3.0 billion up 128.2% from AED 1.31 billion in 2015, and operating income of AED 60.4 million up 176.0% from AED 22.0 million in 2015. Total Islamic financing receivables and Islamic customer deposits reached AED 1.63 billion (2015: AED 587.58 million) and AED 2.93 billion (2015: AED 1.12 billion) respectively. Overall NBF Islamic is 8.4% of total asset base.

NBF Islamic is offering a good mix of retail and corporate banking products complying with Shari'a rules based on structures including Murabaha, Wakala, Qard, Tawarruq, Ijara, Istisna' Forward Ijara and Waad. These Shari'a based product structures cater to various business offerings in retail, corporate and treasury making us one of the unique Islamic Banking platforms which offers such diverse range of products and structures.

The quality of NBF Islamic offerings and its operations from Shari'a compliance perspective is re-affirmed by the Shari'a Audit Report 2016 below:

In the name of Allah, The Most Merciful, The All Beneficent

**NBF Islamic, the Islamic Banking Window of National Bank of Fujairah PJSC (the bank)**

## SHARI'A SUPERVISORY BOARD REPORT FOR THE YEAR ENDED 31 DECEMBER 2016

The Shari'a Supervisory Board has approved and supervised contracts and transactions, in accordance with the principles of Shari'a, entered into by the bank for the year ended 31 December 2016. The Shari'a Supervisory Board has performed its supervision to enable it to express an opinion on the bank's compliance with the provisions and principles of Islamic Shari'a, as well as with fatwas, resolutions and specific guidelines that were issued by it from time to time.

The management of the bank is responsible for compliance with laws and principles of Shari'a in all Islamic banking transactions. The Shari'a Supervisory Board responsibility is limited to expressing an independent opinion based on its monitoring of the bank's operations.

The Shari'a Supervisory Board's annual audit and monitoring included inspecting documentation and procedures of the Islamic Banking undertaken by the bank on the basis of sample testing of all types of transactions.

The Shari'a Supervisory Board planned and executed its audit and monitoring to obtain all information and explanations deemed necessary to review sufficient evidence that Islamic Banking did not contravene the principles of Shari'a.

Based on its monitoring and supervision, the Shari'a Supervisory Board states the following:

a. Contracts and transactions entered into and processes followed by the bank during the year ended 31 December 2016, were conducted in accordance with the principles of Shari'a.

b. All amounts required to be channeled to charity were duly donated to charity organisations approved by the Shari'a Supervisory Board.

Allah Almighty knows best.
Approved By: **National Bank of Fujairah Shari'a Supervisory Board**

Dr. Mohamed Ali Elgari (Chairman) ........................................

Dr. Mohd Daud Bakar (Executive Member) ........................................

Dr. Muhammad Amin Ali Qattan (Member) ........................................

Dr. Osama Al-Dereai (Member) ........................................

## NBF AND THE COMMUNITY

### Dedicated to Sustainability

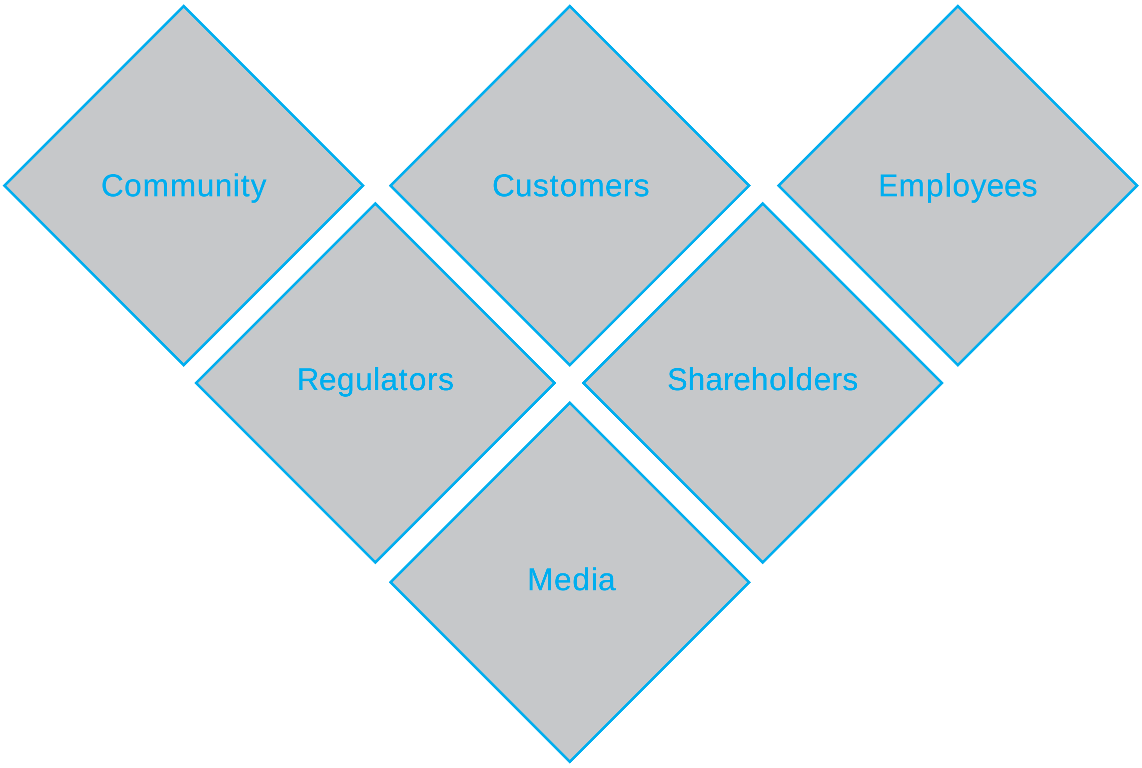
Sustainability requires us to focus on optimising our performance to generate long-term, sustainable and measurable benefits for our customers, shareholders, investors, employees and communities. It also requires us to promote the common good by being proactive, purposeful and accountable. We value giving back to the larger ecosystem that we live in and making it sustainable for inclusive growth as an integral part of our strategy and business goals.

NBF's resilient financial performance has been underpinned by its strong focus and commitment to sustainability. We dare to be different and ensure we are good at it. Our concept of stewardship incorporates more than just our customers' assets and profit, it means taking care of what we leave behind for future generations. This is not measured by financial performance alone, but also by performance relating to the environment, good governance, social impact and other key components of resilience.

To this end, we target to create a sound sustainability approach linking it to our core principles and values; contributing to the wider goal of developing societies.

We recognise our responsibility towards our local communities. We know that our long-term success depends on the health and prosperity of the communities in which we operate. Therefore, our methodology ensures that we consider the prospects of our key stakeholders:

### Our Engagement and Communication Approach



| | |
|---|---|
| **Community** | • Social engagement<br>• Community building initiatives<br>• Training and development<br>• Sponsorships |
| **Customers** | • Knowledge and best practice sharing<br>• Client engagements<br>• Satisfaction surveys<br>• Social, print and digital media |
| **Employees** | • Internal communication channels<br>• Off-sites/town-halls<br>• Training and development, 360 degree feedback, employee satisfaction survey, flexible benefits/reward statements, sports activities<br>• Employee engagement and culture building initiatives |
| **Regulators** | • Regular reporting<br>• Enhanced engagement/pro-active updates<br>• Participation at various committees and feedback process<br>• Highest standards of compliance |
| **Shareholders** | • Annual report covering corporate governance and sustainability reports<br>• Quarterly reports<br>• Presentations and press releases<br>• Pro-active updates, regular engagement, periodic meetings<br>• Investment grade credit ratings<br>• Shareholder meetings/general assembly meetings |
| **Media** | • Advertisements<br>• Editorials<br>• Interviews/features<br>• Press releases |

## Value Generated for Stakeholders

We summarise the key features of the business and the value generated for our stakeholders below:

| CUSTOMERS | | |
|---|---|---|
| **BUSINESS MIX** | | |
| | **Assets** | **Income** |
| Corporate Banking | 58.7% | 54.7% |
| Business Banking | 8.3% | 19.4% |
| Retail Banking | 5.2% | 7.6% |
| Treasury and ALM | 27.8% | 18.3% |
| **Total** | **100.0%** | **100.0%** |

| SERVICE CHANNELS | | |
|---|---|---|
| 16 Branches | 40 ATMs Network | Online and mobile banking |
| Relationship Managers/Sales Team | 3 subsidiaries | Call Centre |

| PRODUCTS AND INCOME | | | |
|---|---|---|---|
| Loans/credit/Islamic financing | Deposits/Islamic deposits | Investments/Islamic investment products | Other financial services |

| | |
|---|---|
| Net interest income and net income from Islamic financing and investment activities | 64.3% of operating income |
| Non-interest income | 35.7% of operating income |
| **COSTS** | |
| Employee expenses | 23.5% of operating income |
| Depreciation and amortisation | 1.7% of operating income |
| Other administration expenses | 9.2% of operating income |
| **RISK CHARGE** | |
| Net impairment losses | 30.7% of operating income |
| **NET RETURNS** | |
| Net profit | 34.9% of operating income |
| Return on average equity | 10.4% |
| Dividends (cash and bonus shares) | 41.4% of net profit |

## Customer Focus

At NBF, we believe in enabling success, enriching lives and empowering people. NBF is known for delivering tailored solutions to its customers and helping them achieve their business goals faster and safer.

### Ratings and Recognition

Our performance and success in the area of sustainability is reflected in important external ratings, rankings and recognitions. We value a strong sense of professionalism in business and third party endorsements matter. To us, this takes the form of our good credit ratings by Moody's, Standard and Poor and Capital Intelligence, all maintaining our investment grade credit ratings with stable outlook.

The bank's customer-centric philosophy and commitment to exceptional service was well recognised in 2016; covered in the awards and accolades section *(page 4)* of the Strategic Report 2016.

NBF's customer satisfaction survey, conducted with the help of an independent research consultancy, continues to reaffirm the bank's strong focus on customer needs and building long lasting relationship with customers. In 2016, the results continue to be robust and consistent. NBF performed more favourably than peer banks in terms of Internet Banking, Mobile Banking, Credit Facilities, Payment Solutions, Staff and Relationship Management, Coverage and General Banking Aspects, and ATM Experience. The recent survey also highlighted some opportunities which the bank can further capitalise on.

As a reflection of our on-going commitment to customer service and thought leadership that constantly looks to educate and provide access to knowledge that delivers long term value to clients, NBF GenNext leadership programme was hosted helping clients develop new leadership pipeline for their businesses. Developed in conjunction with Fitch Learning, the programme gave participants the opportunity to network with NBF's management, who shared their insights on successful business planning.

NBF reports a stable scoring index on customer retention and scored higher than the traditional peer group. The bank's ability to support banking relationships with top-notch service delivery and use of technology driven solutions is well regarded. Customers score us 'Very Good' in terms of executional capabilities across multiple banking areas, while our relationship managers are known for their responsiveness and expertise consistently scoring above their peers. Customer opinion counts, insights into their requirements are valued and every customer is dealt with a personal response. Proactively reaching out to them has helped build meaningful relationships, creating a positive impact mutually.

## People Focus

NBF believes in providing initiatives to empower, educate and nurture organisation talent to create future business leaders. In light of this, we endeavour to attract, enable, develop and engage the best people with the right skills, a responsible mindset and diverse backgrounds. We invest in our employees and seek to ensure that we have effective leadership and human resource practices in place, as well as the structures, technology and training necessary for our employees to deliver on our strategy and meet our customers' needs. These elements help create sustainable value for all of our stakeholders.

### Training and Raising Awareness

In a research study released by Hay Group in January 2016, NBF was ranked amongst the top banks in the region in terms of staff satisfaction. This was achieved by actively engaging and enabling the bank's employees through a combination of wellness, social and talent development initiatives.

Awareness and expertise play an important role in implementing our goals. We continue to work hard to further strengthen our corporate culture, as we are convinced that the right strategy and a strong, cohesive culture drives excellent performance. Hiring and training a pipeline of young talent is a priority for us. NBF's staff are one of the most motivated and engaged group of people in the local banking sector and across the region, a fact borne out by the bank's fifth annual employee satisfaction survey conducted by Hay. The survey results this year have improved over the previous year, underscoring NBF's exceptional transparent and open culture and the value the bank places on talent development and in providing a stimulating work environment.

NBF's commitment to Emiratisation is commendable. NBF won the "Best Employer Brand on LinkedIn" award which has helped position NBF as an Employer of Choice and NBF's LinkedIn community ranks highest in the Talent Brand Index with 32% surpassing bigger peers. We have been the only bank to win this award, is a strong reflection of our high engagement levels with existing and potential employees. NBF won the "Best HR Team" at the MENA HR Excellence Awards 2016 and were also recognised for "Mark of Excellence" for Nationalisation initiatives at the Middle East HR Excellence Awards 2015.

Our Emiratisation ratio stood at 41.7% compared to 42.4% in 2015. NBF continues to progressively build on its human resources practices, from training and development, employee well-being initiatives, performance and reward management to the development of an open and transparent organisational culture, all of which will ensure that NBF has in place a winning team for its ongoing success. We are known for the result oriented team we are and enable success through unconditional support provided mutually.

## Corporate Social Responsibility (CSR)

NBF has been a firm believer of giving back to the community. As a responsible corporate citizen, NBF is committed to engaging with and helping the community, protecting the environment and developing local talent. Since the formation of its corporate social responsibility (CSR) committee half a decade ago, the Group has adopted a comprehensive approach towards championing environmentally-friendly business practices and community engagement efforts. Our social engagement with the community and various initiatives are proof of this.

Recently, NBF participated in the CBUAE/United Nations (UN) CSR workshop for all UAE financial institutions. It was aimed at UN developing a common set of principles/timeline whereby all UAE financial institutions can gradually improve internal CSR practices to reflect an industry commitment in this regard. The CBUAE/UN issued the "Dubai Declaration of financial institutions in the United Arab Emirates on sustainable finance" on behalf of all financial institutions at the upcoming UN Global Roundtable. The declaration outlines a general broad based strategy for industry to adopt over a five year horizon which will lead to improved CSR practices by 2021.

In this connection, the Group would further develop the CSR roadmap to cover the various elements of the declaration recognising the UAE Vision 2021 and supporting the UAE's ambition to become one of the best countries in the world by the time of its Golden Jubilee anniversary. To attain a prosperous society for generations to come, we would also support the sustainable development of this country in line with the UAE Green Agenda 2015-2030.

Noteworthy CSR initiatives over the course of 2016 included:

- Partnering with Angel Appeal in providing relief to seafarers off the coast of Fujairah
- Supporting Emirates Wildlife Society (EWS-WWF) for conserving the Wadi Wurayah National Park in Fujairah
- A Ramadan Charity Drive in association with Fujairah Welfare Association
- Sponsorship of Municipality's UAE National Day celebrations
- Sponsorship of Fujairah Chamber of Commerce & Industry Conferences
- Sponsorship of Breast Cancer Symposium by Ministry of Health & Prevention
- Sponsorship of Zero Nine Exhibition
- Sponsorship of "We are Reading" campaign by General Directorate & Foreign Affairs
- Silver Sponsorship of Sheikh Zayed Tennis Open Championship
- Recycling Drive across NBF Branches

## Looking Ahead

Current market conditions and the rapidly changing operating environment are inevitably concentrating attention on the risks that exist within the global, regional and local economies. NBF's management takes into consideration the challenging operating environment based on a proactive assessment of the situation and addressing effectively by reflecting in its business and risk strategies.

We wish to pursue our growth strategy selectively in the current environment while protecting the Group's core base and developing the foundation for future growth. The Group will proactively balance its pace of growth and remain vigilant of the risks emanating from the current market. It will also continue to invest in longer term priorities:

- Expanding franchise value of NBF and broadening the customer base. Priority banking has been recently launched. Global transaction services and cash management focus will be further augmented.
- Continuing our efforts at achieving industry-beating customer service standards and developing a market reputation for service excellence. Leverage NBF Islamic success by enhanced commercialisation efforts to capture 1% - 2% of the Islamic Banking Market Share by 2018.
- Investment product proposition enhancement for a remarkable customer experience together with investment portfolio built up in fixed income and equity funds on the proprietary front.
- Digital transformation (incorporating Business Process Management) will be progressively achieved. Two pronged strategy adopted, firstly business processes are being re-engineered and progressively digitalised and secondly 'Big data' analysis and advanced customer centric analyses capability being enhanced for differentiated customer service.
- Continuing investment in strengthening risk management and compliance through automation and re-engineering of business processes.
- Proactively adapt to the Regulatory changes such as adoption of Basel III liquidity and capital requirements, IFRS 9, Value Added Tax (VAT) implementation and any other requirement that may become applicable.
- Optimising the deployment of capital and investment spend to deliver profitable growth and further accumulate capital. A shaper focus on economic profit and capital allocation to be undertaken.

While we look ahead, we will continue to focus on our customers, be efficient in our operations, and combine our resources to bring out the best and positvely contribute to the UAE market.

Finally, I would like to thank our customers, all NBF staff and our shareholders for their support in making the NBF franchise a success story.

**Easa Saleh Al Gurg, KCVO, CBE**
Deputy Chairman
25 January 2017

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# CORPORATE GOVERNANCE REPORT

Stakeholder engagement and investor relations continue to be of the utmost priority for NBF.

The NBF Board and management are committed to upholding the highest ethical and corporate governance standards in line with the industry best practices. This approach underpins a sustainable business and maintaining a high level of trust and integrity among various stakeholders of the bank.

The Board of Directors' primary responsibility is to provide effective governance over the bank's affairs for the benefit of its shareholders, and to balance the interests of its diverse stakeholders, including its investors, customers, employees, suppliers, regulators, government and the local communities. The bank's corporate governance structure includes well documented and regularly reviewed governance policies and procedures. The governance structure not only ensures high levels of transparency and accountability, but also provides an appropriate functional independence and control environment to carry out the business activities.

NBF is a regional financial services provider with a diverse range of activities. The bank's shares are listed on the Abu Dhabi Securities Exchange (ADX). NBF is regulated by the UAE Central Bank, the United Arab Emirates (UAE) banking regulator. The UAE Central Bank provides a range of governance and risk management requirements that are adhered to by the bank. NBF subsidiaries [namely NBF Financial Services FZC, NBF Capital Limited and NBF Trade Services (HKG) Limited] are supervised by regulators in the jurisdiction in which they operate, with oversight by the NBF Group.

The Board plays a key role in the approval and oversight of the organisation's strategy, principal policies, risk appetites, senior appointments and supervision and remuneration of senior executives. The bank has clearly defined in its Corporate Governance Framework Manual the responsibilities of the Board of Directors, its corporate governance structure and delegated authorities so as to enable the effective and efficient fulfillment of its responsibilities. In all actions taken by the Board, the Directors ensure compliance with relevant laws, regulations, rules and best banking practices as well as exercise their business judgement in what they reasonably believe to be in the best interests of the bank.

The Board and the bank's management continue to pro-actively review, develop and enhance the corporate governance standards in light of the changes in the bank's strategy and its business, external environment and best practices followed in the market.

The bank's formal disclosure policy is well established and certain disclosures are included within the Annual Consolidated Financial Statements as notes and can be referred to for further information on the bank's governance and risk management framework as follows:

- Note 2: Details of the bank's compliance with all applicable laws and regulations.
- Note 4: Sets out the accounting policies followed.
- Note 5: Explains financial risk management practices.

The corporate and governance documents accessible through the bank's website are:

- The memorandum of association and articles of association.
- The corporate governance framework of the Board of Directors.
- The code of conduct and whistle blowing policy that encourages open communication, compliance, transparency and fair business practices.
- The Shari'a Governance Framework (SGF).

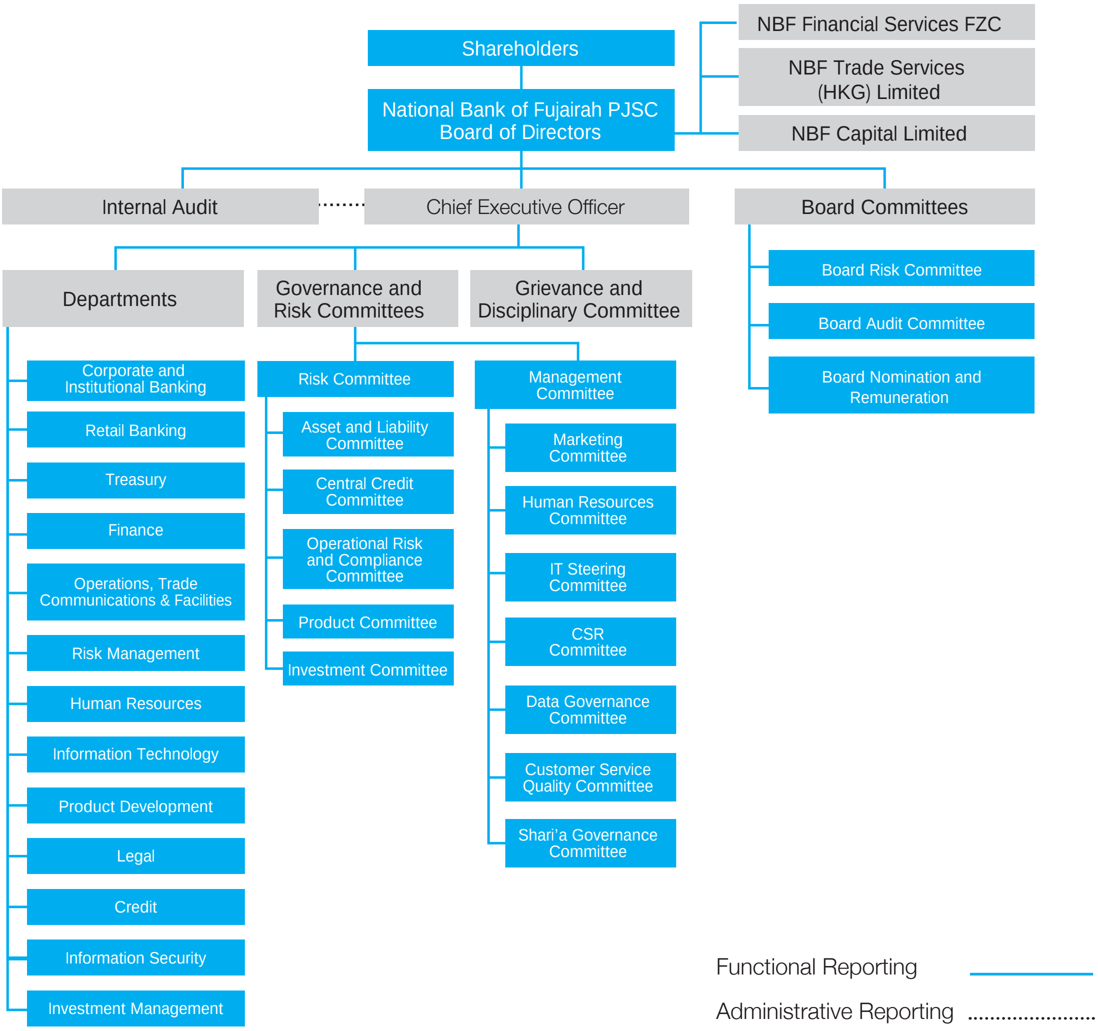
During the year, the bank has further upgraded its website and enhanced its investors and governance disclosures through its investor relations and corporate governance web page. As part of its aspiration and on-going efforts to be recognised as one of the institutions that maintains high standards of corporate governance, the bank continues to periodically and in a timely manner communicate financial and non-financial information to its various stakeholders - shareholders, investors, customers, employees, suppliers, regulators, government and the local communities through disclosures on its website (corporate governance/investor relations pages), annual and quarterly financial reports, investor presentations and various press releases.

The bank also strives to continue to keep its staff aware of all new developments including the bank's vision and mission, strategy and all new initiatives and other relevant information through various internal communication channels, staff off-sites and town hall meetings.

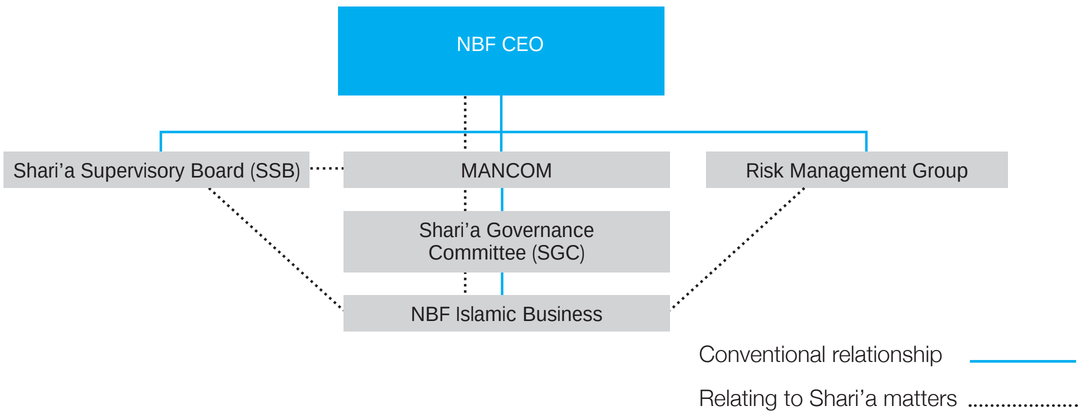
During 2016, in order to ensure compliance with Shari'a of Islamic Products offered through its Islamic window, NBF Islamic, the bank has adopted a Shari'a Governance Framework (SGF) finalised by the Management Committee (MANCOM) duly approved by the Shari'a Supervisory Board (SSB).

## ORGANISATION

The diagram below illustrates the high level organisation chart of the bank. Management Committee and Risk Committee oversee and provide strategic direction to other committees. They also make recommendations to the Board and Board Committees.




## NBF ISLAMIC – SHARI'A GOVERNANCE STRUCTURE



## SHAREHOLDERS

As at 31 December 2016, NBF's shareholders consist of:

| | |
|---|---|
| Department of Industry and Economy - Government of Fujairah | 40.15% |
| Easa Saleh Al Gurg LLC | 21.66% |
| Investment Corporation of Dubai | 9.78% |
| Fujairah Investment Company | 5.22% |
| Citizens/companies of the UAE | 23.19% |

2016: During the year, 39,157 shares representing 0.003% of the bank's shares were traded (2015: 1,390,039 shares representing 0.12% of the bank's shares were traded). The market capitalisation of the bank is AED 6.1 billion (2015: AED 5.5 billion).

The investor relations and external communications are managed through the bank's Finance and Corporate Communications departments respectively:

### Finance Department

Telephone: +971 9 202 9210
Facsimile: +971 9 222 9858
E-mail: NBF-investorrelations@nbf.ae

### Corporate Communications Department

Telephone: +971 4 397 1700
Facsimile: +971 4 397 5385

Website: www.nbf.ae and refer to the investor relations section for further details.

## THE BOARD OF DIRECTORS

The Board has adopted an annual agenda to ensure that its responsibilities are effectively carried out on a consistent basis. In addition, the Board continues to focus on improving engagement and effectiveness by reviewing the bank's governance structures, processes and information flow to and from the Board. The Board has established committees such as the Risk Committee, Nomination and Remuneration Committee and Audit Committee to assist the Board in carrying out its responsibilities.

The Board also regularly reviews the financial performance of the bank and its individual business areas. It is also focused on setting the bank's risk appetite, policies, enterprise governance, risk and control framework and three-year business strategy.

### Professional Development and Performance Evaluation

The continued development of the individual Directors of the bank is fundamental for the effectiveness and efficiency of the functioning of the Board and to the long-term sustainability and success of the organisation. During the year, the Board engaged the services of the Tripod Partners Management Consultants to further enhance its awareness on the world class principles and practices for liquidity and market risk management. Such work helps to inform the continuing improvement of the Board's activities and to further develop the bank's commitment to the highest levels of transparency, governance and managing liquidity and market risk.

### Appointment, Retirement and Re-election

During the year, number of directors were increased from eight to nine in line with the new Federal Law No. 2 of 2015 and Mr. Ahmed Saeed Al Raqbani was elected as the ninth Director. The appointment of a new Board Member, and amendment of the Memorandum and Articles of Association, during the course of the year, ensured that the bank is fully aligned with the latest laws and governance practices crucial for its ongoing success. All Directors are required to seek re-election by shareholders every three years. The Board of Directors were elected on 19 March 2014 for a term of three years to fulfil their duties and responsibilities.

The Chairman, Deputy Chairman and all Directors are Non-Executive Directors.

All Directors declare their interests and directorships on an annual basis. Their dealings in the bank's securities are also on full disclosure and on arm's length basis.

## Details of the Board Members' Current Terms of Office and Their External Positions are:

| Board of Directors and their external positions | NBF, "the bank" |
|---|---|
| **His Highness Sheikh Saleh Bin Mohamed Bin Hamad Al Sharqi**<br>Chairman of Department of Industry & Economy, Government of Fujairah<br>Chairman of Fujairah Port Authority<br>Chairman of Fujairah Petroleum Company<br>Chairman of Fujairah National Group | Chairman |
| **His Excellency Easa Saleh Al Gurg, KCVO, CBE**<br>Chairman of Easa Saleh Al Gurg Group<br>Chairman of Al Gurg Fosroc LLC<br>Chairman of Arabian Explosives Company LLC<br>Chairman of Al Gurg Unilever LLC<br>Chairman of Al Gurg Smollan Commercial Investments LLC<br>Chairman of Al Gurg Decorative Paints LLC | Deputy Chairman |
| **Sheikh Hamad Bin Saleh Bin Mohamed Al Sharqi**<br>Vice Chairman of Fujairah National Group<br>Chairman of Al Sharq Health Care (The Health Care Group of Fujairah National Group) | Member |
| **Mr. Hussain Mirza Al Sayegh**<br>Deputy Chairman of Oilfields Supply Center<br>Deputy Chairman of Al Nasr Leisure Land<br>Director of Emirates National Oil Company<br>Director of Emirates National Bank of Dubai (ENBD)<br>Chairman of Jotun UAE Limited (LLC)<br>Chairman of Jotun Powder Coatings<br>Director, Marsh Insco LLC<br>Director of Mawarid Finance<br>Director, Senses | Member |
| **Dr. Sulaiman Mousa Al Jassim**<br>Former Vice President of Zayed University<br>Board Member in Al Fujairah National Insurance Company<br>Chairman of Al Jassim Trading Group<br>Chairman of Al Jassim Marble and Tile Factory<br>Vice Chairman of Sultan Alowais Culture Foundation in Dubai<br>Chairman of Alkhaleej Investment Education Services<br>Member of Board of Abu Dhabi University | Member |
| **Mr. Saif Sultan Al Salami**<br>Managing Director of Fujairah National Group<br>Board Member of Al Fujairah National Insurance Company<br>Managing Director of Fujairah Investment Company | Member |
| **Mr. Mohamed Obaid Bin Majed Al Aleeli**<br>Director General of Department of Industry & Economy, Government of Fujairah | Member |
| **Mr. Abdulla Fareed Al Gurg**<br>Group General Manager, Easa Saleh Al Gurg Group<br>Director of Al Gurg Fosroc LLC<br>Director of Al Gurg Smollan Commercial Investments LLC<br>Director of Al Gurg Decorative Paints LLC<br>Director of Easa Saleh Al Gurg Charity Foundation | Member |
| **Mr. Ahmed Saeed Al Raqbani**<br>Chairman of Fujairah Building Industries<br>Member of Board - Al Taif Investment<br>Member of the Board of Trustees - University of Fujairah<br>Managing Director of East Coast Group | Member |

## Directors' Interests in the Bank's Shares

| Name (Board of Directors) | Shareholding at 1 Jan 2016 | Shareholding at 31 Dec 2016 | Change |
|---|---|---|---|
| Sheikh Saleh Bin Mohamed Bin Hamad Al Sharqi | – | – | – |
| Easa Saleh Al Gurg, KCVO, CBE | – | – | – |
| Sheikh Hamad Bin Saleh Bin Mohamed Al Sharqi | – | – | – |
| Hussain Mirza Al Sayegh | – | – | – |
| Sulaiman Mousa Al Jassim | 1,129,713 | 1,214,441 | 7.5% |
| Saif Sultan Al Salami | – | – | – |
| Mohamed Obaid Bin Majed Al Aleeli | 287,933 | 309,527 | 7.5% |
| Abdulla Fareed Al Gurg | – | – | – |
| Ahmed Saeed Al Raqbani | – | – | – |

## Board Committees

The Board of Directors has overall responsibility for the establishment and oversight of the Group's enterprise risk management framework. The Board sets the overall risk appetite and strategy in consultation with the senior management and approves all principal policies and guidelines to manage credit, liquidity, market, operational and compliance risks. The Board has established the Board Committees to enhance the oversight mechanism in order to discharge its responsibilities effectively. Each Committee has a formal Charter approved by the Board of Directors.

**Risk Committee of the Board** consists of four Board Members and an independent professional member to assist the Board in fulfilling its oversight responsibilities in respect of the risks inherent in the businesses of the Group and the control processes with respect to such risks, the risk profile of the Group, and the risk management, compliance and control activities of the Group. CEO, Chief Risk Officer (CRO) and Chief Financial Officer (CFO) are invitees. The responsibilities of the Committee include, but are not limited to the following:

- Review the Group's Enterprise Risk Management and Internal Control Framework;
- Review risk appetite of the Group and establish risk policies for implementation;
- Review credit risk rating system;
- Review policies for Asset and Liability management;
- Review financial and other risk exposures and the steps management has taken to identify, measure, monitor, control and report such exposures including and without limitation review of credit, market, fiduciary, liquidity, reputation, insurance, operational (including fraud, business continuity, information security and legal) and strategic risks;
- Review appropriate transaction or trading limits;
- Review reports and significant findings from the Risk Management Division, Risk Committee of the Management and from the regulatory agencies relating to risk issues and management response;
- Review Internal Capital Adequacy Assessment Process (ICAAP) submission to the UAE Central Bank;
- Review quality, structure and adequacy of capital and economic capital allocation methodology;
- Review Basel III, liquidity and leverage review methodology;
- Monitor the Group's compliance with legal and regulatory obligations; and
- Review major disclosure documentation prior to the issue to the market.

**Audit Committee of the Board** consists of five Board members and an independent professional member. Head of Internal Audit (HOIA), CEO, Chief Operations Officer (COO) and CFO are invitees. Steered by the Deputy Chairman of the Board, the Committee receives and considers reports and recommendations from the Head of Internal Audit and the external auditors. Further, receives and considers any reports issued by the regulatory authorities and makes recommendations to the Board in respect of financial reporting, systems of internal control and both internal and external audit processes of the Group. The responsibilities of the Committee include, but are not restricted to the following:

- Confirm and assure the independence of the Internal Auditors;
- Review with the Head of Internal Audit and the External Auditor the scope, plan, coordination and effectiveness of internal and external audit efforts;
- Oversight of the preparation of the financial statements including a review of the interim and year end accounts to monitor that such accounts have been prepared in accordance with proper accounting principles and recommend them for adoption by the Board; and
- Review the Group's Internal Control Systems for effectiveness; and all Internal Audit reports concerning any investigation or significant fraud that occurs at the Group.

**Nomination and Remuneration Committee of the Board** comprises the Board's Chairman, the Board's Deputy Chairman and a Board member. The responsibilities of the Committee include, but are not restricted to the following:

- Make recommendations to the Board concerning the appointment, reappointment and succession planning of the Directors except for the position of the Chairman;
- Consider appointment, termination and succession planning for the CEO and as deemed required, other senior management positions in the Group;
- Review the remuneration policy for the Board and the CEO position and determine their terms of service. The CEO and the full Board will determine and review the Group's Human Resources policy and remuneration levels for the Group;
- Review the structure, size and composition required of the Board and make recommendations to the Board with regard to any changes;
- Evaluate the balance of skills, knowledge and experience on the Board; and
- Review the performance of the Board, and work with the members of the Board to develop recommendations to the Board for any performance adjustments deemed advisable.

In 2016, the Board of Directors met regularly and Directors received information about the activities of the Board Committees, Governance and Risk Committees, and developments in the bank's business.

The members and chairman of the Board's Committees are reviewed on a regular basis to ensure suitability and compliance with requirements. The table "Board and Board Committees' membership and meetings" on the next page provides details of membership and meetings of the Board and Board Committees in 2016.

### Board and Board Committees' membership and meetings

| Name | Expiration of current term of office | Board | Board Risk Committee | Board Audit Committee | Board Nomination and Remuneration Committee |
|---|---|---|---|---|---|
| Sheikh Saleh Bin Mohamed Bin Hamad Al Sharqi | 2017 | C | | | C |
| Easa Saleh Al Gurg, KCVO, CBE | 2017 | DC | | C | M |
| Sheikh Hamad Bin Saleh Bin Mohamed Al Sharqi | 2017 | M | M | | |
| Hussain Mirza Al Sayegh | 2017 | M | | M | |
| Sulaiman Mousa Al Jassim | 2017 | M | | M | |
| Saif Sultan Al Salami | 2017 | M | C | M | M |
| Mohamed Obaid Bin Majed Al Aleeli | 2017 | M | M | M | |
| Abdulla Fareed Al Gurg | 2017 | M | M | | |
| Ahmed Saeed Al Raqbani | 2017 | M | | | |
| Sekhar T N | * | | M | M | |
| Vince Cook | CEO | I | I | I | |
| Adnan Anwar | CFO | I | I | I | |
| Balaji Krishnamurthy | COO | I | | I | |
| Prasant Sarkar (retired at the end of the year 2016) | CRO** | | I | | |
| Kevin Taylor | HOIA | | | I | |
| Total no. of meetings | | 9 | 4 | 4 | 5 |
| Approvals by circulation | | 1 | - | - | - |

C: Chairman DC: Deputy Chairman M: Member I: Invitees * Independent Professional Member ** Current CRO: Justin Morgan-Cooper

All principal members of the management team present their businesses' performance, risk and strategy to the full board at least once in a year.

With effect from 2015, the Board has decided to assume credit and investment approval responsibilities directly and dissolved the Executive Committee of the Board. During 2016, credit applications forwarded to the Board for approval by circulation were 119.

## Board of Directors – Remuneration and Interests in the Bank's Shares

The remuneration of the Board members is a fixed amount for the year and paid annually in line with the approval of the General Assembly Meeting. For 2016, the fee was AED 3 million, which was charged to the statement of income, and is 0.65% of net profit attributed to shareholders of the bank.

| Board member remuneration paid during 2016 for year 2015 | Directors' fees (AED per annum) |
|---|---|
| Chairman | 500,000 |
| Deputy Chairman | 500,000 |
| Director and Board Secretary | 250,000 (Per Person) |

## Management

| | |
|---|---|
| Vince Cook | Chief Executive Officer |
| Adnan Anwar | Chief Financial Officer |
| Balaji Krishnamurthy | Chief Operations Officer |
| Prasant Sarkar (retired at the end of the year 2016) | Chief Risk Officer** |
| Vikram Pradhan | Head of Corporate and Institutional Banking |
| Sharif Mohd. Rafei | Head of Retail Banking and Fujairah Region |
| Mark Domenic Zanelli | Head of Treasury |
| Abdulla Aleter | Head of Human Resources |
| Das P B | Senior Executive Officer - NBF Capital Limited |

** Current Chief Risk Officer: Justin Morgan-Cooper

In order to discharge its responsibilities effectively, the Board has established the Management Committee (MANCOM), Risk Committee (RC), Asset and Liability Committee (ALCO), Central Credit Committee (CCC), Operational Risk and Compliance Committee (ORCC), Product Committee (PC) and Grievance and Disciplinary Committee (GDC). These committees oversee and direct the implementation of the day-to-day activities of the Group in line with the guidelines set by the Board. These committees comprise key officers, who convene regularly for the effective and efficient discharge of their responsibilities. The Group's policies and procedures are established to identify and analyse the risks faced by the Group, to set appropriate risk limits and controls, to monitor risks and adherence to limits, and to ensure effective escalation and reporting. Risk management policies and systems are reviewed regularly to reflect changes in market conditions, products and services offered.

The Management Committee (MANCOM), steered by the CEO, is responsible for the development and monitoring of execution plan of the Group's strategy approved by the Board, implementation of corporate governance, performance measurement and monitoring, deciding on staff related matters, policies and any other administrative matters other than risk matters. MANCOM has further established Marketing Committee (MC), Human Resources Committee (HRC), Corporate Social Responsibility Committee (CSRC), IT Steering Committee (ITSC), Data Governance Committee (DGC), Customer Service Quality Committee (SQC) and Shari'a Governance Committee (SGC) for carrying out its responsibilities effectively.

The Risk Committee (RC), steered by the CEO, is responsible for developing and recommending to the Board through the Risk Committee of the Board, the Group's risk appetite, develop and review the Group's risk policies and ICAAP, recommend allocations of regulatory and economic capital to portfolio segments and business lines, approve scenarios for stress testing for all risk categories and evaluate potential changes to market conditions. Further, the Committee reviews significant financial or other risks and the steps management has taken to monitor, control and report such risks, including, but without limitation to, review of credit, market, fiduciary, liquidity, reputation, operational, compliance, legal, fraud and strategic risks. It obtains assurance that significant risks are being measured, monitored, evaluated, and appropriately escalated through periodic updates, risk reporting, and key risk indicator reviews from ALCO, CCC, ORCC and PC.

The Asset and Liability Committee (ALCO), steered by the CFO, is responsible for directing asset and liability growth and allocations in order to achieve the Group's strategic goals. It monitors the Group's liquidity and market risks and the Group's risk profile in the context of economic developments and market fluctuations, to ensure that the Group's ongoing activities are compatible with the risk appetite approved by the Board. The Committee is also responsible for developing and establishing ALCO metrics and MIS for review, measurement, monitoring and control of all market and liquidity risks and stress testing.

The Central Credit Committee (CCC), steered by the Head of Credit, is responsible for credit decisions for the Group's lending portfolio, setting country and other high level Group risk limits, oversee portfolio reviews with particular focus on quality, dealing with impaired assets and grading of credit facilities. The Committee is also responsible for developing and establishing credit risk metrics and MIS for review, measurement, monitoring and control of all credit risks, stress testing for reviews of credit risk policies, enhancement of credit risk reporting and processing.

The Operational Risk and Compliance Committee (ORCC), steered by the Head of Operational Risk and Compliance, is responsible for independently assessing and monitoring the operational risks of the Group against the Group's operational risk management policies, internal control framework and operational risk appetite as approved by the Board. It is responsible for the review of operational procedures, adequacy of the internal control systems, develop and establish operation risk metrics and MIS for review, measurement, monitor and control of operational risks. Further, it is also responsible for the implementation of the Business Continuity Plan (BCP) and Disaster Recovery Programme (DR), review of anti-money laundering unit reports and adequacy of compliance with relevant laws, regulations and license conditions. The Committee also reviews reports from internal, external and Central Bank audits and monitors progress on actions initiated to address all operational risks covered by these reports.

The Product Committee (PC), steered by the CRO, is responsible for reviewing and approving all risks, designs, pricing, financials, product risk ratings, processes for distribution, product control and MIS processes of proposed new products and services and any changes to existing products and services. It ensures that the products and services fall within the risk appetite and the Group's strategic plans. It is responsible for monitoring the Group's competitiveness in product positioning and developments in technology that could have an impact on risk profile and profitability of products and services.

The Investment Committee (IC), steered by the CEO, is responsible for independently managing the bank's proprietary investments, in a diversified portfolio of marketable securities across various asset classes, geographies and industries. It reviews and approves the investment strategy, strategic asset allocation, investment proposals in line with the risk, returns and liquidity objectives set by the bank's Risk Committee and approved by the Board Risk Committee and the Board. It also reviews, debates and approves the client investment proposition's overall framework, proposed asset allocation mix and approves the selection and termination of external fund managers and any external investment consultants and advisors.

The Marketing Committee (MC), steered by the CEO, is responsible for challenging marketing strategies or plans proposed by the Business Segments and recommend the changes for improving marketing and selling activities. It co-ordinates and monitors the support and resources required, new product and channels development and pricing strategies. It oversees plans for developing business with the Group's key customers and monitors progress together with setting customer service standards.

The Human Resources Committee (HRC), steered by the CEO, is responsible for ensuring internal equity of compensation and overall evaluation of jobs for consistent and accurate assessment. It is responsible for grade and compensation structure together with benchmarking in line with the market conditions. In order to achieve its objectives, the Committee reviews the organisation design and changes/improvements to the rewards and benefits structure and discusses future human resources planning, policies and procedure guidelines.

The IT Steering Committee (ITSC), steered by the CEO, is responsible for providing direction to the Group's key technology initiatives and assisting in the alignment of IT spend with business needs. It is responsible for providing oversight on IT projects and direction on technology dependent projects including prioritisation and resource alignment.

The Corporate Social Responsibility Committee (CSRC), steered by Manager, Internal Audit, is responsible for the oversight of environmental management, community initiatives and communication of CSR initiatives within and outside the Group.

The Grievance and Disciplinary Committee (GDC), steered by the Head of Human Resources, is empowered by the bank's MANCOM to act impartially when dealing with staff grievances and disciplinary cases in accordance with Group rules, policies and UAE laws.

The Data Governance Committee (DGC), steered by CFO, is responsible for the data management with respect to organisational goals and regulatory requirements. It has the responsibility for defining the organisational structure and roles of the governance framework for the purpose of decision making about data policies, processes, data ownership, data security classification, data retention and for defining clear and consistent data structures and models to leverage information-critical business planning and support system-wide coordination and collaboration, effective decision-support, and efficient operations.

The Customer Service Quality Committee (SQC), steered by Head of Corporate and Institutional Banking, drives excellence in service quality across the bank with the objective of achieving external/internal customer satisfaction and loyalty. It is responsible for defining clear customer service goals and deliverables, establish framework to gather and analyse feedback, identify service gaps and initiate process improvements. It undertakes benchmarking with industry to assess service standards, drives quality training sessions and standard certifications for internal units.

Shari'a Governance Committee (SGC), steered by CEO, is responsible to independently assess and manage Shari'a compliance risk of Islamic products of the bank against SGF. The SGC assumes the duty of ensuring the operational execution of the SGF by NBF Islamic. The SGC is ultimately accountable for the establishment and overall governance of the SGF.

## EXTERNAL AUDITORS

PricewaterhouseCoopers (PwC) were appointed external auditors for the bank and its subsidiaries by the shareholders at the General Assembly Meeting (GAM) held on 16 March 2016. The fee for external audit work for the audit of the bank and its subsidiaries for the year ended 31 December 2016 was AED 619,479 (plus out-of-pocket expenses).

PricewaterhouseCoopers
Emaar Square, Building 4, Level 8
PO Box 11987, Dubai, United Arab Emirates
Telephone: +971 4 304 3100
Facsimile: +971 4 330 4100

# INDEPENDENT AUDITOR'S REPORT

NBF is committed to the highest levels of transparency and governance.

## INDEPENDENT AUDITOR'S REPORT TO THE SHAREHOLDERS AND DIRECTORS OF NATIONAL BANK OF FUJAIRAH PJSC

### Report on the Audit to the Financial Statements

#### Our opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the consolidated financial position of National Bank of Fujairah PJSC ("the bank") and its subsidiaries (together referred to as "the Group") as at 31 December 2016, and its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with International Financial Reporting Standards ('IFRS').

#### What we have audited

The Group's consolidated financial statements comprise:

- the consolidated statement of financial position as at 31 December 2016;
- the consolidated statement of income for the year then ended;
- the consolidated statement of comprehensive income for the year then ended;
- the consolidated statement of cash flows for the year then ended;
- the consolidated statement of changes in equity for the year then ended; and
- the notes to the consolidated financial statements, which include a summary of significant accounting policies.

#### Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the *Auditor's responsibilities for the audit of the consolidated financial statements section of our report.*

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

#### Independence

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

## OUR AUDIT APPROACH

### Overview

| | |
|---|---|
| Key Audit Matters | • Impairment of credit facilities |

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

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

### Key Audit Matters

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

| Key Audit Matter | How our audit addressed the Key Audit Matter |
|---|---|
| Impairment of credit facilities<br>*(refer to note 10 of the consolidated financial statements)*<br>Impairment allowances represent management's best estimate of the losses incurred within the credit portfolios at the balance sheet date. They are calculated on a collective basis for portfolios of performing loans of a similar nature and on an individual basis for non-performing loans. The calculation of both collective and individual impairment allowances is inherently judgemental.<br><br>The calculation of collective provision is based on statistical models which approximate the impact of current economic and credit conditions on portfolios of similar loans. The inputs to these models are subject to management judgement.<br><br>For specific impairments, judgement is required to determine when an impairment event has occurred and then to estimate the expected future cash flows related to that loan.<br><br>We focused on this area because management make subjective judgements over both timing of recognition of impairment and the estimation of the size of any impairment.<br><br>We focused our audit specifically relating to:<br><br>• the key assumptions and judgements made by the management that underlie the calculation of modelled impairment. Key assumptions include the probability of default and the loss given default; and<br><br>• the completeness of the customer accounts that are included in the impairment calculation, including how unidentified impairment (customers that have had a loss event that has not yet manifested itself in a missed payment or other indicator) and forbearance are taken account of. | We assessed and tested the design and operating effectiveness of the controls over impairment data and calculations. These controls included those over the identification of which credit facilities were impaired, the data transfer from source systems to impairment models and model output to the general ledger, and the calculation of collective and specific impairment provisions.<br><br>In addition, we performed detailed testing on the models used to calculate both identified and unidentified impairment. This testing typically included testing of the extraction of data used in the model, assessing the appropriateness of the assumptions used in the models and re-performance of the impairment calculation.<br><br>Where impairment was individually calculated, we tested controls over the timely identification of potentially impaired loans.<br><br>We also tested a sample of credit facilities to ascertain whether the loss event (the point at which impairment is recognised) had been identified in a timely manner. Where impairment had been identified, we examined the forecasts of future cash flows prepared by management to support the calculation of the impairment, challenging the assumptions and comparing estimates including collateral valuations, to external evidence, where available.<br><br>We examined a sample of credit facilities which had not been identified by management as potentially impaired and formed our own judgement as to whether that was appropriate including the use of external evidence in respect of the relevant counterparties. |

## Other Information

Management is responsible for the other information. The other information comprises Strategic Report, Directors' Report, Sustainability Report and Corporate Governance Report (but does not include the financial statements and our auditor's report thereon), which we obtained prior to the date of this auditor's report.

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

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

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

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

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

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

Those charged with governance (the "Board of Directors"), are responsible for overseeing the Group's financial reporting process.

## Auditor's Responsibilities for the Audit of the Consolidated Financial Statements

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

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

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

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

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

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

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

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

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

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

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

## Report on Other Legal and Regulatory Requirements

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

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

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

iii. the Group has maintained proper books of account;

iv. the financial information included in the Strategic report and Directors' report, is consistent with the books of account of the Group;

v. as disclosed in note 9 to the consolidated financial statements, the Group has not purchased or invested in any shares during the year ended 31 December 2016;

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

vii. note 25 to the consolidated financial statements discloses the social contributions made during the year; and

viii. based on the information that has been made available to us, nothing has come to our attention which causes us to believe that the Group has contravened during the financial year ended 31 December 2016 any of the applicable provisions of the UAE Federal Law No. (2) of 2015 or in respect of the bank, its Memorandum and Articles of Association which would materially affect its activities or its financial position as at 31 December 2016.

Further, as required by the UAE Union Law No (10) of 1980, as amended, we report that we have obtained all the information and explanations we considered necessary for the purpose of our audit.

**PricewaterhouseCoopers**
**25 January 2017**

**Mohamed ElBorno**
Registered Auditor Number 946
Place: Dubai, United Arab Emirates

# GROUP FINANCIAL STATEMENTS

The bank takes pride in its ability to consistently deliver value to its shareholders, and this year is no exception.

## CONSOLIDATED STATEMENT OF FINANCIAL POSITION

As at 31 December 2016

| | Note | 2016 AED'000 | 2015 AED'000 |
|---|---|---|---|
| **Assets** | | | |
| Cash and balances with the UAE Central Bank | 7 | 6,780,092 | 4,505,567 |
| Due from banks and financial institutions | 8 | 2,142,690 | 2,921,797 |
| Investments and Islamic instruments | 9 | 1,786,279 | 1,407,168 |
| Loans and advances and Islamic financing receivables | 10 | 22,818,496 | 19,688,336 |
| Property and equipment and capital work-in-progress | 12 | 151,795 | 142,467 |
| Other assets | 13 | 1,988,767 | 1,367,821 |
| **Total assets** | | **35,668,119** | **30,033,156** |
| **Liabilities** | | | |
| Due to banks | 14 | 1,110,041 | 873,252 |
| Customer deposits and Islamic customer deposits | 15 | 25,938,491 | 21,612,534 |
| Term borrowings | 14 | 1,906,649 | 1,755,730 |
| Other liabilities | 16 | 2,133,882 | 1,512,023 |
| **Total liabilities** | | **31,089,063** | **25,753,539** |
| **Shareholders' equity** | | | |
| Share capital | 17 | 1,271,188 | 1,182,500 |
| Statutory reserve | 17 | 503,223 | 457,320 |
| Special reserve | 17 | 398,223 | 352,320 |
| Available-for-sale revaluation reserve | | (9,536) | (7,783) |
| Proposed cash dividends | 17 | 95,339 | 88,688 |
| Proposed bonus issue | 17 | 95,339 | 88,688 |
| Retained earnings | | 1,225,280 | 1,117,884 |
| Tier 1 capital notes | 18 | 1,000,000 | 1,000,000 |
| **Total shareholders' equity** | | **4,579,056** | **4,279,617** |
| **Total liabilities and shareholders' equity** | | **35,668,119** | **30,033,156** |

These consolidated financial statements were approved and authorised for issue by the Board of Directors on 25 January 2017 and are signed on its behalf by:

**Saleh Bin Mohamed Bin Hamad Al Sharqi**
Chairman

**Easa Saleh Al Gurg, KCVO, CBE**
Deputy Chairman

The notes on pages 47 to 89 form an integral part of these consolidated financial statements.
The report of the independent auditor is set out on pages 35 to 40.

## CONSOLIDATED STATEMENT OF INCOME

For the year ended 31 December 2016

| | Note | 2016 AED'000 | 2015 AED'000 |
|---|---|---|---|
| Interest income and income from Islamic financing and investment activities | 19 | 1,275,819 | 1,085,409 |
| Interest expense and distribution to Islamic depositors | 20 | (427,618) | (284,105) |
| **Net interest income and net income from Islamic financing and investment activities** | | **848,201** | **801,304** |
| Net fees and commission income | 21 | 311,000 | 294,140 |
| Foreign exchange and derivatives income | | 102,289 | 90,956 |
| Income from investments and Islamic instruments | 22 | 11,131 | 2,707 |
| Other operating income | 23 | 46,486 | 23,990 |
| **Operating income** | | **1,319,107** | **1,213,097** |
| **Operating expenses** | | | |
| Employee benefits expense | 24 | (309,598) | (316,887) |
| Depreciation and amortisation | 12 | (22,675) | (20,560) |
| Other operating expenses | | (120,869) | (108,798) |
| **Total operating expenses** | | **(453,142)** | **(446,245)** |
| **Operating profit** | | **865,965** | **766,852** |
| Net impairment losses | 10 | (405,522) | (208,092) |
| **Profit for the year** | | **460,443** | **558,760** |
| **Earnings per share (basic and diluted)** | 26 | **AED 0.31** | **AED 0.40** |

Appropriations have been reflected in consolidated statement of changes in equity.
The notes on pages 47 to 89 form an integral part of these consolidated financial statements.
The report of the independent auditor is set out on pages 35 to 40.

## CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

For the year ended 31 December 2016

| | 2016 AED'000 | 2015 AED'000 |
|---|---|---|
| **Profit for the year** | **460,443** | **558,760** |
| **Other comprehensive income:** | | |
| **Items that are or may be re-classified subsequently to the statement of income** | | |
| **Changes in available-for-sale investments:** | | |
| Net fair value gains on disposal of available-for-sale investments | (11,570) | (2,950) |
| Net changes in fair value of available-for-sale investments | 9,817 | (4,144) |
| **Net change in available-for-sale investments** | **(1,753)** | **(7,094)** |
| **Total comprehensive income for the year** | **458,690** | **551,666** |

The notes on pages 47 to 89 form an integral part of these consolidated financial statements.
The report of the independent auditor is set out on pages 35 to 40.

## CONSOLIDATED STATEMENT OF CASH FLOWS

For the year ended 31 December 2016

| | Note | 2016 AED'000 | 2015 AED'000 |
|---|---|---|---|
| **Operating Activities** | | | |
| **Profit for the year** | | **460,443** | **558,760** |
| Adjustments for: | | | |
| Depreciation and amortisation | 12 | 22,675 | 20,560 |
| Provision for employee end of service and other long term benefits | 16.1 | 13,071 | 13,749 |
| Gain on disposal of property and equipment | | (6) | - |
| Net impairment losses | 10.3 | 405,522 | 208,092 |
| Net fair value gains on disposal of investments | | (11,570) | (2,950) |
| Net changes in fair value of investments at fair value through profit or loss | | 439 | 243 |
| **Cash flow from operating activities before changes in operating assets and liabilities and payment of employee end of service and other long term benefits** | | **890,574** | **798,454** |
| Payment of employee end of service and other long term benefits | 16.1 | (9,341) | (8,589) |
| Change in statutory reserve with the UAE Central Bank | | (103,281) | (315,609) |
| Change in due from banks and financial institutions | | 276,150 | (418,974) |
| Change in loans and advances and Islamic financing receivables | | (3,535,682) | (3,567,980) |
| Change in other assets | | (620,946) | (42,383) |
| Change in due to banks | | 142,840 | 300,384 |
| Change in customer deposits and Islamic customer deposits | | 4,325,957 | 3,680,803 |
| Change in other liabilities | | 618,129 | 70,702 |
| **Net cash generated from operating activities** | | **1,984,400** | **496,808** |
| **Investing activities** | | | |
| Purchase of property and equipment and capital work-in-progress | | (32,003) | (38,096) |
| Gain on disposal of property and equipment | | 6 | - |
| Purchase of investments and Islamic instruments | | (1,514,768) | (1,377,818) |
| Proceeds from sale of investments and Islamic instruments | | 1,145,035 | 564,399 |
| **Net cash used in investing activities** | | **(401,730)** | **(851,515)** |
| **Financing activities** | | | |
| Proceeds from term borrowings | | 1,047,524 | 988,430 |
| Repayment of term borrowings | | (896,605) | (405,860) |
| Cash dividends | | (88,688) | (82,500) |
| Proceeds from issue of Tier 1 capital notes | | - | 500,000 |
| Tier 1 capital notes coupon paid | | (70,563) | (52,438) |
| Tier 1 capital notes issuance cost | | - | (1,538) |
| **Net cash (used in)/generated from financing activities** | | **(8,332)** | **946,094** |
| **Net change in cash and cash equivalents** | | **1,574,338** | **591,387** |
| Cash and cash equivalents at beginning of the year | | 4,340,988 | 3,749,601 |
| **Cash and cash equivalents at end of the year** | 28 | **5,915,326** | **4,340,988** |

The notes on pages 47 to 89 form an integral part of these consolidated financial statements.
The report of the independent auditor is set out on pages 35 to 40.

## CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

For the year ended 31 December 2016

| | Share capital AED'000 | Statutory reserve AED'000 | Special reserve AED'000 | Available-for-sale revaluation reserve AED'000 | Proposed dividends AED'000 | Retained earnings AED'000 | Tier 1 capital notes AED'000 | Total AED'000 |
|---|---|---|---|---|---|---|---|---|
| **At 1 January 2015** | **1,100,000** | **403,126** | **298,126** | **(689)** | **165,000** | **898,864** | **500,000** | **3,364,427** |
| Total comprehensive income for the year | - | - | - | (7,094) | - | 558,760 | - | 551,666 |
| Issue of Tier 1 capital notes (note 18) | - | - | - | - | - | - | 500,000 | 500,000 |
| Tier 1 capital notes issuance cost (note 18) | - | - | - | - | - | (1,538) | - | (1,538) |
| Tier 1 capital notes coupon paid (note 18) | - | - | - | - | - | (52,438) | - | (52,438) |
| Proposed cash dividends | - | - | - | - | 88,688 | (88,688) | - | - |
| Proposed bonus issue | - | - | - | - | 88,688 | (88,688) | - | - |
| Transfer to reserves | - | 54,194 | 54,194 | - | - | (108,388) | - | - |
| 2014 cash dividends paid | - | - | - | - | (82,500) | - | - | (82,500) |
| 2014 bonus shares issued | 82,500 | - | - | - | (82,500) | - | - | - |
| **At 31 December 2015** | **1,182,500** | **457,320** | **352,320** | **(7,783)** | **177,376** | **1,117,884** | **1,000,000** | **4,279,617** |
| **At 1 January 2016** | **1,182,500** | **457,320** | **352,320** | **(7,783)** | **177,376** | **1,117,884** | **1,000,000** | **4,279,617** |
| Total comprehensive income for the year | - | - | - | (1,753) | - | 460,443 | - | 458,690 |
| Tier 1 capital notes coupon paid (note 18) | - | - | - | - | - | (70,563) | - | (70,563) |
| Proposed cash dividends | - | - | - | - | 95,339 | (95,339) | - | - |
| Proposed bonus issue | - | - | - | - | 95,339 | (95,339) | - | - |
| Transfer to reserves | - | 45,903 | 45,903 | - | - | (91,806) | - | - |
| 2015 cash dividends paid | - | - | - | - | (88,688) | - | - | (88,688) |
| 2015 bonus shares issued | 88,688 | - | - | - | (88,688) | - | - | - |
| **At 31 December 2016** | **1,271,188** | **503,223** | **398,223** | **(9,536)** | **190,678** | **1,225,280** | **1,000,000** | **4,579,056** |

The notes on pages 47 to 89 form an integral part of these consolidated financial statements.
The report of the independent auditor is set out on pages 35 to 40.

For the year ended 31 December 2016

## 1. Legal Status and Activities

National Bank of Fujairah ("the bank") is a Public Joint Stock Company registered under the laws of the United Arab Emirates. The bank operates under a banking licence issued on 29 August 1984 by the Central Bank of the United Arab Emirates ('the UAE Central Bank') and commenced operations on 20 September 1984. The shares of the bank were listed on Abu Dhabi Securities Exchange (ADX) on 23 October 2005.

UAE Federal Law No. 2 of 2015 (Companies Law) which is applicable to the Group has come into effect from 1 July 2015. The Group has assessed and evaluated the relevant provisions of the Companies Law and is in the process of ensuring compliance with the transitional period of this law, which has been extended till 30 June 2017.

The principal activity of the bank is commercial banking which is carried out from its sixteen branches in Fujairah, Abu Dhabi, Dubai, Sharjah, Dibba, Jebel Ali, Musaffah, Masafi, Qidfah, Deira, Ajman, Tawian, Al-Ain, Fujairah City Centre, Al Quoz and Fujairah Free Zone.

The bank has three fully owned subsidiary companies:

- NBF Financial Services FZC was established in December 2004 with limited liability status in the Fujairah Free Trade Zone to provide support services to the bank.
- NBF Capital Limited is registered in the Dubai International Financial Centre (DIFC) as a company limited by shares under DIFC laws and regulations and regulated by the Dubai Financial Services Authority (DFSA). The Company was established on 3 April 2013 and commenced operations on 12 May 2013. The principal business activities of the Company are arranging credit or deals in investments and advising on financial products or credit.
- NBF Trade Services (HKG) Limited is registered in Hong Kong as a company limited by shares governed and regulated under the Hong Kong Companies Ordinance. The Company was established on 10 May 2013. The principal business activity of the Company is the provision of trade processing services.

The consolidated financial statements comprise the bank and its subsidiaries (together referred to as 'the Group').

The registered address of the Group is Hamad Bin Abdullah Street, P. O. Box 887, Fujairah, United Arab Emirates.

## 2. Disclosure Policy

The Group has established a disclosure policy to ensure compliance with all applicable laws and regulations concerning disclosure of material non-public information, including International Financial Reporting Standards (IFRS), the rules of the UAE Central Bank and its Basel II Pillar 3 guidelines and the listing requirements of the Securities and Commodities Authority (SCA) and ADX.

### Frequency and medium of disclosure

The condensed consolidated interim financial information is prepared and presented on a quarterly basis while complete consolidated financial statements are prepared and presented on an annual basis in compliance with the requirements of IFRS, Basel II Pillar 3 and other guidelines from the UAE Central Bank. Disclosures of material non-public financial information are made by the Finance Department of the Group through the following mediums:

- Sending quarterly reviewed and annual audited consolidated financial statements, along with Management Discussion Analysis or Directors' report and any other price sensitive information, to ADX and SCA;
- Hosting quarterly and annual consolidated financial statements on the Group's website;
- Publication of the annual report; and
- Investor presentations.

In addition, the Group's Corporate Communication Department discloses and disseminates information through press releases, media coverage and the Group's website.

## 3. Basis of Preparation

### Statement of compliance

The consolidated financial statements have been prepared in accordance with IFRS as issued by the International Accounting Standards Board (IASB), interpretations issued by International Financial Reporting Interpretations Committee (IFRIC) and applicable requirements of laws of the United Arab Emirates.

Along with these consolidated financial statements, the Group has presented Basel II Pillar 3 disclosures in accordance with the guidelines issued by the UAE Central Bank. The adoption of Basel II Pillar 3 guidelines has impacted the type and amount of disclosures made in these consolidated financial statements, but had no impact on the reported profits or financial position of the Group. In accordance with the requirements of Basel II, the Group has provided full comparative information.

## 4. Significant Accounting Policies

### a. Standards, amendments and interpretations

**Standards, amendments and interpretations that are effective for the Group's accounting period beginning on 1 January 2016**

| New standards and significant amendments to standards applicable to the Group | Effective date |
|---|---|
| Amendment to IAS 16, 'Property, plant and equipment' and IAS 38, 'Intangible assets' regarding depreciation and amortisation.<br>This amendment clarifies that revenue is generally presumed to be an inappropriate basis for measuring the consumption of the economic benefits embodied in an intangible asset.<br><br>The presumption may only be rebutted in certain limited circumstances. | 1 January 2016 |
| IAS 1 Amendments to IAS 1, 'Presentation of financial statements' Disclosure initiative<br>The amendments clarify that it may be necessary to disaggregate some of the line items specified in IAS 1 paragraphs 54 (statement of financial position) and 82 (profit or loss). That disaggregation is required where it is relevant to an understanding of the entity's financial position or performance. | 1 January 2016 |
| Annual improvements 2014<br>These annual improvements amend standards from the 2012 - 2014 reporting cycle. It includes changes to:<br>• IFRS 7, 'Financial instruments: Disclosures' – The amendment related to servicing contracts requires that if an entity transfers a financial asset to a third party under conditions which allow the transferor to derecognise the asset, IFRS 7 requires disclosure of all types of continuing involvement that the entity might still have in the transferred assets.<br>• IAS 19, 'Employee benefits' – The amendment clarifies, when determining the discount rate for post-employment benefit obligations, that it is the currency that the liabilities are denominated in that is important, not the country where they arise.<br>• IAS 34, 'Interim financial reporting', regarding information disclosed elsewhere in the interim financial report. The amendment clarifies what is meant by the reference in the standard to 'information disclosed elsewhere in the interim financial report'. The amendment further amends IAS 34 to require a cross-reference from the interim financial statements to the location of that information. The amendment is retrospective. | 1 January 2016 |

There is no material impact of the above amendments on the consolidated financial statements of the Group.

There are no other IFRSs or IFRIC interpretations that were effective for the first time for the financial year beginning on 1 January 2016 that have had a material impact on the Group's consolidated financial statements.

**Standards, amendments and interpretations issued but not yet effective for the Group's accounting period beginning on 1 January 2016 and not early adopted**

| New standards and significant amendments to standards applicable to the Group | Effective date |
|---|---|
| **IFRS 15, 'Revenue from contracts with customers'**<br>This standard replaces IAS 11, 'Construction contracts', IAS 18, 'Revenue' and related interpretations. Revenue is recognised when a customer obtains control of a good or service and thus has the ability to direct the use of and obtain the benefits from the good or service. The core principle of IFRS 15 is that an entity recognises revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. IFRS 15 also includes a cohesive set of disclosure requirements that will result in an entity providing users of financial statements with comprehensive information about the nature, amount, timing and uncertainty of revenue and cash flows arising from the entity's contracts with customers.<br>**Amendment to IFRS 15, 'Revenue from contracts with customers'**<br>These amendments comprise clarifications on identifying performance obligations, accounting for licences of intellectual property and the principal versus agent assessment (gross versus net revenue presentation). The IASB has also included additional practical expedients related to transition to the new revenue standard. | 1 January 2018 |
| **IFRS 9, 'Financial instruments'**<br>The complete version of IFRS 9 replaces most of the guidance in IAS 39. IFRS 9 retains but simplifies the mixed measurement model and establishes three primary measurement categories for financial assets: amortised cost, fair value through OCI and fair value through P&L. The basis of classification depends on the entity's business model and the contractual cash flow characteristics of the financial asset. Investments in equity instruments are required to be measured at fair value through profit or loss with the irrevocable option at inception to present changes in fair value in OCI. There is now a new expected credit losses model that replaces the incurred loss impairment model used in IAS 39. For financial liabilities, there were no changes to classification and measurement except for the recognition of changes in own credit risk in other comprehensive income, for liabilities designated at fair value, through profit or loss. IFRS 9 relaxes the requirements for hedge effectiveness by replacing the bright line hedge effectiveness tests. It requires an economic relationship between the hedged item and hedging instrument and for the 'hedged ratio' to be the same as the one management actually uses for risk management purposes. Contemporaneous documentation is still required but is different to that currently prepared under IAS 39. | 1 January 2018 |
| **Amendments to IAS 7, 'Statement of cash flows on disclosure initiative'**<br>These amendments to IAS 7 introduce an additional disclosure that will enable users of financial statements to evaluate changes in liabilities arising from financing activities including those from cash flows and other non-cash changes. The new requirement typically entails a reconciliation between the opening and closing balances in the statement of financial position for liabilities arising from financing activities. | 1 January 2017 |

| New standards and significant amendments to standards applicable to the Group | Effective date |
|---|---|
| **IFRS 16, 'Leases'**<br>This standard replaces the current guidance in IAS 17 and is a far reaching change in accounting by lessees in particular. Under IAS 17, lessees were required to make a distinction between a finance lease (on balance sheet) and an operating lease (off balance sheet). IFRS 16 now requires lessees to recognise a lease liability reflecting future lease payments and a 'right-of-use asset' for virtually all lease contracts. The IASB has included an optional exemption for certain short-term leases and leases of low-value assets; however, this exemption can only be applied by lessees.<br><br>For lessors, the accounting stays almost the same. However, as the IASB has updated the guidance on the definition of a lease (as well as the guidance on the combination and separation of contracts), lessors will also be affected by the new standard. At the very least, the new accounting model for lessees is expected to impact negotiations between lessors and lessees. Under IFRS 16, a contract is, or contains, a lease if the contract conveys the right to control the use of an identified asset for a period of time in exchange for consideration. | 1 January 2019 |
| **Amendments to IFRS 10, 'Consolidated financial statements' and IAS 28, 'Investments in associates and joint ventures' regarding the sale or contribution of assets between an investor and its associate or joint venture**<br>These amendments address an inconsistency between IFRS 10 and IAS 28 in the sale or contribution of assets between an investor and its associate or joint venture. A full gain or loss is recognised when a transaction involves a business. A partial gain or loss is recognised when a transaction involves assets that do not constitute a business, even if those assets are in a subsidiary. | Date to be determined |

The Group has taken measures to adhere to the above new standards and amendments to published standards or IFRIC interpretations issued but not yet effective for the Group's financial year beginning on 1 January 2016.

There are no other applicable new standards and amendments to published standards or IFRIC interpretations that have been issued but are not effective for the first time for the Group's financial year beginning on 1 January 2016 that would be expected to have a material impact on the consolidated financial statements of the Group.

### b. Basis of measurement

The consolidated financial statements are prepared under the historical cost convention as modified by the revaluation of the following financial assets:

- Derivative financial instruments are measured at fair value;
- Financial instruments at fair value through profit or loss are measured at fair value; and
- Available-for-sale financial assets are measured at fair value.

### c. Functional and presentation currency

Items included in the consolidated financial statements of the Group are measured and presented in the United Arab Emirates Dirham ("AED") which is the functional currency of the Group.

The accounting policies set out below have been applied consistently by the Group to all periods presented in these consolidated financial statements.

### d. Basis of consolidation

#### Subsidiaries

Subsidiaries are all entities (including structured entities) over which the Group has control. The Group controls an entity when the Group is exposed to, or has rights to, variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity. Subsidiaries are fully consolidated from the date on which control is transferred to the Group. They are deconsolidated from the date that control ceases.

Inter-company transactions, balances, income and expenses on transactions between Group companies are eliminated. Profits and losses resulting from intercompany transactions are also eliminated. Accounting policies of subsidiaries have been changed where necessary to ensure consistency with the policies adopted by the Group.

### e. Financial instruments

#### Classification

A financial instrument is any contract that gives rise to a financial asset/liability for the Group and a financial asset/ liability or equity instrument of another party. All assets and liabilities in the consolidated statement of financial position are financial instruments, except property and equipment, capital work-in-progress, prepayments, advance receipts, provision of employee end of service benefits and shareholders' equity.

### Financial assets are categorised as follows:

**Financial assets at fair value through profit or loss (FVTPL):** This category has two sub-categories: financial assets held-for-trading, and those designated to be fair valued through profit or loss at inception. The Group has designated financial assets at fair value through profit or loss when the assets are managed, evaluated and reported internally on a fair value basis. Derivatives are also categorised as held for trading unless they are designated as hedges.

**Loans and receivables** are non-derivative financial assets with fixed and determinable payments that are not quoted in an active market.

**Held-to-maturity (HTM) assets** are non-derivative financial assets with fixed or determinable payments and fixed maturities, where the Group has the positive intent and ability to hold to maturity. Where the Group sells other than an insignificant amount of held-to-maturity assets, the entire category would be re-classified as available-for-sale.

**Available-for-sale (AFS) assets** are those non-derivative financial assets that are designated as available-for-sale or not classified as (a) loans and receivables, (b) held-to-maturity investments or (c) financial assets at fair value through profit or loss.

### Initial recognition

Regular purchases and sales of financial assets are recognised on the trade-date, the date on which the Group commits to purchase or sell the asset. Financial instruments are initially recognised at fair value plus transaction costs for all financial assets not carried at fair value through profit or loss. Financial assets carried at fair value through profit or loss are initially recognised at fair value, and transaction costs are expensed in the consolidated statement of income. Loans and advances are recognised when cash is advanced to the borrowers.

### De-recognition

Financial assets are derecognised when the rights to receive cash flows from the investments have expired or have been transferred and the Group has transferred substantially all risks and rewards of ownership. Available-for-sale financial assets and financial assets at fair value through profit or loss are subsequently carried at fair value. Loans and receivables are subsequently carried at amortised cost using the effective interest method. A financial liability is derecognised when it is extinguished.

### Measurement

Subsequent to initial recognition, all financial instruments to be fair valued through profit or loss and available-for-sale assets are measured at fair value.

All held-to-maturity financial instruments and loans and advances for which the fair value has not been hedged are measured at amortised cost less impairment losses.

### Amortised cost measurement

The amortised cost of a financial asset or liability is the amount at which the financial asset or liability is measured at initial recognition, minus principal repayments, plus or minus the cumulative amortisation using the effective interest method of any difference between the initial amount recognised and the maturity amount, minus any reduction for impairment. Premiums and discounts including initial transaction costs are included in the carrying amount of the related instrument.

### Fair value measurement principles

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

When available, the fair value of a financial instrument is based on quoted market prices in an active market for that instrument. A market is regarded as active if quoted prices are readily and regularly available and represent actual and regularly occurring market transactions on an arm's length basis. If a quoted market price is not available or if a market for a financial instrument is not active, the fair value is determined by using valuation techniques. Valuation techniques include net present value techniques, discounted cash flow methods, comparison to similar instruments for which market observable prices exist. For investments under management with external fund managers, fair value is provided by the external fund managers, and is determined based on the market value of underlying investments of each fund. In all other cases, the instruments are measured at acquisition cost, including transaction cost, less impairment losses, if any.

Where discounted cash flow techniques are used, estimated future cash flows are based on management's best estimates and the discount rate is a market-related rate at the date of the consolidated statement of financial position for an instrument with similar terms and conditions.

Fair values reflect the credit risk of the instrument and include adjustments to take account of the credit risk of the Group and the counterparty, where appropriate. Fair value estimates obtained from models are adjusted for any other factors, such as liquidity risk or model uncertainties; to the extent that the Group believes a third-party market participant would take them into account in pricing a transaction.

The fair value of derivatives that are not exchange traded is estimated at the amount that the Group would receive or pay to terminate the contract at the date of consolidated statement of financial position, taking into account current market conditions and the current creditworthiness of the counterparty.

### Fair value hierarchy

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

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

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

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

Pursuant to disclosure requirements of IFRS 7 Financial Instruments: Disclosures, the Group has disclosed the relevant information under note 6.2.

### Gains and losses on subsequent measurement

Gains and losses arising from changes in the fair value of the 'financial assets at fair value through profit or loss' category are included in the consolidated statement of income in the period in which they arise.

Gains and losses arising from changes in the fair value of available-for-sale financial assets are recognised in other comprehensive income, until the financial asset is derecognised or impaired at which time the cumulative gain or loss previously recognised in other comprehensive income is reclassified to the consolidated statement of income. In case where the available-for-sale investments with fixed maturity are reclassified to held-to-maturity investments, the fair value gain or loss till the date of the reclassification is held in equity and is amortised to the consolidated statement of income over the remaining life of the held-to-maturity investments using the effective interest rate method.

### Impairment

Financial assets are reviewed at each reporting date to determine whether there is objective evidence of impairment. If any such evidence exists, the asset's recoverable amount is estimated. Impairment loss is the difference between the net carrying value of an asset and its recoverable amount. Any such impairment loss is recognised in the consolidated statement of income. The recoverable amount of loans and advances is calculated as the present value of the expected future cash flows, discounted at the instrument's original effective interest rate. Short-term (up to one year maturity) balances are not discounted.

The Group considers evidence of impairment for loans and advances and held-to-maturity investment securities at both a specific asset and collective level. All individually significant loans and advances and held-to-maturity investment securities are assessed for specific impairment. All individually significant loans and advances and held-to-maturity investment securities found not to be specifically impaired are then collectively assessed for any impairment that has been incurred but not yet identified. Loans and advances and held-to-maturity investment securities that are not individually significant are collectively assessed for impairment by grouping together loans and advances and held-to-maturity investment securities with similar risk characteristics.

If in a subsequent period the amount of an impairment loss decreases and the decrease can be linked objectively to an event occurring after the write down, the write down or allowance is reversed through the consolidated statement of income.

In the case of equity investments classified as available-for-sale, a significant or prolonged decline in the fair value of the security below its cost is considered in determining whether the assets are impaired. If any such evidence exists for available-for-sale investments, the cumulative loss is measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that investment previously recognised in consolidated statement of income, and is removed from the consolidated statement of other comprehensive income and recognised in the consolidated statement of income.

If, in a subsequent period, the fair value of an impaired available-for-sale debt security increases and the increase can be objectively related to an event occurring after the impairment loss was recognised in the consolidated statement of income, the impairment loss is reversed, with the amount of the reversal recognised in the consolidated statement of income.

However, impairment losses recognised in the consolidated statement of income on equity instruments are not reversed through the consolidated statement of income and subsequent increase in fair value is recognised in fair value reserve.

## f. Derivatives

A derivative financial instrument is a financial contract between two parties where payments are dependent upon movements in the price of one or more underlying financial instrument, reference rate or index.

Derivative financial instruments are initially recognised at fair value at trade date, and are subsequently re-measured at fair value at the end of each reporting period. All derivatives are carried at their fair values as assets where the fair values are positive (unrealised gains) and as liabilities where the fair values are negative (unrealised losses). Derivative assets and liabilities arising from different transactions are only offset if the transactions are with the same counterparty, a legal right of offset exists and the parties intend to settle the cash flows on a net basis.

Derivative fair values are determined from quoted prices in active markets where available. Where there is no active market for an instrument, fair value is derived from prices for the derivative's components using appropriate pricing or valuation models.

The method of recognising fair value gains and losses depends on whether derivatives are held for trading or are designated as hedging instruments, and if the latter, the nature of the risks being hedged.

Derivatives may be embedded in another contractual arrangement (a "host contract"). The Group accounts for such embedded derivatives at fair value separately from the host contract when the host contract is not itself carried at fair value through profit or loss, and the characteristics of the embedded derivative are not clearly related to the host contract.

### Hedge accounting

Derivatives designated as hedges are classified as either: (i) hedges of the change in the fair value of recognised assets or liabilities or firm commitments ('fair value hedges'); (ii) hedges of the variability in future cash flows attributable to a particular risk associated with a recognised asset or liability, or a highly probable forecast transaction that could affect future reported net income ('cash flow hedges'); or (iii) a hedge of a net investment in a foreign operation ('net investment hedges'). Hedge accounting is applied to derivatives designated in this way provided certain criteria are met.

At the inception of a hedging relationship, to qualify for hedge accounting, the Group documents the relationship between the hedging instruments and the hedged items as well as its risk management objective and its strategy for undertaking the hedge. The Group prepares a documented assessment, both at hedge inception and on an ongoing basis, of whether or not the hedging instruments, primarily derivatives, that are used in hedging transactions are highly effective in offsetting the changes attributable to the hedged risks in the fair values or cash flows of the hedged items.

### Fair value hedges

Where a hedging relationship is designated as a fair value hedge, the hedged item is adjusted for the change in fair value in respect of the risk being hedged. Gains or losses on the changes in fair value of both the derivative and the hedged item attributable to hedged risk are recognised in the consolidated statement of income and the carrying amount of the hedged item is adjusted accordingly. This applies if the hedged item is otherwise measured at cost. Recognition of the gain or loss attributable to the hedged risk in profit or loss applies if the hedged item is an available-for-sale financial asset. If the derivative expires, is sold, terminated, exercised, no longer meets the criteria for fair value hedge accounting or the designation is revoked, hedge accounting is discontinued. The replacement or rollover of a hedging instrument into another hedging instrument is not an expiration or termination if such replacement or rollover is part of the Group's documented hedging strategy. Any adjustment up to that point to the carrying value of a hedged item, for which the effective interest method is used, is amortised in the consolidated statement of income as part of the recalculated effective interest rate over the period to maturity or derecognition.

### Cash flow hedges

The effective portion of changes in the fair value of derivatives that are designated and qualify as cash flow hedges are recognised in other comprehensive income and accumulated in equity. The gain or loss relating to the ineffective part is recognised immediately in the consolidated statement of income. Amounts accumulated in equity are reclassified from other comprehensive income and transferred to the consolidated statement of income in the periods in which the hedged item affects profit or loss, in the same line of the consolidated statement of income as the recognised hedged item. However, when the forecast transaction that is hedged results in the recognition of a non□financial asset or a non□financial liability, the cumulative gains or losses previously deferred in equity are transferred from equity and included in the initial measurement of the cost of the non□financial asset or non□financial liability. Hedge accounting is discontinued when the Group revokes the hedging relationship, when the hedging instrument expires or is sold, terminated or exercised, or when a hedge no longer meets the criteria for hedge accounting. Any cumulative gains or losses recognised in equity remain in equity until the forecast transaction is recognised, in the case of a non□financial asset or a non□financial liability, or until the forecast transaction affects the consolidated statement of income. If the forecast transaction is no longer expected to occur, the cumulative gains or losses recognised in equity are immediately transferred to the consolidated statement of income from other comprehensive income.

### Hedge effectiveness testing

To qualify for hedge accounting, the Group requires that at the inception of the hedge and through its life, each hedge must be expected to be highly effective (prospective effectiveness) and demonstrate actual effectiveness (retrospective effectiveness) on an ongoing basis.

The documentation of each hedging relationship sets out how the effectiveness of the hedge is assessed. The method the Group adopts for assessing hedge effectiveness depends on its risk management strategy.

For prospective effectiveness, the hedging instrument must be expected to be highly effective in offsetting changes in fair value or cash flows attributable to the hedged risk during the period for which the hedge is designated. For actual effectiveness to be achieved, the changes in fair value or cash flows must offset each other in the range of 80 per cent to 125 per cent. Hedge ineffectiveness is recognised in the consolidated statement of income.

### Derivatives that do not qualify for hedge accounting

All gains and losses from changes in the fair values of derivatives that do not qualify for hedge accounting are recognised immediately in the consolidated statement of income.

## g. Key accounting estimates and judgements

The preparation of the consolidated financial statements requires management to make estimates and assumptions that affect the application of accounting policies and reported amounts of assets, liabilities, income and expenses.

Such estimates are necessarily based on assumptions about several factors involving varying degrees of judgement and uncertainty, and actual results may therefore differ resulting in future changes in these estimates. These disclosures supplement the commentary on financial risk management set out in note 5. In particular, considerable management's judgement is required in the following:

### Impairment losses on loans and receivables and held-to-maturity and available-for-sale investments

The specific counterparty component of the total allowances for impairment applies to financial assets evaluated individually for impairment and is based upon management's best estimate of the present value of the cash flows that are expected to be received. In estimating these cash flows, management makes judgements about a counter party's financial situation and the net realisable value of any underlying collateral.

Each impaired asset is assessed on its merits, and the workout strategy and estimate of cash flows considered recoverable are independently approved by the Credit Risk function. Judgement is also exercised while reviewing factors indicating and determining the objective evidence of impairment in respect of loans and advances and held-to-maturity and available-for-sale investments.

Collectively assessed impairment allowances cover credit losses inherent in portfolios of loans and advances and held-to-maturity investment securities with similar credit risk characteristics when there is objective evidence to suggest that the portfolio contains impaired loans and advances and held-to-maturity investment securities, but the individual impaired items cannot be identified. In assessing the need for collective impairment allowance, management considers factors such as credit quality, portfolio size, concentrations and economic factors.

### Available-for-sale investments

The Group exercises judgement to consider impairment on the available-for-sale investments. This includes determination of whether any decline in the fair value below cost of equity instruments is significant or prolonged. In making this judgement, the Group evaluates among other factors, the normal volatility in market price. In addition, the Group considers impairment to be appropriate when there is evidence of deterioration in the financial health of the investee, industry and sector performance or changes in technology.

### Held-to-maturity investments

The Group follows the guidance of IAS 39 on classifying non-derivative financial assets with fixed or determinable payments and fixed maturity as held-to-maturity. This classification requires significant judgement. In making this judgement, the Group evaluates its intention and ability to hold such investments to maturity.

## h. Due from banks and financial institutions

Amounts due from banks and financial institutions are initially recognised at fair value and measured subsequently at amortised cost using the effective interest method. Impairment of amounts due from banks and financial institutions is assessed as outlined in the accounting policy on financial instruments.

### i. Property and equipment, capital work-in-progress and depreciation

Property and equipment are stated at cost less accumulated depreciation and impairment losses. Cost includes expenditures that are directly attributable to the acquisition of the asset. The cost of replacing an item of property and equipment is recognised in the carrying value of the item if it is probable that the future economic benefits embodied within the part will flow to the Group and its cost can be measured reliably. Depreciation is charged to the consolidated statement of income on a straight line basis over the estimated useful lives of property and equipment. Freehold land is not depreciated.

Where the carrying value of an asset is greater than its estimated recoverable amount, it is written down immediately to its recoverable amount. Gains and losses on disposal are recognised in the consolidated statement of income. The estimated useful lives for various types of assets are as follows:

| | |
|---|---|
| Buildings | 20 to 30 years |
| Leasehold improvements | Over the period of lease |
| Furniture and equipment | 4 years |
| Motor vehicles | 3 years |

Useful life and the depreciation method are re-assessed at each reporting date.

Capital work-in-progress is stated at cost and is transferred to the appropriate asset category when it is brought into use and is depreciated in accordance with the Group's accounting policy.

Software acquired by the Group is stated at cost less accumulated amortisation and impairment losses, if any. Cost of the software represents the costs incurred to acquire and bring the specific software to use.

Amortisation is recognised in the consolidated statement of income on a straight-line basis over the estimated useful life of the software, from the date it is available for use. The useful life of software is estimated to be five years.

### j. Government grants

Land granted by the Government of Fujairah is recorded at nominal value.

### k. Due to banks, term borrowings and customer deposits

Due to banks, term borrowings and customer deposits are initially measured at fair value plus directly attributable transaction costs. Subsequently, these are measured at amortised cost using the effective interest method except where the Group chooses to carry the liabilities at fair value through the consolidated statement of income. Amortised cost is calculated by taking into account any discount or premium on settlement.

### l. Provisions

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

### m. Guarantees

Guarantees are contracts that require the Group to make specified payments to reimburse the holder for a loss it incurs because a specified debtor fails to make payment or provide agreed service when due in accordance with the terms of a debt. Guarantees are recognised at their fair value.

The guarantee liability is subsequently carried at the higher of the amortised cash flow and the best estimate of expenditure required to settle any financial obligation arising as a result of the guarantee.

### n. Employee end of services benefits

Provision is made, in accordance with the provisions of IAS 19, for the end of service benefits due to employees in accordance with the UAE labour law for their periods of service up to the financial position date and the provision arising is disclosed as 'provision for employees' end of service benefits' in the statement of financial position. The Group pays its contributions in respect of UAE citizens under the UAE pension and social security law and no further liability exists.

### o. Interest income and expense

Interest income and expense for all interest bearing financial instruments are recognised in the consolidated statement of income on an accruals basis using the effective interest rates of the financial assets or financial liabilities to which they relate.

The effective interest rate is the rate that discounts estimated future cash receipts and payments earned or paid on a financial asset or a liability through its expected life or, where appropriate, a shorter period to the net carrying amount of the financial asset or financial liability. The effective interest rate is established on initial recognition of the financial asset and liability and is not revised subsequently unless re-priced.

When calculating effective interest rates, the Group estimates cash flows considering all contractual terms of the financial instruments excluding future credit losses. The calculation includes all amounts paid or received by the Group that are an integral part of the effective interest rate, including transaction costs and all other premiums or discounts.

### p. Net fees and commission income

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

Other fees and commission income earned and expense incurred from the provision of services are recognised as revenue and expense, as and when the services are rendered.

### q. Income from investments and Islamic instruments

Gains and losses on investments at fair value through profit or loss, are recognised in the consolidated statement of income.

### r. Dividend income

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

### s. Cash and cash equivalents

For the purposes of the consolidated statement of cash flows, cash and cash equivalents comprise cash on hand and balances with the UAE Central Bank (excluding statutory reserve) and other balances due from (excluding bills discounted) and due to banks maturing within three months. Cash and cash equivalents are carried at amortised cost in the consolidated statement of financial position.

### t. Foreign currencies

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

Non-monetary assets and liabilities denominated in foreign currencies, which are stated at historical cost, are translated at the foreign exchange rate ruling at the date of the transaction. Forward foreign exchange contracts are translated into AED at the mid-market rate of exchange applicable to their maturities ruling at the reporting date. Any resultant gains and losses are recognised in the consolidated statement of income.

### u. Segment reporting

An operating segment is a component of the Group that engages in business activities from which it may earn revenues and incur expenses, including revenues and expenses that relate to transactions with any of the Group's other components. The operating results of each operating segment are reviewed regularly by the management and Chief Executive Officer (together referred to as the "Chief Operating Decision Maker" or "CODM") to make decisions about resources allocated to each segment and assess its performance, and for which discrete financial information is available.

### v. Offsetting

Financial assets and liabilities are offset and the net amount is reported in the consolidated statement of financial position when, and only when, the Group has a legally enforceable right to set off the recognised amounts and it intends either to settle on a net basis or to realise the asset and settle the liability simultaneously.

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

### w. Earnings per share

The Group presents basic and diluted earnings per share (EPS) data for its ordinary shares. Basic EPS is calculated by dividing the profit or loss attributable to ordinary shareholders of the Group by the weighted average number of ordinary shares outstanding during the year. Diluted EPS is determined by adjusting the profit or loss attributable to ordinary shareholders and the weighted average number of ordinary shares outstanding for the effects of all dilutive potential ordinary shares.

### x. Impairment of non-financial assets

The carrying amounts of the Group's non-financial assets are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists then the asset's recoverable amount is estimated based on the higher of fair value less costs to sell and value in use. The reduction in carrying amount is recognised in the consolidated statement of income.

### y. Operating leases

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

### z. Acceptances

Acceptances have been considered within the scope of IAS 39 - Financial Instruments: Recognition and Measurement and are recognised as a financial liability in the consolidated statement of financial position with a contractual right of reimbursement from the customer as a financial asset. Therefore, commitments in respect of acceptances have been accounted for as financial assets and financial liabilities.

## aa. Islamic financing receivables, Islamic instruments and Islamic customer deposits

The Group engages in Shari'a compliant Islamic banking activities through a window called "NBF Islamic". The Islamic operations were launched in 2014 and the various Islamic instruments described below are accounted for, disclosed and presented in accordance with the requirements of the underlying substance of the instruments and IFRS/IAS/IFRIC.

### Murabaha

Murabaha receivables are non-derivative financial assets with fixed payments that are not quoted in an active market. Murabaha is a sale transaction in which the seller (Group) expressly mentions the actual cost of the asset to be sold to the customer, and sells it to the customer on a cost plus mark-up (profit) basis. It is in fact the sale of an asset for a profit, usually on deferred payment basis.

Income on Murabaha financing is recognised on a time apportioned basis over the period of the Murabaha contract, using the effective profit rate method.

### Ijara

Ijara involves a contract where the Group buys and then leases an item to a customer for a specified rental over a specific period. The duration of lease, as well as the basis for rental, are set and agreed in advance. The Group acquires the beneficial ownership of the property to lease the usufruct to the customer.

Income on Ijara financing is recognised on a time apportioned basis over the lease term, using the effective profit rate method.

### Qard

A Qard is the transfer of ownership in tangible wealth (money), from the customer to the Group, and it is binding on the Group to return equal wealth (money) to the customer on demand or as per the agreed terms, which means that the principal is to be repaid on demand. The Islamic current account offered to customers is based on the concept of Qard, a profit free amount received from the customer to the Group, on which no profit or other form of return is payable.

### Sukuk

Certificates of equal value representing undivided shares in ownership of tangible assets, usufructs and services or (in the ownership of) the assets of particular projects or special investment activity. It is an asset backed trust certificate evidencing ownership of an asset or its usufruct (earnings or benefits) and complies with the principle of Shari'a.

### Wa'ad – Structured Shari'a hedging product

Islamic Swaps are based on a Wa'ad (promise) structure between two parties to buy a specified Shari'a compliant commodity at an agreed price on the relevant date in future. It is a conditional promise to purchase a commodity through a unilateral purchase undertaking. Islamic swap structure comprises profit rate swap and currency swap. For profit rate swaps, counterparties generally exchange fixed and floating rate profit payments by executing the purchase/sale of commodity under "Murabaha Sale Agreement" in a single currency.

### Wakala

Wakala involves an agreement, based on the concept of ***Wakala Bil Istithmar,*** where the Group becomes the investment agent *(Wakil)* for its customers *(Muwakkil)* for deposit of their funds in the Wakala investment account to be invested in Shari'a compliant investment instruments. The funds are used to generate profit for the customer by investing in Islamic financing facilities to the Group's other customers or investing in other Shari'a compliant investment instruments.

Income generated from the financing and investment activities are paid to the customers and the Group recognises income in the form of a fixed Wakala fee. Where the income generated exceeds the anticipated profit rate, the Group recognises income in the form of performance fee.

### Istisna' forward Ijara

Istisna' with forward Ijara structure involves an agreement which provides the customer with financing for building and construction of a Shari'a compliant asset; qualifying for an ijara transaction. This broadly includes the condition that the asset should have an identified usufruct and is non-consumable. Although, the asset does not exist in its final form at the signing of the contract, the exact details and specifications of the asset shall be clearly described in both the Istisna' and forward ijara documents.

Income on Istisna' forward Ijara financing is recognised on a time apportioned basis over the lease term, using the effective profit rate method.

## 5. Financial Risk Management

### a. Introduction

Risk is inherent in the Group's activities and is managed through a process of ongoing identification, measurement, mitigation, reporting and monitoring. The Group's exposure can be broadly categorised into the following risks:

- Credit risk
- Liquidity risk
- Market risk
- Operational risk

The Group enhances its risk management culture, practices and processes proactively on an ongoing basis. The bank has implemented the Basel II Internal Ratings Based (IRB) Approach which is used for internal risk management; while regulatory guidelines are awaited to complete the process for use in regulatory capital calculations.

The bank follows both the IRB Approach and Standardised Approach for its risk and capital management. In addition, the bank is also exposed to other risks that are managed along with the key risks, and are quantified, monitored and reported as part of the NBF's Internal Capital Adequacy Assessment Process (ICAAP) Framework. Such risks include, among others, concentration risk, strategic risk, business risk, and legal and compliance risk. The ICAAP covers these approaches and a detailed report is submitted to the UAE Central Bank on an annual basis after being approved by the Board. Work is also in progress for complying with Basel III requirements. The Group is always committed to the implementation of best practices and governance standards.

### b. Governance and risk management framework

This note presents broad information about the Group's objectives, policies and processes for identifying, measuring, reporting and mitigating the above mentioned risks and the Group's management of capital. This note also covers enhanced disclosures relating to Pillar 3 (Market Discipline) of Basel II.

The Board of Directors has overall responsibility for the establishment and oversight of the Group's enterprise risk management framework. The Board sets the overall risk appetite and strategy in consultation with the senior management and approves all principal governance committee charters, policies and guidelines to manage the above mentioned risks. The Board has established committees, as detailed in the Corporate Governance Report, to enhance the oversight mechanism to carry out its responsibilities effectively.

#### Enterprise-wide Risk Management and Internal Control Framework

The Board sets the risk appetite, policies and the enterprise-wide risk management and internal control framework. The bank follows a three lines of defence structure with management control being the first, independent risk management oversight being the second and an independent audit assurance being the third. The principal responsibility for the execution and implementation of policies and procedures and internal controls rests with respective functions and departments in accordance with the approved framework. An independent Risk Management function carries out the oversight through independent review and approval of procedures, spot checks to assess adequacy of internal controls and meeting of compliance requirements, operational risk management, credit review and middle office activities for market and liquidity risks. An independent internal and external audit process provides an independent assurance to the Board.

The Group follows the Board approved whistle blowing policy where staff, customers and other stakeholders of the bank can independently raise matters to the Chief Executive Officer (CEO), the Head of Internal Audit or the Board Secretary. The Group through the Grievance and Disciplinary Committee (GDC) comprising Head of Human Resources, Chief Operations Officer, Head of Corporate & Institutional Banking and Head of Treasury, and reporting to the CEO promotes transparent and fair dealings among staff.

The role of the Internal Audit Function within the Group is to provide independent and objective assurance that the process for identifying, evaluating and managing significant risks faced by the Group is appropriate and effectively applied. In addition, it also provides an independent check on the compliance with laws and regulations and measuring compliance with the Group's policies and procedures. Additionally, Internal Audit provides consulting services which are advisory in nature, and are generally performed at the specific request of the Senior Management. It is led by the Head of Internal Audit who reports to the Audit Committee of the Board, with administrative reporting line to the CEO. To perform its role effectively, Internal Audit has organisational independence from management, to enable unrestricted evaluation of management activities and personnel.

### c. Credit risk

Credit risk is the risk of financial loss to the Group if a customer or counterparty to a financial instrument fails to meet its contractual obligations, and arises principally from the Group's loans and advances and Islamic financing receivables to customers and amounts due from banks and investments portfolio.

The Group is mainly engaged in Corporate and Institutional Banking business which comprises the majority of loans and advances and Islamic financing receivables of the Group and has also been growing its Retail Banking loans and advances and Islamic financing receivables. The credit is assessed based on specific guidelines which are reviewed and approved by the Board Risk Committee and the Board.

### Management of credit risk

An independent Credit Department is responsible for reviewing, recommending and approving underwriting proposals and together with Risk Management Department is responsible for managing credit risk and formulation of credit policies in line with strategic objectives, risk appetite, business growth, regulatory requirements and risk management standards. An independent loan and financing review function within Risk Management Division is responsible for loan and financing review, on a post facto and sample basis, to assess compliance with underwriting approvals according to the policies and review the underwriting standards of the Group. Further, Risk department is also responsible for undertaking a portfolio review of credit risks/quality. Independent departments are responsible for documentation, collateral management, custody and limit management, and audit review of the process is undertaken.

The credit risk management framework includes:

- Risk appetite and policy setting;
- An authorisation structure and limits for the approval and renewal of credit facilities;
- Review and assessment of credit applications in line with credit policies and within the authorisation and limit structure. Renewals of facilities are subject to the same review process;
- Diversification and limiting concentrations of exposure to counterparties, geographies, industries and asset classes;
- Reviewing compliance, on an ongoing basis, with agreed exposure limits relating to counterparties, industries, countries and products and reviewing limits in accordance with the risk management strategy and market trends;
- Remedial management and recoveries; and
- Stress testing.

### Concentration risk

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 Group’s performance to developments affecting a particular industry or geographical location.

In order to avoid excessive concentration of risk, Group risk policies and procedures include specific guidelines to ensure maintenance of diversified portfolios through a series of country, counterparty, industry, sector and product limits.

Credit exposures to individual customers or customer groups are controlled through a tiered hierarchy of delegated approval authorities. Approval is required from the UAE Central Bank for exposures which are likely to exceed single counterparty/group limit(s), keeping in view the regulatory capital base, in accordance with the regulations of monitoring of large exposure limits issued by the UAE Central Bank.

The Group monitors concentrations of credit risk by industry, sector and geographic location. The Group has further defined portfolio caps for its specialised businesses like Marine and Energy and Precious metals/ stones segments.

The tables on the following pages illustrate the sectoral, geographical and currency-wise analysis of loans and advances and Islamic financing receivables. Information about other areas of credit risk is included in the respective notes to the consolidated financial statements.

### Sector analysis

An analysis of sector concentrations of credit risk arising from loans and advances and Islamic financing receivables at 31 December 2016 and 2015 is shown below:

**Loans and advances and Islamic financing receivables**

| 2016 | Funded AED'000 | Unfunded AED'000 | Gross exposure AED'000 | Impaired loans and financing receivables AED'000 | Specific provision AED'000 | Write-off (funded) AED'000 | Past due but not Impaired | |
|---|---|---|---|---|---|---|---|---|
| | | | | | | | Up to 90 days AED'000 | Above 90 days AED'000 |
| Trade | 11,302,590 | 1,946,865 | 13,249,455 | 376,225 | 226,644 | 126,543 | 164,244 | 3,225 |
| Construction | 1,267,537 | 3,442,385 | 4,709,922 | 61,412 | 45,973 | 6,993 | 6,357 | - |
| Government | 283,972 | 6,310 | 290,282 | - | - | - | - | - |
| Manufacturing | 4,151,479 | 748,954 | 4,900,433 | 194,288 | 113,696 | 91,182 | 142,725 | - |
| Financial institutions | 635,414 | 178,644 | 814,058 | 67,337 | 41,368 | 133 | - | - |
| Service industries | 2,993,571 | 250,644 | 3,244,215 | 387,739 | 186,184 | 5,387 | 13,091 | - |
| Real estate | 1,871,196 | - | 1,871,196 | 18,874 | 5,539 | - | 4,880 | - |
| Individuals | 1,517,638 | 328,284 | 1,845,922 | 83,121 | 52,669 | 24,606 | 2,084 | - |
| **Gross amount** | **24,023,397** | **6,902,086** | **30,925,483** | **1,188,996** | **672,073** | **254,844** | **333,381** | **3,225** |

**Loans and advances and Islamic financing receivables**

| 2015 | Funded AED'000 | Unfunded AED'000 | Gross exposure AED'000 | Impaired loans and financing receivables AED'000 | Specific provision AED'000 | Write-off (funded) AED'000 | Past due but not impaired | |
|---|---|---|---|---|---|---|---|---|
| | | | | | | | Up to 90 days AED'000 | Above 90 days AED'000 |
| Trade | 8,953,114 | 1,885,974 | 10,839,088 | 274,846 | 173,647 | 60,843 | 152,515 | - |
| Construction | 1,160,004 | 3,418,925 | 4,578,929 | 66,982 | 52,810 | - | 48,780 | - |
| Government | 275,039 | 3,895 | 278,934 | - | - | - | - | - |
| Manufacturing | 4,014,217 | 826,128 | 4,840,345 | 184,260 | 148,410 | 14,748 | 101,694 | - |
| Financial institutions | 562,291 | 259,868 | 822,159 | 67,482 | 40,888 | 1,879 | - | - |
| Service industries | 2,467,638 | 194,688 | 2,662,326 | 293,306 | 153,140 | - | 3,823 | - |
| Real estate | 1,863,341 | - | 1,863,341 | 13,618 | 1,559 | - | 1,300 | - |
| Individuals | 1,446,915 | 55,355 | 1,502,270 | 78,670 | 54,576 | 1,264 | 1,727 | - |
| **Gross amount** | **20,742,559** | **6,644,833** | **27,387,392** | **979,164** | **625,030** | **78,734** | **309,839** | **-** |

5. Financial Risk Management (continued)
c. Credit risk (continued)

### Geographic location analysis

Based on the location of the borrower, an analysis of geographic concentrations of credit risk arising out of loans and advances and Islamic financing receivables at 31 December 2016 and 2015 is shown below:

| 2016 | Funded AED'000 | Unfunded AED'000 | Gross exposure AED'000 | Impaired loans and financing receivables AED'000 | Specific provision AED'000 | Write-off (funded) AED'000 | Past due but not Impaired | |
|---|---|---|---|---|---|---|---|---|
| | | | | | | | Up to 90 days AED'000 | Above 90 days AED'000 |
| Within UAE | 23,350,217 | 6,749,977 | 30,100,194 | 1,121,659 | 630,705 | 254,844 | 264,388 | 3,225 |
| GCC countries | 163,507 | 79,255 | 242,762 | 67,337 | 41,368 | - | 7,011 | - |
| Other | 509,673 | 72,854 | 582,527 | - | - | - | 61,982 | - |
| **Total** | **24,023,397** | **6,902,086** | **30,925,483** | **1,188,996** | **672,073** | **254,844** | **333,381** | **3,225** |

| 2015 | Funded AED'000 | Unfunded AED'000 | Gross exposure AED'000 | Impaired loans and financing receivables AED'000 | Specific provision AED'000 | Write-off (funded) AED'000 | Past due but not impaired | |
|---|---|---|---|---|---|---|---|---|
| | | | | | | | Up to 90 days AED'000 | Above 90 days AED'000 |
| Within UAE | 20,213,457 | 6,366,617 | 26,580,074 | 911,217 | 583,677 | 76,855 | 309,839 | - |
| GCC countries | 111,704 | 18,114 | 129,818 | 67,349 | 40,755 | 1,879 | - | - |
| Other | 417,398 | 260,102 | 677,500 | 598 | 598 | - | - | - |
| **Total** | **20,742,559** | **6,644,833** | **27,387,392** | **979,164** | **625,030** | **78,734** | **309,839** | **-** |

### Currency-wise analysis

The Group's credit exposure by currency type is as follows:

| | 2016 | | | 2015 | | |
|---|---|---|---|---|---|---|
| | Funded AED'000 | Unfunded AED'000 | Gross exposure AED'000 | Funded AED'000 | Unfunded AED'000 | Gross exposure AED'000 |
| AED | 19,070,600 | 5,046,325 | 24,116,925 | 17,276,636 | 4,793,885 | 22,070,521 |
| USD | 3,581,000 | 1,574,762 | 5,155,762 | 2,765,437 | 1,549,102 | 4,314,539 |
| EUR | 33,201 | 155,254 | 188,455 | 32,552 | 189,655 | 222,207 |
| GBP | 271,947 | 4,729 | 276,676 | 1,453 | 12,320 | 13,773 |
| XAU | 1,056,631 | - | 1,056,631 | 657,603 | - | 657,603 |
| Others | 10,018 | 121,016 | 131,034 | 8,878 | 99,871 | 108,749 |
| **Total** | **24,023,397** | **6,902,086** | **30,925,483** | **20,742,559** | **6,644,833** | **27,387,392** |

### Settlement risk

The Group's activities may give rise to risk at the time of settlement of transactions and trades. Settlement risk is the risk of loss due to the failure of the counterparty to honour its obligations to deliver cash, securities or other assets as contractually due. Any delays in settlement are monitored and quantified as part of the Group's Credit Risk Management.

For certain types of transactions, the Group mitigates this risk by conducting settlements through a settlement/clearing agent to ensure that a trade is settled only when both parties have fulfilled their contractual settlement obligations. Settlement limits form part of the credit approval/limit monitoring process. Acceptance of settlement risk on free settlement trades requires transaction specific or counterparty specific approvals in accordance with the approved credit framework.

### Risk mitigation, collateral and credit enhancements

The Group manages credit exposure by obtaining security where appropriate, and in certain cases, the Group may also close out transactions or assign them to other counterparties to mitigate credit risk.

The amount and type of collateral depends on assessments of the credit risk of the counterparty. The types of collateral mainly include cash, guarantees, pledge over listed shares and mortgage and liens over properties or other securities over assets. Pledged interests over vehicles, ships and equipment are also obtained. Collateral generally is not held against non-trading investments and due from banks and financial institutions.

Management monitors the market value of collateral, and wherever necessary the Group requests additional collateral in accordance with the underlying agreement, and considers collateral obtained during its review of the adequacy of the allowance for impairment losses.

Estimates of fair value are generally assessed on a periodic basis in accordance with the respective credit policies. An estimate of fair value of collateral and other security enhancements held against the loan and Islamic financing portfolio is shown below:

| Particulars | Loans and advances and Islamic financing receivables | | Collaterals | |
|---|---|---|---|---|
| | 2016 AED'000 | 2015 AED'000 | 2016 AED'000 | 2015 AED'000 |
| **Individually impaired** | | | | |
| Pledged deposits | 189,791 | 82,945 | 8,215 | 6,515 |
| Debt/Equity securities | 2,137 | 2,137 | 2,137 | 2,137 |
| Property | 225,892 | 115,692 | 213,009 | 104,065 |
| Others | 771,176 | 778,390 | - | - |
| **Gross amount** | **1,188,996** | **979,164** | **223,361** | **112,717** |
| **Impairment loss** | **(672,073)** | **(625,030)** | **-** | **-** |
| **Carrying amount** | **516,923** | **354,134** | **223,361** | **112,717** |
| **Past due but not impaired** | | | | |
| Pledged deposits | 84,056 | 153,727 | 22,110 | 32,731 |
| Debt/Equity securities | - | - | - | - |
| Property | 127,757 | 85,200 | 59,858 | 29,508 |
| Others | 124,793 | 70,912 | - | - |
| **Gross amount** | **336,606** | **309,839** | **81,968** | **62,239** |
| **Impairment loss** | **-** | **-** | **-** | **-** |
| **Carrying amount** | **336,606** | **309,839** | **81,968** | **62,239** |

| Particulars | Loans and advances and Islamic financing receivables | | Collaterals | |
|---|---|---|---|---|
| | 2016 AED'000 | 2015 AED'000 | 2016 AED'000 | 2015 AED'000 |
| **Neither past due nor impaired** | | | | |
| Pledged deposits | 6,980,559 | 6,587,203 | 2,138,612 | 2,030,712 |
| Debt/Equity securities | 100,331 | 42,356 | 100,331 | 42,356 |
| Property | 6,320,051 | 4,376,047 | 5,111,106 | 3,635,645 |
| Others | 9,096,854 | 8,447,950 | - | - |
| **Gross amount** | **22,497,795** | **19,453,556** | **7,350,049** | **5,708,713** |
| **Collective impairment provision** | **(532,828)** | **(429,193)** | **-** | **-** |
| **Carrying amount** | **21,964,967** | **19,024,363** | **7,350,049** | **5,708,713** |
| **Total** | **22,818,496** | **19,688,336** | **7,655,378** | **5,883,669** |
| **Renegotiated exposure** | **2,155,114** | **1,478,744** | **911,334** | **546,273** |
| **Contingent liabilities** | | | | |
| Pledged deposits | 3,695,335 | 3,360,146 | 424,955 | 449,139 |
| Others | 3,206,751 | 3,284,687 | 441,200 | 312,974 |
| **Total** | **6,902,086** | **6,644,833** | **866,155** | **762,113** |

Past due but not impaired portfolio ageing is as follows:

| | 2016 AED'000 | 2015 AED'000 |
|---|---|---|
| Less than 1 month | 284,738 | 186,149 |
| 1 month to 3 months | 48,643 | 123,690 |
| Greater than 3 months | 3,225 | - |
| **Total** | **336,606** | **309,839** |

## Credit quality

The credit quality of the loans and advances and Islamic financing receivables is managed by the Group using internal credit ratings comprising 22 grades. The risk rating system is used as a credit risk management tool whereby any risks taken on the Group's books are rated against a set of predetermined standards which also complies with the UAE Central Bank guidelines.

The Group's Credit Risk Rating Methodology follows the categorisation of credit risk assets under the following risk classification/grading system:

| Risk Grade | 2016 AED'000 | 2015 AED'000 |
|---|---|---|
| **Neither past due nor impaired/Past due but not impaired (RR 1-19)** | | |
| Grades 1-18: Performing or normal | 21,886,109 | 19,074,966 |
| Grade 19: Other Loans Especially Mentioned (OLEM) | 948,292 | 688,429 |
| | **22,834,401** | **19,763,395** |
| **Individually impaired (RR 20-22)** | | |
| Grade 20: Sub-standard | 423,463 | 167,231 |
| Grade 21: Doubtful | 411,332 | 460,743 |
| Grade 22: Loss | 354,201 | 351,190 |
| | **1,188,996** | **979,164** |
| **Total** | **24,023,397** | **20,742,559** |

### Impaired loans and advances and Islamic financing receivables

Impaired loans and advances and Islamic financing receivables are those financial assets where it is probable that the Group will be unable to collect all principal, interest and profit due according to the contractual terms of the loan and financing agreements.

### Past due but not impaired loans and advances and Islamic financing receivables

Loans and advances and Islamic financing receivables are recognised as past due but not impaired where contractual interest and profit or principal payments are past due but the Group believes that the assets are not impaired on the basis of the level of security/collateral available and/or the stage of collection of amounts owed to the Group.

### Loans and advances and Islamic financing receivables with renegotiated terms

Loans and advances and Islamic financing receivables with renegotiated terms are loans and advances and Islamic financing receivables that have been rescheduled/restructured generally due to deterioration in the borrowers'/financed parties' financial position and where the Group has made concessions that it would not otherwise consider. These loans and advances and Islamic financing receivables are not delinquent; however, impairment is recognised in accordance with IAS 39 to represent the benefits foregone by the Group. The impairment recognised will be gradually unwound to the consolidated statement of income in a manner that corresponds to the performance of the account in line with the restructuring terms.

### Allowances for impairment

The bank is working towards the adoption and implementation of IFRS 9 to ensure compliance with its requirements from the effective date (implementation progress/details covered in the risk management section [page 12] of the Directors' Report 2016). The initial quantitative impact assessment has been submitted to the UAE Central Bank in accordance with the prescribed guidelines.

On a monthly basis, the Group establishes an allowance for impairment losses that represents its estimate of losses in the loans and advances and Islamic financing receivables. The main components of this allowance are a specific loss component that relate to individually significant exposures, and a collective loss allowance established for groups of homogenous assets in respect of losses that may have been incurred but have not been identified on loans and advances and Islamic financing receivables subject to individual assessment for impairment; and the general provision on total credit risk weighted assets in line with the UAE Central Bank's requirements. The methods of assessment of allowances for impairment have been summarised in note 4.

As part of the IRB approach, the bank has designed and implemented an independently validated master credit rating scale, corporate banking rating scale and business banking rating scale linked to the observed historical defaults in the bank's credit portfolio through the cycle which has determined the mean probability of default for the credit portfolio and have assigned individual probabilities of default to each credit risk grade. Together with the Exposure at Default and Loss Given Default, the bank determines the Expected Loss of each of its corporate and commercial borrower. In order to monitor the risk migration of its borrowers, the bank computes the one year credit default migration through transitional matrices while ensuring that the potential impact of the one year default is adequately covered by the overall credit provisioning level and the capital adequacy level.

### Write-off policy

The Group writes off loans and advances and Islamic financing receivables balances (and any related allowances for impairment losses) when it has generally exhausted all possible efforts for collection and determines that the loans and advances and Islamic financing receivables are no longer collectible.

## d. Liquidity risk

Liquidity risk is the risk that the Group will encounter difficulty in meeting its obligations associated with financial liabilities that are settled by delivering cash or another financial asset. It includes the risk of inability to fund assets at appropriate maturities and rates, and inability to liquidate assets at a reasonable price and in an appropriate time frame, and inability to meet obligations as they become due. Liquidity risk can be caused by market disruptions or credit downgrades which may cause certain sources of funding to diminish.

### Management of liquidity risk

The Group's approach to managing liquidity is to maintain, as far as possible, sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or putting the Group's reputation at risk.

Treasury is entrusted with the responsibility of ensuring compliance with both statutory liquidity requirements and internal risk limits. All liquidity risk management policies and procedures are subject to review and approval by Asset and Liability Committee (ALCO), Management Risk Committee (RC), Risk Committee of the Board and the Board.

The Group maintains a portfolio of short-term liquid assets, largely made up of cash and balances with the UAE Central Bank representing **19.0%** (2015: 15.0%) of total assets which also include mandatory cash reserve deposits with the UAE Central Bank. Short-term liquid assets also include investment grade marketable securities, due from banks and financial institutions and other inter-bank facilities, to ensure that sufficient liquidity is maintained both under normal conditions and simulated stress scenarios.

The Group uses lending to stable resource ratio (LSRR) of 1:1 and eligible liquid assets ratio (ELAR) of 10%, which represents high quality liquid assets as stipulated by the UAE Central Bank, as key risk indicators and monitors them on a regular basis. The Group uses more prudent internal LSRR measure of 0.925:1 as a trigger point for action planning. During the year, these ratios were prudently managed:

| | ELAR | | LSRR | |
|---|---|---|---|---|
| | 2016 | 2015 | 2016 | 2015 |
| 12 month - Average | 20.36% | 17.67% | 87.18% | 87.11% |
| 12 month - Highest | 23.25% | 20.90% | 90.06% | 92.22% |
| 12 month - Lowest | 17.20% | 15.91% | 84.85% | 83.96% |

The Group manages its concentration of deposits by continuing to widen the customer base and sources of liabilities and setting in place caps on individual size and varying maturities.

Liquidity positions, key risk indicators and actions are discussed at ALCO to monitor and review achievement of short and long term liquidity strategies and thresholds.

Liquidity risk appetite is prudently and proactively reviewed taking into consideration the market events and relevant risk management standards. Adherence to the longer stress period is being achieved through reliance on both higher quality and adequate level of liquid assets. The Group monitors 30 days stress test under two scenarios of local market crisis and one/two notch downgrade of NBF Issuer Credit Rating in line with its liquidity risk appetite. The bank has also defined a contingency funding plan to manage any liquidity crisis situation.

As part of the ICAAP, the bank assesses the impact on capital adequacy of liquidity risk including concentrations by carrying out stress tests. In preparation for compliance with Basel III requirements, the Group has implemented a system for calculating Liquidity Coverage Ratio (LCR) and Net Stable Funding Ratio (NSFR) in line with the UAE Central Bank's regulations and is working on strengthening processes and qualitative requirements proactively. At 31 December 2016, LCR and NSFR stood at 182% and 103% respectively.

The table below shows the Group's assets and liabilities and commitments on the basis of their earliest possible contractual maturity and/or expected date of settlement or realisation. For example, demand deposits from customers are expected to maintain a stable balance and term deposits are often rolled over on maturity. Loans and advances and Islamic financing receivables are partly revolving in nature. Cash and balances with the UAE Central Bank include certificates of deposit which are readily convertible into cash under repurchase arrangements with the UAE Central Bank. Investments portfolio include available-for-sale investments which can be redeemed before their contractual maturity.

**At 31 December 2016**

| | Less than 1 month AED'000 | 1 month to 3 months AED'000 | Over 3 months to 6 months AED'000 | Over 6 months to 1 year AED'000 | Over 1 year to 5 years AED'000 | Over 5 years AED'000 | Total AED'000 |
|---|---|---|---|---|---|---|---|
| Cash and balances with the UAE Central Bank | 3,405,092 | 1,000,000 | 1,150,000 | 1,150,000 | 75,000 | - | 6,780,092 |
| Due from banks and financial institutions | 1,046,077 | 682,198 | 407,599 | 5,238 | 1,578 | - | 2,142,690 |
| Investments and Islamic instruments | 74,341 | 115,072 | 42,100 | 114,952 | 1,367,915 | 71,899 | 1,786,279 |
| Loans and advances and Islamic financing receivables | 5,319,473 | 5,108,134 | 2,164,384 | 1,435,351 | 6,538,730 | 2,252,424 | 22,818,496 |
| Property and equipment and capital work-in-progress | - | - | - | - | - | 151,795 | 151,795 |
| Other assets | 473,948 | 1,089,417 | 390,398 | 21,337 | 13,667 | - | 1,988,767 |
| **Total assets** | **10,318,931** | **7,994,821** | **4,154,481** | **2,726,878** | **7,996,890** | **2,476,118** | **35,668,119** |
| | | | | | | | |
| Due to banks | 682,691 | 412,924 | 2,831 | 11,595 | - | - | 1,110,041 |
| Customer deposits and Islamic customer deposits | 11,863,721 | 5,154,468 | 3,439,690 | 3,706,976 | 1,763,636 | 10,000 | 25,938,491 |
| Term borrowings | - | 680,554 | 110,190 | 109,860 | 606,045 | 400,000 | 1,906,649 |
| Other liabilities | 473,948 | 1,234,532 | 390,398 | 21,337 | 13,667 | - | 2,133,882 |
| Total shareholders' equity | - | - | - | - | - | 4,579,056 | 4,579,056 |
| **Total liabilities and shareholders' equity** | **13,020,360** | **7,482,478** | **3,943,109** | **3,849,768** | **2,383,348** | **4,989,056** | **35,668,119** |
| **On Balance Sheet Gap** | **(2,701,429)** | **512,343** | **211,372** | **(1,122,890)** | **5,613,542** | **(2,512,938)** | **-** |
| **Cumulative Gap** | **(2,701,429)** | **(2,189,086)** | **(1,977,714)** | **(3,100,604)** | **2,512,938** | **-** | **-** |

### At 31 December 2015

| | Less than 1 month AED'000 | 1 month to 3 months AED'000 | Over 3 months to 6 months AED'000 | Over 6 months to 1 year AED'000 | Over 1 year to 5 years AED'000 | Over 5 years AED'000 | Total AED'000 |
|---|---|---|---|---|---|---|---|
| **Total assets** | **8,681,440** | **6,175,868** | **4,296,139** | **2,579,550** | **6,377,792** | **1,922,367** | **30,033,156** |
| **Total liabilities and shareholders' equity** | **9,916,223** | **5,342,056** | **5,377,933** | **2,191,589** | **2,525,738** | **4,679,617** | **30,033,156** |
| **On Balance Sheet Gap** | **(1,234,783)** | **833,812** | **(1,081,794)** | **387,961** | **3,852,054** | **(2,757,250)** | **-** |
| **Cumulative Gap** | **(1,234,783)** | **(400,971)** | **(1,482,765)** | **(1,094,804)** | **2,757,250** | **-** | **-** |

The table below incorporates guarantees, letters of credit and notional amounts of derivative financial instruments, entered into by the Group, outstanding at the date of consolidated statement of financial position, analysed by the earliest period these can be called. The notional amount is the basis upon which changes in the value of derivatives are measured. The notional amounts indicate the volume of transactions outstanding at the year end and are not indicators of either the market risk or the credit risk. The amounts set out below do not represent expected cash flows.

### At 31 December 2016

| | Less than 1 month AED'000 | 1 month to 3 months AED'000 | Over 3 months to 6 months AED'000 | Over 6 months to 1 year AED'000 | Over 1 year to 5 years AED'000 | Over 5 years AED'000 | Total AED'000 |
|---|---|---|---|---|---|---|---|
| Guarantees | 5,195,822 | - | - | - | - | - | 5,195,822 |
| Letters of credit | 201,786 | 705,155 | 361,327 | 90,587 | 347,409 | - | 1,706,264 |
| Forward foreign exchange contracts | 6,893,449 | 3,388,719 | 2,398,557 | 1,517,651 | 110,268 | - | 14,308,644 |
| Currency options | 206,258 | 447,713 | 72,249 | 759,343 | 3,966,840 | - | 5,452,403 |
| Interest rate derivatives | 222 | 14,998 | 1,010 | - | 2,810,322 | 1,619,815 | 4,446,367 |
| Commodity derivatives | 19,253 | 534,540 | 3,919 | 14,145 | 21,796 | - | 593,653 |
| | **12,516,790** | **5,091,125** | **2,837,062** | **2,381,726** | **7,256,635** | **1,619,815** | **31,703,153** |

**At 31 December 2015**

| | Less than 1 month AED'000 | 1 month to 3 months AED'000 | Over 3 months to 6 months AED'000 | Over 6 months to 1 year AED'000 | Over 1 year to 5 years AED'000 | Over 5 years AED'000 | Total AED'000 |
|---|---|---|---|---|---|---|---|
| Guarantees | 5,318,574 | - | - | - | - | - | 5,318,574 |
| Letters of credit | 214,051 | 722,966 | 243,227 | 96,961 | 49,054 | - | 1,326,259 |
| Forward foreign exchange contracts | 1,834,838 | 1,369,315 | 2,498,960 | 2,314,233 | - | - | 8,017,346 |
| Currency options | 13,442 | 54,678 | 155,340 | 669,583 | - | - | 893,043 |
| Interest rate derivatives | - | - | - | 186,095 | 1,169,099 | 1,292,407 | 2,647,601 |
| Commodity derivatives | 225,319 | 610,905 | 36,662 | 82,248 | - | - | 955,134 |
| | **7,606,224** | **2,757,864** | **2,934,189** | **3,349,120** | **1,218,153** | **1,292,407** | **19,157,957** |

The positive/negative fair values of derivative financial instruments, entered into by the Group, at the reporting date are depicted below:

| | **2016** | | | **2015** | | |
|---|---|---|---|---|---|---|
| | Positive fair value AED'000 | Negative fair value AED'000 | Net AED'000 | Positive fair value AED'000 | Negative fair value AED'000 | Net AED'000 |
| **Derivatives** | | | | | | |
| Forward foreign exchange contracts | 61,284 | 55,790 | 5,494 | 19,937 | 19,479 | 458 |
| Currency options | 18,511 | 17,211 | 1,300 | 4,593 | 4,593 | - |
| Interest rate derivatives | 37,127 | 35,418 | 1,709 | 23,565 | 20,870 | 2,695 |
| Commodity derivatives | 25,874 | 23,443 | 2,431 | 72,110 | 52,476 | 19,634 |
| | **142,796** | **131,862** | **10,934** | **120,205** | **97,418** | **22,787** |

## e. Market risk

Market risk is the risk that changes in market prices, such as interest rate, equity prices, foreign exchange rates, commodity prices and credit spreads will affect the Group's income and/or the value of its holdings of financial instruments.

### Management of market risks

The Group distinguishes its exposure to market risk between trading and non-trading portfolios. Trading portfolio includes positions arising from market-making, proprietary positions and other marked-to-market positions so designated. Non-trading portfolio includes positions other than those with the trading intent that arises from interest rate management of the Group's assets and liabilities and available-for-sale and held-to-maturity investments.

The Group has well-defined policies, procedures and trading limits in place to ensure oversight of Treasury's day-to-day operations, in accordance with the Board's defined risk appetite. These are reviewed periodically to ensure that they remain in line with the Group's general market risk appetite. The Group manages market risk positions within the risk management limits set out by the Board. Overall responsibility for monitoring market risk is vested with the RC.

### Investment price risk

The risk originates primarily from the investment portfolio of the Group which is managed on a fair value basis. The Group manages the risk through diversification of investments in terms of counterparty, industry and country. The Group monitors and reviews portfolio performance on a monthly basis.

Investment Committee (IC) reviews sensitivity of investment price volatility on annualised income. The overall stop loss limit is set at 15% of the purchase price or last year end price, whichever is recent. When the loss reaches 10%, IC shall escalate to RC to decide the strategy of either holding the investment or its disposal. Any loss in excess of 15% will be escalated to the Board.

The table below shows the impact of decline in fair value of investments by 10% on net income and regulatory capital for 2016 and 2015:

| | Assumed level of change % | Impact on net income and regulatory capital 2016 AED'000 | Impact on net income and regulatory capital 2015 AED'000 |
|---|---|---|---|
| **Investments carried at fair value through the income statement** | | | |
| Reference benchmarks:<br>Fair value of managed funds | 10% | 709 | 855 |

| | Assumed level of change % | Impact on equity 2016 AED'000 | Impact on equity 2015 AED'000 |
|---|---|---|---|
| **Available for sale investments** | | | |
| Reference benchmarks:<br>Quoted debt securities/Islamic sukuks | 10% | 103,582 | 97,028 |
| Other Investments | 10% | 21,787 | 101 |

## Currency risk

Currency risk is the risk that the value of a financial instrument will fluctuate due to changes in foreign exchange rates and arises from financial instruments denominated in a foreign currency. The Board of Directors has set limits on positions by currencies which are closely monitored. Exceptions, if any, are only allowed by seeking prior approval of ALCO and RC supported by a business case and ratification by the Board. During the year, the Group complied with the open position limits and exception approval process.

The Group carries out sensitivity analysis on the basis of 5% shift in exchange rate and analyses their impact on annualised exchange income. ALCO reviews currency limits based on these sensitivities.

The UAE currency is pegged to the US Dollar and this is considered while setting the limits and analysing the sensitivity impact.

At 31 December, the Group's open positions [long/(short)] and potential impact of a shift in exchange rate on the statement of income are as follows:

| Currency | USD | EUR | Others |
|---|---|---|---|
| **Open position** | | | |
| 2016 (AED in 000's) | 155,858 | (741) | 17,260 |
| 2015 (AED in 000's) | 190,676 | 2,723 | 33,846 |
| Assumed change in exchange rates | 5% | 5% | 5% |
| **Impact on exchange income from increase in exchange rates** | | | |
| 2016 (AED in 000's) | 7,793 | (37) | 863 |
| 2015 (AED in 000's) | 9,534 | 136 | 1,692 |
| **Impact on exchange income from decrease in exchange rates** | | | |
| 2016 (AED in 000's) | (7,793) | 37 | (863) |
| 2015 (AED in 000's) | (9,534) | (136) | (1,692) |

At 31 December 2016, the impact on exchange income due to change in exchange rate by 5% is **±8.4%** (2015: ±12.5%). Excluding the impact of US$ open position, the impact is **±0.8%** (2015: ±2.0%).

## Interest rate risk

The principal risk to which financial assets and liabilities are exposed is the risk of loss from fluctuations in the future cash flows or fair values of financial instruments because of a change in market interest rates.

The Group's treasury manages interest rate risk principally through monitoring interest rate gaps and matching the interest re-pricing profile of financial assets and liabilities. The Group's long term financial assets and liabilities are priced generally on a floating rate basis, which tracks the changes in market interest rates. Long term loans and advances and Islamic financing receivables that are priced on a fixed rate basis constitute **6.26%** (2015: 7.60%) of the total loans and advances and Islamic financing receivables portfolio.

The Group measures the interest rate sensitive gaps across tenors considering the availability of a contractual ability to re-price all its assets and liabilities. The sensitivity analysis i.e. the impact of a parallel shift in interest rate curves on net interest income (NII) and equity is ascertained and presented to ALCO for review on a monthly basis. Strategies and actions required to mitigate this risk, if any, are approved and monitored by ALCO and executed by Treasury. The Group carries out sensitivity analysis on the net interest income for one year assuming changes (whether increase or decrease) in interest rates. An analysis of the Group's sensitivity to an increase or decrease in market interest rates based on the financial assets and financial liabilities, denominated in various currencies, held at 31 December, assuming no asymmetrical movement in yield curves and a constant statement of financial position, is as follows:

| Currency | AED | USD | EUR | Others | Total |
|---|---|---|---|---|---|
| Assumed change in interest/ profit rates | ±100 bps | ±100 bps | ±100 bps | ±100 bps | ±100 bps |
| **Impact on net interest income and net income from Islamic financing and investment activities from increase in interest/profit rates** | | | | | |
| 2016 (AED in 000's) | 86,371 | (3,945) | 1,401 | (5,322) | 78,505 |
| 2015 (AED in 000's) | 47,415 | 19,157 | 1,270 | (4,738) | 63,104 |
| **Impact on net interest income and net income from Islamic financing and investment activities from decrease in interest/profit rates** | | | | | |
| 2016 (AED in 000's) | (75,091) | 3,945 | (573) | 4,494 | (67,225) |
| 2015 (AED in 000's) | (40,624) | (14,747) | (679) | 4,350 | (51,700) |

An impact of 5% or higher on regulatory capital is considered as a trigger event based on which an action plan is agreed. At 31 December, the impact of 25 bps, 50 bps and 100 bps shift analysis on net interest income and net income from Islamic financing and investment activities and regulatory capital is as follows:

| **Impact on net interest income and net income from Islamic financing and investment activities** | | | | |
|---|---|---|---|---|
| | **2016 (AED in 000's)** | | **2015 (AED in 000's)** | |
| bps | Upward shift | Downward shift | Upward shift | Downward shift |
| 25 | 2.31% | -2.31% | 1.97% | -1.97% |
| 50 | 4.63% | -4.63% | 3.94% | -3.70% |
| 100 | 9.26% | -7.93% | 7.88% | -6.45% |
| **Impact on regulatory capital** | | | | |
| | **2016 (AED in 000's)** | | **2015 (AED in 000's)** | |
| bps | Upward shift | Downward shift | Upward shift | Downward shift |
| 25 | 0.38% | -0.38% | 0.32% | -0.32% |
| 50 | 0.75% | -0.75% | 0.64% | -0.60% |
| 100 | 1.50% | -1.29% | 1.29% | -1.05% |

The Group also conducts interest rate stress testing based on modified duration approach. The results of the shift analysis are reviewed monthly by ALCO, which along with Marketing Committee (MC) and RC has the overall responsibility for managing pricing policy.

The Group's interest rate gap position on financial assets and liabilities based on the earlier of contractual re-pricing or maturity date is as follows:

**At 31 December 2016**

| | Less than 1 month AED'000 | 1 month to 3 months AED'000 | Over 3 months to 6 months AED'000 | Over 6 months to 1 year AED'000 | Over 1 to 5 years AED'000 | Over 5 years AED'000 | Non-interest bearing items AED'000 | Total AED'000 |
|---|---|---|---|---|---|---|---|---|
| Cash and balances with the UAE Central Bank | 1,530,000 | 1,000,000 | 1,150,000 | 1,150,000 | 75,000 | - | 1,875,092 | 6,780,092 |
| Due from banks and financial institutions | 242,456 | 880,854 | 407,599 | 5,238 | 1,578 | - | 604,965 | 2,142,690 |
| Investments and Islamic instruments | 154,246 | 552,464 | 148,714 | 18,586 | 850,477 | 36,964 | 24,828 | 1,786,279 |
| Loans and advances and Islamic financing receivables | 9,308,924 | 8,553,108 | 2,608,428 | 576,491 | 884,945 | 900,557 | (13,957) | 22,818,496 |
| Other assets | - | - | - | - | - | - | 1,952,019 | 1,952,019 |
| **Total financial assets** | **11,235,626** | **10,986,426** | **4,314,741** | **1,750,315** | **1,812,000** | **937,521** | **4,442,947** | **35,479,576** |
| Due to banks | 604,106 | 487,000 | 2,831 | 11,595 | - | - | 4,509 | 1,110,041 |
| Customer deposits and Islamic customer deposits | 5,213,515 | 5,341,399 | 3,424,968 | 3,701,919 | 1,739,963 | 30,000 | 6,486,727 | 25,938,491 |
| Term borrowings | 367,300 | 1,539,349 | - | - | - | - | - | 1,906,649 |
| Other liabilities | - | - | - | - | - | - | 2,057,427 | 2,057,427 |
| **Total financial liabilities** | **6,184,921** | **7,367,748** | **3,427,799** | **3,713,514** | **1,739,963** | **30,000** | **8,548,663** | **31,012,608** |
| **Interest rate sensitivity gap** | | | | | | | | |
| **On-balance sheet** | **5,050,705** | **3,618,678** | **886,942** | **(1,963,199)** | **72,037** | **907,521** | **(4,105,716)** | |
| **Off-balance sheet** | **1,400,078** | **2,257,491** | **715,340** | **-** | **73,460** | **-** | **20,354,698** | |
| **Cumulative** | **6,450,783** | **12,326,952** | **13,929,234** | **11,966,035** | **12,111,532** | **13,019,053** | **29,268,035** | |
| **At 31 December 2015** | | | | | | | | |
| **Cumulative interest rate sensitivity gap** | **5,940,050** | **10,142,854** | **9,164,970** | **9,199,987** | **8,605,655** | **9,586,455** | **16,708,461** | |

### Interest rate yields

The average earning on placements and balances with banks was **0.87%** (2015: 0.81%), on loans and advances and Islamic financing receivables was **5.15%** (2015: 5.22%) and on investments portfolio was **2.11%** (2015: 1.71%). The average cost of customer deposits and Islamic customer deposits was **1.55%** (2015: 1.18%) and of due to banks and term borrowings was **1.31%** (2015: 1.87%).

### Derivative financial instruments

In the ordinary course of business, the Group enters into various types of derivative transactions that are affected by variables in the underlying instruments.

A derivative is a financial instrument or other contract with all three of the following characteristics:

i. Its value changes in response to the change in a specified interest rate, financial instrument price, commodity price, foreign exchange rate, index of prices or rates, credit rating or credit index, or other variable, provided in the case of a non-financial variable that the variable is not specific to a party to the contract (sometimes called the 'underlying');

ii. It requires no initial net investment or an initial net investment that is smaller than would be required for other types of contracts that would be expected to have a similar response to changes in market factors; and

iii. It is settled at a future date.

Derivative financial instruments which the Group enters into includes forward foreign exchange contracts, interest rate derivatives, commodity derivatives and currency options.

The Group uses derivative financial instruments for hedging purposes as part of its asset and liability management activities in order to reduce its own exposure to fluctuations in interest rates.

The Group uses interest rate swaps to hedge interest rate risks. In all such cases, the hedging relationship and objectives including details of the hedged item and hedging instrument are formally documented and the transactions are accounted for based on the type of hedge.

The table below shows the positive (assets) and negative (liabilities) fair values of derivative financial instruments.

| | Fair values | | |
|---|---|---|---|
| 31 December 2016 | Assets AED'000 | Liabilities AED'000 | Notional AED'000 |
| **Derivatives held as fair value hedges** | | | |
| Interest rate swaps | 1,325 | - | 73,460 |
| **Total derivative financial instruments** | 1,325 | - | 73,460 |
| **31 December 2015** | - | - | - |

## f. Operational risk

Operational risk is the risk of direct or indirect loss arising from a wide variety of causes associated with the Group's processes, personnel, technology and infrastructure and from external factors other than credit, market and liquidity risks, such as those arising from legal and regulatory requirements and generally accepted standards of corporate behaviour. Operational risks arise from all of the Group's operations and are faced by all business entities. Potential loss may be in the form of financial loss or other damages, for example loss of reputation and public confidence that will impact the Group's credibility and ability to do business.

The Group's objective in managing operational risk is to balance avoidance of financial losses and damage to the Group's reputation with overall cost effectiveness.

The Group has defined policies and procedures which are followed to manage operational risk through the Operational Risk and Compliance Committee (ORCC) forum. Compliance with Group standards is supported by a programme of periodic risk and internal control assessments and reviews undertaken by Internal Audit and Operational Risk and Compliance. The results of reviews are discussed with the businesses and functional units to which they relate and regular reports are provided to the Internal Audit, RC, Risk Committee of the Board and the Board.

The regulatory risk capital charge allocation with respect to Operational Risk is computed based on the Standardised Approach. However, the bank, as part of the ICAAP, computes the risk capital charge allocation for Pillar II risks related to Strategic Risk, Reputational Risk, Residual Risk and Settlement Risk through an internally designed but externally independently validated scorecard approach which encompasses a broad range of best industry practices including the regulatory requirements and guidance issued from time to time, locally and internationally.

## g. Management of capital

The Group's lead regulator, the UAE Central Bank, sets and monitors regulatory capital requirements. The requirements of capital for subsidiaries, NBF Financial Services FZC, NBF Capital Limited and NBF Trade Services (HKG) Limited, are determined by the Free Zone Authority of Fujairah, DFSA and Hong Kong Companies Registry respectively.

The Group's objectives and strategy when managing capital are:

- To safeguard the Group's ability to continue as a going concern and to increase returns for shareholders;
- To maintain adequate level and achieve an optimum structure for the Group's capital commensurate to its strategy, risk profile and relative positioning in the market;
- To comply with regulatory capital requirements set by the Central Bank of the UAE;
- To efficiently allocate capital to various businesses leading to enhanced shareholder value and optimal risk reward;
- To ensure effective internal organisation and processes and to assess and manage material risks on an ongoing basis; and
- To provide for any unforeseen losses.

The Group's capital management is carried out centrally and determines the level of risk-weighted asset growth and the optimal amount and mix of capital required to support planned business growth.

The Group and its subsidiaries have complied with all externally imposed capital requirements throughout the year.

In implementing capital requirements, the Group calculates its capital adequacy ratio in accordance with the guidelines issued by the UAE Central Bank dated 17 November 2009. The UAE Central Bank introduced the implementation of Basel II with Standardised Approach which the Group follows while at the same time has developed and implemented risk management measurement tools and robust practices to become a Basel II Foundation Internal Rating Based Approach (FIRB) compliant bank. The UAE Central Bank places considerable emphasis on the ICAAP and the Group has developed an economic capital model to comply with the UAE Central Bank requirements.

The Group's regulatory capital adequacy ratio is set by the UAE Central Bank which is 12 % analysed in two tiers, of which Tier 1 capital adequacy ratio must not be less than 8%. The Group has complied with its capital adequacy ratio calculation in accordance with Basel II Standardised Approach for credit, market and operational risks.

### Regulatory Capital

The bank's RWA are weighted as to their relative credit, market and operational risk. Credit risk includes both on and off-balance sheet risks. The bank is following the standardised measurement approach for credit, market and operational risk, as per Pillar 1 of Basel II.

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

- Tier 1 capital, which includes ordinary share capital, statutory reserve, special reserve, retained earnings and Tier 1 capital notes. In preparation of Basel III compliance, the Group also monitors the common equity ratio separately within Tier 1 capital which excludes Tier 1 capital notes; and
- Tier 2 capital, which includes fair value reserves relating to unrealised gains/losses on investments classified as available-for-sale, collective impairment provision and sub-ordinated facilities. The following limits have been applied for Tier 2 capital:
  - » Total Tier 2 capital shall not exceed 67% of Tier 1 capital;
  - » Subordinated liabilities shall not exceed 50% of total Tier 1 capital; and
  - » Collective impairment provision shall not exceed 1.25% of total credit risk weighted assets.

### Capital Allocation:

- The Group also assesses internally its capital requirements taking into consideration its growth requirements and business plans, and quantifies its regulatory and risk/economic capital requirements within its integrated ICAAP Framework. Risks such as interest rate risk on the banking book, concentration risk, stress testing, strategic risk, legal and compliance risk, and reputational risk are all part of the ICAAP.
- The Group also calculates Risk Adjusted Return on Risk Adjusted Capital (RARORAC) for credit applications that are priced on a risk-adjusted basis.

| | 2016 AED'000 | 2015 AED'000 |
|---|---|---|
| **Tier 1 Capital** | | |
| Share capital | 1,271,188 | 1,182,500 |
| Statutory reserve | 503,223 | 457,320 |
| Special reserve | 398,223 | 352,320 |
| Retained earnings | 1,320,619 | 1,206,572 |
| Tier 1 capital notes | 1,000,000 | 1,000,000 |
| **Total Tier 1** | **4,493,253** | **4,198,712** |
| **Tier 2 Capital** | | |
| Available-for-sale revaluation reserve | (9,536) | (7,783) |
| Subordinated facilities (note 14.2) | 400,000 | 400,000 |
| Collective impairment provision | 342,017 | 312,377 |
| **Total Tier 2** | **732,481** | **704,594** |
| **Deductions from Tier 1 and Tier 2 Capital** | | |
| Investments in unconsolidated subsidiaries | - | - |
| **Total capital base (a)** | **5,225,734** | **4,903,306** |

## Risk-weighted assets

| | 2016 Risk-weighted equivalent AED'000 | 2015 Risk-weighted equivalent AED'000 |
|---|---|---|
| Credit risk | 27,361,373 | 24,990,154 |
| Market risk | 5,249 | 35,928 |
| Operational risk | 2,262,517 | 1,677,033 |
| Total risk-weighted assets (b) | 29,629,139 | 26,703,115 |
| Capital adequacy ratio (a)/(b) - % | 17.64 | 18.36 |
| Tier 1 ratio - % | 15.16 | 15.72 |
| Common equity ratio - % | 11.79 | 11.98 |

The Group prepares an ICAAP document and submits to the UAE Central Bank on an annual basis. The Group's ICAAP report includes assessment and review of the following, keeping in mind a forward-looking approach:

- Risk management framework to assess, measure, monitor and control all the material elements of risks;
- Risk profile and business strategy;
- Capital required to cover all material risks;
- Stress testing risks to assess capital requirement under stressed conditions; and
- Capital planning and budgeting.

Apart from credit, market and operational risk covered in Pillar I, the ICAAP report covers other material risks like liquidity risk, concentration risk, interest rate risk in banking book, strategic risk, residual risk, reputational risk and settlement risk. The ICAAP report also covers the stress testing framework for credit, market, liquidity and interest rate risk on banking book. The Pillar II CAR for the year ended 31 December 2016 was **14.51%** (2015: 15.55%). If the bank were to fully adopt the FIRB approach, its capital adequacy would improve to **18.21%** (2015: 19.64%).

## Risk weights for credit risk

The Group has a diversified funded and unfunded credit portfolio. The exposures are classified as per the approach mentioned under the UAE Central Bank Basel II Capital Adequacy Framework covering the Standardised Approach for credit risk. The descriptions of the counterparty classes along with the risk weights used to derive the risk weighted assets are as follows:

### Claims on sovereigns

These pertain to exposures to governments and their central banks. Claims on central banks and sovereigns are risk weighted in accordance with their ratings from acceptable External Credit Assessment Institutions (ECAIs), except that, for all GCC sovereigns a 0% weight has been applied.

### Claims on Public Sector Entities (PSEs)

Domestic currency claims on GCC non-commercial PSE are treated as claims on GCC sovereigns if their Central Bank or monetary authority treats them as such. Foreign currency claims on GCC PSE are treated one grade less favourable than its sovereign i.e. 20% risk weight are applied.

Claims on other foreign non-commercial PSE are treated one grade less favourable than its sovereign. Claims on commercial PSE are treated as claims on corporate.

### Claims on Multilateral Development Banks (MDBs)

All MDBs are risk weighted in accordance with the respective credit rating except for those members listed in the World Bank Group which are risk weighted at 0%.

### Claims on banks

Claims on banks are risk weighted based on the ratings assigned to them by external rating agencies, however, short term claims denominated in local currency are assigned more favourable risk weighting.

### Claims on corporate portfolio

Claims on corporate are risk weighted in accordance with ratings from acceptable ECAIs. Risk weightings for unrated corporate claims are assigned at 100%.

### Claims on regulatory retail exposures

Retail claims that are included in the regulatory retail portfolio are assigned risk weights of 75%, if it meets the criteria mentioned in the UAE Central Bank Basel II guidelines. Claims which do not meet the criteria are assigned risk weights of 100%.

### Claims secured by residential property

A preferential risk weight of 35% is applied on claims that do not exceed AED 10 million and are secured by residential property with LTV of up to 85%. Other claims secured on residential property are risk weighted at 100%.

### Claims secured by commercial property

100% risk weight is applied on claims secured by commercial property.

### Past due exposures

The unsecured portion of any loan and financing (other than a qualifying residential mortgage loan) that is past due for more than 90 days, net of specific provisions (including partial write-offs), is risk weighted as follows:

- 150% risk weight where specific provisions are less than 20% of the outstanding amount of the loan and financing; and
- 100% risk weight where specific provisions are equal to or greater than 20% of the outstanding amount of the loan and financing.

### Equity portfolios

Equity in banking book is risk weighted at 150%.

### Other exposures

These are risk weighted at 100%.

## Credit risk and risk weights

| **2016** (AED'000) | On and off balance sheet | Credit risk mitigation (CRM) | | | Risk-weighted assets |
|---|---|---|---|---|---|
| | Gross outstanding | Exposure before CRM | CRM | After CRM | |
| Claims on sovereigns | 7,105,199 | 7,105,199 | - | 7,105,199 | - |
| Claims on PSEs | 112,085 | 112,085 | - | 112,085 | - |
| Claims on banks | 3,578,108 | 3,578,108 | - | 3,567,755 | 1,688,046 |
| Claims on corporates and GREs | 27,503,028 | 27,503,028 | 2,856,531 | 25,232,165 | 21,429,209 |
| Regulatory retail exposures | 1,804,599 | 1,804,599 | 109,356 | 1,773,628 | 1,664,272 |
| Residential retail portfolio | 587,227 | 587,227 | 540 | 587,227 | 586,687 |
| Commercial real estate | 994,132 | 994,132 | - | 994,132 | 994,132 |
| Past due exposures | 1,335,999 | 558,099 | 10,001 | 548,804 | 543,879 |
| Higher-risk categories | 8,028 | 8,028 | - | 8,028 | 12,042 |
| Other exposures | 724,426 | 724,426 | - | 724,426 | 443,106 |
| **Total** | **43,752,831** | **42,974,931** | **2,976,428** | **40,653,449** | **27,361,373** |

| **2015** (AED'000) | On and off balance sheet Gross outstanding | Credit risk mitigation (CRM) Exposure before CRM | CRM | After CRM | Risk-weighted assets |
|---|---|---|---|---|---|
| Claims on sovereigns | 4,597,953 | 4,597,953 | - | 4,597,953 | 711 |
| Claims on banks | 4,418,496 | 4,418,496 | - | 4,275,245 | 1,742,762 |
| Claims on corporates and GREs | 24,474,496 | 24,474,496 | 2,451,979 | 2,422,074 | 19,303,784 |
| Regulatory retail exposures | 1,634,857 | 1,634,857 | 43,628 | 1,582,991 | 1,590,339 |
| Residential retail portfolio | 779,066 | 779,066 | 5,488 | 779,066 | 773,578 |
| Commercial real estate | 869,877 | 869,877 | - | 869,877 | 869,877 |
| Past due exposures | 1,113,863 | 408,504 | 6,525 | 392,408 | 385,882 |
| Higher-risk categories | 9,559 | 9,559 | - | 9,559 | 14,338 |
| Other exposures | 628,530 | 628,530 | - | 628,530 | 308,883 |
| **Total** | **38,526,697** | **37,821,338** | **2,507,620** | **15,557,703** | **24,990,154** |

On and off balance sheet exposures include unutilised credit limits which are revocable at the discretion of the bank amounting to **AED 15,859 million** (2015: AED 19,105 million).

The Group uses the following ECAIs: Standards & Poor, Moody's and Fitch. The external rating of ECAI is mapped to the prescribed credit quality assessment scale that in turn produces standard risk weightings. The Group uses Credit Risk Mitigation techniques (CRM) whereby only cash and bank guarantees are used in the calculation of Pillar I Capital requirements.

## Market risk and risk weights

The Group's capital charge, in respect of market risk in accordance with the Standardised methodology, is as follows:

| | 2016 AED'000 | 2015 AED'000 |
|---|---|---|
| Interest rate risk | | |
| » Specific interest rate risk | - | - |
| » General interest rate risk | - | - |
| Equity position risk | - | - |
| Foreign exchange risk | 630 | 4,311 |
| Option risk | - | - |
| **Total market risk capital charge** | **630** | **4,311** |
| **Market risk – risk weighted assets** | **5,249** | **35,928** |

In line with the Basel II Accord, investments designated as fair value through profit or loss form part of the banking book rather than the trading book. Accordingly, the designated investment portfolio has been covered under credit risk.

Capital charge against option risk is **nil** (2015: nil), as all currency options are covered through back-to-back transactions with the respective counter parties.

## Operational risk and risk weights

Capital requirement for operational risk is calculated using the Standardised Approach. The total capital charge is calculated by multiplying the specified eight business lines' three (3) - year average net interest income and net income from Islamic financing and investment activities and net non-interest income by a percentage (beta) assigned to each of the business lines. The beta factors range from 12% to 18%, as specified in the Basel II Accord.

## 6. Financial Assets and Liabilities

### 6.1 Classification

The fair values and carrying values of the financial assets and liabilities at 31 December are shown below:

| 2016 | At fair value through profit or loss AED'000 | At fair value through equity AED'000 | Held-to-maturity AED'000 | Loans and advances AED'000 | Other amortised cost AED'000 | Carrying amount AED'000 |
|---|---|---|---|---|---|---|
| **Financial assets** | | | | | | |
| Cash and balances with the UAE Central Bank | - | - | - | - | 6,780,092 | 6,780,092 |
| Due from banks and financial institutions | - | - | - | - | 2,142,690 | 2,142,690 |
| Investments - at fair value | 7,091 | 1,253,685 | - | - | - | 1,260,776 |
| Investments and Islamic instruments - at cost | - | - | 525,503 | - | - | 525,503 |
| Loans and advances and Islamic financing receivables | - | - | - | 22,818,496 | - | 22,818,496 |
| Other assets | - | - | - | - | 1,952,019 | 1,952,019 |
| **Total financial assets** | **7,091** | **1,253,685** | **525,503** | **22,818,496** | **10,874,801** | **35,479,576** |
| **Financial liabilities** | | | | | | |
| Due to banks | - | - | - | - | 1,110,041 | 1,110,041 |
| Customer deposits and Islamic customer deposits | 1,010 | - | - | - | 25,937,481 | 25,938,491 |
| Term borrowings | - | - | - | - | 1,906,649 | 1,906,649 |
| Other liabilities | - | - | - | - | 2,057,427 | 2,057,427 |
| **Total financial liabilities** | **1,010** | **-** | **-** | **-** | **31,011,598** | **31,012,608** |

| 2015 | At fair value through profit or loss AED'000 | At fair value through equity AED'000 | Held-to-maturity AED'000 | Loans and advances AED'000 | Other amortised cost AED'000 | Carrying amount AED'000 |
|---|---|---|---|---|---|---|
| **Financial assets** | | | | | | |
| Cash and balances with the UAE Central Bank | - | - | - | - | 4,505,567 | 4,505,567 |
| Due from banks and financial institutions | - | - | - | - | 2,921,797 | 2,921,797 |
| Investments - at fair value | 8,553 | 971,289 | - | - | - | 979,842 |
| Investments and Islamic instruments - at cost | - | - | 427,326 | - | - | 427,326 |
| Loans and advances and Islamic financing receivables | - | - | - | 19,688,336 | - | 19,688,336 |
| Other assets | - | - | - | - | 1,352,639 | 1,352,639 |
| **Total financial assets** | **8,553** | **971,289** | **427,326** | **19,688,336** | **8,780,003** | **29,875,507** |
| **Financial liabilities** | | | | | | |
| Due to banks | - | - | - | - | 873,252 | 873,252 |
| Customer deposits and Islamic customer deposits | 1,010 | - | - | - | 21,611,524 | 21,612,534 |
| Term borrowings | - | - | - | - | 1,755,730 | 1,755,730 |
| Other liabilities | - | - | - | - | 1,438,654 | 1,438,654 |
| **Total financial liabilities** | **1,010** | **-** | **-** | **-** | **25,679,160** | **25,680,170** |

## 6.2 Fair value measurement – fair value hierarchy:

| 2016 | Notional AED'000 | Level 1 AED'000 | Level 2 AED'000 | Level 3 AED'000 |
|---|---|---|---|---|
| **Investments and Islamic instruments** | | | | |
| » Debt securities/Islamic sukuks | - | 1,035,819 | - | - |
| » Other investments | - | 217,866 | 7,091 | - |
| Customer deposits and Islamic customer deposits | - | - | 1,010 | - |
| Forward foreign exchange contracts | 14,308,644 | - | 5,494 | - |
| Currency options | 5,452,403 | - | 1,300 | - |
| Interest rate derivatives | 4,446,367 | - | 1,709 | - |
| Commodity derivatives | 593,653 | - | 2,431 | - |

| 2015 | Notional AED'000 | Level 1 AED'000 | Level 2 AED'000 | Level 3 AED'000 |
|---|---|---|---|---|
| **Investments and Islamic instruments** | | | | |
| » Debt securities/Islamic sukuks | - | 970,284 | - | - |
| » Other investments | - | 1,005 | 8,553 | - |
| Customer deposits and Islamic customer deposits | - | - | 1,010 | - |
| Forward foreign exchange contracts | 8,017,346 | - | 458 | - |
| Currency options | 893,043 | - | - | - |
| Interest rate derivatives | 2,647,601 | - | 2,695 | - |
| Commodity derivatives | 955,134 | - | 19,634 | - |

During the year, there were no transfers between Level 1 and Level 2 of the fair value hierarchy above. Further, there has been no change in the valuation techniques in relation to valuation of financial instruments, as discussed in note 4, during the year.

# 7. Cash and Balances with the UAE Central Bank

| | 2016 AED'000 | 2015 AED'000 |
|---|---|---|
| Cash on hand | 281,321 | 319,647 |
| Certificates of deposit (CDs) with the UAE Central Bank | 4,905,000 | 2,375,000 |
| Other balances with the UAE Central Bank (note 7.1) | 1,593,771 | 1,810,920 |
| | **6,780,092** | **4,505,567** |

7.1 Other balances with the UAE Central Bank include regulatory cash reserve deposits of **AED 1,116.5 million** (2015: AED 1,013.2 million).

# 8. Due from Banks and Financial Institutions

## 8.1 By type

| | 2016 AED'000 | 2015 AED'000 |
|---|---|---|
| Placements | 438,057 | 1,422,752 |
| Current accounts/ term deposits | 606,290 | 468,723 |
| Bills discounted | 1,098,343 | 957,312 |
| Certificates of deposit | - | 73,010 |
| | **2,142,690** | **2,921,797** |

As at 31 December 2016, current accounts/term deposits include cash collateral of **AED 30.4 million** (2015: AED 12.7 million) in respect of negative fair value of derivatives, in accordance with the Credit Support Annex (CSA) agreements with the interbank counterparties.

### 8.2 By geographical area

| | 2016 | 2015 |
|---|---|---|
| | AED'000 | AED'000 |
| Within UAE | 1,188,920 | 1,162,278 |
| GCC countries | 123,000 | 505,467 |
| Others | 830,770 | 1,254,052 |
| | **2,142,690** | **2,921,797** |

8.3 The currency wise analysis is set out below:

| | 2016 | 2015 |
|---|---|---|
| | AED'000 | AED'000 |
| AED | 763,117 | 909,134 |
| USD | 1,176,016 | 1,687,853 |
| EUR | 121,688 | 196,727 |
| GBP | 15,648 | 39,649 |
| Others | 66,221 | 88,434 |
| | **2,142,690** | **2,921,797** |

## 9. Investments and Islamic Instruments

| | 2016 | 2015 |
|---|---|---|
| | AED'000 | AED'000 |
| **Investments at fair value through profit or loss (FVTPL) (note 9.1)** | **7,091** | **8,553** |
| **Available-for-sale (AFS)** | | |
| Debt securities/Islamic sukuks (note 9.2) | 1,035,819 | 970,284 |
| Other investments | 217,866 | 1,005 |
| | **1,253,685** | **971,289** |
| **Held-to-maturity (HTM)** | | |
| Debt securities/Islamic sukuks (note 9.2) | 525,503 | 427,326 |
| | **1,786,279** | **1,407,168** |

9.1 Investments at FVTPL include various funds whose fair values are based on the net asset values provided by the fund managers.

9.2 Debt securities aggregating **AED 1,561.3 million** (2015: AED 1,397.6 million) represent the Group's investments in bonds and notes which are quoted on recognised exchanges and prices of which are available on internationally recognised platforms of Reuters and Bloomberg and are liquid in normal market conditions. The debt securities portfolio includes floating rate securities amounting to **AED 625.8 million** (2015: AED 650.7 million).

Debt securities includes Islamic sukuks amounting to **AED 453.6 million** (2015: 270.3 million).

9.3 The dispersion of the investment portfolio is set out below:

| | 2016 | 2015 |
|---|---|---|
| | AED'000 | AED'000 |
| Government | 361,918 | 168,379 |
| Banks and financial institutions | 1,010,630 | 1,081,440 |
| Others | 413,731 | 157,349 |
| | **1,786,279** | **1,407,168** |

9.4 An analysis of investments based on external credit ratings is as follows:

| **2016** | Debt securities/ Islamic sukuks AED'000 | Other investments AED'000 | Total AED'000 |
|---|---|---|---|
| AAA | 18,052 | - | 18,052 |
| AA+ | 90,826 | - | 90,826 |
| AA | 108,152 | - | 108,152 |
| AA- | 186,473 | - | 186,473 |
| A+ | 187,116 | 109,671 | 296,787 |
| A | 206,613 | 90,458 | 297,071 |
| A- | 215,713 | - | 215,713 |
| BBB+ | 311,492 | - | 311,492 |
| BBB | 33,444 | - | 33,444 |
| BBB- | 18,353 | 937 | 19,290 |
| BB | 55,036 | - | 55,036 |
| B+ | 73,677 | - | 73,677 |
| Unrated | 56,375 | 23,891 | 80,266 |
| | **1,561,322** | **224,957** | **1,786,279** |

| 2015 | Debt securities/ Islamic sukuks AED'000 | Other investments AED'000 | Total AED'000 |
|---|---|---|---|
| AA+ | 154,266 | - | 154,266 |
| AA | 18,652 | - | 18,652 |
| AA- | 146,560 | - | 146,560 |
| A+ | 187,500 | - | 187,500 |
| A | 220,972 | - | 220,972 |
| A- | 89,208 | - | 89,208 |
| BBB+ | 312,147 | - | 312,147 |
| BB+ | 54,835 | - | 54,835 |
| BBB- | - | 1,005 | 1,005 |
| Unrated | 213,470 | 8,553 | 222,023 |
| | **1,397,610** | **9,558** | **1,407,168** |

9.5 The geographic dispersion of the investment portfolio is as follows:

| | 2016 AED'000 | 2015 AED'000 |
|---|---|---|
| Within UAE | 297,433 | 258,887 |
| GCC countries | 107,132 | - |
| Others | 1,381,714 | 1,148,281 |
| | **1,786,279** | **1,407,168** |

9.6 The currency wise analysis of the investment portfolio is set out below:

| | 2016 AED'000 | 2015 AED'000 |
|---|---|---|
| USD | 1,629,110 | 1,214,960 |
| EUR | 134,379 | 165,037 |
| GBP | 22,690 | 27,171 |
| JPY | 100 | - |
| | **1,786,279** | **1,407,168** |

## 10. Loans and Advances and Islamic Financing Receivables

10.1 Loans and advances and Islamic financing receivables by type:

| | 2016 AED'000 | 2015 AED'000 |
|---|---|---|
| Overdrafts | 2,008,364 | 1,591,468 |
| Term loans | 16,454,987 | 13,250,914 |
| Loans against trust receipts | 3,415,502 | 3,777,454 |
| Bills discounted | 1,742,085 | 1,696,328 |
| Bills drawn under letters of credit | 402,459 | 426,395 |
| | **24,023,397** | **20,742,559** |
| Allowance for impairment losses (note 10.3) | (1,204,901) | (1,054,223) |
| **Net loans and advances and Islamic financing receivables** | **22,818,496** | **19,688,336** |

10.2 Loans and advances and Islamic financing receivables include Murabaha Tawarruq and Ijara financing activities amounting to **AED 1,631.3 million** (2015: AED 587.6 million) provided through a Shari'a compliant Islamic window, NBF Islamic.

10.3 Allowance for impairment losses on loans and advances and Islamic financing receivables:

| | 2016 AED'000 | 2015 AED'000 |
|---|---|---|
| **Movement in allowances for impairment losses** | | |
| Balance at 1 January | 1,054,223 | 924,865 |
| Net allowance for impairment losses | 405,522 | 208,092 |
| Written-off during the year | (254,844) | (78,734) |
| | **1,204,901** | **1,054,223** |

## 11. Contingent Liabilities and Commitments

Contingent liabilities represent credit related commitments under letters of credit and guarantees which are designed to meet the requirements of the Group's customers towards third parties. Commitments represent credit facilities and other capital expenditure commitments of the Group which are undrawn at the date of consolidated statement of financial position. All credit related commitments are unconditionally cancellable/revocable at the discretion of the Group except for the amounts mentioned in the table below.

| | 2016 AED'000 | 2015 AED'000 |
|---|---|---|
| **Contingent liabilities:** | | |
| Letters of credit covering movement of goods | 1,706,264 | 1,326,259 |
| Financial guarantees and other direct credit substitutes | 759,458 | 763,588 |
| Bid bonds, performance bonds and other transaction related contingencies | 4,436,364 | 4,554,986 |
| | **6,902,086** | **6,644,833** |

| | 2016 AED'000 | 2015 AED'000 |
|---|---|---|
| **Commitments:** | | |
| Undrawn irrevocable commitments – credit related | 397,898 | 467,333 |
| Others | 58,462 | 54,969 |
| | **456,360** | **522,302** |
| | **7,358,446** | **7,167,135** |

The total undrawn credit limits which are revocable at the discretion of the bank amount to **AED 15,859 million** (2015: AED 19,105 million). Many of the contingent liabilities and commitments will expire without being funded in whole or in part. Therefore, the amounts do not necessarily represent expected future cash flows.

## 12. Property and Equipment and Capital Work-In-Progress

| AED'000 | Freehold land | Buildings and leasehold improvements | Motor vehicles, furniture, software and equipment | Total |
|---|---|---|---|---|
| **Cost** | | | | |
| **At 1 January 2015** | **14,066** | **117,815** | **136,321** | **268,202** |
| Additions | - | 8,569 | 16,453 | 25,022 |
| Disposals | - | - | - | - |
| **At 31 December 2015** | **14,066** | **126,384** | **152,774** | **293,224** |
| **At 1 January 2016** | **14,066** | **126,384** | **152,774** | **293,224** |
| Additions | - | 3,694 | 18,775 | 22,469 |
| Disposals | - | - | (450) | (450) |
| **At 31 December 2016** | **14,066** | **130,078** | **171,099** | **315,243** |
| **Depreciation** | | | | |
| **At 1 January 2015** | **-** | **63,840** | **94,113** | **157,953** |
| Charge for the year | - | 5,281 | 15,279 | 20,560 |
| On disposals | - | - | - | - |
| **At 31 December 2015** | **-** | **69,121** | **109,392** | **178,513** |
| **At 1 January 2016** | **-** | **69,121** | **109,392** | **178,513** |
| Charge for the year | - | 4,204 | 18,471 | 22,675 |
| On disposals | - | - | (271) | (271) |
| **At 31 December 2016** | **-** | **73,325** | **127,592** | **200,917** |
| **Net book value** | | | | |
| **At 31 December 2016** | **14,066** | **56,753** | **43,507** | **114,326** |
| **At 31 December 2015** | **14,066** | **57,263** | **43,382** | **114,711** |

The buildings in Fujairah, Dibba, Masafi, Qidfa and Tawian are constructed on land granted to the Group by the Government of Fujairah. The land is shown at a nominal value of AED 1 each (2015: AED 1 each).

Software comprises the cost of the Group's version upgrade of the core banking system, its license cost including customisation cost, and directly attributable implementation costs of the project necessarily incurred to bring the software to the state of use. It also includes software and directly attributable costs relating to the implementation of mobile banking, internet banking and other software purchases. This is being amortised over the estimated useful life of 5 years.

### 12.1 Capital work-in-progress

| | 2016 | 2015 |
|---|---|---|
| | AED'000 | AED'000 |
| | 37,469 | **27,756** |

12.2 Capital work in progress includes costs incurred in respect of the Group's branches, software and directly attributable costs relating to treasury front-end system and other software and equipment purchases.

## 13. Other Assets

| | 2016 | 2015 |
|---|---|---|
| | AED'000 | AED'000 |
| Accrued interest/profit | 143,675 | 107,630 |
| Prepayments and deposits | 14,613 | 10,621 |
| Customer liabilities for acceptances | 1,658,980 | 1,116,318 |
| Fair value of derivatives | 142,796 | 120,205 |
| Others | 28,703 | 13,047 |
| | **1,988,767** | **1,367,821** |

## 14. Due to Banks and Term Borrowings

| | 2016 | 2015 |
|---|---|---|
| | AED'000 | AED'000 |
| **By type** | | |
| Bilateral borrowings (note 14.1) | 1,506,649 | 1,355,730 |
| Sub-ordinated debt (note 14.2) | 400,000 | 400,000 |
| | **1,906,649** | **1,755,730** |
| Due to banks (note 14.3) | 1,110,041 | 873,252 |
| | **3,016,690** | **2,628,982** |
| **By geographical area** | | |
| Within UAE | 204,072 | 275,475 |
| GCC Countries | 514,220 | 488,812 |
| Others | 2,298,398 | 1,864,695 |
| | **3,016,690** | **2,628,982** |

As at 31 December 2016, due to banks include cash collateral of **AED 2.1 million** (31 December 2015: 6.8 million), in respect of positive fair value of derivatives, in accordance with the Credit Support Annex (CSA) agreements with the interbank counterparties.

14.1 Bilateral borrowings comprise of several borrowings obtained from other banks and financial institutions as follows:

| Loan no. | Year obtained | Maturity | Interest rate | 2016 AED '000 | 2015 AED '000 |
|---|---|---|---|---|---|
| 1 | 2016 | July 2018 | Libor + Margin | 91,825 | - |
| 2 | 2016 | May 2018 | Libor + Margin | 183,650 | - |
| 3 | 2016 | March 2018 | Libor + Margin | 110,190 | - |
| 4 | 2016 | February 2018 | Libor + Margin | 110,190 | - |
| 5 | 2016 | November 2017 | Libor + Margin | 36,400 | - |
| 6 | 2016 | October 2017 | Libor + Margin | 73,460 | - |
| 7 | 2016 | June 2017 | Libor + Margin | 36,730 | - |
| 8 | 2016 | March 2017 | Libor + Margin | 238,745 | - |
| 9 | 2016 | March 2017 | Libor + Margin | 61,460 | - |
| 10 | 2016 | March 2017 | Libor + Margin | 31,414 | - |
| 11 | 2016 | March 2017 | Libor + Margin | 36,730 | - |
| 12 | 2016 | February 2017 | Libor + Margin | 36,730 | - |
| 13 | 2015 | November 2018 | Libor + Margin | 110,190 | 110,190 |
| 14 | 2015 | May 2017 | Libor + Margin | 73,460 | 73,460 |
| 15 | 2015 | Mar 2017 | Libor + Margin | 91,825 | 91,825 |
| 16 | 2015 | Mar 2017 | Libor + Margin | 183,650 | 183,650 |
| 17 | 2015 | November 2016 | Libor + Margin | - | 128,555 |
| 18 | 2015 | October 2016 | Libor + Margin | - | 77,133 |
| 19 | 2015 | October 2016 | Libor + Margin | - | 30,670 |
| 20 | 2015 | March 2016 | Libor + Margin | - | 110,190 |
| 21 | 2015 | March 2016 | Libor + Margin | - | 90,932 |
| 22 | 2015 | February 2016 | Libor + Margin | - | 91,825 |
| 23 | 2014 | May 2016 | Libor + Margin | - | 91,825 |
| 24 | 2014 | March 2016 | Libor + Margin | - | 183,650 |
| 25 | 2014 | March 2016 | Libor + Margin | - | 91,825 |
| | | | | **1,506,649** | **1,355,730** |

14.2 On 27 November 2013, the Group arranged a term subordinated loan facility, amounting to AED 400 million, with a finance company. The facility carries an interest rate which is the aggregate of margin and EIBOR, payable quarterly. As per the terms of the facility, the full principal amount of the facility is to be repaid on 27 November 2023. The UAE Central Bank has approved the facility to be considered as Tier 2 capital for regulatory purposes.

14.3 Due to banks include gold related borrowings amounting to **AED 925.1 million** (2015: AED 547.3 million) utilised to finance gold loans extended to customers on a matched basis.

## 15. Customer Deposits and Islamic Customer Deposits

| | 2016<br>AED'000 | 2015<br>AED'000 |
|---|---|---|
| **By type:** | | |
| Demand and margin deposits | 7,532,743 | 6,154,248 |
| Saving deposits | 337,644 | 297,657 |
| Fixed term and notice deposits | 18,068,104 | 15,160,629 |
| | **25,938,491** | **21,612,534** |
| **By geographical area:** | | |
| Within UAE | 23,747,770 | 20,230,091 |
| Others | 2,190,721 | 1,382,443 |
| | **25,938,491** | **21,612,534** |

15.1 Customer deposits and Islamic customer deposits include Qard Islamic current accounts, Murabaha and Wakala deposits amounting to **AED 2,931.5 million** (31 December 2015: AED 1,116.9 million) undertaken through a Shari'a-compliant Islamic window, NBF Islamic.

## 16. Other Liabilities

| | 2016<br>AED'000 | 2015<br>AED'000 |
|---|---|---|
| Accrued interest/profit | 121,941 | 86,182 |
| Employee end of service and other long term benefits (note 16.1) | 43,480 | 39,750 |
| Accrued expenses | 101,994 | 98,261 |
| Directors' annual remuneration | 3,000 | 2,750 |
| Liabilities under acceptances | 1,658,980 | 1,116,318 |
| Fair value of derivatives | 131,862 | 97,418 |
| Others | 72,625 | 71,344 |
| | **2,133,882** | **1,512,023** |

### 16.1 Employee end of service and other long term benefits

| | 2016<br>AED'000 | 2015<br>AED'000 |
|---|---|---|
| At 1 January | 39,750 | 34,590 |
| Charge for the year | 13,071 | 13,749 |
| Payment during the year | (9,341) | (8,589) |
| **At 31 December** | **43,480** | **39,750** |

### 16.2 Provision for employees' end of service benefits

In accordance with the provisions of IAS 19, management has carried out an exercise to assess the present value of its obligations as at 31 December 2016, using the projected unit credit method, in respect of employees' end of service benefits payable under the UAE Labour Law. Under this method, an assessment has been made of employees' expected service life with the Group and the expected basic salary at the date of leaving the service. Management has assumed average increment/promotion costs of 1.5%. The expected liability at the date of leaving the service has been discounted to its net present value using a discount rate of 3.5%.

## 17. Shareholders' Equity

### 17.1 Share capital

| | 2016<br>AED'000 | 2015<br>AED'000 |
|---|---|---|
| **Authorised, issued and fully paid:** | | |
| 1,271,187,500 shares of AED 1 each (2015: 1,182,500,000 shares of AED 1 each) | 1,271,188 | 1,182,500 |

### 17.2 Proposed dividend

The Board of Directors has proposed a cash dividend of **7.5%** (2015: 7.5%) and bonus shares of **7.5%** (2015: 7.5%) of share capital for the year ended 31 December 2016.

### 17.3 Statutory and special reserve

In accordance with the bank's Articles of Association, the provisions of Article 82 of Union Law No. 10 of 1980 and Article 239 of Federal Law No. 2 of 2015, 10% of the bank's profit for the year shall be transferred to a statutory reserve which is not distributable. Additionally, in accordance with the bank's Articles of Association, another 10% of the bank's profit for the year shall be transferred to a special reserve which is to be used for purposes to be determined by the annual general assembly meeting upon the proposal of the Board of Directors.

## 18. Tier 1 Capital Notes

In March 2013, the bank issued Tier 1 capital notes with a principal amount of AED 500 million (the "Capital Notes"). Issuance of these Capital Notes was approved by the bank's Extra Ordinary General Meeting (EGM) in March 2013. The UAE Central Bank has also approved the facility to be considered as Tier 1 capital for regulatory purposes. These Capital Notes bear interest at a fixed rate payable semi-annually in arrears. The Capital Notes are non-cumulative perpetual securities for which there is no fixed redemption date, and are callable by the bank subject to certain conditions. The bank may, at its sole discretion, elect not to make an interest/coupon payment.

In March 2015, the bank issued Tier 1 capital notes with a principal amount of AED 500 million (the "Capital Notes"). Issuance of these Capital Notes was approved by the bank's Extra Ordinary General Meeting (EGM) in March 2013. The UAE Central Bank has also approved the facility to be considered as Tier 1 capital for regulatory purposes. These Capital Notes bear interest at a fixed rate payable semi-annually in arrears during the initial period of five years, and will be reset every five years based on the then prevailing 5-year AED mid swap rate plus margin. The Capital Notes are non-cumulative perpetual securities for which there is no fixed redemption date, and are callable by the bank subject to certain conditions. The bank has also defined conditions for non-viability loss absorption and write-down in line with Basel III guidelines. The bank may, at its sole discretion, elect not to make an interest/coupon payment. Issuance costs of AED 1.538 million were incurred.

## 19. Interest Income and Income from Islamic Financing and Investment Activities

| | 2016 | 2015 |
|---|---|---|
| | AED'000 | AED'000 |
| Loans and advances and Islamic financing receivables (note 19.1) | 1,182,006 | 1,031,324 |
| Due from banks including the UAE Central Bank CDs (note 19.1) | 58,651 | 37,327 |
| Investments and Islamic instruments (note 19.2) | 35,162 | 16,758 |
| | **1,275,819** | **1,085,409** |

19.1 This includes income from Islamic financing activities amounting to **AED 57.3 million** (2015: AED 15.5 million) for the year ended 31 December 2016.

19.2 This includes income from Islamic investment activities amounting to **AED 13.3 million** (2015: AED 3.5 million) for the year ended 31 December 2016.

## 20. Interest Expense and Distribution to Islamic Depositors

| | 2016 | 2015 |
|---|---|---|
| | AED'000 | AED'000 |
| Due to banks including term borrowings | 65,150 | 46,584 |
| Customer deposits and Islamic customer deposits (note 20.1) | 362,468 | 237,521 |
| | **427,618** | **284,105** |

20.1 Includes distribution to Islamic depositors amounting to **AED 41.5 million** (2015: AED 13.25 million) for the year ended 31 December 2016.

## 21. Net Fees and Commission Income

| | 2016 AED'000 | 2015 AED'000 |
|---|---|---|
| **Fees and commission income** | | |
| Letters of credit | 99,793 | 88,587 |
| Letters of guarantee | 47,201 | 47,472 |
| Lending fees | 143,295 | 124,734 |
| Asset management and investment services | 46 | 59 |
| Commission on transfers | 22,027 | 19,091 |
| Others | 16,223 | 32,763 |
| **Total fees and commission income** | **328,585** | **312,706** |
| **Fees and commission expense** | | |
| Brokerage expense | 971 | 748 |
| Card related charges | 13,877 | 13,981 |
| Other charges | 2,737 | 3,837 |
| **Total fees and commission expense** | **17,585** | **18,566** |
| **Net fees and commission income** | **311,000** | **294,140** |

## 22. Income from Investments and Islamic Instruments

| | 2016 AED'000 | 2015 AED'000 |
|---|---|---|
| Net fair value gains on investments and Islamic instruments | 11,131 | 2,707 |

## 23. Other Operating Income

| | 2016 AED'000 | 2015 AED'000 |
|---|---|---|
| Rental income | 176 | 756 |
| Rebates | 7,060 | 6,346 |
| Other miscellaneous income | 39,250 | 16,888 |
| | **46,486** | **23,990** |

## 24. Employee Benefits Expense

Employee benefits expense includes employee bonus of **AED 41.6 million** (2015: AED 55.9 million). The number of employees at 31 December 2016 was **730** including **587** employed by the bank of which **245** were UAE nationals [2015: 728 including 587 employed by the bank of which 249 were UAE nationals].

## 25. Social Contributions

The social contributions made during the year to various beneficiaries amount to **AED 1.0 million** (2015: AED 0.9 million).

## 26. Earnings Per Share

The calculation of earnings per share is based on net profit of **AED 389.9 million** (2015: AED 504.8 million), after deduction of **AED 70.6 million** (2015: AED 54.0 million) of issuance cost and coupon payment on Tier 1 capital notes, divided by the weighted average number of shares of **1,271.2 million** (2015: 1,271.2 million shares after adjusting for bonus shares) outstanding during the year.

## 27. Related Parties

Parties are considered to be related if one party has the ability to control the other party or exercise significant influence over the other party in making financial or operational decisions. In the case of the Group, related parties, as defined in the International Accounting Standard No. 24, include major shareholders of the Group, directors and officers of the Group and companies of which they are principal owners and key management personnel. Banking transactions are entered into with related parties on agreed terms and conditions approved by the Board of Directors. The significant transactions and balances included in the consolidated financial statements, which predominantly relate to directors and shareholders of the Group, are as follows:

| | 2016 AED'000 | 2015 AED'000 |
|---|---|---|
| **Statement of financial position items** | | |
| Loans and advances and Islamic financing receivables | 2,105,129 | 2,151,779 |
| Customer deposits and Islamic customer deposits | 4,777,890 | 4,620,544 |
| Investments and Islamic instruments | 56,552 | 159,537 |

| | 2016 | 2015 |
|---|---|---|
| | AED'000 | AED'000 |
| Acceptances | 36,949 | 33,228 |
| Tier 1 capital notes | 690,000 | 690,000 |
| **Statement of changes in equity items** | | |
| Tier 1 capital notes coupon paid | 48,088 | 41,201 |
| **Contingent liabilities** | | |
| Letters of credit | 109,407 | 121,357 |
| Financial guarantees and other direct credit substitutes | 66,080 | 91,695 |
| Transaction related contingencies | 178,075 | 110,452 |
| **Statement of income items** | | |
| Interest income and income from Islamic financing and investment activities | 65,492 | 47,847 |
| Interest expense and distribution to Islamic depositors | 100,627 | 89,130 |
| Other income | 10,729 | 8,270 |
| **Key management compensation** | | |
| Salaries and other short-term benefits | 21,686 | 20,980 |
| Employee end of service benefits | 680 | 630 |
| Directors' annual remuneration | 3,000 | 2,750 |

No provisions for impairment have been recognised in respect of loans and advances and Islamic financing receivables given to related parties (2015: Nil).

The loans and advances and Islamic financing receivables given to related parties amounting to **AED 2,105.1 million** (2015: AED 2,151.8 million) have been secured against collateral amounting to **AED 1,444.7 million** (2015: AED 1,446.1 million).

In accordance with the requirements of notice no. 226/2015 dated 26 August 2015 and issued by the UAE Central Bank, the Group has complied with article (91) of Union Law No. 10 of 1980.

## 28. Cash and Cash Equivalents

For the purpose of the cash flow statement, cash and cash equivalents comprise the following balances from the date of acquisition:

| | 2016 | 2015 |
|---|---|---|
| | AED'000 | AED'000 |
| Cash on hand | 281,321 | 319,647 |
| Balances with the UAE Central Bank (note 28.1) | 5,382,278 | 3,172,708 |
| Due from banks with less than three months maturity | 889,347 | 1,392,304 |
| | **6,552,946** | **4,884,659** |
| Due to banks with less than three months maturity | (637,620) | (543,671) |
| | **5,915,326** | **4,340,988** |

28.1 Balances with the UAE Central Bank include certificates of deposit. In accordance with UAE Central Bank regulations on issuance of Central Bank certificates of deposit, the bank can enter into repurchase agreements in order to obtain short term liquidity.

## 29. Segmental Reporting

The Group uses business segments for presenting its segment information in line with the Group's management and internal reporting structure. The Group's operations are confined mainly in the UAE.

Business segments pay and receive interest, to and from Treasury on an arm's length basis to reflect allocation of capital and funding costs.

### Business segments

The Group conducts its activity through the following clearly defined business segments:

Corporate and Institutional banking

**Corporate and Institutional segments**

The segment offers a range of products and services, including credit and trade finance products, and services to large and medium sized corporate customers through separate units and to financial institutions, and accepts deposits.

**Business banking segment**

The segment offers a range of products and services, including credit and trade finance products, and services to small and medium sized customers through separate units, and accepts deposits. The segment also offers transactional services to small and medium sized businesses.

### Retail banking

The segment offers a range of products and services to individuals and high net worth individuals, including personal and mortgage loans, credit cards, other transactions and balances, and accepts their deposits.

### Treasury, Asset and Liability Management (ALM) and others

The segment undertakes the Group's asset and liability management centrally and is responsible for optimum utilisation of resources in productive assets and management of exchange and interest positions within the limits and guidelines set by management and approved by the Board.

Treasury also offers various foreign exchange and derivative products to customers and is entrusted with the responsibility of managing the Group's investment portfolio together with Asset and Liability Committee. The Group's capital and investment in subsidiaries is recognised under this segment.

The Group has central shared services which include Operations, Risk Management, Human Resources, Finance, Information Technology, Product Development, Legal, Credit and Internal Audit. The shared services cost is allocated to business segments based on transaction and relevant drivers.

The segment analysis based on business segments is set out below:

| **2016** (AED'000) | Corporate and Institutional segments | Business banking segment | Retail banking | Treasury, ALM and others | **Consolidated** |
|---|---|---|---|---|---|
| Segment revenue | 721,225 | 255,685 | 100,660 | 241,537 | **1,319,107** |
| Segment operating cost | (225,203) | (126,648) | (71,887) | (29,404) | **(453,142)** |
| **Segment operating profit** | **496,022** | **129,037** | **28,773** | **212,133** | **865,965** |
| Net impairment losses | (265,833) | (105,964) | (33,725) | - | **(405,522)** |
| **Profit/(loss)** | **230,189** | **23,073** | **(4,952)** | **212,133** | **460,443** |
| Segment assets | 20,942,447 | 2,944,284 | 1,858,262 | 9,923,126 | **35,668,119** |
| Segment liabilities | 23,971,837 | 2,910,693 | 2,110,570 | 2,095,963 | **31,089,063** |
| Capital expenditure | - | - | - | 31,997 | **31,997** |

| **2015** (AED'000) | Corporate and Institutional segments | Business banking segment | Retail banking | Treasury, ALM and others | **Consolidated** |
|---|---|---|---|---|---|
| Segment revenue | 650,409 | 265,187 | 89,260 | 208,241 | **1,213,097** |
| Segment operating cost | (222,951) | (125,195) | (70,279) | (27,820) | **(446,245)** |
| **Segment operating profit** | **427,458** | **139,992** | **18,981** | **180,421** | **766,852** |
| Net impairment losses | (134,524) | (55,525) | (18,043) | - | **(208,092)** |
| **Profit** | **292,934** | **84,467** | **938** | **180,421** | **558,760** |
| Segment assets | 17,173,275 | 2,939,673 | 1,780,941 | 8,139,267 | **30,033,156** |
| Segment liabilities | 19,226,048 | 2,669,154 | 1,803,881 | 2,054,456 | **25,753,539** |
| Capital expenditure | - | - | - | 38,096 | **38,096** |

## 30. Comparative Figures

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