

MASHREQBANK PSC GROUP

**Report and consolidated financial statements
for the year ended 31 December 2011**

MASHREQBANK PSC GROUP

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INDEPENDENT AUDITOR'S REPORT

The Shareholders
Mashreqbank psc
Dubai
United Arab Emirates

Report on the consolidated financial statements

We have audited the accompanying consolidated financial statements of Mashreqbank psc (the "Bank"), a Public Shareholding Company, and its Subsidiaries (collectively the "Group"), which comprise the consolidated statement of financial position as at 31 December 2011, and the consolidated income statement, consolidated statement of comprehensive income, consolidated statement of changes in equity and consolidated statement of cash flows for the year then ended, and a summary of significant accounting policies and other explanatory information.

Management's responsibility for the consolidated financial statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with the International Financial Reporting Standards, and for such internal control as management determines is necessary to enable the preparation of the consolidated financial statements that are free from material misstatements whether due to fraud or errors.

Auditor's responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements 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 entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

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INDEPENDENT AUDITOR'S REPORT (continued)

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of Mashreqbank psc and its subsidiaries as at 31 December 2011, and the Group's financial performance and cash flows for the year then ended in accordance with International Financial Reporting Standards.

Report on other legal and regulatory requirements

Also, in our opinion, proper books of account are maintained by the Bank. We have obtained all the information and explanations which we considered necessary for the purpose of our audit. According to the information available to us, there were no contraventions during the year of the U.A.E. Federal Commercial Companies Law No. (8) of 1984 (as amended), or of the Bank's Articles of Association which might have a material effect on the financial position of the Bank or its financial performance.

Deloitte & Touche (M.E.)

A handwritten signature in black ink, appearing to be "Anis Sadek", written over a horizontal line.

Anis Sadek
Registration Number 521
1 February 2012

MASHREQBANK PSC GROUP

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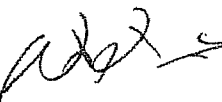
**Consolidated statement of financial position
at 31 December 2011**

		2011		2010	
	Notes	AED'000	USD'000 Equivalent	AED'000	USD'000 Equivalent
ASSETS					
Cash and balances with central banks	5	14,731,800	4,010,836	13,373,722	3,641,090
Deposits and balances due from banks	6	10,147,675	2,762,776	13,651,955	3,716,840
Other financial assets measured at fair value	7	2,552,788	695,014	2,222,680	605,140
Loans and advances measured at amortised cost	8	32,665,962	8,893,537	35,919,982	9,779,467
Islamic financing and investment products measured at amortised cost	9	5,028,547	1,369,057	5,290,904	1,440,486
Other financial assets measured at amortised cost	7	7,181,593	1,955,239	8,083,811	2,200,874
Interest receivable and other assets	10	5,417,102	1,474,844	4,986,426	1,357,589
Investment properties	11	318,028	86,585	172,320	46,915
Property and equipment	12	1,197,827	326,117	1,144,003	311,463
Total assets		79,241,322	21,574,005	84,845,803	23,099,864
LIABILITIES AND EQUITY					
Liabilities					
Deposits and balances due to banks	13	7,223,370	1,966,613	6,038,626	1,644,058
Repurchase agreements with banks	14	2,505,165	682,049	3,368,993	917,232
Customers' deposits	15	40,177,020	10,938,475	46,764,858	12,732,060
Islamic customers' deposits	16	5,239,863	1,426,589	4,488,815	1,222,111
Insurance and life assurance funds	17	972,867	264,870	896,587	244,102
Interest payable and other liabilities	18	5,676,168	1,545,377	4,990,584	1,358,722
Medium-term loans	19	4,634,012	1,261,642	5,903,034	1,607,142
Long-term loans	20	9,007	2,452	9,324	2,539
Total liabilities		66,437,472	18,088,067	72,460,821	19,727,966
Equity					
Capital and reserves					
Issued and paid up capital	21(a)	1,690,770	460,324	1,690,770	460,324
Statutory and legal reserves	21(b)	846,745	230,532	845,385	230,162
General reserve	21(c)	312,000	84,944	312,000	84,944
Cumulative translation adjustment	21(d)	(33,022)	(8,990)	(19,483)	(5,304)
Investments revaluation reserve	21(e)	(346,145)	(94,240)	(284,120)	(77,354)
Retained earnings		9,792,462	2,666,066	9,300,191	2,532,042
Equity attributable to shareholders of the Parent		12,262,810	3,338,636	11,844,743	3,224,814
Non-controlling interests	22	541,040	147,302	540,239	147,084
Total equity		12,803,850	3,485,938	12,384,982	3,371,898
Total liabilities and equity		79,241,322	21,574,005	84,845,803	23,099,864

The accompanying notes form an integral part of these consolidated financial statements.



Abdulla Ahmad Al Ghurair
Chairman



Abdul Aziz Abdulla Al Ghurair
Chief Executive Officer

**Consolidated income statement
for the year ended 31 December 2011**

	Notes	2011		2010	
		AED'000	USD'000 Equivalent	AED'000	USD'000 Equivalent
Interest income	24	3,135,446	853,647	4,040,586	1,100,078
Income from Islamic financing and investment products	25	252,762	68,816	277,103	75,443
Total interest income and income from Islamic financing and investment products		3,388,208	922,463	4,317,689	1,175,521
Interest expense	26	(1,334,303)	(363,273)	(1,863,981)	(507,482)
Distribution to depositors – Islamic products	27	(109,834)	(29,903)	(162,566)	(44,260)
Net interest income and income from Islamic products net of distribution to Depositors		1,944,071	529,287	2,291,142	623,779
Fee and commission income	28	1,940,984	528,447	1,838,556	500,560
Fee and commission expenses	28	(957,928)	(260,803)	(726,086)	(197,682)
Net fee and commission income		983,056	267,644	1,112,470	302,878
Net investment income	29	123,367	33,588	48,094	13,094
Other income, net	30	821,839	223,751	935,168	254,606
Operating income		3,872,333	1,054,270	4,386,874	1,194,357
General and administrative expenses	31	(1,793,683)	(488,343)	(1,763,897)	(480,233)
Allowances for impairment	32	(1,195,839)	(325,576)	(1,767,390)	(481,184)
Profit before taxes		882,811	240,351	855,587	232,940
Overseas income tax expense		(21,769)	(5,926)	(18,985)	(5,169)
Profit for the year		861,042	234,425	836,602	227,771
Attributed to:					
Shareholders of the Parent		820,379	223,354	803,498	218,758
Non-controlling interests		40,663	11,071	33,104	9,013
		861,042	234,425	836,602	227,771
Earnings per share	33	AED 4.85	USD 1.32	AED 4.75	USD 1.29

The accompanying notes form an integral part of these consolidated financial statements.

**Consolidated statement of comprehensive income
for the year ended 31 December 2011**

	2011		2010	
	AED'000	USD'000 Equivalent	AED'000	USD'000 Equivalent
Profit for the year	861,042	234,425	836,602	227,771
Other comprehensive (loss)/income				
Changes in fair value of financial assets measured at fair value through other comprehensive income, net	(80,501)	(21,918)	(7,608)	(2,071)
Exchange difference arising on translating the foreign operations	(11,531)	(3,140)	5,535	1,507
Loss on hedging instruments designated in hedges of the net assets of foreign operations [Note 21(d)]	(2,008)	(546)	-	-
Total other comprehensive loss for the year	(94,040)	(25,604)	(2,073)	(564)
Total comprehensive income for the year	767,002	208,821	834,529	227,207
Attributed to:				
Shareholders of the Parent	756,221	205,886	813,072	221,365
Non-controlling interests	10,781	2,935	21,457	5,842
	767,002	208,821	834,529	227,207

The accompanying notes form an integral part of these consolidated financial statements.

**Consolidated statement of changes in equity
for the year ended 31 December 2011**

	Issued and paid up capital AED'000	Statutory and legal reserves AED'000	General reserve AED'000	Cumulative translation adjustment AED'000	Investments revaluation reserve AED'000	Retained earnings AED'000	Equity attributable to shareholders of the Parent AED'000	Non- controlling interests AED'000	Total AED'000
Balance at 31 December 2009	1,610,257	805,129	312,000	(25,018)	(279,735)	8,850,576	11,273,209	574,283	11,847,492
Profit for the year	-	-	-	-	-	803,498	803,498	33,104	836,602
Other comprehensive income/(loss) for the year	-	-	-	5,535	4,039	-	9,574	(11,647)	(2,073)
Total comprehensive income for the year	-	-	-	5,535	4,039	803,498	813,072	21,457	834,529
Transfer from investment revaluation reserve to retained earnings	-	-	-	-	(8,424)	8,424	-	-	-
Transfer to statutory and legal reserves	-	40,256	-	-	-	(40,256)	-	-	-
Payment of dividends	-	-	-	-	-	(241,538)	(241,538)	(55,501)	(297,039)
Bonus shares issued	80,513	-	-	-	-	(80,513)	-	-	-
Balance at 31 December 2010	1,690,770	845,385	312,000	(19,483)	(284,120)	9,300,191	11,844,743	540,239	12,384,982
Profit for the year	-	-	-	-	-	820,379	820,379	40,663	861,042
Other comprehensive loss for the year	-	-	-	(13,539)	(50,619)	-	(64,158)	(29,882)	(94,040)
Total comprehensive income for the year	-	-	-	(13,539)	(50,619)	820,379	756,221	10,781	767,002
Transfer from investment revaluation reserve to retained earnings	-	-	-	-	(11,406)	11,406	-	-	-
Transfer to statutory and legal reserves	-	1,360	-	-	-	(1,360)	-	-	-
Payment of dividends [Note 21 (f)]	-	-	-	-	-	(338,154)	(338,154)	(8,400)	(346,554)
Purchase of non-controlling interest	-	-	-	-	-	-	-	(1,580)	(1,580)
Balance at 31 December 2011	1,690,770	846,745	312,000	(33,022)	(346,145)	9,792,462	12,262,810	541,040	12,803,850

The accompanying notes form an integral part of these consolidated financial statements

**Consolidated statement of cash flows
for the year ended 31 December 2011**

	2011		2010	
	AED'000	USD'000 Equivalent	AED'000	USD'000 Equivalent
Cash flows from operating activities				
Profit for the year	861,042	234,425	836,602	227,771
Adjustments for:				
Depreciation of property and equipment	158,961	43,278	143,008	38,935
Allowances for impairment	1,195,839	325,576	1,767,390	481,184
Gain on sale of property and equipment	(15,824)	(4,308)	(181,783)	(49,492)
Gain from redemption of medium term loans	(31,859)	(8,674)	(22,928)	(6,242)
Fair value adjustment of other financial assets measured at FVTPL	13,189	3,591	(1,072)	(292)
Fair value adjustments of investment property	61,188	16,659	61,329	16,697
Net realized investment gain from sale of other financial assets measured at FVTPL	(7,373)	(2,007)	(2,573)	(701)
Dividend income from financial assets measured at FVTOCI	(43,056)	(11,722)	(38,211)	(10,403)
Net realized investment (gain)/loss from sale of other financial assets measured at amortised cost	(42,888)	(11,677)	14,290	3,891
Loss on sale of loans and advances in a secondary market	2,571	700	55,722	15,171
Fair value adjustment - derivatives	9,216	2,509	(18,581)	(5,059)
Operating cash flow before changes in operating assets and liabilities	2,161,006	588,350	2,613,193	711,460
(Increase)/decrease in deposits with central banks for regulatory purposes	(4,478,593)	(1,219,328)	6,231,992	1,696,704
Decrease/(increase) in deposits and balances due from banks maturing after three months	2,971,127	808,910	(2,587,416)	(704,442)
Decrease in loans and advances measured at amortised cost	2,276,477	619,787	4,655,544	1,267,504
Decrease in Islamic financing and investment products measured at amortised cost	231,377	62,994	211,584	57,605
(Increase)/decrease in interest receivable and other assets	(588,843)	(160,317)	676,936	184,301
(Increase)/decrease in other financial assets carried at FVTPL	(428,710)	(116,719)	2,367	644
Decrease in repurchase agreements with banks	(863,828)	(235,183)	(4,160,775)	(1,132,800)
Decrease in customers' deposits	(6,587,838)	(1,793,585)	(4,031,910)	(1,097,716)
Increase in Islamic customers' deposits	751,048	204,478	1,627,796	443,179
Decrease in medium-term loans (not qualified as Tier 2 capital)	(1,101,900)	(300,000)	(1,193,725)	(325,000)
Decrease in long-term loans	(317)	(86)	(259)	(71)
Increase/(decrease) in deposits and balances due to banks	1,184,744	322,555	(1,872,042)	(509,677)
Increase/(decrease) in insurance and life assurance funds	76,280	20,768	38,000	10,346
Increase/(decrease) in interest payable and other liabilities	685,584	186,655	(639,176)	(174,020)
Net cash flows (used in)/generated by operating activities	(3,712,386)	(1,010,721)	1,572,109	428,017

The accompanying notes form an integral part of these consolidated financial statements.

**Consolidated statement of cash flows
for the year ended 31 December 2011 (continued)**

	2011		2010	
	AED'000	USD'000 Equivalent	AED'000	USD'000 Equivalent
Cash flows from investing activities				
Purchase of property and equipment	(378,252)	(102,982)	(409,442)	(111,473)
Proceeds from sale of property and equipment	43,004	11,708	208,581	56,788
Purchase of investment properties	(93,105)	(25,348)	-	-
Net decrease in other financial assets measured at amortized cost	940,306	256,005	1,243,761	338,623
Net decrease/(increase) in other financial assets measured atFVTOCI	12,285	3,345	(17,493)	(4,763)
Dividend income from other financial assets measured at FVTOCI	43,056	11,722	38,211	10,403
Purchase of non-controlling interest	(1,580)	(430)	-	-
Net cash generated by investing activities	565,714	154,020	1,063,618	289,578
Cash flows from financing activities				
Dividend paid	(346,554)	(94,352)	(297,039)	(80,871)
Decrease in medium term loans (qualified as Tier 2 capital)	(135,263)	(36,826)	(58,612)	(15,958)
Net cash used in financing activities	(481,817)	(131,178)	(355,651)	(96,829)
Net (decrease)/increase in cash and cash equivalents	(3,628,489)	(987,879)	2,280,076	620,766
Net foreign exchange difference	(13,539)	(3,686)	5,535	1,507
Cash and cash equivalents at 1 January	14,427,686	3,928,036	12,142,075	3,305,763
Cash and cash equivalents at 31 December (Note 35)	10,785,658	2,936,471	14,427,686	3,928,036

The accompanying notes form an integral part of these consolidated financial statements.

**Notes to the consolidated financial statements
for the year ended 31 December 2011**

1 General information

Mashreqbank psc (the “Bank”) was incorporated in the Emirate of Dubai in 1967 under a decree issued by The Ruler of Dubai. The Bank carries on retail banking, commercial banking, investment banking, Islamic banking, brokerage and asset management activities through its branches in the United Arab Emirates, Bahrain, Kuwait, Egypt, Hong Kong, India, Qatar, the United Kingdom and the United States of America.

The address of the Bank’s registered office is P.O. Box 1250, Dubai, United Arab Emirates.

At 31 December 2011, Mashreqbank psc Group (the “Group”) comprises of the Bank and the following subsidiaries:

Name of subsidiary	Place of incorporation (or registration) and operation	Proportion of ownership interest %	Proportion of voting power held %	Principal activity
Osool – a Finance Company (PJSC)	United Arab Emirates	98.00	98.00	Finance
Oman Insurance Company (PSC)	United Arab Emirates	63.65	63.65	Insurance
Mindscape Information Technology L.L.C.	United Arab Emirates	99.00	99.00	Software/Application provider
Mashreq Securities LLC	United Arab Emirates	99.98	99.98	Brokerage
Injaz Services FZ LLC	United Arab Emirates	100.00	100.00	Service provider
Mashreq Al Islami Finance Company (PJSC)	United Arab Emirates	99.80	99.80	Islamic finance company
Mashreq Capital (DIFC) Limited	United Arab Emirates	100.00	100.00	Brokerage and asset & fund management
Makaseb Funds Company BSC	Kingdom of Bahrain	99.90	99.90	Fund manager
Makaseb Funds Company BSC II	Kingdom of Bahrain	99.90	99.90	Fund manager
Bracebridge Limited	British Virgin Islands	*	100.00	Special purpose vehicle
Orriston Limited	British Virgin Islands	*	100.00	Special purpose vehicle

* Bank participation in capital is nominal, however the above subsidiaries are considered to be subsidiaries by virtue of effective control.

**Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)**

2 Adoption of new and revised International Financial Reporting Standards (IFRSs)

2.1 Standards and Interpretations effective for the current year

The following new and revised standards and interpretations have been adopted in the current year with no material impact on the disclosures and amounts reported for the current and prior years but may affect the accounting for future transactions or arrangements:

- Amendments to IAS 24 *Related Party Disclosures* modify the definition of a related party and simplify disclosures for government-related entities.
- Amendments to IAS 32 *Classification of Rights Issues* address the classification of certain rights issues denominated in a foreign currency as either an equity instrument or as a financial liability.
- Amendments to IFRIC 14 *Prepayments of a Minimum Funding Requirement*. The amendments correct an unintended consequence of IFRIC 14 *IAS 19 – The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction*.
- IFRIC 19 *Extinguishing Financial Liabilities with Equity Instruments* provides guidance regarding the accounting for the extinguishment of a financial liability by the issue of equity instruments. In particular equity instruments issued under such arrangements are measured at their fair value, and any difference between the carrying amount of the financial liability extinguished and the fair value of equity instruments issued are recognized in the income statement.
- Improvements to IFRSs issued in 2010 – Amendments to: IFRS 1; IFRS 3 (2008); IAS 1; IAS 27 (2008); IAS34; and IFRIC 13.

2.2 Standards and Interpretations in issue but not yet effective

The Group has not early applied the following new standards, amendments and interpretations that have been issued but not yet effective:

**Effective for
annual periods
beginning on or after**

- Amendments to IFRS 7 *Disclosures – Transfers of Financial Assets* increase the disclosure requirements for transactions involving transfers of financial assets. These amendments are intended to provide greater transparency around risk exposures of transactions when a financial asset is transferred but the transferor retains some level of continuing exposure in the asset. The amendments also require disclosures where transfers of financial assets are not evenly distributed throughout the period.

1 July 2011

**Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)**

**2 Adoption of new and revised International Financial Reporting Standards (IFRSs)
(continued)**

2.2 Standards and Interpretations in issue but not yet effective (continued)

	Effective for annual periods beginning on or after
IFRS 10 <i>Consolidated Financial Statements</i>* uses control as the single basis for consolidation, irrespective of the nature of the investee. IFRS 10 requires retrospective application subject to certain transitional provisions providing an alternative treatment in certain circumstances. Accordingly IAS 27 <i>Separate Financial Statements</i>* and IAS 28 <i>Investments in Associates and Joint Ventures</i>* have been amended for the issuance of IFRS 10.	1 January 2013
IFRS 11 <i>Joint Arrangements</i>* establishes two types of joint arrangements: Joint operations and joint ventures. The two types of joint arrangements are distinguished by the rights and obligations of those parties to the joint arrangement. Accordingly IAS 28 <i>Investments in Associates and Joint Ventures</i> has been amended for the issuance of IFRS 11.	1 January 2013
IFRS 12 <i>Disclosure of Interests in Other Entities</i>* combines the disclosure requirements for an entity's interests in subsidiaries, joint arrangements, associates and structured entities into one comprehensive disclosure Standard.	1 January 2013
IFRS 13 <i>Fair Value Measurement</i> issued in May 2011, establishes a single framework for measuring fair value and is applicable for both financial and non-financial items.	1 January 2013
Amendments to IAS 1 – <i>Presentation of Other Comprehensive Income</i>. The amendments retain the option to present profit or loss and other comprehensive income in either a single statement or in two separate statements. However, items of other comprehensive income are required to be classified into those that will and will not subsequently be reclassified to the income statement	1 July 2012
Amendments to IAS 12 <i>Income Taxes</i> provide an exception to the general principles of IAS 12 for investment property measured using the fair value model in IAS 40 <i>Investment Property</i> by the introduction of a rebuttable presumption that the carrying amount of the investment property will be recovered entirely through sale.	1 January 2012

**Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)**

**2. Adoption of new and revised International Financial Reporting Standards (IFRSs)
(continued)**

2.2 Standards and Interpretations in issue but not yet effective (continued)

	Effective for annual periods beginning on or after
• Amendments to IAS 19 Employee Benefits eliminate the “corridor approach” and therefore require an entity to recognize changes in defined benefit plan obligations and plan assets when they occur.	1 January 2013
• Amendments to IFRS 7 <i>Financial Instruments: Disclosures</i> enhancing disclosures about offsetting of financial assets and liabilities.	1 January 2013
• Amendments to IAS 32 <i>Financial Instruments: Presentation</i> relating to application guidance on the offsetting of financial assets and financial liabilities.	1 January 2013

* In May 2011, a package of five Standards on consolidation, joint arrangements, associates and disclosures was issued, including IFRS 10, IFRS 11, IFRS 12, IAS 27 (as revised in 2011) and IAS 28 (as revised in 2011). These five standards are effective for annual periods beginning on or after 1 January 2013. Earlier application is permitted provided that all of these five standards are applied early at the same time.

The management anticipates that the adoption of these Standards and Interpretations will have no material impact on the consolidated financial statements of the Group in the year of initial application.

3 Summary of significant accounting policies

3.1 Statement of compliance

The consolidated financial statements of the Group have been prepared in accordance with International Financial Reporting Standards (IFRS) and Central Bank of the U.A.E. requirements as related to the impairment of loans and advances measured at amortised cost and calculation of the capital adequacy ratio.

3.2 Basis of preparation

The consolidated financial statements of the Group are prepared under the historical cost basis except for certain financial instruments and investment properties which are measured at fair value. Historical cost is generally based on the fair value of the consideration given in exchange for assets.

The principal accounting policies are set out below:

**Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)**

3 Summary of significant accounting policies (continued)

3.3 Basis of consolidation

The consolidated financial statements incorporate the financial statements of the Bank and entities controlled by the Bank (its subsidiaries). Control is achieved where the Bank has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities.

Income and expenses of subsidiaries acquired or disposed of during the year are included in the consolidated statement of comprehensive income from the effective date of acquisition and up to the effective date of disposal, as appropriate. Total comprehensive income of subsidiaries is attributed to the shareholders of the Parent and to the non-controlling interests even if this results in the non-controlling interests having a deficit balance.

Where necessary, adjustments are made to the financial statements of subsidiaries to bring their accounting policies into line with those used by other members of the Group.

All intra-group transactions, balances, income and expenses are eliminated in full on consolidation.

Non-controlling interests in the net assets (excluding goodwill) of consolidated subsidiaries are identified separately from the Group's equity therein. The interests of non-controlling shareholders may be initially measured either at fair value or at the non-controlling interests' proportionate share of the fair value of the acquiree's identifiable net assets. The choice of measurement basis is made on an acquisition-by-acquisition basis. Subsequent to acquisition, the carrying amount of non-controlling interests is the amount of those interests at initial recognition plus the non-controlling interests' share of subsequent changes in equity. Total comprehensive income is attributed to non-controlling interests even if this results in the non-controlling interests having a deficit balance.

Changes in the Group's ownership interests in subsidiaries that do not result in the Group losing control over the subsidiaries are accounted for as equity transactions. The carrying amounts of the Group's interests and the non-controlling interests are adjusted to reflect the changes in their relative interests in the subsidiaries. Any difference between the amount by which the non-controlling interests are adjusted and the fair value of the consideration paid or received is recognised directly in equity and attributed to shareholders of the Parent.

When the Group loses control of a subsidiary, the profit or loss on disposal is calculated as the difference between (i) the aggregate of the fair value of the consideration received and the fair value of any retained interest and (ii) the previous carrying amount of the assets (including goodwill), and liabilities of the subsidiary and any non-controlling interests. When assets of the subsidiary are carried at revalued amounts or fair values and the related cumulative gain or loss have been recognised in other comprehensive income and accumulated in equity, the amounts previously recognised in other comprehensive income and accumulated in equity are accounted for as if the Parent had directly disposed of the relevant assets (i.e. reclassified to profit or loss or transferred directly to retained earnings as specified by applicable IFRSs). The fair value of any investment retained in the former subsidiary at the date when control is lost is regarded as the fair value on initial recognition for subsequent accounting under IFRS 9 *Financial Instruments* or, when applicable, the cost on initial recognition of an investment in an associate or a jointly controlled entity.

**Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)**

3 Summary of significant accounting policies (continued)

3.4 Revenue recognition

Interest income and expense

Interest income and expense for all interest-bearing financial instruments, except for other financial assets measured at fair value through profit and loss (FVTPL), are recognized within 'interest income' and 'interest expense' in the consolidated income statement using the effective interest method. Interest income from other financial assets measured at FVTPL is recognized within 'net investment income' in the consolidated income statement.

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

Once a financial asset or a group of similar financial assets has been written down as a result of an impairment loss, interest income is recognised using the rate of interest used to discount the future cash flows for the purpose of measuring the impairment loss. Recoveries in respect of loans and advances previously provided for are accounted for on a cash receipt basis.

Income from Islamic financing and investments products

The Group's policy for recognition of income from Islamic financing and investments products is described in Note 3.21 (iii).

Fee and commission income and expenses

Fee and commission income and expenses are accounted for on the date the transaction arises.

Dividend revenue

Dividend revenue from investments is recognized in the consolidated income statement when the Group's right to receive payment has been established.

Insurance contracts revenue and insurance commission income

Premiums on general insurance policies are accounted for on the date of writing of policies except premium income on marine cargo policies which is accounted for on the expected date of voyage. Premiums are adjusted for unearned premium.

Premium on life assurance policies are accounted for on the date of writing of policies and on subsequent due dates.

Insurance commission income is recognised when the policies are written based on the terms and percentages agreed with the reinsurers.

**Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)**

3 Summary of significant accounting policies (continued)

3.4 Revenue recognition (continued)

Gain or loss from redemption of medium term loans

Gain or loss from redemption of medium term loans represents the difference between the amount paid and the carrying amount of the liability on the date of redemption.

Rental income

The Group's policy for recognition of revenue from operating leases is described in 3.5 below.

3.5 Leasing

Leases are classified as finance leases whenever the terms of the lease transfer substantially all the risks and rewards of ownership to the lessee. All other leases are classified as operating leases.

The Group as lessor

Rental income from operating leases is recognised on a straight-line basis over the term of the relevant lease. Initial direct costs incurred in negotiating and arranging an operating lease are added to the carrying amount of the leased asset and recognised on a straight-line basis over the lease term.

The Group as lessee

Operating lease payments are recognised as an expense on a straight-line basis over the lease term, except where another systematic basis is more representative of the time pattern in which economic benefits from the leased asset are consumed. Contingent rentals arising under operating leases are recognised as an expense in the period in which they are incurred.

In the event that lease incentives are received to enter into operating leases, such incentives are recognised as a liability. The aggregate benefit of incentives is recognised as a reduction of rental expense on a straight-line basis, except where another systematic basis is more representative of the time pattern in which economic benefits from the leased asset are consumed.

**Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)**

3 Summary of significant accounting policies (continued)

3.6 Foreign currencies

The individual financial statements of each Group entity are presented in the currency of the primary economic environment in which the entity operates (its functional currency). For the purpose of the consolidated financial statements, the results and financial position of each entity are expressed in U.A.E.

Dirham (AED), which is the functional currency of the Group, and the presentation currency for the consolidated financial statements.

The presentation currency of the Group is the U.A.E. Dirham (AED); however, for presentation purposes only, additional columns for US Dollar (USD) equivalent amounts have been presented in the consolidated statement of financial position, consolidated income statement, consolidated statement of comprehensive income and consolidated statement of cash flows and certain notes to the consolidated financial statements using a conversion rate of USD 1.00 = AED 3.673.

In preparing the financial statements of the individual entities, transactions in currencies other than the Group's functional currency (foreign currencies) are recorded at the rates of exchange prevailing at the dates of the transactions. At each reporting date, monetary items denominated in foreign currencies are retranslated at the rates prevailing at the reporting date. Non-monetary items carried at fair value that are denominated in foreign currencies are retranslated at the rates prevailing at the date when the fair value was determined. Non-monetary items that are measured in terms of historical cost in a foreign currency are not retranslated.

Exchange differences are recognised in consolidated income statement in the period in which they arise except for:

- exchange differences which relate to assets under construction for future productive use, which are included in the cost of those assets when they are regarded as an adjustment to interest costs on foreign currency borrowings;
- exchange differences on transactions entered into in order to hedge certain foreign currency risks; and
- exchange differences on monetary items receivable from or payable to a foreign operation for which settlement is neither planned nor likely to occur, which form part of the net investment in a foreign operation, and which are recognised in the foreign currency translation reserve and recognised in consolidated income statement on disposal of the net investment.

For the purpose of presenting consolidated financial statements, the assets and liabilities of the Group's foreign operations are expressed in AED using exchange rates prevailing at the reporting date. Income and expense items are translated at the average exchange rates for the year, unless exchange rates fluctuated significantly during that year, in which case the exchange rates at the dates of the transactions are used. Exchange differences arising, if any, are classified as equity and recognised in the Group's cumulative translation adjustment. Such exchange differences are recognised in the consolidated income statement in the period in which the foreign operation is disposed.

**Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)**

3 Summary of significant accounting policies (continued)

3.7 Property and equipment

Property and equipment are stated at cost less accumulated depreciation and any accumulated impairment losses, except for capital work-in-progress which is carried at cost less any accumulated impairment losses.

Depreciation is charged so as to write off the cost of assets, other than land and capital work in progress, using the straight-line method, over the estimated useful lives of the respective assets, as follows:

	<u>Years</u>
Properties for own use	20 – 25
Furniture, fixtures, equipments and vehicles	3 - 7
Improvements to freehold properties and others	5 - 10

The estimated useful lives, residual values and depreciation method are reviewed at each year end, with the effect of any changes in estimate accounted for on a prospective basis.

The gain or loss arising on the disposal or retirement of an item of property and equipment is determined as the difference between the sales proceeds and the carrying amount of the asset and is recognised in the consolidated income statement.

One year after property and equipment are fully depreciated, they are maintained at a net book value of one currency unit by setting off accumulated depreciation against cost.

Capital work in progress is carried at cost, less any accumulated impairment losses. Cost includes professional fees and, for qualifying assets, borrowing costs capitalised in accordance with the Group's accounting policy. Depreciation of these assets commences when the assets are ready for their intended use.

3.8 Investment property

Investment properties are properties held to earn rentals and/or for capital appreciation (including property under construction for such purposes). Investment properties are measured initially at cost, including transaction costs. Subsequent to initial recognition, investment properties are measured at fair value. Gains and losses arising from changes in the fair value of investment properties are included in the consolidated income statement in the period in which they arise.

An investment property is derecognised upon disposal or when the investment property is permanently withdrawn from use and no future economic benefits are expected from the disposal. Any gain or loss arising on derecognition of the property (calculated as the difference between the net disposal proceeds and the carrying amount of the asset) is included in the consolidated income statement in the period in which the property is derecognised.

3.9 Impairment of tangible assets

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

**Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)**

3 Summary of significant accounting policies (continued)

3.9 Impairment of tangible assets (continued)

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

If the recoverable amount of an asset (or cash-generating unit) is estimated to be less than its carrying amount, the carrying amount of the asset (or cash-generating unit) is reduced to its recoverable amount. An impairment loss is recognized in the consolidated income statement.

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

3.10 Provisions

Provisions are recognised when the Group has a present obligation (legal or constructive) as a result of a past event, it is probable that the Group will be required to settle the obligation, and a reliable estimate can be made of the amount of the obligation.

The amount recognised as a provision is the best estimate of the consideration required to settle the present obligation at the reporting date, taking into account the risks and uncertainties surrounding the obligation. Where a provision is measured using the cash flows estimated to settle the present obligation, its carrying amount is the present value of those cash flows.

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

3.11 Financial instruments

Financial assets and financial liabilities are recognised when the Group becomes a party to the contractual provisions of the instrument.

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

**Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)**

3 Summary of significant accounting policies (continued)

3.11 Financial instruments (continued)

3.11.1 Financial assets

All regular way purchases or sales of financial assets are recognised and derecognised on a trade date basis. Regular way purchases or sales are purchases or sales of financial assets that require delivery of assets within the time frame established by regulation or convention in the marketplace.

All recognised financial assets are subsequently measured in their entirety at either amortised cost or fair value, depending on the classification of the financial assets.

Classification of financial assets

For the purposes of classifying financial assets, an instrument is an 'equity instrument' if it is a non-derivative and meets the definition of 'equity' for the issuer except for certain non-derivative puttable instruments presented as equity by the issuer. All other non-derivative financial assets are 'debt instruments'.

Debt instruments, including loans and advances and Islamic financing and investments products, are measured at amortised cost if both of the following conditions are met:

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

All other financial assets are subsequently measured at fair value.

Amortised cost and effective interest method

The effective interest method is a method of calculating the amortised cost of a debt instrument and of allocating interest income over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash receipts (including all fees and points paid or received that form an integral part of the effective interest rate, transaction costs and other premiums or discounts) through the expected life of the debt instrument, or, where appropriate, a shorter period, to the net carrying amount on initial recognition.

Income is recognised on an effective interest basis for debt instruments (other than those financial assets designated as FVTPL) are measured subsequently at amortised cost. Interest income is recognised in the consolidated income statement.

**Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)**

3 Summary of significant accounting policies (continued)

3.11 Financial instruments (continued)

3.11.1 Financial assets (continued)

Financial assets at fair value through other comprehensive income (FVTOCI)

At initial recognition, the Group can make an irrevocable election (on an instrument-by-instrument basis) to designate investments in equity instruments as at FVTOCI. Designation at FVTOCI is not permitted if the equity investment is held for trading.

A financial asset is held for trading if:

- it has been acquired principally for the purpose of selling it in the near term;
- on initial recognition it is part of a portfolio of identified financial instruments that the Group manages together and has evidence of a recent actual pattern of short-term profit-taking; or
- it is a derivative that is not designated and effective as a hedging instrument or a financial guarantee.

Investments in equity instruments at FVTOCI are initially measured at fair value plus transaction costs. Subsequently, they are measured at fair value with gains and losses arising from changes in fair value recognised in other comprehensive income and accumulated in the investments revaluation reserve. Where the asset is disposed of, the cumulative gain or loss previously accumulated in the investments revaluation reserve is not transferred to consolidated income statement, but is reclassified to retained earnings.

Dividends on these investments in equity instruments are recognised in the consolidated income statement when the Group's right to receive the dividends is established in accordance with IAS 18 *Revenue*, unless the dividends clearly represent a recovery of part of the cost of the investment.

Financial assets at fair value through profit or loss (FVTPL)

Investments in equity instruments are classified as at FVTPL, unless the Group designates an investment that is not held for trading as at fair value through other comprehensive income (FVTOCI) on initial recognition (as described above).

Debt instruments that do not meet the amortised cost criteria (as described above) are measured at FVTPL. In addition, debt instruments that meet the amortised cost criteria but are designated as at FVTPL are measured at FVTPL. A debt instrument may be designated as at FVTPL upon initial recognition if such designation eliminates or significantly reduces a measurement or recognition inconsistency that would arise from measuring assets or liabilities or recognising the gains and losses on them on different bases.

Debt instruments are reclassified from amortised cost to FVTPL when the business model is changed such that the amortised cost criteria are no longer met. Reclassification of debt instruments that are designated as at FVTPL on initial recognition is not allowed.

**Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)**

3 Summary of significant accounting policies (continued)

3.11 Financial instruments (continued)

3.11.1 Financial assets (continued)

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

Financial assets at FVTPL are measured at fair value at the end of each reporting period, with any gains or losses arising on remeasurement recognised in the consolidated income statement. The net gain or loss recognised in the consolidated income statement is included in the 'net investment income' line item in the consolidated income statement. Fair value is determined in the manner described in note 42 to the consolidated financial statements.

Interest income on debt instruments as at FVTPL is included in the net gain or loss described above and is included in the 'net investment income' line item.

Dividend income on investments in equity instruments at FVTPL is recognised in the consolidated income statement when the Group's right to receive the dividends is established in accordance with IAS 18 *Revenue* and is included in the net gain or loss described above.

Foreign exchange gains and losses

The fair value of financial assets denominated in a foreign currency is determined in that foreign currency and translated at the spot rate at the end of each reporting period. The foreign exchange component forms part of its fair value gain or loss. Therefore,

- for financial assets that are classified as at FVTPL, the foreign exchange component is recognised in the consolidated income statement; and
- for financial assets that are designated as at FVTOCI, any foreign exchange component is recognised in other comprehensive income.

For foreign currency denominated debt instruments measured at amortised cost at the end of each reporting period, the foreign exchange gains and losses are determined based on the amortised cost of the financial assets and are recognised in the consolidated income statement.

Impairment of financial assets

Financial assets that are measured at amortised cost are assessed for impairment at the end of each reporting period. Financial assets are considered to be impaired when there is objective evidence that, as a result of one or more events that occurred after the initial recognition of the financial assets, the estimated future cash flows of the asset have been affected.

Objective evidence of impairment could include:

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

**Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)**

3 Summary of significant accounting policies (continued)

3.11 Financial instruments (continued)

3.11.1 Financial assets (continued)

Impairment of financial assets (continued)

The amount of the impairment loss recognised is the difference between the asset's carrying amount and the present value of estimated future cash flows reflecting the amount of collateral and guarantee, discounted at the financial asset's original effective interest rate.

The carrying amount of the financial asset is reduced by the impairment loss directly for all financial assets with the exception of loans and advances and due from banks, where the carrying amount is reduced through the use of an allowance account. When a loan is considered uncollectible, it is written off against the allowance account. Subsequent recoveries of amounts previously written off are credited against the allowance account. Changes in the carrying amount of the allowance account are recognised in the consolidated income statement.

If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised, the previously recognised impairment loss is reversed through the consolidated income statement to the extent that the carrying amount of the financial asset at the date the impairment is reversed does not exceed what the amortised cost would have been had the impairment not been recognised.

Impairment of loans and advances measured at amortised costs are assessed by the Group as follows:

(i) Individually assessed loans

These represent mainly corporate loans which are assessed individually by the Group's Credit Risk Unit in order to determine whether there exists any objective evidence that a loan is impaired.

Impaired loans are measured based on the present value of expected future cash flows discounted at the loan's effective interest rate or at the loan's observable market price, if available, or at the fair value of the collateral if the recovery is entirely collateral dependent.

Impairment loss is calculated as the difference between the loan's carrying value and its present value calculated as above.

(ii) Collectively assessed loans

Impairment losses of collectively assessed loans include the allowances on:

- a) Performing commercial and other loans
- b) Retail loans with common features which are rated on a portfolio basis and where individual loan amounts are not significant.

**Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)**

3 Summary of significant accounting policies (continued)

3.11 Financial instruments (continued)

3.11.1 Financial assets (continued)

Impairment of financial assets (continued)

(ii) *Collectively assessed loans (continued)*

(a) *Performing commercial and other loans*

Where individually assessed loans are evaluated and no evidence of loss is present or has been identified, there may be losses based upon risk rating and expected migrations, product or industry characteristics.

Impairment covers losses which may arise from individual performing loans that are impaired at the reporting date but were not specifically identified as such until sometime in the future.

The estimated impairment is calculated by the Group's management for each identified portfolio and based on historical experience, credit rating and expected migrations in addition to the assessed inherent losses which are reflected by the economic and credit conditions and taking into account the requirements of the Central Bank of the U.A.E.

(b) *Retail loans with common features which are rated on a portfolio basis and where individual loan amounts are not significant*

Impairment of retail loans is calculated by applying a formulaic approach whereby a provision of 25% of loan balance is made when it is past due by more than 90 days and a provision of 50% of loan balance is made when is past due by more than 120 days. All loans that are past due by more than 180 days are written off.

Derecognition of financial assets

The Group derecognises a financial asset only when the contractual rights to the cash flows from the asset expire, or when it transfers the financial asset and substantially all the risks and rewards of ownership of the asset to another entity. If the Group neither transfers nor retains substantially all the risks and rewards of ownership and continues to control the transferred asset, the Group recognises its retained interest in the asset and an associated liability for amounts it may have to pay. If the Group retains substantially all the risks and rewards of ownership of a transferred financial asset, the Group continues to recognise the financial asset and also recognises a collateralised borrowing for the proceeds received.

On derecognition of a financial asset measured at amortised cost, the difference between the asset's carrying amount and the sum of the consideration received and receivable is recognised in the consolidated income statement.

On derecognition of a financial asset that is classified as FVTOCI, the cumulative gain or loss previously accumulated in the investments revaluation reserve is not reclassified to the consolidated income statement, but is reclassified to retained earnings.

3.11.2 Financial liabilities and equity instruments

Classification as debt or equity

Debt and equity instruments issued by the Group are classified as either financial liabilities or as equity in accordance with the substance of the contractual arrangement and the definitions of a financial liability and an equity instrument.

**Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)**

3 Summary of significant accounting policies (continued)

3.11 Financial instruments (continued)

3.11.2 Financial liabilities and equity instruments (continued)

Equity instruments

An equity instrument is any contract that evidences a residual interest in the assets of an entity after deducting all of its liabilities. Equity instruments issued by the Group are recognised at the proceeds received, net of direct issue costs.

Financial liabilities

All financial liabilities are subsequently measured at amortised cost using the effective interest rate method or at FVTPL.

However, financial liabilities that arise when a transfer of a financial asset does not qualify for derecognition or when the continuing involvement approach applies, financial guarantee contracts issued by the Group, and commitments issued by the Group to provide a loan at below-market interest rate are measured in accordance with the specific accounting policies set out below.

Financial liabilities subsequently measured at amortised cost

Financial liabilities that are not held-for-trading and are not designated as at FVTPL are measured at amortised cost at the end of subsequent accounting periods. The carrying amounts of financial liabilities that are subsequently measured at amortised cost are determined based on the effective interest method. Interest expense that is not capitalised as part of costs of an asset is included in the consolidated income statement.

The effective interest method is a method of calculating the amortised cost of a financial liability and of allocating interest expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments (including all fees and points paid or received that form an integral part of the effective interest rate, transaction costs and other premiums or discounts) through the expected life of the financial liability, or (where appropriate) a shorter period, to the net carrying amount on initial recognition.

Foreign exchange gains and losses

For financial liabilities that are denominated in a foreign currency and are measured at amortised cost at the end of each reporting period, the foreign exchange gains and losses are determined based on the amortised cost of the instruments and are recognised in the consolidated income statement.

The fair value of financial liabilities denominated in a foreign currency is determined in that foreign currency and translated at the spot rate at the end of the reporting period.

Financial guarantee contracts

A financial guarantee contract is a contract that requires the issuer to make specified payments to reimburse the holder for a loss it incurs because a specified debtor fails to make payments when due in accordance with the terms of a debt instrument.

Financial guarantee contracts issued by the Group are initially measured at their fair values and, if not designated as at FVTPL, are subsequently measured at the higher of:

- the amount of the obligation under the contract, as determined in accordance with IAS 37 Provisions, Contingent Liabilities and Contingent Assets; and
- the amount initially recognised less, where appropriate, cumulative amortisation recognised in accordance with the revenue recognition policies.

**Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)**

3 Summary of significant accounting policies (continued)

3.11 Financial instruments (continued)

3.11.2 Financial liabilities and equity instruments (continued)

Financial liabilities (continued)

De-recognition of financial liabilities

The Group derecognises financial liabilities when, and only when, the Group's obligations are discharged, cancelled or they expire. The difference between the carrying amount of the financial liability derecognised and the consideration paid and payable, including any non-cash assets transferred or liabilities assumed, is recognised in consolidated income statement.

3.12 Offsetting of financial assets and liabilities

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

3.13 Derivative financial instruments

The Group deals with derivatives such as forward foreign exchange contracts, interest rate futures, forward rate agreements, currency and interest rate swaps, currency and interest rate options (both written and purchased).

Derivatives are initially recognised at fair value at the date the derivative contracts are entered into and are subsequently remeasured to their fair value at the end of each reporting period. The resulting gain or loss is recognised in consolidated income statement immediately. All derivatives are carried at their fair values as assets where the fair values are positive and as liabilities where the fair values are negative.

Fair values are generally obtained by reference to quoted market prices, discounted cash flow models and recognized pricing models as appropriate.

Embedded derivatives

Derivatives embedded in non-derivative host contracts that are not financial assets within the scope of IFRS 9 (e.g. financial liabilities) are treated as separate derivatives when their risks and characteristics are not closely related to those of the host contracts and the host contracts are not measured at FVTPL.

3.14 Hedge accounting

The Group designates certain hedging instruments, which include derivatives and non-derivatives in respect of foreign currency risk, as either fair value hedges or hedges of net investments in foreign operations.

At the inception of the hedge relationship, the Group documents the relationship between the hedging instrument and the hedged item, along with its risk management objectives and its strategy for undertaking various hedge transactions. Furthermore, at the inception of the hedge and on an ongoing basis, the Group documents whether the hedging instrument is highly effective in offsetting changes in fair values or cash flows of the hedged item attributable to the hedged risk.

Note 42 sets out details of the fair values of the derivative instruments used for hedging purposes.

**Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)**

3 Summary of significant accounting policies (continued)

3.14 Hedge accounting (continued)

Fair value hedges

Changes in the fair value of derivatives that are designated and qualify as fair value hedges are recognised in profit or loss immediately, together with any changes in the fair value of the hedged asset or liability that are attributable to the hedged risk. The change in the fair value of the hedging instrument and the change in the hedged item attributable to the hedged risk are recognised in the consolidated income statement relating to the hedged item.

Hedge accounting is discontinued when the Group revokes the hedging relationship, when the hedging instrument expires or is sold, terminated, or exercised, or when it no longer qualifies for hedge accounting. The fair value adjustment to the carrying amount of the hedged item arising from the hedged risk is amortised to the consolidated income statement from that date.

Hedges of net investments in foreign operations

Hedges of net investments in foreign operations are accounted for similarly to cash flow hedges. Any gain or loss on the hedging instrument relating to the effective portion of the hedge is recognised in other comprehensive income and accumulated under the heading of cumulative translation reserve. The gain or loss relating to the ineffective portion is recognised immediately in the consolidated income statement.

Gains and losses on the hedging instrument relating to the effective portion of the hedge accumulated in the cumulative translation reserve are reclassified to the consolidated income statement on the disposal of the foreign operation.

3.15 Insurance claims

Claims, comprising amounts payable to contract holders and third parties and related loss adjustment expenses, net of salvage and other recoveries are charged to consolidated income statement as incurred. Provision for incurred but not reported claims is included within additional reserve.

The Group generally estimates its claims based on previous experience. Independent loss adjusters normally estimate property claims. Any difference between the provisions at the reporting date and settlements and provisions for the following year is included in the underwriting account for that year.

**Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)**

3 Summary of significant accounting policies (continued)

3.16 Insurance liability adequacy test

At the end of each reporting period, insurance liability adequacy tests are performed to ensure the adequacy of the contract liabilities. In performing these tests, current best estimates of future contractual cash flows and claims handling and administration expenses, as well as investment income from the assets backing such liabilities, are used. Any deficiency is immediately charged to the consolidated income statement establishing a provision for losses arising from liability adequacy tests.

3.17 Reinsurance

The Group cedes insurance risk in the normal course of business for all of its businesses. Reinsurance assets represent balances due from reinsurance companies. Recoverable amounts are estimated in a manner consistent with the outstanding claims provisions and are in accordance with reinsurance contract. Premiums and claims are presented on a net basis for both ceded and assumed reinsurance.

3.18 Life assurance fund

The fund is determined by independent actuarial valuation of future policy benefits at the end of each reporting period. Actuarial assumptions include a margin for adverse deviation and generally vary by type of policy, year of issue and policy duration. Mortality and withdrawal rate assumptions are based on experience and industry mortality tables. Adjustments to the balance of the fund are effected by charging to the consolidated income statement.

3.19 Receivables and payables related to insurance contracts

Receivables and payables related to insurance contracts are recognised when due. These include amounts due to and from agents, brokers and insurance contract holders.

If there is objective evidence that the insurance receivable is impaired, the Group reduces the carrying amount of the insurance receivable accordingly and recognises that impairment loss in the consolidated income statement.

3.20 Taxation

Where applicable, provision is made for current and deferred taxes arising from the operating results of overseas branches that are operating in taxable jurisdictions.

3.21 Islamic financing and investment products

In addition to conventional banking products, the Group offers its customers certain non-interest based banking products, which are approved by its Sharia'a Supervisory Board.

All Islamic banking products are accounted for in conformity with the accounting policies described below:

**Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)**

3 Summary of significant accounting policies (continued)

3.21 Islamic financing and investment products (continued)

(i) Definitions

The following terms are used in Islamic financing:

Murabaha

An agreement whereby the Group sells to a customer a commodity or an asset, which the Group has purchased and acquired, based on a promise received from the customer to buy the item purchased according to specific terms and conditions. The selling price comprises the cost of the commodity and an agreed profit margin.

Ijara

An agreement whereby the Group acting as a lesser, purchases or constructs an asset for lease according to the customer's request (lessee), based on his promise to lease the asset for an agreed rent and a specific period that could end by transferring the ownership of the leased asset to the lessee.

Musharaka

An agreement between the Group and a customer to contribute to a certain investment enterprise or the ownership of a certain property ending up with the acquisition by the customer of the full ownership. The profit or loss is shared as per the terms of the agreement.

Mudaraba

An agreement between the Group and a customer whereby the Group would provide a certain amount of funds, which the customer would then invest in a specific enterprise or activity against a specific share in the profit. The customer would bear the loss in case of default, negligence or violation of any of the terms and conditions of the Mudaraba.

Wakala

An agreement whereby the Group provides a certain sum of money to an agent who invests it according to specific conditions in return for a certain fee (a lump sum of money or a percentage of the amount invested). The agent is obliged to return the invested amount in case of default, negligence or violation of any of the terms and conditions of the Wakala.

(ii) Accounting policy

Islamic financing and investing products are measured at amortised cost, using the effective profit method, less any amounts written off, allowance for doubtful accounts and unearned income.

The effective profit rate is the rate that exactly discounts estimated future cash flow through the expected life of the financial asset or liability, or, where appropriate, a shorter period.

**Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)**

3 Summary of significant accounting policies (continued)

3.21 Islamic financing and investment products (continued)

(ii) Accounting policy (continued)

Allowance for impairment is made against Islamic financing and investing products when their recovery is in doubt taking into consideration IFRS requirements (as explained in Note 3.11.1). Islamic financing and investing products are written off only when all possible courses of action to achieve recovery have proved unsuccessful.

(iii) Revenue recognition policy

Income from Islamic financing and investing assets are recognised in the consolidated income statement using the effective profit method.

The calculation of the effective profit rate includes all fees paid or received, transaction costs, and discounts or premiums that are an integral part of the effective profit rate. Transaction costs are incremental costs that are directly attributable to the acquisition, issue or disposal of a financial asset.

Murabaha

Murabaha income is recognised on effective profit rate basis over the period of the contract based on the principal amounts outstanding.

Ijara

Ijarah income is recognised on effective profit rate basis over the lease term.

Musharaka

Income is accounted for on the basis of the reducing balance on a time proportion basis that reflects the effective yield on the asset.

Mudaraba

Income or losses on Mudaraba financing are recognised on an accrual basis if they can be reliably estimated. Otherwise, income is recognised on distribution by the Mudarib, whereas the losses are charged to income on their declaration by the Mudarib.

Wakala

Estimated income from Wakala is recognized on an accrual basis over the period, adjusted by actual income when received. Losses are accounted for on the date of declaration by the agent.

(iv) Islamic customers' deposits and distributions to depositors

Islamic customers' deposits are initially measured at fair value which is normally consideration received net of directly attributable transaction costs incurred, and subsequently measured at their amortised cost using the effective profit method.

Distributions to depositors (Islamic products) are calculated according to the Group's standard procedures and are approved by the Group's Sharia'a Supervisory Board.

**Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)**

4 Critical accounting judgements and key sources of estimation uncertainty

In the application of the Group's accounting policies, which are described in Note 3, the management is required to make judgements, estimates and assumptions about the carrying amounts of assets and liabilities that are not readily apparent from other sources. The estimates and associated assumptions are based on historical experience and other factors that are considered to be relevant. Actual results may differ from these estimates.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised if the revision affects only that period, or in the period of the revision and future periods if the revision affects both current and future periods.

Significant areas where management has used estimates, assumptions or exercised judgements are as follows:

(i) Impairment of financial assets measured at amortised cost

The Group's accounting policy for allowances in relation to impaired financial assets carried at amortised cost is described in Note 3. Impairment is calculated on the basis of discounted estimated future cash flows or by applying a certain percentage on the performing unclassified loans and advances book based on market trend and historical pattern of defaults. For retail loans and advances impairment is calculated based on a formulaic approach depending on past due instalments and payments.

The allowance for loans and advances losses is established through charges to income in the form of an allowance. Increases and decreases in the allowance due to changes in the measurement of the impaired loans and advances are included in the allowance for loans and advances losses and affect the consolidated income statement accordingly.

Individually assessed loans and advances

Impairment losses for individually assessed loans and advances are determined by an evaluation of exposure on a case-by-case basis. This procedure is applied to all classified corporate loans and advances which are individually significant accounts or are not subject to the portfolio-based approach.

The following factors are considered when determining impairment losses on individually assessed accounts:

1. The customer's aggregate borrowings.
2. The customer's risk rating, i.e. ability to perform profitable business and generate sufficient cash to repay the borrowed amount.
3. The value of the collateral and the probability of successful repossession.
4. The cost involved to recover the debts.

**Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)**

4 Critical accounting judgements and key sources of estimation uncertainty (continued)

(i) Impairment of financial assets measured at amortised cost (continued)

Individually assessed loans and advances (continued)

The Group's policy requires regular review of the level of impairment allowances on individual facilities.

Impaired loans and advances continue to be classified as impaired unless they are brought fully current and the collection of scheduled interest and principal is considered probable.

Collectively assessed loans and advances

The management of the Group assesses, based on historical experience and the prevailing economical and credit conditions, the magnitude of loans and advances which may be impaired but not identified as of the reporting date.

These portfolio allowances are reassessed on a periodical basis and allowances are adjusted accordingly based on the judgement of management and guidance received from the Central Bank of the UAE.

Collectively assessed allowances are also made in respect of losses incurred in portfolios of retail loans with common features and where individual loan amounts are not significant.

Impairment of retail loans is calculated by applying a formulaic approach whereby a provision of 25% of loan balance is made when it is past due by more than 90 days and a provision of 50% of loan balance is made when is past due by more than 120 days and less than 180 days. All loans that are past due by more than 180 days are written off.

(ii) Property and equipment

The cost of property and equipment is depreciated over the estimated useful life, which is based on expected usage of the asset, expected physical wear and tear, which depends on operational factors. The management has not considered any residual value as it is deemed immaterial.

(iii) Fair value of financial instruments

Where the fair values of financial assets and financial liabilities recorded on the consolidated statement of financial position cannot be derived from active markets, they are determined using a variety of valuation techniques that include the use of mathematical models. The inputs to these models are derived from observable market data where possible, but where observable market data are not available, judgment is required to establish fair values. The judgments include considerations of liquidity and model inputs such as volatility for longer dated derivatives and discount rates, prepayment rates and default rate assumptions for asset backed securities. The management believes that the chosen valuation techniques and assumptions used are appropriate in determining the fair value of financial instruments.

**Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)**

4 Critical accounting judgements and key sources of estimation uncertainty (continued)

(iv) Derivative financial instruments

Subsequent to initial recognition, the fair values of derivative financial instruments measured at fair value are generally obtained by reference to quoted market prices, discounted cash flow models and recognized pricing models as appropriate. When prices are not available, fair values are determined by using valuation techniques which refer to observable market data. These include comparison with similar instruments where market observable prices exist, discounted cash flow analysis, option pricing models and other valuation techniques commonly used by market participants. The main factors which management considers when applying a model are:

- (a) The likelihood and expected timing of future cash flows on the instrument. These cash flows are usually governed by the terms of the instrument, although management judgment may be required in situations where the ability of the counterparty to service the instrument in accordance with the contractual terms is in doubt; and
- (b) An appropriate discount rate of the instrument. Management determines this rate, based on its assessment of the appropriate spread of the rate for the instrument over the risk-free rate. When valuing instruments by reference to comparable instruments, management takes into account the maturity, structure and rating of the instrument with which the position held is being compared. When valuing instruments on a model basis using the fair value of underlying components, management considers, in addition, the need for adjustments to take account of a number of factors such as bid-offer spread, credit profile, servicing costs of portfolios and model uncertainty.

(v) Investment properties

The Group values its investment properties at fair value on the basis of market valuations prepared by independent property consultants. The valuations are based on assumptions which are mainly based on market conditions existing at each reporting date. Therefore, any future change in the market conditions could have an impact on the fair value.

(vi) The ultimate liability arising from claims made under insurance contracts

The estimation of ultimate liability arising from the claims made under insurance contracts is one of the Group's most critical accounting estimates. There are sources of uncertainty that need to be considered in the estimate of the liability that the Group will eventually pay for such claims. Estimates have to be made at the end of the reporting period for both the expected ultimate cost of claims reported and for the expected ultimate cost of claims incurred but not reported ("IBNR"). Liabilities for unpaid reported claims are estimated using the input of assessments for individual cases reported to the Group and management estimates based on past claims settlement trends for the claims incurred but not reported. At the end of each reporting period, prior year claims estimates are reassessed for adequacy and changes are made to the provision.

(vii) Classification and measurement of financial assets

The classification and measurement of the financial assets depend on the management's business model for managing its financial assets and on the contractual cash flow characteristics of the financial asset assessed. Management is satisfied that the Group's investments in securities are appropriately classified and measured.

**Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)**

5 Cash and balances with central banks

(a) The analysis of the Group's cash and balances with central banks as at 31 December is as follows:

	2011 AED'000	2010 AED'000
Cash on hand	491,159	614,965
Balances with central banks:		
Current accounts and other balances	1,957,226	4,953,935
Statutory deposits	3,007,415	2,462,822
Certificates of deposit	9,276,000	5,342,000
	<u>14,731,800</u>	<u>13,373,722</u>

(b) The geographical analysis of the cash and balances with central banks is as follows:

	2011 AED'000	2010 AED'000
Balances within the U.A.E.	13,004,314	8,522,334
Balances outside the U.A.E.	1,727,486	4,851,388
	<u>14,731,800</u>	<u>13,373,722</u>

(c) The Group is required to maintain statutory deposits with various central banks on demand, time and other deposits as per the statutory requirements. The statutory deposits are not available for use in the Group's day-to-day operations. Cash on hand and current accounts and other balances are not interest-bearing. Certificate of deposits are interest-bearing.

(d) As of 31 December 2011 AED 367.3 million (2010: AED nil) of the above certificates of deposit provided as collateral for Central Bank of the U.A.E. under repurchase agreements "Repos" (Note 14)

6 Deposits and balances due from banks

(a) The analysis of the Group's deposits and balances due from banks is as follows:

	2011 AED'000	2010 AED'000
Demand	2,328,251	1,827,938
Overnight	1,188,494	212,525
Time	7,218,623	12,146,250
	<u>10,735,368</u>	<u>14,186,713</u>
Less: Allowance for impairment	(587,693)	(534,758)
	<u>10,147,675</u>	<u>13,651,955</u>

**Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)**

6 Deposits and balances due from banks (continued)

(b) The above represent deposits and balances due from:

	2011 AED'000	2010 AED'000
Banks within the U.A.E.	2,737,258	5,765,209
Banks outside the U.A.E.	7,998,110	8,421,504
	10,735,368	14,186,713
Less: Allowance for impairment	(587,693)	(534,758)
	10,147,675	13,651,955

(c) Allowance for impairment movement

	2011 AED'000	2010 AED'000
At 1 January	534,758	480,137
Charged during the year	11,640	53,372
Interest in suspense	41,295	37,056
Written off during the year	-	(35,807)
At 31 December	587,693	534,758

**Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)**

7 Other financial assets

(a) The analysis of the Group's other financial assets as at 31 December is as follows:

	2011 AED'000	2010 AED'000
Other financial assets measured at fair value		
(i) Investments measured at fair value through profit and loss (FVTPL)		
<i>Debt securities</i>		
Corporate bonds and Treasury bills	520,422	341,511
Sukuk	19,587	21,302
	540,009	362,813
<i>Equities</i>		
Quoted	39,699	117,072
Unquoted	652	678
	40,351	117,750
Mutual and other funds	433,664	110,567
	1,014,024	591,130
(ii) Investments measured at fair value through other comprehensive income (FVTOCI)		
<i>Equities</i>		
Quoted	871,772	925,947
Unquoted	390,794	436,589
	1,262,566	1,362,536
Mutual and other funds	276,198	269,014
	1,538,764	1,631,550
Total other financial assets measured at fair value (A)	2,552,788	2,222,680
(iii) Other financial assets measured at amortised cost		
<i>Debt securities</i>		
Bonds	4,951,842	4,944,056
Sukuk	2,229,751	3,139,755
	7,181,593	8,083,811
Total other financial assets measured at amortised cost (B)	7,181,593	8,083,811
Total other financial assets [(A) +(B)]	9,734,381	10,306,491

**Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)**

7 Other financial assets (continued)

(b) The geographic analysis of investments is as follows:

	2011 AED'000	2010 AED'000
Balances within the U.A.E.	6,051,962	7,556,238
Balances outside the U.A.E.	3,682,419	2,750,253
	9,734,381	10,306,491
	9,734,381	10,306,491

(c) The analysis of investments by industry sector is as follows:

	2011 AED'000	2010 AED'000
Government and Public Sector	3,758,068	3,400,307
Commercial and Business	548,762	699,912
Financial Institutions	4,968,161	5,394,774
Other	459,390	811,498
	9,734,381	10,306,491
	9,734,381	10,306,491

- (d) The fair value of other financial assets measured at amortised cost amounted to AED 6,851.66 million as of 31 December 2011 (2010: AED 7,755.23 million).
- (e) The above other financial assets include debt securities aggregating to AED 3,095.74 million (2010: AED 4,691.47 million) which were sold under repurchase agreement (Repos) (Note 14).
- (f) Other financial assets measured at FVTOCI are strategic investments in equity instruments and mutual funds that are not held to benefit from changes in their fair value and are not held for trading. The management believes therefore that designating these instruments as at FVTOCI provides a more meaningful presentation of its medium to long-term interest in its investments than holding the investments at fair value through profit and loss.
- (g) Other financial assets measured at FVTOCI includes AED 218.21 million (2010: AED 214.54 million) which represents investments in Emerging Markets Credit Opportunities Fund, Makaseb Income Fund, Mashreq Al Islami Income Fund, MCF Series and Mashreq Arab Tigers Fund. These funds are managed by the Group and have no fixed maturity or coupon rate. The fair value of these investments is based on quoted market prices.
- (h) As of 31 December 2011, there are no significant concentrations of credit risk for debt instruments measured at amortised cost. The carrying amount reflected above represents the Group's maximum exposure for credit risk for such assets.
- (i) During the year ended 31 December 2011, dividends received from financial assets measured at FVTOCI amounting to AED 43.06 million (2010: AED 38.21 million) were recognized as investment income in the consolidated income statement (Note 29).

**Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)**

8 Loans and advances measured at amortised cost

(a) The analysis of the Group's loans and advances measured at amortised cost is as follows:

	2011	2010
	AED'000	AED'000
Loans	29,577,932	31,511,847
Overdrafts	4,037,985	5,566,230
Credit cards	1,482,708	1,764,167
Other	161,743	177,452
	35,260,368	39,019,696
Less: Allowance for impairment	(2,594,406)	(3,099,714)
	32,665,962	35,919,982

(b) The analysis of loans and advances measured at amortised cost by industry sector is as follows:

	2011	2010
	AED'000	AED'000
Manufacturing	2,805,029	1,873,389
Construction	2,566,833	3,522,034
Trade	6,479,620	6,361,922
Transport and communication	1,092,463	1,446,582
Services	4,624,304	4,263,202
Financial institutions	2,823,938	2,934,528
Personal	9,442,197	10,377,708
Government and public sector	5,383,134	8,184,883
Other	42,850	55,448
	35,260,368	39,019,696
Less: Allowance for impairment	(2,594,406)	(3,099,714)
	32,665,962	35,919,982

(c) As at 31 December 2011, AED Nil (2010: AED 756.49 million) of the above balances was sold under repurchase agreement (Repos) (Note 15).

**Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)**

8 Loans and advances measured at amortised cost (continued)

- (d) In certain cases, the Group continues to carry classified doubtful debts and delinquent accounts on its books even after making 100% provision for impairment. Interest is accrued on most of those accounts for litigation purposes only and accordingly not taken to consolidated income statement. Accounts are written off only when all legal and other avenues for recovery or settlement are exhausted. The value of loans and advances on which interest is not taken to consolidated income statement, including fully provided accounts, amounted to AED 4,861.94 million at 31 December 2011 (2010: AED 3,774.52 million).
- (e) The movement in the allowance for impairment of loans and advances measured at amortised cost during the year was as follows:

	2011 AED'000	2010 AED'000
At 1 January	3,099,714	1,947,274
Impairment allowance for the year	640,286	928,974
Interest in suspense	220,476	274,060
Recoveries during the year	(50,715)	(50,594)
Written off during the year	(1,315,355)	-
At 31 December	2,594,406	3,099,714

- (f) In determining the recoverability of loans and advances, the Group considers any change in the credit quality of the loans and advances measured at amortised cost from the date credit was initially granted up to the end of the reporting period. The concentration of credit risk is limited due to the fact that the customer base is large and unrelated.

**Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)**

9 Islamic financing and investment products measured at amortised cost

- (a) The analysis of the Group's Islamic financing and investment products measured at amortised cost is as follows:

	2011 AED'000	2010 AED'000
<u>Financing</u>		
Murabaha	2,614,266	1,971,632
Ijara	1,417,406	2,234,472
	4,031,672	4,206,104
<u>Investment</u>		
Musharakah	807,876	919,329
Mudaraba	363,230	320,106
	1,171,106	1,239,435
Total	5,202,778	5,445,539
Less: Unearned income	(108,940)	(18,542)
Allowance for impairment	(65,291)	(136,093)
	5,028,547	5,290,904

**Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)**

9 Islamic financing and investment products measured at amortised cost (continued)

- (b) The analysis of Islamic financing and investment products measured at amortised cost by industry sector is as follows:

	2011 AED'000	2010 AED'000
Government and public sector	1,211,744	1,866,707
Construction	1,228,353	1,492,325
Services	1,312,529	1,312,940
Financial institutions	257,361	350,816
Personal	923,281	352,736
Transport and communication	9,016	38,321
Trade	172,738	10,555
Other	87,756	21,139
Total	5,202,778	5,445,539
Less: Unearned income	(108,940)	(18,542)
Allowance for impairment	(65,291)	(136,093)
	5,028,547	5,290,904

- (c) The value of Islamic financing and investment products on which profit is not taken to consolidated income statement, including fully provided accounts, amounted to AED 239.97 million as at 31 December 2011 (2010: AED 174.96 million).

- (d) Allowance for impairment movement

	2011 AED'000	2010 AED'000
At 1 January	136,093	52,560
Charged during the year	30,980	69,205
Profit in suspense	1,916	14,328
Written off during the year	(103,698)	-
At 31 December	65,291	136,093

- (e) In determining the recoverability of Islamic financing and investment products, the Group considers any change in the credit quality of the Islamic financing and investment products measured at amortised cost from the date credit was initially granted up to the end of the reporting period. The concentration of credit risk is limited due to the fact that the customer base is large and unrelated.
- (f) As of 31 December 2011, AED Nil (2010: AED 285.5 million) of the above balances was sold under repurchase agreement (Repos) (Note 16).

**Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)**

10 Interest receivable and other assets

	2011 AED'000	2010 AED'000
Interest receivable	139,394	147,391
Property acquired in settlement of debts**	230,508	230,683
Prepayments	82,209	69,133
Acceptances*	2,334,057	1,883,478
Positive fair value of derivatives (Note 40)	1,415,577	1,117,578
Insurance related receivables	979,427	971,111
Credit card interchange receivables	37,654	31,771
Taxes paid in advance	20,753	20,398
Other	177,523	514,883
	5,417,102	4,986,426
	5,417,102	4,986,426

* Acceptances are recognized as a financial liability (Note 18) in the consolidated statement of financial position with a contractual right of reimbursement from the customer as a financial asset.

** As of 31 December 2011, property acquired in settlement of debts includes land with a carrying amount of AED 227 million which is registered in the name of the Group's Chief Executive Officer on trust and for the benefit of the Group.

11 Investment properties

	2011 AED'000	2010 AED'000
<i>At fair value</i>		
At 1 January	172,320	233,649
Purchases	93,105	-
Transfers from other assets	113,791	-
Change in fair value during the year (Note 30)	(61,188)	(61,329)
	318,028	172,320
	318,028	172,320

The fair value of investment properties for the Group's subsidiaries Osool - A Finance Company (PJSC) (AED 2.25 million) and Oman Insurance Company (PSC) (AED 315.78 million) as of 31 December 2011 has been arrived at on the basis of a valuation carried out in December 2011 by independent professionally qualified valuers. The valuation, which conforms to international valuation standards, was arrived at by the reference to market comparable evidence of transaction prices for similar properties.

All of the Group's investment properties are held under free hold interest and located in the U.A.E.

Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)

12 Property and equipment

Cost	Properties for own use AED'000	Furniture, fixtures, equipments & vehicles AED'000	Improvements to freehold properties and others AED'000	Capital work-in- progress AED'000	Total AED'000
31 December 2009	637,934	348,916	312,691	41,458	1,340,999
Additions	272,269	47,034	61,403	28,736	409,442
Disposals/write-offs	(71,643)	(17,555)	(52,569)	(690)	(142,457)
Transfers	-	5,382	(39)	(5,343)	-
31 December 2010	838,560	383,777	321,486	64,161	1,607,984
Additions	180,560	68,301	124,055	5,336	378,252
Disposals/write-offs	(8,964)	(57,462)	(56,634)	(4,556)	(127,616)
Transfers	46,419	7,020	14	(53,453)	-
31 December 2011	1,056,575	401,636	388,921	11,488	1,858,620
Accumulated depreciation and impairment					
31 December 2009	99,536	136,849	126,637	-	363,022
Charge for the year	14,536	65,425	63,047	-	143,008
Disposals/write-offs	(63,791)	(14,463)	(46,795)	-	(125,049)
Impairment of property and equipment (Note 32)	83,000	-	-	-	83,000
31 December 2010	133,281	187,811	142,889	-	463,981
Charge for the year	17,202	68,811	72,948	-	158,961
Disposals/write-offs	(5,518)	(42,380)	(52,538)	-	(100,436)
Impairment of property and equipment (Note 32)	138,287	-	-	-	138,287
31 December 2011	283,252	214,242	163,299	-	660,793
Carrying amount					
31 December 2011	773,323	187,394	225,622	11,488	1,197,827
31 December 2010	705,279	195,966	178,597	64,161	1,144,003

**Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)**

13 Deposits and balances due to banks

(a) The analysis of deposits and balances due to banks is as follows:

	2011 AED'000	2010 AED'000
Time	5,663,231	4,477,913
Demand	1,082,654	1,130,926
Overnight	477,485	429,787
	7,223,370	6,038,626

(b) The above represent borrowings from:

	2011 AED'000	2010 AED'000
Banks within the U.A.E.	2,451,347	1,434,782
Banks outside the U.A.E.	4,772,023	4,603,844
	7,223,370	6,038,626

(c) Deposits and balances due to banks abroad include an amount of AED 1,836.50 million (USD 500 million) (2010: AED 1,836.50 million (USD 500 million)) being a 5 years syndicated loan obtained through a syndicate of banks maturing in July 2012. The loan carries a floating rate of interest which is fixed by reference to 3 months LIBOR.

**Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)**

14 Repurchase agreements with banks

Tenure	Due date	Interest rate	2011 AED'000	2010 AED'000
6 months	January 2012	1.20% per annum	483,824	-
1 month	January 2012	1.20% per annum	23,203	-
1 month	January 2012	1.50% per annum	284,430	-
1 month	January 2012	1.50% per annum	187,197	-
1 month	January 2012	0.50% per annum	8,207	-
1 month	January 2012	0.45% per annum	11,155	-
1 month	January 2012	0.50% per annum	11,875	-
1 month	January 2012	0.70% per annum	367,300*	-
1 month	January 2012	1.50% per annum	739,000*	-
3 months	February 2012	1.64% per annum	388,974	-
1 month	January 2011	1.27% per annum	-	257,026
3 months	January 2011	2.30% per annum	-	1,488,630
1 month	January 2011	1.25% per annum	-	48,623
1 month	January 2011	1.50% per annum	-	907,000*
3 months	March 2011	0.70% per annum	-	23,090
3 months	March 2011	0.80% per annum	-	517,538
1 year	October 2011	3 months USD Libor	-	127,086
			2,505,165	3,368,993

*Amount represents repurchase agreements with the U.A.E. Central Bank.

Collateral given against these repo borrowings is disclosed in Notes 5 and 7 to the consolidated financial statements.

15 Customers' deposits

(a) The analysis of customers' deposits is as follows:

	2011 AED'000	2010 AED'000
Current and other accounts	14,125,443	11,637,824
Saving accounts	3,127,472	2,308,704
Time deposits	22,924,105	32,818,330
	40,177,020	46,764,858

(b) As at 31 December 2011, customers' deposits include AED Nil (2010: AED 416 million) under repurchase borrowing agreements (Repo) with customers. Collateral given against these repo borrowings is disclosed in Note 8 to the consolidated financial statements.

**Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)**

15 Customers' deposits (continued)

(c) Analysis by industry sector:

	2011 AED'000	2010 AED'000
Government and public sector	4,960,330	9,981,839
Commercial and business	22,234,986	20,865,352
Personal	10,725,104	12,882,886
Financial institutions	2,184,264	2,203,579
Other	72,336	831,202
	40,177,020	46,764,858

16 Islamic customers' deposits

(a) The analysis of Islamic customers' deposits is as follows:

	2011 AED'000	2010 AED'000
Current and other accounts	375,724	337,146
Saving accounts	189,705	17,461
Time deposits	4,674,434	4,134,208
	5,239,863	4,488,815

(b) As at 31 December 2011, customer deposits include AED Nil (2010: AED 161 million) repurchase borrowing agreements (Repo) with customers. Collateral given against these repo borrowings is disclosed in Note 9 to the consolidated financial statements.

(c) Analysis by industry sector:

	2011 AED'000	2010 AED'000
Government and public sector	278,542	3,198
Commercial and business	4,212,088	3,951,447
Personal	737,756	519,026
Financial institutions	9,024	15,144
Other	2,453	-
	5,239,863	4,488,815

**Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)**

17 Insurance and life assurance funds

	Outstanding claims AED'000	Unearned premium reserve AED'000	Additional reserve AED'000	Life assurance fund AED'000	Total AED'000
At 1 January 2010	239,006	419,215	92,413	107,953	858,587
Increase/(decrease)	41,114	(29,681)	8,000	18,567	38,000
At 31 December 2010	280,120	389,534	100,413	126,520	896,587
Increase/(decrease)	23,805	(43,464)	28,554	67,385	76,280
At 31 December 2011	303,925	346,070	128,967	193,905	972,867

Unearned premium reserve is calculated as a percentage of annual premiums earned, net of reinsurance. Additional reserves are also made for the estimated excess of potential claims and claims incurred but not reported at the reporting date.

Life assurance fund is determined by an independent actuarial valuation of future policy benefits.

18 Interest payable and other liabilities

	2011 AED'000	2010 AED'000
Interest payable	169,173	295,809
Negative fair value of derivatives (Note 40)	1,382,807	1,094,956
Acceptances*	2,334,057	1,883,478
Insurance premium collected in advance	457,691	401,523
Accrued expenses	432,002	511,713
Income received in advance – discounted bills	84,563	68,349
Pay orders issued	139,353	107,289
Provision for employees' end of service indemnity**	147,991	145,241
Credit card related	103,362	61,834
Provision for taxation	25,225	25,792
Other	399,944	394,600
	5,676,168	4,990,584

* Acceptances are recognized as a financial liability in the consolidated statement of financial position with a contractual right of reimbursement from the customer as a financial asset (Note 10).

** Provision for employees' end of service indemnity is made for estimated amounts required to cover employees' end of service indemnity at the reporting date as per U.A.E. Labour Law. In the opinion of management, the provision would not have been materially different had it been calculated on an actuarial basis.

**Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)**

19 Medium-term loans

	2011 AED'000	2010 AED'000
Tier 2 loan from the Ministry of Finance of the U.A.E.	3,443,593	3,443,593
Medium term floating rate notes	1,190,419	2,459,441
	4,634,012	5,903,034

(a) Tier 2 loan from the Ministry of Finance of the U.A.E.

The Tier 2 loan from the Ministry of Finance of the U.A.E. will mature in 2016 and qualifies for Tier 2 subordinated loan capital for the first 2 years and thereafter it is amortised at the rate of 20% per annum for the last five years until its maturity on 31 December 2016 for capital adequacy calculation purposes.

Interest is paid every three months and calculated at a rate of 4.00% for the first and second year, 4.50% for the third year, 5.00% for the fourth year and 5.25% for the last three years.

(b) Medium term floating rate notes

The maturities of the bonds (FRN) issued under the programme are as follows:

Due date	Interest rate	2011 AED'000	2010 AED'000
6 April 2011	3 months Libor + 0.380%	-	1,101,900
24 January 2017	3 months Libor + 0.625%	1,190,419	1,357,541
		1,190,419	2,459,441

During 2004, the Bank established a Euro Medium Term Note (EMTN) programme for USD 750 million (AED 2,754 million) under fiscal agency agreement dated 4 February 2004. The EMTN programme was increased to USD 2,000 million (AED 7,346 million) under fiscal agency agreement dated 21 March 2006. On 15 March 2010, the EMTN programme limit was further increased to USD 5,000 million (AED 18,365 million).

AED 1.19 billion is a subordinated floating rate note ("FRN") and qualifies for Tier 2 subordinated loan capital for the first 5 years till 2012 and thereafter it will be amortised at the rate of 20% per annum for next five years until 2017 for capital adequacy calculation purposes. However, the FRN is callable in 5 years (i.e. in 2012 if not redeemed on completion of 5 years, there is provision of step up in coupon rate by 0.5% for next 5 years). This subordinated FRN has been approved by U.A.E. Central Bank as Tier 2 capital.

**Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)**

20 Long-term loans

These represent long-term loans provided by the Real Estate Committee of the U.A.E. to refinance real estate loans made by the Group to various U.A.E. citizens, which are included in loans and advances measured at amortised cost.

21 Issued and paid up capital and reserves

(a) Issued and paid up capital

As of 31 December 2011, 169,076,975 ordinary shares of AED 10 each (31 December 2010: 169,076,975 ordinary shares of AED 10 each) were fully issued and paid up.

(b) Statutory and legal reserves

In accordance with Union Law 10/80 of U.A.E., 10% of the profit for the year is to be transferred to statutory reserve. Such transfers to reserves may cease when they reach the levels established by the respective regulatory authorities (in the U.A.E. this level is 50% of the issued and paid up share capital). The legal reserve relates to the Group's foreign operations. Neither the statutory reserve nor the legal reserve is available for distribution.

(c) General reserve

The general reserve is computed pursuant to the Bank's Articles of Association and can be used for the purposes determined by the Ordinary General Meeting.

(d) Cumulative translation adjustment

Exchange differences relating to the translation of the results and net assets of the Group's foreign operations from their functional currencies to the Group's presentation currency (i.e. AED), are recognised directly in other comprehensive income and accumulated in the cumulative translation adjustment reserve. Gains and losses on hedging instruments that are designated as hedging instruments for hedges of net investments in foreign operations are included in the cumulative translation adjustment reserve. Exchange differences previously accumulated in the cumulative translation adjustment reserve (in respect of translating both the net assets of foreign operations and hedges of foreign operations) are reclassified to the consolidated income statements on the disposal of the foreign operation.

(e) Investments revaluation reserve

Investment revaluation reserve shows the effects from the fair value measurement of other financial assets measured at FVTOCI.

(f) Dividends on equity instruments

During the year ended 31 December 2011, a proposed 20% cash dividend amounting to AED 338.15 million was approved by the Board of Directors and ratified by the shareholders at the Annual General Meeting held on 6 March 2011.

**Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)**

22 Non-controlling interests

	2011 AED'000	2010 AED'000
At 1 January	540,239	574,283
Dividends paid	(8,400)	(55,501)
Changes in fair value of financial assets measured at fair value through other comprehensive income, net	10,781	21,457
Purchase of non-controlling interests	(1,580)	-
At 31 December	541,040	540,239

23 Contra accounts and commitments

(a) The analysis of the Group's contra accounts and commitments is as follows:

	2011 AED'000	2010 AED'000
(i) Contra accounts (memoranda)		
Guarantees	38,335,059	36,942,725
Letters of credit	6,279,121	4,185,968
	44,614,180	41,128,693
(ii) Commitments for acquisition of property and equipment	45,965	141,384
(iii) Operating lease commitments	67,283	76,516
Total contra accounts and commitments	44,727,428	41,346,593

(b) Outstanding granted but unutilised facilities as at 31 December 2011 amounted to AED 115,707 million (2010: AED 53,061 million).

**Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)**

23 Contra accounts and commitments (continued)

(c) Contra accounts – maturity profile

The maturity profile of the Group's contra accounts were as follows:

2011

	Within 3 months AED'000	Over 3 to 6 months AED'000	Over 6 to 12 months AED'000	Over 1 to 5 years AED'000	Over 5 years AED'000	Total AED'000
Guarantees	14,026,686	2,018,797	2,327,120	6,617,369	13,345,087	38,335,059
Letters of credit	3,830,823	871,959	957,490	618,849	-	6,279,121
Total	17,857,509	2,890,756	3,284,610	7,236,218	13,345,087	44,614,180

2010

	Within 3 months AED'000	Over 3 to 6 months AED'000	Over 6 to 12 months AED'000	Over 1 to 5 years AED'000	Over 5 years AED'000	Total AED'000
Guarantees	15,222,045	1,627,878	2,111,036	5,884,359	12,097,407	36,942,725
Letters of credit	2,341,926	376,044	648,404	819,594	-	4,185,968
Total	17,563,971	2,003,922	2,759,440	6,703,953	12,097,407	41,128,693

The analysis of commitments and contingencies by geographic region and industry sector is shown in Note 37 to the consolidated financial statements.

(d) Operating lease commitments

The future minimum lease payments payable under non-cancellable operating leases where the Group is the lessee are as follows:

	2011 AED'000	2010 AED'000
Less than 1 year	37,164	37,113
1 to 5 years	28,186	37,080
Over 5 years	1,933	2,323
Total	67,283	76,516

**Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)**

24 Interest income

	2011 AED'000	2010 AED'000
Loans and advances	2,441,091	3,180,830
Banks	344,854	425,404
Other financial assets	284,793	312,292
Central Bank of the U.A.E.	64,708	122,060
	3,135,446	4,040,586

25 Income from Islamic financing and investment products

	2011 AED'000	2010 AED'000
<u>Financing</u>		
Murabaha	104,008	102,295
Ijara	66,288	85,496
Others	29,624	32,232
	199,920	220,023
<u>Investment</u>		
Mushakara	43,838	47,599
Mudaraba	8,923	9,275
Wakala	81	206
	52,842	57,080
Total	252,762	277,103

**Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)**

26 Interest expense

	2011 AED'000	2010 AED'000
Customers' deposits	786,814	1,265,077
Deposits and balances due to central banks	14,196	40,807
Deposits and balances due to other banks	377,901	395,113
Medium-term loans	155,392	162,984
	1,334,303	1,863,981

27 Distribution to depositors – Islamic products

This represents the share of income allocated to depositors of the Group. The allocation and distribution to depositors is approved by the Group's Sharia'a Supervisory Board.

28 Net fee and commission income

	2011 AED'000	2010 AED'000
Fee and commission income		
Commission income	811,084	560,096
Brokerage and asset management	9,359	8,421
Insurance commission	141,558	138,569
Fees and charges on banking services	345,301	444,650
Credit Card related fee	577,093	622,367
Others	56,589	64,453
	1,940,984	1,838,556
Fee and commission expenses		
Commission expense	(340,361)	(100,353)
Brokerage and asset management	(277)	(219)
Insurance commission	(218,645)	(260,748)
Credit Card related expenses	(372,524)	(345,744)
Others	(26,121)	(19,022)
	(957,928)	(726,086)
Total fee and commission expenses	(957,928)	(726,086)
Net fee and commission income	983,056	1,112,470

**Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)**

29 Net investment income

	2011 AED'000	2010 AED'000
Net realized investment gain from sale of other financial assets measured at FVTPL	7,373	2,573
Fair value adjustments of other financial assets measured at FVTPL	(13,189)	1,072
Interest income from debt securities at FVTPL	41,801	19,877
Dividends income from other financial assets measured at FVTPL	1,438	651
Net realized investment gain/(loss) from sale of other financial assets measured at amortised cost	42,888	(14,290)
Dividend income from financial assets measured at FVTOCI	43,056	38,211
	123,367	48,094

30 Other income, net

	2011 AED'000	2010 AED'000
Fair value adjustments of investment properties (Note 11)	(61,188)	(61,329)
Foreign exchange gains, net	204,754	161,672
Insurance and other related income [Note 30(a)]	594,681	563,067
Gain on sale of property and equipment	15,824	181,783
Rental income from properties	7,484	4,548
Fair value adjustment – derivatives	(9,216)	18,581
Gain from redemption of medium-term loans	31,859	22,928
Loss on sale of loans and advances in a secondary market	(2,571)	(55,722)
Other	40,212	99,640
	821,839	935,168

**Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)**

30 Other income, net (continued)

(a) Insurance and other related income

	2011 AED'000	2010 AED'000
Net insurance premium revenue	1,236,137	1,291,781
Net claims incurred	(562,734)	(629,857)
	673,403	661,924
Excess of loss reinsurance premium	(44,191)	(60,643)
Policies surrendered and maturities paid	(25,925)	(29,169)
Insurance business fees	(8,606)	(9,045)
	594,681	563,067

31 General and administrative expenses

	2011 AED'000	2010 AED'000
Salaries and employees related expenses	987,671	962,917
Depreciation on property and equipment (Note 12)	158,961	143,008
Other	647,051	657,972
	1,793,683	1,763,897

Pension and national insurance contribution for U.A.E. citizens are made by the Group in accordance with Federal Law No. 7 of 1999.

**Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)**

32 Allowances for impairment

2011

	Retail AED'000	Corporate and others AED'000	Collective impairment AED'000	Total AED'000
Allowance for impaired loans and advances	169,477	386,961	83,848	640,286
Allowance for impaired balances due from banks	-	11,640	-	11,640
Impairment of other financial assets measured at amortised cost	-	4,800	-	4,800
Allowance for other debtors	-	35,160	-	35,160
Allowance for Islamic assets	16,616	12,164	2,200	30,980
Write-off of impaired loans and advances	493,617	-	-	493,617
Impairment of property and equipment (Note 12)	-	138,287	-	138,287
Recovery of impaired loans and advances	-	(50,715)	-	(50,715)
Recovery of loans and advances previously written off	(76,604)	(31,612)	-	(108,216)
	<u>603,106</u>	<u>506,685</u>	<u>86,048</u>	<u>1,195,839</u>

2010

	Retail AED'000	Corporate and others AED'000	Collective impairment AED'000	Total AED'000
Allowance for impaired loans and advances	55,164	708,474	165,336	928,974
Allowance for impaired balances due from banks	-	53,372	-	53,372
Impairment of other financial assets measured at amortised cost	-	20,034	-	20,034
Allowance for other debtors	-	14,604	-	14,604
Allowance for Islamic assets	12,041	52,664	4,500	69,205
Write-off of impaired loans and advances	746,098	5,979	-	752,077
Impairment of property and equipment (Note 12)	-	83,000	-	83,000
Recovery of impaired loans and advances	-	(50,594)	-	(50,594)
Recovery of loans and advances previously written off	(81,590)	(21,692)	-	(103,282)
	<u>731,713</u>	<u>865,841</u>	<u>169,836</u>	<u>1,767,390</u>

**Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)**

33 Earnings per share

Earnings per share are calculated by dividing the profit for the year by the number of shares outstanding during the year as follows:

	2011 AED	2010 AED
Profit for the year (AED'000) (Attributed to shareholders of the parent)	820,379	803,498
Number of ordinary shares outstanding	169,076,975	169,076,975
Earnings per share (AED)	4.85	4.75
Diluted earnings per share (AED)	4.85	4.75

34 Proposed dividends

The Board of Directors has proposed 20% cash dividend at their meeting held on 1 February 2012.

35 Cash and cash equivalents

Cash and cash equivalents consist of cash on hand, current accounts and other balances with central bank certificates of deposits, balances with banks and money market placements which are maturing within three months from the date of the deposit or placement, as follows:

	2011 AED'000	2010 AED'000
Cash on hand	491,159	614,965
Balances with central banks:		
Current accounts and other balances	1,957,226	4,953,935
Deposits and balances due from banks maturing within 3 months	8,337,273	8,858,786
	10,785,658	14,427,686

**Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)**

36 Related party transactions

- (a) Certain “related parties” (such as, directors and major shareholders of the Group and companies of which they are principal owners) are customers of the Group in the ordinary course of business. Transactions with such related parties are made on substantially the same terms, including interest rates and collateral, as those prevailing at the same time for comparable transactions with external customers and parties. Such related party transactions are disclosed below.
- (b) The Group is controlled by Al Ghurair Family members who own 82.27% of the issued and paid up capital. The remaining shares are widely held.
- (c) Related party balances included in the consolidated statement of financial position are as follows:

	2011	2010
	AED '000	AED '000
Loans and advances measured at amortised cost	2,199,530	2,197,299
Customers' deposits	980,263	1,144,987
Letters of credit and guarantee	2,023,979	2,284,953

- (d) Profit for the year includes related party transactions as follows:

	2011	2010
	AED '000	AED '000
Interest income	126,120	138,114
Interest expense	18,639	46,895
Other income, net	105,214	72,653

- (e) Compensation of key management comprises salaries, bonuses and other benefits amounting in total to AED 64.41 million (2010: AED 59.26 million).

Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)

37 Concentrations of assets, liabilities and off balance sheet items

(a) Geographic regions

	2011			2010		
	Assets AED'000	Liabilities AED'000	Off balance sheet items AED'000	Assets AED'000	Liabilities AED'000	Off balance sheet items AED'000
U.A.E.	55,629,687	50,205,351	32,554,579	60,557,551	56,938,923	30,663,824
Other Middle East Countries	13,651,395	9,488,602	5,602,383	17,040,556	7,332,294	3,774,371
O.E.C.D.	6,911,906	5,139,391	3,358,309	5,463,396	6,726,174	3,309,285
Other	3,048,334	1,604,128	3,098,909	1,784,300	1,463,430	3,381,213
	<u>79,241,322</u>	<u>66,437,472</u>	<u>44,614,180</u>	<u>84,845,803</u>	<u>72,460,821</u>	<u>41,128,693</u>

(b) Industry Sector

	2011			2010		
	Assets AED'000	Liabilities AED'000	Off balance sheet items AED'000	Assets AED'000	Liabilities AED'000	Off balance sheet items AED'000
Government and Public Sector	10,161,488	8,728,419	-	13,191,531	13,396,561	-
Commercial & Business	21,745,271	28,819,468	30,890,007	20,310,792	27,588,803	27,137,162
Personal	9,583,113	11,842,460	912,153	10,282,269	13,522,758	11,615
Financial Institutions	33,948,127	14,193,948	12,769,062	36,591,634	15,910,867	13,050,194
Other	3,803,323	2,853,177	42,958	4,469,577	2,041,832	929,722
	<u>79,241,322</u>	<u>66,437,472</u>	<u>44,614,180</u>	<u>84,845,803</u>	<u>72,460,821</u>	<u>41,128,693</u>

**Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)**

38 Segmental information

Reportable segments

Operating segments are identified on the basis of internal reports about the components of the Group that are regularly reviewed by the Group's CEO (the Group's chief operating decision maker) in order to allocate resources to the segment and to assess its performance. Information reported to the Group's CEO for the purpose of resource allocation and assessment of performance is based on following strategic business units offering products and services to different markets.

The Group's reportable segments under IFRS 8 are therefore as follows:

1. The **Domestic Corporate** segment comprises of corporate and commercial banking customers in the U.A.E. Trade finance, contracting finance, project finance, investment banking, corporate advisory, cash management, wealth management, and SME & private banking are the major products and / or business lines making up this segment.
2. The **Domestic Retail** segment includes products and services offered to individuals or small businesses within the U.A.E. The product offerings to customers include, current accounts, savings accounts, fixed deposits, investment products, "Mashreq Millionaire" deposits, personal loans, auto loans, mortgage loans, business loans, credit cards with unique loyalty programs, bank assurance, overdraft, priority banking and wealth management services.
3. The **Treasury & Capital Markets** segment consists of customer flow business and proprietary business. Customer flow business includes transactions for Foreign Exchange, Derivatives, Margin FX, Futures, Hedging, Investment Products, Domestic Equities (brokerage) and Asset Management undertaken on behalf of customers. The proprietary business includes trading and investing activity undertaken on behalf of the Group.
4. The **International Banking** segment consists of Retail and Corporate business for the Group's overseas banking branches in Qatar, Egypt, Bahrain & Kuwait and the Group's correspondent banking business in other overseas branches which includes trade services, reimbursements, reimbursement undertaking, reimbursement financing, export bills collection, risk participations.
5. All Islamic banking products offered to customers are included under the **Islamic Banking** segment. These products are Ijara Home Finance, Mudarabah Deposit, Mudarabah savings account, Musharaka finance, Murabaha commodity finance, Ijara Equipment Finance, Sukuk Underwriting, Musharaka LC, Murabaha LC, TR Murabaha, Kafala, Wakala Deposit, Reverse Murabaha Deposit & Sukuk Advisory.
6. The Insurance subsidiary, Oman Insurance Company (PSC) – comprises the **Insurance** segment. The product offerings to customers include life, health, motor, marine cargo and hull, aviation, fire and general accident, engineering, liability and personal lines insurance.
7. The **Head office** consists of certain investments and assets held centrally due to their strategic significance to the Group.

The accounting policies of the reportable segments are the same as the Group's accounting policies described in Note 3 to the consolidated financial statements. Segment profit represents the profit earned by each segment without allocation of general and administrative expenses, allowances for impairment and overseas tax expenses. This is the measure reported to the chief operating decision maker for the purposes of resource allocation and assessment of segment performance.

38 Segmental information (continued)

2011

	Domestic corporate AED'000	Domestic retail AED'000	Treasury & capital markets AED'000	International banking AED'000	Islamic banking AED'000	Insurance AED'000	Head office AED'000	Total AED'000
Net interest income and earnings from								
Islamic products	720,560	846,652	(89,538)	225,240	142,927	6,725	91,505	1,944,071
Other income, net	402,959	332,914	293,613	299,861	48,274	485,409	65,232	1,928,262
Total operating income	1,123,519	1,179,566	204,075	525,101	191,201	492,134	156,737	3,872,333
General and administrative expenses								
Allowances for impairment								(1,793,683)
								(1,195,839)
Profit before taxes								882,811
Overseas income tax expense								(21,769)
Profit for the year								861,042
Attributed to:								
Shareholders of the Parent								820,379
Non-controlling interests								40,663
								861,042
Segment Assets	18,986,258	7,168,489	22,384,443	14,420,975	5,951,210	3,278,274	7,051,673	79,241,322
Segment Liabilities	23,582,382	8,792,900	11,209,000	11,478,905	5,280,891	1,882,036	4,211,358	66,437,472

38 Segmental information (continued)

2010

	Domestic corporate AED'000	Domestic retail AED'000	Treasury & capital markets AED'000	International banking AED'000	Islamic banking AED'000	Insurance AED'000	Head office AED'000	Total AED'000
Net interest income and earnings from								
Islamic products	684,223	1,050,596	4,353	199,183	114,537	26,807	211,443	2,291,142
Other income, net	385,400	516,077	244,285	274,738	40,953	404,227	230,052	2,095,732
Total operating income	1,069,623	1,566,673	248,638	473,921	155,490	431,034	441,495	4,386,874
General and administrative expenses								
Allowances for impairment								(1,763,897)
								(1,767,390)
Profit before taxes								855,587
Overseas income tax expense								(18,985)
Profit for the year								836,602
Attributed to:								
Shareholders of the Parent								803,498
Non-controlling interests								33,104
								836,602
Segment Assets	20,051,692	9,149,994	24,880,979	14,748,296	6,203,239	3,542,003	6,269,600	84,845,803
Segment Liabilities	30,351,066	9,367,700	13,226,200	8,489,066	4,509,800	2,101,456	4,415,533	72,460,821

**Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)**

38 Segmental information (continued)

Geographical information

The Group operates in four principal geographical areas – U.A.E. (country of domicile), other Middle East Countries (Kuwait, Bahrain, Egypt and Qatar), O.E.C.D. (USA and UK) and other countries (India, and Hong Kong).

The Group's revenue from continuing operations from external customers and information about its non-current assets by geographical location are detailed below:

	Operating income external customers *		Non-current assets **	
	2011	2010	2011	2010
	AED'000	AED'000	AED'000	AED'000
U.A.E.	3,522,812	4,044,988	1,448,165	1,240,549
Other Middle East countries	231,788	253,304	62,245	72,563
O.E.C.D.	81,123	60,911	4,367	2,664
Other countries	36,610	27,671	1,078	547
	3,872,333	4,386,874	1,515,855	1,316,323

* Operating income from external customers is based on the Group's operational centres.

** Non-current assets excluding financial instruments, deferred tax assets (if any), and assets arising from insurance contracts.

Revenue from major products and services

Revenue from major products and services are disclosed in Notes 24, 25, 28, 29 and 30 in the consolidated financial statements.

Information about major customers

No single customer contributed 10% or more to the Group's revenue for both years ended 31 December 2011 and 2010.

**Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)**

39 Classification of financial assets and liabilities

- (a) The table below sets out the Group's classification of each class of financial assets and liabilities and their carrying amounts as at 31 December 2011:

	FVTPL AED'000	FVTOCI AED'000	Amortised cost AED'000	Total AED'000
Financial assets:				
Cash and balances with central banks	-	-	14,731,800	14,731,800
Deposits and balances due from banks	-	-	10,147,675	10,147,675
Other financial assets measured at fair value	1,014,024	1,538,764	-	2,552,788
Loans and advances measured at amortised cost	-	-	32,665,962	32,665,962
Islamic financing and investment products measured at amortised cost	-	-	5,028,547	5,028,547
Other financial assets measured at amortised cost	-	-	7,181,593	7,181,593
Interest receivable and other assets	1,415,577	-	3,668,055	5,083,632
Total	2,429,601	1,538,764	73,423,632	77,391,997
Financial liabilities:				
Deposits and balances due to banks	-	-	7,223,370	7,223,370
Repurchase agreements with banks	-	-	2,505,165	2,505,165
Customers' deposits	-	-	40,177,020	40,177,020
Islamic customers' deposits	-	-	5,239,863	5,239,863
Interest payable and other liabilities	1,382,807	-	3,577,891	4,960,698
Medium-term loans	-	-	4,634,012	4,634,012
Long-term loans	-	-	9,007	9,007
Total	1,382,807	-	63,366,328	64,749,135

**Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)**

39 Classification of financial assets and liabilities (continued)

- (b) The table below sets out the Group's classification of each class of financial assets and liabilities and their carrying amounts as at 31 December 2010:

	FVTPL AED'000	FVTOCI AED'000	Amortised cost AED'000	Total AED'000
Financial assets:				
Cash and balances with central banks	-	-	13,373,722	13,373,722
Deposits and balances due from banks	-	-	13,651,955	13,651,955
Other financial assets measured at fair value	591,130	1,631,550	-	2,222,680
Loans and advances measured at amortised cost	-	-	35,919,982	35,919,982
Islamic financing and investment products measured at amortised cost	-	-	5,290,904	5,290,904
Other financial assets measured at amortised cost	-	-	8,083,811	8,083,811
Interest receivable and other assets	1,117,578	-	3,548,634	4,666,212
Total	1,708,708	1,631,550	79,869,008	83,209,266
Financial liabilities:				
Deposits and balances due to banks	-	-	6,038,626	6,038,626
Repurchase agreements with banks	-	-	3,368,993	3,368,993
Customers' deposits	-	-	46,764,858	46,764,858
Islamic customers' deposits	-	-	4,488,815	4,488,815
Interest payable and other liabilities	1,094,956	-	3,254,723	4,349,679
Medium-term loans	-	-	5,903,034	5,903,034
Long-term loans	-	-	9,324	9,324
Total	1,094,956	-	69,828,373	70,923,329

**Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)**

40 Derivatives

In the ordinary course of business, the Group utilizes the following derivative financial instruments for both trading and hedging purposes:

- (a) Swaps are commitments to exchange one set of cash flows for another. For interest rate swaps, counter-parties generally exchange fixed and floating rate interest payments in a single currency without exchanging principal. For currency swaps, fixed interest payments and principal are exchanged in different currencies. For cross-currency rate swaps, principal, fixed and floating interest payments are exchanged in different currencies.
- (b) Credit Default Swap (CDS) is a swap contract in which the buyer of the CDS makes a series of payments to the seller and, in exchange, receives a payoff if a debt instrument goes into default and fails to pay.
- (c) Forwards and futures are contractual agreements to either buy or sell a specified currency, commodity or financial instrument at a specified price and date in the future. Forwards are customized contracts transacted in the over-the-counter market. Foreign currency and interest rate futures are transacted in standardized amounts on regulated exchanges and changes in futures contract values are marked to market daily.
- (d) Forward rate agreements are similar to interest rate futures, but are individually negotiated. They call for a cash settlement for the difference between a contracted interest rate and the market rate on a specified future date, on a notional principal for an agreed period of time.
- (e) Options are contractual agreements under which the seller (writer) grants the purchaser (holder) the right, but not the obligation, to either buy or sell at fixed future date or at any time during a specified period, a specified amount of a currency, commodity or financial instrument at a pre-determined price.

Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)

40 Derivatives (continued)

Statement of Derivatives as at 31 December 2011

	Positive fair value AED'000	Negative fair value AED'000	Notional amount AED'000	Notional amount by term maturity				
				Up to 3 months AED'000	3 – 6 months AED'000	6 – 12 months AED'000	1 year to 5 years AED'000	Over 5 years AED'000
Forward foreign exchange contract	128,504	115,026	23,297,382	16,105,966	3,774,214	1,441,099	1,976,103	-
Foreign exchange options (bought)	-	31,768	5,542,410	486,742	2,113,199	2,626,834	315,635	-
Foreign exchange options (sold)	31,642	-	7,001,116	1,975,745	2,092,581	2,617,156	315,634	-
Interest rate swaps	1,246,603	1,220,309	22,220,366	4,103,569	1,929,112	2,282,951	6,095,313	7,809,421
Credit Default Swaps	-	6,982	102,849	-	-	-	102,849	-
Equity options	1,140	1,034	663,141	486,978	87,784	7,346	81,033	-
Futures contracts purchased (Customer)	-	6,447	172,065	170,978	1,087	-	-	-
Futures contracts sold (Customer)	1,241	-	178,890	178,838	52	-	-	-
Futures contracts sold (Bank)	6,447	-	172,065	170,978	1,087	-	-	-
Futures contracts purchased (Bank)	-	1,241	178,890	178,838	52	-	-	-
	1,415,577	1,382,807	59,529,174	23,858,632	9,999,168	8,975,386	8,886,567	7,809,421

Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)

40 Derivatives (continued)

Statement of Derivatives as at 31 December 2010

	Positive fair value AED'000	Negative fair value AED'000	Notional amount AED'000	Notional amount by term maturity				
				Up to 3 months AED'000	3 – 6 months AED'000	6 – 12 months AED'000	1 year to 5 years AED'000	Over 5 years AED'000
Forward foreign exchange contract	237,255	202,764	30,627,886	21,221,183	3,431,627	5,823,216	151,860	-
Foreign exchange options (bought)	-	84,895	8,972,288	5,324,298	3,116,773	349,993	181,224	-
Foreign exchange options (sold)	84,990	-	12,709,233	5,247,860	3,106,550	4,173,599	181,224	-
Interest rate swaps	787,935	796,010	16,058,219	796,064	319,092	3,620,272	8,910,226	2,412,565
Equity derivatives	5,277	9,166	286,480	13,763	26,993	89,303	156,421	-
Futures contracts purchased (Customer)	-	7	104,452	104,452	-	-	-	-
Futures contracts sold (Customer)	-	2,114	109,601	107,068	-	2,533	-	-
Futures contracts sold (Bank)	7	-	104,452	104,452	-	-	-	-
Futures contracts purchased (Bank)	2,114	-	109,601	107,068	-	2,533	-	-
	1,117,578	1,094,956	69,082,212	33,026,208	10,001,035	14,061,449	9,580,955	2,412,565

**Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)**

41. Capital management

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

- To comply with the capital requirements set by the BCBS (Basel Committee) and the regulators of the banking markets where the entities within the Group operate;
- To safeguard the Group's ability to continue as a going concern so that it can continue to provide returns for shareholders and benefits for other stakeholders; and
- To maintain a strong capital base and capital buffer to support the development of its business.

Regulatory capital

The Central Bank of the U.A.E. sets and monitors capital requirements for the Group as a whole. The parent company and overseas banking operations are directly supervised by their local regulators.

The Central Bank of the U.A.E. adopted the Basel Two capital regime in November 2009. The Bank calculates its Capital Adequacy Ratio in line with guidelines issued by the Central Bank of the U.A.E. The minimum capital ratio prescribed by the Central Bank is 12% of Risk Weighted Assets (RWA) calculated as per the guidelines issued by them.

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

- Tier 1 capital, which includes issued and paid-up share capital, retained earnings, cumulative translation adjustment and non-controlling interests in the equity of subsidiaries less than wholly owned, after deductions for goodwill and intangible assets, if any.
- Tier 2 capital, which includes general provisions (Collective allowance for impairment subject to a limit of 1.25% of RWA), qualifying subordinated liabilities and the element of the investment revaluation reserve (up to a maximum of 45% of the excess of market value over the net book value) relating to unrealised gains on investments classified as other financial assets measured at FVTOCI.
- Deductions from the total of tier 1 capital and tier 2 capital must be made for investments in the insurance subsidiary to prevent the multiple use of the same capital resources in different parts of the Group; however the Regulator may allow use of excess capital (over regulatory limits) invested.

**Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)**

41 Capital management (continued)

Regulatory capital (continued)

Various limits are applied to elements of the capital base. The qualifying tier 2 capital cannot exceed tier 1 capital; and qualifying term subordinated loan capital may not exceed 50 percent of tier 1 capital. The tier 1 capital must be a minimum of 7% of RWA and Tier 2 Capital cannot exceed 67% of Tier 1 Capital.

The Group's assets are risk weighted as to their relative credit, market, and operational risk. Credit risk includes both on and off-balance sheet risks. Market risk is defined as the risk of losses in on and off-balance sheet positions arising from movements in market prices and includes interest rate risk, foreign exchange risk, equity exposure risk, commodity risk, and options risk. Operational risk is defined as the risk of loss resulting from inadequate or failed internal processes, people or systems, or from external events. For U.A.E. Central Bank reporting purposes, the bank is currently following the standardized measurement approach for credit, market and operational risk, as per Pillar 1 of Basel 2.

The Group's policy is to maintain a strong capital base so as to maintain market confidence and to sustain future development of the business. The impact of the level of capital on shareholders' return is also recognised and the Group recognises the need to maintain a balance between the higher returns that might be possible with greater gearing and the advantages and security afforded by a sound capital position. Historically the Group has followed a conservative dividend policy to increase capital from internal resources to meet future growth. To further strengthen the capital base and to ensure effective management of capital, the Group issued in the year ended 31 December 2007 medium-term floating rates notes which have been approved by the U.A.E. Central bank to be treated as Tier 2 capital. In addition, the U.A.E. Ministry of Finance provided long term loans in 2009 which are also treated as Tier 2 capital.

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

There have been no material changes in the Group's management of capital during the year.

The Group's regulatory capital positions as at 31 December 2011 and 2010 were as follows:

**Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)**

41 Capital management (continued)

Regulatory capital (continued)

	2011 AED'000	2010 AED'000
<i>Tier 1 capital</i>		
Issued and paid up capital	1,690,770	1,690,770
Statutory and legal reserve	846,745	845,385
General reserve	312,000	312,000
Cumulative translation adjustment	(33,022)	(19,483)
Retained earnings	9,792,462	9,300,191
Non-controlling interest	5,271	13,948
Total	12,614,226	12,142,811
<i>Tier 2 capital</i>		
Allowance for collective impairment	767,639	682,152
Investments revaluation reserve	(346,145)	(284,120)
Qualifying subordinated liabilities*	4,634,012	4,801,134
Total	5,055,506	5,199,166
Deduction from capital	(31,825)	(31,825)
Total capital base (A)	17,637,907	17,310,152
<i>Risk-weighted assets</i>		
Credit risk	71,108,245	70,589,478
Market risk	309,477	348,316
Operational risk	6,472,458	5,351,405
Total risk-weighted assets (B)	77,890,180	76,289,199
Risk asset ratio [(A)/(B) x 100]	22.64%	22.69%

* Qualifying subordinated liabilities represents the following:

	2011 AED'000	2010 AED'000
Tier 2 loan from the Ministry of Finance of the U.A.E. [Note 19(a)]	3,443,593	3,443,593
Medium-term floating rate notes [Note 19(b)]	1,190,419	1,357,541
	4,634,012	4,801,134

**Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)**

41 Capital management (continued)

Capital allocation

The allocation of capital between specific operations and activities is, to a large extent, driven by optimisation of the return achieved on the capital allocated. The amount of capital allocated to each operation or activity is based on the inherent risk it carries. The process of allocating capital to specific operations and activities is undertaken independently of those responsible for the operation, by Finance and Risk Groups, and is subject to review by the Bank's Assets and Liabilities Committee (ALCO) as appropriate.

Although maximisation of the return on risk-adjusted capital is the principal basis used in determining how capital is allocated within the Group to particular operations or activities, it is not the sole basis used for decision making. Account also is taken of synergies with other operations and activities, the availability of management and other resources, and the fit of the activity with the Group's longer term strategic objectives. The Group's policies in respect of capital management and allocation are reviewed regularly by the Board of Directors.

42 Risk management

The Group has set up a risk management infrastructure supported by adoption of best practices in the field of risk management to manage and monitor the following major risks arising out of its day to day operations:

- Credit risk management
- Operational risk management
- Market risk management (Interest rate risk and currency risk)
- Liquidity risk management

The Risk Committee, Assets and Liabilities Committee (ALCO) and Investment Committee work under the mandate of the Board of Directors (BOD) to set up risk limits and manage the overall risk in the Group. These committees approve risk management policies of the Group developed by the Risk Management Group.

The Risk Committee has overall responsibility for the oversight of the risk management framework and the risk appetite of the Group. It has established detailed policies and procedures in this regard along with senior management committees to ensure adherence to the approved policies and close monitoring of different risks within the Group. In addition to setting the credit policies of the Group, the Risk Committee also establishes various concentration limits, approves policy exceptions and monitors periodic portfolio reviews to ascertain portfolio quality.

The Risk Management Group function is independent of the business and is led by a qualified Risk Management Head, with enterprise-wide responsibility for the function. The Risk Management Group is responsible for developing credit, market and operational risk policies. Experienced and trained Risk Managers have delegated authority within the risk management framework to approve credit risk transactions and monitor market and operational risks.

**Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)**

42 Risk management (continued)

The Credit Risk and Control Unit within Risk Management Group is responsible for developing, validating and revalidating Basel 2 risk models for risk ratings and scoring, including calculating and recalibrating Probability of Default (“PD”), Loss Given Default (“LGD”), and Exposure At Default (“EAD”) variables.

The Economic Capital team within Risk Management Group is responsible for calculating the Group’s economic capital requirement and managing the Group’s Internal Capital Adequacy Assessment Process (ICAAP). This entails monitoring the Group’s capital adequacy under a variety of stressed scenarios to assess and report the impact upon the Group’s capital buffer (measured as available capital less risk capital demand) and recommending appropriate actions, as required.

The Group has a progressive risk rating system in place, and a conservative policy for early recognition of impairment and for providing for non-performing assets. As part of its analysis of portfolio pressure points, the Group carries out periodic stress testing to its entire portfolio and takes appropriate action to (i) mitigate risks arising out of specific obligors or industries and/or due to global risk events and their implications on the Group’s client base, and (ii) determine portfolio direction and resource allocation accordingly.

The Risk Management Group oversees credit, market and operational risks. Different credit underwriting procedures are followed for commercial and institutional lending, and retail lending, as described below.

Credit risk management

Credit risk is the potential for financial loss arising from a borrower’s or counterparty’s inability to meet its obligations.

All credit policies are reviewed and approved by the Group’s Risk Committee.

Whenever possible, loans are secured by acceptable forms of collateral in order to mitigate credit risk. The Group further limits risk through diversification of its assets by geography and industry sectors.

Wholesale credit risk management

The Wholesale Credit Risk Management team centrally approves all credit facilities and limits for all corporate, treasury and capital markets, financial institutions and SME clients of the Group. Such approvals are carried out in accordance with the Group’s credit policy as set out in the Wholesale Credit Policy Manual. Periodic policy revisions and updates are posted as Policy Bulletins.

All credit lines or facilities extended by the Group are granted subject to prior approval pursuant to a set of delegated credit authority limits as recommended by the Risk Management Head in line with the Wholesale Credit Policy, and approved by the Group’s Chief Executive Officer (the “CEO”). At least two signatures are required to approve any credit application. Depending on factors such as the nature of the applicant, magnitude of credit, its risk rating, the client type or a specific policy issue, a third concurring signature may sometimes be required, as defined in the Credit Policy Manual.

All credit applications for commercial and institutional lending are subject to the Group’s credit policies, underwriting standards and industry caps (if any) and to regulatory requirements, as applicable from time to time. The Group does not lend to companies operating in industries that are considered by the Group inherently risky and where specialized industry knowledge is required.

Limit setting is based on a combination of factors, including a detailed evaluation of each customer’s creditworthiness based on proven performance, industry, management and financial analysis (both historical and projected), risk rating, and analysis of facilities (tenor & types of facilities, pricing, collateral and support).

**Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)**

42 Risk management (continued)

Credit risk management (continued)

Wholesale credit risk management (continued)

Credit and Marketing functions are segregated. Furthermore, all credit facilities are independently administered and monitored by the Credit Operations (Administration) Department, which separately reports to Operations & Technology Group.

The Group has established limits for managing transferability and convertibility, together defined as cross-border limits. These limits are regularly reviewed by the Risk Management Group and periodically by the Risk Committee. Individual country limits are set out based on each country's financial strength and stability, using a set of metrics such as external debt, overall fiscal position, exports, imports, foreign exchange reserves and external debt service ratio. These limits are then applied to all international transaction flows where there is a risk of default represented by convertibility and/or transferability restrictions.

Wholesale Credit Risk Management includes Special Assets Management Group that manages credits that are rated as watch list and worse. Special Assets Management Group was established to have a more focused view on all remedial accounts and, on a pro-active basis, identify and take timely actions on potential weak credits.

Retail credit risk management

Retail credit risk is managed on a product basis. Each retail credit application is considered for approval according to a product program, which is devised in accordance with guidelines set out in the product policy approved by the Group's Risk Committee. The evaluation of a customer's creditworthiness is determined on the basis of statistically validated scoring models and policies.

Going forward, as part of its customer-centric strategy, retail credit will monitor risk at both the customer and product level.

All approval authorities are delegated by the Chief Executive Officer (the "CEO") acting on behalf of the Board of Directors. Different authority levels are specified for approving product programs and exceptions thereto, and individual loans and credits under product programs. Each product program contains detailed credit criteria (such as customer demographics and income eligibility) and regulatory, compliance and documentation requirements, as well as other operating requirements. Credit authority levels range from Level 1 (approval of a credit application meeting all the criteria of an already approved product program) to Level 5 (the highest level where the Risk Committee approval of the specific credit application is necessary).

Credit review procedures

Specialists within the Audit, Review and Compliance group undertake regular reviews of the portfolio. In the wholesale portfolio this involves sampling of assets. In retail the focus is on testing the Risk Management Process including pre-odid review of retail assets portfolio quality and related provision. The specialists subject the Group's risk assets to an independent quality evaluation on a regular basis in conformity with the guidelines of the Central Bank of U.A.E. and the Group's internal policies in order to assist in the early identification of accrual and potential performance problems, they validate the risk ratings of those commercial and institutional clients and ensure approved credit policies, guidelines and operating procedures across the Group are implemented or highlight identified gaps in their reports.

**Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)**

42 Risk management (continued)

Credit risk management (continued)

Loan classification

All commercial and institutional loan facilities of the Group are assigned one of twenty five risk ratings. Non-classified obligors are those rated from 1 – 22. Obligors at the higher risk end rated 21 and 22 are categorized as “Watch List”. Classified exposures fall into 5 categories representing escalating degrees of severity. Assets rated 23 and 24 are categorized as “Specially Mentioned I” and 25 are categorized as “Specially Mentioned II”. All Loans and advances rated from 21 to 25 are considered as Grade 4 – Watch-List in the note below.

Outside the 25 point scale, there are 4 ratings – Non-Accrual Under Restructuring (NAUR), Sub-standard, Doubtful and Loss, categorized as Non-Performing assets. NAUR rating is assigned to borrowers that are past due by more than 90 days on payment of interest and where negotiation for re-structuring is in progress and where there is no loss of principal is envisaged. Sub-standard loans are assets where the ability to service the debt has been severely impacted and where the principal or interest is past due for over 90 days and there is no immediate prospects of a restructuring. Provisions and loans classification are taken on Sub-standard, Doubtful and Loss categories in line with the Central Bank of U.A.E. guidelines.

When interest or principal of a credit is overdue for ninety days or more, interest is suspended and is not credited to consolidated income statement. Once a loan is designated as non-accrual, all previously accrued but uncollected interest is reversed and charged against interest income. Interest accruals are no longer recorded as income, and the amortization into income of deferred loan fees ceases. Collections subsequent to a loan being placed on non-accrual status are applied on a cash basis. Specific allowance for impairment of classified assets is made based on recoverability of exposure and the risk ratings of the assets. Any exception to this policy required the approval of the CRO and is only considered when interest is current and principal is under “good faith” restructuring discussions.

Impairment of retail loans is calculated by applying a formulaic approach whereby a provision of 25% of loan balance is made when it is past due by more than 90 days and a provision of 50% of loan balance is made when is past due by more than 120 days and less than 180 days. Retail loans are written off at a maximum of 180 days past their due date, based on the characteristics of the underlying product. The written off amount includes the unpaid interest accrued to the advance till the date of write off and the principal outstanding. Interest accrual to retail advances stop on the date of write off. The only exception to this is high risk mortgage loans to individuals where the loan amount is written off at 180 days. For all other cases of mortgage defaults the bank provisions for the full amount of negative equity at 180 days.

Impaired loans and securities

Impaired loans and other financial assets are loans and other financial assets for which the Group determines that it is probable that it will be unable to collect all principal and interest due according to the contractual terms of the loans and other financial assets agreements. These assets are graded Non Accrual Under Restructuring, Substandard, Doubtful or Loss in the Group’s internal credit risk grading system for wholesale credits. It also includes assets where interest has been suspended or stopped pending conclusion of the re-structuring.

**Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)**

42 Risk management (continued)

Credit risk management (continued)

Past due but not impaired loans and securities

Past due but not impaired loans and other financial assets are those loans and other financial assets where contractual interest or principal payments are past due, but the Group believes that impairment is not appropriate on the basis of the level of security or collateral available and/or the stage of collection of amounts owed to the Group.

Allowances for impairment

The Group establishes an allowance for impairment losses that represents its estimate of incurred losses in its loan portfolio. The main components of this allowance are a specific loss component that relates to individually significant exposures, and a collective impairment allowance established for groups of homogeneous assets in respect of losses that have been incurred but have not been identified on loans subject to individual assessment for impairment.

The Group also complies with International Accounting Standards 39 (IAS 39) and International Financial Reporting Standards 9 (IFRS 9) in accordance with which it assesses the need for any impairment losses on its loans portfolio by calculating the net present value using the original effective interest rate of the expected future cash flows for each loan or its recoverability based on either collateral value or the market value of the asset where such price is available.

Write-off policy

The Group writes off a loan or other financial asset (and any related allowances for impairment losses) when the Group Credit determines that the loans or other financial assets are uncollectible in whole or in part. This determination is reached after considering information such as the occurrence of significant changes in the borrower or issuer's financial position such that the borrower or issuer can no longer pay its obligation in full, or that proceeds from collateral will not be sufficient to pay back the entire exposure. For smaller balance standardized loans, charge off decisions generally are based on a product specific past due status. Assets are written-off against provisions up to the extent of amount considered un-collectible

**Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)**

42 Risk management (continued)

Credit risk management (continued)

Set out below is an analysis of the gross and net (of allowances for impairment) amounts of impaired assets by risk grade.

	Due from banks		Loans and advances		Islamic financing and Investment		Other financial assets	
	2011 AED'000	2010 AED'000	2011 AED'000	2010 AED'000	2011 AED'000	2010 AED'000	2011 AED'000	2010 AED'000
Impaired								
Renegotiated and impaired loans	-	-	-	1,354,215	-	-	-	-
Non Accrual Under Restructuring	-	-	1,632,960	-	135,010	-	-	-
Substandard	-	-	689,899	269,430	23,404	12,912	-	-
Doubtful	607,338	593,182	2,263,032	3,226,960	31,243	100,014	17,601	22,401
Loss	-	-	276,053	278,133	50,310	62,030	-	-
Gross amount	607,338	593,182	4,861,944	5,128,738	239,967	174,956	17,601	22,401
Interest/profit suspended	(97,709)	(56,910)	(505,361)	(446,824)	(8,710)	(20,564)	-	-
Specific allowance for impairment	(489,984)	(477,848)	(1,229,465)	(1,975,238)	(49,881)	(111,028)	-	-
	19,645	58,424	3,127,118	2,706,676	181,376	43,364	17,601	22,401
Past due but not impaired								
Past due by less than 90 days	-	-	47,946	302,859	184,904	1,016	-	-
Past due beyond 90 days	4,660	-	263,744	66,757	-	-	-	-
Past due retail loans beyond 30 days	-	-	384,854	666,781	16,710	80,000	-	-
	4,660	-	696,544	1,036,397	201,614	81,016	-	-
Neither past due nor impaired								
Gross amount	10,123,370	13,593,531	29,701,880	32,854,561	4,652,257	5,171,024	7,163,992	8,061,410
Other allowances	-	-	(98,641)	-	-	-	-	-
Collective allowance for impairment	-	-	(760,939)	(677,652)	(6,700)	(4,500)	-	-
	10,123,370	13,593,531	28,842,300	32,176,909	4,645,557	5,166,524	7,163,992	8,061,410
Carrying amount	10,147,675	13,651,955	32,665,962	35,919,982	5,028,547	5,290,904	7,181,593	8,083,811

**Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)**

42 Risk management (continued)

Credit risk management (continued)

Renegotiated and impaired loans represent the net carrying value of loans and advances to Dubai Government Related Entities that have been restructured resulting in concessions agreed to by the Group concerning an extended repayment period and reduced interest rates from the original loan terms. These concessions, representing value foregone by the Group, have been recognised as impairments in accordance with International Financial Reporting Standards. The impairment charge will be gradually released to the consolidated income statement over the remaining life of the loan subject to satisfactory performance of the account according to the restructured terms.

During the year ended 31 December 2011, renegotiated loans amounting to AED 1,354 million have been transferred from impaired to neither past due nor impaired category (i.e. performing) following a period of 12 months during which the loan performed satisfactorily in accordance with the agreed terms of the restructuring.

Other allowances represent the difference between the carrying amount prior to renegotiating Dubai Government Related Entities loans mentioned above and the net present value of the future cashflows using the original effective interest rate.

The credit quality of the portfolio of loans and advances measured at amortised cost and Islamic financing and investing products at amortised costs that were neither past due nor impaired as at 31 December 2011 and 2010 can be assessed by reference to the Group's standard credit grading system. The following information is based on the system:

Grades	Loans and advances		Islamic financing and investment products	
	2011	2010	2011	2010
	AED'000	AED'000	AED'000	AED'000
Grade 1 – Low risk	3,202,529	2,688,734	284,512	271,727
Grade 2 – Satisfactory risk	19,910,282	18,764,661	2,305,165	2,799,428
Grade 3 – Fair Risk	2,856,737	3,984,695	439,863	493,812
Grade 4 – Watch List	3,732,332	7,416,471	1,622,717	1,606,057
	29,701,880	32,854,561	4,652,257	5,171,024

Collateral against loans and advances measured at amortised cost is generally held in the form of mortgage interests over property, other registered securities over assets, and guarantees. Estimates of fair value are based on the value of collateral assessed at the time of borrowing, and generally are not updated except when a loan is individually assessed as impaired. Collateral generally is not held over amounts due from banks, except when securities are held as part of reverse repurchase and securities borrowing activity. Collateral usually is not held against other financial assets, and no such collateral was held at 31 December 2011 or 2010.

**Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)**

42 Risk management (continued)

Credit risk management (continued)

The table below details the fair value of the collateral as at the date of granting loans and advances except for the fair value of debt and equity securities collaterals which are updated regularly for fair value and at the reporting date:

	Loans and advances and Islamic financing and investment products		Due from banks	
	2011	2010	2011	2010
	AED'000	AED'000	AED'000	AED'000
Against individually impaired loans and advances:				
Property	1,269,073	1,820,066	-	-
Equities	641,545	801,297	-	-
Cash	20,397	11,567	-	-
Others	86,922	118,054	-	-
Against loans and advances not impaired:				
Property	9,244,454	8,255,773	-	-
Equities	967,799	1,023,378	-	-
Cash	1,736,750	2,153,084	86,830	156,711
Others	2,654,792	1,836,114	-	-
Total	16,621,732	16,019,333	86,830	156,711

The distributions by geographical concentration of impaired loans and advances measured at amortised cost and impairment allowance for credit losses are as follows:

	U.A.E.	Middle East	O.E.C.D.	Other	Total
	AED'000	countries	AED'000	countries	AED'000
	AED'000	AED'000	AED'000	AED'000	AED'000
2011					
Impaired loans and advances	2,366,289	2,465,806	29,849	-	4,861,944
Impairment allowance for credit losses inclusive of interest in suspense	(484,189)	(1,233,098)	(17,539)	-	(1,734,826)
	1,882,100	1,232,708	12,310	-	3,127,118
2010					
Impaired loans and advances	2,163,250	2,937,348	28,140	-	5,128,738
Impairment allowance for credit losses inclusive of interest in suspense	(419,495)	(1,986,939)	(15,628)	-	(2,422,062)
	1,743,755	950,409	12,512	-	2,706,676

**Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)**

42 Risk management (continued)

Credit risk management (continued)

The distributions by geographical concentration of impaired Islamic financing and investment products measured at amortised cost and impairment allowance for credit losses are as follows:

	U.A.E. AED'000	Middle East countries AED'000	O.E.C.D. AED'000	Other countries AED'000	Total AED'000
2011					
Impaired Islamic financing and investment products	221,738	18,229	-	-	239,967
Impairment allowance for credit losses inclusive of profit in suspense	(58,591)	-	-	-	(58,591)
	<u>163,147</u>	<u>18,229</u>	<u>-</u>	<u>-</u>	<u>181,376</u>
2010					
Impaired Islamic financing and investment products	79,469	95,487	-	-	174,956
Impairment allowance for credit losses inclusive of profit in suspense	(49,968)	(81,624)	-	-	(131,592)
	<u>29,501</u>	<u>13,863</u>	<u>-</u>	<u>-</u>	<u>43,364</u>

Operational risk management

Operational risk is the risk of loss resulting from inadequate or failed internal processes, people, systems or external events.

Operational risk is inherent in each of the Group's businesses and support activities. Operational risk can manifest itself in various ways, including errors, fraudulent acts, business interruptions, employee misdeeds, or non-compliance to contract by vendors. These events could result in financial losses and other damage to the Group, including reputational harm.

To monitor and control operational risk, the Group maintains a system of comprehensive policies, procedures and a control framework designed to provide a sound and well-controlled operational environment. The goal is to keep operational risk at appropriate levels, in relation to the Group's financial strength, business characteristics, competitive environment and regulatory environment of the markets in which the Group operates. Notwithstanding these control measures, the Group incurs operational losses.

The Group has established an independent Operational Risk Function under the Risk Management Group; this Function has designed and implemented a detailed Group level Operational Risk Policy, which has since been approved by the Risk Management Committee.

**Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)**

42 Risk management (continued)

Operational risk management (continued)

The Group's operational risk framework is supported by an operational risk software tool customised to meet the Group's specific framework requirements. This helps integrate the individual components of the operational risk management framework into a unified, web-based tool and enhances the capture, reporting and analysis of operational risk data. For purposes of identification, monitoring, reporting and analysis, the Group categorizes operational risk events in line with standard Basel II risk event types.

Risk identification is the recognition of the operational risk events that risk owners and management believe may give rise to operational losses. Post implementation of the operational risk software, the management has required all businesses to utilize the Group's Standard Risk Control Self-Assessment process and supporting architecture as a dynamic risk management tool. The goal of the self-assessment process is for each business to identify the key operational risks specific to its environment and capture the view of the risk owner as to the degree to which it maintains appropriate controls. Action plans are expected to be developed for control issues identified, and businesses are held accountable for tracking and resolving these issues on a timely basis.

Operational risk monitoring

The Group has a process for monitoring operational risk-event data, permitting analysis of errors and losses as well as trends. Such analysis is performed at Group level, Business level and at each product, entity and risk type level, along with capture of loss event data being the experience of the Group in relation to actualization of operational risk events. The data reported enables the Group to back-test against self-assessment results.

Market risk management

Market Risk is the risk that the Group's positions will be adversely affected by changes in the levels or volatilities of market factors such as interest rates, currency rates, equity prices, commodity prices and credit spreads. The Market Risk Management Group is independent of the business. The Head of Market Risk reports to the Head of Risk Management.

Market risk arises from the Group's trading and non-trading activities. The Market Risk Management function addresses risks arising from trading activities. Interest risk exposure arising from non-trading activities is managed by the Assets & Liabilities Committee (ALCO).

Trading risks are concentrated in Treasury and Capital Markets (TCM) and managed by a solid framework of market risk limits that reflect the Group's market risk appetite. Limits are placed on position sizes as well as on factor sensitivities. Positions are monitored daily against the established limits and position monitoring reports are circulated to the Market Risk Management team and the respective Business Heads. In case of a limit exception, corrective action is taken in line with the Market Risk Policy and the concerned trading desk's limits package.

**Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)**

42 Risk management (continued)

Market risk management (continued)

In addition to a Market Risk Limits Package, each trading desk has a Permitted Product List which is a list of products and structures which have been determined to be appropriate for the TCM desk to trade. Any addition to this list is made after approval from the TCM Product Policy Committee which assesses the risks associated with the product and verifies that they can be controlled effectively prior to approving the product.

One of the techniques used to measure risk is Value at Risk (VaR). VaR is an estimate of the potential losses arising in a portfolio over a specified time horizon due to adverse changes in market factors. The management calculates one-day VaR at a 99% confidence interval using Monte Carlo simulations. This means that under normal market conditions, on ninety-nine days in a hundred, the decline in the value of a portfolio will be less than the estimated VaR number. Only on one day in a hundred will it exceed this number. The model is back-tested regularly to ensure that actual losses are in fact below the potential losses estimated by VaR.

Stress testing is conducted by generating extreme, but plausible scenarios, such as significant movements in interest rates, credit spreads, etc. and analyzing their effect on the Group's trading positions.

During the year ended 31 December 2011, VaR was calculated regularly and as of 31 December 2011 the 99% VaR was USD 0.35 million (31 December 2010: USD 1.34 million).

There has been no change to the Group's exposure to market risks or the manner in which these risks are managed and measured.

Interest rate risk management

Interest rate risk arises from the possibility that changes in interest rates will affect the value of financial instruments. The Group is exposed to interest rate risk as a result of mismatches or gaps in the amounts of assets and liabilities.

The Group uses simulation-modelling tools to measure and monitor interest rate sensitivity. The results are analyzed and monitored by Assets and Liabilities Committee ("ALCO"). Since most of the Group's assets and liabilities are floating rate, deposits and loans generally reprice simultaneously providing a natural hedge, which reduces interest rate exposure. Moreover, the majority of the Group's assets and liabilities reprice within one year, thereby further limiting interest rate risk.

The impact of 50 basis points sudden movement in benchmark interest rate on profit over a 12 months period as at 31 December 2011 would have been an decrease in profit by 4.07% (in case of decrease of interest rate) and would have been an increase in profit by 4.18% (in case of increase of interest rate) [2010: -2.4% and +3.2%] respectively.

During the year ended 31 December 2011, the effective interest rate on due from banks and certificates of deposits with central banks was 1.16% (2010: 1.71%), on loans and advances measured at amortised cost 6.24% (2010: 7.12%), on customers' deposits 1.60% (2010: 2.50%) and on due to banks (including repurchase agreements) 0.95% (2010: 1.70%).

The following table depicts the interest rate sensitivity position and interest rate gap position based on contractual repricing arrangement:

Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)

42 Risk management (continued)

Market risk management (continued)

Interest rate risk management (continued)

Interest rate repricing analysis:

2011	Within 3 months AED'000	Over 3 to 6 months AED'000	Over 6 to 12 months AED'000	Over 1 to 5 years AED'000	Over 5 years AED'000	Non- interest bearing items AED'000	Total Sensitive AED'000
Assets							
Cash and balances with central banks	3,200,569	6,150,000	368,000	-	-	5,013,231	14,731,800
Deposits and balances due from banks	5,820,466	703,963	1,096,138	171,725	27,132	2,328,251	10,147,675
Other financial assets measured at fair value	216,609	147,249	139,292	226,055	-	1,823,583	2,552,788
Loans and advances measured at amortised cost	12,059,402	670,331	12,903,843	5,655,542	1,375,989	855	32,665,962
Islamic financing and investment products measured at amortised cost	1,305,306	92,940	3,184,489	263,649	182,163	-	5,028,547
Other financial assets measured at amortised costs	5,010,779	1,460,004	643,102	65,730	-	1,978	7,181,593
Interest receivable and other assets	-	-	-	-	-	5,417,102	5,417,102
Investment properties	-	-	-	-	-	318,028	318,028
Property and equipment	-	-	-	-	-	1,197,827	1,197,827
Total assets	27,613,131	9,224,487	18,334,864	6,382,701	1,585,284	16,100,855	79,241,322

Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)

42 Risk management (continued)

Market risk management (continued)

Interest rate risk management (continued)

Interest rate repricing analysis (continued)

2011	Within 3 months AED'000	Over 3 to 6 months AED'000	Over 6 to 12 months AED'000	Over 1 to 5 years AED'000	Over 5 years AED'000	Non- interest bearing items AED'000	Total AED'000
Liabilities and equity							
Deposits and balances due to banks	5,817,878	223,871	140,264	128,520	-	912,837	7,223,370
Repurchase agreements with banks	2,505,165	-	-	-	-	-	2,505,165
Customers' deposits	19,294,916	2,720,648	2,031,186	744,953	133,942	15,251,375	40,177,020
Islamic customers' deposits	4,283,976	341,335	163,923	77,923	-	372,706	5,239,863
Insurance and life assurance funds	-	-	-	-	-	972,867	972,867
Interest payable and other liabilities	-	-	-	-	-	5,676,168	5,676,168
Medium-term loans	1,190,419	-	-	-	3,443,593	-	4,634,012
Long-term loans	-	-	-	-	9,007	-	9,007
Equity attributable to shareholders of the Parent	-	-	-	-	-	12,262,810	12,262,810
Non-controlling interest	-	-	-	-	-	541,040	541,040
Total liabilities and equity	33,092,354	3,285,854	2,335,373	951,396	3,586,542	35,989,803	79,241,322
On Balance Sheet gap	(5,479,223)	5,938,633	15,999,491	5,431,305	(2,001,258)	(19,888,948)	-
Off Balance Sheet gap	376,261	885,905	(107,592)	221,882	(1,376,456)	-	-
Cumulative interest rate sensitivity gap	(5,102,962)	1,721,576	17,613,475	23,266,662	19,888,948	-	-

**Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)**

42 Risk management (continued)

Market risk management (continued)

Interest rate risk management (continued)

Interest rate repricing analysis (continued)

2010	Within 3 months AED'000	Over 3 to 6 months AED'000	Over 6 to 12 months AED'000	Over 1 to 5 years AED'000	Over 5 years AED'000	Non- interest bearing items AED'000	Total Sensitive AED'000
Assets							
Cash and balances with central banks	2,462,822	1,932,000	3,410,000	-	-	5,568,900	13,373,722
Deposits and balances due from banks	7,380,750	3,329,551	851,813	407,551	210,687	1,471,603	13,651,955
Other financial assets measured at fair value	3,164	129,933	103,372	95,198	31,148	1,859,865	2,222,680
Loans and advances measured at amortised cost	13,205,072	2,319,304	6,199,890	10,580,468	3,614,939	309	35,919,982
Islamic financing and investment products measured at amortised cost	1,969,982	281,893	442,828	1,930,483	665,718	-	5,290,904
Other financial assets measured at amortised costs	3,716,724	3,873,414	402,143	60,550	26,553	4,427	8,083,811
Interest receivable and other assets	-	-	-	-	-	4,986,426	4,986,426
Investment properties	-	-	-	-	-	172,320	172,320
Property and equipment	-	-	-	-	-	1,144,003	1,144,003
Total assets	28,738,514	11,866,095	11,410,046	13,074,250	4,549,045	15,207,853	84,845,803

Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)

42 Risk management (continued)

Market risk management (continued)

Interest rate risk management (continued)

Interest rate repricing analysis (continued)

2010	Within 3 months AED '000	Over 3 to 6 months AED '000	Over 6 to 12 months AED '000	Over 1 to 5 years AED '000	Over 5 years AED '000	Non- interest bearing items AED '000	Total AED '000
Liabilities and equity							
Deposits and balances due to banks	4,597,553	249,298	490,328	87,700	-	613,747	6,038,626
Repurchase agreements with banks	3,241,907	-	127,086	-	-	-	3,368,993
Customers' deposits	26,152,014	4,642,514	4,485,517	674,549	517,385	10,292,879	46,764,858
Islamic customers' deposits	3,582,281	297,023	269,074	4,323	115	335,999	4,488,815
Insurance and life assurance funds	-	-	-	-	-	896,587	896,587
Interest payable and other liabilities	-	-	-	-	-	4,990,584	4,990,584
Medium-term loans	2,459,441	-	-	-	3,443,593	-	5,903,034
Long-term loans	-	-	-	-	9,049	275	9,324
Equity attributable to shareholders of the Parent	-	-	-	-	-	11,844,743	11,844,743
Non-controlling interest	-	-	-	-	-	540,239	540,239
Total liabilities and equity	40,033,196	5,188,835	5,372,005	766,572	3,970,142	29,515,053	84,845,803
On Balance Sheet gap	(11,294,682)	6,677,260	6,038,041	12,307,678	578,903	(14,307,200)	-
Off Balance Sheet gap	(494,341)	22,510	211,792	260,039	-	-	-
Cumulative interest rate sensitivity gap	(11,789,023)	(5,089,253)	1,160,580	13,728,297	14,307,200	-	-

Notes to the consolidated financial statements for the year ended 31 December 2011 (continued)

42 Risk management (continued)

Market risk management (continued)

Interest rate risk management (continued)

Interest rate swap contracts used as hedging instruments

Under interest rate swap contracts, the Group agrees to exchange the difference between fixed and floating rate interest amounts calculated on agreed notional principal amounts. Such contracts enable the Group to mitigate the risk of changing interest rates on the fair value of issued fixed rate debt. The fair value of interest rate swaps at the end of the reporting period is determined by discounting the future cash flows using the curves at the end of the reporting period and the credit risk inherent in the contract, and is disclosed below. The average interest rate is based on the outstanding balances at the end of the reporting period.

The following tables detail the notional principal amounts and remaining terms of interest rate swap contracts outstanding at the end of the reporting period.

Fair value hedges:

		<u>Notional amount by term maturity</u>							
	Average contracted fixed interest rate	Positive fair value AED'000	Negative fair value AED'000	Notional amount AED'000	Up to 3 months AED'000	3 – 6 months AED'000	6 – 12 months AED'000	1 year to 5 years AED'000	Over 5 years AED'000
2011									
Interest rate swaps	5.25%	5,545	2,862	556,460	-	-	-	123,046	433,414

Interest rate swap contracts exchanging fixed rate interest for floating rate interest are designated and effective as fair value hedges in respect of interest rates. During the year, the hedge was effective in hedging the fair value exposure to interest rate movements and as a result the carrying amount of the other financial assets measured at amortized cost were adjusted by AED 2.68 million which was included in profit or loss at the same time that the fair value of the interest rate swap was included in profit or loss.

**Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)**

42 Risk management (continued)

Market risk management (continued)

Currency risk management

Currency risk represents the risk of change in the value of financial instruments due to changes in foreign exchange rates. Limits on positions by currencies are monitored. The Group's exposures on 31 December are:

	Net spot position AED'000	2011 Forward position AED'000	Total AED'000	Net spot position AED'000	2010 Forward position AED'000	Total AED'000
U.S. Dollars	8,582,247	(804,355)	7,777,892	8,179,352	(1,190,036)	6,989,316
Qatari Riyals	940,003	(6,476)	933,527	5,332,490	(491,683)	4,840,807
Indian Rupees	44,918	49,483	94,401	71,764	22,468	94,232
Pound Sterling	(156,262)	184,884	28,622	(456,644)	473,211	16,567
Singapore Dollar	(1,269)	3	(1,266)	694	-	694
Egyptian Pound	(19,068)	25,206	6,138	(129,764)	-	(129,764)
Euro	(54,170)	61,612	7,442	55,238	(61,238)	(6,000)
Bahrain Dinar	286,262	-	286,262	277,106	-	277,106
Saudi Riyal	14,153	-	14,153	(245,654)	226,090	(19,564)
Japanese Yen	910	2	912	256,119	(255,579)	540
Swiss Francs	549	1	550	1,234	3	1,237
Pakistani Rupees	15,224	-	15,224	15,956	-	15,956
Kuwaiti Dinar	(673,381)	663,028	(10,353)	(1,190,507)	1,197,415	6,908
Canadian Dollars	2,049	(73)	1,976	597	(1,737)	(1,140)
Australian Dollars	1,352	(1)	1,351	1,760	-	1,760
Omani Riyal	1,138	-	1,138	9,934	(1,647)	8,287
Other	(5,509)	10,388	4,879	4,529	(2,228)	2,301
Total	8,979,146	183,702	9,162,848	12,184,204	(84,961)	12,099,243

The exchange rate of AED against US Dollar is pegged since November 1980 and the Group's exposure to currency risk is limited to that extent.

Most of the positions are in currencies that are pegged to the U.A.E. Dirham; therefore, any change in their exchange rates will have insignificant sensitivity on the consolidated income statement or consolidated statement of comprehensive income.

Liquidity risk management

Liquidity Risk is the risk that the Group's entities, in various locations and in various currencies, will be unable to meet a financial commitment to a customer, creditor, or investor when due.

**Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)**

42 Risk management (continued)

Liquidity risk management (continued)

The Group's senior management's focus on liquidity management is to:

- Better understand the various sources of liquidity risk, particularly under stressed conditions;
- Ensure the Group's short term and long term resilience, as measured by the Basel 3 proposals, is sufficiently robust to meet realistic adverse scenarios;
- Develop effective contingency plans to deal with liquidity crises;
- Develop liquidity risk tolerance levels within the Internal Capital Adequacy Assessment Process (ICAAP) framework; and
- Demonstrate that the bank can survive the closure of one or more funding markets by ensuring that finance can be readily raised from a variety of sources.

Assets and Liabilities Committee ("ALCO") has a broad range of authority delegated by the Board of Directors to manage the Group's assets and liabilities structure and funding strategy. ALCO meets on a monthly basis or more often as circumstances dictate to review liquidity ratios, asset and liability structure, interest rate and foreign exchange exposures, internal and statutory ratio requirements, funding gaps and general domestic and international economic and financial market conditions. ALCO formulates liquidity risk management guidelines for the Group's operation on the basis of its review.

The members of ALCO are the Chief Executive Officer, the Head of Corporate Affairs, the Head of Retail Banking Group, the Head of Risk Management, the Head of Financial Institutions Group, the Head of International Banking and the Head of Treasury's Capital Markets.

The Group has historically relied on customer deposits for its funding needs. Over the years, the Group has successfully introduced various cash managed products and retail savings' schemes which have enabled it to mobilize low cost, broad base deposits. In order to diversify the funding sources, the Euro Medium Term Notes program was launched in 2004 and, to date; this has outstanding balance of AED 1.2 billion [Note 19(b)] in medium-term loans. During the year ended 31 December 2007, the Group raised AED 1.8 billion for 5 years through a syndicated borrowing arrangement.

To manage liquidity risk tolerance, the Group uses various indicators including the regulatory ratio of utilization of funds to stable resources. Other indicators include loans and advances to customers' deposits and stable funds, liquid assets to customers' deposits and liquid assets to total assets ratios, plus deposit concentration risk indicators. Any breach of any tolerance level needs to be reported to ALCO and remedied within a short period.

The Treasury function in the Group is responsible to manage the liquidity and it follows strict guidelines for deployment of liquid assets within each liquidity bucket. Periodic stress tests are performed to ensure the availability of funds during stressed situations.

Inter-bank borrowing lines and repo facilities with global banks and the Central Bank of U.A.E. are part of the contingency funding options maintained by the Treasury.

The following table summarizes the maturity profile of Group's assets and liabilities based on contractual repayment arrangements. The contractual maturities of assets and liabilities have been determined on the basis of the remaining period at the reporting date to the contractual maturity date:

Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)

42 Risk management (continued)

Liquidity risk management (continued)

Maturity profile:

The maturity profile of assets, liabilities and equity as at 31 December 2011 were as follows:

Assets	Within 3 months AED'000	Over 3 to 6 months AED'000	Over 6 to 12 months AED'000	Over 1 to 5 years AED'000	Over 5 years AED'000	Total AED'000
Cash and balances with central banks	8,213,801	6,150,000	367,999	-	-	14,731,800
Deposits and balances due from banks	8,337,273	800,183	774,986	192,285	42,948	10,147,675
Other financial assets measured at fair value	288,914	146,250	106,855	136,317	1,874,452	2,552,788
Loans and advances measured at amortised cost	13,763,656	1,860,492	3,255,437	9,236,120	4,550,257	32,665,962
Islamic financing and investment products measured at amortised cost	3,102,061	514,600	55,223	578,977	777,686	5,028,547
Other financial assets measured at amortised cost	1,094,364	636,194	734,447	2,224,196	2,492,392	7,181,593
Interest receivable and other assets	1,984,265	1,787,046	105,577	789,314	750,900	5,417,102
Investment properties	-	-	-	-	318,028	318,028
Property and equipment	-	-	-	-	1,197,827	1,197,827
Total assets	36,784,334	11,894,765	5,400,524	13,157,209	12,004,490	79,241,322

Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)

42 Risk management (continued)

Liquidity risk management (continued)

Maturity profile: (continued)

	Within 3 months AED'000	Over 3 to 6 months AED'000	Over 6 to 12 months AED'000	Over 1 to 5 years AED'000	Over 5 years AED'000	Total AED'000
Liabilities and equity						
Deposits and balances due to banks	6,730,715	243,028	121,107	128,520	-	7,223,370
Repurchase agreements with banks	2,505,165	-	-	-	-	2,505,165
Customers' deposits	34,116,620	2,744,115	2,078,940	1,078,751	158,594	40,177,020
Islamic customers' deposits	4,656,682	341,335	163,923	77,923	-	5,239,863
Insurance and life assurance funds	-	-	649,994	322,873	-	972,867
Interest payable and other liabilities	2,047,132	1,591,930	586,056	898,103	552,947	5,676,168
Medium-term loans	-	-	-	-	4,634,012	4,634,012
Long-term loans	-	-	-	-	9,007	9,007
Equity attributable to shareholders of the Parent	-	-	-	-	12,262,810	12,262,810
Non-controlling interest	-	-	-	-	541,040	541,040
Total liabilities and equity	50,056,314	4,920,408	3,600,020	2,506,170	18,158,410	79,241,322

Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)

42 Risk management (continued)

Liquidity risk management (continued)

Maturity profile: (continued)

The maturity profile of assets, liabilities and equity as at 31 December 2010 were as follows:

Assets	Within 3 months AED'000	Over 3 to 6 months AED'000	Over 6 to 12 months AED'000	Over 1 to 5 years AED'000	Over 5 years AED'000	Total AED'000
Cash and balances with central banks	8,031,722	1,931,431	3,410,000	569	-	13,373,722
Deposits and balances due from banks	8,858,786	3,329,551	337,173	915,757	210,688	13,651,955
Other financial assets measured at fair value	152,707	121,945	148,626	1,733,933	65,469	2,222,680
Loans and advances measured at amortised cost	13,204,535	2,319,369	6,200,019	10,581,118	3,614,941	35,919,982
Islamic financing and investment products measured at amortised cost	1,934,862	296,893	442,828	1,950,603	665,718	5,290,904
Other financial assets measured at amortised cost	936,996	364,073	498,294	3,955,064	2,329,384	8,083,811
Interest receivable and other assets	1,557,791	1,775,706	647,121	499,829	505,979	4,986,426
Investment properties	-	-	-	-	172,320	172,320
Property and equipment	-	-	-	-	1,144,003	1,144,003
Total assets	34,677,399	10,138,968	11,684,061	19,636,873	8,708,502	84,845,803

Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)

42 Risk management (continued)

Liquidity risk management (continued)

Maturity profile: (continued)

	Within 3 months AED'000	Over 3 to 6 months AED'000	Over 6 to 12 months AED'000	Over 1 to 5 years AED'000	Over 5 years AED'000	Total AED'000
Liabilities and equity						
Deposits and balances due to banks	3,247,714	249,298	617,414	1,924,200	-	6,038,626
Repurchase agreements with banks	3,368,993	-	-	-	-	3,368,993
Customers' deposits	36,486,493	4,645,721	4,486,017	626,586	520,041	46,764,858
Islamic customers' deposits	3,918,280	297,023	269,074	4,323	115	4,488,815
Insurance and life assurance funds	-	389,533	280,120	226,934	-	896,587
Interest payable and other liabilities	1,823,242	1,165,089	1,126,800	542,778	332,675	4,990,584
Medium-term loans	-	1,101,900	-	-	4,801,134	5,903,034
Long-term loans	-	-	-	-	9,324	9,324
Equity attributable to shareholders of the Parent	-	-	-	-	11,844,743	11,844,743
Non-controlling interest	-	-	-	-	540,239	540,239
Total liabilities and equity	48,844,722	7,848,564	6,779,425	3,324,821	18,048,271	84,845,803

**Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)**

42 Risk management (continued)

Fair value of financial instruments

Fair value is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable willing parties in an arm's length transaction. As such, differences can arise between book values and the fair value estimates. Underlying the definition of fair value is the presumption that the Group is a going concern without any intention or requirement to materially curtail the scale of its operation or to undertake a transaction on adverse terms.

Fair value of financial assets carried at amortised cost

Except as detailed in the following table, the management considers that the carrying amounts of financial assets and financial liabilities measured at amortised cost in the consolidated financial statements approximate their fair values.

	2011		2010	
	Carrying amount AED'000	Fair Value AED'000	Carrying amount AED'000	Fair value AED'000
<i>Financial assets</i>				
- Other financial assets measured at amortised cost	7,181,593	6,851,658	8,083,811	7,755,233
<i>Financial liabilities</i>				
- Medium-term floating rate notes	1,190,419	986,536	2,459,441	2,173,030

The fair value for other financial assets measured at amortised cost is based on market prices or broker/dealer price quotations. Where this information is not available, fair value is estimated using quoted market prices for securities with similar credit, maturity and yield characteristics.

Medium-term floating rate notes are notes listed in Luxembourg Securities Exchange. The fair value for these notes is determined with reference to quoted market prices.

**Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)**

42 Risk management (continued)

Fair value of financial instruments (continued)

Valuation techniques and assumptions applied for the purposes of measuring fair value

The fair values of financial assets and financial liabilities are determined as follows.

- The fair values of financial assets and financial liabilities with standard terms and conditions and traded on active liquid markets are determined with reference to quoted market prices (includes listed redeemable notes, bills of exchange, debentures and perpetual notes).
- The fair values of other financial assets and financial liabilities (excluding derivative instruments) are determined in accordance with generally accepted pricing models based on discounted cash flow analysis using prices from observable current market transactions and dealer quotes for similar instruments.
- The fair values of derivative instruments are calculated using quoted prices. Where such prices are not available, a discounted cash flow analysis is performed using the applicable yield curve for the duration of the instruments for non-optional derivatives, and option pricing models for optional derivatives. Foreign currency forward contracts are measured using quoted forward exchange rates and yield curves derived from quoted interest rates matching maturities of the contracts. Interest rate swaps are measured at the present value of future cash flows estimated and discounted based on the applicable yield curves derived from quoted interest rates.

Fair value measurements recognised in the consolidated statement of financial position

The following table provides an analysis of financial instruments that are measured subsequent to initial recognition at fair value, grouped into Levels 1 to 3 based on the degree to which the fair value is observable.

- Level 1 fair value measurements are those derived from quoted prices (unadjusted) in active markets for identical assets or liabilities.
- Level 2 fair value measurements are those derived from inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices).
- Level 3 fair value measurements are those derived from valuation techniques that include inputs for the asset or liability that are not based on observable market data (unobservable inputs).

Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)

42 Risk management (continued)

Fair value of financial instruments (continued)

Fair value measurements recognised in the consolidated statement of financial position (continued)

31 December 2011

	Level 1 AED'000	Level 2 AED'000	Level 3 AED'000	Total AED'000
<i>Financial assets measured at fair value</i>				
Other financial assets measured at FVTPL				
- Debt securities	109,579	430,430	-	540,009
- Equities	39,699	-	652	40,351
- Mutual and other funds	169,699	263,965	-	433,664
Other financial assets measured at FVTOCI				
- Equities	871,772	-	390,794	1,262,566
- Mutual and other funds	276,198	-	-	276,198
Total	1,466,947	694,395	391,446	2,552,788
<i>Other assets</i>				
Positive fair value of derivatives	128,504	1,287,073	-	1,415,577
<i>Other liabilities</i>				
Negative fair value of derivatives	115,026	1,267,781	-	1,382,807

**Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)**

42 Risk management (continued)

Fair value of financial instruments (continued)

Fair value measurements recognised in the consolidated statement of financial position (continued)

31 December 2010

	Level 1 AED'000	Level 2 AED'000	Level 3 AED'000	Total AED'000
<i>Financial assets measured at fair value</i>				
Other financial assets measured at FVTPL				
- Debt securities	151,066	211,747	-	362,813
- Equities	117,072	-	678	117,750
- Mutual and other funds	110,567	-	-	110,567
Other financial assets measured at FVTOCI				
- Equities	925,947	-	436,589	1,362,536
- Mutual and other funds	269,014	-	-	269,014
Total	1,573,666	211,747	437,267	2,222,680
<i>Other assets</i>				
Positive fair value of derivatives	237,255	880,323	-	1,117,578
<i>Other liabilities</i>				
Negative fair value of derivatives	202,764	892,192	-	1,094,956

There were no transfers between Level 1 and 2 during the years ended 31 December 2011 and 2010.

**Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)**

42 Risk management (continued)

Fair value of financial instruments (continued)

Reconciliation of Level 3 fair value measurement of other financial assets measured at FVTOCI

	2011 AED'000	2010 AED'000
At 1 January	437,267	499,588
Purchases	13,318	24,397
Cost of sales	(4,803)	(2,840)
Change in fair value	(54,336)	(83,878)
At 31 December	391,446	437,267

The investments classified under Level 3 category have been fair-valued based on information available for each investment. Based on the information available the valuation has been carried on net asset value or valuation provided by the portfolio managers.

All gain and losses included in other comprehensive income relate to unquoted investments in equity instruments held at the end of the reporting period and are reported as changes of 'investments revaluation reserve'.

Fair value sensitivity analysis

The following table shows the sensitivity of fair values to 10% increase or decrease as at 31 December 2011:

	Reflected in statement of income		Reflected in other comprehensive income	
	Favourable change AED'000	Unfavourable change AED'000	Favourable change AED'000	Unfavourable change AED'000
2011				
Other financial assets measured at fair value	101,402	(101,402)	153,876	(153,876)
2010				
Other financial assets measured at fair value	59,113	(59,113)	163,155	(163,155)

Majority of the derivatives financial instruments are back to back; therefore, any change to the fair value of the derivatives resulting from price inputs chances will have insignificant impact on the consolidated income statement or consolidated statement of comprehensive income.

**Notes to the consolidated financial statements
for the year ended 31 December 2011 (continued)**

43 Fiduciary activities

Assets held by the Group in trust, in a fiduciary and custodial capacity on behalf of its customers, are not included in these consolidated financial statements. These include assets held in a fiduciary capacity for a related party as of 31 December 2011 of AED 509.60 million (2010: AED 949.86 million).

44 Fund management

Makaseb Funds Company BSC and Mashreq Capital (DIFC) Limited (subsidiaries – Note 1) manage a number of funds which are not consolidated in these consolidated financial statements. The funds have no recourse to the general assets of the Group; further the Group has no recourse to the assets of the funds.

45 Foreign restricted assets

Net assets equivalent to AED 72.70 million as at 31 December 2011 (2010: AED 79.02 million) maintained by certain branches of the Bank, operating outside the United Arab Emirates, are subject to exchange control regulations of the countries in which these branches operate.

46 Approval of consolidated financial statements

The consolidated financial statements for the year ended 31 December 2011 were approved by the Board of Directors and authorized for issue on 1 February 2012.