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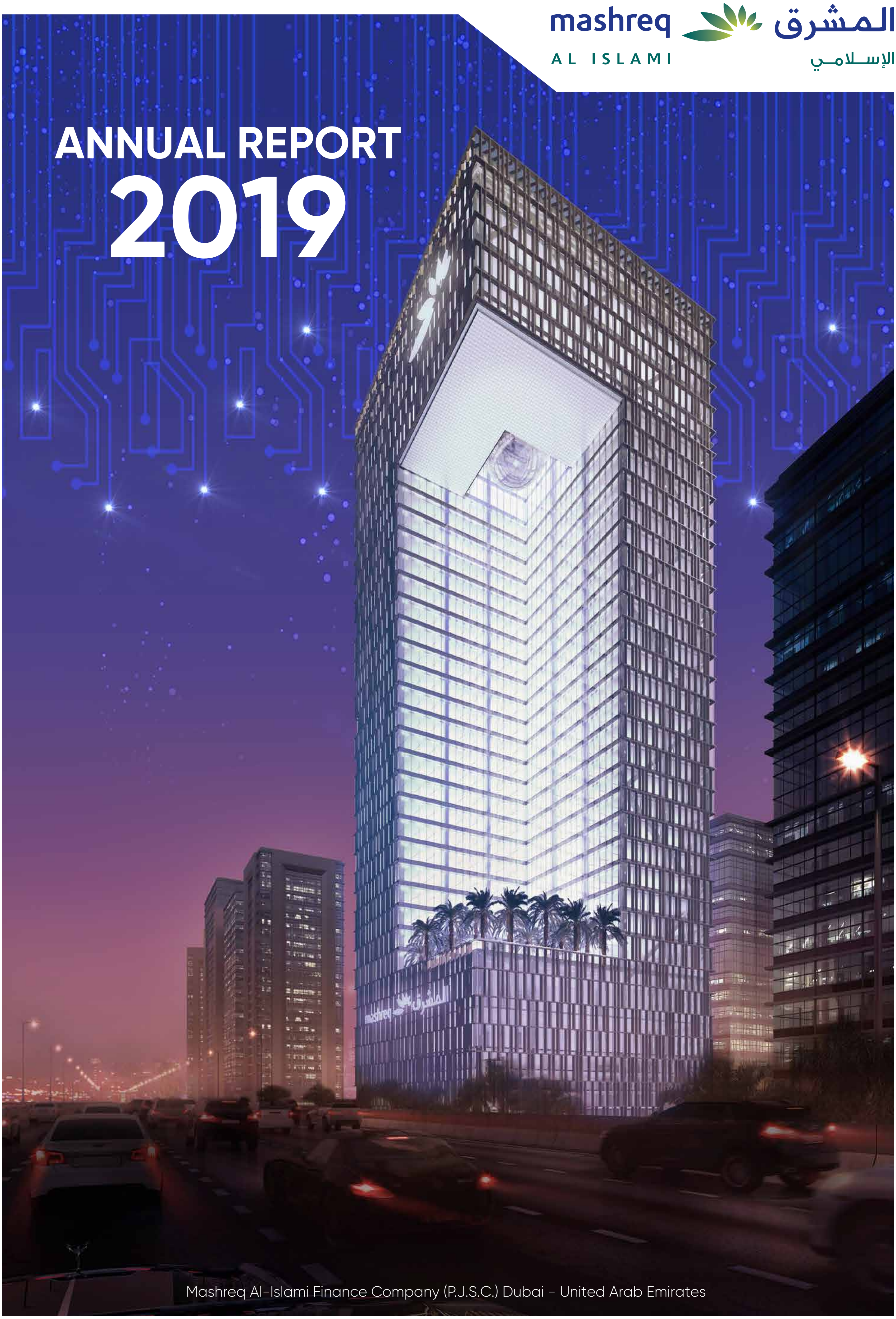
ANNUAL REPORT 2019



Mashreq Al-Islami Finance Company (P.J.S.C.) Dubai - United Arab Emirates

Mashreq Al-Islami Finance Company (P.J.S.C.)
Dubai - United Arab Emirates

Report and financial statements
for the year ended 31 December 2019

Mashreq Al-Islami Finance Company (P.J.S.C.)

Contents

Mashreq Al-Islami Finance Company (P.J.S.C.)

Board of Directors' report

The Board of Directors have pleasure in submitting their report and the audited financial statements for the year ended 31 December 2019.

Incorporation and registered offices

Mashreq Al-Islami Finance Company (P.J.S.C.) (the "Company") is a private joint-stock company and is a subsidiary of Mashreqbank PSC (the "Parent Company"). The Company was incorporated in the United Arab Emirates under a trade license issued by the Department of Economic Development of the Government of Dubai. The address of the registered office of the Company is P.O. Box 1250, Dubai, United Arab Emirates.

Principal activities

The Company carries out financing activities through various Islamic instruments, in accordance with Islamic Shari'ah principles that include prohibition of usury, as determined by the Shari'ah Supervisory Board.

Financial position and results

The financial position and results of the Company for the year ended 31 December 2019 are set out in the accompanying financial statements.

Directors

The following were the Directors of the Company for the year ended 31 December 2019:

- H.E. Abdul Aziz Abdulla Al Ghurair
- Ali Rashed Lootah
- Ali Raza Khan
- Subroto Som
- Aladdin Al Deesi

Auditors

The financial statements for the year ended 31 December 2019 have been audited by PricewaterhouseCoopers.

By order of the Board of Directors

Ali Raza Khan
29 March 2020

Independent auditor's report to the shareholders of Mashreq Al-Islami Finance Company (P.J.S.C.)

Report on the audit of the financial statements

Our qualified opinion

In our opinion, except for the effects of the matter described in the *Basis for qualified opinion* section in our report, the financial statements present fairly, in all material respects, the financial position of Mashreq Al-Islami Finance Company (P.J.S.C.) (the "Company") as at 31 December 2019, and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

What we have audited

The Company's financial statements comprise:

- the statement of financial position as at 31 December 2019;
- the statement of comprehensive income for the year then ended;
- the statement of changes in equity for the year then ended;
- the statement of cash flows for the year then ended; and
- the notes to the financial statements, which include a summary of significant accounting policies.

Basis for qualified opinion

As set out in note 7, other assets at 31 December 2019 comprise properties held for sale with a carrying amount of AED 73 million. In order to comply with regulatory requirements of the Central Bank of the UAE, the properties are classified as held for sale and carried at AED 73 million lower than the fair value less costs to sell as at that date. This is a departure from International Financial Reporting Standards. Had these properties been presented as properties held for sale and reflected at their fair value less costs to sell at 31 December 2019, other assets, total assets, retained earnings and equity would have all increased by AED 73 million at that date and loss for the year then ended would have decreased by AED 73 million.

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

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

Independence

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

Independent auditor's report to the shareholders of Mashreq Al-Islami Finance Company (P.J.S.C.) (continued)

Other information

The Directors are responsible for the other information. The other information comprises of the Directors' report (but does not include the financial statements and our auditor's report thereon).

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

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

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

Responsibilities of directors and those charged with governance for the financial statements

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

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

Those charged with governance are responsible for overseeing the Company's financial reporting process.

Auditor's responsibilities for the audit of the financial statements

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

Independent auditor's report to the shareholders of Mashreq Al-Islami Finance Company (P.J.S.C.) (continued)

Auditor's responsibilities for the audit of the financial statements (continued)

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

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

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

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

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

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

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

Independent auditor's report to the shareholders of Mashreq Al-Islami Finance Company (P.J.S.C.) (continued)

Report on other legal and regulatory requirements

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

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

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

(iii) the Company has maintained proper books of account;

(iv) the financial information included in the Director's report is consistent with the books of account of the Company;

(v) as disclosed in note 22 to the financial statements the Company has not purchased or invested in any shares during the financial year ended 31 December 2019;

(vi) note 10 to the financial statements discloses material related party transactions and the terms under which they were conducted; and

(vii) based on the information that has been made available to us, nothing has come to our attention which causes us to believe that the Company has contravened during the financial year ended 31 December 2019 any of the applicable provisions of the UAE Federal Law No. (2) of 2015 or of its Articles of Association which would materially affect its activities or its financial position as at 31 December 2019.

Further, as required by the Article (114) of the Decretal Federal Law No. (14) of 2018, we report that we have obtained all the information and explanations we considering necessary for the purpose of our audit.

PricewaterhouseCoopers
29 March 2020

Douglas O'Mahony
Registered Auditor Number: 834
Place: Dubai, United Arab Emirates

Statement of financial position

	Note	As at 31 December 2019 AED'000	2018 AED'000
ASSETS			
Cash and cash equivalents	5	**1,267**	1,267
Islamic financing products measured at amortised cost	6	**1,192,731**	1,326,825
Other assets	7	**72,935**	26
Property and equipment	8	**-**	211,224
Total assets		**1,266,933**	1,539,342
LIABILITIES AND EQUITY			
LIABILITIES			
Due to Parent Company	10	**495,177**	661,522
Other liabilities	9	**2,878**	3,781
Total liabilities		**498,055**	665,303
EQUITY			
Issued and paid up share capital	11	**500,000**	500,000
Statutory reserve	12	**36,861**	36,861
Retained earnings		**232,017**	337,178
Total equity		**768,878**	874,039
Total liabilities and equity		**1,266,933**	1,539,342

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Ali Raza Khan

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

Statement of comprehensive income

		For the year ended 31 December	
		2019	2018
	Note	**AED'000**	AED'000
Income			
Income from Murabahah		**9,293**	26,863
Income from Ijarah		**57,942**	55,799
Total income from Islamic financing products measured at amortised cost		**67,235**	82,662
Fees and commission income	13	**2,001**	3,287
Total income		**69,236**	85,949
Expenses			
General and administrative expenses	14	**(18,404)**	(22,605)
Allowance for impairment, net	15	**(17,704)**	(21,384)
Total expenses		**(36,108)**	(43,989)
Change in fair value of properties	7	**(65,354)**	-
Provision on properties	7	**(72,935)**	-
(Loss) / profit for the year		**(105,161)**	41,960
Other comprehensive income		**-**	-
Total comprehensive (loss) / income for the year		**(105,161)**	41,960

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

Statement of changes in equity

	Issued and paid up share capital AED'000	**Statutory reserve AED'000**	**Retained earnings AED'000**	**Total AED'000**
Balance at 1 January 2018	500,000	32,665	299,414	832,079
Profit for the year	-	-	41,960	41,960
Total comprehensive income for the year	-	-	41,960	41,960
Transferred to statutory reserve	-	4,196	(4,196)	-
Balance at 31 December 2018	**500,000**	**36,861**	**337,178**	**874,039**
Loss for the year	**-**	**-**	**(105,161)**	**(105,161)**
Total comprehensive loss for the year	**-**	**-**	**(105,161)**	**(105,161)**
Balance at 31 December 2019	**500,000**	**36,861**	**232,017**	**768,878**

Statement of cash flows

	Note	For the year ended 31 December 2019 AED'000	2018 AED'000
Cash flows from operating activities			
(Loss) / profit for the year		**(105,161)**	41,960
Adjustments for			
Allowance for impairment, net	15	**17,704**	21,384
Fair value adjustment on properties	7	**65,354**	-
Provision on properties	7	**72,935**	-
Operating cash flows before changes in operating assets and liabilities		**50,832**	63,344
Changes in assets and liabilities			
Decrease in Islamic financing products measured at amortised cost		**116,390**	392,506
Decrease in other assets		**26**	5
Decrease in other liabilities		**(903)**	(1,597)
Net cash generated from operating activities		**166,345**	454,258
Cash flows from financing activity			
Decrease in due to Parent Company		**(166,345)**	(454,249)
Net increase in cash and cash equivalents		**-**	9
Cash and cash equivalents at 1 January		**1,267**	1,258
Cash and cash equivalents at 31 December	5	**1,267**	1,267

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

1 General information

Mashreq Al-Islami Finance Company (P.J.S.C.) (the “Company”) is a private joint-stock company and incorporated in the United Arab Emirates under a trade license issued by the Department of Economic Development of the Government of Dubai.

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

The shareholders and their respective share holdings are as follows:

	%
Mashreqbank PSC	99.70
Injaz Services FZ-LLC	0.10
Abdulla Bin Ahmed Al Ghurair	0.10
Abdul Aziz Abdulla Al Ghurair	0.10
	100.00

The Company carries out financing activities through various Islamic products & instruments, in accordance with Islamic Shari’ah principles that include prohibition of usury, as determined by the Shari’ah Supervisory Board.

Shari’ah Supervisory Board

The Company’s business activities are subject to the supervision of the Shari’ah Supervisory Board. The Shari’ah Supervisory Board is an independent body of Shari’ah Scholars experts in the field of Islamic financial jurisprudence. The Shari’ah Supervisory Board reviews and directs the Company for its financial activities in accordance with the Shari’ah rules and principles including the Shari’ah Standards published by the Accounting and Auditing Organization for Islamic Financial Institutions.

2 Application of new and revised International Financial Reporting Standards ("IFRS")

2.1 New and revised IFRS applied on the financial statements

The following new and revised IFRS, which became effective for annual periods beginning on or after 1 January 2019, have been adopted in these financial statements. The application of these revised IFRSs has not had any material impact on the amounts reported for the current and prior years.

- **IFRS 16, ‘Leases’** - This standard replaces the current guidance in IAS 17 and is a far reaching change in accounting by lessees in particular. Under IAS 17, lessees were required to make a distinction between a finance lease (on balance sheet) and an operating lease (off balance sheet). IFRS 16 now requires lessees to recognise a lease liability reflecting future lease payments and a ‘right-of-use asset’ for virtually all lease contracts. The IASB has included an optional exemption for certain short-term leases and leases of low-value assets; however, this exemption can only be applied by lessees.

2 Application of new and revised International Financial Reporting Standards ("IFRS") (continued)

2.1 New and revised IFRS applied on the financial statements (continued)

- **IFRS 16, 'Leases'** (continued)

  For lessors, the accounting remains mainly unchanged. However, as the IASB has updated the guidance on the definition of a lease (as well as the guidance on the combination and separation of contracts), lessors will also be affected by the new standard. At the very least, the new accounting model for lessees is expected to impact negotiations between lessors and lessees. Under IFRS 16, a contract is, or contains, a lease if the contract conveys the right to control the use of an identified asset for a period of time in exchange for consideration.

There is no material impact on the financial statements of the Company from the adoption of above standard on 1 January 2019.

- **IFRIC 23, 'Uncertainty over Income Tax Treatments' –** The interpretation address the determination of taxable profit (tax loss) tax bases, unused tax credits and tax rates, when there is uncertainty over income tax treatments under IAS 12. It specifically considers

  - Whether tax treatments should be considered collectively
  - Assumptions for taxation authorities
  - The determination of taxable profit (tax loss), tax bases, unused tax losses, and tax rates
  - The effect of changes in facts and circumstances

There is no material impact on the financial statements of the Company from the adoption of above amendment on 1 January 2019.

- **Amendment to IFRS 9, Financial instruments', on prepayment features with negative compensation and modification of financial liabilities -** This amendment confirmed two points: (1) that reasonable compensation for prepayments can be both negative or positive cash flows when considering whether a financial asset solely has cash flows that are principal and profit and (2) that when a financial liability measured at amortised cost is modified without this resulting in de-recognition, a gain or loss should be recognised immediately in profit or loss. The gain or loss is calculated as the difference between the original contractual cash flows and the modified cash flows discounted at the original effective profit rate. This means that the difference cannot be spread over the remaining life of the instrument which may be a change in practice from IAS 39.

There is no material impact on the financial statements of the Company from the adoption of above amendment on 1 January 2019.

2 Application of new and revised International Financial Reporting Standards ("IFRS") (continued)

2.2 New and revised IFRS in issue but not yet effective

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

New standards, amendments and interpretations	Effective for annual periods beginning on or after
Amendment to IFRS 9, IAS 39 and IFRS 7, 'Profit rate benchmark reform'- These amendments provide certain reliefs in connection with profit rate benchmark reform. The reliefs relate to hedge accounting and have the effect that IBOR reform should not generally cause hedge accounting to terminate. However, any hedge ineffectiveness should continue to be recorded in the income statement. Given the pervasive nature of hedges involving IBOR based contracts, the reliefs will affect companies in all industries.	1 January 2020
Amendments to IAS 1 and IAS 8 on the definition of material - These amendments to IAS 1, 'Presentation of financial statements', and IAS 8, 'Accounting policies, changes in accounting estimates and errors', and consequential amendments to other IFRSs: i) use a consistent definition of materiality throughout IFRSs and the Conceptual Framework for Financial Reporting; ii) clarify the explanation of the definition of material; and iii) incorporate some of the guidance in IAS 1 about immaterial information.	1 January 2020
Amendments to IFRS 3, 'definition of a business'-This amendment revises the definition of a business. According to feedback received by the IASB, application of the current guidance is commonly thought to be too complex, and it results in too many transactions qualifying as business combinations.	1 January 2020

2 Application of new and revised International Financial Reporting Standards ("IFRS") (continued)

2.2 New and revised IFRS in issue but not yet effective (continued)

New standards, amendments and interpretations	**Effective for annual periods beginning on or after**
IFRS 17, 'Insurance contracts' - On 18 May 2017, the IASB finished its long-standing project to develop an accounting standard on insurance contracts and published IFRS 17, 'Insurance Contracts'. IFRS 17 replaces IFRS 4, which currently permits a wide variety of practices. IFRS 17 will fundamentally change the accounting by all entities that issue insurance contracts and investment contracts with discretionary participation features. The standard applies to annual periods beginning on or after 1 January 2023, with earlier application permitted if IFRS 15, 'Revenue from contracts with customers' and IFRS 9, 'Financial instruments' are also applied. IFRS 17 requires a current measurement model, where estimates are remeasured in each reporting period. The measurement is based on the building blocks of discounted, probability-weighted cash flows, a risk adjustment and a contractual service margin ("CSM") representing the unearned profit of the contract. A simplified premium allocation approach is permitted for the liability for the remaining coverage if it provides a measurement that is not materially different from the general model or if the coverage period is one year or less. However, claims incurred will need to be measured based on the building blocks of discounted, risk-adjusted, probability weighted cash flows. The Company is currently assessing the impact of the above new standard on the financial statements.	1 January 2023

There are no other relevant applicable new standards and amendments to published standards or IFRIC interpretations that have been issued but are not effective for the first time for the Company's financial year beginning on 1 January 2019 that would be expected to have a material impact on the financial statements of the Company.

3 Summary of significant accounting policies

3.1 Statement of compliance

The financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS), the Shari'ah rules and principles as determined by the Company's Shari'ah Supervisory Board to the extent that those are compatible with IFRS and applicable requirements of the laws of the United Arab Emirates ("UAE").

3.2 Basis of preparation

The financial statements of the Company have been prepared on the historical cost basis except for 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 financial statements are presented in Arab Emirates Dirham (AED) and all values are rounded to the nearest thousands AED, except where otherwise indicated.

The principal accounting policies adopted are set out below.

3.3 Revenue recognition

(a) Income from Islamic financing and investments products

The Company's policy for recognition of income from Islamic financing and investments products is described in Note 3.9.

(b) Fee and commission income and expenses

Fees and other income from financing services are recognized on an accrual basis as the service is performed, when it is probable that associated economic benefits will flow to the Company and a reliable estimate of amount can be made. Fees and commission income and expense that are integral to the effective profit rate on a financial asset or liability are included in the measurement of the effective profit rate.

3.4 Foreign currency transactions

(a) Functional and presentation currency

Items included in the financial statements of the Company are measured using the currency in which the majority of its transactions are denominated ('the functional currency'). These financial statements are presented in United Arab Emirates Dirham (AED), which is the currency of the country in which the Company is domiciled.

3 Summary of significant accounting policies (continued)

3.4 Foreign currency transactions (continued)

(b) Transactions and balances

Transactions denominated in foreign currencies are initially recorded at the rates of exchange prevailing on the dates of the transactions. Monetary assets and liabilities denominated in such currencies are translated at the rates prevailing at the end of the reporting year. Gains and losses arising from foreign currency transactions are included in the statement of comprehensive income.

3.5 Impairment of non-financial assets

At the end of each reporting period, the Company reviews the carrying amounts of its non-financial 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). When it is not possible to estimate the recoverable amount of an individual asset, the Company estimates the recoverable amount of the cash-generating unit to which the asset belongs. When 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.

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 discount rate that reflects current market assessments of the time value of money and the risks specific to the asset for which the estimates of future cash flows have not been adjusted.

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 recognised in the statement of comprehensive income.

When 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 recognised for the asset (or cash-generating unit) in prior years.

3 Summary of significant accounting policies (continued)

3.6 Provisions

Provisions are recognised when the Company has a present obligation (legal or constructive) as a result of a past event, it is probable that the Company 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.

3.7 Financial instruments

Financial assets and financial liabilities are recognised when the Company 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 or loss) are added to or deducted from the fair value of the financial assets or financial liabilities, as appropriate, on initial recognition.

3 Summary of significant accounting policies (continued)

3.7 Financial instruments (continued)

Transaction costs directly attributable to the acquisition of financial assets or financial liabilities at fair value through profit or loss are recognised immediately in the statement of comprehensive income.

Immediately after initial recognition, an expected credit loss ("ECL") allowance is recognised for financial assets measured at amortised cost, as described in note 18, which results in an accounting loss being recognised in profit or loss when an asset is newly originated.

When the fair value of financial assets and liabilities differs from the transaction price on initial recognition, the entity recognises the difference as follows:

(a) When the fair value is evidenced by a quoted price in an active market for an identical asset or liability (i.e. a Level 1 input) or based on a valuation technique that uses only data from observable markets, the difference is recognised as a gain or loss.

(b) In all other cases, the difference is deferred and the timing of recognition of deferred day one profit or loss is determined individually. It is either amortised over the life of the instrument, deferred until the instrument's fair value can be determined using market observable inputs, or realised through settlement.

3.7.1 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.

(i) Classification of financial assets

The Company has applied IFRS 9 which has the following measurement categories:

- Fair value through profit or loss (FVTPL);
- Fair value through other comprehensive income (FVOCI); and
- Amortized cost

The classification requirement for financial assets and equity instruments are described below.

Financial assets are those instruments that meet the definition of a financial liability from the issuer's perspective, such as investments in Islamic financing instruments.

3 Summary of significant accounting policies (continued)

3.7 Financial instruments (continued)

3.7.1 Financial assets (continued)

(i) Classification of financial assets (continued)

Classification and subsequent measurement of financial assets depend on:

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

Based on these factors, the Company classifies its financial instruments into one of the following three measurement categories:

- Amortised cost: Assets that are held for collection of contractual cash flows where those cash flows represent solely payments of principal and profit ('SPPP'), and that are not designated at fair value through profit or loss (FVTPL), are measured at amortised cost. The carrying amount of these assets is adjusted by any expected credit loss allowance recognized and measured as described in Note 18. Profit income from these financial assets is included in "Income from Islamic financing products measured at amortised cost" using the effective profit rate method.

- Fair value through other comprehensive income (FVTOCI): Financial assets that are held for collection of contractual cash flows and for selling the assets, where the assets' cash flows represent solely payments of principal and profit, and that are not designated at FVTPL, are measured at FVTOCI. Movement in carrying amount are taken through Other Comprehensive Income (OCI), except for the recognition of impairment gains and losses, profit income and foreign exchange gains and losses on the instruments' amortised cost which are recognized in profit or loss. When the financial asset is derecognized, the cumulative gain or loss previously recognized in OCI is reclassified from equity to profit or loss and recognized in 'Net Investment Income'.

- Fair value through profit or loss (FVTPL): Assets that do not meet the criteria for amortised cost or FVTOCI are measured at fair value through profit or loss. A gain or loss on a financial asset that is subsequently measured at fair value through profit or loss and is not part of a hedging relationship is recognized in profit or loss and presented in the statement of comprehensive income within 'Net investment income' in the period in which it arises, unless it arises from financial assets that were designated at fair value or which are not held for trading, in which case they are presented separately in statement of comprehensive income.

3 Summary of significant accounting policies (continued)

3.7 Financial instruments (continued)

3.7.1 Financial assets (continued)

(i) Classification of financial assets (continued)

Business model: the business model reflects how the Company manages the assets in order to generate cash flows. That is, whether the Company's objective is solely to collect the contractual cash flows from the assets or is to collect both the contractual cash flows and cash flows arising from the sale of assets. If neither of these is applicable (e.g. financial assets are held for trading purposes), then the financial assets are classified as part of 'other' business model and measured at FVTPL. Factors considered by the Company in determining the business model for a group of assets include past experience on how the cash flows for these assets were collected, how the asset's performance is evaluated and reported to key management personnel, how risks are assessed and managed and how managers are compensated.

SPPP: Where the business model is to hold assets to collect contractual cash flows or to collect contractual cash flows and sell, the Company assesses whether financial instruments' cash flows represent solely payments of principal and profit (the 'SPPP test'). In making this assessment, the Company considers whether contractual cash flows are consistent with a basic financing arrangement i.e. profit includes only consideration for the time value of money, credit risk, other basic financing risks and a profit margin that is consistent with basic financing arrangement. Where the contractual terms introduce exposure to risk or volatility that are inconsistent with a basic financing arrangement, the related financial asset is classified and measured at fair value through profit or loss.

The Company reclassifies financial assets when its business model for managing those assets changes. The reclassification takes place from the start of the first reporting period following the change. Such changes are expected to be very infrequent and there were no material reclassification during the year.

Equity instruments:

Equity instruments are instruments that meet the definition of equity from the issuer's perspective; that is, instruments that do not contain a contractual obligation to pay and that evidence a residual interest in the issuer's net assets. Examples of equity instruments include basic ordinary shares.

The Company subsequently measures all equity investments at fair value through profit or loss, except where the Company's management has elected, at initial recognition, to irrevocably designate an equity investment at fair value through other comprehensive income. The Company's policy is to designate equity investments as FVTOCI when those investments are held for purposes other than to generate investment returns. When this election is used, fair value gains and losses are recognized in OCI and are not subsequently reclassified to profit or loss, including on disposal. Impairment losses (and reversal of impairment losses) are not reported separately from other changes in fair value. Dividends, when representing a return on such investments, continue to be recognized in profit or loss as other income when the Company's right to receive payments is established.

3 Summary of significant accounting policies (continued)

3.7 Financial instruments (continued)

3.7.1 Financial assets (continued)

(ii) Measurement methods

<u>Amortised cost and effective profit rate</u>

The amortised cost is the amount at which the financial asset or financial liability is measured at initial recognition minus the principal repayments, plus or minus the cumulative amortization using the effective profit rate method of any difference between that initial amount and the maturity amount and, for financial assets, adjusted for any loss allowance.

The effective profit rate is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial asset or financial liability to the gross carrying amount of a financial asset (i.e. its amortised cost before any impairment allowance) or to the amortised cost of a financial liability. The calculation does not consider expected credit losses and includes transaction costs, profit or discounts and fees paid or received that are integral to the effective profit rate, such as origination fees.

When the Company revises the estimates of future cash flows, the carrying amount of the respective financial asset or financial liability is adjusted to reflect the new estimate discounted using original effective profit rate. Any changes are recognized in profit or loss.

Profit income is calculated by applying the effective profit rate to the gross carrying amount of financial assets, except for financial assets that have subsequently become credit-impaired (or stage 3), for which profit income is calculated by applying the effective profit rate to their amortised cost (i.e. net of the expected credit loss provision).

(iii) Impairment of financial assets

The Company assesses on a forward-looking basis the expected credit loss (‘ECL’) associated with its financial assets carried at amortised cost that are Islamic financing instruments. The Company recognizes a loss allowance for such losses at each reporting date. The measurement of ECL reflects:

- An unbiased and probability-weighted amount that is determined by evaluating a range of possible outcomes;
- The time value of money; and
- Reasonable and supportable information that is available without undue cost or effort at the reporting date about past events, current conditions and forecasts of future economic conditions.

Note 18 provides more detail of how the expected credit loss allowance is measured.

3 Summary of significant accounting policies (continued)

3.7 Financial instruments (continued)

3.7.1 Financial assets (continued)

(iv) Modification of financing *facilities*

The Company sometimes renegotiates or otherwise modifies the contractual cash flows of financings to customers. Where this happens, the Company assesses whether or not the new terms are substantially different to the original terms. The Company does this by considering, among others, the following factors:

- If the customer is in financial difficulty, whether the modification merely reduces the contractual cash flows to amounts the customer is expected to be able to pay.
- Whether any substantial new terms are introduced, such as a profit share / equity-based return that substantially affects the risk profile of the facility.
- Significant extension of the financing term when the customer is not in financial difficulty.
- Significant change in the profit rate.
- Change in the currency the financing is denominated in.
- Insertion of collateral, other security or credit enhancements that significantly affect the credit risk associated with the financing facility.

If the terms are substantially different, the Company derecognizes the original financial asset and recognizes a ‘new’ asset at fair value and recalculates a new effective profit rate for the asset. The date of renegotiation is consequently considered to be the date of initial recognition for impairment calculation purposes, including for the purpose of determining whether a significant increase in credit risk has occurred. However, the Company also assesses whether the new financial asset recognized is deemed to be credit-impaired at initial recognition, especially in circumstances where the renegotiation was driven by the customer being unable to make the originally agreed payments. Differences in the carrying amount are also recognized in profit or loss as a gain or loss on derecognition.

If the terms are not substantially different, the renegotiation or modification does not result in the derecognition, and the Company recalculates the gross carrying amount based on the revised cash flows of the financial asset and recognizes a modification gain or loss in profit or loss. The new gross carrying amount is recalculated by discounting the modified cash flows at the original effective profit rate.

(v) Derecognition other than on a modification

Financial assets, or a portion thereof, are derecognized when the contractual rights to receive the cash flows from the assets have expired, or when they have been transferred and either,

(i) the Company transfers substantially all the risks and rewards of ownerships, or
(ii) the Company neither transfers nor retains substantially all the risks and rewards of ownership and the Company has not retained control.

3 Summary of significant accounting policies (continued)

3.7 Financial instruments (continued)

3.7.1 Financial assets (continued)

(v) Derecognition other than on a modification (continued)

The Company enters into transactions where it retains the contractual rights to receive cash flows from assets but assumes a contractual obligation to pay those cash flows to other entities and transfers substantially all of the risks and rewards.

These transactions are accounted for as 'pass through' transfers that result in derecognition if the Company:

- has no obligation to make payments unless it collects equivalent amounts from the assets;
- is prohibited from selling or pledging the assets; and
- has an obligation to remit any cash it collects from the assets without material delay.

3.7.2 Financial liabilities

(i) Classification and subsequent measurement

Financial liabilities (including balance due to bank) are initially recognised as fair value and subsequently measured at amortised cost.

(ii) Derecognition

Financial liabilities are derecognised when they are extinguished (i.e. when the obligation specified in the contract is discharged, cancelled or expires).

3.7.3 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 statement of comprehensive income;
- for financial assets that are monetary items and designated as at FVTOCI, any foreign exchange component is recognized in statement of comprehensive income;
- for financial assets that are non-monetary items and designated as at FVTOCI, any foreign exchange component is recognised in the statement of comprehensive income; and
- for foreign currency denominated financial 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 statement of comprehensive income.

3 Summary of significant accounting policies (continued)

3.8 Offsetting of financial assets and liabilities

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

3.9 Islamic financing products

Any conventional terminologies that are used only for reasons of legal requirement, explanation and/or clarity will be considered as replaced with its Shari'ah compliant equivalent and will not impact the Islamic products or documentation in terms of their Shari'ah compliance.

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

(i) Definitions

The following terms are used in Islamic financing:

Murabahah

An agreement whereby the Company sells to a customer a commodity or an asset, which the Company 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.

Ijarah

An agreement whereby the Company 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.

Wakalah

An agreement whereby the Company 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 Wakalah.

Sukuk

These comprise asset backed Shari'ah compliant trust certificates. The trust certificate owners share the return and bear the losses in proportion to the certificates held by them.

3 Summary of significant accounting policies (continued)

3.9 Islamic financing products (continued)

(ii) Accounting policy

Islamic financing 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.

Allowance for impairment is made against Islamic financing and investment products when their recovery is in doubt taking into consideration IFRS requirements [as explained in Note 18(a)]. Islamic financing 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 products are recognised in the statement of comprehensive income 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.

Murabahah

Murabahah income is recognised on effective profit rate basis over the period of the contract based on the balance outstanding.

Ijarah

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

Wakalah

Estimated income from Wakalah is recognised 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.

Sukuk

Profit and coupon revenue is accrued on time basis, by reference to the principal outstanding and at the effective profit rate applicable, which is the rate that exactly discounts estimated future cash through the expected life of the financial assets to that assets' net carrying amount.

3 Summary of significant accounting policies (continued)

3.10 Non-current assets held for sale

Non-current assets are classified as held for sale if their carrying amount will be recovered principally through a sale transaction rather than through continuing use and a sale is considered highly probable, management is committed to a plan to sell the asset, and an active programme to locate a buyer and complete the plan is initiated. They are measured at the lower of their carrying amount and fair value less costs to sell.

3.11 Cash and cash equivalents

For the purposes of the statement of cash flows, cash and cash equivalents comprise balance in current account. Cash and cash equivalents are carried at amortized cost in the statement of financial position.

4 Critical accounting judgments and key sources of estimation uncertainty

In the application of the Company’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:

4.1 Measurement of the expected credit loss allowance

The measurement of the expected credit loss allowance for financial assets measured at amortised cost, is an area that requires the use of complex models and significant assumptions about future economic conditions and credit behaviour (e.g. the likelihood of customers defaulting and the resulting losses). Explanation of the inputs, assumptions and estimation techniques used ifn measuring Expected Credit Loss (ECL) is further detailed in note 18.

A number of significant judgements are also required in applying the accounting requirements for measuring ECL, such as:

- Determining the criteria for significant increase in credit risk;
- Determining the criteria and definition of default;
- Choosing appropriate models and assumptions for the measurement of ECL;
- Establishing the number and relative weightings of forward-looking scenarios for each type of product/market and the associated ECL; and
- Establishing groups of similar financial assets for the purposes of measuring ECL.

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

4.2 Fair valuation of properties

The Company values its 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.

5 Cash and cash equivalents

Cash and cash equivalents comprise cash at bank held with the Parent Company.

	2019	2018
	AED'000	AED'000
Cash at banks:		
Current accounts (Note 10)	**1,267**	1,267

As at 31 December 2019 and 2018, the balances with bank in current accounts are profit free and repayable on demand.

6 Islamic financing products measured at amortised cost

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

	2019	2018
	AED'000	AED'000
Financing		
Murabahah	**89,930**	246,022
Ijarah	**1,162,389**	1,146,767
	1,252,319	1,392,789
Less: Unearned income	**(14,590)**	(28,197)
Allowance for impairment	**(44,998)**	(37,767)
	1,192,731	1,326,825

(b) The Company's Islamic financing products measured at amortised cost include facilities extended to retail customers only.

6 Islamic financing products measured at amortised cost (continued)

(c) Allowance for impairment movement:

	2019 AED'000	2018 AED'000
At 1 January	**37,767**	44,488
Charge / (reversal) during the year	**4,967**	(8,084)
Profit in suspense	**2,264**	1,363
At 31 December	**44,998**	37,767

(d) In certain cases, the Company continues to carry certain classified doubtful financing and delinquent accounts on its books which have been fully provided. Profit is accrued on most of these accounts for litigation purposes only. As at 31 December 2019 and 2018, legal proceedings are pursued for some of these accounts by the Company in the normal course of business.

(e) In determining the recoverability of Islamic financing products, the Company considers any change in the credit quality of the Islamic financing 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.

7 Other assets

As at 31 December 2019, the Company formalized its intention to sell the properties included in property and equipment, and accordingly has reclassified these properties as held for sale which are included in other assets at 31 December 2019. These properties are carried at AED 73 million as at 31 December 2019 which is lower than the fair value less costs to sell of the properties at 31 December 2019 by an equivalent amount in order to comply with regulatory requirements to impair the properties to the extent of 50% as set out in a letter from the UAE Central Bank dated 2 September 2019. The properties are registered in the name of the Parent Company on trust and for the benefit of the Company.

8 Property and equipment

Property and equipment represent freehold land in the Emirate of Sharjah, United Arab Emirates.

	AED'000
Cost	
At 1 January 2018	211,224
Impairment	-
At 31 December 2018	**211,224**
Transfer to other assets (Note 7)	**(211,224)**
At 31 December 2019	**-**

9 Other liabilities

	2019 AED'000	2018 AED'000
Accrued expenses	**1,614**	2,535
Commission income collected in advance	**1,043**	915
Others	**221**	331
	2,878	3,781

Accrued expenses include AED 1.5 million (2018: AED 2.4 million) for management fee expense payable to the Parent Company (Note 10).

10 Related party balances and transactions

The Company enters into transactions with the parties that fall within the definition of a related party as contained in International Accounting Standard 24 (IAS 24): Related Party Disclosures. Related parties comprise companies and entities under common ownership and/or common management / control and key management personnel.

Related party balances included in the statement of financial position are as follows:

	2019 AED'000	2018 AED'000
Parent Company		
Current accounts (Note 5)	**1,267**	1,267
Accrued expenses (Note 9)	**(1,539)**	(2,416)
Due to Parent Company (Note 10.1)	**(495,177)**	(661,522)

Accrued expenses represent amount payable to the Parent Company for Management fee expense (Note 14).

Letter of guarantee provided by the ultimate Parent Company amounted to AED 200 million (2018: AED 200 million) (Note 16).

Related party transactions for the year are as follows:

	2019 AED'000	2018 AED'000
Parent Company		
Management Fees	**18,224**	22,303

Management fee represents amount paid by the Company in lieu of services rendered by the Parent Company for the IT support, risk management and compliance, and other administrative functions.

10 Related party balances and transactions (continued)

10.1 Due to Parent Company

Amount due to Parent Company is payable to the ultimate Parent Company that includes balances as follows:

	2019 **AED'000**	2018 AED'000
Demand	**281,746**	447,520
Time	**212,853**	212,853
Others	**578**	1,149
	495,177	661,522

Demand deposit includes an unsecured overdraft facility, which is without any fixed repayment schedule. No profit is charged on the amount due to Parent Company.

Time deposit includes deposits with the Parent Company which is renewable on a quarterly basis and on which no profit is charged.

11 Issued and paid up share capital

The issued and fully paid-up capital of the Company comprises of 5,000,000 shares of AED 100 each. As at 31 December 2019 and 2018, share capital is held by the following parties:

	Number of shares	**Amount AED'000**
Mashreqbank PSC – U.A.E.	**4,985,000**	**498,500**
Injaz Services FZ LLC – U.A.E.	**5,000**	**500**
Abdul Aziz Abdulla Al Ghurair	**5,000**	**500**
Abdulla Bin Ahmed Al Ghurair	**5,000**	**500**
	5,000,000	**500,000**

12 Statutory reserve

As required by the Commercial Companies Law and the Company's Articles of Association, 10% of the profit for the year is transferred to statutory reserve. The Company may resolve to discontinue such annual transfers when the reserve totals 50% of paid up share capital. This reserve is not available for distribution except in the circumstances as stipulated by U.A.E. Commercial Companies Law.

13 Fees and commission income

	2019	2018
	AED'000	AED'000
Takaful related income	**431**	861
Prepayment and settlement income	**1,174**	1,475
Processing fees and others	**396**	951
	2,001	3,287

14 General and administrative expenses

	2019	2018
	AED'000	AED'000
Management fees (Note 10)	**18,224**	22,303
Other expenses	**180**	302
	18,404	22,605

15 Allowance for impairment, net

	2019	2018
	AED'000	AED'000
Islamic financing products measured at amortised cost written off / charge during the year	**21,130**	24,678
Recovery of Islamic financing product measured at amortised cost previously written off	**(3.426)**	(3,294)
	17,704	21,384

16 Contingencies

	2019	2018
	AED'000	AED'000
Letter of guarantee (Note 10)	**200,000**	200,000

The letter of guarantee has been issued on behalf of the Company by the Parent Company without any commission charges, in favor of Central Bank of the U.A.E., in consideration of the license granted to the Company.

17 Capital management

The Company manages its capital to ensure that the Company will be able to continue as a going concern while maximising the return to shareholders through the optimisation of the funding and equity balance. The Company's overall strategy remains unchanged from the year ended 31 December 2018.

18 Risk management

The Parent Company sets and monitors the risk management function of the Company. The Company has risk management infrastructure supported by adoption of the best practices in the field of risk management to manage and monitor the following major risks arising out of its day to day operations:

(a) Credit risk
(b) Liquidity risk
(c) Market risk
(d) Operational risk

The Parent Company's Risk Committee works under the mandate of the Board of Directors (BOD) to set up risk limits and manage the overall risk in the Company. The Board of Directors (the "BOD") through the Board Risk Committee (the "BRC") has overall responsibility for the establishment and oversight of the Company's risk management framework and they are assisted by various committees including the Enterprise Risk Committee, Management Credit Committee (MCC), Assets and Liabilities Committee (ALCO) and Investment Committee etc. These committees except the MCC work under the terms of reference set by the BOD and approve all risk management policies for the Company.

While the Board carries ultimate responsibility for overall risk management within the Company, the BRC will assist the Board in discharging its responsibilities in relation to 'Risk Management', which includes identifying, analyzing, assessing, treating, monitoring and communicating the risks associated with all activities, functions and processes within the Company. The BRC will make recommendations to the Board for approval of the Company's overall Risk Appetite.

18 Risk management (continued)

The Enterprise Risk Committee has overall responsibility for the oversight of the risk management framework and the risk appetite of the Company. The Enterprise Risk Committee is responsible for the approval of credit policies and procedures of the Company and to ensure adherence to the approved policies and close monitoring of different risks within the Company. The Enterprise Risk Committee also monitors and establishes various concentration limits, approves policy exceptions and monitors periodic portfolio reviews to ascertain asset quality.

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

The Audit, Fraud and Prevention Group (AFPG) are independent of Risk Management. AFPG provides independent assurance to stakeholders and senior management on compliance with all credit policies and procedures in the Company and the effectiveness of credit management processes. This is undertaken by a periodic review of all risk-taking units, in addition to Risk Management.

18 Risk management (continued)

(a) Credit risk management

Credit risk is the risk of suffering financial loss, should any of the Company's customers fail to fulfil their contractual obligations to the Company. Credit risk related to the Company arises from Islamic financing products.

Credit risk is the single largest risk from the Company's business of extending Islamic financing products; management therefore carefully manages its exposure to credit risk. The credit risk management and control is centralized under the CCO function with regular monitoring performed by Enterprise Risk Committee.

The estimation of credit exposure for risk management purposes is complex and requires the use of models, as the exposure varies with changes in market conditions, expected cash flows and the passage of time. The assessment of credit risk of a portfolio of assets entails further estimations as to the likelihood of defaults occurring of the associated loss ratios and of default correlations between counterparties. The Company measures credit risk using the concept of Expected Loss which requires the following measures

-Probability of Default (PD)
-Loss Given Default (LGD)
-Exposure at Default (EAD)

Under IFRS 9 expected loss is replaced by expected Credit Loss (ECL), which is based on macro adjusted PD, LGD & EAD measures. Additionally it also captures deterioration and lifetime likelihood of defaults.

Credit risk grading

The Company use specific internal rating models tailored to the various industry segments/counterparties. Customer and financing specific information collected at the time of application (such as disposable income and level of collateral) is fed into this rating model.

The credit grades are calibrated such that risk of default increases exponentially at each higher risk grade. For example, this means that the difference in the PD between a 6 and 8 rating grade is lower than the difference in the PD between a 18 and 20 rating grade.

The Risk Rating system for performing assets ranges from 1 to 25, each grade being associated with a Probability of Default ("PD"). Non-performing clients are rated 50, 60, 70, 80 and 99, corresponding to NAUR (Non-accrual Under Restructuring), Substandard, Doubtful, Loss classifications and Write-off.

These risk ratings have been mapped into 5 Grades which are defined below:

Grade	**Risk Rating**	**Definition**
Grade 1	1-12	Low risk
Grade 2	13-17	Satisfactory risk
Grade 3	18-20	Fair risk
Grade 4	21-25	Watch list
Grade 5	50,60,70,80,90	Impaired

18 Risk management (continued)

(a) Credit risk management (continued)

Expected credit loss measurement

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

- A financial instrument that is not credit-impaired on initial recognition is classified in 'Stage 1' and has its credit risk continuously monitored by the Company.
- If a significant increase in credit risk ('SICR') since initial recognition is identified, the financial instrument is moved to 'Stage 2' but is not yet deemed to be credit-impaired. The identification of SICR is measured via a change in one year probability of default between the date of inception of facility and the date of IFRS 9 ECL run.
- If the financial instrument is credit-impaired, the financial instrument is then moved to 'Stage 3'.
- Financial assets in Stage 1 have their ECL measured at an amount equal to the portion of lifetime expected credit losses that result from default events possible within the next 12 months. Instruments in Stages 2 or 3 have their ECL measured based on expected credit losses on a lifetime basis.
- A pervasive concept in measuring the ECL in accordance with IFRS 9 is that it should consider forward-looking information.

Significant increase in credit risk (SICR)

The Company considers a financial asset to have experienced a significant increase in credit risk when a significant change in one year probability of default occurs between the origination date of a specific facility and the IFRS 9 ECL run date. Further, exposures that are 30 Days Past Due (DPD) and/or have undergone a restructuring in the last 2 years are also considered as an additional criterion for SICR. Where the 30 days past due presumption is rebutted on the basis that there has not been a significant increase in credit risk, the Company shall accompany the assertion by sufficiently documented, reasonable and supportable information that a more lagging criterion is appropriate

Definition of default and credit-impaired assets

The Company defines a facility in default, which is fully aligned with the definition of credit-impaired, when it meets one or more of the following criteria:

Quantitative criteria

The obligor is more than 90 days past due on its contractual payments.

18 Risk management (continued)

(a) Credit risk management (continued)

Definition of default and credit-impaired assets (continued)

Qualitative criteria:

According to the Basel definition, default is considered to have occurred with regards to particular obligors when either one of the following events have taken place:

- The Company considers that the obligor is unlikely to pay its credit obligation to the Company in full without recourse by the Company to actions like realizing security (if held).
- The Company puts the credit obligation on a non-accrued status.
- The Company makes a charge-off or account-specific provision resulting from a perceived decline in credit quality subsequent to the Company taking on the exposure.
- The Company sells the credit obligation at a material credit-related economic loss.
- The Company consents to a distressed restructuring of the credit obligation where this is likely to result in a diminished financial obligation caused by the material forgiveness or postponement of principal, profit and other fees.
- The Company has filed for the obligor's bankruptcy or similar order in respect of the obligor's credit obligation to the Company.
- The obligor is past due more than 90 days on any material credit obligation to the Company.

The criteria above have been applied to all financial instruments held by the Company and are consistent with the definition of default used for internal credit risk management purposes. The default definition has been applied consistently to model the Probability of Default (PD), Exposure at Default (EAD), and Loss Given Default (LGD) throughout the Company's expected loss calculations.

An instrument is considered to no longer be in default (i.e. to have cured) when it no longer meets any of the default criteria for a consecutive period of twelve months. This period of twelve months has been determined based on an analysis which considers the likelihood of a financial instrument returning to default status after cure using different cure definitions.

Measuring ECL – Explanation of inputs, assumptions and estimation techniques

The Expected Credit Loss (ECL) is measured on either a 12-month (12M) or lifetime basis depending on whether a significant increase in credit risk has occurred since the initial recognition of a specific facility or whether an asset is considered credit-impaired. The Company has adopted a forward exposure method for computing the ECL for each facility. The Company has opted for a monthly granular computation of PD, EAD and LGD.

18 Risk management (continued)

(a) Credit risk management (continued)

Measuring ECL – Explanation of inputs, assumptions and estimation techniques (continued)

- The PD represents the likelihood of a customer defaulting on its financial obligation (as per 'Definition of default and credit-impaired' above), either over the next 12 months (12M PD), or over the remaining lifetime (Lifetime PD) of the obligation.
- EAD is based on the amounts the Company expected to be owed at the time of default, over the next 12 months (12M EAD) or over the remaining lifetime (Lifetime EAD).
- LGD represents the Company's expectation of the extent of loss on a defaulted exposure. LGD varies by type of product, type and seniority of claim and availability of collateral or other credit support. LGD is expressed as a percentage loss per unit of exposure at the time of default (EAD). LGD is calculated on a 12-month or lifetime basis, where 12-month LGD is the percentage of loss expected to be made if the default occurs in the next 12 months and lifetime LGD is the percentage of loss expected to be made if the default occurs over the remaining expected lifetime of the financing.

The ECL is determined by projecting the PD, LGD and EAD for each future month and for each individual exposure or collective segment. These three components are multiplied together and adjusted for the likelihood of survival (i.e. the exposure has not prepaid or defaulted in an earlier month). This effectively calculates an ECL for each future month, which is then discounted back to the reporting date and summed. The discount rate used in the ECL calculation is the effective profit rate or an approximation thereof.

Lifetime expected credit losses are expected credit loss resulting from all probable default events over the expected lifetime of the financial instrument. Expected credit losses are the probability-weighted average of credit losses and the weighing factor is the Probability of Default (PD) for a lifetime.

The Parent Company has implemented macro-economic models that are used to forecast future credit transitions using Moody's research macro-economic forecast under the IFRS 9 scenarios i.e. upwards and downwards.

The 12-month and lifetime EADs are determined based on the expected payment profile, which varies by product type.

- For amortising products and bullet repayments financing products, this is based on the contractual repayments owed by the customer over a 12 month period or lifetime basis.
- For revolving products, the exposure at default is predicted by taking current drawn balance and adding a "credit conversion factor" which allows for the expected drawdown of the remaining committed limit by the time of default.

18 Risk management (continued)

(a) Credit risk management (continued)

Measuring ECL – Explanation of inputs, assumptions and estimation techniques (continued)

The Parent Company has adopted a workout methodology for LGD computation.

The 12-month and lifetime LGDs are determined based on the factors which impact the recoveries made post default. These vary by product type.

- For secured products, this is primarily based on collateral type and projected collateral values, historical discounts to market/book values due to forced sales, time to repossession and recovery costs observed.
- For unsecured products, LGDs are typically set at product level due to the limited differentiation in recoveries achieved across different customers. These LGDs are influenced by collection strategies.

Forward-looking economic information is also included in determining the 12-month and lifetime PD.

There have been no significant changes in estimation techniques or significant assumptions made during the year.

Forward looking information incorporated in the ECL models

The assessment of SICR and the calculation of ECL both incorporate forward-looking information. The Company has performed historical analysis and identified the key economic variables impacting credit risk and expected credit losses for each portfolio.

These economic variables and their associated impact on the PD, EAD and LGD vary by financial instrument. Forecasts of these economic variables (the "base economic scenario") are provided by the Economics team and provide the best estimate view of the economy over the next five years.

The Company considers these forecasts to represent its best estimate of the possible outcomes and has analyzed the non-linearities and asymmetries within the Company's different portfolios to establish that the chosen scenarios are appropriately representative of the range of possible scenarios.

18 Risk management (continued)

(a) Credit risk management (continued)

Maximum exposure to credit risk – Financial instruments subject to impairment

The following table contains an analysis of the credit risk exposure of financial assets which are subject to ECL. The gross carrying amount of financial assets below also represents the Company's maximum exposure to credit risk on these assets:

	2019				**2018**			
Credit risk exposures relating to on-balance sheet assets are as follows:	**Stage 1 12-month AED'000**	**Stage 2 Lifetime AED'000**	**Stage 3 Lifetime AED'000**	**Total AED'000**	**Stage 1 12-month AED'000**	**Stage 2 Lifetime AED'000**	**Stage 3 Lifetime AED'000**	**Total AED'000**
Cash and cash equivalents								
Investment-grade	**1,267**	**-**	**-**	**1,267**	1,267	-	-	1,267
Loss allowance	**-**	**-**	**-**	**-**	-	-	-	-
Carrying amount	**1,267**	**-**	**-**	**1,267**	1,267	-	-	1,267

18 Risk management (continued)

(a) *Credit risk management* (continued)

Maximum exposure to credit risk – Financial instruments subject to impairment (continued)

	2019				**2018**			
Islamic financing products measured at amortised cost	**Stage 1 12-month AED'000**	**Stage 2 Lifetime AED'000**	**Stage 3 Lifetime AED'000**	**Total AED'000**	**Stage 1 12-month AED'000**	**Stage 2 Lifetime AED'000**	**Stage 3 Lifetime AED'000**	**Total AED'000**
Grading 1	**39,195**	**5,496**	**-**	**44,691**	124,372	20,927	-	145,299
Grading 2	**970,115**	**72,591**	**-**	**1,042,706**	1,052,324	55,436	-	1,107,760
Grading 3	**-**	**58,064**	**-**	**58,064**	1,263	50,140	-	51,403
Grading 4	**-**	**-**	**-**	**-**	-	-	-	-
Grading 5	**-**	**-**	**92,268**	**92,268**	-	-	60,130	60,130
	1,009,310	**136,151**	**92,268**	**1,237,729**	1,177,959	126,503	60,130	1,364,592
Loss allowance	**(8,826)**	**(5,874)**	**(30,298)**	**(44,998)**	(7,984)	(6,716)	(23,067)	(37,767)
Carrying amount	**1,000,484**	**130,277**	**61,970**	**1,192,731**	1,169,975	119,787	37,063	1,326,825

18 Risk management (continued)

(a) *Credit risk management* (continued)

Collateral and other credit enhancements

Collateral against financial assets measured at amortised cost is generally held in the form of mortgage interests over vehicles and real estate properties. Estimates of fair value are based on the value of the collateral assessed at the time of financing.

The Company closely monitors collateral held for financial assets considered to be credit impaired, as it becomes more likely that the Company will take possession of the collateral to mitigate potential credit losses. The Company holds collateral against its Islamic financing products, the fair value of which as at 31 December 2019 is AED 1,113 million (2018: AED 1,125 million).

18 Risk management (continued)

(a) Credit risk management (continued)

Gross carrying amount

The following table further explains the changes in the gross carrying amount from 1 January to 31 December 2019:

	2019				**2018**			
	Stage 1 12-month AED'000	**Stage 2 Lifetime AED'000**	**Stage 3 Lifetime AED'000**	**Total AED'000**	**Stage 1 12-month AED'000**	**Stage 2 Lifetime AED'000**	**Stage 3 Lifetime AED'000**	**Total AED'000**
Cash and cash equivalents								
Gross carrying amount as at 1 January	**1,267**	**-**	**-**	**1,267**	1,258	-	-	1,258
New financial assets originated	**-**	**-**	**-**	**-**	9	-	-	9
Gross carrying amount as at 31 December	**1,267**	**-**	**-**	**1,267**	**1,267**	**-**	**-**	**1,267**

18 Risk management (continued)

(a) Credit risk management (continued)

Gross carrying amount (continued)

	2019				**2018**			
Islamic financing products measured at amortised cost	**Stage 1 12-month AED'000**	**Stage 2 Lifetime AED'000**	**Stage 3 Lifetime AED'000**	**Total AED'000**	**Stage 1 12-month AED'000**	**Stage 2 Lifetime AED'000**	**Stage 3 Lifetime AED'000**	**Total AED'000**
Gross carrying amount as at 1 January	**1,177,959**	**126,503**	**60,130**	**1,364,592**	1,674,928	61,058	49,217	1,785,203
Transfers								
Transfer from Stage 1 to Stage 2	**(99,016)**	**99,016**	**-**	**-**	(116,484)	116,484	-	-
Transfer from Stage 1 to Stage 3	**(25,795)**	**-**	**25,795**	**-**	(11,988)	-	11,988	-
Transfer from Stage 2 to Stage 1	**15,519**	**(15,519)**	**-**	**-**	-	-	-	-
Transfer from Stage 2 to Stage 3	**-**	**(19,781)**	**19,781**	**-**	-	(6,105)	6,105	-
Transfer from Stage 3 to Stage 2	**-**	**-**	**-**	**-**	-	8,087	(8,087)	-
New financial assets originated	**153,501**	**286**	**-**	**153,787**	103,983	714	-	104,697
Repayments and other movements	**(212,858)**	**(54,354)**	**(13,438)**	**(280,650)**	(472,480)	(53,735)	907	(525,308)
Gross carrying amount as at 31 December	**1,009,310**	**136,151**	**92,268**	**1,237,729**	1,177,959	126,503	60,130	1,364,592

18 Risk management (continued)

(a) Credit risk management (continued)

Loss allowance

The following table explain the changes in the loss allowance from 1 January 2019 to 31 December 2019:

	2019				2018			
	Stage 1 12-month ECL AED'000	**Stage 2 Lifetime ECL AED'000**	**Stage 3 Lifetime ECL AED'000**	**Total AED'000**	**Stage 1 12-month ECL AED'000**	**Stage 2 Lifetime ECL AED'000**	**Stage 3 Lifetime ECL AED'000**	**Total AED'000**
Islamic financing products measured at amortised cost								
Loss allowance as at 1 January	**7,984**	**6,716**	**23,067**	**37,767**	15,480	9,220	19,788	44,488
Transfers								
Transfer from Stage 1 to Stage 2	**(822)**	**822**	**-**	**-**	(937)	937	-	-
Transfer from Stage 1 to Stage 3	**(97)**	**-**	**97**	**-**	(428)	-	428	-
Transfer from Stage 2 to Stage 1	**99**	**(99)**	**-**	**-**	-	-	-	-
Transfer from Stage 2 to Stage 3	**-**	**(1,284)**	**1,284**	**-**	-	(844)	844	-
Transfer from Stage 3 to Stage 2	**-**	**-**	**-**	**-**	-	437	(437)	-
New financial assets originated	**36**	**9**	**-**	**45**	111	109	-	220
Changes in PDs/LGDs/EADs	**1,626**	**(290)**	**5,850**	**7,186**	(6,242)	(3,143)	2,444	(6,941)
Loss allowance as at 31 December	**8,826**	**5,874**	**30,298**	**44,998**	7,984	6,716	23,067	37,767

18 Risk management (continued)

(a) Credit risk management (continued)

Write-off policy

The Company writes off financial assets, in whole or in part, when it has exhausted all practical recovery efforts and has concluded that there is no reasonable expectation of recovery. The Company may write-off financial assets that are still subject to enforcement activity. The Company still seeks to recover amounts it is legally owned in full, but which have been partially or fully written off due to no reasonable expectation of recovery.

However, as per Central Bank of the UAE guidelines, retail financing is written off at a maximum of 180 days past their due date, based on the characteristics of the underlying product. The write off amount includes the unpaid profit accrued to the facility till the date of write off and the principal outstanding. Profit accrual on retail facility stops on the date of write off. The only exception to this is high risk mortgage financings to individuals where the financing amount is written off at 180 days or is fully provided for net of collateral. For all other cases of mortgage defaults, the Company provides for the full amount of negative equity at 180 days.

(b) Liquidity risk management

Liquidity Risk is the risk that the Company will be unable to meet a financial commitment to a customer, creditor, or investor when due.

The Company's approach to managing liquidity is to ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the Company's reputation.

While the Company is subject to a liquidity limit imposed by its local regulator, the Company is responsible for managing its overall liquidity within the regulatory limit in co-ordination with parent company's Central Treasury, who monitors compliance with local regulatory limits on a daily basis.

The following table summarizes the maturity profile of Company'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:

18 Risk management (continued)

(b) Liquidity risk management (continued)

The following table summarises the maturity profile of Company'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.

Maturity profile:

The maturity profile of assets, liabilities and equity as at 31 December 2019 were as follows:

	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
Assets						
Cash and cash equivalents	1,267	-	-	-	-	1,267
Islamic financing products measured at amortised cost	56,913	23,352	46,370	253,667	812,429	1,192,731
Other assets	-	-	-	72,935	-	72,935
Total assets	58,180	23,352	46,370	326,602	812,429	1,266,933
Liabilities and equity						
Due to Parent Company	495,177	-	-	-	-	495,177
Other liabilities	2,878	-	-	-	-	2,878
Equity	-	-	-	-	768,878	768,878
Total liabilities and equity	498,055	-	-	-	768,878	1,266,933

18 Risk management (continued)

(b) Liquidity risk management (continued)

Maturity profile:

The maturity profile of assets, liabilities and equity as at 31 December 2018 were as follows:

	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
Assets						
Cash and cash equivalents	1,267	-	-	-	-	1,267
Islamic financing products measured at amortised cost	84,317	39,855	68,735	301,987	831,931	1,326,825
Other assets	-	-	26	-	-	26
Property and equipment	-	-	-	-	211,224	211,224
Total assets	85,584	39,855	68,761	301,987	1,043,155	1,539,342
Liabilities and equity						
Due to Parent Company	661,522	-	-	-	-	661,522
Other liabilities	3,781	-	-	-	-	3,781
Equity	-	-	-	-	874,039	874,039
Total liabilities and equity	665,303	-	-	-	874,039	1,539,342

18 Risk management (continued)

(c) Market risk management

Market risk is the risk that the Company's position will be adversely affected by changes in the levels or volatilities of market factors such as profit rates, currency rates and equity prices. The Company is not exposed to significant market risk, as the Company does not undertake any major trading and non-trading activities.

Currency risk

The majority of the Company's assets and liabilities are denominated in Arab Emirates Dirhams (AED) and accordingly the Company's exposure to the currency risk is very limited. Some current accounts held at banks are denominated in U.S. Dollars to which AED is pegged and accordingly currency risk is limited on U.S. Dollar currency exposures.

Rate of return risk

Profit rate risk, comprising market and valuation risks, are managed on the basis of pre-determined asset allocations across various asset categories, a continuous appraisal of market conditions and trends and management's estimate of long and short term changes in fair value. Overall pricing or rate of return risk positions are managed by the Company's assets and liabilities committee.

The Company is not significantly exposed to risk in terms of the re-pricing of its assets and liabilities since majority are at fixed profit rates.

Fair value of financial instruments

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date, regardless of whether that price is directly observable or estimated using another valuation technique. In estimating the fair value of an asset or a liability, the Company takes into account the characteristics of the asset or liability if market participants would take those characteristics into account when pricing the asset or liability at the measurement date.

In addition, for financial reporting purposes, fair value measurements are categorised into Level 1, 2 or 3 based on the degree to which the inputs to the fair value measurements are observable and the significance of the inputs to the fair value measurement in its entirety, which are described as follows:

- Level 1 inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities that the entity can access at the measurement date;

- Level 2 inputs are inputs, other than quoted prices included within Level 1, that are observable for the asset or liability, either directly or indirectly; and

- Level 3 inputs are unobservable inputs for the asset or liability.

18 Risk management (continued)

(c) Market risk management (continued)

Fair value of financial instruments (continued)

During the year ended 31 December 2019 and 2018, the Company has no financial assets that are measured at fair value.

(d) 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 the Company's business 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 Company, including reputational harm. Operational risk inherent in the Company's business and support activities also include "Shari'ah Non-Compliance Risk", due to mishandling of an Islamic financing transaction/documentation leading to non-compliance with Shari'ah rules and principles. The Shari'ah non-compliance in a transaction may also lead to revenue loss, as the income earned on the effected transactions may need to be created to Charity.

To monitor and control operational risk, the Parent Company 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 Company's financial strength, business characteristics, competitive environment and regulatory environment of the market in which the Company operates. Notwithstanding these control measures, the Company incurs operational losses.

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

The Parent Company's operational risk framework is supported by an operational risk software tool customised to meet the specific framework requirements of its entities. 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.

18 Risk management (continued)

(d) Operational risk management (continued)

Operational risk monitoring

The Parent Company has a process for monitoring operational risk-event data, permitting analysis of errors and losses as well as trends. Such analysis is performed at business level and at each product and risk type level. The risk management framework of the parent entity also takes care of Shari'ah compliance through staff trainings, compliance reviews and Shari'ah audits in addition to periodic risk and compliance self-assessments.

19 Calculation of Zakah

The ultimate responsibility to pay Zakah rests with the shareholders of the Company.

20 Classification of financial assets and liabilities

The table below sets out the Company's classification of each class of financial assets and liabilities and their carrying amounts as at 31 December 2019:

	Amortised cost AED'000	Carrying amount AED'000
Financial assets		
Cash and cash equivalents	**1,267**	**1,267**
Islamic financing products measured at amortised cost	**1,192,731**	**1,192,731**
	1,193,998	**1,193,998**

	Amortised cost AED'000	Carrying amount AED'000
Financial liabilities		
Due to Parent Company	**495,177**	**495,177**
Other liabilities	**1,835**	**1,835**
	497,012	**497,012**

21 Classification of financial assets and liabilities (continued)

The table below sets out the Company's classification of each class of financial assets and liabilities and their carrying amounts as at 31 December 2018:

	Amortised cost AED'000	Carrying amount AED'000
Financial assets		
Cash and cash equivalents	1,267	1,267
Islamic financing products measured at amortised cost	1,326,825	1,326,825
	1,328,092	1,328,092

	Amortised cost AED'000	Carrying amount AED'000
Financial liabilities		
Due to Parent Company	661,522	661,522
Other liabilities	2,866	2,866
	664,388	664,388

The management considers that the carrying amounts of financial assets and financial liabilities measured at amortised cost in the financial statements approximate their fair values.

22 Investment in equity instruments

During the year ended 31 December 2019 and 2018, the Company neither purchased nor disposed any of the equity shares. Further, as at 31 December 2019, the Company does not hold any equity shares.

23 Subsequent events

The existence of novel coronavirus (Covid-19) was confirmed in early 2020 and has spread across mainland China and beyond, causing disruptions to businesses and economic activity. The Company considers this outbreak to be a non-adjusting post balance sheet event. As the situation is fluid and rapidly evolving, we do not consider it practicable to provide a quantitative estimate of the potential impact of this outbreak on the Company. The impact of this outbreak on the macroeconomic factors will be considered in 2020.

24 Approval of financial statements

The financial statements for the year ended 31 December 2019 were approved by the Board of Directors and authorized for issue on 29 March 2020.