CAPITAL intelligence

BANK RATING

United Arab Bank

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Bank Rating Report

United Arab Bank

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UNITED ARAB BANK

Sharjah, United Arab Emirates
28 July 2017

RATINGS

	Current	Last Changed From	Date
Sovereign			
Long-Term:	**AA-**	-	-
Short-Term:	**A1+**	-	-
Outlook	**Stable**	-	-
Foreign Currency			
Long-Term:	**BBB**	BBB+	Jun 17
Short-Term:	**A2**	A3	Jul 16
Financial Strength	**BBB**	BBB+	Jun 17
Support	**3**	-	-
Outlook			
Foreign Currency	**Stable**	Negative	Jun 17
Financial Strength	**Stable**	Negative	Jun 17

FINANCIAL HIGHLIGHTS

USD (mn) / AED (mn)	2016 USD	2016 AED	2015 AED	2014 AED
Total Assets	5,787	21,252	23,664	25,709
Net Loans	3,634	13,346	15,672	17,941
Customer Deposits	4,231	15,538	16,775	18,718
Total Capital	568	2,087	2,570	2,912
Gross Income	235	861	1,196	1,373
Net Profit	-142	-523	-183	605
Exchange Rate (units per USD)		*3.6725*	*3.6725*	*3.6725*

%	2016	2015	2014
NPL / Gross Loans	7.26	4.95	2.93
Loan loss Reserves /NPLs	95.05	100.28	97.10
Capital Adequacy Ratio	13.10	14.60	14.70
Net Loans / Stable Funds	70.56	74.21	78.12
Estimated Net Interest Margin	2.82	4.00	4.27
Cost / Income	43.26	41.08	28.67
ROAA	-2.33	-0.74	2.56

RATINGS DRIVERS

Supporting the Rating

- Good and improving loan-based liquidity ratios; high quasi-liquid asset ratio.
- More than full coverage for impaired loans and a substantial fall in past due advances in Q1 2017. However, one corporate default in the core portfolio pushed up the non-performing loan (NPL) ratio last year.
- Strategic shareholder, The Commercial Bank Q.S.C. (Cb) holds 40% of shares.

Constraining the Rating

- Capital ratios declined and remain lower than the peer group average.
- Margins and operating profitability have been adversely impacted by reduced loan volumes, a higher proportion of corporate credit in the loan mix (in line with new strategies), and increased low-yielding investments. High provision charges have led to net losses for two consecutive years.
- Challenging operating environment due to slow economic growth; rising funding costs have strained margins across the banking sector.
- In common with peers, customer concentrations in the deposit base and loans remain high; relatively small balance sheet.

RATING RATIONALE

Capital Intelligence Ratings (CI Ratings or CI) has reduced the Financial Strength Rating (FSR) of United Arab Bank (UAB) to ±BBBqfrom ±BBB+q The Bankφ capital ratios have weakened and remain lower than those of banks with similar ratings. In addition, UABφ key profitability ratios declined in 2016 and Q1 2017 and there is a strong likelihood that these ratios will remain weak until the Bank is able to build its core businesses. UABφ lower profitability and capital ratios make it more vulnerable to external shocks. Other factors constraining the rating are the challenging operating environment and

the resultant elevated credit risks in certain sectors, rising funding costs that continue to strain margins in the banking sector and UABqs high, though improving, customer concentration levels in loans and deposits.

If the current state of strained relations between the UAE and Qatar sovereigns persists over an extended period of time, this could have an impact on the ability of the principal shareholder to extend capital and business support. Cbqs joint participation in business deals in the UAE, which partly underpins UABqs corporate banking business strategy could become difficult. UAB may not be able to borrow from its largest shareholder in case of need, if restrictions are placed on interbank dealings between the two countries or because of possible liquidity pressures in the Qatari banking sector.

For the same reasons that the FSR was reduced, UABqs Long-Term Foreign Currency Rating (FCR) is also adjusted downwards to ±BBBqfrom ±BBB+q Despite the current strained relations between UAE and Qatar which temporarily restricts the level of assistance that Cb can offer, UABqs Support Rating is maintained at ±3q signifying a high likelihood of support from the federal government in case of need. The Short-Term FCR is maintained at ±A2qin view of the Bankqs overall strong liquidity metrics.

Going forward, CI expects the Bankqs financial fundamentals, particularly the coverage ratio, CAR, and liquidity, to be maintained at their Q1 2017 levels, giving the Bank a moderate buffer in case of exigencies. The Outlook for the ratings is therefore changed to ±Stableqfrom ±Negativeq An increase in capital, would have a favourable impact on the Bankqs prospects and possibly on the ratings. However, any weakening of the CAR and/or deterioration in asset quality and profitability could adversely impact all the ratings.

UAB is in the process of transitioning to a simpler business model, which it believes can deliver sustainable returns while reducing overall risk. In the first phase (which began in late 2015 and accelerated in 2016) the focus was on unwinding legacy issues with the emphasis on reducing risk, bringing down the cost base, ±churningqthe asset portfolio, and managing recoveries. Resolving NPLs and exiting from non-core, stressed assets is more time consuming than was originally believed and this has resulted in a disproportionate drag on income as it tied up capital.

There are challenges in the profitability area. The substantial fall in UABqs non-core, but high-yielding, loan book over the last eighteen months or so (in line with new strategies) has contributed to the decline in profitability. This was partly offset by reduced operating costs on the back of staff lay offs, the closure of branches and the winding down of businesses that are not part of the new strategies. Despite this, operating profit fell in 2016 due to lower gross income levels and a large risk charge led to a net loss, as in the previous year.

There was a small quarter-on-quarter increase in corporate loans in Q1 2017 but loan growth had to be restricted due to the low capital base. The Board is considering all the options available to raise capital. UAB has the UAE regulatorqs approval to issue AT1 securities as well as the option to launch a rights offering of shares. The Bank would be better placed to expand its stock of risk-weighted assets next year after its capital base expands. The Bank is expected to record a small net profit in 2017 in view of the strong likelihood that risk charges would remain lower than before (since the non-core, problematic book is now small). However, operating profitability is likely to continue to decline and ROAA is expected to remain low this year. The Bankqs current weak profitability is a principal constraining factor.

Over the last 18 months UAB contracted its non-core business to a very low level. The quality of the balance sheet has strengthened. Investments in government, public sector, and bank paper now account for nearly a third of the asset base and NPLs, despite rising, continue to be fully provisioned. However, some of these developments have taken a toll on profitability, which weakened in 2016 and again in Q1 2017. Liquidity levels are good and capital ratios are expected to strengthen after the proposed increase in capital later this year.

UABqs strong liquidity ratios support the ratings. Customer deposits and capital continue to be the Bankqs principal resources and short-term interbank liabilities remain low. The Bank has a moderate

amount of medium-term obligations on its balance sheet. Customer concentrations in the deposit base remain high but have fallen in recent periods. Liquid assets and non-government marketable securities together represent a high percentage of the balance sheet. This along with the prudent level of net loans to customer deposits ratio contributed to the decline in the net interest margin (NIM) and operating profitability in 2016 and Q1 2017.

A major factor supporting the rating is managementqs commitment to maintaining a strong coverage ratio on impaired loans. The increase in NPLs last year was due to the classification of one corporate account, which had sizeable unpaid debts to several banks in the country . this contributed to the Bankqs large provision charge in 2016 resulting in a net loss. UAB was nevertheless able to maintain its coverage ratio at a high level. Since UABqs non-core portfolio is now significantly reduced, further impairments are likely to remain low, barring a surprise. The easing of fiscal pressures in recent months has made payment delays by government entities less likely going forward and this would reduce some of the asset quality concerns of the banking sector. UAB reported a significant reduction in past due loans in Q1 2017 suggesting that NPL accretions in the coming quarters are likely to be low.

PERFORMANCE OUTLOOK

The core portfolio has grown quarter-on-quarter since Q3 2016. The easing of government austerity measures in recent months could result in better demand for loans in the second half of the year. The latest economy tracker index shows that Dubai experienced an improvement in business conditions at the beginning of the second quarter . this could translate into opportunities for banks operating in the emirate. The strong growth in UABqs current and savings account (CASA) balances in the first quarter of 2017 is encouraging. Demand balances are likely to rise further as business volumes increase. The banking sector has experienced a steady rise in funding costs, but the growth in CASA balances could help the Bank to rein in its interest expenses. There is further scope for operating costs to be reduced . the Bank is cutting its branch network and staffing levels will also fall. By the end of 2017 the Bank will operate only 14 branches as against the current 21.

The proposed capital increase later this year would support the increase in lending next year . UAB expects its CAR to strengthen substantially after the infusion of capital. The NPL ratio is likely to have peaked. With the non-core portfolio now down to a very small level, NPL accretions are expected to be low from now on unless of course there is an unexpected default . as in 2016 . in the core portfolio. Risk charges are likely to be significantly lower than in the previous year. The Bank expects to report a small net profit in 2017 after making sufficient provisions following the transition to an ±expected lossqmodel under IFRS 9.

Bank History

United Arab Bank (UAB) was incorporated in the emirate of Sharjah in 1975 by leading UAE businessmen and France's Societe Generale (SocGen). For strategic reasons, SocGen sold its 20% stake in early 2005.

Table 1: Major Shareholders (March 2017)	
The Commercial Bank Q.S.C.	40.0%
H E Sheikh Faisal bin Sultan Al Qassimi	8.3%
GIBCA Company Ltd	5.6%
Juma Al Majed Abdullah Muhairi	5.3%

In late 2007 The Commercial Bank Q.S.C. acquired a 34.7% interest in UAB and entered into a strategic alliance with the Bank. Cb raised its holdings to 40% at end-March 2008. Cb, which is the second largest bank in Qatar, is a publicly-held company listed on the Doha Securities Market. It has four representatives on UABqs nine-member board.

Cb is considerably larger than UAB and is a major bank in Qatar with a diversified business base. Many of its key financial ratios weakened in 2016 (see Table 2). There was some deterioration in asset quality and profitability and liquidity remains tight, in common with other Qatari banks. Offsetting this is the Bankqs good capital position and the high CET 1 ratio after the January 2017 rights issue.

CI recently lowered the FSR of Cb to ±BBB+qfrom ±A-qin view of the weaker financial parameters, but the Outlook was changed to ±Stableqfrom ±Negativeq (See CI Ratings Report on The Commercial Bank Q.S.C. dated April 2017).

Cb expanded in the GCC through the acquisition of strategic interests in regional financial institutions (National Bank of Oman, Turkeyqs Alternatifbank and UAB to date). UAB benefits from Cbqs strengths in different business, and although access to Qatari corporates will increase, this is unlikely to make a significant difference given the largely domestic flavour of UABqs corporate business.

Table 2: The Commercial Bank Q.S.C Key Financials	2016	2015
Total Assets (USD billion)	35.8	33.9
Total Capital (USD billion)	5.3	4.2
Net Profit (USDmn)	138	400
ROAA	0.40	1.20
NPLs/Gross Loans (%)	5.24	4.20
LLRs/NPLs (%)	75.48	71.25
Capital Adequacy Ratio (%)	15.19	13.51

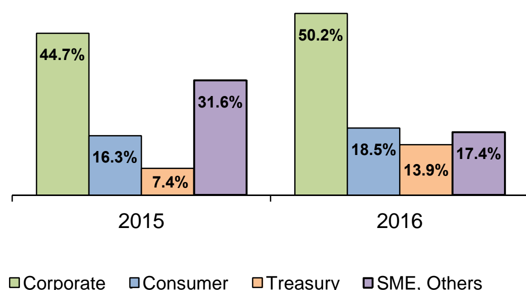
UABqs other shareholders with more than 5% of equity each are UAE businessmen (see Table 1). H.E. Sheikh Faisal Bin Sultan Al Qassimi, a member of the ruling family of Sharjah and an important founder shareholder, continues as chairman of UAB.

Current Business Model

Substantial changes in the business model. The business model changed from the last quarter of 2015, following a substantial increase in bad loans from the SME segment.

Chart 1 shows the relative shares of the corporate, consumer, treasury and other (mainly SME) segments in the Bankqs gross income in 2015 and 2016. The shares of corporate, retail and treasury increased in 2016, while the share of other segments has fallen substantially. However, all segments except treasury reported net losses last year (Corporate . AED246mn, Retail . AED45mn and SME and others . AED310mn) due to impairment provisions.

Chart 1: Gross Income of Major Businesses



The core portfolio is now a significant portion of total loans The Bankqs core business from Q4 2015 onwards has been corporate and institutional banking, which primarily focuses on large and mid-corporate customers in both private and public sectors. The non-core portfolio comprising 1) the SME book, 2) retail loans for self-employment activities, and 3) corporate loans which are not part of the new corporate and institutional banking business, was wound down gradually throughout 2016 and the first quarter of 2017 via repayments and write-offs, and no new loans have been made to any of these segments since the last quarter of 2015. At end Q1 2017, the core portfolio formed a high 96% of total loans.

The branch network continues to be rationalised Retail banking activities now primarily complement the corporate and institutional banking divisions; new growth is to come from the sales of personal and mortgage loans and credit cards to the employees of the Bankqs corporate and institutional customers. The downsizing of retail operations, particularly the closure of eight branches last year and one in Q1 this year, the reduction in headcount and lower marketing and publicity expenses, have generated cost savings for the Bank. The number of branches is expected to reduce by another seven in the last three quarters of this year to 14. However, the core banking platform is being upgraded.

UAB is now primarily a corporate banking institution offering a range of corporate and treasury services to mainly medium-sized and large companies in the UAE. These are chiefly well established companies with multiple sources of revenues and diversified businesses, which have experienced steady growth over several years. State-owned entities and financial institutions are also

major customer segments being targeted. The Bank intends to offer customised services and build strong relationships with target client groups.

Changes in the top management team. The previous CEO left in 2015 after nearly six years at the helm. His replacement and presently Acting CEO, Mr Samer Tamimi, was previously the Deputy CEO of the Bank. Mr Tamimi is an experienced banker, who moved from Arab Bank in Qatar where he was country manager. A number of appointments were made at the senior level in 2015 and 2016 and the top management team is now in place. UAB has a management services agreement with The Commercial Bank Q.S.C. under which fees are paid if certain conditions are met. Risk functions are overseen by the board credit committee (which approves high value credit proposals) as well as by the board audit and risk committees.

Principal Business Strategies

UAB is in the process of transitioning from a corporate/SME and retail business model to essentially a corporate and institutional bank, which is supported by trade finance, retail banking and treasury services. The new organisational structure will see a significant deepening of customer relationships in the corporate sector, while treasury and retail banking growth will essentially be driven by cross selling of key products to the main corporate/institutional segment. The first phase of the transition, which focuses on unwinding the legacy portfolio, is almost at and end. In the second phase the Bank aims to rebuild and deepen customer relationships and expand business volumes. The Bank also aims to grow its core businesses after the injection of new capital.

The deleveraging of the riskier asset portfolio, the upgrading of the core banking platforms and the building of cash management and trade finance offerings are to be completed by end Q4 2017. The Bank will not be paying dividends in the 2017-19 period as it completes its transformation. UAB intends to maintain medium-term borrowings at the end 2016 level and ensure that customer deposits remain the core source of funds. UAB expects to deliver a small net profit this year through continuing cost reductions and some growth in income. The overriding focus is on improving profitability by transitioning to a lower risk business model.

RECENT ECONOMIC AND FINANCIAL SECTOR DEVELOPMENTS

See Appendix at the end of the report.

KEY FINANCIAL ISSUES

The 2016 consolidated accounts, comprising the financial statements of the Bank and its small 100% owned subsidiary (for investments and advisory services), were audited by PWC in accordance with the International Standards on Auditing. The financial statements were prepared in accordance with International Financial Reporting Standards (IFRS) and the requirements under UAE law. The auditor's report is unqualified.

Key Audit Matters highlighted and addressed by the auditor includes the impairment of credit facilities and the AED1 billion of impairment losses incurred by the Bank to establish additional provisions against certain non-core higher risk portfolios that the Bank is in the process of liquidating.

Prior year errors relating to hedge effectiveness and investment property were corrected in the 2016 financial statements. However, these changes had only a small impact on the financial statement. The net profit for 2015 was reduced by AED17mn with a corresponding increase in other comprehensive income. For restatement of the 2014 error, retained earnings were reduced by AED15mn with a corresponding rise in cumulative changes in fair value. An error in the valuation of an investment property included in the financial statements for the year ended 2014 resulted in its overstatement by

AED18mn. This was adjusted against retained earnings as at 1 January 2015 and 1 January 2016. Investment property and retained earnings were reduced by AED18mn each.

Balance sheet disclosures including Pillar III disclosures are good. New accounting standards and interpretations (IFRS 9 and IFRS 15) that were not effective as of end-December 2016 have not been early adopted. The impact of these standards is currently being assessed.

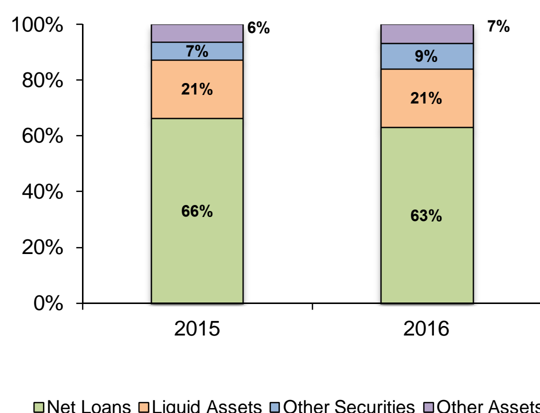
Peer group/sector averages in the following analysis are taken from CI Ratingsqpeer group table. These ratios are the size-weighted averages of 16 banks that accounted for 70% of the total assets in the banking system.

BALANCE SHEET

Asset Quality

Balance sheet totals continued to decline for the second consecutive year in line with strategies emphasising consolidation. Total assets fell by 10% in 2016 to AED21.3 billion due to a substantial 15% fall in loans and advances (reflecting ongoing deleveraging activities) and reduced levels of deposits with banks, which were partly offset by higher investments in marketable securities.

Chart 2: Total Assets Breakdown



The balance sheet structure continued to change; net loans fell to 62.8% of total assets at year end, from 66.2% at end 2015, while marketable securities (other than government paper) rose to 9.3% from 6.5% a year ago. Despite falling, the Bankqs net loans to total assets ratio remains above the peer group average of 59.6% at end 2016.

While the decline in net loans has adversely impacted UABqs net interest margin (NIM) it has had a favourable impact on the Bankqs loan-based liquidity ratios which are now more in line with the peer group average. The bulk of the asset base represents UAE exposures.

Small, but growing, investment portfolio. The Bank built up its high quality liquid asset base last year to meet regulatory ratios. Net investments increased by nearly 30% in 2016 to AED3.3 billion, which amounted to nearly 16% of total assets, up from 11% a year ago. A significant 93% of the portfolio was available-for-sale (AFS) category, and 7% in held-for-trading. Almost the entire portfolio consisted of debt securities at end 2016 and about 40% of that was paper issued by sovereigns. Other debt securities were issued by banks and government-related entities, including well-managed Dubai-government entities with strong operations. Market prices are available for the entire portfolio, which was at Level 1 in the fair value hierarchy. The investment book has no impairments. A little over half of investments consisted of securities rated ±A-q and 22% were rated at ±Aq level internally, while the remainder were mainly in the ±BBBq category or were unrated securities.

Table 3: Sectoral Loan Distribution at end 2016

Sector	AEDmn	% of Total	%Δ over 2015	NPL Ratio* 2016 (%)	NPL Ratio* 2015 (%)
Retail Loans	3,658	25.5	-24.6	**2.09	**3.12
Trade	2,402	16.8	-16.8	10.68	7.33
Personal Loans - Business	1,988	13.9	8.6	**	**
Manufacturing	1,822	12.7	-17.0	3.65	2.82
Services	1,451	10.1	4.3	23.70	6.57
Financial Institutions	1,225	8.5	-10.8	-	-
Construction	772	5.4	-1.4	3.06	10.90
Government/Public Sector	601	4.2	-13.3	-	-
Transport and Communications	396	2.8	-17.8	0.50	0.44
Others	20	0.1	-	-	-
Gross Loans*	14,335	100.0	-13.1	5.76	4.01
Non-Core Portfolio	658	4.59	-62.5	-	-

**as percentage of gross sector loans, NPLs exclude PDNI>90 days; **Retail and Personal Business loans aggregated under Retail loans*

The loan book continued to shrink in 2016 with the ongoing contraction of the non-core portfolio. Gross loans declined by 13% in 2016 to AED14.3 billion with the Bank continuing to reduce its non-core book comprising exposures to SMEs and unsecured personal loans. The non-core portfolio fell to AED658mn at end 2016 or 5% of gross loans from AED1.8 billion (10.6%) a year earlier. Much of the decline took place in the trade and manufacturing sectors and unsecured retail loans.

However, the core book comprising the Bank's target customers also fell, to AED13.7 billion from AED14.7 billion at end 2015, which represented a decline of around 7%. In fact, there were declines across all sectors, except the services sector and personal business loans (see Table 3). Retail loans continued to form the single largest segment at 25.5% of gross loans at end 2016, followed by trade (16.8%), personal business loans (13.9%,) and manufacturing (12.7%). Private sector corporate loans as a group were down by 8%; however, the portfolio represented 70% of gross loans, as against 66% at end 2015.

Moderately high levels of customer concentrations; some increase in 2016. Customer concentrations in the loan portfolio tend to be lower than those of peers given the relatively small average size of UAB's corporate loans. Nevertheless, partly due to the decline in lending, credit outstanding to the 20 largest borrowing customers increased to 31% of gross loans at end 2016, from 22% a year ago. The ten largest borrowing groups accounted for 19% of gross loans, up from 15% at end 2015. The largest exposure was to the government. Only one customer in the top ten had a low internal rating of 8.

Growth in home mortgages has slowed. The book declined in 2015 and 2016 since it is not a core business. Mortgage loans were down by 9% in 2016 and accounted for 13% of gross loans at year end. Only purchases of homes in completed projects in Dubai and Abu Dhabi have been financed.

Other retail loans comprised mainly personal loans against the assignment of salaries and end-of-service benefits. These were offered primarily to employees of government institutions and corporate customers on the Bank's approved list of companies. Impaired loans in the personal loan book (retail and business) fell to 2.09% of gross loans in these two segments at end 2016, from 3.12% of gross a year ago. The Bank also regularly writes off past due retail loans.

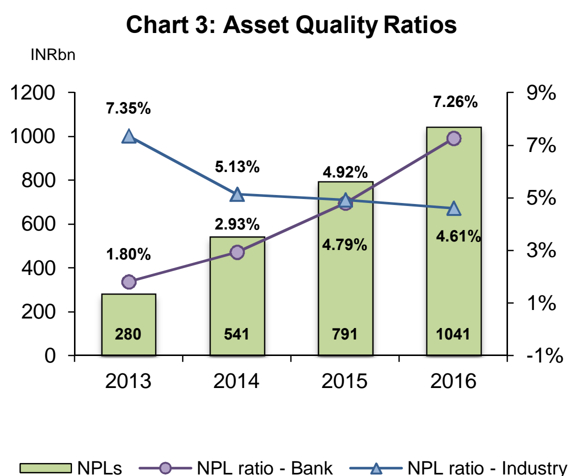
Low real estate exposure. The Bank does not have exposures to real estate developers working on freehold or other properties in Dubai. However, UAB does have indirect exposures via loans secured by real estate and its home mortgage portfolio.

Loan maturities are spread across a wide spectrum. The net loans portfolio is spread more or less evenly across the three major maturity buckets in Table 4. Short-term loans maturing in less than a year represented a third of net loans at end 2016, a little over a third had medium-term tenors and a little less than a third had maturities exceeding five years. The short-term component in the table above is likely to rise with the growth of working capital finance, which is a major part of the Bank's core business.

Table 4: Loans by Maturity (%)

	<1year	1-5 years	>5 years	Total
2016	33	35	32	100
2015	32	40	28	100
2014	38	44	18	100
2013	39	35	25	100

Related-party exposures as a percentage of total capital increased in 2016 but declined in the first quarter of 2017; related party liabilities are also substantial. UAB's related-party loans and investments (AED417mn at end 2016) and off-balance sheet exposures (AED287mn) rose to 34% of total capital, from 27% a year earlier. This was partly because of a decline in total capital last year after the Bank incurred a loss. This is higher than comparable ratios of banks of similar size. However, the related party exposures to total capital ratio fell to a more acceptable 25% at end Q1 2017. There were no impairments in the ratio at end 2016 or at end Q1 2017.



Liabilities from related parties, comprising customer deposits and medium-term borrowings, were also high at AED466mn at end 2016 and AED417mn at end Q1 2017.

Note: CI Ratings' definition of NPLs includes all loans over 90 days past due. UAB has identified certain loans as past due not impaired (PDNI) even though these are more than 90 days overdue. This is either because recovery is imminent or the loans are adequately collateralised or being restructured.

NPLs increased further in 2016 NPLs, including PDNI over 90 days rose by 32% in 2016 to AED1 billion. This was due to:

- A 25% rise in impaired loans on account of default by a mid-sized company. This was an unexpected default of a previously well performing services company and one which took many banks by surprise; impaired loans increased to 5.80% of gross loans, from 4.00% at end 2015. Significant provisions have been made against this impaired loan.
- A 38% rise in PDNI over 90 days loans; these represented 1.50% of gross loans at end 2016, as against 0.94% at end 2015

The NPL ratio (i.e. impaired loans plus PDNI over 90 days) rose to 7.26% at end 2016, above the peer group average of 4.61% (see Chart 3) from 4.95% at end 2015.

The Bank wrote off AED860mn of loans in 2016, up from AED609mn in the previous year. The high write-offs masked the actual NPL accretion rate which is estimated at 140% in 2016 (2015: 159%, 2014: 142%).

PDNI over 90 days loans declined significantly in Q1 2017. Excluding these loans, the NPL ratio was 5.80% at end 2016 (see Table 5), which is closer to the peer group average. Moreover, these loans dropped to just 0.09% of gross loans at end Q1 2017, from 1.50% at end 2016.

Table 5: Asset Quality Excluding PDNI>90 days

	2016	2015
Impaired Loans Ratio (%)	5.80	4.00
Impaired Loans (AEDmn)	825	661
Coverage Ratio (%)	119.83	123.88

The trade sector (SME businesses) and the services sector (a single corporate default) accounted for most of the year-on-year increase in impaired loans. There was a AED45mn increase in impaired loans in the wholesale trade sector but this sector's share of impaired loans was more or less unchanged at 31%. UAB had stopped extending fresh credit to the SME and other sectors, which it considered non-core in 2015 and these additional impairments represent residual problems in the portfolio. The services sector saw a large AED253mn increase in impairments (owing to one major default) and impaired services sector loans amounted to a sizeable 42% of total impairments, as against 14% a year ago. NPLs in the manufacturing sector recorded a small increase. Other sectors saw declines in NPLs. Total retail impairments dropped to AED122mn at end 2016 from AED180mn a year ago. These comprised mainly unsecured personal loans and mortgages . and NPL outstandings in both segments fell last year. There were also reductions in impaired loans in the construction and transport and communications sectors.

The slow growth of the domestic economy had created stresses in the SME segment. A prolonged period of low oil prices and the slow economic activity over the last few years, along with lower levels of liquidity have impacted small businesses in the country resulting in higher impaired loans not just at UAB but across the banking sector. Several expatriate business owners in the commodities trading and small contracting sectors are believed to have fled the country leaving sizeable unpaid debt. The country's inadequate bankruptcy laws, which put issuers of bounced cheques behind bars, had contributed to the problem of fleeing expatriates. These laws have been amended and going forward loans to SMEs may pose less of a risk than they have in the past.

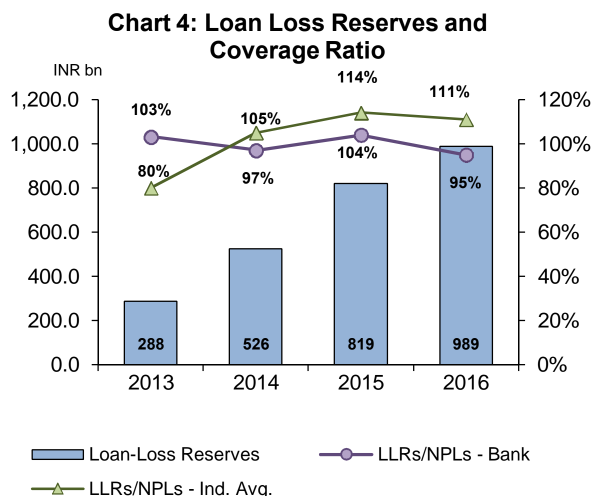
The Bank had maintained strong asset quality in the post 2008 period unlike many other banks in the country. Apart from the current slowdown in the local economy resulting from a prolonged period of low oil prices, the substantial growth in unsecured lending and the seasoning of the portfolio over time have also contributed to the growth in NPLs over the last few years. UAB had fared much better than many of its competitors during the post-2008 financial crisis due to nil exposures to Dubai World and real estate developers in the country as well as very low cross-border loans. This helped the Bank maintain its NPL ratio at a better than the peer group average in the 2008-14 period.

Other overdue loans have declined substantially, although watch listed exposures increased. Past due loans less than 90 days old fell to AED133mn at end 2016, from AED528mn at end 2015. This augurs well for future asset quality. However, loans identified as 'watch listed' (sub-standard), though performing, rose to AED1.7 billion from AED0.7 billion at end 2015. These loans formed a high 12% of gross loans, as against 4% at end 2015. In addition, loans that have been renegotiated but are still categorised as performing increased to 9.9% of gross loans at end 2016 from 4.30% a year earlier. However, collateral and provisions covered 84% of renegotiated loans.

Table 6: Loans Under Varying Degrees of Stress as % of Gross Loans

(% of Gross Loans)	2016	2015
Past Due Not Impaired <90 days	0.93	5.31
Watch listed Loans	11.87	4.05
Renegotiated But Performing	9.90	4.30

High loan loss reserve coverage ratio; capital provides further cover. Apart from writing off a large amount of loans in recent years, the Bank has made sizeable provisions (both specific and general) . the loan loss provisioning expense to gross loans ratio was a high 7.06% in 2016 and 5.38% in 2015. The peer group average of this ratio was a low 1.29% in 2016.



Excluding PDNI over 90 day loans (on which no provisions are made given that recovery is imminent), the Bank's loan loss reserve coverage ratio dropped to 120% at end 2016 from 124% a year earlier. Including PDNI over 90 days loans the coverage ratio was lower but still strong at 95%. That ratio declined from 100% at end 2015 on account of the increase in PDNI over 90 days loans. However, many of these PDNI over 90 days loans were recovered in Q1 2017 and the coverage ratio strengthened to 116%.

In addition, the Bank holds some collateral in the form of cash, securities, properties and letters of guarantee; the fair value of such collateral was AED255mn at end 2016. The Bank states that 51% of the value of corporate exposures is secured by collateral.

Due to the decline in capital last year and the increase in NPLs, the effective NPL coverage ratio (defined as the number of times that capital and loan loss reserves cover NPLs) fell to a low 2.4 times from 3.5 times a year ago. The average for the sector is nearly 6 times. UAB's ratio has fallen steadily over the years from a peak of nearly 16 times at end 2011. The Bank has reasonably good operating profit despite declines in 2015 and 2016 to make further provisions if necessary.

Capital Adequacy

Capital adequacy ratio (CAR) has declined over the years and continued to be well below the peer group average; but the Bank plans to raise new capital. The Bank's Basel II CAR fell to 13.10% at end 2016 from 14.60% at end 2015. This was only slightly above the regulatory minimum of 12% and was well below the peer group average of 19% at end 2016. The Tier 1 ratio also fell last year to 12.2% from 13.9% a year ago. The fall in capital ratios reflects the sizeable 18% decline in regulatory capital last year owing to the large net loss. Risk-weighted assets also recorded a decline – of around 8% – due to the contraction in the loan book. The Bank intends to raise capital and the board is currently examining all options before it which includes an AT1 issuance (for which it has the regulator's approval) and a rights issue of shares.

The Bank's relatively low CAR restricts future asset growth particularly given that tougher Basel III guidelines are being introduced. No dividends have been paid over the last two years; in earlier years the Bank had gradually reduced its cash dividend payment in an effort to plough back its earnings into capital. Shareholders were given bonus shares over this period instead of cash dividends.

The capital to total assets ratio has declined and is below the peer group average. UAB's capital fell by 19% in 2016 to AED2.1 billion owing to the large AED523mn net loss, which was partly offset by a small AED39mn fair value gain in other comprehensive income. Total capital formed 9.8% of total assets at year end, down from 10.9% at end 2015. The peer group average of this ratio was 13.1%. Most of the other banks of similar size had much higher capital to total assets ratios.

Liquidity

Customer deposits fund a large portion of the balance sheet. Customer deposits funded 73% of the UAB's balance sheet at end 2016, up from 71% at end 2015 and capital contributed 10%. This is supplemented by a moderate amount of medium-term borrowings and due from banks of over one year tenor (9% of total assets, excluding the current portion of long-term debt) and short-term interbank liabilities (4%). The Bank had raised medium-term funding in the past to reduce its asset/liability maturity gaps and to widen its sources of funds. Refinancing risks are not significant at present given the moderate size of total borrowings, which are maturing over the next few years. The Bank can refinance or rely partly on internal cash flows to repay these obligations as they mature. UAB also has access to funding from Cb, who is a major shareholder, however, the latter's tight liquidity position may mean that support might not be unquestioned.

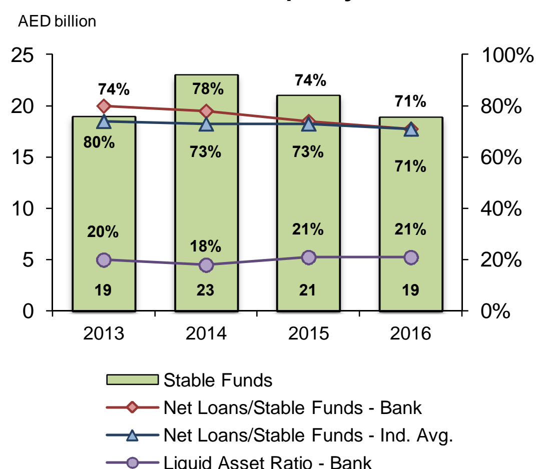
Customer deposits declined in 2015 but since there was a reduction in loans, key liquidity ratios improved. Customer deposits fell by 7% in 2016 to AED15.5 billion; there had been a 10% fall in the previous year as well. The decline over the last two years was more or less in line with the contraction of the loan book. All major deposit categories – demand, savings and time – shrank last year. This primarily reflects the reduction in corporate banking activity and withdrawals by exiting SMEs and other non-core corporate customers. UAB's CASA balances had fallen to 29% of total customer deposits at end 2016, from 41% a year ago, but the strong growth in demand balances in Q1 2017 pushed up CASA to 36% at the end of the first quarter. Time deposits represented 64% of total customer funds at end Q1 2017 as against 71% at end 2016.

Liquidity ratios improved last year. Since net loans contracted at a faster pace than customer deposits, the net loans to customer deposits ratio strengthened to 86% from 93% at end 2015 – this was better than the peer group average of 92%. The net loans to stable funds ratio moved to the peer group average of 71% last year from 74% at end 2015 (see Chart 5).

Customer deposits are largely short-term funds. In common with most of the sector, the bulk of UAB's customer deposits have short-term maturities of less than three months (72% at end 2016) and 95% had maturities of less than a year. All banks in the UAE have wide gaps in the short end of the maturity spectrum due to the high level of short-term deposits on their balance sheets.

Customer concentrations are high, but improved in 2016. The 20 largest depositors accounted for 36% of customer deposits at end 2016 as against 40% a year ago and the ten largest represented 24%, down from 27% at end 2015. Five of the top 20 depositors were GREs.

Liquid asset ratio was good at end 2016; strong quasi-liquid asset ratio. UAB's liquid asset ratio was a stable 21% at end 2016; liquid assets consisted mainly of cash and balances with the Central Bank (62%) and government securities (30%), which were supplemented by a small amount of deposits with banks (8%). In addition, the Bank has investments in other non-government marketable securities (9% of total assets at end 2016), which can be disposed of, or repo'd through a Central Bank window, to create liquidity. Liquid and quasi-liquid assets together formed a high 30% of total assets at year end. The net liquid asset ratio (after reducing short-term interbank liabilities) was also good at 17%.



In addition, the Bank has access to the central bank's liquidity support facility that will allow it to borrow up to 120% of its cash reserves.

Maturity gaps widened in the less-than-three-month bucket. UAB's negative gap in the less-than-three-months maturity bucket represented a high 30% of total assets reflecting its sizeable short-term deposits. The Bank relies on a large portion of its time deposits being rolled over on maturity. Although reduced corporate banking activities led to the contraction of demand balances, historically, the behavioural maturity of demand balances has been more than two years and these have constituted stable funding for many years. Maturity gaps therefore tend to be much smaller than seen in Table 7. In addition, a high percentage of customer deposits with tenors of less than three months is rolled over on maturity. The Bank has tried to address the maturity gap problem by raising medium-term wholesale funding.

Table 7: Assets *Less* Liabilities as a percentage of total assets

%	2016	2015
0-3 months	-30	-25
3-12 months	-10	-11
1-5 years	17	19
Over 5 years	23	17

FINANCIAL PERFORMANCE

Chart 6: Profitability

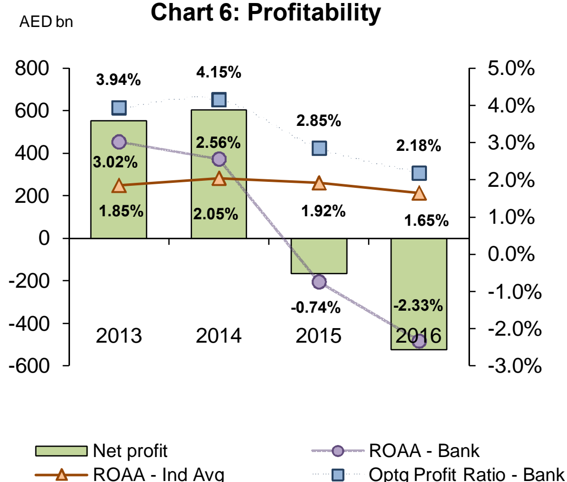
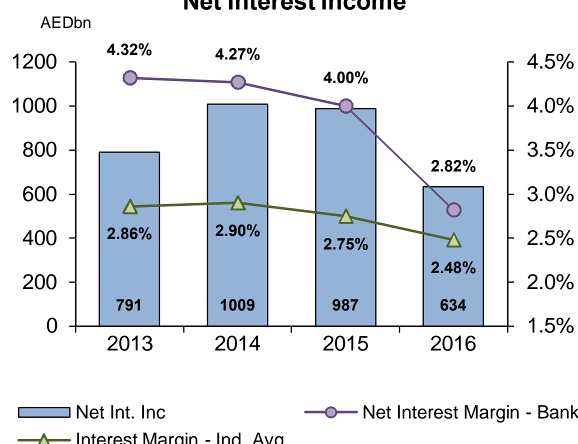


Chart 7: Net Interest Margin and Net Interest Income



Operating profitability continued to drop owing to ongoing balance sheet consolidation, but remains moderately good. UAB's operating profit fell by 31% in 2016 to AED489mn primarily due to a sizeable fall in net interest income, which was partly offset by a 9% increase in non-interest income and a 24% decline in operating costs. The operating profit to average total assets ratio slumped to 2.18% in 2016 from a much higher 2.85% in the previous year; the ratio fell below the peer group average of 2.45% in 2016. The decline in operating profit largely reflects the changes in the Bank's strategies focusing on low-risk corporate accounts and the reduction in exposures to high-yielding, but higher-risk, SME and small business customers. Going forward, UAB's operating cost base is likely to moderate further and its operating profitability ratio is expected to be closer to the level of 2016.

Higher impairments in the credit book led to a 14% increase in provisioning expenses last year. At AED1 billion, the net charge represented a very high 4.50% of average total assets, up from 3.60% a year ago. Impairment charges are expected to taper off as the Bank builds its high-quality business. For the sector as a whole the net charge to average total assets ratio was 1.26% in 2016. UAB reported a net loss of AED522mn in 2016, up from AED183mn in the previous year.

Net interest income declined due to lower credit volumes, a change in the asset mix in favour of higher quality loans and investments and an increase in the funding cost. UAB's net interest income fell by 36% in 2016 to AED634mn, primarily because interest income declined by 22% while

interest costs surged by 35%. The NIM consequently narrowed by a substantial 118 basis points to 2.82%. At this level the Bank's NIM was still higher than the peer group average (see Chart 7).

The decline in interest income is attributed to the contraction in lending volumes last year and a change in the credit mix in favour of corporate banking loans as well as the higher percentage of liquid assets on the balance sheet compared to the previous year. The substantial increase in interest costs was due to the increase in interest rates last year resulting in higher payments on customer deposits and interbank liabilities. The Bank's funding cost rose by 45 basis points to 1.38%, which was above the peer group average of 1.02%. UAB's funding cost has historically been higher than the peer group average but the difference between the two widened in 2016, partly reflecting the higher proportion of time deposits in the customer deposit base compared to two years ago. UAB's demand balances are likely to rise as a percentage of customer funds as the Bank builds its corporate banking activities and introduced cash management and transaction banking products. Indeed, there was a good improvement in CASA balances in Q1 of this year.

Core fee and commission income continued to decline reflecting lower business volumes. Fee and commission income fell by 19% in 2016 to AED84mn; in the previous year there had been a 15% decline in this revenue stream. Foreign exchange trading profits also fell . by 10% to AED68mn. This was offset by an AED46mn increase in miscellaneous income to AED76mn which was mainly due to realised gains on sales of AFS investments and related hedge accounting adjustments. Consequently, non-interest income rose by a moderate 9% to AED228mn and the non-interest income to average total assets ratio moved up to a little over 1.00% from 0.85% a year ago. This was still lower than the peer group average of 1.36%. In the past the Bank's ratio had been higher than the average for the sector.

Operating costs declined in 2016 but the cost to income ratio increased because of the decline in gross income. Operating costs fell by 24% in 2016 to AED373mn due to staff retrenchments and the consolidation of branches and businesses. Staff related costs fell by 20% and other overheads declined by 40%. However, the cost to income ratio moved up to 43% in 2016 from 41% a year ago on account of the substantial 28% fall in gross income.

CURRENT YEAR UPDATE (Q1 2017)

The table below highlights UAB's unaudited financials for the first quarter of 2017.

Note: All ratios on average total assets for interim periods are on annualised basis. Changes in values relating to the interim income statement are over the same period in the previous year unless otherwise specified. Changes in balance sheet figures are over the end 2016 level unless otherwise specified.

AEDmn	**Mar 17**	**Dec 16**	**Δ%**
Total Assets	21,273	21,252	0.1
Impaired Loans	844	825	2.2
PDNI>90 days	13	215	-94.2
Provisions	991	989	0.2
Net Loans	13,384	13,346	0.3
Customer Deposits	15,673	15,538	0.9
Total Capital	2,160	2,087	3.5

%	**Mar 17**	**Dec 16**
NPLs/Gross Loans	5.96	7.26
LLRs/NPLs	115.72	95.05
Capital Adequacy Ratio	13.20	13.10
Net Loans/Stable Funds	72.59	70.56
Liquid Asset Ratio	19.71	20.99
Net Interest Margin	*2.24	2.82
Non-Int. Inc/Average Total Assets	0.97	1.01
Cost To Income	50.70	43.26
Optg. Profit/Average Total Assets	*1.58	2.18
ROAA	*0.52	-2.33

AEDmn	**Q1 17**	**Q1 16**	**Δ%**
Net Interest Income	119	189	-36.7
Non-Interest Income	51	61	-15.1
Gross Income	**171**	**249**	**-31.5**
Operating Expenses	86	90	-3.4
Operating Profit	**84**	**159**	**-47.2**
Provisions	-56	-114	-50.8
Tax	-	-	-
Net Profit	**28**	**45**	**-38.2**

**Annualised*

CAPITAL intelligence

Balance sheet.

Asset quality metrics strengthened owing to lower PDNI over 90 days loans. Strong loan loss reserve coverage ratio and improved effective NPL coverage. Capital ratios improved due to profit retention and balance sheet consolidation. Liquidity metrics continued to be satisfactory.

- The balance sheet total at end Q1 2017 rose marginally over the end 2016 level, with reduced cash and Central Bank balances and due from banks offset by increased investments and other assets. Net loans recorded a marginal rise and accounted for 63% of total assets, with exposures to the core corporate and retail portfolios rising for the second consecutive quarters, while the non-core portfolio declined by 14% over the three months to AED565mn or 4% of net loans. Investments represented 16% of total assets and the portfolio mix was largely unchanged from end 2016.

- The NPLs to gross loans ratio fell to 5.96% at end Q1 2017 from 7.26% at end 2016. The effective NPL coverage ratio at end Q1 2017 improved to 3.7 times from 2.4 times at end 2016. Impaired loans (excluding PDNI over 90 days) rose by 2.2% and accounted for 5.87% of gross loans at end Q1, as against a slightly lower 5.76% at end 2016. There was a sharp decline in PDNI over 90 days to 0.09% of gross loans from 1.50% at end 2016. The coverage ratio remained strong at 116%. The past due not impaired book less than 90 days is low.

- Liquidity ratios were largely stable with customer deposit growth more than matching the increase in net loans. Medium-term liabilities did not change and capital rose by 3.5% owing to the small net profit and AED46mn fair value gains in other comprehensive income. The net loans to customer deposits ratio was 85%, and the net loans to stable funds ratio was 73% . both ratios are at comfortable levels. The liquid asset ratio remained good at 20% and the quasi-liquid asset ratio was also high at 29%.

- There was a slight improvement in the CAR . which rose by 10bps to 13.20% at the end of Q1.

Profit and Loss.

Key profitability ratios continued to decline reflecting reduced business volumes during the period of transition. A fall in the NIM and lower non-interest income led to a contraction in gross income, despite continuing reduction in operating costs, but risk costs halved, indicating a turnaround.

- Reduced average volumes of loans and advances and a change in the loan mix in favour of corporate loans contributed to lower net interest income compared to the corresponding period of the previous year. Also the investment portfolio, which consists mainly of bonds issued by banks, governments and GREs, was larger than in Q1 2016 and contributed to the lower yields.

- In addition, the funding cost continued to rise in line with the general increase in interest rates in the country. These factors led to the substantial year-on-year contraction in the NIM to 2.24% from 3.25% in Q1 2016 (both ratios annualised). The Bank's non-interest income base was also lower than in Q1 2016 and this again reflected reduced business volumes overall. Operating profit was down by 47% and the operating profit on average total assets ratio was a low 1.58% (annualised).

- Operating costs declined by 3% year-on-year in line with strategies to rationalise the branch network and reduced staffing levels. However, this was partly offset by expenditure on hiring new talent, setting up cash management, trade finance and other supporting businesses and the revamping of the IT architecture. The cost to income ratio was a high 51% in Q1 2017 as against 36% in the corresponding period of the previous year owing to reduced gross income.

- **The most noteworthy development is the significant fall in the risk charge to AED56mn, from AED114mn in the same period of the previous year**. This partly includes additional provisioning that would be required under IFRS 9. This was the first time over the last five quarters that the risk charge has fallen well below AED100mn and this was mainly because of the significant decline in the non-core portfolio which now represents just 4% of gross loans.

- The Bank reported a small net profit of AED28mn and a low ROAA of 0.52%.

APPENDIX

RECENT ECONOMIC AND FINANCIAL SECTOR DEVELOPMENTS

GDP growth rate slowed in 2016. UAE's GDP growth rate is projected to have slowed to 2.3% in 2016 (according to the IMF) from a 4% rise seen in the previous year. However, the economy continues to be fairly resilient, compared to neighbouring markets, due to the country's diversified business base, the general ease of doing business and government initiatives which have stressed on diversification and the growth of non-oil sectors. Moreover, financial buffers have allowed fiscal consolidation to proceed more gradually. The non-oil sectors are expected to have grown at around 3.5% in 2016.

The growth rate in 2017 is likely to be largely stable. If oil prices settle at satisfactory levels by the end of 2017 as projected this could reduce the pressure on the government's budget and boost business sentiment in the country. There may not be any significant fiscal stimulus this year but spending cuts are also not likely. As a result of the slight easing of fiscal pressures, government departments are now making more timely payments on their outstanding bills, which is bound to favourably impact bank asset quality. Activities related to the Expo 2020 and other construction projects are expected to pick up. Investment programmes announced by the government in health, education, energy, transport, water, and technology sectors could boost the non-oil sectors of the economy. These developments could provide more lending opportunities for the banks in the country. The IMF has projected a 3.3% rise in non-oil growth in 2017. Abu Dhabi's GDP is expected to rise by 1.7%, while Dubai's economy is expected to grow at 3.6%. For the country as a whole it has projected an increase of 2.5% in 2017.

High rated sovereign. In January 2017 CI affirmed the UAE's Foreign Currency Long-Term Rating at 'AA-' and the Short-Term at 'A1+' in view of the country's satisfactory capacity to weather the prolonged period of decline in hydrocarbon prices while maintaining a sound level of accumulated financial assets. Continued efforts to strengthen the fiscal framework and the likelihood that the oil-rich emirate of Abu Dhabi would be willing to support federal institutions were other factors underpinning the high ratings. The principal constraining factors are the weaknesses in the economic structure and institutions and fiscal shortcomings.

The UAE has undertaken several structural reforms.

1) These include water, electricity and fuel subsidy reforms linking domestic pricing to international prices, which have helped to consolidate fiscal finances.
2) Instead of relying significantly on drawing upon government deposits to manage fiscal needs, in 2016 the Abu Dhabi government improved its financing mix by issuing a USD5 billion Eurobond.
3) A new bankruptcy law was issued in 2016 which has a wider application than the repealed insolvency regime that was in place till then. It decriminalises non-payment of debt within 30 days and bounced cheques. These measures are expected to be particularly helpful for small businesses, and improve the credit environment.
4) A new investment law has been proposed that could allow 100% foreign ownership in certain areas (outside of the free zones) from the current 49%, potentially boosting foreign direct investment.
5) Dubai and Abu Dhabi have stepped up oversight of their respective GREs. The Dubai Supreme Fiscal Council and the Abu Dhabi Debt Management Office closely review debt issuance by their GREs. In addition, bank exposures to GREs are regulated through risk concentration limits set by the Central Bank. However, grants and capital transfers to GREs have been scaled back in the interest of fiscal consolidation.
6) The UAE has also been co-ordinating with other GCC countries to increase taxes through VAT by 2018. Abu Dhabi introduced a 3% tax on expatriate real estate rentals and Dubai is charging transiting airline passengers a fee.

However, fiscal finances continue to be vulnerable to oil price volatility While CI views the government's commitment to fiscal reform as positive, within the current context of a limited non-hydrocarbon tax base and ongoing delay in imposing VAT, public finances would remain relatively

vulnerable to volatility in hydrocarbon prices as the non-hydrocarbon deficit remains high, at 20% of non-hydrocarbon GDP. Moreover, the federal government has announced its intention to keep the fees on foreign businesses unchanged – slowing the efforts for a speedier fiscal consolidation.

That said, it is noted that Abu Dhabi’s fiscal breakeven price for oil is low compared to many other countries and this could help to stretch the period during which fiscal consolidation will be undertaken. Dubai particularly has benefited from the flight of wealth and people from Arab countries affected by popular uprisings. Abu Dhabi’s solid economic fundamentals and the very low levels of social tensions across all seven emirates make for social and political stability in the UAE. Abu Dhabi’s external financial assets, which are held by the Abu Dhabi Investment Authority, are estimated at around a substantial USD770 billion.

Dubai’s trade sector remains resilient. Dubai’s reputation as a trading hub, its location as a convenient transit point for Africa, Asia and Europe and its excellent infrastructure continues to sustain its preeminent position as a major entrepot in the region. Dubai’s non-oil foreign trade slipped only marginally to AED1.28 trillion in 2016 despite the slow down in international markets. The sector’s overall resilience is underpinned by a very diversified foreign trade business, business friendly policies and substantial infrastructure investments by local authorities. Financing trade flows remains an important activity for the banking sector.

The restructurings of the debts of major GREs, which have been an important source of economic development, are now complete and these entities have been making repayments, some of them ahead of maturities. However, the GRE debt is large and rollover risks have risen with increasing USD interest rates and the large fiscal financing needs of the local governments. Dubai’s total public debt (including GRE debt) was a high 126% of Dubai’s GDP in 2015 (according to the IMF). Roughly half of that was GRE debt. Abu Dhabi GRE debt, by contrast, was relatively lower at 27% of total Abu Dhabi GDP. About USD80.5 billion of debt mature in the 2016-2019 period, of which the IMF estimates that USD51.6 billion is debt owed by Dubai GREs. Loans to GREs are reported to have increased by 6% in the first half of 2016 and accounted for nearly 8% of banking sector assets.

Abu Dhabi Plan 2030 document envisages an ambitious investment in energy and non-oil sectors. Abu Dhabi’s GDP, which represents a little over half of the UAE GDP, is projected to be around AED185 billion in 2016; the hydrocarbon sector accounts for 50% of Abu Dhabi’s economy. Partly to diversify away from the energy sector, the government of Abu Dhabi is spending on infrastructure, tourism, aviation, aerospace, defence industries, education and healthcare services. Some of the projects are in housing, renewable energy, transport, communications, railways and the expansion of the airport. The emirate is setting up new industrial clusters in previously under-developed regions and is investing in major civil projects. Abu Dhabi is also in the process of setting up a new international financial free trade zone to connect the economies in the Middle East, Africa and South Asia with world markets.

Challenging 2016 for the banking sector. The banking sector had to contend with the impact of fiscal consolidation and reduced confidence on the back of lower oil prices and a strong US dollar, which affected non-oil private sector businesses. Demand for loans from both the corporate and retail sectors declined last year and the economic slowdown and job losses contributed to higher impairments in the SME and retail portfolios. The banking sector’s total assets rose by 5.4% in 2016 to AED2.6 trillion, while gross credit expanded by 6% to AED1.6 trillion. The major driver of growth last year was lending to the private sector of which a sizeable portion represented credit to businesses and industrial establishments. Funding pressures eased in 2016 with deposits in the banking sector rising by 6% to AED1.6 trillion; much of the increase is attributed to private sector deposit growth. The banking sector remained well capitalised with an average capital adequacy ratio of 19.0% and a Tier 1 ratio of 17.3% (Source: UAE Central Bank).

Stable business growth and asset quality metrics expected in 2017. Credit grew at a slow 1.2% in the first three months of 2017 but could pick up in the second half of the year. Bank managements are exercising more caution given the slower economic growth. Demand from the corporate sector has fallen slightly. Banks have tightened their credit underwriting standards and retail loans

particularly may grow at a much slower rate than in the past. Retail delinquencies have slowed but are likely to stay at an elevated level given the continuing job losses in many sectors (energy, real estate, construction, banks, some SMEs to name a few). On the SME front, the situation appears to have eased somewhat with the UAE Banks Federation taking steps to encourage SME owners to return and settle their debts. The few cases of SME owners leaving the country in recent quarters have been attributed to frauds. The real estate sector, which is better regulated now, has matured and prices are less volatile. That said, average house prices fell slightly in 2016**.** No major corporate account has defaulted thus far and banks generally report that that side of the business remains sound. In the opinion of CI, asset quality metrics in the banking sector are likely to remain stable.

Liquidity ratios are likely to improve further in 2017. The net loans to customer deposits ratio strengthened to 92% in 2016 from 95% a year ago owing to good deposit growth. With capital rising by 6% and several banks borrowing under their EMTN programmes the net loans to stable funds ratio improved to 71% from 72% at end 2015. The liquid asset ratio improved to 26% from 24% a year ago and the net liquid asset ratio rose to 16% from 15%. (Source: CIqs peer group ratios). CI expects the sectorqs overall liquidity ratios to improve slightly. There is no dearth of funding in the sector with both government and private sector deposits continuing to rise, while risk appetites remain muted. The implementation of Basel III liquidity norms has led to higher levels of liquid assets across many banks. Several banks have plans to raise medium-term funds during the year partly to refinance maturing borrowings. This should not be a problem given that total volumes are fairly low in the international context and there is considerable interest among investors for UAE paper.

Profitability ratios slipped in 2016 but could remain stable in 2017, if asset quality metrics hold. The peer group average of the ROAA fell to 1.65% in 2017 from 1.94% in 2015, reflecting lower operating profitability (2.45% as against 2.72% in 2015) on the back of reduced margins as a result of rising funding costs as well as higher provisioning expenses on account of SME and retail delinquencies. (Source: CIqs peer group ratios). CI projects key profitability ratios to remain stable this year. The sectorqs net interest margin remains on its downward trend due to rising funding costs, which is partly driven by higher USD rates. Banks may not be able to pass on the rate increase immediately to their top-rated corporate customers given the tough competition in the market. Interest rates on retail credit are expected to rise but volume growth in this segment is not likely to be significant this year. Falling margins could be compensated by lower operating costs as banks strive to reduce their sales-related expenses in view of the subdued growth in their retail business. Risk charges are also likely to fall as CI expects lower NPL accretions than in 2016 and 2015 but there may be some growth in provisions related to the implementation of IFRS 9.

Banking sector reforms; Basel III capital standards. Some liquidity requirements (liquidity coverage ratio and liquid asset ratio) were imposed from 2016 on the larger banks. The net stable funding ratio will become effective from 1 January 2018 for the larger banks; this ensures that long term assets on the banksqbalance sheet are funded using a sufficient amount of stable liabilities and it also requires some stable funding to cover a portion of the contingent liabilities. All banks are required to report their NPLs, loan loss reserves, and overdue and rescheduled loans on a daily basis to the central bank. A draft regulation to phase in Basel III capital standards was introduced in Q1 this year. The Central Bank has proposed a Basel III minimum CAR of 13%, a Tier 1 ratio of 11.5% and a CET1 ratio of 10% by 2019, including the capital conservation buffer. In addition the Central Bank may insist on a counter-cyclical buffer varying from 0% to 2.5%. The minimum leverage ratio is 3%.

New central bank law under preparation. The Central Bank ensures that credit risks are well provided for before allowing banks to distribute their profits. A new central bank and banking law is under preparation, which is expected to set up a sound institutional framework for financial stability oversight and address shortcomings of safety nets and resolution frameworks.

A discount window provides overnight funding for the banking sector. The UAE central bank has a discount window, known as the Interim Marginal Lending Facility, which offers all the banks operating in the country overnight liquidity against a wide range of collateral; this includes securities and a wide range of sukuk issued by federal and local governments and their respective GREs, as well as top-tier banks, financial institutions and corporations. For Islamic banks, there is a Collateralised Murabaha Facility.

UNITED ARAB BANK

AE020

PERFORMANCE RATIOS	Audited	AUD 12/2016	AUD 12/2015	AUD 12/2014	AUD 12/2013
A . SIZE FACTORS (USD 000)					
1 . Total Assets		5,786,670	6,443,464	7,000,486	5,867,871
2 . Total Capital		568,201	699,784	792,828	675,706
3 . Net Profit		-142,326	-49,856	164,849	150,437
B . ASSET QUALITY					
4 . Total Assets Growth Rate (YoY%)		-10.19	-7.96	19.30	43.54
5 . Estimated Non-Peforming Loans (NPLs) Net Accretion Rate (%)		132.65	163.45	142.32	94.04
6 . NPL Ratio (%)		7.26	4.95	2.93	1.80
7 NPAs (Including NPLs) To Total Assets (%)		4.90	3.45	2.11	1.30
8 . Loan-Loss Reserve To NPLs (%)		95.05	100.28	97.10	102.87
9 . Loan-Loss Reserve To Gross Loans (%)		6.90	4.97	2.85	1.85
10 . Unprovided Non-Performing Loans To Free Capital (%)		3.43		0.63	
11 . Effective NPL Coverage Ratio (Times)		2.39	3.43	5.59	9.14
12 . Unprovided NPLs To Operating Profit (Months)		1.27		0.19	
13 . Loan-Loss Provisioning Expense To Gross Loans (%)		7.06	5.38	2.03	1.08
14 . Related Party Exposure To Total Capital (%)		33.77	26.85	29.18	30.52
15 . Total Contingents To Total Assets (%)		29.91	26.50	25.95	27.57
C . CAPITAL ADEQUACY					
16 Reported Common Equity Tier 1 Ratio To Local Standards (%)					
17 . Reported Tier 1 Ratio To Local Standards (%)		12.20	13.90	13.90	15.20
18 . Reported Total Capital Adequacy Ratio To Local Standards (%)		13.10	14.60	14.70	15.90
19 . Internal Capital Generation (%)		-18.80	-7.18	19.17	15.31
20 . Total Capital Growth Rate (YOY %)		-18.80	-11.74	17.33	10.39
21 . Total Capital To Total Assets (%)		9.82	10.86	11.33	11.52
22 . Total Capital To Gross Loans (%)		14.56	15.58	15.77	15.93
23 . Free Capital (AED 000)		1,502,392	1,982,237	2,502,546	2,269,239
24 . Free Capital To Total Capital (%)		72.00	77.13	85.95	91.45
25 . Dividend Payout Ratio (%)		0.00	0.00	18.93	27.05
D . LIQUIDITY					
26 . Stable Funds (AED 000)		18,913,280	21,118,729	22,965,091	18,993,021
27 . Net Loans To Total Assets (%)		62.80	66.23	69.78	70.93
28 . Net Loans To Total Customer Deposits (%)		85.89	93.42	95.85	101.67
29 . Net Loans To Total Deposits (%)		81.95	88.22	90.43	94.97
30 . Net Loans To Stable Funds (%)		70.56	74.21	78.12	80.48
31 . Net Investments To Total Assets (%)		15.59	10.82	9.67	7.50
32 . Liquid Asset Ratio (%)		20.99	20.95	18.25	19.64
33 . Net Liquid Asset Ratio (%)		17.48	16.76	13.88	14.72
34 . Quasi-Liquid Asset Ratio (%)		30.33	27.46	24.23	22.11
35 . Short-Term Funding Coverage Ratio (%)		863.28	656.44	555.13	449.28
36 . Net FX Currency Assets (AED 000)					
37 . FX Deposits Less FX Loans (AED 000)					
38 . Net Interbank Assets (AED 000)		-381,538	-125,660	810,910	787,579
E . PROFITABILITY					
39 . Return on Average Assets (%)		-2.33	-0.74	2.56	3.02
40 . Operating Profit To Average Assets (%)		2.18	2.85	4.15	3.94
41 . Gross Income To Average Assets (%)		3.84	4.85	5.81	5.69
42 . Estimated Funding Cost (%)		1.38	0.93	0.95	0.94
43 . Estimated Interest on Average Total Assets (%)		4.20	4.93	5.22	5.27
44 . Estimated Net Interest Margin (%)		2.82	4.00	4.27	4.32
45 . Non-Interest Income To Gross Income (%)		26.44	17.46	26.49	23.95
46 . Operating Expenses To Gross Income (%)		43.26	41.08	28.67	30.64
47 Operating Expenses To Average Assets (%)		1.66	1.99	1.67	1.74
48 . Operating Profit Growth Rate (YOY %)		-30.64	-28.05	35.86	35.66
49 . Risk Provisioning Expense To Operating Profit (%)		206.95	125.98	38.19	23.37
50 . Return on Average Equity (%)		-22.45	-6.68	22.45	23.36
RATES					
. Exchange Rate (Units per USD)		3.67	3.67	3.67	3.67
. Inflation Rate (%)		1.80	4.10	2.30	1.10
. Benchmark Interest Rate (AED)		1.26	0.87	0.68	0.81

NOTES:

UNITED ARAB BANK

BALANCE SHEET - ASSETS (AED 000) External Audit	12/2016 USD 000	AUD 12/2016	AUD 12/2015	AUD 12/2014	AUD 12/2013	Growth (%) 12/2016	Growth (%) 12/2015	Growth (%) 12/2014	Growth (%) 12/2013	Breakdown (%) 12/2016	Breakdown (%) 12/2015	Breakdown (%) 12/2014	Breakdown (%) 12/2013
CASH & EQUIVALENT ASSETS:													
Cash	29,303	107,616	138,719	124,190	84,367	-22.42	11.70	47.20	30.05	0.51	0.59	0.48	0.39
Central Bank	724,006	2,658,912	2,936,633	1,686,368	1,217,408	-9.46	74.14	38.52	14.07	12.51	12.41	6.56	5.65
Treasury Bills													
Government Securities	362,098	1,329,806	1,017,445	947,643	1,083,065	30.70	7.37	-12.50	134.92	6.26	4.30	3.69	5.03
Reverse Repos													
Other													
TOTAL CASH & EQUIVALENT ASSETS	1,115,407	4,096,334	4,092,797	2,758,201	2,384,840	0.09	48.39	15.66	49.69	19.28	17.30	10.73	11.07
DEPOSITS WITH BANKS:													
Short - Up to 1 Year	99,408	365,076	864,386	1,933,231	1,848,253	-57.76	-55.29	4.60	38.73	1.72	3.65	7.52	8.58
Medium - Over 1 Year													
TOTAL DEPOSITS WITH BANKS	99,408	365,076	864,386	1,933,231	1,848,253	-57.76	-55.29	4.60	38.73	1.72	3.65	7.52	8.58
TOTAL LIQUID ASSETS	1,214,816	4,461,410	4,957,183	4,691,432	4,233,093	-10.00	5.66	10.83	44.70	20.99	20.95	18.25	19.64
OTHER MARKETABLE SECURITIES	540,217	1,983,947	1,541,905	1,538,887	532,352	28.67	0.20	189.07	-39.19	9.34	6.52	5.99	2.47
LOANS AND ADVANCES:													
Short Term	3,903,214	14,334,554	5,286,051	7,089,648	6,142,416	171.18	-25.44	15.42	-0.17	67.45	22.34	27.58	28.50
Medium/Long Term (MLT)			11,204,605	11,376,786	9,431,000	-100.00	-1.51	20.63	92.19		47.35	44.25	43.76
Other													
Leasing and Factoring													
of which : Non-Performing Loans	283,334	1,040,543	816,740	541,239	279,907	27.40	50.90	93.36	55.79	4.90	3.45	2.11	1.30
GROSS LOANS AND ADVANCES	3,903,214	14,334,554	16,490,656	18,466,434	15,573,416	-13.07	-10.70	18.58	40.81	67.45	69.69	71.83	72.27
Loan-Loss Reserve	-269,297	-988,992	-819,025	-525,531	-287,935	20.75	55.85	82.52	61.59	-4.65	-3.46	-2.04	-1.34
NET LOANS AND ADVANCES	3,633,917	13,345,562	15,671,631	17,940,903	15,285,481	-14.84	-12.65	17.37	40.47	62.80	66.23	69.78	70.93
NON-MARKETABLE SECURITIES													
SUBSIDIARIES & AFFILATES													
NET NON-PERFORMING ASSETS (Excluding NPLs)													
FIXED ASSETS	159,108	584,325	587,718	409,115	212,292	-0.58	43.66	92.71	24.06	2.75	2.48	1.59	0.99
OTHER ASSETS	238,611	876,300	905,186	1,128,948	1,286,538	-3.19	-19.82	-12.25	708.89	4.12	3.83	4.39	5.97
TOTAL ASSETS	5,786,670	21,251,544	23,663,623	25,709,285	21,549,756	-10.19	-7.96	19.30	43.54	100.00	100.00	100.00	100.00
CONTINGENT ACCOUNTS:													
Financial Guarantees / SLCs / Acceptances	876,309	3,218,243	3,023,975	3,225,904	2,821,154	6.42	-6.26	14.35	-12.92	15.14	12.78	12.55	13.09
Irrevocable Commitments	739,814	2,716,966	2,784,629	2,667,483	2,586,948	-2.43	4.39	3.11	16.15	12.78	11.77	10.38	12.00
Documentary L/Cs	114,517	420,563	461,358	777,624	533,224	-8.84	-40.67	45.83	-25.94	1.98	1.95	3.02	2.47
Bid / Performance / Retention Bonds													
TOTAL CONTINGENT ACCOUNTS	1,730,639	6,355,772	6,269,962	6,671,011	5,941,326	1.37	-6.01	12.28	-3.97	29.91	26.50	25.95	27.57

BALANCE SHEET - LIABILITIES (AED 000) External Audit	42,733 USD 000	AUD 12/2016	AUD 12/2015	AUD 12/2014	AUD 12/2013	Growth (%) 12/2016	Growth (%) 12/2015	Growth (%) 12/2014	Growth (%) 12/2013	Breakdown (%) 12/2016	Breakdown (%) 12/2015	Breakdown (%) 12/2014	Breakdown (%) 12/2013
SHORT-TERM INTERBANK LIABILITIES:													
ST Placements From Banks	178,300	654,806	670,716	846,914	1,060,674	-2.37	-20.80	-20.15	-12.18	3.08	2.83	3.29	4.92
Current Portion of LT Bank Debt	24,999	91,808	319,330	275,407		-71.25	15.95			0.43	1.35	1.07	
Repos With Banks													
Interbank Liability To Parent / Related Party													
TOTAL SHORT-TERM INTERBANK LIABILITIES	203,299	746,614	990,046	1,122,321	1,060,674	-24.59	-11.79	5.81	-12.18	3.51	4.18	4.37	4.92
CUSTOMER DEPOSITS:													
Demand	1,118,814	4,108,846	4,701,183	7,880,146	6,075,774	-12.60	-40.34	29.70	86.48	19.33	19.87	30.65	28.19
Savings	102,057	374,806	525,040	608,002	722,283	-28.61	-13.65	-15.82	83.28	1.76	2.22	2.36	3.35
Time	3,010,038	11,054,363	11,548,820	10,230,149	8,236,780	-4.28	12.89	24.20	27.86	52.02	48.80	39.79	38.22
Other													
TOTAL CUSTOMER DEPOSITS	4,230,909	15,538,015	16,775,043	18,718,297	15,034,837	-7.37	-10.38	24.50	48.94	73.11	70.89	72.81	69.77
OFFICIAL DEPOSITS													
TOTAL DEPOSITS + ST INTERBANK LIABILITIES	4,434,208	16,284,629	17,765,089	19,840,618	16,095,511	-8.33	-10.46	23.27	42.41	76.63	75.07	77.17	74.69
NON-BANK SHORT-TERM DEBT													
MEDIUM / LONG TERM FUNDING	509,972	1,872,873	2,361,449	1,744,248	1,688,945	-20.69	35.38	3.27	39.96	8.81	9.98	6.78	7.84
SUBORDINATED DEBT													
HYBRID CAPITAL													
OTHER LIABILITIES	274,289	1,007,325	967,130	1,212,758	1,283,769	4.16	-20.25	-5.53	401.59	4.74	4.09	4.72	5.96
TOTAL LIABILITIES	5,218,469	19,164,827	21,093,668	22,797,624	19,068,225	-9.14	-7.47	19.56	49.38	90.18	89.14	88.67	88.48
CAPITAL:													
Paid Up Capital	374,413	1,375,033	1,375,034	1,145,861	996,401	0.00	20.00	15.00		6.47	5.81	4.46	4.62
Reserves	193,787	711,684	1,194,921	1,765,800	1,485,130	-40.44	-32.33	18.90	18.67	3.35	5.05	6.87	6.89
Minority Interest													
TOTAL CAPITAL	568,201	2,086,717	2,569,955	2,911,661	2,481,531	-18.80	-11.74	17.33	10.39	9.82	10.86	11.33	11.52
TOTAL LIABILITIES + TOTAL CAPITAL	5,786,670	21,251,544	23,663,623	25,709,285	21,549,756	-10.19	-7.96	19.30	43.54	100.00	100.00	100.00	100.00
REGULATORY CAPITAL	619,384	2,274,686	2,777,786	3,153,718	2,652,578	-18.11	-11.92	18.89		10.70	11.74	12.27	12.31

PROFIT AND LOSS ACCOUNT (AED 000) External Audit	42,733 USD 000	AUD 42,733	AUD 42,368	AUD 42,003	AUD 41,638	Growth (%) 12/2016	Growth (%) 12/2015	Growth (%) 12/2014	Growth (%) 12/2013	% of Average Total Assets 12/2016	% of Average Total Assets 12/2015	% of Average Total Assets 12/2014	% of Average Total Assets 12/2013
Interest Income	257,042	943,988	1,216,833	1,233,842	962,531	-22.42	-1.38	28.19	33.56	4.20	4.93	5.22	5.27
Interest Expense	-84,514	-310,378	-229,613	-224,453	-171,972	35.17	2.30	30.52	11.93	-1.38	-0.93	-0.95	-0.94
Net Interest Income	172,528	633,610	987,220	1,009,389	790,559	-35.82	-2.20	27.68	39.42	2.82	4.00	4.27	4.32
Net Fees and Commissions	22,837	83,870	103,247	121,074	110,272	-18.77	-14.72	9.80	36.82	0.37	0.42	0.51	0.60
FX Trading Income	18,591	68,275	75,947	87,207	57,627	-10.10	-12.91	51.33	58.98	0.30	0.31	0.37	0.32
Derivatives Income													
Gain / Loss on Securities													
Other Investment Income													
Gains/Loss on Real Estate Held For Investment													
Share of Profits From Associates													
Net Insurance Income													
Other Income	20,589	75,614	29,683	155,510	81,037	154.74	-80.91	91.90	-0.12	0.34	0.12	0.66	0.44
Total Non-Interest Income	62,017	227,759	208,877	363,791	248,936	9.04	-42.58	46.14	25.74	1.01	0.85	1.54	1.36
GROSS INCOME	234,546	861,369	1,196,097	1,373,180	1,039,495	-27.99	-12.90	32.10	35.88	3.84	4.85	5.81	5.69
Operating Expenses	101,464	372,626	491,402	393,697	318,552	-24.17	24.82	23.59	36.36	1.66	1.99	1.67	1.74
OPERATING PROFIT	133,082	488,743	704,695	979,483	720,943	-30.64	-28.05	35.86	35.66	2.18	2.85	4.15	3.94
Total Provisioning Expenses	-275,407	-1,011,434	-887,791	-374,075	-168,464	13.93	137.33	122.05	38.53	-4.50	-3.60	-1.58	-0.92
GROSS PROFIT / (LOSS)	-142,326	-522,691	-183,096	605,408	552,479	185.47	-130.24	9.58	34.81	-2.33	-0.74	2.56	3.02
Extraordinary Items													
Tax & Equivalent													
NET PROFIT (or -LOSS)	-142,326	-522,691	-183,096	605,408	552,479	185.47	-130.24	9.58	34.81	-2.33	-0.74	2.56	3.02
Net Changes in Fair Value	10,743	39,453	-26,024	-15,018	-57,995	-251.60	73.29	-74.10	-373.86	0.18	-0.11	-0.06	-0.32
Net FX Translation Gains				-928	-6,465		-100.00	-85.65				0.00	-0.04
Other													
COMPREHENSIVE INCOME	-131,583	-483,238	-209,120	590,390	493,556	131.08	-135.42	19.62	16.26	-2.15	-0.85	2.50	2.70
Proposed Cash Dividends				114,586	149,460		-100.00	-23.33	-40.00			0.48	0.82

RATIO FORMULAE

Category	Ratio	Formula
A.SIZE FACTORS (USD 000)	1. TOTAL ASSETS	TOTAL ASSETS
	2. TOTAL CAPITAL	TOTAL CAPITAL
	3. NET PROFIT	NET PROFIT
B.ASSET QUALITY	4. TOTAL ASSETS GROWTH RATE (YOY%)	(CURRENT YEAR TOTAL ASSETS – PREVIOUS YEAR TOTAL ASSETS) X 100 PREVIOUS YEAR TOTAL ASSETS
	5. ESTIMATED NON-PEFORMING LOANS (NPLS) NET ACCRETION RATE (%)	(NON-PERFORMING LOANS + WRITEOFFS- NON-PERFORMING LOANS(PREVIOUS YEAR)) X 100 NON-PERFORMING LOANS(PREVIOUS YEAR)
	6. NPL RATIO (%)	NON-PERFORMING LOANS X 100 GROSS LOANS
	7. NPAS (INCLUDING NPLS) TO TOTAL ASSETS (%)	(NON-PERFORMING ASSETS + NON-PERFORMING LOANS) X 100 TOTAL ASSETS
	8. LOAN-LOSS RESERVE TO NPLS (%)	LOAN-LOSS RESERVE X 100 NON-PERFORMING LOANS
	9. LOAN-LOSS RESERVE TO GROSS LOANS (%)	LOAN-LOSS RESERVE X 100 GROSS LOANS
	10. UNPROVIDED NON-PERFORMING LOANS TO FREE CAPITAL (%)	(NON-PERFORMING LOANS - LOAN LOSS RESERVE) X 100 FREE CAPITAL
	11. EFFECTIVE NPL COVERAGE RATIO (TIMES)	(LOAN-LOSS RESERVE + FREE CAPITAL) NPLs
	12. UNPROVIDED NPLS TO OPERATING PROFIT (MONTHS)	(NON-PERFORMING LOANS - LOAN LOSS RESERVE) X 12 OPERATING PROFIT
	13. LOAN-LOSS PROVISIONING EXPENSE TO GROSS LOANS (%)	PROVISIONS FOR LOANS (SPEC + GEN) X 100 GROSS LOANS
	14. RELATED PARTY EXPOSURE TO TOTAL CAPITAL (%)	RELATED-PARTY EXPOSURE (FUNDED + UNFUNDED) X 100 TOTAL CAPITAL
	15. TOTAL CONTINGENTS TO TOTAL ASSETS (%)	(TOTAL CONTINGENT ACCOUNTS) X 100 TOTAL ASSETS
C.CAPITAL ADEQUACY	16. REPORTED COMMON EQUITY TIER 1 RATIO TO LOCAL STANDARDS (%)	AS REPORTED ACCORDING TO LOCAL STANDARDS
	17. REPORTED TIER 1 RATIO TO LOCAL STANDARDS (%)	AS REPORTED ACCORDING TO LOCAL STANDARDS
	18. REPORTED TOTAL CAPITAL ADEQUACY RATIO TO LOCAL STANDARDS (%)	AS REPORTED ACCORDING TO LOCAL STANDARDS
	19. INTERNAL CAPITAL GENERATION (%)	(COMPREHENSIVE INCOME – PROPOSED CASH DIVIDENDS – EXTRAORDINARY ITEMS) X 100 PREVIOUS YEAR TOTAL CAPITAL
	20. TOTAL CAPITAL GROWTH RATE (YOY %)	(CURRENT YEAR TOTAL CAPITAL – PREVIOUS YEAR TOTAL CAPITAL) X 100 PREVIOUS YEAR TOTAL CAPITAL
	21. TOTAL CAPITAL TO TOTAL ASSETS (%)	TOTAL CAPITAL X 100 TOTAL ASSETS
	22. TOTAL CAPITAL TO GROSS LOANS (%)	TOTAL CAPITAL X 100 GROSS LOANS
	23. FREE CAPITAL (AED 000)	TOTAL CAPITAL – SUBSIDIARIES AND AFFILIATES – FIXED ASSETS
	24. FREE CAPITAL TO TOTAL CAPITAL (%)	FREE CAPITAL X 100 TOTAL CAPITAL
	25. DIVIDEND PAYOUT RATIO (%)	PROPOSED CASH DIVIDENDS X 100 NET PROFIT
D.LIQUIDITY	26. STABLE FUNDS (AED 000)	TOTAL CUSTOMER DEPOSITS + MEDIUM & LONG-TERM FUNDING + SUBORDINATED DEBT + HYBRID CAPITAL + FREE CAPITAL
	27. NET LOANS TO TOTAL ASSETS (%)	NET LOANS X 100 TOTAL ASSETS
	28. NET LOANS TO TOTAL CUSTOMER DEPOSITS (%)	NET LOANS X 100 TOTAL CUSTOMER DEPOSITS
	29. NET LOANS TO TOTAL DEPOSITS (%)	NET LOANS X 100 TOTAL CUST. DEP. + OFFICIAL DEP. + ST PLACEMENTS FROM BANKS + INTERBANK DEP. TO PARENT OR RELATED PARTY
	30. NET LOANS TO STABLE FUNDS (%)	NET LOANS X 100 STABLE FUNDS
	31. NET INVESTMENTS TO TOTAL ASSETS (%)	(TREAS BILLS & GOV. SEC. + OTHER MKT SEC. + NON-MKT SEC.) X 100 TOTAL ASSETS
	32. LIQUID ASSET RATIO (%)	TOTAL LIQUID ASSETS X 100 TOTAL ASSETS
	33. NET LIQUID ASSET RATIO (%)	(TOTAL LIQUID ASSETS – TOTAL ST INTERBANK LIABILITIES - NON-BANK ST DEBT) X 100 TOTAL ASSETS
	34. QUASI-LIQUID ASSET RATIO (%)	(TOTAL LIQUID ASSETS + OTHER MARKETABLE SECURITIES) X 100 TOTAL ASSETS
	35. SHORT-TERM FUNDING COVERAGE RATIO (%)	(TOTAL LIQUID ASSETS + OTHER MARKETABLE SECURITIES) X 100 TOTAL ST INTERBANK LIABILITIES + NON-BANK SHORT-TERM DEBT
	36. NET FX CURRENCY ASSETS (AED 000)	FOREIGN CURRENCY ASSETS – FOREIGN CURRENCY LIABILITIES
	37. FX DEPOSITS LESS FX LOANS (AED 000)	FOREIGN CURRENCY LOANS – FOREIGN CURRENCY DEPOSITS
	38. NET INTERBANK ASSETS (AED 000)	TOTAL DEPOSITS WITH BANKS – TOTAL ST INTERBANK LIABILITIES

RATIO FORMULAE

E.PROFITABILITY	39. RETURN ON AVERAGE ASSETS (%)	NET PROFIT X 100 / AVERAGE TOTAL ASSETS
	40. OPERATING PROFIT TO AVERAGE ASSETS (%)	OPERATING PROFIT X 100 / AVERAGE TOTAL ASSETS
	41. GROSS INCOME TO AVERAGE ASSETS (%)	GROSS INCOME X 100 / AVERAGE TOTAL ASSETS
	42. ESTIMATED FUNDING COST (%)	INTEREST EXPENSE X 100 / AVERAGE TOTAL ASSETS
	44.ESTIMATED INTEREST ON AVERAGE TOTAL ASSETS	INTEREST INCOME X 100 / AVERAGE TOTAL ASSETS
	44. ESTIMATED NET INTEREST MARGIN (%)	ESTIMATED INTEREST ON AVERAGE TOTAL ASSETS (%) – ESTIMATED FUNDING COST (%)
	45. NON-INTEREST INCOME TO GROSS INCOME (%)	NON-INTEREST INCOME X 100 / GROSS INCOME
	46. OPERATING EXPENSES TO GROSS INCOME (%)	OPERATING EXPENSES X 100 / GROSS INCOME
	47. OPERATING EXPENSES TO AVERAGE ASSETS (%)	OPERATING EXPENSES X 100 / AVERAGE TOTAL ASSETS
	48. OPERATING PROFIT GROWTH RATE (YOY %)	(CURRENT-YEAR OPERATING PROFIT – PREV-YEAR OPERATING PROFIT) X 100 / PREV-YEAR OPERATING PROFIT
	49. RISK PROVISIONING EXPENSE TO OPERATING PROFIT (%)	TOTAL PROVISONING EXPENSES X 100 / OPERATING PROFIT
	50. RETURN ON AVERAGE EQUITY (%)	NET PROFIT X 100 / AVERAGE TOTAL CAPITAL
F. COUNTRY SPECIFIC RATIOS	. EXCHANGE RATE (UNITS PER USD)	
	. INFLATION RATE (%)	
	. BENCHMARK INTEREST RATE (AED)	

CAPITAL intelligence

RATINGS DEFINITIONS

International Issuer Credit Ratings: Foreign Currency and Local Currency

CI's international issuer credit ratings indicate the general creditworthiness of an entity (such as a bank, corporate or sovereign) and the likelihood that it will meet its financial obligations in a timely manner. Foreign currency ratings refer to an entity's ability and willingness to meet its foreign currency denominated financial obligations as they come due. Foreign currency ratings take into account the likelihood of a government imposing restrictions on the conversion of local currency to foreign currency or on the transfer of foreign currency to residents and non-residents.

Local currency ratings are an opinion of an entity's ability and willingness to meet all of its financial obligations on a timely basis, regardless of the currency in which those obligations are denominated and absent transfer and convertibility restrictions. Both foreign currency and local currency ratings are internationally comparable assessments.

Foreign and local currency ratings take into account the economic, financial and country risks that may affect creditworthiness, as well as the likelihood that an entity would receive external support in the event of financial difficulties.

Ratings assigned to banks and corporates are generally not higher than the ratings assigned by CI to the relevant sovereign government. However, it may be possible for an issuer with particular strengths and attributes such as inherent financial strength, geographically diversified cash flow, substantial foreign assets, and guaranteed external support, to be rated above the sovereign.

CI may assign either a public rating or an internal 'shadow' rating to the sovereign. Shadow sovereign ratings are not intended for publication and are used to ensure that sovereign risk factors are adequately reflected in the ratings of non-sovereign issuers.

The following rating scale applies to both foreign currency and local currency ratings. Short-term ratings assess the time period up to one year.

Long-Term Issuer Ratings

Investment Grade

AAA — The highest credit quality. Exceptional capacity for timely fulfilment of financial obligations and most unlikely to be affected by any foreseeable adversity. Extremely strong financial condition and very positive non-financial factors.

AA — Very high credit quality. Very strong capacity for timely fulfilment of financial obligations. Unlikely to have repayment problems over the long term and unquestioned over the short and medium terms. Adverse changes in business, economic and financial conditions are unlikely to affect the institution significantly.

A — High credit quality. Strong capacity for timely fulfilment of financial obligations. Possesses many favourable credit characteristics but may be slightly vulnerable to adverse changes in business, economic and financial conditions.

BBB — Good credit quality. Satisfactory capacity for timely fulfilment of financial obligations. Acceptable credit characteristics but some vulnerability to adverse changes in business, economic and financial conditions. Medium grade credit characteristics and the lowest investment grade category.

Speculative Grade

BB — Speculative credit quality. Capacity for timely fulfilment of financial obligations is vulnerable to adverse changes in internal or external circumstances. Financial and/or non-financial factors do not provide significant safeguard and the possibility of investment risk may develop.

B Significant credit risk. Capacity for timely fulfilment of financial obligations is very vulnerable to adverse changes in internal or external circumstances. Financial and/or non-financial factors provide weak protection; high probability for investment risk exists.

C Substantial credit risk is apparent and the likelihood of default is high. Considerable uncertainty as to the timely repayment of financial obligations. Credit is of poor standing with financial and/or non-financial factors providing little protection.

RS Regulatory supervision (this rating is assigned to financial institutions only). The obligor is under the regulatory supervision of the authorities due to its weak financial condition. The likelihood of default is extremely high without continued external support.

SD Selective default. The obligor has failed to service one or more financial obligations but CI believes that the default will be restricted in scope and that the obligor will continue honouring other financial commitments in a timely manner.

D The obligor has defaulted on all, or nearly all, of its financial obligations.

Short-Term Issuer Ratings

Investment Grade

A1 Superior credit quality. Highest capacity for timely repayment of short-term financial obligations that is extremely unlikely to be affected by unexpected adversities. Institutions with a particularly strong credit profile have a "+" affixed to the rating.

A2 Very strong capacity for timely repayment but may be affected slightly by unexpected adversities.

A3 Strong capacity for timely repayment that may be affected by unexpected adversities.

Speculative Grade

B Adequate capacity for timely repayment that could be seriously affected by unexpected adversities.

C Inadequate capacity for timely repayment if unexpected adversities are encountered in the short term.

RS Regulatory supervision (this rating is assigned to financial institutions only). The obligor is under the regulatory supervision of the authorities due to its weak financial condition. The likelihood of default is extremely high without continued external support.

SD Selective default. The obligor has failed to service one or more financial obligations but CI believes that the default will be restricted in scope and that the obligor will continue honouring other financial commitments in a timely manner.

D The obligor has defaulted on all, or nearly all, of its financial obligations.

Capital Intelligence appends "+" and "-" signs to foreign and local currency **long term** ratings in the categories from "AA" to "C" to indicate that the strength of a particular rated entity is, respectively, slightly greater or less than that of similarly rated peers.

Outlook – expectations of improvement, no change or deterioration in a bank or corporate rating over the 12 months following its publication are denoted Positive, Stable or Negative. The time horizon for a sovereign rating outlook is longer, at 12-24 months.

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Financial Strength Ratings

CI's financial strength ratings provide an opinion of a bank's inherent financial strength, soundness and risk profile. These ratings do not address sovereign risk factors, including transfer risk, which may affect an institution's capacity to honour its financial obligations, be they local or foreign currency. Financial strength ratings also exclude support factors, which are addressed by foreign and local currency ratings, as well as CI's support ratings. However, financial strength ratings do take into account the bank's operating environment including the economy, the structure, strength and stability of the financial system, the legal system, and the quality of banking regulation and supervision. Financial strength ratings do not assess the likelihood that specific obligations will be repaid in a timely manner.

The following rating scale applies to the financial strength rating.

AAA Financially in extremely strong condition with positive financial trends; significant strengths in other non-financial areas. Operating environment likely to be highly attractive and stable.

AA Financially in very strong condition and significant strengths in other non-financial areas. Operating environment likely to be very attractive and stable.

A Strong financial fundamentals and very favourable non-financial considerations. Operating environment may be unstable but institution's market position and/or financial strength more than compensate.

BBB Basically sound overall; slight weaknesses in financial or other factors could be remedied fairly easily. May be limited by unstable operating environment.

BB One or two significant weaknesses in the bank's financial makeup could cause problems. May be characterised by a limited franchise; other factors may not be sufficient to avoid a need for some degree of temporary external support in cases of extraordinary adversity. Unstable operating environment likely.

B Fundamental weaknesses are present in the bank's financial condition or trends, and other factors are unlikely to provide strong protection from unexpected adversities; in such an event, the need for external support is likely. Bank may be constrained by weak market position and/or volatile operating environment.

C In a very weak financial condition, either with immediate problems or with limited capacity to withstand adversities. May be operating in a highly volatile operating environment.

D Extremely weak financial condition and may be in an untenable position.

Capital Intelligence appends "+" and "-" signs to financial strength ratings in the categories from "AA" to "C" to indicate that the strength of a particular institution is, respectively, slightly greater or less than that of similarly rated peers.

Outlook – expectations of improvement, no change or deterioration in a rating over the 12 months following its publication are denoted Positive, Stable or Negative.

Support Ratings

CI's support ratings assess the likelihood that, in the event of difficulties, a bank would receive sufficient financial assistance from the government or private owners to enable it to continue meeting its financial obligations in a timely manner. Support ratings complement CI's financial strength ratings which, in effect, indicate the likelihood that a bank will fail due to inherent financial weaknesses and/or an unstable operating environment and therefore may require external support to avoid defaulting on its obligations. Neither financial strength ratings nor support ratings take account of transfer and convertibility risks associated with sovereign events. The overall creditworthiness of an institution and default risk is captured by CI's foreign currency ratings. Foreign currency ratings take into account all factors affecting the likelihood of repayment including inherent financial strength, external support, the operating environment, and sovereign-related risks.

Although subjective, support ratings are based on a thorough assessment of a bank's ownership, market position and importance within the sector and economy, as well as the country's regulatory and supervisory framework and the credit standing of potential supporters.

The following rating scale applies to support ratings.

1. The likelihood of a bank receiving support in the event of difficulties is extremely high. The characteristics of a bank with this support rating may include strong government ownership and/or clear legal guarantees on the part of the state. The bank may also be of such importance to the national economy that state intervention is virtually assured. The ability and willingness of potential supporters to provide sufficient and timely support is extremely strong.

2. The likelihood of support is very high. The ability and willingness of potential supporters to provide sufficient and timely support is very strong.

3. The likelihood of support is high. The ability and willingness of potential supporters to provide sufficient and timely support is strong.

4. The likelihood of support is moderate. There is some uncertainty about the ability and willingness of potential supporters to provide sufficient and timely assistance.

5. The likelihood of support is low. There is considerable uncertainty about the ability and willingness of potential supporters to provide sufficient and timely assistance.

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ATTRIBUTES AND LIMITATIONS OF CREDIT RATINGS

Users of Capital Intelligence's (CI) credit ratings should be aware of the following attributes and limitations of the ratings:

- CI's credit ratings are statements of opinion and not statements of fact. They are an independent opinion of the creditworthiness of an entity or obligor either in general (an issuer rating) or with regard to a specific financial obligation (an issue rating).
- CI's credit ratings are intended to provide a relative ranking of credit risk among rated entities and obligations based on fundamental credit analysis and expressed in rating symbols from 'AAA' to 'D'. Reflecting the limited number of gradations, entities or obligations with the same rating may not be of exactly the same credit quality, but they will share substantially similar credit risk characteristics.
- CI's credit ratings are assigned by, and all subsequent rating actions (including upgrades, downgrades and changes in outlook) determined by, rating committees and never by an individual analyst.
- CI's credit ratings indicate the likelihood of default, but they do not indicate a specific probability of default over any given time period.
- CI may initiate credit ratings on issuers without the request of the issuer provided there is adequate public information available to form a credible opinion of the issuer's creditworthiness.
- CI does not audit or verify the accuracy of information obtained from issuers as part of the rating process and may, in some cases, rely on unaudited financial data.
- A credit rating may, at any time, be raised, lowered, placed under review, suspended or withdrawn in accordance with CI's policies and procedures.
- CI may assign private 'shadow' sovereign ratings – internal assessments of sovereign risk that are not intended for publication and are used as an input into other rating assessments. Shadow sovereign ratings may constrain or cap the ratings of other rated issuers within a country. Shadow sovereign ratings may be based on a lower level of information or less detailed analysis compared to public sovereign ratings and, although monitored, may be reviewed less frequently than every six months. They do not represent a full rating opinion.

CI's credit ratings may be used as an analytical input into, but are not a substitute for, investors' own risk management. Investors in particular should be aware that:

- CI's credit ratings focus on one aspect of investment risk – credit (or repayment) risk – and do not explicitly capture loss severity or recovery prospects.
- CI's ratings are not recommendations to purchase, sell, or hold stocks or shares in an institution or particular security.
- CI's ratings do not assess or indicate the likelihood of changes in the market price of rated instruments due to market-related factors such as changes in interest rates or liquidity.
- CI's ratings do not provide an opinion of the liquidity in the market of an issuer's securities.