

Basel II – Pillar III

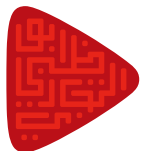
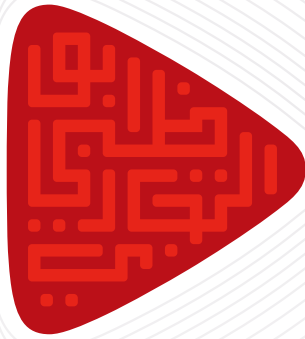


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1 SUMMARY OF DIFFERENCES BETWEEN PILLAR III DISCLOSURES AND RISK REVIEW IN THE AUDITED CONSOLIDATED FINANCIAL STATEMENTS

The details included in this report are from a regulatory perspective on certain aspects of credit, market and operational risk. The quantitative disclosures will not be directly comparable with the risk review in the audited consolidated financial statements, as the former are largely based on the Basel II standardised approach rules whereas quantitative risk disclosures in the audited consolidated financial statements are based on International Financial Reporting Standards (IFRS). This is most pronounced for the credit risk disclosures,

where credit exposure is defined as the maximum loss the Bank has estimated under specified Basel II rules. This differs from similar information in the audited consolidated financial statements such as the off-balance-sheet exposures which are disclosed post-credit conversion factors (CCFs) and may not reflect the off-balance-sheet exposures reported in the risk review section in the audited consolidated financial statements.

Topic	Risk review in the audited consolidated financial statements	Pillar III disclosures
Basis of requirements	The Bank's annual report is prepared in accordance with the requirements of IFRS and UAE Federal Law No. 2 of 2015.	The Bank's Pillar III disclosures provide detail on risk from a regulatory perspective as required by the Basel II standardised approach requirements, which have been implemented in the UAE through the Central Bank of the UAE guidelines issued in November 2009.
Basis of preparation	<ul style="list-style-type: none">▶ The quantitative credit risk disclosures in the risk review section are set out based on IFRS.▶ Loans and advances are analysed net of impairment and interest in suspense, and off-balance-sheet exposures are considered at maximum exposure levels.▶ Market risk disclosures are presented using VaR methodology and sensitivity analysis for the trading and non-trading books.	<ul style="list-style-type: none">▶ Provides details from a regulatory perspective on credit, market risk and operational risk. The capital calculation and the disclosures are based on the standardised approach as recommended by the Central Bank of UAE.▶ Loans and advances are analysed gross of impairment, and off-balance-sheet exposures are disclosed at post-CCF levels.▶ Market risk and operational risk disclosures are based on the capital required.

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2 SUMMARY OF CROSS-REFERENCES BETWEEN PILLAR III DISCLOSURES AND RISK REVIEW IN THE AUDITED CONSOLIDATED FINANCIAL STATEMENTS

Topic	Risk review in the audited consolidated financial statements	Pillar III disclosures
Credit risk management and measurement, and risk-grading	<ul style="list-style-type: none"> ▶ An overview of credit, liquidity and market risk management and measurement along with the quantitative disclosures are set out in Notes 43, 45 and 47 to the audited financial statements, respectively. ▶ Maximum exposure to credit risk net of impairment and interest in suspense and credit risk concentration are provided in Notes 43.1 and 43.2 to the audited consolidated financial statements. ▶ Internal credit risk grading analysis provided by business for loans neither past due nor impaired and available-for-sale investments is provided in Note 43.5 to the audited consolidated financial statements. ▶ Note 52 to the audited consolidated financial statements provides the overall capital adequacy of the Bank split into Tier 1 and Tier 2 ratios. 	<ul style="list-style-type: none"> ▶ A detailed analysis of credit risk exposure and risk-weighted assets (RWAs) calculated according to the standardised approach is set out in sections 11 and 12 of this report. ▶ A more detailed analysis of credit risk exposure pre- and post-credit risk mitigants (CRMs) and after applying credit conversion factors (CCFs) to the off-balance-sheet exposure is disclosed in sections 11 and 12 of this report. ▶ Section 12 of this report provides an indicative mapping of the Bank's rated and unrated exposure. ▶ Minimum regulatory capital requirements for credit, market and operational risk are set out in section 9 of this report.
Credit risk mitigation	An overview of CRM is provided in Note 43.4 to the audited consolidated financial statements.	Provides description of total CRM held by the Bank and those eligible from a regulatory perspective. This report also provides total exposure post- and pre-CRM (eligible under Basel II standardised approach). The eligible collaterals for the Bank's standardised portfolio are also disclosed in section 17 of this report.
Concentration of credit risk	Disclosures on concentration of credit risk by geography and by economic and industry sector are provided in Note 43.2 to the audited consolidated financial statements.	Disclosures on concentration of credit risk by currency, geography, residual maturity and economic sector calculated based on the Basel II rules are provided in sections 13, 14, 15 and 16 of this report.
Credit risk management and impairment allowance	Provisioning approach and definition of impaired loans along with disclosures of impaired loans, past due but not impaired loans, past due and impaired loans, individual impairment charge and collective impairment charge are set out in Note 43.6 to the audited consolidated financial statements.	Disclosures of impaired loans, impairment balance and interest in suspense by geography and economic sector are set out in section 18 of this report. Qualitative and quantitative disclosures as required by paragraph 825 of International Convergence of Capital Measurement and Capital Standards, issued by the Basel Committee, have been disclosed in Note 43 to the audited consolidated financial statements.
Market risk	A description of market risk management and measurement, along with quantitative disclosures on VaR and sensitivity analysis, is set out in Note 47 to the audited consolidated financial statements.	Sections 19 and 20 of this report provide quantitative disclosures of capital requirements for market risk (including equity risk).
Operational risk	Description of operational risk management is set out in Note 48 to the audited consolidated financial statements.	A detailed description of operational risk, including information system and regulatory risk faced by the Bank, is set out in section 21.

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3 COMPARISON BETWEEN THE AUDITED CONSOLIDATED BALANCE SHEET AND CREDIT RISK EXPOSURE AT DEFAULT AS AT 31 DECEMBER 2015

AED'000

Assets	Assets per Bank's statement of financial position	Effect of regulatory adjustments*	Assets subject to market risk only	Equity in Banking book	Regulatory balance sheet for credit risk (Gross exposure pre-CCF and -CRM)	Individual impairment and IIS adjustments used in capital calculation	Regulatory balance sheet for credit risk (Net exposure pre-CCF and -CRM)	Recognition of off-balance-sheet and PFE on OTC derivatives	Credit risk mitigants (CRMs)**	Credit risk EAD after all adjustments
2015										
Cash and balances with central banks	20,180,277	-	-	-	20,180,277	-	20,180,277	-	-	20,180,277
Deposits and balances due from banks	14,954,997	-	-	-	14,954,997	-	14,954,997	-	-	14,954,997
Reverse-repo placements	4,256,277	-	-	-	4,256,277	-	4,256,277	-	-	4,256,277
Trading securities	62,261	-	(62,261)	-	-	-	-	-	-	-
Derivative financial instruments	4,001,908	-	(4,001,908)	-	-	-	-	7,683,891	-	7,683,891
Investment securities	20,863,607	-	-	(558,196)	20,305,411	-	20,305,411	-	-	20,305,411
Loans and advances, net	153,677,386	7,719,839	-	-	161,397,225	(4,528,666)	156,868,559	28,017,803	(25,995,510)	158,890,852
Investment in associate	197,156	(197,156)	-	-	-	-	-	-	-	-
Investment properties	647,647	-	-	-	647,647	-	647,647	-	-	647,647
Other assets	8,571,640	(7,188,593)	-	-	1,383,047	-	1,383,047	-	-	1,383,047
Property and equipment, net	835,145	-	-	-	835,145	-	835,145	-	-	835,145
Intangible assets	18,800	(18,800)	-	-	-	-	-	-	-	-
	228,267,101	315,290	(4,064,169)	(558,196)	223,960,026	(4,528,666)	219,431,360	35,701,694	(25,995,510)	229,137,544

*Effect of regulatory adjustments includes adjustments for impairment, acceptances (treated off-balance-sheet), investment in associates and intangible assets.

**Guarantees amounting to AED 6,551,330 are excluded, as they are used to substitute credit risk weights and are not set off against the exposure value.

AED'000

Assets	Assets per Bank's statement of financial position	Effect of regulatory adjustments*	Assets subject to market risk only	Equity in Banking book	Regulatory balance sheet for credit risk (Gross exposure pre-CCF and -CRM)	Individual impairment and IIS adjustments used in capital calculation	Regulatory balance sheet for credit risk (Net exposure pre-CCF and -CRM)	Recognition of off-balance-sheet and PFE on OTC derivatives	Credit risk mitigants (CRMs)**	Credit risk EAD after all adjustments
2014										
Cash and balances with central banks	15,092,192	-	-	-	15,092,192	-	15,092,192	-	-	15,092,192
Deposits and balances due from banks	16,019,461	-	-	-	16,019,461	-	16,019,461	-	-	16,019,461
Trading securities	199,599	-	(199,599)	-	-	-	-	-	-	-
Derivative financial instruments	4,288,506	-	(4,288,506)	-	-	-	-	7,460,088	(3,569,466)	3,890,622
Investment securities	21,651,838	-	-	(544,875)	21,106,963	-	21,106,963	-	-	21,106,963
Loans and advances, net	140,562,498	8,148,742	-	-	148,711,240	(4,750,124)	143,961,116	19,928,218	(24,205,304)	139,684,030
Investment in associate	195,854	(195,854)	-	-	-	-	-	-	-	-
Investment properties	615,778	-	-	-	615,778	-	615,778	-	-	615,778
Other assets	4,551,844	(3,072,456)	-	-	1,479,388	-	1,479,388	-	-	1,479,388
Property and equipment, net	806,188	-	-	-	806,188	-	806,188	-	-	806,188
Intangible assets	35,705	(35,705)	-	-	-	-	-	-	-	-
	204,019,463	4,844,727	(4,488,105)	(544,875)	203,831,210	(4,750,124)	199,081,086	27,388,306	(27,774,770)	198,694,622

*Effect of regulatory adjustments includes adjustments for impairment, acceptances (treated off-balance-sheet), investment in associates and intangible assets.

**Guarantees amounting to AED 6,047,852 are excluded, as they are used to substitute credit risk weights and are not set off against the exposure value.

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disclosures for the year ended 31 December 2015

4 OVERVIEW OF BASEL II REQUIREMENTS

The Bank complies with the Basel II framework which has been implemented in the UAE through the Central Bank of the UAE guidelines issued in November 2009. Basel II is structured around three 'pillars' which are outlined below:

Pillar I deals with maintenance of regulatory capital calculated for three major components of risk that a bank faces: credit risk, market risk and operational risk. Other risks are not considered fully quantifiable at this stage;

Pillar II allows banks and supervisors to take a view on whether the bank should hold additional capital to cover the three Pillar I risk types, or to cover other risks. A bank's own internal models and assessments support this process. The second pillar deals with the regulatory response to the first pillar, giving regulators much-improved tools over those available to them under Basel I. It also provides a framework for dealing with all the other risks a bank may face, such as systemic risk, concentration risk, strategic risk, reputational risk, liquidity risk and legal risk, which the accord combines under the title of residual risk. This risk and capital assessment is commonly referred to as the Internal Capital Adequacy Assessment Process (ICAAP).

Pillar III covers external communication of risk and capital information by banks as specified in the Basel rules. The aim of Pillar III is to provide a consistent and comprehensive disclosure framework by requiring institutions to disclose details on the scope of application, capital, risk exposures, risk assessment processes and capital adequacy of the institution. It must be consistent with how the senior management, including the board, assess and manage the risks of the institution.

This report should be read in conjunction with the risk disclosures in the ADCB 2015 Annual Report and the audited consolidated financial statements.

Basel II also provides for different approaches to calculating capital requirements.

Standardised approach—Under this approach, the assets (including off-balance-sheet post-CCF) are classified into asset types to enable better risk sensitivity. The risk weights used to assess capital requirements against credit exposures are consistent across the industry.

Internal-ratings-based approach (IRB)—Under this approach, the risk weights are derived from the Bank's internal models. The IRB approach is further sub-divided into two alternative applications, Foundation and Advanced:

► **Foundation IRB (FIRB)**—Under this approach, the banks are allowed to develop their own models to estimate the PD (probability of default) for individual clients or groups of clients and use supervisory values for LGD (loss given default) and EAD (exposure at default) estimates. Banks can use this approach only subject to approval from their local regulators.

► **Advanced IRB (AIRB)**—Under this approach, the banks are allowed to develop their own model to quantify required capital for credit risk. PD, LGD and EAD can be determined using the Bank's internal models. Banks can use this approach only subject to approval from their local regulators.

5 ADCB'S APPROACH TO PILLAR I

Credit risk—The Bank uses the standardised approach for calculating its capital requirements for credit risk. This approach allows the use of external ratings from designated credit-rating agencies, wherever available, in determining the appropriate risk weights. The risk weights are determined by the asset class and the external rating of the counterparty. The net exposure incorporates off-balance-sheet exposures after applying the credit conversion (CCF) and credit risk mitigation (CRM) factors.

Market risk—For the regulatory market risk capital requirements, the Bank uses the standardised approach.

Operational risk—The Bank uses the standardised approach for computing capital requirements for operational risk.

6 FUTURE DEVELOPMENTS

The regulation and supervision of financial institutions continues to undergo significant change in response to the global financial crisis.

In December 2010, the Basel Committee issued final rules in two documents: A global regulatory framework for more resilient banks and banking systems and an international framework for liquidity risk measurement, standards and monitoring, which together are commonly referred to as 'Basel III'. Basel III will require banks to hold 4.5% of common equity (up from 2% in Basel II) and 6% of Tier 1 capital (up from 4% in Basel II) of risk-weighted assets (RWAs). Basel III also introduces additional capital buffers: (i) a mandatory capital conservation buffer of 2.5%, and (ii) a discretionary countercyclical buffer, which allows national regulators to require up to another 2.5% of capital during periods of high credit growth.

In addition, Basel III introduces a minimum 3% leverage ratio and two required liquidity ratios. The Liquidity Coverage Ratio requires a bank to hold sufficient high quality liquid assets to cover its total net cash flows over 30 days; the Net Stable Funding Ratio requires the available amount of stable funding to exceed the required amount of stable funding over a one-year period of extended stress.

In May 2015, the Central Bank of the UAE published "Regulations relating to Liquidity at Banks". Starting on 1 January 2015, minimum liquidity coverage will be 60%. This coverage will increase by 10% each year to reach 100% by 1 January 2019. The NSFR requirement to be introduced in January 2018 is 100%. The methodology for estimating the LCR and NSFR is based on an interpretation of the Basel standards and includes a number of assumptions that are subject to change. ADCB monitors its position against the anticipated LCR and NSFR requirements to ensure the Bank's ability to comply with the standards.

IMPACT ON ADCB

At the end of 2015, the capital ratio and the Tier 1 ratio of the Bank were 19.76% and 16.29%, respectively. Additionally, the composition of the Bank's capital is of high-quality equity based with lesser reliance on Tier 2 capital supply (i.e. hybrid instruments). Further, the UAE Central Bank has a set total capital adequacy ratio of 12% and Tier 1 capital adequacy ratio of 8%, which are higher than the target 2019 Basel III ratios of 8% and 6%, respectively.

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disclosures for the year ended 31 December 2015

BASIS OF CONSOLIDATION

The Bank's Pillar III disclosures are presented on a consolidated basis for the year ended 31 December 2015. The consolidation basis used is the same as that used for regulatory capital adequacy.

In accordance with paragraph 825 of International Convergence of Capital Measurement and Capital Standards, issued by the Basel Committee, general disclosures of credit risk provided in this report have a wide range of information about overall credit exposure and may not be necessarily based on information prepared for regulatory purposes.

7 VERIFICATION

The Pillar III disclosures for the year ended 31 December 2015 have been appropriately verified internally, but are not subject to audit by the Bank's external auditor.

8 RISK PROFILE OF ADCB

The Government of Abu Dhabi indirectly owns 58.083% of the Bank's issued share capital via the Abu Dhabi Investment Council. ADCB enjoys strong government support as evidenced by historical capital, liquidity and strategic support by its de-facto owners. As at 31 December 2015, the Chairman, Vice-Chairman and four out of nine members of the Board were nominated by the Abu Dhabi Investment Council.

9 CAPITAL ADEQUACY AND CAPITAL MANAGEMENT

The allocation of capital between specific operations and activities is, to a large extent, driven by optimisation of the return achieved on the capital allocated. The amount of capital allocated to each operation or activity is based primarily upon the regulatory capital, but in some cases the regulatory requirements do not reflect fully the varying degree of risk associated with different activities. In such cases, the capital requirements may be flexed to reflect differing risk profiles, subject to the overall level of capital to support a particular operation or activity not falling below the minimum required for regulatory purposes. The process of allocating capital to specific operations and activities is undertaken with consultation with the Board Risk & Credit Committee (BRCC) and Finance, and is subject to review by the Assets & Liabilities Management Committee (ALCO), Management Risk & Credit Committee (MRCC), BRCC and the Board, as appropriate.

	2015		2014	
	Capital charge (AED'000)	Capital ratio	Capital charge (AED'000)	Capital ratio
Capital requirements				
1 Credit risk				
Standardised approach	18,877,742		16,408,829	
2 Market risk				
Standardised approach	678,284		539,649	
3 Operational risk				
Standardised approach	1,522,728		1,420,270	
Total capital requirement	21,078,754		18,368,748	
Capital ratios:				
Total for the Bank		19.76%		21.03%
Tier 1 for the Bank		16.29%		17.01%

Qualitative and quantitative disclosures on capital structure as required by paragraph 822 of the International Convergence of Capital Measurement and Capital Standards, issued by the Basel

Committee, have been disclosed in Note 52 to the audited consolidated financial statements.

10 QUALITATIVE RISK DISCLOSURES

For each separate risk area (credit, market, operational and equity risk), banks are required to describe their risk management objectives and policies, which primarily include strategies, processes, organisation framework, reporting and measurement systems. These

disclosures are discussed and are set out in the "Risk Management" section of the ADCB 2015 Annual Report and Notes 42–48 of the audited consolidated financial statements. Also, refer to section 2 of this report for cross-referencing information.

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11 GROSS CREDIT RISK EXPOSURE BY ASSET CLASS – STANDARDISED APPROACH

AED'000

Asset Class	Gross exposure		Credit risk mitigation (CRM)					Credit risk-weighted assets
	On-balance-sheet	Off-balance-sheet (post-CCF)	Gross exposure (on- & off-balance-sheet post-CCF)	Exposure pre-CRM (net of specific provision and IIS)	CRM*	Net exposure post-CCF, -CRM and other adjustments		
2015**								
Claims on sovereigns	43,122,223	1,551,626	44,673,849	44,673,850	4,244,797	40,429,053	4,914,150	
Claims on non-commercial public sector enterprises (PSEs)	2,039,502	498,617	2,538,119	2,538,119	50	2,538,069	–	
Claims on multilateral development banks	87,912	–	87,912	87,912	–	87,912	–	
Claims on financial institutions***	45,029,689	12,966,083	57,995,772	57,532,409	6,528,519	51,040,881	32,731,362	
Claims on securities firms	244,756	917,816	1,162,572	1,162,572	668,958	705,478	645,743	
Claims on government-related entities (GREs)	21,464,574	2,190,673	23,655,247	23,519,993	1,378,009	25,414,956	21,491,439	
Claims on Corporate	28,703,228	16,583,127	45,286,355	45,229,927	11,912,962	34,106,708	32,916,152	
Claims included in the regulatory retail portfolio	30,662,585	876,451	31,539,036	31,366,926	4,723,506	28,119,085	21,006,469	
Claims secured by residential property	5,487,844	117,301	5,605,145	5,603,499	3,701	5,599,798	2,853,285	
Claims secured by commercial real estate	38,130,737	–	38,130,737	37,657,611	2,575,683	35,845,998	35,186,973	
Past due loans	5,800,423	–	5,800,423	2,573,692	510,655	2,063,059	2,382,397	
Higher-risk categories	–	–	–	–	–	–	–	
Other assets	3,186,553	–	3,186,553	3,186,547	–	3,186,547	3,186,547	
Claims on securitised assets	–	–	–	–	–	–	–	
Credit derivatives (banks selling protection)	–	–	–	–	–	–	–	
Total Credit Risk	223,960,026	35,701,694	259,661,720	255,133,057	32,546,840	229,137,544	157,314,517	
2014								
Claims on sovereigns	31,101,772	865,082	31,966,854	31,966,854	33,317	31,933,537	2,999,476	
Claims on non-commercial public sector enterprises (PSEs)	2,578,897	509,001	3,087,898	3,087,898	–	3,087,898	–	
Claims on multilateral development banks	–	–	–	–	–	–	–	
Claims on financial institutions***	46,140,405	8,705,489	54,845,894	54,440,656	11,314,528	43,162,858	25,711,220	
Claims on securities firms	497,402	835,617	1,333,019	1,333,019	134,906	1,288,884	1,194,396	
Claims on government-related entities (GREs)	21,771,093	3,918,434	25,689,527	25,233,640	3,311,709	24,722,016	21,933,183	
Claims on Corporate	29,065,935	12,058,677	41,124,612	41,015,353	9,761,077	32,257,942	30,537,724	
Claims included in the regulatory retail portfolio	26,042,208	361,250	26,403,458	26,273,961	5,183,173	21,800,853	16,873,733	
Claims secured by residential property	5,272,336	134,756	5,407,092	5,405,879	1,783	5,404,096	2,529,857	
Claims secured by commercial real estate	33,649,722	–	33,649,722	33,072,997	3,371,306	31,108,226	30,689,887	
Past due loans	5,680,007	–	5,680,007	2,607,702	710,823	1,896,879	2,239,331	
Higher-risk categories	–	–	–	–	–	–	–	
Other assets	2,031,433	–	2,031,433	2,031,433	–	2,031,433	2,031,433	
Claims on securitised assets	–	–	–	–	–	–	–	
Credit derivatives (banks selling protection)	–	–	–	–	–	–	–	
Total Credit Risk	203,831,210	27,388,306	231,219,516	226,469,392	33,822,622	198,694,622	136,740,240	

*Eligible guarantees used to substitute credit risk weights are included in CRM.

**In 2015, certain loans and advances pertaining to government-related entities (GREs) guaranteed by the Government of Abu Dhabi have been classified as sovereigns. The corresponding guarantees against these loans have been reflected under credit risk mitigation.

***Claims on financial institutions include exposure to all credit institutions, investment firms and finance companies.

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12 GROSS CREDIT RISK EXPOSURE BY EXTERNALLY RATED/UNRATED – STANDARDISED APPROACH

AED'000

Asset Class	Gross exposure		Credit risk mitigation (CRM)					Credit risk-weighted assets
	Rated	Unrated	Gross exposure (on- & off-balance-sheet post-CCF)	Exposure pre-CRM (net of specific provision and IIS)	Net exposure post-CCF, -CRM and other adjustments			
					CRM*			
2015**								
Claims on sovereigns	44,673,849	–	44,673,849	44,673,850	4,244,797	40,429,053	4,914,150	
Claims on non-commercial public sector enterprises (PSEs)	2,538,119	–	2,538,119	2,538,119	50	2,538,069	–	
Claims on multilateral development banks	87,912	–	87,912	87,912	–	87,912	–	
Claims on financial institutions***	41,541,588	16,454,185	57,995,773	57,532,409	6,528,519	51,040,881	32,731,362	
Claims on securities firms	465,457	697,115	1,162,572	1,162,572	668,958	705,478	645,743	
Claims on government-related entities (GREs)	596,228	23,059,019	23,655,247	23,519,993	1,378,009	25,414,956	21,491,439	
Claims on Corporate	4,671,150	40,615,204	45,286,354	45,229,927	11,912,962	34,106,708	32,916,152	
Claims included in the regulatory retail portfolio	–	31,539,036	31,539,036	31,366,926	4,723,506	28,119,085	21,006,469	
Claims secured by residential property	–	5,605,145	5,605,145	5,603,499	3,701	5,599,798	2,853,285	
Claims secured by commercial real estate	–	38,130,737	38,130,737	37,657,611	2,575,683	35,845,998	35,186,973	
Past due loans	–	5,800,423	5,800,423	2,573,692	510,655	2,063,059	2,382,397	
Higher-risk categories	–	–	–	–	–	–	–	
Other assets	–	3,186,553	3,186,553	3,186,547	–	3,186,547	3,186,547	
Claims on securitised assets	–	–	–	–	–	–	–	
Credit derivatives (banks selling protection)	–	–	–	–	–	–	–	
Total Credit Risk	94,574,303	165,087,417	259,661,720	255,133,057	32,546,840	229,137,544	157,314,517	
2014								
Claims on sovereigns	31,966,854	–	31,966,854	31,966,854	33,317	31,933,537	2,999,476	
Claims on non-commercial public sector enterprises (PSEs)	3,087,898	–	3,087,898	3,087,898	–	3,087,898	–	
Claims on multilateral development banks	–	–	–	–	–	–	–	
Claims on financial institutions***	40,251,548	14,594,346	54,845,894	54,440,655	11,314,528	43,162,857	25,711,219	
Claims on securities firms	422,016	911,003	1,333,019	1,333,019	134,906	1,288,884	1,194,396	
Claims on government-related entities (GREs)	7,701,900	17,987,627	25,689,527	25,233,640	3,311,709	24,722,017	21,933,184	
Claims on Corporate	6,149,937	34,974,675	41,124,612	41,015,353	9,761,077	32,257,942	30,537,724	
Claims included in the regulatory retail portfolio	–	26,403,458	26,403,458	26,273,962	5,183,173	21,800,853	16,873,733	
Claims secured by residential property	–	5,407,092	5,407,092	5,405,879	1,783	5,404,096	2,529,857	
Claims secured by commercial real estate	–	33,649,722	33,649,722	33,072,997	3,371,306	31,108,226	30,689,887	
Past due loans	–	5,680,007	5,680,007	2,607,702	710,823	1,896,879	2,239,331	
Higher-risk categories	–	–	–	–	–	–	–	
Other assets	–	2,031,433	2,031,433	2,031,433	–	2,031,433	2,031,433	
Claims on securitised assets	–	–	–	–	–	–	–	
Credit derivatives (banks selling protection)	–	–	–	–	–	–	–	
Total Credit Risk	89,580,153	141,639,363	231,219,516	226,469,392	33,822,622	198,694,622	136,740,240	

*Eligible guarantees used to substitute credit risk weights are included in CRM.

**In 2015, certain loans and advances pertaining to government-related entities (GREs) guaranteed by the Government of Abu Dhabi have been classified as sovereigns. The corresponding guarantees against these loans have been reflected under credit risk mitigation.

***Claims on financial institutions include exposure to all credit institutions, investment firms and finance companies.

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13 GROSS CREDIT RISK BY CURRENCY

	AED'000								
	Loans	Investment securities	Other assets	Total funded	Commitments (post-CCF)	OTC derivatives	Other off-balance-sheet exposures (post-CCF)	Total non-funded	Total
2015									
AED	128,526,980	–	20,280,657	148,807,637	4,819,835	5,132,797	6,213,214	16,165,846	164,973,483
USD	31,784,686	15,769,998	25,303,151	72,857,835	1,739,315	1,507,163	12,564,839	15,811,317	88,669,152
EUR	18,850	2,628,969	571,316	3,219,135	–	346,235	716,167	1,062,402	4,281,537
CHF	–	334,633	16,528	351,161	–	–	525	525	351,686
GBP	16,689	–	46,347	63,036	–	89,089	55,568	144,657	207,693
MYR	–	–	3,901	3,901	–	–	–	–	3,901
Other	1,050,020	1,571,811	3,204,206	5,826,037	–	608,607	1,908,340	2,516,947	8,342,984
Less: Acceptances	–	–	(7,168,716)	(7,168,716)	–	–	–	–	(7,168,716)
Total	161,397,225	20,305,411	42,257,390	223,960,026	6,559,150	7,683,891	21,458,653	35,701,694	259,661,720
2014									
AED	115,842,946	89,875	20,508,153	135,069,975	2,698,868	1,491,580	5,921,226	10,111,673	145,181,648
USD	32,089,205	18,000,044	12,196,307	62,285,556	3,440,332	5,120,766	6,108,639	14,669,737	76,955,293
EUR	33,706	1,177,759	237,378	1,448,843	–	451,531	526,749	978,280	2,427,123
CHF	–	–	30,396	30,396	–	51,019	439	51,458	81,854
GBP	17,551	–	528,209	545,760	–	101,100	22,484	123,584	669,344
MYR	–	–	33,212	33,212	–	45,173	–	45,173	78,385
Other	727,832	1,839,285	3,385,772	5,952,889	–	198,920	1,209,481	1,408,401	7,361,290
Less: Acceptances	–	–	(2,906,420)	(2,906,420)	–	–	–	–	(2,906,420)
Total	148,711,240	21,106,963	34,013,007	203,831,210	6,139,200	7,460,088	13,789,018	27,388,306	231,219,516

BASEL II – PILLAR III

disclosures for the year ended 31 December 2015

14 GROSS CREDIT RISK BY GEOGRAPHY

	AED'000								
	Loans	Investment securities	Other assets	Total funded	Commitments (post-CCF)	OTC derivatives	Other off-balance-sheet exposures (post-CCF)	Total non-funded	Total
2015									
Domestic (UAE)	146,907,782	8,827,837	35,926,583	191,662,202	5,922,741	3,295,578	16,096,648	25,314,967	216,977,169
Other GCC countries	4,776,623	1,585,466	7,251,305	13,613,394	472,580	66,102	412,156	950,838	14,564,232
Other Arab countries	273,934	1,232,926	4,468	1,511,328	–	31,519	76,371	107,890	1,619,218
Asia	6,061,118	4,134,947	190,537	10,386,602	73,070	153,221	1,385,772	1,612,063	11,998,665
Europe	1,597,902	2,570,783	3,723,831	7,892,516	35,461	4,127,221	943,071	5,105,753	12,998,269
USA	6,006	1,219,978	2,193,179	3,419,163	1,845	10,250	2,428,334	2,440,429	5,859,592
Rest of the world	1,773,860	733,475	136,202	2,643,537	53,453	–	116,301	169,754	2,813,291
Less: Acceptances	–	–	(7,168,716)	(7,168,716)	–	–	–	–	(7,168,716)
Total	161,397,225	20,305,411	42,257,390	223,960,026	6,559,150	7,683,891	21,458,653	35,701,694	259,661,720
2014									
Domestic (UAE)	134,361,813	8,760,018	27,478,554	169,229,386	5,947,751	3,098,221	11,828,626	20,874,598	190,103,984
Other GCC countries	3,618,299	3,377,627	3,477,360	10,473,286	77,485	4,503	531,793	613,781	11,087,067
Other Arab countries	234,954	282,309	4,670	521,933	–	6,425	110	6,535	528,468
Asia	8,146,840	2,515,360	962,496	11,624,696	100,321	139,877	462,637	702,836	12,327,532
Europe	1,377,743	2,591,094	4,223,835	8,192,672	–	4,198,064	678,541	4,876,605	13,069,277
USA	191,650	2,819,635	303,267	3,314,552	–	12,997	127,194	140,191	3,454,743
Rest of the world	779,941	760,920	469,245	2,010,106	13,643	–	160,117	173,760	2,183,866
Less: Acceptances	–	–	(2,906,420)	(2,906,420)	–	–	–	–	(2,906,420)
Total	148,711,240	21,106,963	34,013,007	203,831,210	6,139,200	7,460,088	13,789,018	27,388,306	231,219,516

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15 GROSS CREDIT RISK BY RESIDUAL MATURITY

	AED'000								
	Loans	Investment securities	Other assets	Total funded	Commitments (post-CCF)	OTC derivatives	Other off-balance-sheet exposures (post-CCF)	Total non-funded	Total
2015									
Less than 3 months	25,710,491	2,289,375	39,333,270	67,333,136	4,819,835	929,674	6,213,214	11,962,723	79,295,859
3 months to less than 6 months	2,811,237	2,095,029	3,336,085	8,242,351	1,739,315	412,437	12,564,839	14,716,591	22,958,942
6 months to less than 1 year	4,585,329	1,810,265	5,293,836	11,689,430	–	494,037	716,167	1,210,204	12,899,634
1 year to 3 years	22,515,638	6,174,564	647,647	29,337,849	–	1,456,709	525	1,457,234	30,795,083
Over 3 years	105,774,530	7,936,178	815,268	114,525,976	–	4,391,034	1,963,908	6,354,942	120,880,918
Less: Acceptances	–	–	(7,168,716)	(7,168,716)	–	–	–	–	(7,168,716)
Total	161,397,225	20,305,411	42,257,390	223,960,026	6,559,150	7,683,891	21,458,653	35,701,694	259,661,720
2014									
Less than 3 months	21,396,566	2,185,274	26,850,719	49,061,560	496,085	1,185,435	9,100,727	10,782,247	59,843,807
3 months to less than 6 months	3,880,910	2,173,418	5,253,783	11,308,111	254,536	223,909	1,165,584	1,644,029	12,952,140
6 months to less than 1 year	4,559,945	3,259,557	3,388,445	11,207,947	2,231,596	193,424	2,042,633	4,467,653	15,675,600
1 year to 3 years	19,453,338	7,113,340	4,514	26,571,192	2,157,834	1,342,320	1,344,797	4,844,951	31,416,143
Over 3 years	99,420,481	6,375,374	1,421,966	107,217,821	999,149	4,515,000	135,277	5,649,426	112,867,247
Less: Acceptances	–	–	(2,906,420)	(2,906,420)	–	–	–	–	(2,906,420)
Total	148,711,240	21,106,963	34,013,007	203,831,210	6,139,200	7,460,088	13,789,018	27,388,306	231,219,516

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16 GROSS CREDIT RISK BY ECONOMIC SECTOR

	AED'000								
	Loans	Investment securities	Other assets	Total funded	Commitments (post-CCF)	OTC derivatives	Other off-balance-sheet exposures (post-CCF)	Total non-funded	Total
2015									
Agriculture	216,646	–	–	216,646	–	–	2,221	2,221	218,867
Energy	293,703	38,901	–	332,604	64,940	1,968	15,208	82,116	414,720
Trading	4,926,018	–	–	4,926,018	516,180	113,239	2,003,211	2,632,630	7,558,648
Real estate & hospitality	54,382,905	429,100	647,647	55,459,652	2,419,012	15,397	7,213,223	9,647,632	65,107,284
Transport	2,380,189	–	–	2,380,189	160,903	263,809	73,100	497,812	2,878,001
Personal	39,312,380	99,071	–	39,411,451	768,567	1,631	102,494	872,692	40,284,143
Government & public sector entities	33,080,419	11,511,612	22,016,778	66,608,809	1,103,017	1,735,103	1,314,173	4,152,293	70,761,102
Financial institutions	19,917,279	8,119,498	17,374,773	45,411,550	197,607	5,535,528	8,134,770	13,867,905	59,279,455
Manufacturing	3,283,190	64,392	–	3,347,582	83,540	182	379,977	463,699	3,811,281
Services	1,778,780	–	–	1,778,780	1,181,605	13,011	2,204,285	3,398,901	5,177,681
Others	450,764	42,837	9,386,908	9,880,509	63,779	4,023	15,991	83,793	9,964,302
Add: Interest in Suspense	1,374,952	–	–	1,374,952	–	–	–	–	1,374,952
Less: Acceptances	–	–	(7,168,716)	(7,168,716)	–	–	–	–	(7,168,716)
Total	161,397,225	20,305,411	42,257,390	223,960,026	6,559,150	7,683,891	21,458,653	35,701,694	259,661,720
2014									
Agriculture	208,394	–	–	208,394	–	–	12,963	12,963	221,357
Energy	3,381,224	–	–	3,381,224	353,692	12,426	527,955	894,073	4,275,297
Trading	3,475,611	–	–	3,475,611	416,773	26,624	1,347,357	1,790,754	5,266,365
Real estate & hospitality	48,829,006	22,396	615,778	49,467,180	3,747,969	64,731	5,879,830	9,692,530	59,159,710
Transport	2,189,191	–	–	2,189,191	29,328	722,276	152,236	903,840	3,093,031
Personal	34,221,066	93,962	–	34,315,028	247,537	30,818	66,015	344,370	34,659,398
Government & public sector entities	30,709,795	10,422,767	15,092,192	56,224,754	–	57,892	12,596	70,488	56,295,242
Financial institutions	20,085,616	10,524,785	16,019,461	46,629,862	232,840	4,965,906	4,412,663	9,611,411	56,241,272
Manufacturing	2,474,109	–	–	2,474,109	241,477	1,246,980	582,051	2,070,508	4,544,617
Services	1,221,080	43,053	–	1,264,133	170,824	153,322	584,251	908,397	2,172,530
Others	545,149	–	5,191,996	5,737,145	698,760	179,113	211,099	1,088,972	6,826,117
Add: Interest in Suspense	1,370,999	–	–	1,370,999	–	–	–	–	1,370,999
Less: Acceptances	–	–	(2,906,420)	(2,906,420)	–	–	–	–	(2,906,420)
Total	148,711,240	21,106,963	34,013,007	203,831,210	6,139,200	7,460,088	13,789,018	27,388,306	231,219,516

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17 CREDIT RISK AND RISK MEASUREMENT AND MITIGATION POLICIES

Loans and advances and commitments to customers, investment in securities held in the available-for-sale (AFS) portfolio and derivatives are the main sources of credit risk for the Bank. The Bank's risk management policies and processes are designed to identify, analyse and measure risk, to set appropriate risk appetite, limits and controls, and to monitor the risks and adherence to limits by means of reliable and timely data review. The Bank assesses the probability of default of each counterparty using internal rating tools tailored for various categories of counterparties.

Exposure to credit risk is also managed through regular analysis of the ability of borrowers and potential borrowers to meet interest and capital repayment obligations, and by changing these lending limits or taking pre-emptive action through additional collateral/margin calls, structural enhancements, etc., where appropriate.

The Credit Risk Management Group has policies and procedures in place setting out the circumstances where acceptable and appropriate collateral is to be secured to mitigate credit risk, including valuation parameters, review frequency and independence of valuation. The acceptable collateral types are set out in the credit policy of the Bank, which is approved by the BRCC. The type, liquidity and realisation costs on collateral held are key determinants of the LGD percentage that is assigned to a credit risk exposure.

The Bank primarily has the following categories of collateral:

LOANS AND ADVANCES

- (a) Real estate collateral—The Bank accepts real estate collateral (residential, commercial and mixed use) to either back corporate exposures or as income-producing real estate as the repayment source for the facility. Both of these segments are treated separately and governed by separate policies. In all cases, real estate collaterals are subject to regular re-evaluation by Bank-approved valuers and mortgage registration with the appropriate regulatory authorities. In lending new facilities, the Bank has a policy to obtain multiple valuations (based on the facility size) to ensure conservatism in determining Loan to Value (LTV) ratio. As at 31 December 2015, the Bank had total mortgage collateral of AED 82,585 mn (2014: AED 78,298 mn), almost all of it in the UAE and over 50% in Abu Dhabi, with the rest across other Emirates. The Bank also holds as collaterals secondary mortgages and assignment over lease-hold properties which are not included in the mortgage collateral value.
- (b) Financial instruments collateral—Only publicly listed company shares are accepted as collateral for corporate and high-net-worth individual facilities. There is a process to evaluate mark to market on a daily basis, and this affects the drawing power against these facilities. All share and bond collaterals are pledged either at the market or at the broker level. These would also include a small amount of mutual funds. As at 31 December 2015, the Bank had total share collateral of AED 26,998 mn (2014: AED 34,544 mn), predominantly listed on the Abu Dhabi Stock Exchange.

- (c) Cash collateral—The Bank also takes cash collateral primarily from small and medium-size enterprise (SME) customers and as trade margins for trade finance transactions. As at 31 December 2015, the Bank had AED 12,657 mn in cash and near-cash collaterals (2014: AED 7,272 mn).
- (d) Guarantees from highly rated banks and corporates—In addition to collaterals, the Bank regularly accepts guarantees from highly rated corporates or banks and transfers the risk of the exposure to the better-rated entities. Almost all company loans have the corporate guarantee of the parent. Most of our guarantees are executed using the Bank's standard legal documentation to ensure they are unconditional guarantees to qualify as credit risk mitigants. As at 31 December 2015, the guarantee accepted by the Bank amounted to AED 6,551 mn (2014: AED 6,048 mn).
- (e) Charge over company's assets, including stock debtors and work in progress—The Bank regularly obtains the company's assets inventory and stock debtors as collateral whilst extending working capital facilities to them.
- (f) Charge over assets being financed (e.g. vehicles, equipment)—For asset-backed financing, the asset being financed is usually secured as a collateral. The total value of such collateral was AED 12,882 mn as at 31 December 2015 (2014: AED 10,467 mn).

TREASURY PRODUCTS

The Bank mitigates its credit exposure for Treasury products by entering into master netting arrangements with counterparties with which it undertakes a significant volume of transactions. Counterparty credit risk is reduced by a master netting arrangement to the extent that if an event of default occurs, all amounts with the counterparty are terminated and settled on a net basis. The Bank mitigates its counterparty credit risk exposure from dealing in global markets products through the use of Credit Support Annexes (CSAs). CSAs require the counterparty (or the Group) to post collateral when mark-to-market positions exceed threshold and minimum transfer amounts. Most of our Treasury counterparties are covered by ISDA and/or CSA. There is a regular mark-to-market process and all valuation methodologies are approved by the Market Risk department. As at 31 December 2015, the Bank held AED 76 mn of collateral for CSA purposes. In general, the Bank does not use credit derivatives or credit default swaps as a credit risk mitigant.

As per the Basel II standardised approach, the following CRMs are considered eligible for capital calculation purposes:

- ▶ Netting—applicable only with legally enforceable netting agreements in place. However, to use this mitigant, the ability to systematically calculate net exposure must be demonstrated.
- ▶ Collateral—either the simple or comprehensive approaches may be applied. ADCB uses the comprehensive approach.
- ▶ Guarantees and credit derivatives—these mitigants can be used provided they are direct, explicit, irrevocable and unconditional.

The Central Bank of the UAE must be satisfied that the Bank has suitable risk management tools in place to adopt the use of such mitigants.

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ELIGIBLE CREDIT RISK MITIGANTS AND RWA RELIEF

	AED'000	
	2015	2014
RWA pre-CRM	185,647,317	166,308,921
RWA relief:		
On-balance-sheet netting	–	(1,623,539)
Eligible financial collateral (cash and securities)	(23,340,447)	(22,836,282)
Guarantees (credit substitution)	(4,992,353)	(5,108,860)
Net exposures after credit risk mitigation	157,314,517	136,740,240

ELIGIBLE CREDIT RISK MITIGANTS USED IN CAPITAL CALCULATION

	AED'000	
Type of credit risk mitigants*	2015	2014
Exposure reduction:		
Cash	8,238,662	4,044,467
Other eligible financial collateral (main index shares and bonds)	17,756,848	20,160,837
Netting agreements	–	3,569,466
Credit substitution:	25,995,510	27,774,770
Guarantees	6,551,330	6,047,852
Total eligible credit risk mitigants	32,546,840	33,822,622

* To the extent utilised in capital calculation.

18 IMPAIRMENT ANALYSIS

PORTFOLIO MONITORING AND IDENTIFYING CREDIT RISK AND IMPAIRMENT

Credit Risk Management monitors the portfolio through system-generated MIS and periodic reviews giving due consideration to industry and general economic trends, market feedback and media reports. Movement of the individual and collective impairment allowance on loans and advances was as follows:

	AED'000	
	2015	2014
Opening balance of impairment allowance	6,777,743	6,889,947
Charge for the year		
a. Individual impairment	704,764	714,991
b. Collective impairment	48,082	325,560
Less: Write-off of impaired loans to income statement	(806,219)	(718,638)
Less: Recovery of loan loss provisions	(252,566)	(229,352)
Less: Discount unwind/currency translation	(126,917)	(204,765)
Closing balance of impairment allowance	6,344,887	6,777,743

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PORTFOLIO MONITORING AND IDENTIFYING CREDIT RISK AND IMPAIRMENT

Impaired loans by geography

	AED'000					
	Overdue (gross of interest in suspense & individual impairment)		Impairment allowance as at 31 December		Total impaired assets (net of interest in suspense & individual impairment)	
	90 days and above	Total	Individual	Collective		
2015						
Domestic (UAE)	5,699,815	5,699,815	3,141,070	–	1,200,101	1,358,644
Other GCC countries	492,425	492,425	222,849	–	170,866	98,710
Other Arab countries	–	–	–	–	–	–
Asia	16,811	16,811	12,079	–	3,978	754
Europe	3	3	–	–	3	–
Rest of the world	4	4	–	–	4	–
Total	6,209,058	6,209,058	3,375,998	2,968,889	1,374,952	1,458,108
2014						
Domestic (UAE)	5,336,643	5,336,643	3,566,526	–	1,214,731	555,386
Other GCC countries	556,792	556,792	266,354	–	137,914	152,524
Other Arab countries	–	–	–	–	–	–
Asia	13,500	13,500	12,675	–	314	512
Europe	2	2	–	–	2	–
Rest of the world	74,937	74,937	11,241	–	18,037	45,659
Total	5,981,874	5,981,874	3,856,796	2,920,947	1,370,999	754,080

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Impaired loans by economic sector

	AED'000					
	Overdue (gross of interest in suspense & individual impairment)		Impairment allowance as at 31 December		Interest in suspense	Total impaired assets (net of interest in suspense & individual impairment)
	90 days and above	Total	Individual	Collective		
2015						
Agriculture	251,896	251,896	99,244	–	53,947	98,705
Energy	1,667	1,667	–	–	131	1,536
Trading	238,426	238,426	165,836	–	19,791	52,799
Real estate & hospitality	2,076,131	2,076,131	892,387	–	569,176	614,568
Transport	353,914	353,914	161,687	–	73,214	119,013
Personal	2,861,268	2,861,268	1,412,911	–	548,689	899,668
Government & public sector entities	–	–	135,254	–	–	(135,254)
Financial institutions	361,526	361,526	471,186	–	99,930	(209,590)
Manufacturing	28,119	28,119	20,172	–	3,338	4,609
Services	33,768	33,768	15,547	–	6,438	11,783
Others	2,343	2,343	1,774	–	298	271
Total	6,209,058	6,209,058	3,375,998	2,968,889	1,374,952	1,458,108
2014						
Agriculture	234,683	234,683	98,975	–	36,779	98,929
Energy	7	7	–	–	1	7
Trading	22,582	22,582	72,352	–	4,558	(54,328)
Real estate & hospitality	2,040,468	2,040,468	1,092,971	–	549,177	398,320
Transport	276,460	276,460	109,516	–	51,829	115,115
Personal	3,022,101	3,022,101	1,608,343	–	653,648	760,111
Government & public sector entities	–	–	455,866	–	–	(455,866)
Financial institutions	330,589	330,589	405,869	–	68,211	(143,492)
Manufacturing	32,212	32,212	12,880	–	3,140	16,192
Services	20,846	20,846	1	–	3,459	17,386
Others	1,926	1,926	23	–	197	1,706
Total	5,981,874	5,981,874	3,856,796	2,920,947	1,370,999	754,080

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19 MARKET RISK

CAPITAL CALCULATION

Capital is allocated in respect of market risk under the general guidelines and framework set out under Basel II Section VI, Market Risk, which defines this risk as the risk of losses in on- and off-balance-sheet positions arising from movements in market prices.

The market risks subject to a capital charge are as follows:

- ▶ interest rate risk;
- ▶ foreign exchange risk;
- ▶ equity exposure risk;
- ▶ commodity risk; and
- ▶ options risk.

CAPITAL REQUIREMENT FOR MARKET RISK UNDER STANDARDISED APPROACH

	AED'000	
	2015	2014
Interest rate risk	540,172	455,614
Equity position risk	–	–
Foreign exchange risk	34,856	29,138
Commodity risk	23,394	26,090
Options risk	79,862	28,807
Total Capital Requirement	678,284	539,648

	2015		2014	
	Risk-weighted assets	Capital requirements	Risk-weighted assets	Capital requirements
Interest rate risk—trading book				
Specific risk	1,492	179	67,425	8,091
General risk—maturity-based	4,499,942	539,993	3,729,355	447,523
General risk—duration-based	–	–	–	–
Foreign exchange risk	290,467	34,856	242,813	29,138
Equity exposure risk- trading book	–	–	–	–
General risk	–	–	–	–
Specific risk	–	–	–	–
Commodity risk- trading book	194,950	23,394	217,415	26,090
Options risk	–	–	–	–
Simplified approach	–	–	–	–
Intermediate approach	665,517	79,862	240,071	28,807
Total market risk capital charge	5,652,368	678,284	4,497,079	539,649

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20 EQUITY POSITION IN BANKING BOOKS

	AED'000			
	2015		2014	
	Publicly traded/quoted	Privately held/unquoted	Publicly traded/quoted	Privately held/ unquoted
Equities	144,126	414,069	166,659	378,216
Collective investment schemes	–	–	–	–
Any other investments	–	–	–	–
Total equity position	144,126	414,069	166,659	378,216

	AED'000	
	2015	2014
Realised, unrealised and latent revaluation gains (losses) during the year		
Realised gains (losses) from sales and liquidations	–	14,572
Unrealised gains (losses) recognised in the balance sheet but not through profit and loss account	53,083	44,183
Latent revaluation gains (losses) for investment recorded at cost but not recognised in balance sheet or profit or loss account	–	–
Total	53,083	58,755

	AED'000	
	2015	2014
Items in table above included in Tier 1/Tier 2 capital		
Amount included in Tier 1 capital	–	14,572
Amount included in Tier 2 capital	23,887	19,882
Total	23,887	34,454
Capital requirements by Equity Groupings		
Strategic investments	–	–
Available-for-sale	100,475	98,078
Held-for-trading	–	–
Total Capital Requirement	100,475	98,078

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21 OPERATIONAL RISK

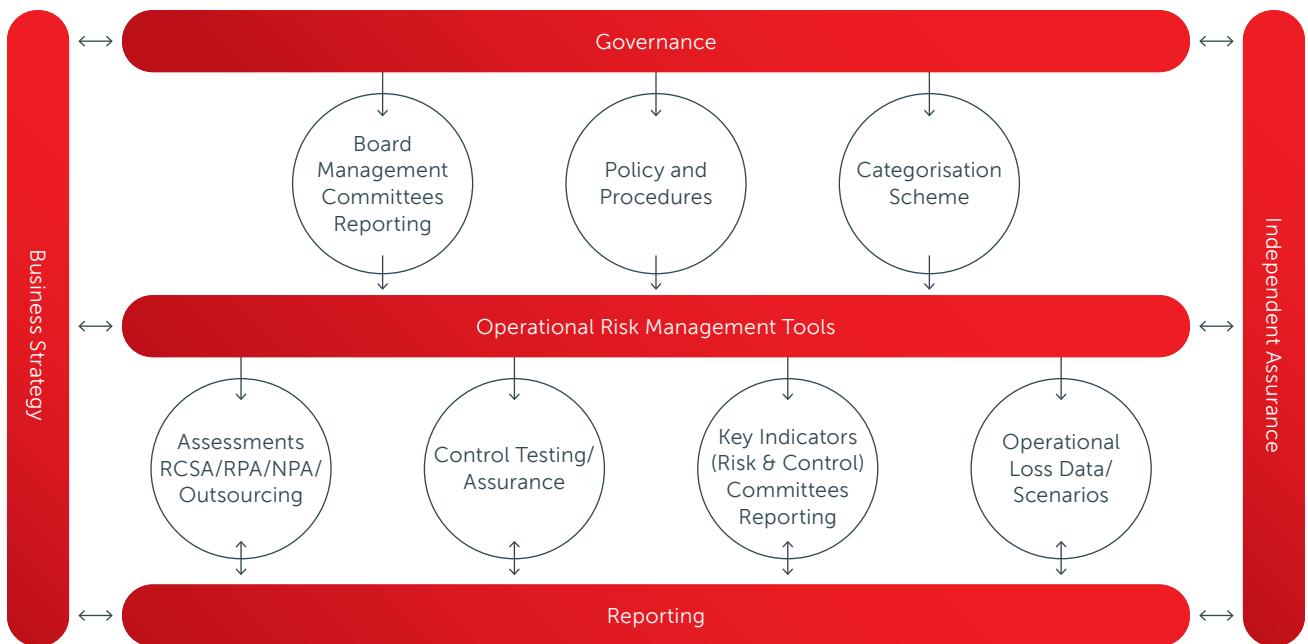
The Bank defines operational risk as “the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events.” Operational risks can expose the Bank to potentially large losses as well. Whilst the Bank cannot eliminate all operational risks, it has developed a comprehensive process of identifying, assessing, controlling, mitigating, monitoring and reporting operational risk.

The ultimate responsibility for Bank-wide operational risk profile, as well as compliance with laws and regulations, rests with the Board of Directors, even though this responsibility has been delegated to the senior management. Ongoing management of operational risk is coordinated by the Operational Risk Management Department (ORMD) and reviewed and controlled by the MRCC and Management Executive Committee (MEC) as applicable for policy purposes.

The operational Risk Governance Framework as shown below is built on a number of elements which allow the Bank to effectively manage and measure its operational risk profile and to calculate the amount of operational risk capital that the Bank needs to hold to absorb potential losses.

The Internal Audit function provides further independent review of the Bank’s operational risk management processes, systems and controls, and reports independently to the Board.

For operational risk measurement, ADCB follows the standardised approach under Basel II. The capital charge for the year ended 31 December 2015 was AED 1,522,728 thousand (2014: AED 1,420,270 thousand).



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Like other risk management disciplines, operational risk management also follows the three lines of defence philosophy:

- ▶ first line of defence (Business Unit)—owns and manages its risks and controls;
- ▶ second line of defence (Operational Risk management)—provides policy, tools and infrastructure to assist business units in managing their risks; and
- ▶ third line of defence (Group Internal Audit)—provides independent assurance on the effectiveness of the risk management process.

RISK IDENTIFICATION, MONITORING AND REPORTING

The risk identification and assessment process involves risk assessment of new initiatives, including new products, new systems and new and material process changes, including outsourcing arrangements. Risk assessment methodology employs more granular and objective assessment of operational risk exposures for material risks identified through the risk identification processes, which enables us to prioritise risks and related actions.

A robust system of controls that is commensurate with the level of operational risks being managed is in place. Since the risk environment is not static, processes are in place for ongoing review of key mitigating controls. This dynamic process helps us to identify gaps early and facilitate timely remedial action for potential risk exposures.

The escalation of issues and events (and therefore greater risk transparency across the organisation) is a critical component of ADCB's operational risk management process. The escalation process was enhanced to ensure that relevant information is received by the decision makers in a timely manner so that appropriate actions are taken.

Monitoring and reporting processes are in place for periodic monitoring of key operational risk data and matrices. The reports are submitted to the BRCC, the MEC and also Group Heads for information and resolution.

FRAUD RISK

Proactive fraud-risk management is a key success factor in combating the increasing number of frauds perpetrated against financial institutions around the globe. ADCB continued to strengthen its anti-fraud activities during the year through an enhanced anti-fraud strategy and a centralised function, which led to the initiation of anti-fraud projects and initiatives aimed at fraud prevention and detection capabilities. The projects are at various levels of maturity.

BUSINESS CONTINUITY MANAGEMENT

The safety of employees and the ability to recover from a crisis in a timely fashion are of utmost importance to ADCB. To appropriately handle crisis situations, emergency response procedures and business continuity plans (BCPs) were significantly enhanced.

ADCB's business continuity framework has been designed to ensure that the Bank can continue to achieve its business objectives in the face of an unexpected disruptive event. The plans identify the teams, and list critical processes and systems, evacuation procedures and the respective recovery sites where the teams will report to in the event of a disaster. Emergency response procedures contain evacuation guidelines, response measures, and roles and responsibilities in dealing with various threats.

The plans are tested periodically and involve mobilising staff from a primary site to a recovery site and enabling them to carry out critical activities.