FIT22
Fund. Invest. Transform

OUR WAY FORWARD

ANNUAL REPORT 2017

RHB

RHB ISLAMIC BANK BERHAD

OUR WAY FORWARD

Having gained tremendous traction and momentum in our transformation journey, our way forward is guided by an enhanced set of strategies that will strengthen our core competencies and drive our performance. To propel our way forward, we have charted a 5-year strategy known as “FIT22” comprising 22 initiatives, driven by three key pillars, namely:

- **F**und our Journey
- **I**nvest to Win
- **T**ransform for Success

Under this strategic plan, our priorities will be to strengthen Malaysia as our core and win in our targeted segments, focus on our niche and strengths overseas while we explore partnerships, and build a winning operating model.

While scale effects are still important, we aim to differentiate ourselves and win through Digital initiatives, customer intimacy and an Agile way of working.

In driving digitalisation, we aim to strengthen our digital capabilities by introducing market-leading features and providing superior customer experiences. Our customers are our priority, therefore we are constantly enhancing our product and service offering to deliver customised innovative solutions. We are adopting the Agile way of working which is a working culture that brings together key resources from multiple disciplines to achieve common goals and to reimagine customer journeys to deliver superior performance by responding to the market faster while increasing productivity customer centricity and new talent acquisition and development.

AGILITY:
MANAGING CHANGE

VALUES

PROFESSIONAL	RESPECT	INTEGRITY	DYNAMIC	EXCELLENCE
We are committed to maintain a high level of proficiency, competency and reliability in all that we do.	We are courteous, humble and we show empathy to everyone through our actions and interactions.	We are honest, ethical and we uphold a high standard of governance.	We are proactive, responsive and forward thinking.	We will continuously achieve high standards of performance and service deliverables.

VISION

To be a Top 3 Bank by Performance

FIT22: Our Way Forward

BRAND PROMISE

Together We Progress

Being your trusted partner

Delivering simple, fast and seamless experiences

Providing solutions that help achieve your goals

Nurturing future generations

CORE BUSINESSES

- Group Retail Banking
- Group Business & Transaction Banking
- Group Wholesale Banking
- Singapore Business Operations
- Group International Business
- Group Insurance
- Group Shariah Business

CONTENTS

ABOUT OUR REPORT

CORPORATE GOVERNANCE

STATUTORY FINANCIAL STATEMENTS

BASEL II PILLAR 3 DISCLOSURES

BRANCH NETWORK

Our Report provides cross-references to our suite of reporting publications:

AR

Annual Report
Our annual report is issued in accordance with the Bursa Main Market Listing requirements.

FR

Financial Report
The financial statements and remuneration report are prepared in accordance with International Financial Reporting Standards, together with the report of the Audit Committee.

PDF Version
These reports are available on our website
www.rhbgroup.com

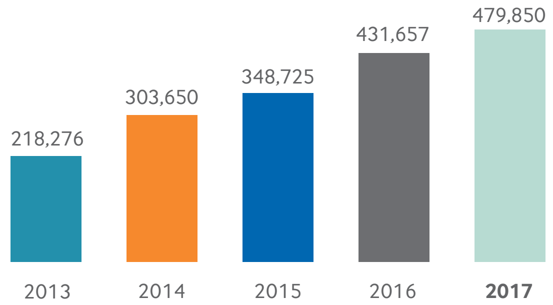
FIVE-YEAR FINANCIAL SUMMARY

	2017	2016	2015	2014	2013
RESULTS					
Operating revenue	**2,508,509**	2,238,504	1,859,681	1,455,197	1,211,922
Profit before zakat and taxation	**479,850**	431,657	348,725	303,650	218,276
Net profit	**367,392**	324,784	254,853	224,315	166,500
STATEMENT OF FINANCIAL POSITION					
Shareholders' equity	**3,311,849**	2,928,442	2,496,407	2,252,397	2,027,132
Total assets	**55,717,463**	48,116,641	44,076,741	36,113,786	29,131,089
Gross financing and advances	**42,975,682**	34,087,124	31,124,322	25,503,231	18,721,218
Total deposits [N1]	**50,347,704**	42,472,593	39,589,255	31,770,545	25,461,734
FINANCIAL RATIOS					
Net return on average equity (%)	**11.77**	11.97	10.73	10.48	8.95
Net return on average assets (%)	**0.71**	0.70	0.64	0.69	0.61
Common Equity Tier I Capital Ratio (%)	**10.376**	10.868	11.041	12.875	13.864
Tier I Capital Ratio (%)	**10.376**	10.868	11.041	12.875	13.864
Total Capital Ratio (%)	**14.134**	14.002	14.608	16.336	14.424

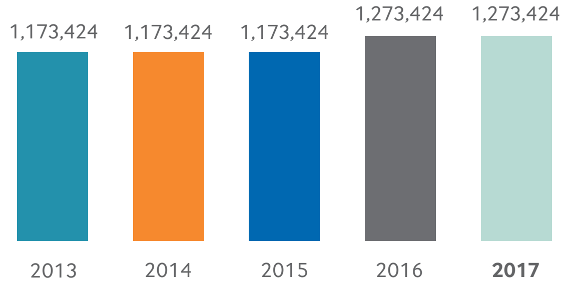
N1: Inclusive of deposits from customers, deposits and placements of banks and other financial institutions and investment account due to designated financial institutions.

SUMMARY FIVE-YEAR GROWTH

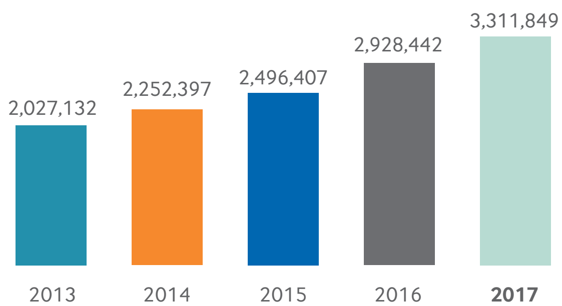
Profit Before Zakat and Taxation (RM'000)



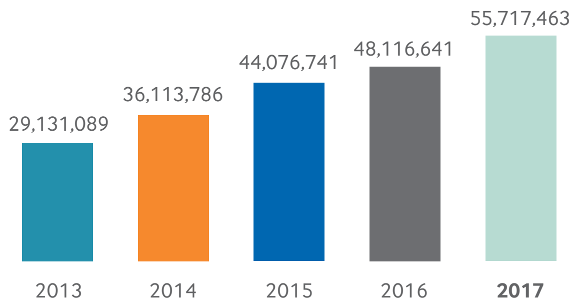
Share Capital (RM'000)



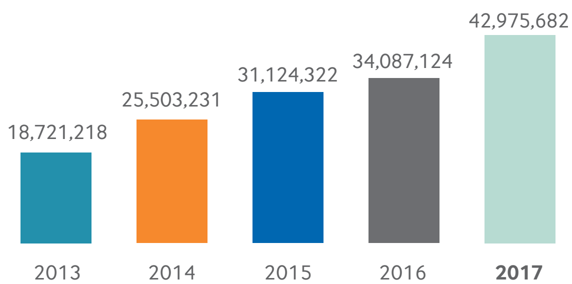
Shareholders' Equity (RM'000)



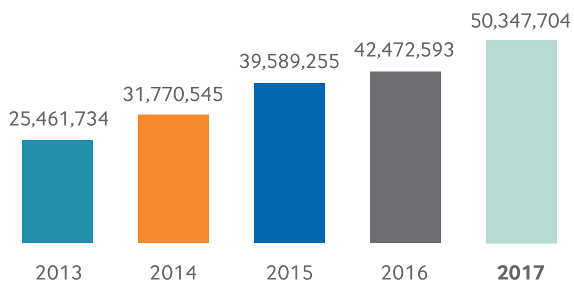
Total Assets (RM'000)



Gross Financing and Advances (RM'000)



Total Deposits (RM'000) N1



N1: Inclusive of deposits from customers, deposits and placements of banks and other financial institutions and investment account due to designated financial institutions.

CORPORATE INFORMATION
AS AT 15 FEBRUARY 2018

BOARD OF DIRECTORS

01 **Dato' Abd Rahman Dato' Md Khalid**
Senior Independent
Non-Executive Director

02 **Datuk Haji Faisal Siraj**
Non-Independent
Non-Executive Director

03 **Dato' Foong Chee Meng**
Independent
Non-Executive Director

04 **Ong Ai Lin**
Independent
Non-Executive Director

05 **Dato' Adissadikin Ali**
Chief Executive Officer/
Managing Director

BOARD RISK COMMITTEE#

Tan Sri Saw Choo Boon
Senior Independent
Non-Executive Director/Chairman

Patrick Chin Yoke Chung
Non-Independent
Non-Executive Director

Chin Yoong Kheong
Independent
Non-Executive Director

Ong Ai Lin
Independent
Non-Executive Director

BOARD NOMINATING & REMUNERATION COMMITTEE#

Tan Sri Saw Choo Boon
Senior Independent
Non-Executive Director/Chairman

Tan Sri Azlan Zainol
Non-Independent
Non-Executive Director

Tan Sri Ong Leong Huat @ Wong Joo Hwa
Non-Independent
Non-Executive Director

Ong Ai Lin
Independent
Non-Executive Director

Tan Sri Dr Rebecca Fatima Sta Maria
Independent
Non-Executive Director

BOARD AUDIT COMMITTEE#

Tan Sri Dr Rebecca Fatima Sta Maria
Independent
Non-Executive Director/Chairman

Tan Sri Saw Choo Boon
Senior Independent
Non-Executive Director

Ong Ai Lin
Independent
Non-Executive Director

BOARD CREDIT COMMITTEE#

Patrick Chin Yoke Chung
Non-Independent
Non-Executive Director/Chairman

Tan Sri Ong Leong Huat @ Wong Joo Hwa
Non-Independent
Non-Executive Director

Dato' Abd Rahman Dato' Md Khalid
Senior Independent
Non-Executive Director

Note:
The Committee is shared with the relevant subsidiaries of the Group.

ISLAMIC RISK MANAGEMENT COMMITTEE^

Dato' Abd Rahman Dato' Md Khalid
Senior Independent
Non-Executive Director/Chairman

Dato' Foong Chee Meng
Independent
Non-Executive Director

Ong Ai Lin
Independent
Non-Executive Director

SHARIAH COMMITTEE^

Dr. Ghazali Jaapar *(Chairman)*

Assoc. Prof. Dr. Amir Shaharuddin

Wan Abdul Rahim Kamil Wan Mohamed Ali

Mohd Fadhly Md Yusoff

Shabnam Mohamad Mokhtar

Note:
^ The Committee resides at RHB Islamic Bank Berhad.

GROUP SENIOR MANAGEMENT & GROUP INTERNAL AUDIT

Dato' Khairussaleh Ramli
Group Managing Director/
Chief Executive Officer

Syed Ahmad Taufik Albar
Group Chief Financial Officer

Dato' Adissadikin Ali
Managing Director/Chief Executive Officer – RHB Islamic Bank Berhad

Robert Huray
Chief Executive Officer,
RHB Investment Bank Berhad/
Head, Group Investment Banking

Nazri Othman
Acting Head, Group Retail Banking

Jeffrey Ng Eow Oo
Head, Group Business & Transaction Banking

Mike Chan Cheong Yuen
Country Head and
Chief Executive Officer,
RHB Bank Singapore

Kong Shu Yin
Managing Director,
RHB Insurance Berhad

Mohd Rashid Mohamad
Group Treasurer

Rohan Krishnalingam
Group Chief Operations Officer

Gan Pai Li
Group Chief Strategy Officer

Patrick Ho Kwong Hoong
Group Chief Risk Officer

Jamaluddin Bakri
Group Chief Human Resource Officer

Norazzah Sulaiman
Group Chief Communications Officer/
Chief Executive Officer, RHB Foundation

Abdul Sani Abdul Murad
Group Chief Marketing Officer

Alex Tan Aun Aun
Group Chief Internal Auditor

COMPANY SECRETARIES

Azman Shah Md Yaman
(LS 0006901)

Ivy Chin So Ching
(MAICSA No. 7028292)

REGISTERED OFFICE

Level 9, Tower One
RHB Centre, Jalan Tun Razak
50400 Kuala Lumpur
Tel : 603 9287 8888
Fax : 603 9281 9314
Website : www.rhbgroup.com

COMPANY NO.

680329-V

AUDITORS

PricewaterhouseCoopers PLT
Chartered Accountants
Level 10, 1 Sentral
Jalan Rakyat, Kuala Lumpur Sentral
50470 Kuala Lumpur
P. O. Box 10192, 50706 Kuala Lumpur
Tel : 603 2173 1188
Fax : 603 2173 1288

SHARE REGISTRAR

Symphony Share Registrars Sdn Bhd
Level 6, Symphony House
Pusat Dagangan Dana 1
Jalan PJU 1A/46
47301 Petaling Jaya, Selangor
Tel : 603 7849 0777
Fax : 603 7841 8151/8152

CUSTOMER CARE CENTRE

Call Centre : 603 9206 8118
(Peninsular Malaysia – 24 hours)

6082 276 118
(Sabah & Sarawak – 7 a.m. to 7 p.m.)

GROUP CORPORATE STRUCTURE

AS AT 15 FEBRUARY 2018

RHB Bank Berhad

COMMERCIAL BANKING GROUP

- 100.00% RHB Islamic Bank Berhad
- 100.00% RHB Bank (L) Ltd
  - 100.00% RHB International Trust (L) Ltd
    - 100.00% RHB Corporate Services Sdn Bhd
- 100.00% RHB Leasing Sdn Bhd
- 100.00% RHB Capital Nominees (Tempatan) Sdn Bhd
  - 100.00% RHB Capital Nominees (Asing) Sdn Bhd
- 100.00% RHB Capital Properties Sdn Bhd
- 100.00% Utama Assets Sdn Bhd
- 100.00% RHB Bank Nominees Pte Ltd (Singapore)
- 100.00% Banfora Pte Ltd (Singapore)
- 100.00% RHB Investment Ltd (Singapore)
- 100.00% RHB Trade Services Limited (Hong Kong)
- 100.00% Utama Gilang Sdn Bhd(3)
- 100.00% UMBC Sdn Bhd*
- 100.00% RHB Delta Sdn Bhd(3)
- 100.00% RHB Indochina Bank Limited
- 100.00% RHB Bank Lao Limited

INVESTMENT BANKING GROUP

100.00% RHB Investment Bank Berhad

- 100.00% RHB International Investments Pte Ltd
  - 100.00% RHB Asset Management Pte Ltd
    - 40.00% RHB GC-Millennium Capital Pte Ltd(5)
- 100.00% RHB Hong Kong Limited
  - 100.00% RHB Securities Hong Kong Limited
  - 100.00% RHB Futures Hong Kong Limited
  - 100.00% RHB Finance Hong Kong Limited
  - 100.00% RHB Capital Hong Kong Limited
  - 100.00% RHB Fundamental Capital Hong Kong Limited
  - 100.00% RHB Asset Management Limited
  - 100.00% RHB Wealth Management Hong Kong Limited
  - 100.00% RHB (China) Investment Advisory Co Ltd
- 99.00% PT RHB Sekuritas Indonesia
  - 99.62% PT RHB Asset Management Indonesia
- 100.00% RHB Securities Singapore Pte Ltd
  - 100.00% RHB Nominees Singapore Pte Ltd#
  - 100.00% Summit Nominees Pte Ltd#
  - 100.00% RHB Research Institute Singapore Pte Ltd
- 99.95% RHB Securities (Thailand) Public Company Limited
- 100.00% RHB Indochina Securities Plc.

94.70% RHB Insurance Berhad

- 100.00% RHB Futures and Options Sdn Bhd*
- 100.00% RHB Research Sdn Bhd[7]
- 100.00% RHB International Asset Management Sdn Bhd*
- 100.00% RHBIB Nominees (Tempatan) Sdn Berhad[7]
- 100.00% RHBIB Nominees (Asing) Sdn Berhad[7]
- 100.00% TCL Nominees (Tempatan) Sdn Bhd[7]
- 100.00% TCL Nominees (Asing) Sdn Bhd[7]
- 100.00% KE-ZAN Nominees (Tempatan) Sdn Bhd[7]
- 100.00% KE-ZAN Nominees (Asing) Sdn Bhd[7]
- 80.00% RHB Trustees Berhad[6] 20.00%
- 80.00% Malaysian Trustees Berhad[6] 20.00%
- 100.00% RHBIM Berhad*
- 100.00% RHB Asset Management Sdn Bhd
  - 100.00% RHB Islamic International Asset Management Berhad
  - 100.00% RHB Islamic Asset Management Sdn Bhd*
- 100.00% RHB Research Institute Sdn Bhd
- 100.00% RHB Merchant Nominees (Tempatan) Sdn Bhd
  - 100.00% RHB Merchant Nominees (Asing) Sdn Bhd
- 100.00% RHB Nominees Sdn Bhd
- 100.00% RHB Nominees (Tempatan) Sdn Bhd
- 100.00% RHB Nominees (Asing) Sdn Bhd
- 100.00% RHB Excel Sdn Bhd[4]
- 100.00% RHB Progressive Sdn Bhd[4]
- 100.00% RHB Marketing Services Sdn Bhd[3]
- 100.00% RHB Unit Trust Management Berhad[4]
- 100.00% RHB Private Equity Holdings Sdn Bhd
  - 100.00% RHB Private Equity Management Ltd
  - 100.00% RHB Private Equity Fund Ltd (Cayman Islands)

- 40.05% RHB Finexasia.Com Sdn Bhd 59.95%
  - 100.00% RHB Stock 188.Com Sdn Bhd*
- 49.00% Vietnam Securities Corporation[5]

OTHERS

- 100.00% RHB Equities Sdn Bhd[1]
  - 100.00% KYB Sdn Bhd[4]
- 100.00% RHB Capital (Jersey) Limited
  - 100.00% RHB (Philippines) Inc[2]*
- 100.00% RHB Property Management Sdn Bhd
- 100.00% RHBF Sdn Bhd*
- 100.00% RHB Kawal Sdn Bhd

Notes:

* Dormant Company
# Inactive
(1) With effect from 1 July 2001, the company's activities relate primarily to recovery of outstanding debts.
(2) The company has ceased operations from the close of business on 10 December 2001.
(3) The company has commenced members' voluntary winding-up on 16 February 2011.
(4) The company has commenced members' voluntary winding-up on 28 March 2012.
(5) Jointly controlled entity.
(6) Held by: (i) RHB Investment Bank Berhad; (ii) RHB Nominees (Tempatan) Sdn Bhd; (iii) RHB Nominees (Asing) Sdn Bhd; (iv) RHB Futures and Options Sdn Bhd; and (v) RHB Bank Berhad with direct shareholdings of 20.00% each.
(7) The company has commenced members' voluntary winding-up on 30 June 2017.

PROFILE OF THE SHARIAH COMMITTEE

DR. GHAZALI BIN JAAPAR
Chairman,
RHB Islamic Bank Berhad
Age 47, Male, Malaysian

Date Appointed: 01 April 2011
Date of Last Re-appointment: 01 April 2017
Number of Shariah Committee Meetings Attended in the Financial Year: 10/10

Qualifications

- B.A. Shariah (Hons.), University of Malaya, Kuala Lumpur
- Master of Comparative Law, International Islamic University Malaysia, Kuala Lumpur
- Ph.D. Islamic Jurisprudence, University of Birmingham, United Kingdom

Area of Expertise

- Islamic Legal System
- Principles of Islamic Jurisprudence (*Usul al-Fiqh*)
- Islamic Law of Transaction (*Fiqh al-Mu'amalat*)
- Islamic Legal Maxims (*Qawaid Fiqhiyyah*)
- Shariah-oriented policy (*Siyasah Shar'iyyah*)

Shariah Committee Membership in Other Institutions

- HSBC Amanah Takaful

Experience & Achievements

- Currently serving as Assistant Professor of Ahmad Ibrahim Kulliyyah of Laws (AIKOL), International Islamic University Malaysia (IIUM).
- Prior to that, he was the Director of Harun M. Hashim Law Centre, IIUM.
- Started his career as a lecturer at AIKOL IIUM in 2007 and is still attached with the university, teaching several subjects including Islamic Legal System and *Usul al-Fiqh* for LLB course (Undergraduate), *Siyasah Syar'iyyah* for LLM (Administration of Islamic Law) students and Islamic Legal Maxims for Certificate in Islamic Law (Bank Negara Malaysia and Standard & Chartered).
- He has written numerous journals and articles and participated in various workshops, seminars and conferences on Islamic finance locally and abroad.

ASSOC. PROF. DR. AMIR BIN SHAHARUDDIN
Member,
RHB Islamic Bank Berhad
Age 40, Male, Malaysian

Date Appointed: 01 April 2011
Date of Last Re-appointment: 01 April 2017
Number of Shariah Committee Meetings Attended in the Financial Year: 10/10

Qualifications

- B.A. Shariah (Hons), Al-Azhar University, Egypt
- Master of Business Administration in Islamic Banking & Finance, International Islamic University Malaysia, Kuala Lumpur
- Ph.D. in Islamic Studies, University of Exeter, United Kingdom

Area of Expertise

- Islamic Banking & Finance
- Islamic Law Principles of Islamic Jurisprudence (*Usul al-Fiqh*)
- Islamic Legal Maxims
- *Siyasah Shar'iyyah* (Shariah-oriented policy)
- Zakat

Shariah Committee Membership in Other Institutions

- Malaysian Airport Consultancy Berhad
- Malaysian Electronic Payment System (MEPS)

Experience & Achievements

- Presently the Dean of Economic and Muamalat Faculty, Universiti Sains Islam Malaysia (USIM) since December 2013.
- The first recipient of "Scholar of Residence in Islamic Finance Award", jointly initiated by Malaysia Securities Commission and Oxford Centre for Islamic Studies (OCIS).
- Published numerous articles in journals including Journal of Muamalat and Islamic Finance Research, Arab Law Quarterly and ISRA International Journal of Islamic Finance.
- Wrote articles in Islamic Banking & Finance, Zakat, Principles of Islamic Jurisprudence (*Usul al-Fiqh*), Islamic Legal Maxims and *Siyasah Shar'iyyah* (Shariah-oriented policy) for forums and seminars.
- Presented academic papers in various international seminars in Indonesia, Bahrain, United Kingdom and Italy.

WAN ABDUL RAHIM KAMIL BIN WAN MOHAMED ALI
Member,
RHB Islamic Bank Berhad
Age 69, Male, Malaysian

Date Appointed: 13 April 2013
Date of Last Re-appointment: 01 April 2017
Number of Shariah Committee Meetings Attended in the Financial Year: 9/10

Qualifications

- Professional Member, Institute of Statisticians, United Kingdom
- Post Graduate Degree in Islamic Banking & Economics, International Institute of Islamic Banking & Economics, Turkish Cyprus (in association with Al Azhar University, Cairo)

Area of Expertise

- Islamic Banking & Finance
- Islamic Capital Market
- Debt Capital Market
- Corporate Advisory

Experience & Achievements

- Pioneered the development of Islamic Capital Market in Malaysia and has innovated development of several benchmark capital market securities through securitisation of Islamic contracts.
- Islamic Capital Market consultant, regular trainer and speaker for various seminars and in-house training workshops organised by the World Bank, Bank Negara Malaysia (BNM), Securities Industries Development Corporation (SIDC), Islamic Banking and Finance Institute Malaysia (IBFIM) and other event organisers, both locally and internationally.
- Recently awarded "Most Oustanding Individual Contribution to Islamic Finance" at Kuala Lumpur Islamic Finance Forum 2017.
- Awarded "Outstanding Leadership in Islamic Finance" by London Sukuk 2011 organised by ICG Events and UK Trade and Industry Ministry, United Kingdom.
- Member of Task Force on Islamic Banking and Takaful for Labuan Offshore Financial Services Authority (LOFSA) Malaysia, Islamic Capital Markets Working Group (ICMWG) of Securities Commission Malaysia and represented LOFSA in Market & Product Development Committee under International Islamic Financial Market (IIFM), Bahrain.

MOHD FADHLY BIN MD. YUSOFF
Member,
RHB Islamic Bank Berhad
Age 47, Male, Malaysian

Date Appointed: 13 April 2013
Date of Last Re-appointment: 01 April 2017
Number of Shariah Committee Meetings Attended in the Financial Year: 10/10

Qualifications

- Bachelor of Syariah (1st Class Honours) from University of Malaya

Area of Expertise

- Islamic Banking & Finance
- Islamic Capital Market & Derivatives

Shariah Committee Membership in Other Institutions

- Sun Life Malaysia Takaful Bhd
- Opus Asset Management Sdn Bhd
- Apex Investment Services Berhad
- Universiti Tenaga Nasional
- National Farmers Organization (NAFAS)

Experience & Achievements

- 1995 – 2008: Manager at Islamic Capital Market Department of Securities Commission Malaysia where he was involved in Shariah compliance supervision in relation to submissions for the issuances of Sukuk, structured products, collective investment schemes and Islamic Real Estate Investment Trusts (REITs).
- Undertook in-depth research for the development of new Islamic Capital Market instruments and provided technical inputs for the preparation of various guidelines issued by Securities Commission Malaysia.
- Actively participated in various industry development initiatives namely the International Organization of Securities Commission (IOSCO) Task Force on Islamic Capital Market, Islamic Financial Services Board's (IFSB) Governance of Islamic Investment Funds Working Group, technical member for the publication of *Resolutions of the Securities Commission Shariah Advisory Council* and Islamic Capital Market educational and promotional programs.

SHABNAM BINTI MOHAMAD MOKHTAR
Member,
RHB Islamic Bank Berhad
Age 40, Female, Malaysian

Date Appointed: 01 May 2015
Date of Last Re-appointment: 01 April 2017
Number of Shariah Committee Meetings Attended in the Financial Year: 10/10

Qualifications

- Bachelor of Accountancy, University Putra Malaysia
- Master of Accounting, University of Illinois, Urbana-Champaign, U.S.A

Area of Expertise

- Finance & Islamic Finance
- Accounting & Islamic Accounting
- Islamic Capital Market & Derivatives

Experience & Achievements

- Presently the Vice President of SHAPE® Knowledge Services; an Islamic finance consulting firm based in Kuwait.
- Spearheads research and development activities including financial analysis, strategic & business plan formulation, design and implementation of customised survey, research and training for different customers at SHAPE®.
- Formerly headed the capital markets research for International Shariah Research Academy (ISRA), an institution established by the Central Bank of Malaysia.
- Conducted various training programs on Islamic banking, sukuk & Islamic capital market products, risk management and financial reporting for customers in ASEAN region, Gulf Cooperation Council (GCC) and European market.
- Contributed chapters in Housing the Nation (Cagamas 2013), Managing Fund Flows, Risks and Derivatives: Applications in Islamic Institutions (Sweet & Maxwell 2012), Islamic Financial System: Principles & Operations Market (ISRA, 2011), Sukuk (Sweet & Maxwell 2009), and Partnership Accounting, Principles and Practice (McGraw Hill).
- 2010 – 2014: Member of Shariah Advisory Panel of Malaysian Ratings Corporation (MARC).

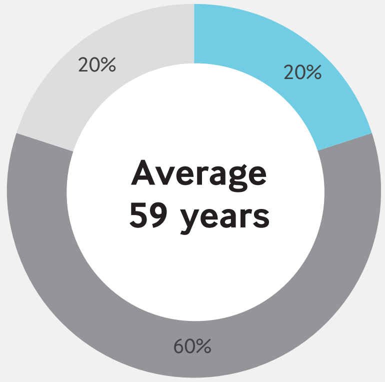
BOARD DIVERSITY

The diversity and skills of the Board ensure that RHB Islamic Bank Berhad is steered to deliver growth to all our stakeholders.

BOARD COMPOSITION

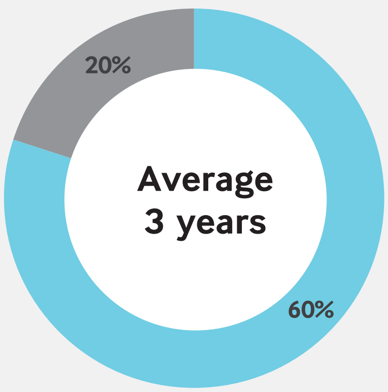
Independent Non-Executive Directors	2
Non-Independent Non-Executive Directors	1
Senior Independent Non-Executive Director	1
Chief Executive Officer/ Managing Director	1

AGE



66 years & above	1
51 years – 65 years	3
50 years & below	1

BOARD TENURE



Below 5 years	4
More than 9 years	1

GENDER

Male	4
Female	1

ETHNICITY

Malay	3
Chinese	2

NATIONALITY

Malaysians	5

KEY FEATURES OF OUR BOARD

- The Board comprises majority Independent Directors
- The position of Chairman has been left vacant since the demise of the late Chairman, Tuan Haji Md Ja'far Abdul Carrim on 19 October 2017
- The roles of the Chairman and the Managing Director are distinct

PROFILE OF THE BOARD OF DIRECTORS

AS AT 15 FEBRUARY 2018

DATO' ABD RAHMAN DATO' MD KHALID

Senior Independent
Non-Executive Director

Malaysian | Age 62

Date of Appointment:
2 January 2017

Length of Service:
1 year and 1 month

Date of Last Re-Election:
25 April 2017

Board Committee Memberships:
- Board Credit Committee

Directorship in Other Public Companies:
Listed Entities:
- Nil

Public Companies:
- Nil

No. of Board Meetings Attended in the Financial Year:
- 14/14

Qualifications:
- Diploma in Business Studies from Mara Institute of Technology

Skills and Experience:
Dato' Abd Rahman started his career with Maybank Group, and held various positions within the Group, most notably, the position of Chief Executive Officer/ President Director for PT Bank Maybank Nusa International. His last position with the Maybank Group was as the Chief Credit Officer.

Prior to joining RHB Banking Group, he was the Group Managing Director for Amanah Raya Berhad overseeing the various businesses and operations of Amanah Raya Berhad and its subsidiaries.

Dato' Abd Rahman has extensive experience in banking specifically on Credit Management. He has attended various courses and programmes commensurate with his knowledge and experience. He also has attended a Mandatory Accreditation Programme for Directors of Public Listed Companies.

Declaration:
- Conflict of interest with the company: Nil
- Family relationship with any director and/or major shareholder: Nil
- List of conviction for offences within the past 5 years: Nil
- Particulars of any public sanction or penalty imposed by the relevant bodies during the financial year: Nil

DATUK HAJI FAISAL SIRAJ

Non-Independent
Non-Executive Director

Malaysian | Age 72

Date of Appointment:
3 December 2007

Length of Service:
10 years 2 months

Date of Last Re-Election:
11 May 2016

Board Committee Memberships:
- Islamic Risk Management Committee

Directorship in Other Public Companies:
Listed Entities:
- Nil

Public Companies:
- RHB Insurance Berhad
- RHB Capital Berhad (in Members' Voluntary Winding Up)

No. of Board Meetings Attended in the Financial Year:
- 13/14

Qualifications:
- Fellow of the Institute of Chartered Accountants in England & Wales.
- Member of the Malaysian Institute of Accountants.
- Member of the Malaysian Institute of Certified Public Accountants.

Skills and Experience:
Datuk Faisal started his career in 1968 with KPMG, London. On his transfer from KPMG, London to KPMG, Kuala Lumpur, he was posted to KPMG Kota Kinabalu until 1976. Datuk Faisal joined the Malaysia Mining Corporation ("MMC") Group in 1976. He was the Group Executive Director and a Board member of MMC from 1981 to 1994. In 1995, he joined DRB-HICOM Berhad ("DRB-HICOM") as the Group Chief Financial Officer in the capacity of Senior Group Director, Financial Services and Treasury Division and was also a Board member of DRB-HICOM, before his retirement in 2005.

Declaration:
- Conflict of interest with the company: Nil
- Family relationship with any director and/or major shareholder: Nil
- List of conviction for offences within the past 5 years: Nil
- Particulars of any public sanction or penalty imposed by the relevant bodies during the financial year: Nil

DATO' FOONG CHEE MENG

Independent
Non-Executive Director

Malaysian | Age 51

Date of Appointment:
1 August 2017

Length of Service:
7 months

Date of Last Re-Election:
Not Applicable

Board Committee Memberships:
- Nil

Directorship in Other Public Companies:
Listed Entities:
- Matang Berhad
- Kumpulan Jetson Berhad

Public Companies:
- Nil

No. of Board Meetings Attended in the Financial Year:
- 6/6

Qualifications:
- Master of Law from University of Sydney, Australia
- Bachelor of Laws (Hons) from University of Sydney, Australia
- Bachelor of Economics from University of Sydney, Australia

Skills and Experience:
Dato' Foong has more than 25 years of experience in legal practice and is currently a Managing Partner of a niche corporate boutique law firm, Foong & Partners which he set up in 2003. Aside from being an Advocate & Solicitor at High Court of Malaya, he is also a practicing Advocate & Solicitor at the Federal Court of Australia and Supreme Court of New South Wales, Australia.

Dato' Foong has been involved in structuring and executing major mergers and acquisitions, strategic alliances and joint ventures in various industry groups which comprise manufacturing, property, construction, telecommunications, food and newsprint industries.

He also advises local and foreign companies and investors on a wide variety of corporate matters including foreign investments, regulatory compliance, joint ventures and acquisitions of Malaysian businesses.

Declaration:
- Conflict of interest with the company: Nil
- Family relationship with any director and/or major shareholder: Nil
- List of conviction for offences within the past 5 years: Nil
- Particulars of any public sanction or penalty imposed by the relevant bodies during the financial year: Nil

ONG AI LIN

Independent
Non-Executive Director

Malaysian | Age 62

Date of Appointment:
1 September 2017

Length of Service:
6 months

Date of Last Re-Election:
Not Applicable

Board Committee Memberships:
- Board Nominating and Remuneration Committee
- Board Risk Committee
- Board Audit Committee

Directorship in Other Public Companies:
Listed Entities:
- RHB Bank Berhad

Public Companies:
- Nil

No. of Board Meetings Attended in the Financial Year:
- 5/5

Qualifications:
- Qualified Auditor, Digital Signature Act 1997 from Suruhanjaya Komunikasi dan Multimedia Malaysia
- Certified Business Continuity Professional from Disaster Recovery Institute, United States of America
- Certified Information System Auditor from Information Systems Audit and Control Association, United States of America
- Member of The Malaysian Institute of Accountants, Malaysia
- Associate of The Institute of Chartered Accountants, England & Wales
- Bachelor of Arts (Honours) in Economics from University of Leeds, United Kingdom

Skills and Experience:
Ms Ong began her career with Deloitte Haskins & Sells (DH&S) in London in 1978, prior to joining PricewaterhouseCoopers ("PwC") in 1991 as Senior Manager. At PwC, she built the IT audit practice, an integral part of the firm's financial audit services. She was then appointed as Partner/Senior Executive Director of PwC in 1993 and was the Business Continuity Management and Information Security Practice Leader for PwC Malaysia.

Ms Ong has over 30 years of experience in providing Business Continuity Management, Information Security, Cybersecurity, Technology Risk and Governance, and Data Privacy services in the United Kingdom, Singapore, Indonesia, Thailand, Vietnam, Philippines, Sri Lanka, Cambodia, and Malaysia.

Declaration:
- Conflict of interest with the company: Nil
- Family relationship with any director and/or major shareholder: Nil
- List of conviction for offences within the past 5 years: Nil
- Particulars of any public sanction or penalty imposed by the relevant bodies during the financial year: Nil

DATO' ADISSADIKIN ALI

Chief Executive Officer/
Managing Director

Malaysian | Age 47

Date of Appointment:
1 August 2016

Length of Service:
6 months

Date of Last Re-Election:
25 April 2017

Board Committee Memberships:
- Nil

Directorship in Other Public Companies:
Listed Entities:
- Nil

Public Companies:
- Nil

No. of Board Meetings Attended in the Financial Year:
- 13/14

Qualifications:
- Chartered Banker from The Asian Institute of Chartered Banker
- Advanced Management Program of Harvard Business School
- Master of Business Administration (Finance) from University Malaya
- Bachelor of Business (Banking & Finance) from Monash University, Melbourne, Australia
- Diploma in Investment Analysis from Universiti Teknologi Mara

Skills and Experience:
He started his career with the Renong Group of Companies in various positions within the Group. In 1999, he joined Pengurusan Danaharta Nasional Berhad for 4 years. Subsequently, Dato' Adissadikin joined Bank Muamalat Malaysia Berhad as Special Assistant to the Chief Executive Officer. Thereon, Dato' Adissadikin accumulated experience in formulating and executing corporate strategic plan, business process re-engineering as well as bank-wide transformation programme. Dato' Adissadikin was involved in the turn-around of Bank Islam Malaysia Berhad.

He was appointed the President/Chief Executive Officer of Export-Import Bank of Malaysia (EXIM) in October 2010 and served until June 2015. Prior to joining RHB Banking Group in August 2016, he was the Chief Executive Officer at Alkhair International Islamic Bank Berhad, the first foreign Islamic Bank in Malaysia.

Declaration:
- Conflict of interest with the company: Nil
- Family relationship with any director and/or major shareholder: Nil
- List of conviction for offences within the past 5 years: Nil
- Particulars of any public sanction or penalty imposed by the relevant bodies during the financial year: Nil

Note: *Tuan Haji Md Ja'far Abdul Carrim, the Chairman of RHB Islamic Bank Berhad, passed away on 19 October 2017. With his demise, RHB Islamic Bank Berhad's Senior Independent Non-Executive Director, YBhg Dato' Abd Rahman Dato' Md Khalid has been appointed to chair RHB Islamic Bank Berhad's Board meetings pending the appointment of a new Chairman for RHB Islamic Bank Berhad.*

STATEMENT ON CORPORATE GOVERNANCE

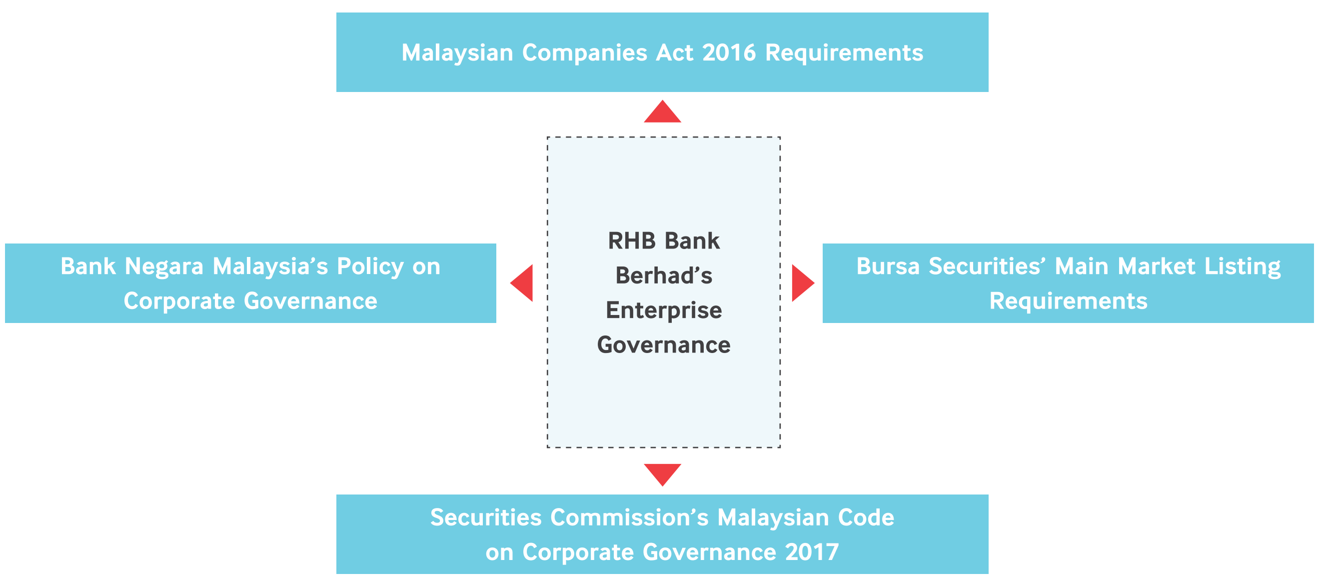
"In these times, moral courage, integrity and transparency will be more important than ever. We must be brave enough to pursue the right course of action, doing the right thing, unpopular as they may be in the short-term. We must also be accountable for our decisions. This requires that we engage and communicate with the public as never before... It is also important that we foster a culture and environment that prioritises these values at the level of the individual... This will require leadership, incentives and structures that will enable individuals to be clear-eyed and independent-minded... Integrity is best demonstrated through the transparency and thoroughness of disclosures. The publication of financial and non-financial information is the central means by which the public can truly hold... institutions to account".

– Bank Negara Malaysia's Governor Tan Sri Muhammad Ibrahim's Remarks
at the National PSA Conference 2017 on 15 August 2017

ENTERPRISE GOVERNANCE

The Board of RHB Islamic Bank Berhad ("RHBIB" or "Company") fully supports adoption of best practices in good corporate governance beyond regulatory requirements. RHBIB, recognises that enterprise governance, which is a balancing act of steering the Group's performance while it conforms to best compliance practices, whether in accordance with mandatory or voluntary requirements, is fundamental in strengthening and ensuring long-term sustainability of the Group.

The Company continuously strives to stimulate and sustain value creation by subscribing to the principles set out in the following essential requirements and practices:



CORPORATE GOVERNANCE – *Commitment to Conformance*

RHBIB is fully committed to protect the interests of all its stakeholders by conforming to good corporate governance practices, including greater transparency and sustainable disclosure. This commitment is translated into a corporate culture and manifested across the Group, from the Board of Directors, to the Senior Management and all the Employees. A dedicated Business Risk and Compliance Officer is appointed in each respective business, functional units and branches to propagate and ensure a high standard of compliance to all regulatory and internal requirements. This control function is part of the Group's enterprise risk management framework.

The continuous enhancement in the Company's corporate governance practices has borne significant results in the way that the Group operates. Emphasis placed by the Board of Directors on its fiduciary duty as guardian of public deposits, customers' investments and account holders' policies, through sustainable boardroom scrutiny, decision-making and directives have gained the trust of the stakeholders and in return, built lasting commercial relationships with the its business partners. These efforts were recognised by reputable and independent third parties' assessments which have currently positioned the holding company among the **Top 6** of Malaysian Public Listed Companies ("PLCs") and **Top 50** of Association of Southeast Asian Nations ("ASEAN") Public Listed Companies, in terms of quality disclosures and scope of corporate governance practices.

During 2017, the Group also received the following recognitions:

- Winner of **'Excellence Award for Corporate Governance Disclosure'** in the MSWG-ASEAN Corporate Governance Recognition 2017 hosted by the Minority Shareholder Watchdog Group on 6 December 2017
- **Constituent of the FTSE4Good Bursa Malaysia Index** for good demonstration of Environmental, Social & Governance (E.S.G.) practices as independently assessed by FTSE Russell during 2017 semi-annual reviews
- Winner of **'Merit Award for Board Diversity'** in the MSWG-ASEAN Corporate Governance Recognition 2017 hosted by the Minority Shareholder Watchdog Group on 6 December 2017
- Winner of **'Merit Award: Finalist'** in the National Annual Corporate Report Awards (NACRA) 2017 hosted by the Malaysian Institute of Certified Public Accountants (MICPA), the Malaysian Institute of Accountants (MIA) & Bursa Malaysia on 23 November 2017
- Winner of **'Merit Award for Most Improved Corporate Governance Disclosure'** in the MSWG-ASEAN Corporate Governance Recognition 2017 hosted by the Minority Shareholder Watchdog Group on 6 December 2017
- Joint Gold Winner of **'Best Governed & Most Transparent Award'** in The Global Good Governance Awards 2017 hosted by The Pinnacle Group International on 30 March 2017 (2016: Silver Winner)
- Ranked **11th** among Malaysia's Top 100 Public Listed Companies in terms of **Transparency in Corporate Reporting** as accorded by the Malaysian Institute of Corporate Governance (MICG) on 8 August 2017. The assessment mainly covers on 3 dimensions, namely *Anti-Corruption Programme (40%), Organisational Transparency (30%) and Sustainability (30%).*

Excellence in **corporate governance** is central to promoting the Company's financial services in the areas where it operates. This compliance culture fosters the Group's Directors, Senior Management and the rest of the Employees to embrace professional business ethics and be self-adherent to internal and external requirements.

MSWG - ASEAN
CORPORATE GOVERNANCE RECOGNITION
2017

FTSE4Good

2016

- Enlisted on the FTSE4Good Bursa Malaysia Index for demonstrating good Environmental, Social and Governance (ESG) practices beyond threshold limit

"FTSE Russell (the trading name of FTSE International Limited and Frank Russell Company) confirms that RHB Bank has been independently assessed according to the FTSE4Good criteria, and has satisfied the requirements to become a constituent of the FTSE4Good Index Series. Created by the global index provider FTSE Russell, the FTSE4Good Index Series is designed to measure the performance of companies demonstrating strong Environmental, Social and Governance (ESG) practices. The FTSE4Good indices are used by a wide variety of market participants to create and assess responsible investment funds and other products."

- Excellence Award for Corporate Governance Disclosure
- Merit Award for Board Diversity
- Merit Award for Most Improved Corporate Governance Disclosure

ASEAN Corporate Governance Scorecard

2015

- Top 50 ASEAN Public Listed Companies

Public listed companies in Southeast Asia were assessed on good governance and transparency practices using the scorecard methodology, based on the Organisation for Economic Co-operation and Development ("OECD")'s Principles of Corporate Governance.

BUSINESS GOVERNANCE – *Commitment to Performance*

RHB Bank aspires to become amongst the Top 3 **Multinational Financial Services Group**, in terms of performance by 2022. This vision commits the Company to deliver complete solutions to its customers through differentiated segment offerings and an ecosystem that supports simple, fast and seamless customer experience. This mission intent has been translated into the Group's Core **Shared Values** namely P.R.I.D.E. (**P**rofessional, **R**espect, **I**ntegrity, **D**ynamic & **E**xcellence), the Company's Annual Balanced Scorecard, Sustainable Key Performance Indicators and the Group's **I.G.N.I.T.E.** principles, namely **Innovative** in approach, **Growth** oriented, **Nimble** in action, **Impactful** in outcomes, **Teamwork** to succeed and **Excellence** in delivery. A new 5-year strategic plan, known as FIT22 (**F**und our Journey, **I**nvest to Win and **T**ransform for Success 20**22**) comprising 22 initiatives has now been put in place commencing 2018 to achieve its objectives and aspirations by 2022.

A key component of the new strategic plan is the Group's brand promise of **Together We Progress**, basically promoting the idea of the Company, walking hand-in-hand with its internal and external stakeholders, towards achieving sustainable operations as the Company runs and manages its business in an orderly fashion. This includes utilisation of the Group's capitals (financial, manufactured, intellectual, human, social relationship and natural) at optimal level to improve its integrated value chain while safeguarding its assets and the environment for future generations.

The Board of RHBIB has also adopted sustainability principles in 2017 by including Economic, Environment and Social ("EES") considerations into the Company's Board Charter and the Group's business strategies to further emphasise the creation of sustainable business operations and share value. An overview of the Group's EES considerations is laid out in its holding company's Sustainability Report 2017.

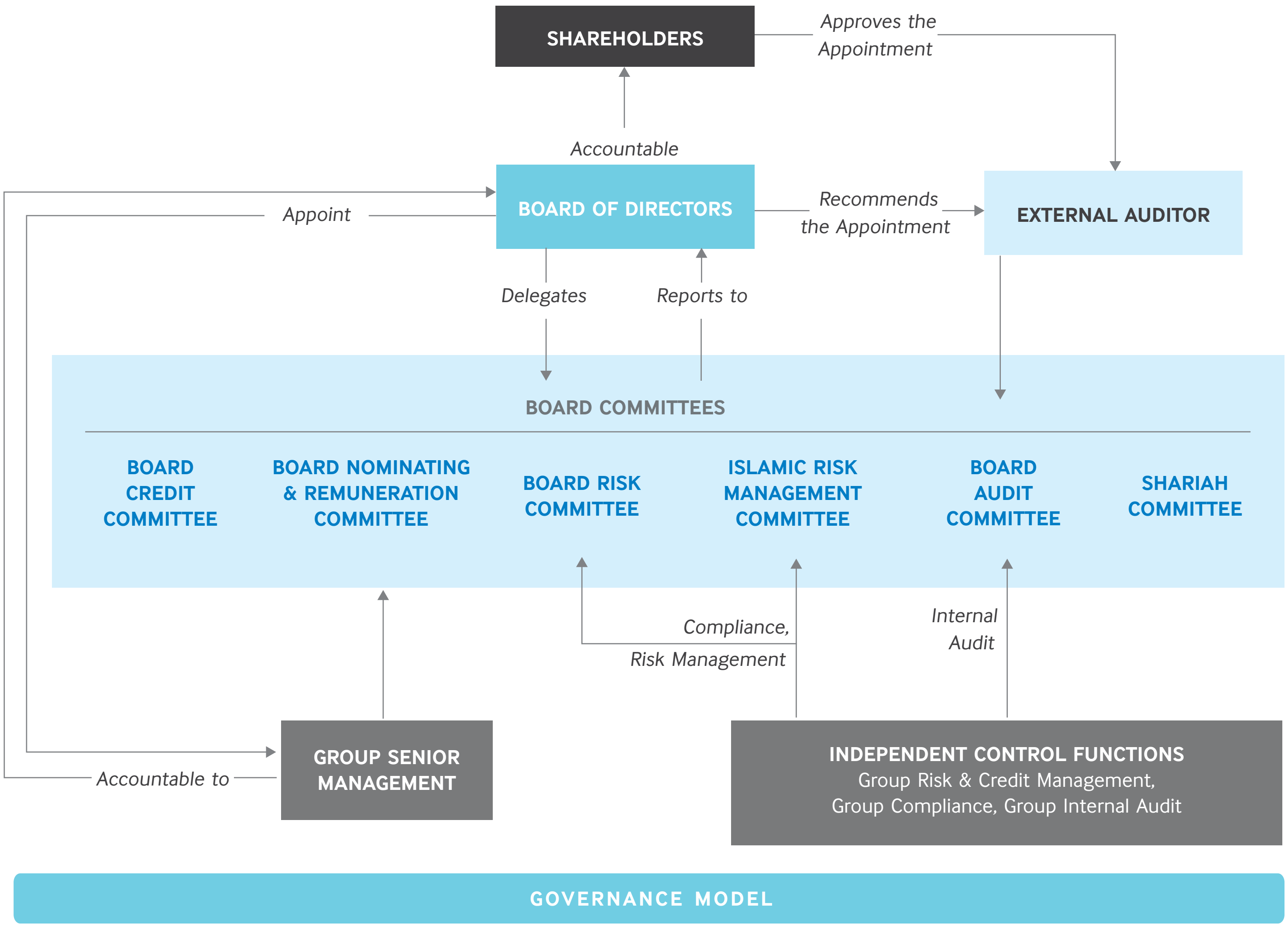
Excellence in **business governance** is essential towards attaining stakeholders' confidence in the Company's sustainable operations. The Group, through its journey in adopting integrated reporting for the past three years, aims to achieve this goal of communicating effectively to stakeholders, matters which are most relevant, material and important to them and to the Group, covering both financial and non-financial information.

ORGANISATIONAL CULTURE

A corporate culture that embraces the correct behaviours to achieve a company's objectives is fundamental in ensuring sustainable long-term growth and success for any organisation. The latest Board Effectiveness Evaluation exercise was designed internally for the first time, specifically to assess the tone at the top in areas such as leadership, decision-making, communication, group dynamics and mind-set of the Board as a collective unit and Board members as individuals. Actions will then be taken to address identified gaps to enhance the performance of the Board.

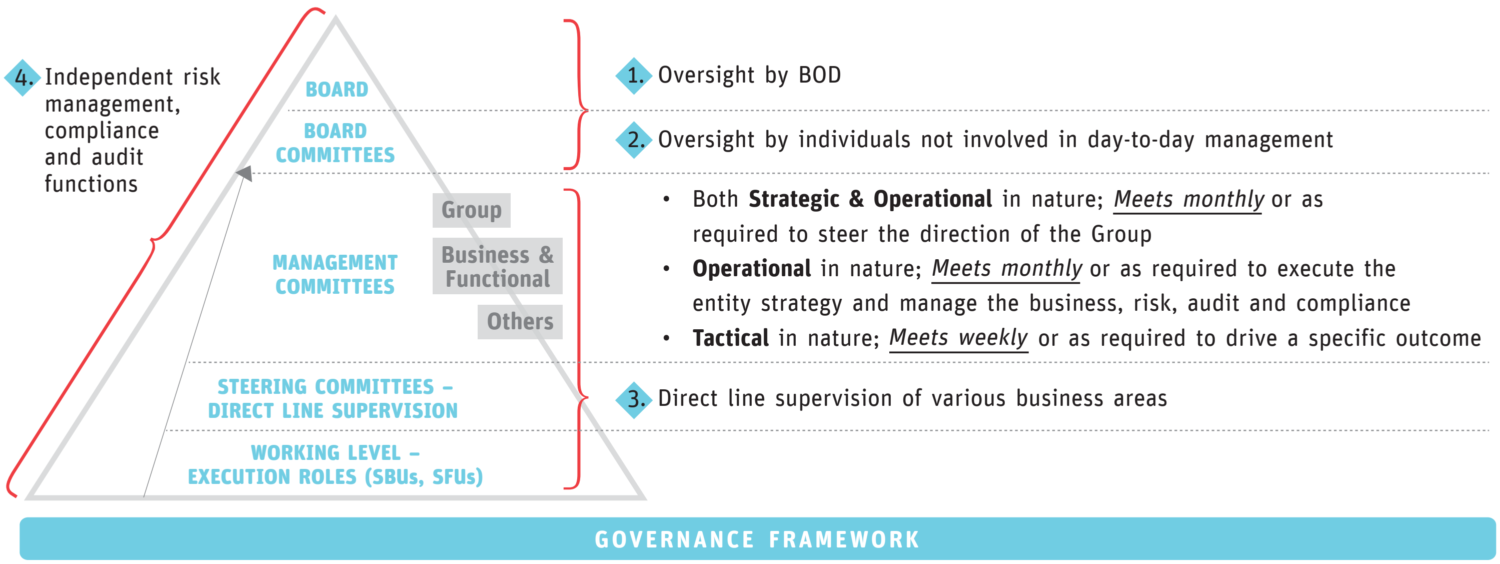
In leading the organisation and ensuring that all the Group's strategic objectives and business scorecards are met within the approved risk appetites, the Board is bound by its Charter, Terms of Reference ("ToR") for its various Board Committees, Group Code of Ethics & Business Conduct for Directors, and other internal guidelines. To complement the Charter, various policies and guidelines including the Group Manual of Authority, Power of Attorney, Delegated Lending & Financing Authority (Discretionary Powers), Group Code of Ethics & Conduct for Employees, Group Whistleblowing Policy and Group Gifts & Hospitality Guidelines were approved or endorsed by the Board to ensure good governance practice and fiduciary duties are implemented by the Senior Management and other key personnel.

GOVERNANCE MODEL & FRAMEWORK



The Board continuously explores enhancements to the Group's governance processes to ensure it remains robust as it continues to expand. The governance model and framework are currently being used as a guide and reference to build a strong governance structure and conformance culture within the Company and other RHB entities in the banking group. The **Governance Model** outlines a clear organisational structure with robust internal controls and risk management mechanisms which promote high standards of governance and of integrity, transparency and well-defined accountabilities and responsibilities of Shareholders, Board and Board Committees, Senior Management, External and Internal Auditors and other Independent Control Functions.

The Board has also approved and established the **Group Governance Framework** as a basis of an effective governance and oversight to support the overall RHB Banking Group's strategies.



Under this framework, there are various levels of oversights operating across the Group's business and functional activities. These include amongst others; direct supervision, Senior Management, independent parties comprising of risk management, compliance and internal audit, Group Managing Director ("Group MD"), Managing Directors ("MDs"), Board Committees and the Board. A clear and transparent governance structure for various central and sub-committees set by the Board members and the Senior Management has institutionalised the Company as a risk-focused organisation with proper control functions and good corporate governance practice.

BOARD GOVERNANCE MANUAL

The main documents governing the Board are the Company's Memorandum & Articles of Association (*moving forward to be known as the* "Constitution"), the Board Charter and the Code of Ethics and Business Conduct for Directors. The Board is also guided by the Approval Framework on Directors' Expenses, the Boardroom Diversity Policy, Policy and Guidelines on Fit and Proper for Key Responsible Persons, Guidelines on Tenure of Non-Executive Directors' Appointment, Procedures for Independent Professional Advice and also Procedures on Directors' In-House Orientation & Continuing Education Programme. All these frameworks, policies, procedures and processes serve as guidance to the Board in discharging their duties effectively, efficiently and responsibly.

BOARD COMMITTEES

To ensure effectiveness in discharging its roles and responsibilities, the Board delegates specific authorities to the relevant Board Committees. This delegation of authority is expressly stipulated in the Terms of References ("TOR") of the respective Board Committees. The TORs are reviewed periodically to ensure effective and efficient decision making in the Group. The Board Committees also act as oversight committees, evaluating and recommending matters under their purview for the Board to consider and approve.

The Board receives updates from the respective chairmen/representatives of the Board Audit Committee, Board Risk Committee and Board Nominating & Remuneration Committee on matters that require specific mention that have been deliberated and considered at the meetings of Board Committees. This practice also applies for other entities within the Group.

Board Nominating & Remuneration Committee

The key objectives of the Board Nominating & Remuneration Committee ("BNRC") are, as follows:-

- Review and assess the appointment/re-appointments of Directors, Board Committee members, Shariah Committee and key Senior Management officers for recommendation to the Boards.
- Advise the Boards on optimal size and mix of skills of Boards/Board Committees/Shariah Committees.
- Provide oversight and direction on HR matters and operations, and recommend to the Boards for approval of remuneration and human resource (HR) strategies.

The BNRC comprises five NEDs, of whom three are INEDs and two are NINEDs, representing the respective entities within the Group. The BNRC is chaired by YBhg Tan Sri Saw Choo Boon, the SINED of RHB Bank. The composition of the BNRC consisting of majority Independent Directors, complies with the Bursa Malaysia Listing Requirements, Malaysian Code on Corporate Governance 2017 and Bank Negara Malaysia's Policy Document on Corporate Governance 2016. Similar composition was recorded throughout the calendar year of 2017 from 1st January until the retirement of Mr Ong Seng Pheow, an INED of the Company effective 19 November 2017. The vacancy on the BNRC was then filled-in by YBhg Tan Sri Dr Rebecca Fatima Sta Maria, also an INED effective 15 February 2018.

Board Risk Committee

The Board recognises the importance of a sound system of risk management and internal control to ensure good corporate governance and to safeguard shareholders' investments as well as the Company's and the Group's assets. A Group Risk Management Framework has been established to provide a holistic overview of the risk and control environment of the Group, as well as to set out strategic progression of risk management towards becoming a value creation enterprise. Detailed disclosures on the features, adequacy and effectiveness of this framework are available in the Statement on Risk Management & Internal Control on pages 30 to 36.

The Board Risk Committee ("BRC") provides oversight and governance of risks for the Group to ensure that the Group's risk management processes are functional and effective. The BRC also oversees Senior Management's activities in managing risk, ensuring that the risk management process in each of the Group's entities function in accordance with a risk-return performance management framework. Furthermore, the BRC supports and leads the Senior Management in driving the appropriate Risk Culture and Risk Ownership in the Group.

The BRC's other duties and functions among others include the following:

- To provide oversight to ensure that the Group's risk management framework, processes, organisation and systems are functioning commensurate with its nature, scale, complexity of activities and risk appetite.
- To deliberate and assess the nature and materiality of risk exposures, potential risks and impact on capital and the Group's sustainability.
- To review and approve proposed changes to Delegated Lending (Financing) Authorities/Discretionary Powers/Powers of Attorney, limits for business and operations.
- To review and approve changes to policies and frameworks (excluding HR related policies and framework), risk methodologies/models and other significant risk management matters, in line with the approved risk strategy.
- To review and approve new/existing products with material variations in product features.

The BRC comprises a **majority** of Independent Directors. The board committee currently comprises four NEDs, of whom three are INEDs and one NINED, representing the respective entities within the Group. The BRC met 12 times during the financial year 2017.

Pursuant to the Group's current governance framework, RHBIB has adopted the BRC while maintaining a dedicated Risk Management Committee to manage Shariah risk and its associated intricacies.

Board Audit Committee

The Board Audit Committee ("BAC") comprises three INEDs representing RHB Bank and its major operating subsidiaries. The Chair of the BAC is **not** the Chairman of the Board of the Company. The BAC has policies and procedures to assess the suitability, objectivity and independence of the external auditors engaged. Considerations on the appointment of the external auditors to provide audit and non-audit services would include the expertise, adequacy of knowledge and experience required for the services rendered, the tenure of the engagement partner and also the concurring partner, the competitiveness of the fees quoted and the fees threshold established under the internal Group Policy on Non-Audit Fees Paid/Payable to External Auditors.

The BAC provides independent oversight of RHB Banking Group's financial reporting and internal control system, ensuring checks and balances for entities within the Group. The BAC continuously reinforces the independence of the external auditors and provides a line of communication between the Board and the external auditors.

The BAC reviews the integrity and reliability of the Company's and the Group's financial statements on a quarterly basis, prior to recommending the same for the Board's approval and issuance to stakeholders. During the reviews, the Group Chief Financial Officer provides assurance to the BAC that:

- Adequate processes and controls are in place for an effective and efficient financial statement close process;
- Appropriate accounting policies have been adopted and applied consistently; and
- The relevant financial statements give a true and fair view of the state of affairs of the Company and the Group in compliance with the Malaysian Financial Reporting Standards, International Financial Reporting Standards and Companies Act 2016.

The BAC also meets twice a year with the external auditors, without the presence of the Management and the executive Board member, to discuss any key issues/ areas that require attention of the BAC and the Board.

The BAC also emphasises the internal audit function by increasing the objectivity and independence of the internal auditors and provides a forum for discussion that is, among others, independent of the Management. Additionally, the BAC reviews the quality of the audits conducted by internal and external auditors as well as the Group's financial condition and performance. This enhances the perceptions held by stakeholders (including shareholders, regulators, creditors and employees) of the credibility and objectivity of financial reports. Detailed disclosures on BAC's governance structure and primary activities are available on pages 37 to 42 of this Annual Report.

Board Credit Committee

The Board Credit Committee ("BCC") comprises three NEDs, of whom one is INED and two are NINEDs representing the respective banking entities within the Group. The BCC supports the relevant Boards in affirming, vetoing or including additional conditions on all types of credit applications (including under stock/futures broking) and underwriting applications for amounts above the defined thresholds of the Group Credit Committee and/or the Group Investment & Underwriting Committee, both comprise of the Company's management. It also endorses and recommends write-offs as well as approves all policy loans/financing and loans/financing which are required by Bank Negara Malaysia ("BNM") to be approved by the respective Boards.

Shariah Committee

The Shariah Committee is housed at RHBIB comprises five (5) qualified local Shariah scholars.

The main duties and responsibilities of the Shariah Committee are as follows:

- To advise on all Shariah matters to ensure its business operations comply with Shariah Principles, where applicable.
- Where relevant, to consult BNM's Shariah Advisory Council ("SAC") on any Shariah matters which have not been resolved or endorsed by the SAC.
- To perform an oversight role on Shariah matters related to the institution's business operations and activities.

Islamic Risk Management Committee

The Islamic Risk Management Committee ("IRMC") resides at RHBIB and comprises three (3) INEDs of RHBIB. The IRMC provides risk oversight and guidance to ensure that the management of risk exposures in RHBIB are aligned to the principles of Islamic Banking as guided by the relevant regulatory authority, as well as to ensure that core risk policies are consistent with the Group's. The IRMC also oversees the execution of risk policies and related decisions by RHBIB's Board, and provides oversight for major risk categories which are unique to Islamic finance. These include displaced commercial risk, withdrawal risk, rate of return risk, fiduciary risk and Shariah non-compliance risk.

BOARD TRAINING AND DEVELOPMENT

The Board emphasises the importance of continuing education and training for its Directors to ensure they keep up with the latest developments in the areas related to their duties. A budget for Directors' training is provided each year by RHBIB. The Board, as part of the Board Effectiveness Evaluation ("BEE") exercise, assesses the training needs of each Director annually. The training and development of Directors are detailed in the Group's Standard Procedures on Directors' In-house Orientation and Continuing Education Programme for the RHB Banking Group.

The Non-Executive Directors ("NED") of the Company and the Group are encouraged to attend local and/or overseas training programmes organised by credible training organisations under the Board High Performance Programme. This programme is intended to equip the Directors with the necessary knowledge and tools to effectively discharge their duties and responsibilities as well as provide the Directors with global business perspectives and skills that engender organisational excellence. The Company Secretaries facilitate the organisation of internal training programmes and Directors' attendance of external programmes, and keep a complete record of the training received and attended by the Directors.

Learning Process for New Director

Two new NED are on board of the Company for the FYE 2017. The newly appointed Company's NEDs, namely Ms Ong Ai Lin and YBhg Dato' Foong Chee Meng attended an induction programme organised by the Management of the Group on 19 July 2017 and 15 September 2017 respectively to provide them with in-depth information of the industry as well as an overview of the Group's business operations. During the induction programme, the new directors were briefed by relevant Management personnel on the functions and areas of responsibility of their respective divisions. This enables the new Group NEDs to familiarise themselves with the Group's operations and organisational structure and also helps them to establish effective channels of communication and interaction with Management.

In addition, the new NEDs received a comprehensive Director's induction kit to assist them in building a detailed understanding of the Group's operations, its longer-term direction and statutory obligations.

Apart therefrom, they were required to complete the Financial Institutions Directors' Education ("FIDE") programme within one year of their respective appointment. The FIDE programme aims to enhance boardroom governance within the financial sector and develop world class directors who are advocates of best practices and excellence in corporate governance.

Director's Training

During the year, the Directors of RHBIB attended the following training programmes, conferences and seminars:

Name of Director(s)	Training Programme Attended	Training Scope & Description
The Late Tuan Hj Md Ja'far Abdul Carrim	Cryptocurrency and Blockchain Technology by Neuroware	• Cryptocurrency including BitCoin • Blockchain Technology • Potential Use Cases in the Financial Services Industry
	Islamic Banking by 2030: Impact of Digital Economy, Fintech & Sustainability as Forces of Change by SHAPE	• Digital Economy era • Fintech and its Impact • Sustainability & Social Responsibility Investment (SRI)
	FIDE FORUM Invitation – 2nd Distinguished Board Leadership Series & 6th Annual General Meeting	• The role that the board plays in assessing the adequacy of such a remuneration policy, including key questions that boards should ask to ensure that the remuneration policy is sufficiently robust to meet regulatory requirements while attracting the right talent to the FI; • Key issues and challenges in implementing such a remuneration policy; and • Pragmatic steps and quick tips in managing the challenges that arise from the implementation of such a remuneration policy
	Fintech: Opportunities for the Financial Services Industry in Malaysia	• Current Status & Approach in Fintech Adoption Among Malaysian Financial Institutions (FI) • Opportunities for FI-Fintech Collaboration under Regtech Sandbox • Key Areas & Issues for Board's Consideration
	Malaysian Code on Corporate Governance: Expectation and Implications	• The New Approach & Key Features • Board Leadership and Effectiveness • Effective Audit and Risk Management • Integrity in Corporate Reporting and Meaningful Relationship with Stakeholders
	Crypto currency & Block chain Technology, Viewpoints of an Entrepreneur	• Key issues and challenges, as well as opportunities and threats of cryptocurrencies and blockchain technology • Possible strategy for your business models
Datuk Haji Faisal Siraj	Peer-2-Peer (P2P) Lending and Crowdfunding/ Crowdsourcing by Group Chief Operations Officer	• Alternative Funding Models • Licensed P2P Operators • Licensed Equity Crowdfunding Operators • Regulatory Framework Market Potential
	Islamic Banking by 2030: Impact of Digital Economy, Fintech & Sustainability as Forces of Change by SHAPE	• Digital Economy era • Fintech and its Impact • Sustainability & Social Responsibility Investment (SRI)
	Malaysian Code on Corporate Governance: Expectation and Implications by SIDC	• The New Approach & Key Features • Board Leadership and Effectiveness • Effective Audit and Risk Management • Integrity in Corporate Reporting and Meaningful Relationship with Stakeholders

Name of Director(s)	Training Programme Attended	Training Scope & Description
Datuk Haji Faisal Siraj (continue)	Shariah Awareness Programme by Amanie Group	• Global Perspectives in the Islamic Financial Industry • Critical Success Factors and Critical Failure Factors
	AML/CFT & Regulatory Compliance Training for Board of Directors & Senior Management	• Global Trends in 2017 • Insights from PwC Economic Crime Survey 2016 • What does it mean to be AML/CFT compliant • Regulatory landscape • Common AML/CFT challenges faced by FIs in Malaysia
Dato' Abd Rahman Bin Dato' Md Khalid	New Directors' In-House Orientation by Group Company Secretary	• RHB Banking Group's Governance & Shareholding Structure • Group's Core Businesses • Overview by Head/Representative of Group's Strategic Business and Functional Groups
	Cryptocurrency and Blockchain Technology by Neuroware	• Cryptocurrency including BitCoin • Blockchain Technology • Potential Use Cases in the Financial Services Industry
	Business as a force for good: The role of the private sector in achieving the Sustainable Development Goals	• National and Industries' perspectives on achieving the SDGs together • Better business, better opportunities • SDGs and the Private Sector • Responsible Investment and Financing
	Malaysian Code on Corporate Governance: Expectation and Implications	• The New Approach & Key Features • Board Leadership and Effectiveness • Effective Audit and Risk Management • Integrity in Corporate Reporting and Meaningful Relationship with Stakeholders
	FIDE FORUM Invitation – 2nd Distinguished Board Leadership Series & 6th Annual General Meeting	• The role that the board plays in assessing the adequacy of such a remuneration policy, including key questions that boards should ask to ensure that the remuneration policy is sufficiently robust to meet regulatory requirements while attracting the right talent to the FI; • Key issues and challenges in implementing such a remuneration policy; and • Pragmatic steps and quick tips in managing the challenges that arise from the implementation of such a remuneration policy
	Shariah Awareness Programme by Amanie Group	• Global Perspectives in the Islamic Financial Industry • Critical Success Factors and Critical Failure Factors
	RAM Sustainability Impact Rating by Datuk Seri Dr. K.Govindan, Group CEO of RAM Holdings Berhad	• RAM's Role in Sustainable Finance • RAM Consultancy's Sustainability Services • Sustainability Rating • Recent Development

Name of Director(s)	Training Programme Attended	Training Scope & Description
Dato' Abd Rahman Bin Dato' Md Khalid (continue)	AIF Professional Masterclass: Exploring the Dynamics of Leadership	• RECOGNIZE the importance of emotional intelligence • INCREASE one's psychological and social competencies • LEARN what leadership team coaching is all about • RECOGNIZE the darker side of leadership • INDICATE how leaders can derail • RECOGNIZE out-of-awareness behaviour patterns and take appropriate corrective action • IDENTIFY the parameters that make
	Half-Day Seminar: Governance & Leadership In Technology Disruption	• The technological & societal disruptors – a strategic view • The impact of these disruptors on current business practice & governance • Individual SWOT analysis how the participant's organisations will hold up under these oncoming changes • Explore how their existing corporate cultures are a key bottle neck for the need to transform their organisations
	AML/CFT & Regulatory Compliance Training for Board of Directors & Senior Management	• Global Trends in 2017 • Insights from PwC Economic Crime Survey 2016 • What does it mean to be AML/CFT compliant • Regulatory landscape • Common AML/CFT challenges faced by FIs in Malaysia
	Briefing on MFRS 9	• Classification and measurement of financial assets & financial liabilities • Impairment-expected credit losses • General hedge accounting*
Dato' Foong Chee Meng	New Directors' In-House Orientation by Group Company Secretary	• RHB Banking Group's Governance & Shareholding Structure • Group's Core Businesses • Overview by Head/Representative of Group's Strategic Business and Functional Groups
	2nd Securities Commission – FIDE FORUM Dialogue: Leveraging Technology for Growth	• Enhance access to financing the progress of equity crowdfunding (ECF)and peer-to-peer financing (P2P) in Malaysia thus far • Increase investor participation Robo-advisory and Digital Investment Management Framework introduced in May 2017 • Emerging Technologies: Artificial Intelligence for Capital Markets
	AML/CFT & Regulatory Compliance Training for Board of Directors & Senior Management	• Global Trends in 2017 • Insights from PwC Economic Crime Survey 2016 • What does it mean to be AML/CFT compliant • Regulatory landscape • Common AML/CFT challenges faced by FIs in Malaysia
Ms Ong Ai Lin	New Directors' In-House Orientation by Group Company Secretary	• RHB Banking Group's Governance & Shareholding Structure • Group's Core Businesses • Overview by Head/Representative of Group's Strategic Business and Functional Groups

Name of Director(s)	Training Programme Attended	Training Scope & Description
Ms Ong Ai Lin (continue)	Cyber Landscape In The Malaysian Financial Industry by AICB	• Paradigm Shift in Mindset in Managing Cyber Threats • Cyber Risks & Threats Landscape • The World Under Siege: Building Effective Cyber Defense • Balancing Act: Cyber Risks and New Technologies Building Cyber Resilience
	Mandatory Accreditation Programme for Directors of Public Listed Companies by ICLIF	• Understanding the directors' obligation: Board effectiveness & managing risk • Discharging directors' financial reporting responsibility • Demystifying Directors' Key Obligations under The Listing Requirements of Bursa Malaysia Securities Berhad • Audit Committee Expanded Governance Oversight Role
	Malaysian Institute of Accountants Annual Conference 2017	• Post Brexit, Gulf Crisis & Geopolitical Risks: Its Impact on Asian Economy • Public Sector Governance • Impact of MFRS 15 • Tax Opportunities and Challenges in the Digital Economy • Cyber Threat Intelligence: Key Defence Element
	Fundamentals of Blockchain Technology by ICAEW	• Blockchain's Role in Managing Bitcoin • Key Features of Blockchain Technology • Potential Applications
	AML/CFT & Regulatory Compliance Training for Board of Directors & Senior Management	• Global Trends in 2017 • Insights from PwC Economic Crime Survey 2016 • What does it mean to be AML/CFT compliant • Regulatory landscape • Common AML/CFT challenges faced by FIs in Malaysia
	Briefing on MFRS 9	• Classification and measurement of financial assets & financial liabilities • Impairment-expected credit losses • General hedge accounting*
	FIDE CORE Programme: Module A	• Understanding of the role of the board • Equip directors with tools and strategies • Responsibility of the board for promoting a strong risk control culture • Explore plausible and extreme stress scenario

BOARD COMPOSITION AND ATTENDANCE

Details on the **independent status** of the Board of Directors, their **roles** in Board Committees and their **attendance** at the aforesaid meetings in 2017 are set out below:

Company's Director	Position/ Independent Status	Date of Board appointment	Attendance of Meetings					
			Board Meeting	IRMC[1] Meeting	BNRC[2] Meeting	BRC[3] Meeting	BAC[4] Meeting	BCC[5] Meeting
YBhg Dato' Abd Rahman Dato' Md Khalid	Senior Independent Non-Executive Director (SINED) *(Appointed as SINED w.e.f. 25 April 2017)*	2 January 2017	14/14 (100%)	11/11 (100%) *(Appointed as Committee Member/ Chairman w.e.f. 28 February 2017)*	*NA*	*NA*	*NA*	35/38 (92%)
YBhg Datuk Haji Faisal Siraj	Non-Independent Non-Executive Director (NINED)	3 December 2007	13/14 (93%)	3/3 (100%) *(Resigned as committee member w.e.f. 28 February 2017)*	*NA*	*NA*	*NA*	*NA*
YBhg Dato' Foong Chee Meng	Independent Non-Executive Director (INED)	1 August 2017	6/6 (100%)	*NA*	5/5 (100%)	*NA*	*NA*	*NA*
Ms Ong Ai Lin	Independent Non-Executive Director (INED)	1 September 2017	5/5 (100%)	2/2 (100%) *(Appointed as committee member w.e.f. 13 November 2017)*	2/2 (100%) *(Appointed as committee member w.e.f. 1 July 2017)*	1/1 (100%) *(Appointed as committee member w.e.f. 1 November 2017)*	7/7 (100%) *(Appointed as committee member w.e.f. 1 July 2017)*	*NA*
YBhg Dato' Adissadikin Ali	Managing Director (MD)/Chief Executive Officer (CEO)	1 August 2016	13/14 (93%)	*NA*	*NA*	*NA*	*NA*	*NA*
Tuan Haji Md Ja'far Abdul Carrim	Chairman/ Independent Non-Executive Director (INED)	10 August 2009 *(Deceased on 19 October 2017)*	11/11 (100%)	12/12 (100%)	*NA*	*NA*	28/31 (91%)	*NA*

Company's Director	Position/ Independent Status	Date of Board appointment	Attendance of Meetings					
			Board Meeting	IRMC[1] Meeting	BNRC[2] Meeting	BRC[3] Meeting	BAC[4] Meeting	BCC[5] Meeting
YBhg Dato' Sri Haji Syed Zainal Abidin Syed Mohamed Tahir	Independent Non-Executive Director (INED)	6 October 2015 *(Resigned w.e.f. 1 August 2017)*	6/8 (75%)	4/6 (67%) *(Resigned as committee member w.e.f. 28 February 2017)*	4/4 (100%) *(Resigned as committee member w.e.f. 1 July 2017)*	*NA*	15/19 (79%) *(Resigned as committee member w.e.f. 1 July 2017)*	2/2 (100%)
YBhg Dato' Mohd Ali Mohd Tahir	Independent Non-Executive Director (INED)	1 January 2011 *(Resigned w.e.f. 28 February 2017)*	2/2 (100%)	3/3 (100%)	*NA*	*NA*	*NA*	*NA*

Note:
1-5 Abbreviations used denote various main Board Committees.
5 This Board Technology Committee was dissolved with effect from 1 May 2017.
NA Not Applicable

REMUNERATION GOVERNANCE

The remuneration structure of RHBIB's Non-Executive Directors ("NEDs") in the Company for 2017 per BNM Policy disclosure requirement is laid out as follows:

No.	NEDs' Remuneration Scheme	Aggregated Amount of the NEDs' Remuneration	
		Unrestricted/ Non-Deferred (RM'000)	Restricted/ Deferred (RM'000)
A.	Fixed-Type Remuneration		
	i. Cash-based • Fixed Fees – Directors' Fees[1] – Board Committees' Allowances[2] – Chairmen's premium[3]	1,246	Nil
	ii. Shares & share-linked instruments	Nil	Nil
	iii. Others • Benefits-in-kind[5] • Emolument – Farewell Pot[4]	17	Nil
B.	Variable-Type Remuneration		
	i. Cash-based • Meeting Attendance Allowance[6]	233	Nil
	ii. Shares & share-linked instruments	Nil	Nil
	iii. Others • Directors' & Officers' Liability Insurance[7]	374	Nil

Notes:
The overall remuneration package of the NEDs of the Group/Company comprises the following components:

1) Directors' Fees

NEDs are entitled to annual Directors' fees, which are subject to shareholders' approval at the Annual General Meeting ("AGM") of the Company. The Management has recommended that the Group Directors' Fees structure to be revised from RM150,000.00 to RM170,000.00 per annum for the Non-Executive Chairman and from RM120,000.00 to RM135,000.00 per annum for each of every NED retrospective from 1 January 2017. The above proposal is subject to the approval of the shareholder at the forthcoming 2018 Annual General Meeting of the Company.

2) Board Committee Allowances

NEDs who sit on Board Committees are entitled to receive Board Committee allowances which shall be paid on an annual basis at the end of each financial year.

3) Chairmen's Premium

NEDs who sit on various Boards and Board Committees as the chairman are entitled to receive a premium above the normal respective Board and Board Committee allowances, which shall be paid on an annual basis at the end of each financial year.

4) Emoluments

All NEDs will be awarded with 'Farewell Pot' scheme upon exit from the Group while the Group Chairman is accorded with a special allowance, in recognition of their services and commitments to the Group. Under the 'Farewell Pot' scheme, any NED who leaves the Group would be entitled to RM2,000 in cash equivalent for each year of his/her service in the Group or as decided by the BNRC.

5) Benefits-in-kind

Benefits are accorded to the Chairmen of the Group, consisting amongst others the provision of a company car, driver and petrol allowance.

6) Meeting attendance allowance

NEDs are also entitled to meeting attendance allowances when they attend any Board/Board Committee meetings. Total allowances are subject to number of Board/Board Committee sittings and number of meetings attended by each Company's Non-Executive Director.

7) Directors' & Officers' ("D&O") Liability Insurance

The insurance covers the Group's Directors in respect of any liabilities arising from acts committed in their capacity as D&O of RHB Banking Group. However, the insurance policy does not indemnify a Director or principal officer if he or she is proven to have acted negligently, fraudulently or dishonestly, or in breach of his or her duty of trust. The Directors are required to contribute jointly towards a portion of the premiums of the said policy.

All the non-executive directors' remuneration, including the fees, allowances, benefits in-kind and other emoluments will be subject to the shareholders' approval during the Company's annual general meeting ("AGM"), on yearly basis. When the non-executive directors' remuneration matters were presented before the Company's directors during the AGM, the Board members (save for YBhg Dato' Adissadikin Ali, being the MD/CEO) declared their interests in respect of the above proposal. The interested Directors abstained from voting in respect of their direct and/or indirect shareholdings (if any) on the resolution relating thereto.

STATEMENT OF RISK MANAGEMENT & INTERNAL CONTROL

BOARD RESPONSIBILITY

The Board of Directors ("Board") of RHB Islamic Bank Berhad ("Bank") is cognisant of its overall responsibility in establishing a sound risk management and internal control system in the Bank as well as reviewing its adequacy, integrity and effectiveness. Such a system is designed to manage the Bank's risk appetite within the established risk tolerance set by the Board and Management rather than total elimination of risks to achieve the Bank's business objectives. The system can therefore only provide reasonable and not absolute assurance against the occurrence of any material misstatement, loss or fraud. Limitations inherent in the system include among others, human error and potential impact of external events beyond Management control.

In acknowledging that having a sound risk management and internal control system is imperative, the Board has established a governance structure that ensures effective oversight of risks and internal controls in the Bank at all levels. To this end, the Board is assisted by the Board Risk Committee ("BRC"), Board Audit Committee ("BAC") and Islamic Risk Management ("IRMC") which have been delegated with primary oversight responsibilities on the Bank's risk management and internal control system. The Board remains responsible for the governance of risk and for all the actions of the Board Committees with regard to the execution of the delegated oversight responsibilities.

MANAGEMENT RESPONSIBILITY

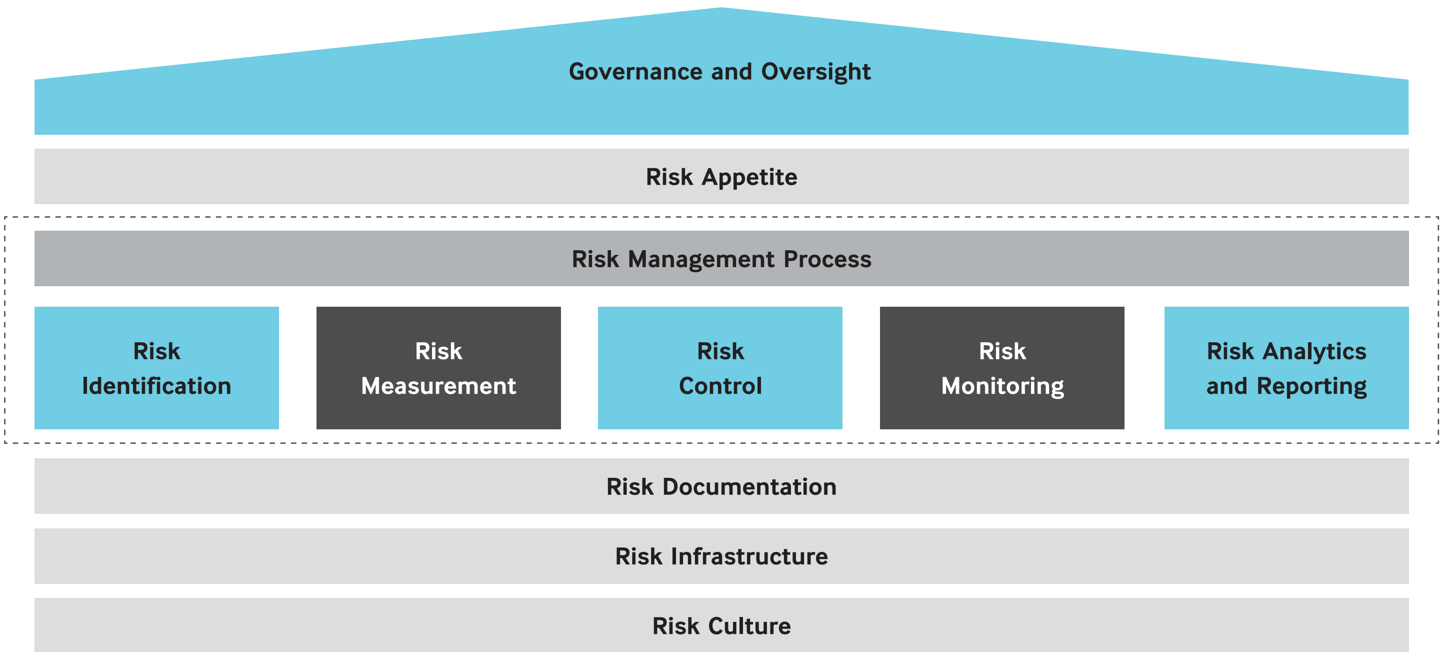
The Management is overall responsible for implementing the Bank's policies and processes to identify, evaluate, measure, monitor and report on risks as well as the effectiveness of the internal control systems, taking appropriate and timely remedial actions as required. Its roles include:

- Identifying and evaluating the risks relevant to the Bank's business and achievement of its business objectives and strategies;
- Formulating relevant policies and procedures to manage risks and the conduct of business;
- Designing and implementing the risk management framework and internal control system, and monitoring its effectiveness;
- Implementing policies approved by the Board;
- Implementing remedial actions to address compliance deficiencies as directed by the Board; and
- Reporting in a timely manner to the Board any changes to the risks and the remedial actions taken.

The Management has provided assurance that the Bank's risk management and internal control system is operating adequately and effectively and that necessary processes have been implemented.

RISK MANAGEMENT FRAMEWORK

The RHB Banking Group, inclusive of the Bank ("Group"), has in place a risk management framework approved by the Board for identifying, measuring, monitoring and reporting of significant risks faced by the Group in the achievement of the Group's business objectives and strategies. The Group's risk management framework ensures that there is an effective on-going process to identify, evaluate and manage risk across the Group and is represented in the following diagram:



Risk Governance and Oversight

The Board, through the BRC and IRMC, provides oversight over the risk management activities for the Group to ensure that the Group's risk management processes are functioning effectively.

The BRC and IRMC also assist the Board to review the Group's overall risk management philosophy, frameworks, policies and models. In discharging its overall duties and responsibilities, the BRC and IRMC are supported by the Group Capital and Risk Committee ("GCRC") and Group Risk & Credit Management function which monitors and evaluates the effectiveness of the Group's risk management system on an on-going basis. The GCRC, comprising Senior Management of the Group and chaired by the Group Managing Director, is responsible for the supervision of the management of enterprise risk and capital matters.

In addition to the risk management framework, the Group has implemented the Internal Capital Adequacy Assessment Process ("ICAAP") framework to ensure that the Group maintains adequate capital levels consistent with the risk profiles including capital buffers to support the Group's current and projected demand for capital under existing and stressed conditions. In order to ensure on-going engagement and assessment of the Group's risk profile and capital adequacy, the ICAAP report is reviewed at least annually and is presented to senior management and relevant Board committees prior to approval by the respective entities' Boards.

Amongst the other committees set up in the Group to manage specific areas of risk are the Group Asset and Liability Committee, Group Credit Committee, IRMC, Board Credit Committee and Group Digital & Technology Committee with their scope of responsibility as defined in their respective terms of reference.

Risk Appetite

Risk appetite for the Group is defined as the amount and the type of risks that the Group is willing to accept in pursuit of its strategic and business objectives. Risk tolerance on the other hand, is the acceptable level of variation relative to the achievement of the Group's strategic and business objectives. It is measured in the same units as the related objectives. It translates risk appetite into operational metrics, and it can be defined at any level of the Group.

The Board, through the BRC, IRMC, GCRC and Group Risk & Credit Management function, establishes the risk appetite and risk tolerance for the Group and relevant entities.

The defined risk appetite and risk tolerance are periodically reviewed by the Management and the Board in line with the Group's business strategies and operating environment. Such review includes identifying and setting new risk appetite metrics for the business entity or removal of risk appetite metrics that are no longer applicable as well as updates on the risk appetite thresholds to be in line with the Group's business strategy and risk posture.

The main business and operations inherent risks that were considered in the risk appetite review include regulatory compliance risk, credit risk, market and liquidity risk, operational and technology risk, and Shariah non-compliance risk.

Risk Management Processes

The risk management processes within the Group seek to identify, evaluate, measure, monitor and control risk so that risk exposures are adequately managed and the expected returns adequately compensate the risks.

- Identification: The identification and analysis of the existing and potential risks is a continuing process, in order to facilitate and ensure that the risks can be managed and controlled within the risk appetite of the Group and specific entity, where necessary.
- Measurement: Risks are measured, assessed and aggregated using comprehensive qualitative and quantitative risk measurement methodologies, and the process also serves as an important tool as it provides an assessment of capital adequacy and solvency.
- Controlling and Monitoring: Controls, triggers and limits are used to manage risk exposures and to facilitate early identification of potential problem on a timely basis.
- Analytics and Reporting: Risk analysis and reports prepared at the respective entities and consolidated level as well as business level are regularly escalated to the senior management and relevant Boards to ensure that the risks remain within the established appetite and to support an informed decision-making process.

Risk Documentation and Infrastructure

The Group recognises that effective implementation of the risk management system and process must be supported by a robust set of documentation and infrastructure. Towards this end, the Group has established frameworks, policies and other relevant control documents to ensure clearly defined practices and processes are implemented consistently across the Group.

In terms of risk infrastructure, the Group has organised its resources and talents into specific functions, and invested into technology, including data management to support the Group's risk management activities.

Risk Culture

Risk management is integral to all aspects of the Group's activities and is the responsibility of all employees across the Group. In line with regulatory requirements and industry best practices, the Group subscribes to the principle that "*Risk and Compliance is Everyone's Responsibility*" and hence, risk management is a core responsibility of the respective businesses and operating units. This has been articulated and documented in the risk management framework of the Group.

Guided by the said principle, the Group has launched a Risk Culture Awareness programme which comprises training, awareness campaigns and roadshows within the Group (including overseas branches and subsidiaries) to promote a healthy risk culture. A strong risk culture minimises the Group's exposure to financial and non-financial risks including reputational impact, over time.

In addition, the Group has implemented the Business Risk & Compliance Officer ("BRCO") programme that aims to cultivate proactive risk and compliance management and to establish a robust risk culture. The BRCO programme entails the appointment of BRCO at the respective business and functional units to provide real time advisory on risk and compliance matters.

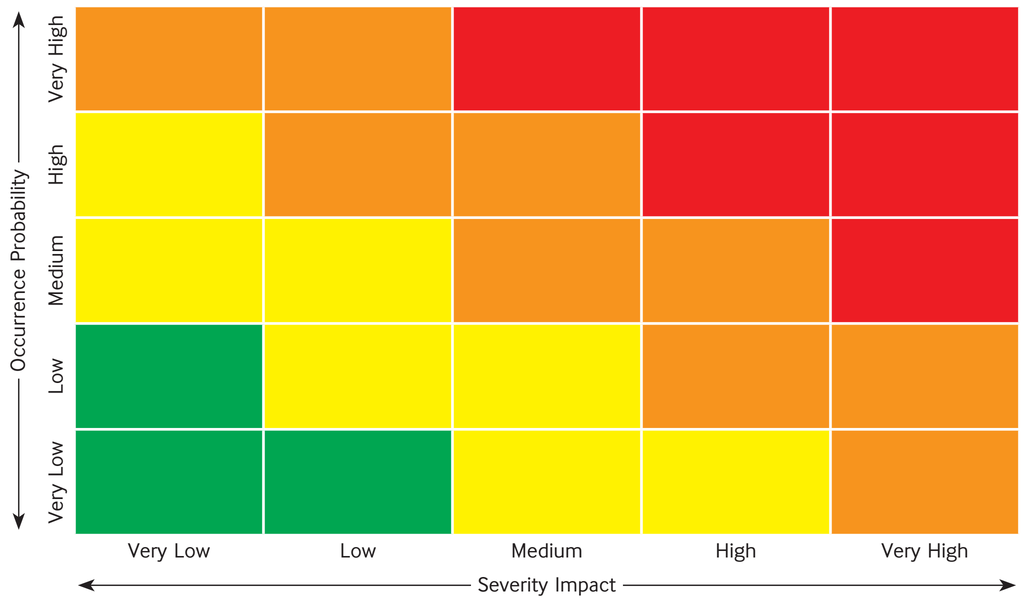
The implementation of the BRCO programme is in line with the 'Three Lines of Defence' model practised globally. There is clear accountability of risk ownership across the Group. The model is depicted in the diagram below:

FIRST LINE	SECOND LINE	THIRD LINE
Business/Functional Level	**Group Risk Management & Group Compliance**	**Group Internal Audit**
• Responsible for managing day-to-day risks and compliance issues • BRCO is to assist business/functional unit in day-to-day risks and compliance matters	• Responsible for oversight, establishing governance and providing support to business/functional unit on risk and compliance matters	• Provide independent assurance to the Board that risk and compliance management functions effectively as designed

Risk Assessment

The Group has an established and comprehensive process for risk identification at every stage of the risk taking activities, namely transactional, product and even at the respective entities and Group level. Risks are also identified through Operational Risk Loss Event reporting and Portfolio thematic analysis. As part of the Group's periodic material risk assessment, the Group reviews the types and components of material risks, determines its quantum of materiality and refinement of processes taking into consideration the feedback received, including the independent reviews.

Material risk assessment is measured from the dimension of occurrence probability and severity impact. In addition, risk assessment also considers amongst others, the effectiveness of controls in place, and the impact to financial and non-financial indicators such as reputational risk. These are translated into a heat map matrix to derive the materiality of the risk as shown in the table below:



The use of the above matrix is a simple mechanism to increase visibility of risks and assist in decision making. The Group considers residual risks which fall within the Amber and Red zones are 'Significant' and 'Material', which may have severe impact to the Group's financials and/or reputation. Significant efforts will be taken to manage and mitigate these risks events.

Risk and Control Self-Assessment

To further support and promote accountability and ownership of risk management, a Risk and Control Self-Assessment ("RCSA") framework has been implemented in the business and functional units within the Group as part of the risk management process. These business and functional units are required to identify and document the controls and processes for managing the risks arising from their business activities and operations, as well as to assess the effectiveness thereof to ensure that the risks identified are adequately managed and mitigated. On completion of the RCSA exercise, all business and functional units within the Group are required to submit their respective results to Group Operational Risk Management and Group Shariah Risk Management for review prior to tabling the RCSA results to the GCRC for deliberation and further action where necessary.

KEY INTERNAL CONTROL PROCESSES

The Group's system of internal control is designed to manage and reduce risks that will hinder the Group from achieving its goals and objectives. It encompasses the policies, procedures, processes, organisational structures and other control aspects that are implemented for assuring the achievement of the Group's objectives in operational effectiveness and efficiency, reliable financial reporting and compliance with laws, regulations and internal policies.

The key processes established by the Board that provide effective governance and oversight of internal control systems include:

CONTROL ENVIRONMENT AND CONTROL ACTIVITIES

Organisation Structure

The Group has a formal organisational structure with clearly defined lines of accountability and responsibility, authority limits and reporting. The organisational structure provides the basic framework to help the Group's operations proceed smoothly and functionally as well as depicting the span of control in ensuring effective supervision of day-to-day business conduct and accountability.

Policies and Procedures

Policies, procedures and processes governing the Group's businesses and operations are documented and communicated group-wide as well as made available to employees through the Group's intranet portal for ease of reference and compliance. These policies, procedures and processes are reviewed and updated by the business and functional units through a structured review and approval process to cater to changes in laws and regulations as well as changes to the business and operational environment.

Authority Limits

The Board has approved the Group Manual of Authority ("MOA") which defines the approving authority with its approving limits delegated to the various levels of Management in the Group to ensure accountability and responsibility. The Group MOA is reviewed periodically and updated in line with changes in the organisation structure, business environment or operational needs.

Information Technology (IT) Security

The Group regards IT security as a very high priority to ensure the confidentiality, integrity and availability of the Group's information assets and IT infrastructure.

IT security in the Group is achieved through the implementation of a risk based control approach which includes documented policies, standards, procedures and guidelines as well as organisational structures and, software and hardware controls.

With the increasing number of cyber threats globally as well as locally, the Group has established a Cyber Coordination and Command Centre to ensure that there is a structured process of prompt monitoring and timely response to cyber threats and incidents.

In order to strengthen and enhance the level of information security management, the Group has obtained certifications of ISO/IEC27001:2013 - Information Security Management System and ISO/IEC 20000:2011 - Information Technology Service Management, in addition to complying with various regulatory requirements on managing information technology risk holistically.

Budgeting Process

A robust budgeting process is established requiring all key operating companies in the Group to prepare budgets and business plans annually for approval by the respective Boards. The Group's budget and business plans as well as strategic initiatives, taking into account the established risk appetite, are deliberated at the Board where the Group budget is presented.

Human Capital Management

One of the key constituents of any internal control system is its people and that our system of risk management and internal control is dependent on the responsibility, integrity and sound judgement that employees apply to their work. Hence, the Group has in place policies and procedures that govern recruitment, appointment, performance management, compensation and reward as well as policies and procedures that govern discipline, termination and dismissal.

For sustainable growth, the Group places emphasis on human capital development, talent management and succession planning. To enhance employee competencies, structured and technical trainings as well as management and leadership workshops are provided to them based on their identified needs during the annual performance assessment. For talent management, initiatives such as Leadership Development Programme, Individual Development Plan and mentoring are implemented to develop identified talents in the Group to facilitate the continuous supply of high potentials and suitable successors for future leadership roles.

Group Code of Ethics and Conduct

The Bank Negara Malaysia's Code of Ethics for banking institutions has been adopted and institutionalised within the Group. The Group Code of Ethics and Conduct ("the Code") sets out the standards of good and ethical banking practices, as well as aims to maintain confidence in the security and integrity of the Group's business practices. It is a requirement that all employees of the Group understand and observe the Code. New recruits are briefed on the Code and are required to sign the Employee Declaration of Compliance Form upon joining the Group.

The Group has also established the Gifts and Hospitability Guidelines to promote integrity and transparency for giving and receiving gifts. The Guidelines complement the Code and are designed to help the Group and its employees understand the respective parties' obligations in upholding corporate integrity about gifting.

Group Anti-Money Laundering and Counter Financing of Terrorism Policy

The Group Anti-Money Laundering and Counter Financing of Terrorism ("AML/CFT") Policy is drawn up in accordance with the Anti-Money Laundering, Anti-Terrorism Financing and Proceeds of Unlawful Activities Act 2001 and Bank Negara Malaysia's standards on AML/CFT. It sets out the high level standards towards building a stronger and robust AML/CFT compliance regime within the Group, facilitates consistency in managing the AML/CFT compliance risk across the local and regional entities within the Group, and sets out the Group's policy statements in respect of the general principles and key measures to which the Group adheres to.

Pursuant to the Group AML/CFT Policy, the entities and/or employees within the Group are required to adopt Risk Based Approach ("RBA") to customer acceptance and implement the AML/CFT Compliance Programme framework which includes customer due diligence ("CDD") requirements, monitoring of customer activities/transactions, reporting of suspicious transactions, record keeping, AML/CFT training, protection of customer information, and enforcement actions for non-compliance to the requirements.

The Group AML/CFT Policy also outlines the roles and responsibilities as well as establishes clear accountability of the Board of Directors, Senior Management and all employees within the Group.

The Board has an oversight responsibility for establishing the AML/CFT policies and minimum standards while the Senior Management is accountable for the implementation and management of AML/CFT compliance programmes in accordance with the policies and procedures as approved by the Board.

Group Fraud Risk Management Policy

The Group Fraud Risk Management Policy is designed to promote consistent organisational behaviour through the development, implementation, and regular review of fraud prevention, detection and response strategies. The Policy defines the core governing principles for fraud management within the Group which include leadership and ethical culture, fraud awareness and prevention, fraud control and detection, fraud reporting and escalation as well as fraud response with appropriate corrective actions.

Business Continuity Management

The Group recognises and is fully committed to the need to provide uninterrupted critical services to its customers, ensure the safety of its employees, protect its assets/data and safeguard the interest of its key stakeholders that collectively ensure the viability of the organisation. The Group's Business Continuity Management ("BCM") Programme is based on good business continuity practices and guidelines which are in line with the Bank Negara Malaysia and internationally recognised standards. The overall framework is to build organisational resilience with effective response mechanism to safeguard the interests of key stakeholders, reputation and brand.

The Board has an oversight function on the Group's BCM readiness through the BRC, IRMC and GCRC. The Group Business Continuity Steering Committee is the management committee established to oversee the Group's business continuity framework, policies, budget and plans, and reports to GCRC.

The Group has ongoing and actively managed BCM programmes, which include effective crisis management to deal with real life crisis. The BCP Programmes are subject to regular testing/exercising to ensure their efficacy, reliability and functionality. Simulation exercises and drills are conducted to familiarise and equip staff with the skills and techniques required to ensure that in the event of any disruption, critical business processes can continue or be recovered in a timely manner.

INFORMATION AND COMMUNICATION

Performance Review

Regular and comprehensive information is provided by Management to monitor its performance against the strategic business plan and the annual budget approved by the Board. This information covers all key financial and operational indicators as well as key strategic initiatives undertaken by the Group during the year.

The Board and the Group Management Committee ("GMC") receive and review financial reports on the Group's monthly and quarterly financial performance against approved targets and the reasons for any significant variances as well as measures that are being put in place to meet such targets.

The heads of the core businesses and functions in the Group present their respective management reports to the GMC at its monthly meeting, covering areas such as financial performance, key activity results and new business proposal or process for information of and deliberation by the GMC.

Group Whistle Blower Policy

There is an established process for reporting anyone found to be abusing or circumventing processes and controls of the Group. All employees are made aware of the Group's whistle blowing policy and its processes and are accorded the opportunity to report via the whistle-blowing mechanism with the assurance that the report will be dealt with confidentially that the complainant's identity will be protected and that the complainant will be protected from any harassment or victimisation at work due to the disclosure.

Incident Management Reporting

To complement the Group's system of internal control, a comprehensive incident management reporting system has been implemented to ensure proper escalation and management of incidents according to the level of severity. The incident management reporting system also ensures that all incidences with material risk and losses are escalated promptly to Senior Management and the Board with necessary steps taken to mitigate any potential risks that may arise. This enables the decision makers to undertake informed decision making and be kept up to date on situations as well as manage risks effectively.

MONITORING

Board Committees

Board Committees have been set up to assist the Board to perform its oversight functions, namely the BRC, BAC, Board Nominating & Remuneration Committee, Board Credit Committee, Board Technology Committee and IRMC. These Board Committees have been delegated with specific duties to review and consider all matters within their scope of responsibility as defined in their respective terms of reference.

Group Management Committee

The Group Management Committee ("GMC") comprises the Group Managing Director as the Chairman, the Chief Executive Officers/Managing Directors of the relevant key operating subsidiaries and the key Senior Management of the Group. The GMC provides the leadership and direction in the implementation of strategies and policies approved by the Board and meets monthly to discuss and deliberate strategic matters that impact the Group's operations.

Management Audit Committee

Management Audit Committees ("MACs") are established at the key operating entities in the Group to ensure timely rectification of any audit findings and the underlying causes highlighted by the internal and external auditors, and regulators. The status of rectification of all audit findings and the mitigation actions taken by Management to adequately address the underlying causes are closely monitored by the MACs at every meeting.

The Bank's MAC comprising senior level representatives from different business/ functional groups is chaired by the Managing Director of the Bank. The Bank's MAC meet monthly and the minutes of meetings together with the relevant audit reports are subsequently tabled to the BAC for information, deliberation and direction for further action where required.

Group Compliance

Compliance is the collective responsibility of the Board, Senior Management and every employee of the Group. The compliance function forms an integral part of the Group's risk management and internal control framework. Because a strong compliance culture reflects a corporate culture of high integrity and ethics, everyone is expected to promote self-regulation and be accountable for his or her own activities while maintaining ethical principles and behaviour.

In addition to day-to-day monitoring, Group Compliance's commitment towards instilling a strong compliance culture across the Group is demonstrated through the establishment of a robust compliance monitoring framework which includes, amongst others, implementation of comprehensive compliance policies, periodic compliance risk assessment/reviews, regular engagement sessions with business and functional units and conduct of continuous training/awareness programmes across the Group to ensure that all employees are well informed of the latest regulatory requirements.

The Group Shariah Business Compliance has also been established in the Group in order to assist Group Compliance in monitoring the Bank's Islamic banking activities.

Further, the Boards and Senior Management are apprised of the Group's state of compliance through the submission of the Group Compliance report on a periodic basis.

Shariah Compliance

In line with the Shariah Governance Framework for Islamic Financial Institutions issued by Bank Negara Malaysia, a comprehensive Shariah Governance Framework has also been put in place by the Group which encompasses the concept of Shariah, Shariah governance and its reporting structure, roles and responsibilities, and the key principles underpinning the components of the Shariah governance structure.

Various activities involving Shariah reviews, control self-assessment, research, trainings and briefings aimed at creating awareness as well as continuous learning programmes were conducted throughout the year to educate employees on the importance of Shariah requirements and compliance surveillance.

INTERNAL AUDIT

Group Internal Audit ("GIA") reports functionally to the BAC and is independent of the operations and activities it audits. The GIA's main responsibility is to provide an objective and independent assessment on the adequacy and effectiveness of the Group's risk management, control and governance processes implemented by the Management.

The internal audit universe covers all key activities of the Group, including that of its branches, business centres, overseas operations, representative offices, subsidiaries as well as outsourced activities. GIA adopts a risk-based approach in determining the auditable units and frequency of audits in ensuring that the audit resources are prioritised in line with the Group's key risks and areas of focus which are identified based on GIA's risk assessment methodology.

The areas to be audited are documented in the internal audit plan that is developed based on a risk-based approach and is approved by the BAC annually. Audit reports which include detailed audit findings, GIA's comments and recommendations, and Management's response are tabled to MACs and BAC on a monthly basis. In addition, Shariah Audit reports are also tabled to the Shariah Committee for information and deliberation.

The established MACs are tasked to ensure that issues raised by GIA, external auditor and regulators are addressed within an appropriate and agreed timeline. Confirmation to this effect must be provided by Management to GIA for verification before the issues concerned can be closed at the MACs.

The Group Chief Internal Auditor reports functionally to the BAC and administratively to the Group Managing Director to ensure GIA's independence from Management.

Further information on the GIA function is provided in the Board Audit Committee Report of this Annual Report.

CONCLUSION

The Board, through the BAC, BRC and IRMC, confirms that it has reviewed the adequacy and effectiveness of the Bank's risk management and internal control system.

The Board has further obtained assurance from the Managing Director of the Bank and the Group Chief Financial Officer that the Bank's risk management and internal control system is operating adequately and effectively in all material aspects, based on the risk management and internal control system of the Bank.

Based on the monthly updates from its Board Committees and the assurance received from the Management, the Board is of the view that the Bank's risk management and internal control system is operating adequately and effectively for the financial year under review and up to the date of approval of this statement.

BOARD AUDIT COMMITTEE REPORT

COMPOSITION AND ATTENDANCE OF MEETINGS

During the year, a total of thirteen (13) Board Audit Committee ("BAC") meetings were held. The BAC comprises the following members who are all independent directors and the details of attendance of each member at the BAC meetings held during the year are as follows:

Composition of BAC	Attendance at Meetings
1. Tan Sri Dr Rebecca Fatima Sta Maria (Chairperson/Independent Non-Executive Director)	13/13 (100%)
2. Tan Sri Saw Choo Boon (Member/Senior Independent Non-Executive Director)	12/13 (92%)
3. Ms Ong Ai Lin (Member/Independent Non-Executive Director) – Appointed on 1 July 2017	7/7 (100%)
4. Mr Ong Seng Pheow (Member/Independent Non-Executive Director) – Retired on 19 November 2017	9/11 (82%)
5. Dato' Sri Haji Syed Zainal Abidin Syed Mohamed Tahir (Member/Independent Non-Executive Director) – Resigned on 1 July 2017	4/6 (67%)

The BAC meetings were also attended by the Managing Director of RHB Islamic Bank Berhad and the Group Chief Internal Auditor while the attendance of other Senior Management is by invitation, depending on the matters deliberated by the BAC.

The BAC undertakes the functions of the Audit Committee of the major operating entities within the Group encompassing RHB Bank Berhad ("RHB Bank"), RHB Investment Bank Berhad, RHB Islamic Bank Berhad and RHB Insurance Berhad.

Key matters deliberated at the BAC meetings together with the BAC's recommendations and decisions are summarised and presented to the Board, in the same month, by the Chairperson or representative of the BAC. This allows the Board to be timely apprised of significant matters deliberated by the BAC and for the Board to provide direction, if necessary. Extracts of the minutes of the BAC meetings held were provided to the Board for their information.

AUTHORITY

The BAC is authorised by the Board to, among others, review and investigate any matters within its terms of reference; have direct communication channels with the external and internal auditors; obtain independent professional advice, if necessary, at the Company's expense; and access to Management as well as resources to enable effective discharge of its functions. The full terms of reference, including the authority, duties and responsibilities of the BAC are published in RHB Bank's website.

SUMMARY OF BAC ACTIVITIES IN 2017

The work carried out by the BAC in the discharge of its duties and responsibilities during the financial year are summarised as follows:

1. Financial Reporting

a) Reviewed the quarterly unaudited financial results and the annual audited financial statements of RHB Islamic Bank Berhad before recommending them for the Board's approval. The review process encompassed the following:

- Reviewed changes in accounting policy and adoption of new or updated accounting standards, and its impact to the financial statements.
- Reviewed the financial statements and sought explanations from the Senior Management including the Group Chief Financial Officer on any significant changes between the current and corresponding quarter/period to assess their reasonableness.

b) Discussed with the external auditors the following matters identified during the statutory audit for the financial year ended 31 December 2017 as highlighted in their Audit Committee Report:

- Significant audit and accounting matters including credit, impairment assessment and taxation related matters;
- Summary of uncorrected misstatements; and
- Updates on the extended audit procedures on MFRS 9 implementation.

2. Internal Audit

a) Reviewed and approved the Group Internal Audit ("GIA")'s annual audit plan for the financial year 2017 in November 2016 to ensure adequacy of scope, coverage and resources for the identified auditable areas.

b) Reviewed GIA's risk-based methodology in assessing the risk levels of the Group's various business and functional areas for the audit planning purpose with emphasis on high and above average risk areas which are required to be audited annually whilst moderate and low risk areas are subject to a cycle audit.

c) Reviewed the staffing requirements of GIA including the skillsets and core competencies of the internal auditors to ensure effective discharge of GIA's duties and responsibilities.

d) Reviewed the GIA's audit activities undertaken for the financial year covering the planned audit assignments, ad-hoc audit projects, review of policies, processes and procedures, and IT project participation.

e) Reviewed and appraised the performance of the Group Chief Internal Auditor and assessed the effectiveness of the internal audit function.

f) Reviewed and deliberated on the minutes of all MAC meetings, internal audit reports, audit recommendations and Management's responses to these recommendations as well as the timely mitigation actions taken by Management to improve the system of internal controls and its processes on the areas highlighted.

g) Reviewed and deliberated on the investigation reports tabled to the BAC and provided directions, where necessary, to address and improve the internal control weaknesses highlighted.

h) Reviewed the inspection and examination reports issued by the regulatory authorities and the Management's response as well as the remedial actions taken by Management in respect of the reported findings to ensure that all matters highlighted in these reports had been adequately and promptly addressed by Management.

3. **External Audit**

a) Reviewed the 2017 audit plan of the external auditors for RHB Banking Group at the BAC meeting held on 17 October 2017 covering the audit strategy, risk assessment, areas of audit emphasis for the year.

b) Reviewed with the external auditors, the results of their audit together with their recommendations and Management's response to their findings as detailed in the following reports, and provided BAC's views and directions on areas of concern where necessary:

Audit Report issued by External Auditors in 2017	Date tabled to BAC
Final Audit Committee Report for the financial year 2016	20 January 2017
Internal Control Report for the financial year 2016	23 March 2017
Limited review of the unaudited financial statements of RHB Bank and RHB Islamic Bank for the financial period ended 30 June 2017	21 July 2017

The BAC further directed the respective MACs to track the audit findings highlighted by the external auditors in their Internal Control Report to ensure timely resolution of all matters by Management.

c) Met twice with the external auditors on 20 January 2017 and 17 October 2017 without the presence of Management and Executive Directors to enable the external auditors to discuss on matters with the BAC privately.

d) Reviewed the appointment of the external auditors for the provision of non-audit services before recommending them for the Board's approval. Areas that are considered include the external auditors' expertise, adequacy of knowledge and experience required for the services rendered, competitiveness of fees quoted and whether its independence and objectivity would be impaired.

Reviewed on a quarterly basis, the non-audit services rendered by the external auditors and the related fees taking into consideration the fee threshold established under the Group policy to ensure that the external auditors' independence and objectivity were not compromised. The total non-audit fees incurred as a percentage of the total statutory audit and other audit related services fees for the financial year 2017 for RHB Banking Group was 57.41% which is within the policy threshold.

For the financial year 2017, the main non-audit services rendered by the external auditors are as follows:

- Conducted validation of impairment models for the purpose of Malaysian Financial Reporting Standard ("MFRS") 9 implementation;
- Provided services in relation to the proposed merger (the merger discussion subsequently ceased); and
- Performed statutory requirement of Perbadanan Insurans Deposit Malaysia ("PIDM") validation program for assessment year 2017.

e) Reviewed the external auditors' performance and independence before recommending them to the Board for reappointment as external auditors for the Group:

- The external auditors have declared in their 2017 audit plan, which was tabled to the BAC in October 2017, that they have maintained their independence for the audit of the financial statements of the Group in accordance with the firm's requirements and with the provisions of the By-Laws on Professional Independence of the Malaysian Institute of Accountants. They have further declared that the non-audit services provided to the Group during the year have not compromised their independence as external auditors of the Group.
- The annual assessment on the external auditors covering the key areas of performance, independence and objectivity in accordance with the BNM Guidelines on External Auditor.
- The performance of the external auditors was also assessed through a survey completed by the Management personnel of the Group based on their dealings with the external auditors covering areas such as the quality of audit work, coordination during planning and execution of audit work, technical accounting and business knowledge, timeliness and staff continuity.

- A comprehensive review was also conducted in December 2017 prior to the reappointment of the external auditors to assess its independence and the potential risk of familiarity threat at all the banking entities within the Group. The comprehensive review covered the following three main categories:

Categories	Main areas assessed
(i) Governance and independence	Rotation of audit partner and key engagement team staff; meeting with the BAC without Management to discuss their objectivity and independence; any relationship between the external auditors, its staff and the Group; any safeguards in place to protect the external auditors' independence when approving non-audit services; and nature of non-audit services provided by the external auditors to the Group.
(ii) Communication and interaction	Communication to the BAC on a timely basis in relation to audit planning, audit strategy, significant audit and accounting issues, and related risks and control weaknesses, areas of significant judgements made by Management and their impact on the financial statements.
(iii) Quality of services and resources	Audit firm's presence internationally; external auditors demonstrate appropriate technical knowledge and expertise; external audit team made up of sufficient and suitably experienced staff; meeting deadlines in providing their services; and responded timely to issues.

The comprehensive review was conducted by Group Finance and independently verified by GIA prior to tabling to the BAC for deliberation.

4. Related Party Transactions and Conflict of Interest

a) Reviewed the reports of related party transactions ("RPTs") on a quarterly basis covering the nature and amount of the transactions including any possible conflict of interest ("COI") situations in ensuring that the terms and conditions of the transactions are commercially based and at arm's length.

b) The review covered the aggregate consideration of Recurrent RPTs ("RRPTs") which are individually tracked and monitored against the ceiling set to ensure proper reporting and disclosures in accordance with the regulatory requirements.

c) The Group has in place an approved policy on RPTs which governs the process of identifying, evaluating, approving, reporting and monitoring of RPTs, RRPTs and potential COI situations as well as outlining the duties and responsibilities of the relevant parties involved in the RPT process.

TRAINING

During the year, the BAC members have attended various training programmes, conferences and seminars to keep abreast of latest developments as well as to enhance their knowledge for the discharge of their duties and responsibilities.

Details of the trainings attended by BAC members are as follows:

Name of Director(s)	Training Programme Attended
YBhg Tan Sri Dr Rebecca Fatima Sta Maria	Peer-2-Peer (P2P) Lending and Crowdfunding/ Crowdsourcing by Group Chief Operations Officer
	Cryptocurrency and Blockchain Technology by Neuroware
	Islamic Banking by 2030: Impact of Digital Economy, Fintech & Sustainability as Forces of Change by SHAPE
	Capital Market Director Programme by SIDC: – Module 1 – Module 2A – Module 2B – Module 3 – Module 4
	Workshop on Forensic Accounting and Digital Forensics by Alliance IFA

Name of Director(s)	Training Programme Attended
YBhg Tan Sri Saw Choo Boon	Peer-2-Peer (P2P) Lending and Crowdfunding/ Crowdsourcing by Group Chief Operations Officer
	Cryptocurrency and Blockchain Technology by Neuroware
	Islamic Banking by 2030: Impact of Digital Economy, Fintech & Sustainability as Forces of Change by SHAPE
	Board Excellence: How to Engage and Enthuse Beyond Compliance with Sustainability by Bursa Malaysia
	Promoting Prosperity by Improving Women's Rights by The World Bank
	National Conference: Companies Act - From Policies to Implementation by Companies Commission of Malaysia
	Fraud Risk Management Workshop by Bursa Malaysia
	Business Ethics and Integrity: Key to Sustainability in the Digital Economy by Federation of Malaysian Manufacturers
	National Convention on Good Regulatory Practice by Malaysia Productivity Corporation
	ASEAN Economic Conference
Ms Ong Ai Lin	New Directors' In-House Orientation by Group Company Secretary
	Cyber Landscape In The Malaysian Financial Industry by AICB
	Mandatory Accreditation Programme for Directors of Public Listed Companies by ICLIF
	Malaysian Institute of Accountants Annual Conference 2017
Mr Ong Seng Pheow	Cryptocurrency and Blockchain Technology by Neuroware
	Islamic Banking by 2030: Impact of Digital Economy, Fintech & Sustainability as Forces of Change by SHAPE
	Workshop on Forensic Accounting and Digital Forensics by Alliance IFA
	Malaysian Code on Corporate Governance: Expectation and Implications by SIDC
	Bankruptcy (Amendment) Act 2017 by Messrs Shook Lin & Bok
	Fintech Opportunities for the Financial Services Industry in Malaysia by FIDE Forum
	Board In The Digital Economy by SIDC
	Malaysian Code on Corporate Governance: Expectation and Implications by SIDC

INTERNAL AUDIT FUNCTION

RHB Banking Group has an in-house internal audit function, which is guided by its Internal Audit Charter, Bank Negara Malaysia ("BNM") Guidelines on Internal Audit Function of Licensed Institutions (BNM/RH/GL 013-4) and the Institute of Internal Auditors' latest International Professional Practices Framework. GIA's main responsibility is to provide an objective and independent assessment on the adequacy and effectiveness of the Group's risk management, internal control and governance processes implemented by the Management.

The GIA is headed by Mr Alex Tan Aun Aun who has more than 25 years of multifaceted experience in the banking business, with 10 years' experience in internal auditing. He holds a Bachelor of Commerce (Finance) degree from the University of Toronto and is a member of The Institute of Internal Auditors Malaysia.

The Group Chief Internal Auditor ("Group CIA") reports functionally to the BAC and administratively to the Group Managing Director. To further preserve the independence of the GIA function, the Group CIA's appointment and performance appraisal, as well as the GIA's scope of work and resources, are approved by the BAC.

Internal Audit Charter

The Internal Audit Charter ("Audit Charter") defines the purpose, authority and responsibility of the internal audit function and is approved by the Board. The approved Audit Charter is published in the Group's intranet portal, which can be viewed by all employees of the Group.

The Audit Charter is reviewed by the Group CIA every two years to assess whether the GIA's purpose, authority and responsibility, as defined in the Audit Charter, continue to be adequate and relevant to enable the audit function to accomplish its objectives.

Summary of GIA's Activities

The main activities undertaken by GIA during the financial year are summarised as follows:

a) Prepared the annual risk-based audit plan for RHB Banking Group which includes the audit objectives and scope, and manpower requirements for each planned auditable unit.

b) Conducted audits as per the approved audit plan as well as ad hoc reviews and investigations requested by Management or regulators during the year.

c) Audited key areas during the financial year which included the Branches, Credit Underwriting, Business Centres, Treasury Operations, IT Security, Head Office functions, Shariah Compliance, Investment Banking Business, Asset Management, Insurance Business and Overseas Operations.

d) Conducted audits as per regulatory requirements such as compliance with BNM's Guidelines on Anti-Money Laundering and Counter Financing of Terrorism, Disclosure of Customer Documents or Information, Single Counterparty Exposure Limit, Outsourcing, Product Transparency & Disclosure and PayNet's applicable rules, procedures and manual for payment and debt securities systems.

e) Carried out ad-hoc compliance and validation reviews as requested by regulators.

f) Monitored and followed up through the respective MACs on the timely rectification of any reported audit findings and the underlying causes highlighted by the internal and external auditors, and regulators. The status of any outstanding audit findings is summarised and reported to the BAC on a monthly basis.

g) Reviewed new or updated policies, procedures and processes as requested by Management to provide feedback on the adequacy of internal control systems.

h) Participated in system or product development activities to provide recommendations upfront on the relevant control features to be considered by Management.

i) Assisted the BAC in the annual exercise on the reappointment of external auditors by assessing its independence and potential risk of familiarity threat at all the banking entities within the Group.

j) Attended Management meetings as permanent invitee on a consultative and advisory capacity to provide independent feedback where necessary on internal control related matters.

k) Organised the MACs meetings, preparing meeting materials and preparing minutes of meetings for submission to BAC.

l) Prepared the BAC Report and the Statement on Risk Management and Internal Control for inclusion in the Annual Report 2017 of RHB Bank and the major operating entities in the Group (inclusive of RHB Islamic Bank Berhad).

Internal Audit Resources

The Group CIA, in consultation with the BAC and the Group Managing Director, decides on the appropriate resources required for the GIA taking into consideration the size and complexity of operations of the Group. The primary organisation chart/structure of GIA is reviewed and approved by the BAC annually.

As at 31 December 2017, GIA has 153 internal auditors with relevant academic/professional qualifications and experience to carry out the activities of the internal audit function.

Professional Proficiency

The Group CIA ensures that the internal auditors are suitably qualified and provided with the necessary trainings and continuous professional development for the purpose of enhancing their audit and relevant technical skills to perform their duties and responsibilities.

The internal auditors are further guided by the GIA Learning Development Framework to pursue the relevant certification programmes such as those offered by the Institute of Internal Auditors and Asian Institute of Chartered Banker in order for them to be proficient and competent in the relevant disciplines.

Based on each staff's Individual Development Plan for the year 2017, the internal auditors attended the relevant technical as well as leadership and management programmes offered by RHB Academy, the Group's Learning and Development Centre, and external programmes. For the year 2017, the internal auditors attended a total of 1,163 days of training, which translates to approximately 7.5 days per auditor.

Internal Audit Quality Assurance Review

To ensure effectiveness of the internal audit function, the Group CIA has developed and maintained a quality assurance and improvement programme that covers all aspects of the internal audit activities. The quality assurance programme assesses the effectiveness of processes within the internal audit function and identifies opportunities for improvement through both internal and external assessments.

The internal assessment is performed according to the approved annual Quality Assurance Review ("QAR") plan by a QAR team within GIA. The Head of QAR function reports directly to the Group CIA to maintain its independence of the internal audit activities within GIA.

In addition to the internal assessment, external quality assessment is conducted every three years by qualified professionals. The appointment of independent reviewer is subject to the Group's established procurement process and endorsed by the BAC.

The review covered a broad scope that includes conformance with the Definition of Internal Auditing, the Standards, and the Code of Ethics, and the internal audit charter, audit plan, policies and procedures in line with the requirements of the International Standards for the Professional Practice of Internal Auditing of the Institute of Internal Auditors ("IIA") and BNM guidelines.

In end 2016, a leading consulting firm was engaged to conduct an external quality assurance review on GIA. Based on the QAR report issued, GIA's activities conformed with the International Standards for the Professional Practice of Internal Auditing and IIA's Code of Ethics as well as its Definition of Internal Auditing, Internal Audit Charter, Policies, Manual and Procedures. There were also opportunities for improvement recommended which GIA had implemented accordingly.

SHARIAH COMMITTEE REPORT

INTRODUCTION

The Shariah Committee is established under RHB Islamic Bank Berhad ("the Bank" or "RHB Islamic Bank") with the following main objectives:

1. To perform an oversight and independent advisory role to the Board of Directors and/or the Management of the Bank on Shariah matters pertaining to the Bank's Islamic banking and finance business and operations.
2. To ensure effective working arrangements are established between the Shariah Committee, the Shariah Advisory Council ("SAC") of Bank Negara Malaysia ("BNM") as well as that of the Securities Commission ("SC").
3. To ensure the establishment of appropriate procedures in leading to the prompt compliance with Shariah principles.

SHARIAH GOVERNANCE

In ensuring the Bank's Islamic businesses and operations comply with Shariah principles, the Shariah Committee has been guided by the guiding principles and best practices to establish sound and robust Shariah governance. The Shariah governance structure of RHB Islamic Bank comprises the following functions:

i) The Board oversight on Shariah compliance aspects of the Bank's overall operations. It is the ultimate responsibility of the Board to establish appropriate Shariah governance framework of the Bank;

ii) Establishment of Shariah Committee with qualified members who are able to deliberate Islamic finance issue brought before them and provide sound Shariah decisions;

iii) Supportive and effective management responsible in providing adequate resources and capable manpower support to every function involved in the implementation of Shariah governance, to ensure the execution of business operations are in accordance with Shariah;

iv) Shariah Advisory over the processes and deliverables that is conducted on a continuous basis, to ensure all processes and outcomes satisfy the needs of Shariah;

v) Shariah Compliance to conduct regular assessment on Shariah compliance in the activities and operations of the Bank;

vi) Shariah Audit to conduct annual review and verify the Bank's key functions and business operations comply with Shariah;

vii) Shariah Risk Management is responsible to facilitate identification of potential Shariah non-compliance risk, and where appropriate recommend risk mitigation mechanism through implementation of risk management tools.

viii) Shariah Research to conduct a comprehensive and deep research on Shariah; and issuance and dissemination of Shariah decisions to the relevant stakeholders

SHARIAH COMMITTEE MEMBERS

The Shariah Committee comprises six* (6) qualified Shariah scholars. The assortment of knowledge, experience and approach from these mixed Shariah scholars are needed to position the Bank's operations and products to be globally accepted. Majority of the members have the prerequisite Shariah qualifications degree imposed by BNM. The remaining members are professionals from various backgrounds who possess expertise in the Islamic banking and finance industry.

The Shariah Committee members are:

No	Name of Shariah Committee Member	Nationality	Status
1.	Dr. Ghazali bin Jaapar	Malaysian	Chairman
2.	Assoc. Prof. Dr. Amir bin Shaharuddin	Malaysian	Member
3.	En. Mohd Fadhly bin Md. Yusoff	Malaysian	Member
4.	En. Wan Abdul Rahim Kamil bin Wan Mohamed Ali	Malaysian	Member
5.	Pn. Shabnam binti Mohamad Mokhtar	Malaysian	Member
6.	Prof. Dr. Joni Tamkin bin Borhan	Malaysian	Member

Note: Due to the demise of Prof. Dr. Joni Tamkin on 19 May 2017, the Shariah Committee of RHB Islamic Bank has been functioning with five (5) members.

DUTIES & RESPONSIBILITIES

The main duties and responsibilities of the Shariah Committee are:

1. Advise the Bank on Shariah matters in order to ensure that the Islamic banking and financing business and operations are Shariah compliant at all times;
2. Endorse the all framework, policies, manuals and procedures prepared by the Bank which have Shariah concern and to ensure that the contents do not contain any elements which are not in line with Shariah;
3. Endorse and validate the following documentation to ensure that the products comply with Shariah principles:
    i. the terms and conditions contained in proposal forms, contracts, agreements or other legal documentation used in executing transactions; and
    ii. the product manual, marketing advertisement, sales illustration and brochures used to describe a product.

4. Assess the work carried out by Shariah Compliance and Shariah Audit in order to ensure compliance with Shariah matters.
5. Provide advice to the Bank's legal counsel, auditor or consultant on Shariah matters as and when required to ensure compliance with Shariah principles;
6. Advise on matters to be referred to SAC of BNM, particularly matters which have not be resolved or endorsed by the SAC of BNM;
7. Provide written Shariah opinions particularly in the following circumstances:
    i. Where the Bank makes reference to the SAC of BNM for advice; or
    ii. Where the Bank submits applications to BNM or SC for new product approval in accordance with guidelines on product approval issued by BNM and SC.
8. Articulate Shariah issues involved and ensure that all advice and/or opinion be supported by relevant Shariah jurisprudential literature from established sources. The Shariah Committee is also expected to assist the SAC of BNM on any matters referred by the Bank.
9. Ensure that SAC of BNM's decisions/opinion/advice are properly implemented and adhered to by the Bank;
10. Prepare a report to certify the Annual Audited Account of RHB Islamic Bank for the financial period concerned.
11. In respect of matters concerning Islamic Capital Market (upon mandated):
    i. Ensure that the instruments are managed and administered in accordance with Shariah principles;
    ii. Provide expertise and guidance in all matters relating to Shariah principles, including the instrument's deed and prospectus, its structure and investment process, and other operational and administrative matters;
    iii. Scrutinise the instrument's compliance report as provided by the compliance officer, and investment transaction reports provided by, or duly approved by, the trustee to ensure that the investments are in line with Shariah principles; and
    iv. Prepare a report to be included in the interim and annual reports certifying whether the instrument had been managed and administered in accordance to Shariah principles for the period concerned.
12. Advise on payment of Zakat to the appropriate authority.

MEETINGS

A total of ten (10) meetings were held during the financial year ended 31 December 2017 which consist of eight (8) regular meetings and two (2) special meetings. All existing members have satisfied the minimum attendance requirement under BNM's Shariah Governance Framework which provides that a Shariah Committee member is required to attend at least 75% of the Shariah Committee meetings held in each financial year. Details of attendance of each member are as follows:

Name of Shariah Committee Member	Number of Meetings	
	Held	Attended
Dr. Ghazali Jaapar	10	10
Assoc. Prof. Dr. Amir Shaharuddin	10	10
En. Mohd Fadhly Md. Yusoff	10	10
En. Wan Abdul Rahim Kamil	10	9
Pn. Shabnam Mohamad Mokhtar	10	10
Prof. Dr. Joni Tamkin Borhan**	4	4

** Deceased on 19 May 2017

SPECIAL ENGAGEMENT & TRAINING

As part of the initiatives towards maintaining effective communication between the Shariah Committee and the Management and Board of Directors of RHB Islamic Bank, the following special engagement sessions were conducted in 2017:

1. Talk on "Impact of Digital Economy, FinTech & Sustainability as Force of Change"
2. Talk on "Global Perspective on Critical Success & Failure Factors in Islamic Financial Industry in 21st Century Banking"

In addition, the Shariah Committee members have actively participated in conferences and courses held locally and internationally as follows:

a. 38th Al-Barakah Annual Symposium on Islamic Economics, Jeddah, Saudi Arabia

b. 1st Salalah International Forum on Islamic Finance, Salalah, Sultanate of Oman

c. 17th Muzakarah Cendekiawan Syariah Nusantara 2017, Kuala Lumpur, Malaysia

d. 12th Muzakarah Penasihat Syariah Kewangan Islam 2017 (in conjunction with 14th Kuala Lumpur Islamic Finance Forum (KLIFF) 2017), Kuala Lumpur, Malaysia

e. Muzakarah Ahli Majlis Penasihat Syariah Institusi Kewangan di Malaysia ke-13, Jabatan Kemajuan Islam Malaysia, Kuala Lumpur, Malaysia

f. Shariah Investing Forum 2017, Kuala Lumpur, Malaysia

SHARIAH COMMITTEE ASSESSMENT

In compliance with BNM's Shariah Governance Framework, the Shariah Committee undergoes the process of assessing the effectiveness of the individual members and the Committee as a whole on a yearly basis. The Shariah Committee annual assessment exercise is primarily based on detailed questionnaire which distributed to the respective Committee members and the permanent invitees to the Shariah Committee meeting. The questionnaire encompasses considerations on the effectiveness of the Committee in discharging its duties and responsibilities as well as the individual member's level of skills and competency in the areas of expertise expected of a Shariah Committee member.

The results of the assessment are tabled to the Board Nominating & Remuneration Committee for review and recommendation and subsequently to the Bank's Board of Directors for approval.

CONTENTS

RESPONSIBILITY STATEMENT BY THE BOARD OF DIRECTORS

In the course of preparing the annual audited financial statements of the Bank, the Directors are collectively responsible in ensuring that the audited financial statements are drawn up in accordance with Malaysian Financial Reporting Standards, International Financial Reporting Standards and the provisions of the Companies Act, 2016 in Malaysia.

It is the responsibility of the Directors to ensure that the annual audited financial statements of the Bank present a true and fair view of the state of affairs of the Bank as at 31 December 2017 and of the financial results and cash flows of the Bank for the financial year ended 31 December 2017.

The audited financial statements are prepared on the going concern basis and the Directors have ensured that proper accounting records are kept, appropriate accounting policies are applied on a consistent basis and accounting estimates made are reasonable and fair so as to enable the preparation of the financial statements of the Bank with reasonable accuracy.

The Directors have also taken the necessary steps to ensure that appropriate systems are in place for the assets of the Bank to be properly safeguarded for the prevention and detection of fraud and other irregularities. The systems, by their nature, can only provide reasonable and not absolute assurance against material misstatements, whether due to fraud or error.

DIRECTORS' REPORT

The Directors submit herewith their report together with the audited financial statements of RHB Islamic Bank Berhad ('the Bank') for the financial year ended 31 December 2017.

PRINCIPAL ACTIVITIES

The Bank is principally engaged in the Islamic banking business and is committed to offer customers a comprehensive range of products and services in accordance with its Articles of Association and Shariah principles.

There have been no significant changes in these principal activities during the financial year.

FINANCIAL RESULTS

	RM'000
Net profit for the financial year	367,392

DIVIDENDS

No dividend has been paid or declared by the Bank since the end of the previous financial year.

The Directors do not propose any final dividend in respect of the current financial year at the forthcoming Annual General Meeting.

RESERVES AND PROVISIONS

All material transfers to or from reserves and provisions during the financial year are disclosed in the financial statements.

ISSUE OF SHARES

There were no issue of shares in the Bank during the financial year.

BAD AND DOUBTFUL DEBTS AND FINANCING

Before the financial statements of the Bank were made out, the Directors took reasonable steps to ascertain that proper actions have been taken in relation to the writing off of bad financing and advances and the making of allowance for impaired financing and advances, and satisfied themselves that all known bad financing and advances have been written off and adequate allowance had been made for impaired financing and advances.

At the date of this report, the Directors are not aware of any circumstances which would render the amount written off for bad financing and advances or the amount of allowance for non-performing financing and advances in the financial statements of the Bank inadequate to any substantial extent.

CURRENT ASSETS

Before the financial statements of the Bank were made out, the Directors took reasonable steps to ensure that any current assets, other than financing and advances, which were unlikely to realise in the ordinary course of business, their values as shown in the accounting records of the Bank, had been written down to an amount which they might be expected to realise.

At the date of this report, the Directors are not aware of any circumstances which would render the values attributed to the current assets in the financial statements of the Bank misleading.

VALUATION METHOD

At the date of this report, the Directors are not aware of any circumstances which have arisen which render adherence to the existing methods of valuation of assets or liabilities of the Bank misleading or inappropriate.

CONTINGENT AND OTHER LIABILITIES

At the date of this report, there does not exist:

(a) any charge on the assets of the Bank which has arisen since the end of the financial year which secures the liabilities of any other person; or

(b) any contingent liability of the Bank which has arisen since the end of the financial year other than in the ordinary course of business.

No contingent or other liability of the Bank has become enforceable, or is likely to become enforceable within the period of twelve months after the end of the financial year which, in the opinion of the Directors, will or may substantially affect the ability of the Bank to meet its obligations as and when they fall due.

CHANGE OF CIRCUMSTANCES

At the date of this report, the Directors are not aware of any circumstances not otherwise dealt with in this report or the financial statements of the Bank which would render any amount stated in the financial statements misleading or inappropriate.

ITEMS OF AN UNUSUAL NATURE

The results of the operations of the Bank for the financial year were not, in the opinion of the Directors, substantially affected by any item, transaction or event of a material and unusual nature.

There has not arisen in the interval between the end of the financial year and the date of this report any item, transaction or event of a material and unusual nature likely, in the opinion of the Directors, to affect substantially the results of the operations of the Bank for the financial year in which this report is made.

DIRECTORS OF THE BANK

The Directors of the Bank in office during the financial year and during the period from the end of the financial year to the date of the report are:

Dato' Abd Rahman Dato' Md Khalid	
Datuk Haji Faisal Siraj	
Dato' Foong Chee Meng	(Appointed on 1 August 2017)
Ong Ai Lin	(Appointed on 1 September 2017)
Dato' Adissadikin Ali	
Haji Md Ja'far Abdul Carrim	(Deceased on 19 October 2017)
Dato' Mohd Ali Mohd Tahir	(Resigned on 28 February 2017)
Dato' Sri Haji Syed Zainal Abidin Syed Mohamed Tahir	(Resigned on 1 August 2017)

In accordance with Article 68 of the Bank's Articles of Association, Datuk Haji Faisal Siraj retires by rotation at the forthcoming Annual General Meeting and, being eligible, offers himself for re-election.

In accordance with Article 73 of the Bank's Articles of Association, Dato' Foong Chee Meng and Ong Ai Lin retire at the forthcoming Annual General Meeting and, being eligible, offer themselves for re-election.

DIRECTORS' INTERESTS

None of the Directors holding office at the end of the financial year held any interest in the securities of the Bank or its related corporations during the financial year.

DIRECTORS' BENEFITS

Since the end of the previous financial year, no Director has received or become entitled to receive any benefit (other than Directors' remuneration and benefits-in-kind as disclosed in Note 30 to the financial statements) by reason of a contract made by the Bank or a related corporation with the Director or with a firm of which the Director is a member, or with a company in which the Director has a substantial financial interest.

During and at the end of the financial year, no arrangements subsisted to which the Bank is a party, being arrangements with the object or objects of enabling the Directors of the Bank to acquire benefits by means of the acquisition of shares in, or debentures of, the Bank or any other body corporate.

AUDITORS' REMUNERATION

Details of auditors' remuneration are set out in Note 29 to the financial statements.

HOLDING COMPANY

The Directors regard RHB Bank Berhad, a company incorporated in Malaysia and listed on Bursa Malaysia Securities Berhad, as the holding company.

ZAKAT OBLIGATION

The Bank only pays zakat on its business to zakat state authorities. The Bank does not pay zakat on behalf of the shareholder or depositors.

AUDITORS

The auditors, PricewaterhouseCoopers PLT (LLP0014401-LCA & AF 1146), have expressed their willingness to continue in office.

PricewaterhouseCoopers PLT (LLP0014401-LCA & AF 1146) was registered on 2 January 2018 and with effect from that date, PricewaterhouseCoopers (AF 1146), a conventional partnership was converted to a limited liability partnership.

This report was approved by the Board of Directors on 27 February 2018. Signed on behalf of the Board of Directors:

DATO' ABD RAHMAN DATO' MD KHALID
DIRECTOR

DATO' ADISSADIKIN ALI
CHIEF EXECUTIVE OFFICER/MANAGING DIRECTOR

Kuala Lumpur

REPORT OF THE GROUP SHARIAH COMMITTEE

In the name of Allah, The Most Gracious, The Most Merciful

We, Dr. Ghazali Jaapar, Assoc. Prof. Dr. Amir Shaharuddin, Mohd Fadhly Md. Yusoff, Wan Abdul Rahim Kamil Wan Mohamed Ali and Shabnam Mohamad Mokhtar, being five members of the Shariah Committee of RHB Islamic Bank Berhad ('Bank'), do hereby confirm on behalf of the members of the Committee, that we have reviewed the principles and the contracts relating to the transactions and applications introduced by the Bank during the financial year ended 31 December 2017.

We have also conducted our review to form an opinion as to whether the Bank has complied with Shariah rules and the principles and also with the specific rulings and guidelines issued by us.

The Bank's management is responsible for ensuring that the financial institution conducts its business in accordance with Islamic Shariah rules and principles. It is our responsibility to form an independent opinion, based on our review of the operations of the Bank, and to report to you.

We have assessed the work carried out by Shariah review and Shariah audit which included examining, on a test basis, each type of transaction, the relevant documentation and procedures adopted by the Bank.

We have performed our review so as to obtain all the information and explanations, which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the Bank has complied with Shariah rules and principles.

In our opinion:

(a) the main sources of income of the Bank during the financial year ended 31 December 2017 that we have reviewed are in compliance with the Shariah rules and principles;
(b) all investments that have been disclosed to us by the Bank conform to the basis that had been approved by us in accordance with Shariah rules and principles;
(c) all earnings that have been realised from sources or by means prohibited by the Shariah principles have been considered for disposal to charitable causes;
(d) the contracts and legal documents of the products used by the Bank that we reviewed are in compliance with the Shariah rules and principles;
(e) the products proposals including concept used by the Bank which have been reviewed and advised by us are in compliance with the Shariah rules and principles; and
(f) the calculation of zakat is in compliance with Shariah rules and principles.

We beg Allah, The Almighty to grant us success and lead us on the right path.

Wassalamu Alaikum Wa Rahmatullahi Wa Barakatuh

Dr. Ghazali Jaapar
Chairman of the Committee

Assoc. Prof. Dr. Amir Shaharuddin
Member of the Committee

Mohd Fadhly Md. Yusoff
Member of the Committee

Wan Abdul Rahim Kamil Wan Mohamed Ali
Member of the Committee

Shabnam Mohamad Mokhtar
Member of the Committee

Kuala Lumpur
27 February 2018

STATEMENTS OF FINANCIAL POSITION

AS AT 31 DECEMBER 2017

	Note	2017 RM'000	2016 RM'000
ASSETS			
Cash and short term funds	2	**2,029,860**	3,436,239
Securities purchased under resale agreements	3	**1,587,979**	2,353,950
Deposits and placements with banks and other financial institutions	4	**447,210**	537,141
Financial assets held-for-trading ('HFT')	5	**172,536**	10,177
Financial investments available-for-sale ('AFS')	6	**3,394,493**	3,459,647
Financial investments held-to-maturity ('HTM')	7	**3,820,734**	2,820,123
Financing and advances	8	**42,701,794**	33,841,566
Other assets	9	**90,934**	171,730
Derivative assets	10	**327,978**	402,763
Statutory deposits with Bank Negara Malaysia ('BNM')	11	**1,116,200**	1,051,050
Deferred tax assets	12	**16,513**	20,929
Property, plant and equipment	13	**6,193**	6,576
Intangible assets	14	**5,039**	4,750
TOTAL ASSETS		**55,717,463**	48,116,641
LIABILITIES AND EQUITY			
Deposits from customers	15	**37,850,205**	29,419,928
Deposits and placements of banks and other financial institutions	16	**4,394,801**	6,430,194
Investment account due to designated financial institutions	17	**8,102,698**	6,622,471
Obligations on securities sold under repurchase agreements		**604,163**	–
Bills and acceptances payable		**9,216**	9,050
Derivative liabilities	10	**327,723**	400,812
Recourse obligation on financing sold to Cagamas Berhad ('Cagamas')	18	**–**	815,243
Subordinated obligations	19	**755,393**	503,187
Other liabilities	20	**345,792**	957,863
Provision for tax and zakat		**15,623**	29,451
TOTAL LIABILITIES		**52,405,614**	45,188,199
Share capital	21	**1,273,424**	1,273,424
Reserves	22	**2,038,425**	1,655,018
TOTAL EQUITY		**3,311,849**	2,928,442
TOTAL LIABILITIES AND EQUITY		**55,717,463**	48,116,641
COMMITMENTS AND CONTINGENCIES	35	**24,280,522**	21,492,582

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

INCOME STATEMENTS

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2017

	Note	2017 RM'000	2016 RM'000
Income derived from investment of depositors' funds	23	**1,957,052**	1,750,096
Income derived from investment account funds	24	**375,939**	317,988
Income derived from investment of shareholders' funds	25	**175,518**	170,420
Allowance for impairment on financing and advances	26	**(66,734)**	(70,168)
Impairment losses written back/(made) on other assets		**336**	(549)
Total distributable income		**2,442,111**	2,167,787
Income attributable to depositors	27	**(1,329,395)**	(1,223,430)
Profit distributed to investment account holders		**(310,185)**	(260,626)
		802,531	683,731
Personnel expenses	28	**(27,082)**	(32,307)
Other overheads and expenditures	29	**(295,599)**	(219,767)
Profit before zakat and taxation		**479,850**	431,657
Zakat		**(3,500)**	(3,500)
Profit after zakat before taxation		**476,350**	428,157
Taxation	31	**(108,958)**	(103,373)
Net profit for the financial year		**367,392**	324,784
Earnings per share (sen):			
– Basic	32	**28.85**	27.40

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

STATEMENTS OF COMPREHENSIVE INCOME

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2017

	Note	2017 RM'000	2016 RM'000
Net profit for the financial year		**367,392**	324,784
Other comprehensive income/(loss):			
Items that will be reclassified subsequently to profit or loss:			
Financial investments AFS:			
– Unrealised net gain on revaluation		**23,601**	14,889
– Net transfer to income statement on disposal or impairment		**(2,529)**	(5,348)
Income tax relating to components of other comprehensive income	33	**(5,057)**	(2,290)
Other comprehensive income, net of tax, for the financial year		**16,015**	7,251
Total comprehensive income for the financial year		**383,407**	332,035

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

STATEMENTS OF CHANGES IN EQUITY

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2017

		← Non-distributable			→	Distributable	
	Note	Share Capital RM'000	Statutory Reserve RM'000	AFS Reserve RM'000	Regulatory Reserve RM'000	Retained Profits RM'000	Total RM'000
Balance as at 1 January 2017		**1,273,424**	**762,388**	**(31,944)**	**158,516**	**766,058**	**2,928,442**
Net profit for the financial year		**–**	**–**	**–**	**–**	**367,392**	**367,392**
Other comprehensive income/(loss) for the financial year:							
Financial investments AFS:							
– Unrealised net gain on revaluation		**–**	**–**	**23,601**	**–**	**–**	**23,601**
– Net transfer to income statement on disposal or impairment		**–**	**–**	**(2,529)**	**–**	**–**	**(2,529)**
Income tax relating to components of other comprehensive income	33	**–**	**–**	**(5,057)**	**–**	**–**	**(5,057)**
Other comprehensive income, net of tax, for the financial year		**–**	**–**	**16,015**	**–**	**–**	**16,015**
Total comprehensive income for the financial year		**–**	**–**	**16,015**	**–**	**367,392**	**383,407**
Transfer from statutory reserve		**–**	**(762,388)**	**–**	**–**	**762,388**	**–**
Transfer to regulatory reserve		**–**	**–**	**–**	**108,515**	**(108,515)**	**–**
Balance as at 31 December 2017		**1,273,424**	**–**	**(15,929)**	**267,031**	**1,787,323**	**3,311,849**
Balance as at 1 January 2016		1,173,424	681,192	(39,195)	160,361	520,625	2,496,407
Net profit for the financial year		–	–	–	–	324,784	324,784
Other comprehensive income/(loss) for the financial year:							
Financial investments AFS:							
– Unrealised net gain on revaluation		–	–	14,889	–	–	14,889
– Net transfer to income statement on disposal or impairment		–	–	(5,348)	–	–	(5,348)
Income tax relating to components of other comprehensive income	33	–	–	(2,290)	–	–	(2,290)
Other comprehensive income, net of tax, for the financial year		–	–	7,251	–	–	7,251
Total comprehensive income for the financial year		–	–	7,251	–	324,784	332,035
Issuance of shares	21	100,000	–	–	–	–	100,000
Transfer to statutory reserve		–	81,196	–	–	(81,196)	–
Transfer from regulatory reserve		–	–	–	(1,845)	1,845	–
Balance as at 31 December 2016		1,273,424	762,388	(31,944)	158,516	766,058	2,928,442

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

STATEMENTS OF CASH FLOWS

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2017

	2017 RM'000	2016 RM'000
Cash flows from operating activities		
Profit before zakat and taxation	**479,850**	431,657
Adjustments for:		
Depreciation of property, plant and equipment:	**2,591**	1,751
Amortisation of computer software license	**1,846**	2,102
Income from:		
– Investment on financial assets HFT	**(5,146)**	(2,538)
– Investment on financial investments AFS	**(145,448)**	(137,371)
– Investment on financial investments HTM	**(123,833)**	(86,232)
Net gain on disposal of financial investments AFS	**(2,529)**	(5,348)
Net loss on disposal of financial assets HFT	**683**	1,372
Net gain on early redemption of financial investments HTM	**(378)**	(301)
Net loss on fair value hedges	**1,078**	799
Net loss/(gain) on revaluation of derivatives	**11,199**	(116)
Unrealised loss/(gain) from financial assets HFT	**839**	(268)
Allowance for impairment on financing and advances	**79,077**	83,632
Property, plant and equipment written off	**–**	447
Intangible assets written off	**–**	1
Impairment losses (written back)/made on other assets	**(336)**	549
Operating profit before working capital changes	**299,493**	290,136
(Increase)/Decrease in operating assets:		
Securities purchased under resale agreements	**765,971**	(2,353,950)
Deposits and placements with banks and other financial institutions	**89,931**	80,931
Financing and advances	**(8,940,381)**	(3,035,570)
Financial assets HFT	**(158,735)**	11,505
Other assets	**80,796**	(38,446)
Statutory deposits with BNM	**(65,150)**	117,450
	(8,227,568)	(5,218,080)
Increase/(Decrease) in operating liabilities:		
Deposits from customers	**8,430,277**	1,491,899
Deposits and placements of banks and other financial institutions	**(2,035,393)**	1,119,622
Investment account due to designated financial institutions	**1,480,227**	271,817
Obligations on securities sold under repurchase agreements	**604,163**	–
Bills and acceptances payable	**166**	3,501
Subordinated obligations	**2,206**	68
Other liabilities	**(20,349)**	(770)
Amount due to holding company	**(601,227)**	625,000
Recourse obligation on financing sold to Cagamas	**(815,243)**	(167,517)
	7,044,827	3,343,620
Cash used in operations	**(883,248)**	(1,584,324)
Net tax and zakat paid	**(126,927)**	(109,609)
Net cash used in operating activities	**(1,010,175)**	(1,693,933)

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

STATEMENTS OF CASH FLOWS

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2017

	Note	2017 RM'000	2016 RM'000
Cash flows from investing activities			
Financial investments AFS and HTM			
– Purchases		**(1,449,453)**	(3,398,603)
– Proceeds from disposal		**546,222**	2,065,778
Property, plant and equipment:			
– Purchases		**(2,212)**	(390)
– Proceeds from disposal		**4**	–
Purchases of intangible assets		**(1,799)**	(1,289)
Financial assets HFT and financial investments AFS and HTM:			
– Profit income received		**147,329**	133,528
– Investment income received		**113,705**	82,110
Net cash used in investing activities		**(646,204)**	(1,118,866)
Cash flows from financing activities			
Proceeds from issuance of share capital		**–**	100,000
Issuance of subordinated obligations		**250,000**	–
Net cash generated from financing activities		**250,000**	100,000
Net decrease in cash and cash equivalents		**(1,406,379)**	(2,712,799)
Cash and cash equivalents at the beginning of the financial year		**3,436,239**	6,149,038
Cash and cash equivalents at the end of the financial year	2	**2,029,860**	3,436,239

		← Cash Changes	→	Non-Cash Changes	
	Balance as at the beginning of the financial year RM'000	Net cash flow from financing activities RM'000	Net cash flow from operating activities RM'000	Accrued profit RM'000	Balance as at the end of the financial year RM'000
2017					
Subordinated obligations	**503,187**	**250,000**	**(30,867)**	**33,073**	**755,393**
2016					
Subordinated obligations	503,119	–	(24,750)	24,818	503,187

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

SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES AND CRITICAL ACCOUNTING ESTIMATES AND ASSUMPTIONS

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2017

(A) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The following accounting policies have been used consistently in dealing with items which are considered material in relation to the financial statements. These accounting policies have been consistently applied to all the years presented, unless otherwise stated.

(1) BASIS OF PREPARATION OF THE FINANCIAL STATEMENTS

The financial statements of the Bank have been prepared in accordance with Malaysian Financial Reporting Standards ('MFRS'), International Financial Reporting Standards ('IFRS') and the requirements of the Companies Act, 2016 in Malaysia.

The financial statements have been prepared under the historical cost convention, as modified by the revaluation of financial investments AFS, financial assets and financial liabilities (including derivative financial instruments) at fair value through profit or loss.

The financial statements also incorporate those activities relating to Islamic banking which have been undertaken by the Bank. Islamic banking refers generally to the acceptance of deposits, granting of financing and dealing in Islamic securities under the Shariah principles.

The preparation of financial statements in conformity with MFRS requires the use of certain critical accounting estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reported financial year. It also requires Directors to exercise their judgement in the process of applying the Bank's accounting policies. Although these estimates and judgement are based on the Directors' best knowledge of current events and actions, actual results may differ.

The areas involving a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the financial statements are disclosed in Section (B).

(a) Standards, amendments to published standards and interpretations to existing standards that are applicable to the Bank and are effective

The relevant new accounting standards, annual improvements and amendments to published standards and interpretations to existing accounting standards that are effective for the Bank's financial year beginning on or after 1 January 2017 are as follows:

(i) Amendments to MFRS 112 'Income Taxes' – The amendments clarify the requirements for recognising deferred tax assets on unrealised losses where an asset is measured at fair value and that fair value is below the asset's tax base.

In addition, in evaluating whether an entity will have sufficient taxable profits in future periods against which deductible temporary differences can be utilised, the amendments require an entity to compare the deductible temporary differences with future taxable profits that excludes tax deductions resulting from the reversal of those temporary differences.

The amendments shall be applied retrospectively.

(ii) Amendments to MFRS 107 'Statements of Cash Flows' – The amendments introduce additional disclosure which require an entity to evaluate changes in liabilities arising from financing activities, including cash flows and non-cash changes.

The adoption of these annual improvements and amendments to published standards and interpretations to existing accounting standards do not give rise to any material financial impact to the Bank.

(A) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(1) BASIS OF PREPARATION OF THE FINANCIAL STATEMENTS (CONTINUED)

(b) Standards, amendments to published standards and interpretations to existing standards that are applicable to the Bank but not yet effective

(i) MFRS 9 'Financial Instruments' (effective from 1 January 2018) will replace MFRS 139 'Financial Instruments: Recognition and Measurement'.

The Bank has reviewed its financial assets and liabilities and is expecting the following impact from the adoption of the new standard:

(A) Classification

(i) Financial instruments classified as fair value through other comprehensive income ('FVOCI')

Financial instruments classified as FVOCI will be measured at fair value, with changes in fair value recognised in FVOCI reserve.

Gains or losses realised on the sale of financial assets at FVOCI will be transferred to profit or loss on sale, except for equity instruments.

Gains and losses realised on the sales of equity instruments classified as FVOCI will be reclassified below the line from the FVOCI reserve to retained earnings.

The majority of the Bank's debt and equity instruments that are currently classified as financial investments AFS will satisfy the conditions for classification as FVOCI and hence there will be no change to the accounting for these assets.

Arising from the change in business model, the Bank also intend to classify certain financial instruments currently classified as financial investments HTM or financial assets FVTPL to FVOCI going forward. Fair value is measured at reclassification date, and related changes in fair value for financial investments HTM will be adjusted to FVOCI reserve while fair value for financial assets FVTPL becomes its new carrying amount on 1 January 2018.

In addition, financial instruments AFS that did not pass the 'solely payment for principal and interest' ('SPPI') test prescribed under MFRS 9 will be classified to FVTPL. Related fair value gains from AFS investments will have to be transferred from the AFS reserve to retained earnings on 1 January 2018.

(ii) Financial instruments classified as amortised cost

The majority of the Bank's debt instruments currently classified as HTM and measured at amortised cost will meet the conditions for classification at amortised cost under MFRS 9 and continue to be recognised at amortised cost, except for the reclassification of certain debt instruments to FVOCI arising from changes in the Bank's business model mentioned in paragraph (A)(i) above.

(iii) Financial instruments classified as fair value through profit or loss ('FVTPL')

Under MFRS 9, FVTPL is the residual category and financial instruments which do not qualify to be recognised as FVOCI or at amortised cost will be recognised as FVTPL. The majority of instruments currently held at fair value through profit or loss will continue to be measured on the same basis under MFRS 9, except for those financial instruments currently classified under financial investment AFS that do not pass the SPPI test mentioned in paragraph (A)(i) above.

(A) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(1) BASIS OF PREPARATION OF THE FINANCIAL STATEMENTS (CONTINUED)

(b) Standards, amendments to published standards and interpretations to existing standards that are applicable to the Bank but not yet effective (continued)

(i) MFRS 9 'Financial Instruments' (effective from 1 January 2018) will replace MFRS 139 'Financial Instruments: Recognition and Measurement' (continued).

The Bank has reviewed its financial assets and liabilities and is expecting the following impact from the adoption of the new standard (continued):

(B) Financial liabilities

There will be no impact on the Bank's accounting for financial liabilities, as the new requirements only affect the accounting for financial liabilities that are designated at fair value through profit or loss and the Bank do not have any such liabilities. The derecognition rules have been transferred from MFRS 139 'Financial Instruments: Recognition and Measurement' and have not been changed.

(C) Hedge accounting

The new hedge accounting rules will align the accounting for hedging instruments more closely with the Bank's risk management practices. As a general rule, more hedge relationships might be eligible for hedge accounting, as the standard introduces a more principles-based approach. The Bank has confirmed that its current hedge relationships will qualify as continuing hedges upon the adoption of MFRS 9.

Changes in the fair value of foreign exchange forward contracts attributable to forward points, and in the time value of the option contracts, will in future be deferred in a new costs of hedging reserve within equity. The deferred amounts will be recognised against the related hedged transaction when it occurs.

(D) Impairment

The new impairment model requires the recognition of impairment provisions based on expected credit losses ('ECL') rather than only incurred credit losses as is the case under MFRS 139. It applies to financial assets classified at amortised cost, debt instruments measured at FVOCI, lease receivables, loan commitments and certain financial guarantee contracts.

(E) Disclosure requirements

The new standard also introduces expanded disclosure requirements and changes in presentation. These are expected to change the nature and extent of the Bank's disclosures about its financial instruments particularly in the year of the adoption of the new standard.

The Bank is now progressing to the implementation of the identified changes and will complete this process prior to the releasing of the interim results for the financial period ending 31 March 2018. The Bank has therefore not finalised the financial impact of the adoption of MFRS 9. However, based on the preliminary assessments undertaken to-date, the Bank expects an increase in the allowance for impairment on financing and other losses under the new impairment requirements, which will result in a reduction in opening retained profits as of 1 January 2018.

(A) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(1) BASIS OF PREPARATION OF THE FINANCIAL STATEMENTS (CONTINUED)

(b) Standards, amendments to published standards and interpretations to existing standards that are applicable to the Bank but not yet effective (continued)

(ii) MFRS 15 'Revenue from Contracts with Customers' (effective from 1 January 2018) replaces MFRS 118 'Revenue' and MFRS 111 'Construction Contracts' and related interpretations. The core principle in MFRS 15 is that an entity recognises revenue to depict the transfer of promised goods or services to the customer in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services.

Revenue is recognised when a customer obtains control of goods or services, i.e. when the customer has the ability to direct the use of and obtain the benefits from the goods or services.

A new five-step process is applied before revenue can be recognised:

- Identify contracts with customers;
- Identify the separate performance obligations;
- Determine the transaction price of the contract;
- Allocate the transaction price to each of the separate performance obligations; and
- Recognise the revenue as each performance obligation is satisfied.

Key provisions of the new standard are as follows:

- Any bundled goods or services that are distinct must be separately recognised, and any discounts or rebates on the contract price must generally be allocated to the separate elements.
- If the consideration varies (such as for incentives, rebates, performance fees, royalties, success of an outcome etc), minimum amounts of revenue must be recognised if they are not at significant risk of reversal.
- The point at which revenue is able to be recognised may shift: some revenue which is currently recognised at a point in time at the end of a contract may have to be recognised over the contract term and vice versa.
- There are new specific rules on licenses, warranties, non-refundable upfront fees, and consignment arrangements, to name a few.
- As with any new standard, there are also increased disclosures.

The standard permits either a full retrospective or a modified retrospective approach for the adoption. The Bank intends to adopt the standard using the modified retrospective approach which means that the cumulative impact of the adoption will be recognised in retained earnings as of 1 January 2018 and that comparatives will not be restated.

The Bank is in the process of finalising the financial implication arising from the adoption of this new standard, although it is not expected to have any material impact to the Bank.

(A) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(1) BASIS OF PREPARATION OF THE FINANCIAL STATEMENTS (CONTINUED)

(b) Standards, amendments to published standards and interpretations to existing standards that are applicable to the Bank but not yet effective (continued)

(iii) Annual Improvements to MFRS 2014-2016 Cycle:

- MFRS 1 'First-time Adoption of Malaysian Financial Reporting Standards' effective for annual periods beginning on or after 1 January 2018. The amendment deletes short term exemptions covering transition provisions of MFRS 7, MFRS 10 and MFRS 119. Those reliefs provided were available for entities with reporting periods that had passed and therefore no longer applicable.

- IC Interpretation 22 'Foreign Currency Transactions and Advance Consideration' effective for annual periods beginning on or after 1 January 2018. This interpretation applies when an entity recognises a non-monetary asset or non-monetary liability arising from the payment or receipt of advance consideration. MFRS 121 requires an entity to use the exchange rate at the 'date of the transaction' to record foreign currency transactions.

  IC Interpretation 22 provides guidance how to determine 'the date of transaction' when a single payment/receipt is made, as well as for situations where multiple payments/receipts are made.

  The date of transaction is the date when the payment or receipt of advance consideration gives rise to the non-monetary asset or non-monetary liability when the entity is no longer exposed to foreign exchange risk.

  If there are multiple payments or receipts in advance, the entity should determine the date of the transaction for each payment or receipt.

  An entity has the option to apply IC Interpretation 22 retrospectively or prospectively.

(iv) MFRS 16 'Leases' (effective from 1 January 2019) supersedes MFRS 117 'Leases' and the related interpretations.

Under MFRS 16, a lease is a contract (or part of a contract) that conveys the right to control the use of an identified asset for a period of time in exchange for consideration.

MFRS 16 eliminates the classification of leases by the lessee as either finance leases (on balance sheet) or operating leases (off balance sheet). MFRS 16 requires a lessee to recognise a 'right-of-use' of the underlying asset and a lease liability reflecting future lease payments for most leases.

The right-of-use asset is depreciated in accordance with the principle in MFRS 116 'Property, Plant and Equipment' and the lease liability is accreted over time with profit expense recognised in the income statements.

For lessors, MFRS 16 retains most of the requirements in MFRS 117. Lessors continue to classify all leases as either operating leases or finance leases and account for them differently.

(A) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(1) BASIS OF PREPARATION OF THE FINANCIAL STATEMENTS (CONTINUED)

(b) Standards, amendments to published standards and interpretations to existing standards that are applicable to the Bank but not yet effective (continued)

(v) IC Interpretation 23 'Uncertainty over Income Tax Treatments' (effective 1 January 2019) provides guidance on how to recognise and measure deferred and current income tax assets and liabilities where there is uncertainty over a tax treatment.

If an entity concludes that it is not probable that the tax treatment will be accepted by the tax authority, the effect of the tax uncertainty should be included in the period when such determination is made. An entity shall measure the effect of uncertainty using the method which best predicts the resolution of the uncertainty.

IC Interpretation 23 will be applied retrospectively.

The adoption of the above accounting standards, amendments to published standards and interpretations are not expected to give rise to any material financial impact to the Bank except for the cumulative impact of the adoption of MFRS 9 which will be recognised in retained earnings as at 1 January 2018, and enhanced disclosures.

(c) Changes in regulatory requirements

(i) Companies Act, 2016

The Companies Act, 2016 ('New Act') was enacted to replace the Companies Act, 1965 with the objective of creating a regulatory structure that will facilitate business and promote accountability as well as protection of corporate directors and shareholders, taking into consideration the interest of other stakeholders. The New Act was passed on 4 April 2016 by Dewan Rakyat and on 29 April 2016 by Dewan Negara and gazetted on 15 September 2016. On 26 January 2017, the Minister of Domestic Trade, Co-operatives and Consumerism announced that the date on which the New Act comes into operation (except Section 241 and Division 8 of Part III of the New Act) would be 31 January 2017.

Amongst the key changes introduced in the New Act which will affect the financial statements of the Bank upon the commencement of the New Act on 31 January 2017 are:

(1) abolition of the authorised capital; and

(2) abolition of the concept of nominal value in shares.

(ii) Revised Policy Document on Capital Funds

Bank Negara Malaysia ('BNM') had on 3 May 2017, issued a Revised Policy Document on Capital Funds for Islamic Banks ('Revised Policy Document') which is applicable to banking institutions in Malaysia that covers licensed Islamic bank. The issuance of this Revised Policy Document has superseded the guideline issued by BNM previously, namely Capital Funds for Islamic Banks dated 1 July 2013.

The key changes in the Revised Policy Document are:

(1) the removal of the requirement on maintenance of a reserve fund; and

(2) the revised component of capital funds shall exclude share premium and reserve fund.

During the financial year, the Bank had transferred a total of RM762,388,000 from the statutory reserve to retained profits pursuant to the adoption of the Revised Policy Document.

(A) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(1) BASIS OF PREPARATION OF THE FINANCIAL STATEMENTS (CONTINUED)

(c) Changes in regulatory requirements (continued)

(iii) Policy Document on Classification and Regulatory Treatment for Structured Products under the Financial Services Act 2013 and Islamic Financial Services Act 2013 issued by BNM

On 21 June 2017, BNM issued a Policy Document on Classification and Regulatory Treatment for Structured Products under the Financial Services Act 2013 (IFSA') and Islamic Financial Services Act 2013 ('IFSA'). This Policy Document applies to banking institutions in Malaysia that covers licensed commercial bank and licensed Islamic bank.

The Policy Document clarifies that structured products that do not guarantee full repayment of principal amount on demand do not fulfil the definition of deposits under Section 2 of the FSA and IFSA and hence must not be classified as deposits or Islamic deposits.

Effective from June 2017 reporting date onwards, banking institutions shall report structured products (in accordance with the accounting treatment adopted) under either of these items:

- 'Financial Liabilities Designated at Fair Value through Profit or Loss' if applying fair value options; or
- 'Other Liabilities' if accounted for separately from the embedded derivative.

(iv) Financial Reporting and Financial Reporting for Islamic Banking Institutions

On 2 February 2018, BNM issued the revised policy document on Financial Reporting and Financial Reporting for Islamic Banking Institutions which prescribes the regulatory reserves to be maintained by banking institutions. With effect from 1 January 2018, the Bank must maintain, in aggregate, loss allowance for non-credit impaired exposures and regulatory reserves of no less than 1% of total credit exposures, net of loss allowance for credit-impaired exposures. The adoption of this requirement is expected to have minimal impact to the capital ratios of the Bank as the Bank is currently maintaining, in aggregate, collective impairment provisions and regulatory reserves of no less 1.2% of total outstanding loans/financing, net of individual impairment provisions.

(2) FINANCIAL ASSETS

(a) Classification

The Bank classifies its financial assets in the following categories: at fair value through profit or loss, financing, advances and receivables, financial investments AFS and HTM. The classification depends on the purpose for which the financial assets were acquired. Management determines the classification at initial recognition and in the case of assets classified as held-to-maturity, re-evaluates this designation at the end of each reporting period.

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

Financial assets at fair value through profit or loss are financial assets held-for-trading. A financial asset is classified in this category if it is acquired or incurred principally for the purpose of selling or repurchasing in the near term. Derivatives are also classified in this category unless they are designated as hedges. Refer to accounting policy Note 4 on hedge accounting.

(A) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(2) FINANCIAL ASSETS (CONTINUED)

(a) Classification (continued)

(ii) Financing, advances and receivables

Financing, advances and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market.

Financing and receivables consist of Bai' Bithaman Ajil, Ijarah, Murabahah, Musyarakah, and Bai'Inah contracts. These contracts are initially recognised at fair value, including direct and incremental transactions costs, and subsequently measured at amortised cost using the effective profit method. These contracts are stated net of unearned income and any amounts written off and/or impaired.

(iii) Financial investments AFS

Financial investments AFS are non-derivatives that are either designated in this category or not classified in any of the other categories.

(iv) Financial investments HTM

Financial investments HTM are non-derivative financial assets with fixed or determinable payments and fixed maturities that the Bank's management has the positive intention and ability to hold to maturity. If the Bank sells other than an insignificant amount of financial investments HTM, the whole category would be tainted and reclassified as financial investments AFS.

(b) Recognition and initial measurement

Regular purchases and sales of financial assets are recognised on the settlement date on which the Bank commits to purchase or sell the asset.

Financial assets are initially recognised at fair value plus transaction costs for all financial assets not carried at fair value through profit or loss. Financial assets carried at fair value through profit or loss are initially recognised at fair value, and transaction costs are expensed in income statement.

(c) Subsequent measurement – gain and loss

Financial investments AFS and financial assets at fair value through profit or loss are subsequently carried at fair value. Financing, advances and receivables and financial investments HTM are subsequently carried at amortised cost using the effective profit method.

Changes in the fair values of financial assets at fair value through profit or loss, including the effects of currency translation, profit and dividend income are recognised in other operating income in income statement in the period in which the changes arise.

Changes in the fair value of financial investments AFS are recognised in other comprehensive income, except for impairment losses (refer to accounting policy Note 17 on impairment of financial assets) and foreign exchange gains and losses on monetary assets. The exchange differences on monetary assets are recognised in income statement, whereas exchange differences on non-monetary assets are recognised in other comprehensive income as part of fair value change.

Profit and dividend income on financial investments AFS are recognised separately in income statement. Profit on financial investments AFS calculated using the effective profit method is recognised in income statement. Dividend income on financial investments AFS is recognised in other operating income in income statement when the Bank's right to receive payment is established.

(A) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(2) FINANCIAL ASSETS (CONTINUED)

(d) De-recognition

Financial assets are derecognised when the rights to receive cash flows from the investments have expired or have been transferred and the Bank has transferred substantially all risks and rewards of ownership.

Financing, advances and receivables that are factored out to banks and other financial institutions with recourse to the Bank are not derecognised until the recourse period has expired and the risks and rewards of the financing, advances and receivables have been fully transferred. The corresponding cash received from the financial institutions is recorded as borrowings.

When financial investments AFS are sold, the accumulated fair value adjustments recognised in other comprehensive income are reclassified to income statement.

(e) Offsetting financial instruments

Financial assets and liabilities are offset and the net amount presented in the statement of financial position when there is a legally enforceable right to offset the recognised amounts and there is an intention to settle on a net basis, or realise the asset and settle the liability simultaneously. The legally enforceable right must not be contingent on future events and must be enforceable in the normal course of business and in the event of default, insolvency or bankruptcy.

(3) REPURCHASE AGREEMENTS

Securities purchased under resale agreements are securities which the Bank has purchased with a commitment to resell at future dates. The commitment to resell the securities is reflected as an asset on the statement of financial position.

Conversely, obligations on securities sold under repurchase agreements are securities which the Bank has sold from its portfolio, with a commitment to repurchase at future dates. Such financing and the obligation to repurchase the securities is reflected as a liability on the statement of financial position.

The difference between sale and repurchase price as well as purchase and resale price are amortised as profit and expense respectively on an effective yield method.

(4) DERIVATIVE FINANCIAL INSTRUMENTS AND HEDGE ACCOUNTING

Derivatives are initially recognised at fair value on the date on which derivative contracts are entered into and are subsequently re-measured at their fair values. Fair values are obtained from quoted market prices in active markets, including recent market transactions, and valuation techniques, including discounted cash flow models and option pricing models, as appropriate. All derivatives are carried as assets when fair values are positive and as liabilities when fair values are negative.

The best evidence of the fair value of a derivative at initial recognition is the transaction price (i.e. the fair value of the consideration given or received) unless the fair value of that instrument is evidenced by comparison with other observable current market transactions in the same instrument (i.e. without modification or repackaging) or based on a valuation technique whose variables include only data from observable markets. When such evidence exists, the Bank recognises profits on day one.

(A) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(4) DERIVATIVE FINANCIAL INSTRUMENTS AND HEDGE ACCOUNTING (CONTINUED)

The method of recognising the resulting fair value gain or loss depends on whether the derivative is designated as a hedging instrument, and if so, the nature of the item being hedged. Derivatives that do not qualify for hedge accounting are classified as held for trading and accounted for in accordance with the accounting policy set out in Note 2. The Bank designates certain derivatives as either: (1) hedges of the fair value of recognised assets or liabilities or firm commitments (fair value hedge); or (2) hedges of highly probable future cash flows attributable to a recognised asset or liability, or a forecasted transaction (cash flow hedge). Hedge accounting is used for derivatives designated in this way provided certain criteria are met.

The Bank documents, at the inception of the transaction, the relationship between hedging instruments and hedged items, as well as its risk management objective and strategy for undertaking various hedge transactions. The Bank also documents its assessment, both at hedge inception and on an on-going basis, whether the derivatives that are used in hedging transactions are highly effective in offsetting changes in fair values or cash flows of hedged items.

(a) Fair value hedge

Changes in the fair value of derivatives that are designated and qualify as fair value hedges are recorded in the income statement, together with any changes in the fair value of the hedged assets or liabilities that are attributable to the hedged risk.

If the hedge no longer meets the criteria for hedge accounting, the adjustment to the carrying amount of a hedged item for which the effective profit method is used is amortised to the income statement over the period to maturity.

(b) Cash flow hedge

The effective portion of changes in the fair value of derivatives that are designated and qualify as cash flow hedges is recognised in other comprehensive income and accumulated in reserves within equity. The gain or loss relating to the ineffective portion is recognised immediately in the income statement.

Amounts accumulated in equity are recycled to the income statement in the periods when the hedged item affects income or loss (for example, when the forecast sale that is hedged takes place).

When a hedging instrument expires or is sold or terminated, or when a hedge no longer meets the criteria for hedge accounting, any cumulative gain or loss existing in equity at that time remains in equity and is recognised when the forecast transaction is ultimately recognised in the income statement. When a forecast transaction is no longer expected to occur, the cumulative gain or loss that was reported in equity is immediately transferred to the income statement.

(c) Derivatives that do not qualify for hedge accounting

Certain derivative instruments do not qualify for hedge accounting. Changes in the fair value of any derivative instruments that does not qualify for hedge accounting are recognised immediately in the income statement.

(A) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(5) INTANGIBLE ASSETS – COMPUTER SOFTWARE LICENSES

Acquired computer software licenses are capitalised on the basis of the costs incurred to acquire and bring to use the specific software. Computer software licenses are subsequently carried at cost less accumulated amortisation and impairment losses. The costs are amortised over the estimated useful lives of 5 years to 10 years.

At the end of the reporting period, the Bank assesses whether there is any indication of impairment on computer software licenses. Where an indication of impairment exists, the carrying amount of the asset is written down to its recoverable amount. Refer to accounting policy Note 18 on impairment of non-financial assets.

Gains and losses arising from de-recognition of computer software licenses are measured as the difference between net disposal proceeds and the carrying amount of the computer software licenses and are recognised in income statement when the asset is de-recognised.

(6) PROPERTY, PLANT AND EQUIPMENT AND DEPRECIATION

Property, plant and equipment are stated at cost less accumulated depreciation and impairment losses, if any. Cost includes expenditure that is directly attributable to the acquisition of the items. Subsequent costs are included in the asset's carrying amount or recognised as a separate asset as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Bank and the cost of the item can be measured reliably. The carrying amount of the replaced part is de-recognised. All other repair and maintenance costs are recognised as expense in income statement during the financial period in which they are incurred.

Renovations in progress are not depreciated. Other property, plant and equipment are depreciated on a straight-line basis to write down their costs to their residual values over their estimated useful lives. The principal annual depreciation rates are as follows:

Renovations	10%
Office equipment and furniture	20%
Computer equipment	14⅓% to 33⅓%
Motor vehicles	20%

The asset's residual values and useful lives are reviewed, and adjusted if appropriate, at the end of each reporting period. There are no material adjustments arising from the review that would require disclosure in the financial statements.

Gains or losses on disposals are determined by comparing proceeds with carrying amounts and are included in other operating income in income statement.

At the end of the reporting period, the Bank assesses whether there is any indication of impairment. Where an indication of impairment exists, the carrying amount of the asset is written down to its recoverable amount. Refer to accounting policy Note 18 on impairment of non-financial assets.

(A) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(7) FINANCIAL LIABILITIES

Financial liabilities are measured at amortised cost, except for trading liabilities designated at fair value, which are held at fair value through profit or loss. Financial liabilities are initially recognised at fair value plus transaction costs for all financial liabilities not carried at fair value through profit or loss. Financial liabilities at fair value through profit or loss are initially recognised at fair value, and transaction costs are expensed in income statement. Financial liabilities are de-recognised when extinguished.

(a) Financial liabilities at fair value through profit or loss

This category comprises two sub-categories: financial liabilities as held-for-trading, and financial liabilities designated at fair value through profit or loss upon initial recognition.

A financial liability is classified as held-for-trading if it is acquired or incurred principally for the purpose of selling or repurchasing it in the near term or if it is part of a portfolio of identified financial instruments that are managed together and for which there is evidence of a recent actual pattern of short term profit-taking. Derivatives are also categorised as held-for-trading unless they are designated as hedges. Refer to accounting policy Note 4 on hedge accounting.

(b) Other financial liabilities measured at amortised cost

Other financial liabilities are initially recognised at fair value plus transaction costs. Subsequently, other financial liabilities are re-measured at amortised cost using the effective profit rate.

Other financial liabilities measured at amortised cost are deposits from customers, deposits and placements of banks and other financial institutions, investment account due to designated financial institutions, obligations on securities sold under repurchase agreements, bills and acceptances payable, recourse obligation on financing sold to Cagamas and other financial liabilities.

(c) Borrowings measured at amortised cost

Borrowings are initially recognised at fair value, net of transaction costs incurred. Borrowings are subsequently carried at amortised cost, any difference between initial recognised amount and the redemption value is recognised in the income statement over the period of the borrowings using the effective profit method.

All other borrowing costs are recognised in income statement in the period in which they are incurred.

Borrowings measured at amortised cost are subordinated obligations.

(A) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(8) INVESTMENT ACCOUNT ('IA')

IA is defined by the application of Shariah contracts as investment with non-principal guarantee feature. Under the Islamic Financial Services Act, 2013, the priority payment for IA upon liquidation of Islamic Financial Institution ('IFI') is treated separately from Islamic deposit, in accordance with the rights and obligations accrued to the investment account holders. IA is further categorised to Restricted Investment Account ('RIA') and Unrestricted Investment Account ('URIA').

RIA refers to a type of investment account where the Investment Account Holder ('IAH') provides a specific investment mandate to the IFI such as purpose, asset class, economic sector and period for investment while URIA refers to a type of investment account where the IAH provides the IFI with the mandate to make the ultimate investment decision without specifying any particular restrictions or conditions.

IA are contracts based on the Shariah concept below:

(a) Mudharabah between two parties, customer and the Bank, to finance a business venture where the customer provides capital and the business venture is managed solely by the Bank. The profit of the business venture will be shared based on pre-agreed ratios with the Bank as Mudharib (manager or manager of funds), and losses shall be borne solely by customers.

(b) Wakalah, a trust-based contract in which a party (muwakkil) appoints another party as his agent (wakil) to perform a particular task, in matters that may be delegated, either voluntarily or with imposition of a fee. The fee shall be recognised based on agreement.

(c) Details of the IA are as disclosed in Note 17 to the financial statements.

(9) RECOURSE OBLIGATION ON FINANCING SOLD TO CAGAMAS

In the normal course of banking operations, the Bank sells financing to Cagamas but undertake to administer the financing on behalf of Cagamas and to buy back any financing which are regarded as defective. Such financing transactions and the obligation to buy back the financing are reflected as a liability on the statement of financial position.

(10) OPERATING LEASE

Leases of assets where a significant portion of the risks and rewards of ownership are retained by the lessor are classified as operating leases. Payments made under operating leases (net of any incentives received from the lessor) are charged to the income statement on a straight-line basis over the period of the lease.

The up-front payments made for leasehold land represent prepaid lease rentals and are amortised on straight-line basis over the lease term.

Where an operating lease is terminated before the lease period has expired, any payment required to be made to the lessor by way of penalty is recognised as an expense in the period when termination takes place.

(A) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(11) PROVISIONS

Provisions are recognised when the Bank has a present legal or constructive obligation, as a result of past events, it is probable that an outflow of resources will be required to settle the obligation and a reliable estimate of the amount of obligation can be made.

Where the Bank expects a provision to be reimbursed (for example, under an insurance contract), the reimbursement is recognised as a separate asset but only when the reimbursement is virtually certain. Provisions are not recognised for future operating losses.

Where there are a number of similar obligations, the likelihood that an outflow will be required in settlement is determined by considering the class of obligations as a whole. A provision is recognised even if the likelihood of an outflow with respect to any one item included in the same class of obligations may be small.

Provisions are measured at the present value of the expenditure expected to be required to settle the obligation using a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the obligation. The increase in the provision due to passage of time is recognised as finance cost expense.

(12) FINANCIAL GUARANTEE CONTRACTS

Financial guarantee contracts are contracts that require the Bank to make specified payments to reimburse the holder for a loss it incurs because a specified debtor fails to make payments when due, in accordance with the terms of a debt instrument. Such financial guarantees are given to financial institutions and other bodies on behalf of customers to secure financing and advances, overdrafts and other banking facilities.

Financial guarantee contracts are recognised as a financial liability at the time the guarantee is issued. The fair value of a financial guarantee at the time of issuance is zero because all guarantees are agreed on arm's length terms and the value of the premium agreed corresponds to the value of the guarantee obligation. No receivable for the future premium is recognised.

The fair value of financial guarantee is determined as the present value of the difference in net cash flows between the contractual payments under the debt instrument and the payments that would be required without the guarantee, or the estimated amount that would be payable to a third party for assuming the obligations.

(13) CONTINGENT LIABILITIES AND CONTINGENT ASSETS

The Bank does not recognise a contingent liability but discloses its existence in the financial statements. A contingent liability is a possible obligation that arises from past events whose existence will be confirmed by the occurrence or non-occurrence of one or more uncertain future events beyond the control of the Bank or a present obligation that is not recognised because it is not probable that an outflow of resources will be required to settle the obligation. A contingent liability also arises in the extremely rare case where there is a liability that cannot be recognised because it cannot be measured reliably. However, contingent liabilities do not include financial guarantee contracts.

A contingent asset is a possible asset that arises from past events whose existence will be confirmed by the occurrence or non-occurrence of one or more uncertain future events beyond the control of the Bank. The Bank does not recognise contingent assets but discloses their existence where inflows of economic benefits are probable, but not virtually certain.

Subsequent to the initial recognition, the Bank measures the contingent liabilities that are recognised separately at the date of acquisition at the higher of the amount that would be recognised in accordance with the provision of MFRS 137 'Provision, Contingent Liabilities and Contingent Assets' and the amount initially recognised as profit or loss, less, when appropriate, cumulative amortisation recognised in accordance with MFRS 118 'Revenue'.

(A) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(14) SHARE CAPITAL

(a) Classification

Ordinary shares are classified as equity. Other shares, if issued, are classified as equity and/or liability according to the economic substance of the particular instrument.

(b) Share issue cost

Incremental costs directly attributable to the issue of new shares or options are shown in equity as a deduction, net of tax, from the proceeds.

(c) Dividend distribution

Distributions to holders of an equity instrument is debited directly to equity, and the corresponding liability is recognised in the period in which the shareholders' right to receive the dividends are established or the dividends are approved.

(15) CASH AND CASH EQUIVALENTS

Cash and cash equivalents consist of cash and bank balances and short term deposits maturing within one month.

(16) REVENUE RECOGNITION

(a) Profit income is recognised using the effective profit method. The effective profit rate is the rate that discounts estimated future cash receipts or payments through the expected life of the financial instrument or, when appropriate, a shorter period to its carrying amount. The calculation includes significant fees and transaction costs that are integral to the effective profit rate, as well as premiums or discounts.

When a financing, advances and receivable is impaired, the Bank reduces the carrying amount to its recoverable amount, being the estimated future cash flows discounted at the original effective profit rate of the instrument, and continue unwinding the discount as profit income. Profit income on impaired financing and receivables is recognised using the original effective profit rate.

Bai' Bithaman Ajil

A contract of sale of an asset in which the payment of price is deferred either be paid in lump-sum or instalment basis within an agreed period of time. Income is recognised on effective profit rate basis over the expected life of the contract based on outstanding financing amount.

Ijarah

A contract that transfers ownership of a permitted usufruct and/or service for a specified period in exchange for a specified consideration.

Murabahah

A contract of sale where the assets cost and profit margin shall be made transparent and agreed upon between buyer and seller. Income is recognised on effective profit rate basis over the expected life of the contract based on outstanding financing amounts.

Musyarakah

Partnership between two or more parties, which may take effect through contractual relationship or by operation of Islamic law, whereby all contracting parties will share the profit and bear loss from the partnership.

Bai'Inah

An arrangement that involves sale of an asset to the purchaser on a deferred basis and subsequent purchase of the asset at a cash price lower than the deferred sale price or vice versa, and which complies with the specific requirements of Bai'Inah.

(A) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(16) REVENUE RECOGNITION (CONTINUED)

(b) Financing arrangement fees, commissions and placement fees are recognised as income when all conditions precedent are fulfilled.

(c) Guarantee fees are recognised as income upon issuance of guarantees.

(d) Commitment fees are recognised as income based on time apportionment.

(e) Corporate advisory fees are recognised as income on completion of each stage of the engagement and issuance of invoice.

(f) Dividends from all investments are recognised when the shareholders' right to receive payment is established.

(g) Income from bancatakaful agreement is amortised on a straight line basis throughout the exclusive service agreement period.

(17) IMPAIRMENT OF FINANCIAL ASSETS

(a) Assets carried at amortised cost

The Bank assesses at the end of the reporting period whether there is objective evidence that a financial asset or group of financial assets is impaired. A financial asset or a group of financial assets is impaired and impairment losses are incurred only if there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the asset (a 'loss event') and that loss event (or events) has an impact on the estimated future cash flows of the financial asset or group of financial assets that can be reliably estimated.

The criteria that the Bank uses to determine whether there is objective evidence of an impairment loss include:

- Significant financial difficulty of the issuer or obligor;
- A breach of contract, such as a default or delinquency in profit or principal payments;
- The Bank, for economic or legal reasons relating to the borrower's financial difficulty, granting to the borrower a concession that the lender would not otherwise consider;
- It becomes probable that the borrower will enter bankruptcy or other financial reorganisation;
- Disappearance of an active market for that financial asset because of financial difficulties; or
- Observable data indicating that there is a measurable decrease in the estimated future cash flows from a portfolio of financial assets since the initial recognition of those assets, although the decrease cannot yet be identified with the individual financial assets in the portfolio, including:

    (i) Adverse changes in the payment status of borrowers in the portfolio; and

    (ii) National or local economic conditions that correlate with defaults on the assets in the portfolio.

The amount of the impairment loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future credit losses that have not been incurred) discounted at the financial asset's original effective profit rate. The asset's carrying amount is reduced and the amount of the loss is recognised in income statement. If 'financing, advances and receivables' or a 'HTM investment' have a variable profit rate, the discount rate for measuring any impairment loss is the current effective profit rate determined under the contract.

If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised (such as an improvement in the debtor's credit rating), the reversal of the previously recognised impairment loss is recognised in income statement.

(A) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(17) IMPAIRMENT OF FINANCIAL ASSETS (CONTINUED)

(a) Assets carried at amortised cost (continued)

When an asset is uncollectible, it is written off against the related allowance account. Such assets are written off after all the necessary procedures have been completed and the amount of the loss has been determined.

For financing and advances, the Bank first assesses whether objective evidence of impairment exists individually for financing and advances that are individually significant, and individually or collectively for financing and advances that are not individually significant. If the Bank determines that no objective evidence of impairment exists for individually assessed financing and advances, whether significant or not, it includes the asset in a group of financing and advances with similar credit risk characteristics and collectively assess them for impairment.

The Bank addresses impairment of financing and advances via either individually assessed allowance or collectively assessed allowance.

(i) Individual impairment allowance

The Bank determines the allowance appropriate for each individual significant financing and advances on an individual basis. The allowances are established based primarily on estimates of the realisable value of the collateral to secure the financing and advances and are measured as the difference between the carrying amount of the financing and advances and the present value of the expected future cash flows discounted at the original effective profit rate of the financing and advances. All other financing and advances that have been individually evaluated, but not considered to be individually impaired, are assessed collectively for impairment.

(ii) Collective impairment allowance

Financing and advances which are not individually significant and financing and advances that have been individually assessed with no evidence of impairment loss are grouped together for collective impairment assessment. These financing and advances are grouped within similar credit risk characteristics for collective assessment, whereby data from the financing portfolio (such as credit quality, levels of arrears, credit utilisation, financing to collateral ratios etc.) and concentrations of risks (such as the performance of different individual groups) are taken into consideration.

Future cash flows in a group of financial assets that are collectively evaluated for impairment are estimated based on the historical loss experience of the Bank. Historical loss experience is adjusted on the basis of current observable data to reflect current conditions on which the historical loss experience is based on and to remove the effects of conditions in the historical period that do not exist currently. Estimates of changes in future cash flows reflect, and are directionally consistent with, changes in related observable data from year to year. The methodology and assumptions used for estimating future cash flows are reviewed regularly to reduce any differences between loss estimates and actual loss experience.

(iii) Regulatory reserve

The Bank has adopted the requirement to maintain, in aggregate, the collective impairment allowances and regulatory reserves of no less than 1.2% of total outstanding financing, net of individual impairment allowances. The regulatory reserve is debited against retained earnings.

(A) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(17) IMPAIRMENT OF FINANCIAL ASSETS (CONTINUED)

(b) Assets classified as AFS

The Bank assesses at the end of the reporting period whether there is objective evidence that a financial asset or a group of financial assets is impaired.

For debt securities, the Bank uses criteria and measurement of impairment loss applicable for 'assets carried at amortised cost' above. If, in a subsequent period, the fair value of a debt instrument classified as AFS increases and the increase can be objectively related to an event occurring after the impairment loss was recognised in income statement, the impairment loss is reversed through income statement.

In the case of equity securities classified as AFS, in addition to the criteria for 'assets carried at amortised cost' above, a significant or prolonged decline in the fair value of the security below its cost is also considered as an indicator that the assets are impaired. If any such evidence exists for AFS financial assets, the cumulative loss that had been recognised directly in equity is removed from equity and recognised in income statement. The amount of cumulative loss that is reclassified to income statement is the difference between the acquisition cost and the current fair value, less any impairment loss on that financial asset previously recognised in income statement. Impairment losses recognised in income statement on equity instruments classified as AFS are not reversed through income statement.

(18) IMPAIRMENT OF NON-FINANCIAL ASSETS

Non-financial assets that have an indefinite useful life are not subject to amortisation and are tested annually for impairment. Non-financial assets that are subject to amortisation are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognised for the amount by which the carrying amount of the non-financial assets exceeds its recoverable amount.

The recoverable amount is the higher of a non-financial assets' fair value less costs to sell and value in use. For the purpose of assessing impairment, non-financial assets are grouped at the lowest levels for which there is separately identifiable cash flows or cash generating unit. Non-financial assets that suffered impairment are reviewed for possible reversal of the impairment at each reporting period.

The impairment loss is charged to the income statement. Any subsequent increase in recoverable amount is recognised in the income statement.

(19) EMPLOYEE BENEFITS

(a) Short term employee benefits

The Bank recognises a liability and an expense for bonuses. The Bank recognises a provision where contractually obliged or where there is a past practice that has created a constructive obligation.

Wages, salaries, paid annual leave and sick leave, bonuses and non-monetary benefits are accrued in the period in which the associated services are rendered by employees of the Bank.

(b) Defined contribution plans

A defined contribution plan is a pension plan under which the Bank pays fixed contributions to the national pension scheme, the Employees' Provident Fund. The Bank's contributions to defined contribution plans are charged to the income statement in the period to which they relate. Once the contributions have been paid, the Bank has no further legal or constructive obligations.

(c) Termination benefits

Termination benefits are payable whenever an employee's employment is terminated before the normal retirement date or whenever an employee accepts voluntary redundancy in exchange for these benefits.

(A) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(20) CURRENT AND DEFERRED INCOME TAXES

The tax expense for the period comprises current and deferred tax. Tax is recognised in income statement, except to the extent that it relates to items recognised in other comprehensive income or directly in equity. In this case, the tax is recognised in other comprehensive income or directly in equity, respectively.

Current tax expense is determined according to the tax laws of each jurisdiction in which the Bank operate and include all taxes based upon the taxable profits.

Deferred income tax is provided in full, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements. However, deferred tax is not accounted for if it arises from initial recognition of an asset or liability in a transaction other than a business combination that at the time of the transaction affects neither accounting nor taxable profit or loss.

Deferred tax assets are recognised to the extent that it is probable that future taxable profits will be available against which the deductible temporary differences or unused tax losses can be utilised.

Deferred tax is determined using tax rates (and tax laws) that have been enacted or substantially enacted by the date of statement of financial position and are expected to apply when the related deferred tax asset is realised or the deferred tax liability is settled.

Deferred and income tax assets and liabilities are offset when there is a legally enforceable right to offset current tax assets against current tax liabilities and when the deferred income tax assets and liabilities relate to taxes levied by the same taxation authority on either the taxable entity or different taxable entities where there is an intention to settle the balances on a net basis.

(21) CURRENCY CONVERSION AND TRANSLATION

(a) Functional and presentation currency

The financial statements are presented in Ringgit Malaysia, which is the Bank's functional and presentation currency.

(b) Transactions and balances

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised in the income statement, except when deferred in other comprehensive income as qualifying cash flow hedges. Foreign exchange gains and losses are presented in income statement within other operating income.

Changes in the fair value of monetary securities denominated in foreign currency classified as AFS are analysed between translation differences resulting from changes in the amortised cost of the security and other changes in the carrying amount of the security. Translation differences related to changes in amortised cost are recognised in income statement, and other changes in carrying amount are recognised in other comprehensive income.

Translation differences on non-monetary financial assets and liabilities such as equities held at fair value through profit or loss are recognised in income statement as part of the fair value gain or loss. Translation differences on non-monetary financial assets, such as equities classified as available-for-sale, are included in other comprehensive income.

(A) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

(22) SEGMENT REPORTING

Operating segments are reported in a manner consistent with the internal reporting provided to the chief operating decision-maker, who is responsible for allocating resources to and assessing performance of the operating segments of an entity. The Bank has determined RHB Bank's Group Management Committee as its chief operating decision-maker.

(23) ZAKAT

This represents business zakat which is an obligatory amount payable by the Bank to comply with the principles of Shariah and as approved by the Group Shariah Committee. The Bank only pays zakat on its business and does not pay zakat on behalf of depositors or shareholders. Zakat provision is calculated based on the "Working Capital Method", at 2.5% on the adjusted net assets of the Bank.

(B) CRITICAL ACCOUNTING ESTIMATES AND ASSUMPTIONS

The Bank makes estimates and assumptions that affect the reported amounts of assets and liabilities within the next financial year. Estimates and judgements are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. The estimates and assumptions that have a significant risk of causing a material adjustment to the carrying amount of assets within the next financial year are outlined below:

Allowance for impairment of financial assets

In determining impairment of financial assets, management considers objective evidence of impairment and exercises judgement in estimating cash flow and collateral values.

The Bank makes allowance for losses based on assessment of recoverability. Management's judgement is made in estimation of the amount and timing of future cash flows in assessing allowance for impairment of financial assets. Among the factors considered are the Bank's aggregate exposure to the borrower, the net realisable value of the underlying collateral value, the viability of the customer's business model, the capacity to generate sufficient cash flows to service debt obligations and the aggregate amount and ranking of all other creditor claims. The actual amount of the future cash flows and their timing may differ from the estimates used by management and consequently may cause actual losses to differ from the impairment made.

NOTES TO THE FINANCIAL STATEMENTS

FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2017

1 GENERAL INFORMATION

RHB Islamic Bank Berhad, is a licensed Islamic Bank under the Islamic Financial Services Act, 2013, a limited liability company domiciled in Malaysia, and is principally engaged in the Islamic banking business and is committed to offer customers a comprehensive range of products and services in accordance with its Articles of Association and Shariah principals.

There have been no significant changes in these principal activities during the financial year.

The address of the registered office of the Bank is Level 9, Tower One, RHB Centre, Jalan Tun Razak, 50400 Kuala Lumpur, Malaysia.

2 CASH AND SHORT TERM FUNDS

	2017 RM'000	2016 RM'000
Cash and balances with banks and other financial institutions	**90,792**	18,906
Money at call and deposit placements maturing within one month	**1,939,068**	3,417,333
	2,029,860	3,436,239

3 SECURITIES PURCHASED UNDER RESALE AGREEMENTS

	2017 RM'000	2016 RM'000
Malaysian Government Investment Issues	**1,587,979**	2,353,950

4 DEPOSITS AND PLACEMENTS WITH BANKS AND OTHER FINANCIAL INSTITUTIONS

	2017 RM'000	2016 RM'000
Licensed bank	**14,641**	–
Licensed Islamic banks	**432,569**	180,771
Other financial institutions	**–**	356,370
	447,210	537,141

5 FINANCIAL ASSETS HELD-FOR-TRADING ('HFT')

	2017 RM'000	2016 RM'000
At fair value		
Money market instruments:		
Malaysian Government Investment Issues	**172,536**	10,177

6 FINANCIAL INVESTMENTS AVAILABLE-FOR-SALE ('AFS')

	2017 RM'000	2016 RM'000
At fair value		
Money market instruments:		
Malaysian Government Investment Issues	**648,592**	691,196
Wakala Global Sukuk	**–**	14,718
Khazanah bonds	**9,403**	8,995
Cagamas bonds	**30,485**	40,018
Unquoted securities:		
In Malaysia		
Corporate sukuk	**2,505,393**	2,504,101
Perpetual sukuk	**200,620**	200,619
	3,394,493	3,459,647
At cost		
Unquoted securities:		
In Malaysia		
Shares in Islamic Bank and Financial Institutions of Malaysia ('IBFIM')	**549**	549
	3,395,042	3,460,196
Accumulated impairment losses	**(549)**	(549)
	3,394,493	3,459,647
Movements in allowance for impairment losses:		
Balance as at the beginning of the financial year	**549**	–
Charge during the financial year	**–**	549
Balance as at the end of the financial year	**549**	549

7 FINANCIAL INVESTMENTS HELD-TO-MATURITY ('HTM')

	2017 RM'000	2016 RM'000
At amortised cost		
Money market instruments:		
Malaysian Government Investment Issues	**335,325**	402,619
Sukuk Perumahan Kerajaan	**9,985**	9,971
Khazanah bonds	**21,799**	20,872
Cagamas bonds	**–**	150,095
Negotiable Islamic debt certificates	**1,838,090**	895,234
Unquoted securities:		
In Malaysia		
Corporate sukuk	**1,615,535**	1,341,332
	3,820,734	2,820,123

Included in financial investments HTM are securities acquired and funded via the RIA, as part of arrangement between the Bank and its holding company, RHB Bank Berhad ('RHB Bank'). As at 31 December 2017, the gross exposure to RIA financing is RM790,275,000 (2016: RM199,000,000) as disclosed in Note 17.

8 FINANCING AND ADVANCES

2017	Bai' Bithaman Ajil ('BBA') RM'000	Ijarah RM'000	Murabahah RM'000	Musyarakah RM'000	Bai'Inah RM'000	Others RM'000	Total RM'000
At amortised cost							
Cashline	–	–	532,334	–	–	3,442	535,776
Term financing:							
– Housing financing	448,118	–	823,499	10,575,089	–	400	11,847,106
– Syndicated term financing	–	76,405	1,713,643	–	–	18,899	1,808,947
– Hire purchase receivables	–	6,145,221	–	–	–	40,503	6,185,724
– Other term financing	1,791	490,417	16,156,732	–	1,509,993	3,778	18,162,711
Bills receivables	–	–	1,041,682	–	–	3,428	1,045,110
Trust receipts	–	–	15,558	–	–	–	15,558
Staff financing	2,592	–	–	–	–	–	2,592
Credit/charge card receivables	–	–	–	–	–	267,577	267,577
Revolving financing	–	–	3,104,581	–	–	–	3,104,581
Gross financing and advances	452,501	6,712,043	23,388,029	10,575,089	1,509,993	338,027	42,975,682
Fair value changes arising from fair value hedge							(1,231)
							42,974,451
Allowance for impaired financing and advances:							
– Individual impairment allowance							(42,612)
– Collective impairment allowance							(230,045)
Net financing and advances							42,701,794

8 FINANCING AND ADVANCES (CONTINUED)

2016	Bai' Bithaman Ajil ('BBA') RM'000	Ijarah RM'000	Murabahah RM'000	Musyarakah RM'000	Bai'Inah RM'000	Others RM'000	Total RM'000
At amortised cost							
Cashline	–	–	401,337	–	–	1,463	402,800
Term financing:							
– Housing financing	512,215	–	2,913	8,541,764	–	454	9,057,346
– Syndicated term financing	–	93,884	1,309,912	–	–	18,899	1,422,695
– Hire purchase receivables	–	5,600,165	–	–	–	33,345	5,633,510
– Other term financing	3,126	494,435	13,103,916	–	1,862,705	12,204	15,476,386
Bills receivables	–	–	790,186	–	–	3,097	793,283
Trust receipts	–	–	13,773	–	–	253	14,026
Staff financing	3,394	–	–	–	–	–	3,394
Credit/charge card receivables	–	–	–	–	–	274,532	274,532
Revolving financing	–	–	1,009,152	–	–	–	1,009,152
Gross financing and advances	518,735	6,188,484	16,631,189	8,541,764	1,862,705	344,247	34,087,124
Fair value changes arising from fair value hedge							6,831
							34,093,955
Allowance for impaired financing and advances:							
– Individual impairment allowance							(15,864)
– Collective impairment allowance							(236,525)
Net financing and advances							33,841,566

(a) Included in financing and advances are exposures to RIA as part of arrangement between the Bank and its holding company, RHB Bank.

As at 31 December 2017, the gross exposures to RIA financing are RM7,030,030,000 (2016: RM5,804,399,000) and the portfolio allowance for impairment losses for financing and advances relating to RIA amounting to RM45,287,000 (2016: RM33,626,000) is recognised in the financial statements of RHB Bank. There is no individual impairment being made for such RIA financing.

(b) Included in term financing are hire purchase receivables and other term financing sold to Cagamas amounting to Nil (2016: RM791,238,000).

8 FINANCING AND ADVANCES (CONTINUED)

	2017 RM'000	2016 RM'000
(i) By type of customer		
Domestic non-bank financial institutions:		
– Others	**1,287,745**	995,486
Domestic business enterprises:		
– Small medium enterprises	**3,085,019**	2,526,817
– Others	**12,985,826**	10,374,884
Government and statutory bodies	**4,005,023**	3,087,891
Individuals	**21,173,536**	16,688,969
Other domestic entities	**100,176**	103,742
Foreign entities	**338,357**	309,335
	42,975,682	34,087,124
(ii) By profit rate sensitivity		
Fixed rate:		
– Housing financing	**448,398**	512,441
– Hire purchase receivables	**4,452,465**	5,630,979
– Other fixed rate financing	**8,238,412**	7,277,587
Variable rate:		
– Base financing rate/Base rate plus	**27,774,276**	19,858,808
Cost-plus	**2,062,131**	807,309
	42,975,682	34,087,124
(iii) By purpose		
Purchase of securities	**1,758,308**	65,524
Purchase of transport vehicles	**6,156,435**	5,573,799
Purchase of landed property:		
– Residential	**11,272,138**	8,709,537
– Non-residential	**3,208,523**	2,536,021
Purchase of property, plant and equipment other than land and building	**661,901**	755,946
Personal use	**2,798,313**	2,162,519
Credit card	**267,577**	274,532
Construction	**980,050**	550,030
Working capital	**9,309,504**	7,422,039
Merger and acquisition	**1,319,919**	1,437,555
Other purposes	**5,243,014**	4,599,622
	42,975,682	34,087,124

Included in other purposes are financing to the Government of the Malaysia's related agency for the purpose of education and government's staff housing financing.

8 FINANCING AND ADVANCES (CONTINUED)

	2017 RM'000	2016 RM'000
(iv) By geographical distribution		
Malaysia	**42,975,682**	34,087,124
(v) By remaining contractual maturities		
Maturing within one year	**7,861,965**	3,681,561
One to three years	**5,113,144**	2,945,639
Three to five years	**3,599,350**	6,443,749
Over five years	**26,401,223**	21,016,175
	42,975,682	34,087,124
(vi) Impaired financing and advances		
(i) Movement in impaired financing and advances		
Balance as at the beginning of the financial year	**393,096**	362,736
Classified as impaired	**472,890**	514,915
Reclassified as non-impaired	**(385,958)**	(352,703)
Amount recovered	**(77,000)**	(78,617)
Amount written off	**(59,067)**	(53,235)
Balance as at the end of the financial year	**343,961**	393,096
(ii) By purpose		
Purchase of securities	**205**	–
Purchase of transport vehicles	**55,009**	54,189
Purchase of landed property:		
– Residential	**108,195**	159,833
– Non-residential	**42,351**	47,259
Purchase of property, plant and equipment other than land and building	**1,049**	2,826
Personal use	**5,131**	4,869
Credit card	**4,583**	5,362
Working capital	**97,964**	96,456
Other purposes	**29,474**	22,302
	343,961	393,096
(iii) By geographical distribution		
Malaysia	**343,961**	393,096

8 FINANCING AND ADVANCES (CONTINUED)

(vii) Movement in allowance for impaired financing and advances

	2017 RM'000	2016 RM'000
Individual impairment allowance		
Balance as at the beginning of the financial year	**15,864**	22,649
Net allowance made/(written back)	**29,204**	(3,438)
Amount written off	**(2,456)**	(3,347)
Balance as at end of the financial year	**42,612**	15,864
Collective impairment allowance		
Balance as at the beginning of the financial year	**236,525**	199,653
Net allowance made	**37,562**	77,902
Amount written off	**(44,042)**	(41,030)
Balance as at the end of the financial year	**230,045**	236,525
Collective impairment allowance as % of gross financing and advances (excluding RIA financing) less individual impairment allowance	**0.64%**	0.84%

9 OTHER ASSETS

	2017 RM'000	2016 RM'000
Prepayments	**15,998**	11,751
Deposits	**1,732**	1,305
Other receivables	**73,204**	158,674
	90,934	171,730

10 DERIVATIVE ASSETS/(LIABILITIES)

Derivative financial instruments are financial instruments whose values change in response to changes in prices or rates (such as foreign exchange rates, profit rates and security prices) of the underlying instruments. These instruments are used by the Bank for economic hedges and for proprietary trading purposes. The default classification for derivative financial instruments is trading, unless designated in a hedge relationship and are in compliance with the stringent requirements of hedge accounting mentioned in the Bank's accounting policies.

The table below shows the Bank's derivative financial instruments as at the date of statement of financial position. The contractual or underlying principal amounts of these derivative financial instruments and their corresponding gross positive (derivative assets) and gross negative (derivative liabilities) fair values at the date of statement of financial position are analysed below.

	2017 RM'000	2016 RM'000
Derivative assets:		
– Trading derivatives	**327,948**	401,864
– Fair value hedging derivatives	**30**	899
	327,978	402,763
Derivative liabilities:		
– Trading derivatives	**(323,235)**	(392,598)
– Fair value hedging derivatives	**(4,488)**	(8,214)
	(327,723)	(400,812)

10 DERIVATIVE ASSETS/(LIABILITIES) (CONTINUED)

	Contract or underlying principal amount RM'000	Year-end positive fair value RM'000	Year-end negative fair value RM'000
2017			
Trading derivatives:			
Foreign exchange related contracts:			
– Forwards	**7,906,672**	**240,620**	**(236,924)**
– Cross currency profit rate swaps	**2,665,997**	**84,008**	**(82,908)**
Profit rate related contracts:			
– Swaps	**917,338**	**3,320**	**(3,403)**
Fair value hedging derivatives:			
Profit rate related contracts:			
– Swaps	**1,325,000**	**30**	**(4,488)**
		327,978	**(327,723)**
2016			
Trading derivatives:			
Foreign exchange related contracts:			
– Forwards	7,467,323	310,313	(301,957)
– Cross currency profit rate swaps	1,875,919	88,563	(87,079)
Profit rate related contracts:			
– Swaps	597,448	2,988	(3,562)
Fair value hedging derivatives:			
Profit rate related contracts:			
– Swaps	1,907,000	899	(8,214)
		402,763	(400,812)

Fair value hedging is used by the Bank for protection against the changes in fair value of financial assets and financial liabilities due to movements in market profit rates. The Bank uses profit rate swaps to hedge against profit rate risk of specific identified fixed rate long term as well as portfolio homogenous pools of financing and advances. Included in other operating income as disclosed in Note 25 is the net gains and losses arising from fair value hedges for the financial year as follows:

	2017 RM'000	2016 RM'000
Gain/(Loss) on hedging instruments	**6,916**	(15,725)
(Loss)/Gain on hedged items attributable to the hedged risk	**(7,994)**	14,926
	(1,078)	(799)

11 STATUTORY DEPOSITS WITH BANK NEGARA MALAYSIA ('BNM')

The non-profit bearing statutory deposits are maintained with BNM in compliance with Section 26(2)(c) of the Central Bank of Malaysia Act, 2009. The amount is determined at a set percentage of total eligible liabilities.

12 DEFERRED TAX ASSETS

Deferred income tax assets and liabilities are offset when there is a legally enforceable right to set off current tax assets against current tax liabilities and when the deferred taxes relate to the same authority. The following amounts determined after appropriate set off, are shown in the statement of financial position:

	2017 RM'000	2016 RM'000
Deferred tax assets	**16,513**	20,929
Deferred tax assets:		
– Settled more than twelve months	**5,532**	10,619
– Settled within twelve months	**11,608**	15,129
Deferred tax liabilities:		
– Settled within twelve months	**(627)**	(4,819)
	16,513	20,929

The movements in deferred tax assets and liabilities during the financial year comprise the following:

	Note	Intangible assets-computer software license RM'000	Property, plant and equipment RM'000	Financial investments AFS RM'000	Other liabilities RM'000	Total RM'000
2017						
Balance as at the beginning of the financial year		**(4,819)**	**666**	**10,085**	**14,997**	**20,929**
Transfer from/(to) income statement	31	**4,192**	**(36)**	**–**	**(3,515)**	**641**
Transfer to equity		**–**	**–**	**(5,057)**	**–**	**(5,057)**
Balance as at the end of the financial year		**(627)**	**630**	**5,028**	**11,482**	**16,513**
2016						
Balance as at the beginning of the financial year		(4,877)	904	12,375	3,562	11,964
Transfer from/(to) income statement	31	58	(238)	–	11,435	11,255
Transfer to equity		–	–	(2,290)	–	(2,290)
Balance as at the end of the financial year		(4,819)	666	10,085	14,997	20,929

13 PROPERTY, PLANT AND EQUIPMENT

	Note	Renovations RM'000	Office equipment and furniture RM'000	Computer equipment RM'000	Motor vehicles RM'000	Total RM'000
2017						
Cost						
Balance as at the beginning of the financial year		**15,691**	**8,327**	**12,300**	**1,157**	**37,475**
Additions		**1,772**	**237**	**203**	**–**	**2,212**
Disposal		**–**	**(27)**	**(256)**	**(4)**	**(287)**
Written off		**–**	**(61)**	**(374)**	**(4)**	**(439)**
Balance as at the end of the financial year		**17,463**	**8,476**	**11,873**	**1,149**	**38,961**
Less: Accumulated depreciation						
Balance as at the beginning of the financial year		**10,973**	**7,576**	**11,424**	**926**	**30,899**
Charge for the financial year	29	**1,610**	**373**	**496**	**112**	**2,591**
Disposal		**–**	**(23)**	**(256)**	**(4)**	**(283)**
Written off		**–**	**(61)**	**(374)**	**(4)**	**(439)**
Balance as at the end of the financial year		**12,583**	**7,865**	**11,290**	**1,030**	**32,768**
Net book value as at the end of the financial year		**4,880**	**611**	**583**	**119**	**6,193**
2016						
Cost						
Balance as at the beginning of the financial year		17,083	8,916	12,739	1,634	40,372
Additions		7	67	316	–	390
Disposal		–	–	–	(477)	(477)
Written off		(1,399)	(656)	(755)	–	(2,810)
Balance as at the end of the financial year		15,691	8,327	12,300	1,157	37,475
Less: Accumulated depreciation						
Balance as at the beginning of the financial year		10,354	7,823	12,523	1,288	31,988
Charge for the financial year	29	1,629	373	(366)	115	1,751
Disposal		–	–	–	(477)	(477)
Written off		(1,010)	(620)	(733)	–	(2,363)
Balance as at the end of the financial year		10,973	7,576	11,424	926	30,899
Net book value as at the end of the financial year		4,718	751	876	231	6,576

13 PROPERTY, PLANT AND EQUIPMENT (CONTINUED)

The above property, plant and equipment includes the following assets under construction:

	2017 RM'000	2016 RM'000
Cost		
Renovations	**671**	262

14 INTANGIBLE ASSETS

	Note	2017 RM'000	2016 RM'000
Computer software license			
Cost			
Balance as at the beginning of the financial year		**15,453**	14,182
Additions		**1,799**	1,289
Written off		**(863)**	(18)
Balance as at the end of the financial year		**16,389**	15,453
Less: Accumulated amortisation			
Balance as at the beginning of the financial year		**9,504**	7,419
Charge for the financial year	29	**1,846**	2,102
Written off		**–**	(17)
Balance as at the end of the financial year		**11,350**	9,504
Less: Accumulated impairment loss			
Balance as at the beginning of the financial year		**1,199**	1,199
Reversal for the financial year		**(336)**	–
Written off		**(863)**	–
Balance as at the end of the financial year		**–**	1,199
Net book value as at the end of the financial year		**5,039**	4,750

15 DEPOSITS FROM CUSTOMERS

	2017 RM'000	2016 RM'000
Savings Deposits:		
– Wadiah	**1,353,675**	1,221,616
Demand Deposits:		
– Wadiah	**6,392,228**	3,764,386
– Commodity Murabahah	**55,952**	5,926
Term Deposits:		
– Commodity Murabahah	**24,813,727**	16,716,463
Specific Investment Account:		
– Commodity Murabahah	**5,098,668**	7,556,178
General Investment Account:		
– Mudharabah	**135,955**	155,359
	37,850,205	29,419,928

(a) The maturity structure of investment accounts and term deposits are as follows:

	2017 RM'000	2016 RM'000
Due within six months	**22,074,985**	20,429,737
Six months to one year	**7,966,481**	3,953,480
One year to three years	**4,814**	44,335
Three years to five years	**2,070**	448
	30,048,350	24,428,000

(b) By type of customer

	2017 RM'000	2016 RM'000
Government and statutory bodies	**4,313,279**	3,993,795
Business enterprises	**23,926,425**	19,129,387
Individuals	**9,224,592**	5,735,775
Others	**385,909**	560,971
	37,850,205	29,419,928

16 DEPOSITS AND PLACEMENTS OF BANKS AND OTHER FINANCIAL INSTITUTIONS

	2017 RM'000	2016 RM'000
Non-Mudharabah Funds:		
– Licensed Islamic banks	**2,945,973**	4,179,222
– Licensed banks	**1,115,096**	1,591,693
– Licensed investments banks	**298,349**	99,761
– BNM	**20,689**	3,890
	4,380,107	5,874,566
Mudharabah Funds:		
Licensed Islamic banks		
– Other financial institutions	**14,694**	555,628
	4,394,801	6,430,194

17 INVESTMENT ACCOUNT DUE TO DESIGNATED FINANCIAL INSTITUTIONS

	2017 RM'000	2016 RM'000
Mudharabah Restricted Investment Account		
Funding inflows/(outflows) – Principal (Note a):		
Balance as at the beginning of the financial year	**6,337,446**	6,084,508
New placement during the financial year	**3,746,999**	4,408,821
Redemption during the financial year	**(2,264,140)**	(4,155,883)
Balance as at the end of the financial year	**7,820,305**	6,337,446
Profit attributable to investment account holders – Total profit payable:		
Balance as at the beginning of the financial year	**285,025**	266,146
Profit distributed to investment account holders during the financial year	**310,130**	260,622
Profit paid to investment account holders during the financial year	**(312,762)**	(241,743)
Balance as at the end of the financial year	**282,393**	285,025
Net balance as at the end of the financial year	**8,102,698**	6,622,471
(a) Investment asset (principal):		
– Housing financing	**300,000**	300,000
– Hire purchase receivables	**700,000**	700,000
– Other term financing	**6,030,030**	4,804,399
– Short term fund	**–**	334,047
– Securities	**790,275**	199,000
– Total investment	**7,820,305**	6,337,446
(b) By type of counterparty		
– Licensed banks	**8,102,698**	6,622,471

17 INVESTMENT ACCOUNT DUE TO DESIGNATED FINANCIAL INSTITUTIONS (CONTINUED)

	Average profit sharing ratio %	Average rate of return %
2017		
– Below 1 year	**88**	**4.56**
– Between 1 to 2 years	**81**	**4.35**
– Between 2 to 5 years	**85**	**4.29**
– More than 5 years	**83**	**4.44**
2016		
– Below 1 year	–	–
– Between 1 to 2 years	88	4.28
– Between 2 to 5 years	74	4.31
– More than 5 years	–	–

18 RECOURSE OBLIGATION ON FINANCING SOLD TO CAGAMAS BERHAD ('CAGAMAS')

Recourse obligation on financing sold to Cagamas represents those acquired from the originators and sold to Cagamas with recourse. Under the agreement, the Bank undertakes to administer the financing on behalf of Cagamas and to buy back any financing which are regarded as defective based on pre-determined and agreed-upon prudential criteria with recourse against the originators. Such financing transactions and the obligation to buy back the financing are reflected as a liability on the statement of financial position. The financing are not de-recognised and are analysed in Note 8.

19 SUBORDINATED OBLIGATIONS

	2017 RM'000	2016 RM'000
4.95% RM500 million Tier II Subordinated Sukuk Murabahah 2014/2024	**503,187**	503,187
4.88% RM250 million Tier II Subordinated Sukuk Murabahah 2017/2027	**252,206**	–
	755,393	503,187

On 15 May 2014, the Bank issued RM500 million nominal value of Subordinated Sukuk Murabahah, being part of RM1 billion Subordinated Sukuk Murabahah Programme.

On 27 April 2017, the Bank had further issued RM250 million nominal value of Subordinated Sukuk Murabahah under the same RM1 billion programme.

Tranche	Principal RM'million	Maturity date	Profit rate	Profit payment
2014/2024	500	15 May 2024 (Callable on 2019)	4.95% per annum chargeable to 15 May 2024	Accrued and payable semi-annually in arrears
2017/2027	250	27 April 2027 (Callable on 2022)	4.88% per annum chargeable to 27 April 2027	Accrued and payable semi-annually in arrears

20 OTHER LIABILITIES

	Note	2017 RM'000	2016 RM'000
Sundry creditors		**4,691**	10,692
Amount due to holding company	(a)	**168,364**	769,591
Amounts due to other related companies	(a)	**259**	668
Deferred income		**31,682**	43,947
Short term employee benefits		**5,391**	7,397
Accrual for operational expenses		**10,206**	9,993
Other accruals and payables	(b)	**125,199**	115,575
		345,792	957,863

(a) The amounts due to holding company and other related companies are unsecured, non-profit bearing and repayable within the normal credit period.

(b) Included in the other accruals and payables is undistributed charity funds amounting to RM88,000 (2016: RM93,000). The funds are sourced from ta'widh (late payment charges).

Movement of sources and uses of charity funds are as follows:

	2017 RM'000	2016 RM'000
Undistributed funds as at the beginning of the financial year	**93**	98
Funds collected/received during the year	**–**	–
Uses of funds during the year	**(5)**	(5)
Contribution to non-profit organisation	**(5)**	(5)
Undistributed funds as at the end of the financial year	**88**	93

21 SHARE CAPITAL

	2017 RM'000	2016 RM'000
Issued and fully paid:		
Balance as at the beginning of financial year	**1,273,424**	1,173,424
Issued during the financial year	**–**	100,000
Balance as at the end of financial year	**1,273,424**	1,273,424

In 2016, the Bank increased its issued and paid up share capital from RM1,173,424,002 to RM1,273,424,002 via the issuance of 100,000,000 new ordinary shares of RM1.00 each to RHB Bank, its holding company.

The new ordinary shares issued during the financial year rank *pari passu* in all aspects with the existing ordinary shares of the Bank.

22 RESERVES

	Note	2017 RM'000	2016 RM'000
Statutory reserve	(a)	**–**	762,388
AFS reserve	(b)	**(15,929)**	(31,944)
Regulatory reserve	(c)	**267,031**	158,516
Retained profits		**1,787,323**	766,058
		2,038,425	1,655,018

(a) Pursuant to the revised policy document on Capital Funds for Islamic Banks by BNM whereby the previous requirement to maintain a reserve fund is no longer required given the implementation of the Capital Conservation Buffer under the Capital Adequacy Framework, statutory reserve which was previously maintained by the Bank is no longer required and had been transferred to retained profits.

(b) The AFS reserve arises from a change in the fair value of financial investments classified as AFS. The unrealised gains or losses are transferred to the income statement upon disposal, de-recognition or impairment of such securities.

(c) Regulatory reserve represents the Bank's compliance with BNM's Policy on Classification and Impairment Provisions for Financing, to maintain, in aggregate, the collective impairment allowances and regulatory reserve of no less than 1.2% of total outstanding financing, net of individual impairment allowances.

23 INCOME DERIVED FROM INVESTMENT OF DEPOSITORS' FUNDS

	2017 RM'000	2016 RM'000
Income derived from investment of:		
(i) General investment deposits	**7,019**	8,096
(ii) Other deposits	**1,950,033**	1,742,000
	1,957,052	1,750,096

(i) Income derived from investment of general investment deposits:

	2017 RM'000	2016 RM'000
Financing and advances	**5,430**	6,105
Securities purchased under resale agreements	**176**	263
Financial assets HFT	**18**	11
Financial investments AFS	**505**	615
Financial investments HTM	**248**	342
Money at call and deposits with banks and other financial institutions	**600**	707
Total finance income and hibah	**6,977**	8,043
Other operating income (Note a)	**42**	53
	7,019	8,096
Of which:		
Financing income earned on impaired financing	**38**	55
(a) Other operating income comprise of:		
Commission	**28**	24
Guarantee fees	**9**	9
Net (loss)/gain on revaluation of financial assets HFT	**(3)**	1
Net loss on disposal of financial assets HFT	**(2)**	(6)
Net gain on disposal of financial investments AFS	**9**	24
Net gain on early redemption of financial investments HTM	**1**	1
	42	53

23 INCOME DERIVED FROM INVESTMENT OF DEPOSITORS' FUNDS (CONTINUED)

(ii) Income derived from investment of other deposits:

	2017 RM'000	2016 RM'000
Financing and advances	**1,508,577**	1,313,738
Securities purchased under resale agreements	**48,946**	56,534
Financial assets HFT	**4,967**	2,444
Financial investments AFS	**140,384**	132,272
Financial investments HTM	**68,827**	73,566
Money at call and deposits with banks and other financial institutions	**166,803**	152,163
Total finance income and hibah	**1,938,504**	1,730,717
Other operating income (Note a)	**11,529**	11,283
	1,950,033	1,742,000
Of which:		
Financing income earned on impaired financing	**10,507**	11,769
(a) Other operating income comprise of:		
Commission	**7,700**	5,070
Guarantee fees	**2,493**	1,837
Net (loss)/gain on revaluation of financial assets HFT	**(810)**	258
Net loss on disposal of financial assets HFT	**(660)**	(1,321)
Net gain on disposal of financial investments AFS	**2,441**	5,149
Net gain on early redemption of financial investments HTM	**365**	290
	11,529	11,283

24 INCOME DERIVED FROM INVESTMENT ACCOUNT FUNDS

	2017 RM'000	2016 RM'000
Financing and advances	**318,824**	303,862
Financial investments HTM	**52,523**	9,830
Money at call and deposits with banks and other financial institutions	**4,592**	4,296
Total finance income and hibah	**375,939**	317,988

25 INCOME DERIVED FROM INVESTMENT OF SHAREHOLDERS' FUNDS

	2017 RM'000	2016 RM'000
Financing and advances	**48,990**	44,532
Securities purchased under resale agreements	**1,591**	1,916
Financial assets HFT	**161**	83
Financial investments AFS	**4,559**	4,484
Financial investments HTM	**2,235**	2,494
Money at call and deposits with banks and other financial institutions	**5,417**	5,158
Total finance income and hibah	**62,953**	58,667
Other operating income (Note a)	**112,565**	111,753
	175,518	170,420
Of which:		
Financing income earned on impaired financing	**341**	398
(a) Other operating income comprise of:		
Commission	**22,690**	13,697
Service charges and fees	**63,534**	61,453
Guarantee fees and underwriting fees	**81**	62
Foreign exchange profit	**38,471**	37,007
Net (loss)/gain on revaluation of financial assets HFT	**(26)**	9
Net loss on disposal of financial assets HFT	**(21)**	(45)
Net gain on disposal of financial investments AFS	**79**	175
Net gain on early redemption of financial investments HTM	**12**	10
Net loss on fair value hedges (Note 10)	**(1,078)**	(799)
Net (loss)/gain on revaluation of derivatives	**(11,199)**	116
Other income	**22**	68
	112,565	111,753

26 ALLOWANCE FOR IMPAIRMENT ON FINANCING AND ADVANCES

	2017 RM'000	2016 RM'000
Allowance for impairment on financing and advances:		
– Individual impairment allowance/(written back)	**29,204**	(3,438)
– Collective impairment allowance	**37,562**	77,902
– Impaired financing recovered	**(12,343)**	(13,464)
– Impaired financing written off	**12,311**	9,168
	66,734	70,168

27 INCOME ATTRIBUTABLE TO DEPOSITORS

	2017 RM'000	2016 RM'000
Deposits from customers:		
– Mudharabah funds	**4,621**	5,064
– Non-Mudharabah funds	**1,097,763**	973,022
Deposits and placements of banks and other financial institutions:		
– Non-Mudharabah funds	**172,012**	176,872
Subordinated obligations	**33,073**	24,818
Recourse obligations on financing sold to Cagamas	**21,672**	43,654
Obligations on securities sold under repurchase agreements	**254**	–
	1,329,395	1,223,430

28 PERSONNEL EXPENSES

	2017 RM'000	2016 RM'000
Salaries, allowances and bonuses	**21,597**	25,219
Contributions to Employees' Provident Fund	**3,053**	4,081
Other staff related costs	**2,432**	3,007
	27,082	32,307

Included in the personnel expenses is the Managing Director's remuneration (excluding benefits-in-kind) totalling RM1,843,000 (2016: RM3,532,000), as disclosed in Note 30.

29 OTHER OVERHEADS AND EXPENDITURES

	2017 RM'000	2016 RM'000
Establishment costs		
Property, plant and equipment:		
– Depreciation	**2,591**	1,751
– Written off	**–**	447
Computer software license		
– Amortisation	**1,846**	2,102
– Written off	**–**	1
Information technology expenses	**3,123**	3,988
Repair and maintenance	**733**	912
Rental of premises	**4,704**	4,650
Water and electricity	**569**	857
Rental of equipment	**2**	7
Printing and stationeries	**3,477**	8,275
Insurance	**3,633**	3,049
Others	**3,757**	4,174
	24,435	30,213
Marketing expenses		
Advertisement and publicity	**2,135**	2,223
Sales commission	**8,898**	8,326
Travelling expenses	**297**	438
Motor vehicle expenses	**191**	196
Others	**2,353**	1,620
	13,874	12,803
Administration and general expenses		
Auditors' remuneration:		
– Statutory audit	**174**	164
– Limited review	**57**	55
– Other audit related	**100**	100
Communication expenses	**4,306**	5,321
Legal and professional fee	**1,960**	2,489
Management fee	**239,036**	158,318
Others	**11,657**	10,304
	257,290	176,751
	295,599	219,767

Included in the administration and general expenses of the Bank are other Director's remuneration (excluding benefits-in-kind) totaling RM1,246,000 (2016: RM977,000) as disclosed in Note 30.

30 REMUNERATION OF MANAGING DIRECTOR ('MD'), NON-EXECUTIVE DIRECTORS AND SHARIAH COMMITTEE MEMBERS

2017	Salary and other remuneration RM'000	Benefits-in-kind (based on an estimated monetary value) RM'000	Bonus RM'000	Total RM'000
Managing Director				
Dato' Adissadikin Ali	1,143	7	700	1,850
	1,143	7	700	1,850

	Fees RM'000	Benefits-in-kind (based on an estimated monetary value) RM'000	Other remuneration RM'000	Total RM'000
Non-executive Directors				
Dato' Abd Rahman Dato' Md Khalid	135	–	133	268
Datuk Haji Faisal Siraj	135	–	79	214
Dato' Foong Chee Meng (appointed on 1 August 2017)	57	–	24	81
Ong Ai Lin (appointed on 1 September 2017)	45	–	29	74
Haji Md Ja'far Abdul Carrim (deceased on 19 October 2017)	136	17	253	406
Dato' Mohd Ali Mohd Tahir (resigned on 28 February 2017)	21	–	42	63
Dato' Sri Haji Syed Zainal Abidin Syed Mohamed Tahir (resigned on 1 August 2017)	78	–	79	157
	607	17	639	1,263

	Fees RM'000
Shariah Committee	
Dr. Ghazali Jaapar (Chairman)	95
Prof. Dr. Joni Tamkin Borhan (deceased on 19 May 2017)	34
Assoc. Prof. Dr. Amir Shaharuddin	82
Wan Abdul Rahim Kamil Wan Mohamed Ali	81
Mohd Fadhly Md. Yusoff	82
Shabnam Mohamad Mokhtar	82
	456

Note:
During the financial year, Directors of the Bank are covered under the Directors' Liability Insurance in respect of liabilities arising from acts committed in their respective capacity as, inter alia, Directors of the Bank subject to the term of the policy. The total amount of Directors' Liability Insurance effected for the Directors of the Bank was RM100.0 million. The total amount of premium paid for the Directors' Liability Insurance by the Bank was RM280,000.

30 REMUNERATION OF MANAGING DIRECTOR ('MD'), NON-EXECUTIVE DIRECTORS AND SHARIAH COMMITTEE MEMBERS (CONTINUED)

2016	Salary and other remuneration RM'000	Benefits-in-kind (based on an estimated monetary value) RM'000	Bonus RM'000	Total RM'000
Managing Director				
Dato' Adissadikin Ali (appointed on 1 August 2016)	526	3	282	811
Haji Ibrahim Hassan (resigned on 1 August 2016)	866	7	1,858	2,731
	1,392	10	2,140	3,542

	Fees RM'000	Benefits-in-kind (based on an estimated monetary value) RM'000	Other remuneration RM'000	Total RM'000
Non-executive Directors				
Haji Md Ja'far Abdul Carrim	150	22	187	359
Datuk Haji Faisal Siraj	120	–	65	185
Dato' Mohd Ali Mohd Tahir	120	–	56	176
Dato' Sri Haji Syed Zainal Abidin Syed Mohamed Tahir	120	–	102	222
Charles Lew Foon Keong (retired at Annual General Meeting on 11 May 2016)	43	–	14	57
	553	22	424	999

	Fees RM'000
Shariah Committee	
Dr. Ghazali Jaapar	95
Prof. Dr. Joni Tamkin Borhan	84
Assoc. Prof. Dr. Amir Shaharuddin	84
Wan Abdul Rahim Kamil Wan Mohamed Ali	83
Mohd Fadhly Md. Yusoff	83
Shabnam Mohamad Mokhtar	84
	513

31 TAXATION

	2017 RM'000	2016 RM'000
Malaysian income tax:		
– Current tax	**110,354**	113,283
– (Over)/under provision in respect of prior financial years	**(755)**	1,345
Deferred tax (Note 12)	**(641)**	(11,255)
	108,958	103,373

The numerical reconciliation between the effective tax rate and the applicable statutory income tax rate are as follows:

	2017 %	2016 %
Tax at Malaysian statutory income tax rate	**24.0**	24.0
Tax effects in respect of:		
– Expenses not deductible for tax purposes	**0.1**	0.1
– (Over)/under provision in respect of prior financial years	**(0.2)**	0.3
– Temporary differences not recognised in prior financial years	**(0.8)**	(0.3)
– Non-taxable income	**(0.4)**	(0.2)
Effective tax rate	**22.7**	23.9

32 EARNINGS PER SHARE

Basic earnings per share is calculated by dividing the net profit for the financial year by the weighted average number of ordinary shares in issue during the financial year.

	2017	2016
Net profit for the financial year (RM'000)	**367,392**	324,784
Weighted average number of ordinary shares in issue ('000)	**1,273,424**	1,185,446
Basic earnings per share (sen)	**28.85**	27.40

33 INCOME TAX EFFECTS RELATING TO COMPONENTS OF OTHER COMPREHENSIVE INCOME

	2017			2016		
	Before tax RM'000	**Tax effects RM'000**	**Net of tax RM'000**	**Before tax RM'000**	**Tax effects RM'000**	**Net of tax RM'000**
Financial investments AFS:						
– Net fair value gain and net amount transfer to income statement	**21,072**	**(5,057)**	**16,015**	9,541	(2,290)	7,251

34 RELATED PARTY TRANSACTIONS

(a) Related parties and relationships

The related parties of, and their relationship with the Bank, are as follows:

Related parties	**Relationship**
RHB Bank Berhad	Holding company
Employees' Provident Fund ('EPF')	Holding company's substantial shareholder, a fund body that is significantly influenced by government
Subsidiaries of RHB Bank Berhad as disclosed in its financial statements	Subsidiaries of the holding company
Subsidiaries, associates and joint ventures of EPF as disclosed in its financial statements	Reporting entities that EPF has control or significant influence
Key management personnel	The key management personnel of the Bank consists of: – All Directors of the Bank and – Members of the Group Management Committee ('GMC')
Related parties of key management personnel (deemed as related to the Bank)	(i) Close family members and dependents of key management personnel (ii) Entities that are controlled, jointly controlled or significantly influenced by, or for which voting power in such entity resides with, directly or indirectly by key management personnel or its close family members

(b) Related party transaction

In addition to related party disclosures mentioned elsewhere in the financial statements, set out below are other significant related party transactions and balances.

Other related parties of the Bank comprise of transactions or balances with the companies in the RHB Bank Berhad Group.

All related party transactions are entered into in the normal course of business at agreed terms between the related parties.

34 RELATED PARTY TRANSACTIONS (CONTINUED)

(b) Related party transaction (continued)

2017	Holding company RM'000	EPF and EPF Group of companies RM'000	Key management personnel RM'000	Other related companies RM'000
Income				
Commission	–	–	–	146
Income derived from investment of depositors' funds	50,727	19,746	–	–
Other income	77,693	4	–	–
	128,420	19,750	–	146
Expenditure				
Profit expense on deposits and placements	26,816	108	4,971	1,251
Profit expense on investment account	310,130	–	–	–
Reimbursement of operating expenses to holding company	239,036	–	–	–
Other expenses	435	–	–	1,584
	576,417	108	4,971	2,835
Amounts due from				
Cash and short term funds	10,403	–	–	–
Deposits and placements with banks and other financial institutions	14,613	–	–	–
Securities purchased under resale agreements	1,587,979	–	–	–
Financial investments AFS	–	45,214	–	–
Financing and advances	–	792,394	–	–
Derivative assets	321,607	–	–	–
	1,934,602	837,608	–	–
Amounts due to				
Derivative liabilities	14,588	–	–	–
Demand and investment deposits	–	101,668	755	25,861
Deposits and placements of banks and other financial institutions	211,477	–	–	–
Investment account due to designated financial institutions	8,102,698	–	–	–
Other liabilities	168,364	–	–	259
	8,497,127	101,668	755	26,120

34 RELATED PARTY TRANSACTIONS (CONTINUED)

(b) Related party transaction (continued)

2016	**Holding company RM'000**	**EPF and EPF Group of companies RM'000**	**Key management personnel RM'000**	**Other related companies RM'000**
Income				
Commission	–	–	–	132
Income derived from investment of depositors' funds	58,713	30,737	–	–
Other income	–	–	–	6
	58,713	30,737	–	138
Expenditure				
Profit expense on deposits and placements	33,521	382	–	606
Profit expense on investment account	260,622	–	–	–
Reimbursement of operating expenses to holding company	158,318	–	–	–
Other expenses	1,898	–	–	3,363
	454,359	382	–	3,969
Amounts due from				
Securities purchased under resale agreements	2,353,950	–	–	–
Financing and advances	–	765,640	–	–
Derivative assets	46,452	–	–	–
	2,400,402	765,640	–	–
Amounts due to				
Derivative liabilities	364,325	–	–	–
Demand and investment deposits	1,797	382,658	77	20,564
Deposits and placements of banks and other financial institutions	1,142,864	–	–	–
Investment account due to designated financial institutions	6,622,471	–	–	–
Other liabilities	769,591	–	–	668
	8,901,048	382,658	77	21,232

34 RELATED PARTY TRANSACTIONS (CONTINUED)

(c) Key management personnel

The remuneration of key management personnel are as follows:

	2017 RM'000	2016 RM'000
Short term employee benefits:		
– Fees	**607**	553
– Salary and other remuneration	**2,264**	3,529
– Defined contribution plan	**218**	427
– Benefits-in-kind (based on an estimated monetary value)	**24**	32
	3,113	4,541

The above remuneration includes Directors' remuneration as disclosed in Note 30.

(d) Credit exposures arising from transactions with connected parties

Credit exposures with connected parties as per BNM's revised Guidelines on Credit Transactions and Exposures with Connected Parties are as follows:

	2017	2016
Outstanding credit exposure with connected parties (RM'000)	**1,767,706**	1,607,926
Percentage of outstanding credit exposures to connected parties as proportion of total credit exposures (%)	**3.74**	4.22
Percentage of outstanding credit exposures with connected parties which is non-performing or in default (%)	**–**	0.01

The credit exposures above are derived based on BNM's revised Guidelines on Credit Transactions and Exposures with Connected Parties, which are effective on 1 January 2008.

35 COMMITMENTS AND CONTINGENCIES

In the normal course of business, the Bank makes various commitments and incurs certain contingent liabilities with legal recourse to customers.

	2017 RM'000	2016 RM'000
Transaction-related contingent items	**195,298**	127,119
Short term self-liquidating trade-related contingencies	**111,779**	74,479
Obligations under underwriting agreements	**–**	76,000
Commitment to buy back the Islamic securities arising from the Sell and Buy Back ('SBBA') transaction	**629,085**	–
Irrevocable commitments to extend credit:		
– Maturity more than one year	**5,800,512**	4,824,220
Foreign exchange related contracts*:		
– Less than one year	**7,910,145**	7,577,185
– One year to less than five years	**1,713,345**	766,434
– More than five years	**949,178**	999,623
Profit rate related contracts*:		
– Less than one year	**3,690,000**	2,585,000
– One year to less than five years	**767,338**	2,279,448
Any commitments that are unconditionally cancelled at any time by the Bank without prior notice or that effectively provide for automatic cancellation due to deterioration in a borrower's creditworthiness	**2,513,842**	2,183,074
	24,280,522	21,492,582

* These derivatives are revalued on gross position basis and the unrealised gains or losses has been reflected in the income statement and statement of financial position as derivative assets and liabilities.

36 OPERATING LEASE COMMITMENTS

The Bank has lease commitments in respect of rented premises which are classified as operating leases. A summary of the non-cancellable long term commitments, net of sub-leases, is as follows:

	2017 RM'000	2016 RM'000
Within one year	**4,250**	3,552
Between one to five years	**5,069**	2,103
	9,319	5,655

37 CAPITAL COMMITMENTS

	2017 RM'000	2016 RM'000
Capital expenditure for property, plant and equipment:		
– Authorised and contracted for	**6,460**	3,084

38 FINANCIAL RISK MANAGEMENT

(a) Financial Risk Management Objectives and Policies

Risk is inherent in the Bank's activities and is managed through a process of on-going identification, measurement and monitoring, subject to limits and other controls. Besides credit risk, the Bank is exposed to a range of other risk types such as market, liquidity, operational, legal, Shariah, strategic and cross-border, as well as other forms of risk inherent to its strategy, product range and geographical coverage.

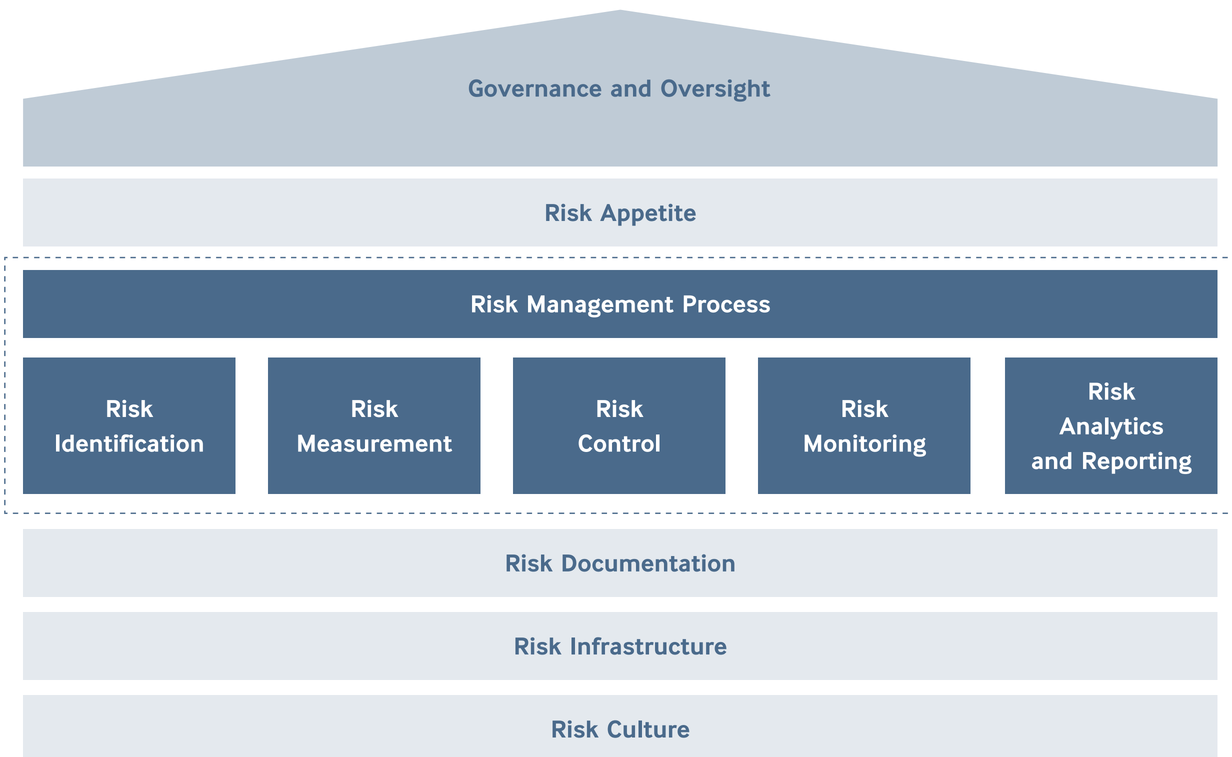
Effective risk management is fundamental to being able to drive sustainable growth and shareholder's value, while maintaining competitive advantage, and is thus a central part of the proactive risk management of the Bank's operating environment.

The Group Risk Management Framework governs the management of risks in the Group, as follows:

(1) It provides a holistic overview of the risk and control environment of the Group, with risk management aimed towards loss minimisation and protection against losses which may occur through, principally, the failure of effective checks and controls in the organisation.

(2) It sets out the strategic progression of risk management towards becoming a value creation enterprise. This is realised through building up capabilities and infrastructure in risk management sophistication, and enhanced risk quantification to optimise risk-adjusted returns.

The Group Risk Management Framework is represented in the following diagram:



38 FINANCIAL RISK MANAGEMENT (CONTINUED)

(a) Financial Risk Management Objectives and Policies (continued)

The Risk Management Framework contains five fundamental principles that drive the philosophy of risk management in the Group. They are:

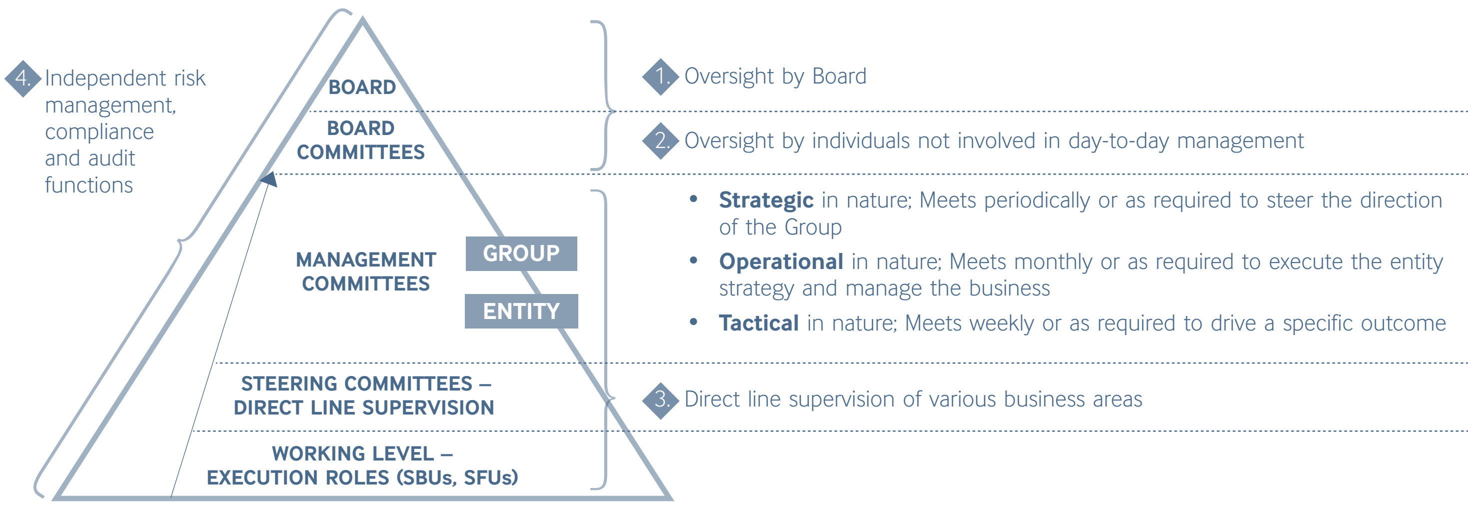
(1) Risk governance from the Board of Directors of various operating entities within the Group

The ultimate responsibility of the Boards of Directors in the Group is to ensure that an effective risk management strategy is in place and uniformly understood across the Group. The Group has a structured framework to support the Board's oversight responsibilities.

Risk Governance and Organisation

The Board Risk Committee ('BRC') is the principal Board Committee that provides oversight over risk management for the Group to ensure that the Group's risk management process is in place and functional. The BRC assists the Board to review the Group's overall risk management philosophy, frameworks, policies and models. An Islamic Risk Management Committee ('IRMC') has also been established to assist the Board of Directors of the Bank on issues relevant and unique to Islamic finance.

The responsibility for the supervision of the day-to-day management of enterprise risk and capital matters is delegated to the Group Capital and Risk Committee ('GCRC') comprising Senior Management of the Group and which reports to the BRC/IRMC and the GMC. There are other committees set up to manage specific areas of risks in the Group. An overview of this governance framework at Group level is as below:



38 FINANCIAL RISK MANAGEMENT (CONTINUED)

(a) Financial Risk Management Objectives and Policies (continued)

The Risk Management Framework contains five fundamental principles that drive the philosophy of risk management in the Group. They are (continued):

Risk Culture

(2) Clear understanding of risk management ownership

Proactive risk ownership is important for effective management of risk. This promotes a risk awareness culture throughout the Group. The Group adopts the principle that 'Risk and Compliance is Everyone's Responsibility'.

The Strategic Business Groups ('SBGs') and Strategic Functional Groups ('SFGs') of the respective operating entities in the Group are collectively responsible for identifying, managing and reporting risks. The business units manage certain defined risks supported by the services provided by the functional units, including the risk management function. The approach is based on the 'three lines of defence' model as depicted below:

FIRST LINE **Business/Functional Level**	• Responsible for managing day-to-day operational risks and compliance issues • Business Risk and Compliance Officer is to assist business/functional unit in day-to-day risks and compliance matters
SECOND LINE **Group Risk Management & Group Compliance**	• Responsible for oversight, establishing governance and providing support to business/functional unit on risk and compliance matters
THIRD LINE **Group Internal Audit**	• Provide independent assurance to the Board that risk and compliance management functions effectively as designed

Risk Environment and Infrastructure

(3) Institutionalisation of a risk-focused organisation

In addition to risk ownership, a risk-focused culture is promoted throughout the Group through strengthening of the central risk management function and continuous reinforcement of a risk and control environment within the Group. There is a continuous review of business activities and processes to identify significant risk areas and implement control procedures to operate within established corporate policies and limits.

Group Risk and Credit Management is independent of the business function to ensure that the necessary balance in risk/return decisions is not compromised by short term pressures to generate revenues. The said function is headed by the Group Chief Risk Officer.

The business and functional heads are accountable for risk management in their businesses and functions, and for overseas operations where they have governance responsibilities. The business and functional units have clear segregation of duties to ensure that business processes are functioning effectively. There is accountability delegated to the appropriate authority to enable them to execute their respective authorities in meeting the business strategies without compromising the risk management process.

The primary responsibility for managing risks, therefore, rests with the business managers who are best equipped to ensure that risk management and control are continuously focused on the way business is conducted. There is a continuous review of business activities and processes to identify significant risk areas and implement control procedures to operate within established corporate policies and limits.

38 FINANCIAL RISK MANAGEMENT (CONTINUED)

(a) Financial Risk Management Objectives and Policies (continued)

The Risk Management Framework contains five fundamental principles that drive the philosophy of risk management in the Group. They are (continued):

Risk Environment and Infrastructure (continued)

(3) Institutionalisation of a risk-focused organisation (continued)

The risk management processes within the Bank seek to identify, measure, monitor and control risk so that risk exposures are adequately managed and the expected returns adequately compensate the risks.

- Identification: The identification and analysis of the existing and potential risks is a continuing process, in order to facilitate and ensure that the risks can be managed and controlled within the risk appetite of the Bank and specific entity, where necessary.
- Measurement: Risks are measured, assessed and aggregated using comprehensive qualitative and quantitative risk measurement methodologies, and the process also serves as an important tool as it provides an assessment of capital adequacy and solvency.
- Controlling and Monitoring: Controls, triggers and limits are used to manage risk exposures and to facilitate early identification of potential problem on a timely basis.
- Analytics and Reporting: Risk analysis and reports prepared at the respective entities and consolidated level as well as business level are regularly escalated to the senior management and relevant Boards to ensure that the risks remain within the established appetite and to support an informed decision-making process.

The Bank recognises that effective implementation of the risk management system and process must be supported by a robust set of documentation and infrastructure. Towards this end, the Bank has established frameworks, policies and other relevant control documents to ensure clearly defined practices and processes are implemented consistently across the Bank.

In terms of risk infrastructure, the Bank has organised its resources and talents into specific functions, and invested into technology, including data management to support the Bank's risk management activities.

Risk Appetite

(4) Alignment of risk management to business strategies

The Group Risk Management Framework serves to align the Group's business strategy to risk strategy, and vice-versa. This is articulated through the risk appetite setting and the Group's annual business and financial budgetary plan, which is facilitated by the integration of risk measures in capital management.

Risk appetite is set by the Board and reported through various metrics that enable the Bank to manage capital constraints and shareholder's expectations. The risk appetite is a key component of the management of risks and describes the types and level of risk that the Bank is prepared to accept in delivering its strategy.

(5) Optimisation of risk-adjusted return

One of the objectives of capital management is to reflect a risk-adjusted return assumed by the businesses throughout the Group. By linking risk to capital, the risk-adjusted return measure contributes to the creation of shareholder value by facilitating the allocation of capital to the businesses.

The medium to long-term strategy and principle of risk management of the Group is to intensify the integration of capital management within the Group. The Group is progressively implementing a risk-adjusted return based framework for allocation of capital to business units and for performance measurement and management.

38 FINANCIAL RISK MANAGEMENT (CONTINUED)

(a) Financial Risk Management Objectives and Policies (continued)

The Risk Management Framework contains five fundamental principles that drive the philosophy of risk management in the Group. They are (continued):

Major Areas of Risk

As a banking institution with key activities covering retail, business banking, corporate banking and advisory services, treasury products and services, the Bank is subject to business risks which are inherent in the financial services industry. Generally, these business risks can be broadly classified as follows:

(i) Market risk – the risk of loss arising from adverse movements in market indicators, such as profit rates, credit spreads, equity prices, currency exchange rates and commodity prices.

(ii) Liquidity risk – the risk of the Bank being unable to maintain sufficient liquid assets to meet its financial commitments and obligations when they fall due and transact at a reasonable cost. Liquidity risk also arises from the inability to manage unplanned decreases or changes in funding sources.

(iii) Credit risk – the risk of loss arising from customers' or counterparties' failure to fulfil their financial and contractual obligations in accordance with the agreed terms. It stems primarily from the Bank's lending/financing, trade finance and its funding, investment and trading activities from both on- and off-balance sheet transactions.

(iv) Operational risk – the risk of loss resulting from inadequate or failed internal processes, people, systems and/or external events, which also includes IT, legal and Shariah non-compliance risk but excludes strategic and reputational risk.

To mitigate the various business risks of the Bank, the following has been put in place:

Market Risk

- A framework of risk policies, measurement methodologies and limits, as approved by the Board, which controls the Bank's financial market activities as well as to identify potential risk areas early in order to mitigate against any adverse effects arising from market volatility.
- The Group Asset and Liability Committee ('Group ALCO') and the GCRC performs a critical role in the oversight of the management of market risk and supports the IRMC and BRC in the overall market risk management.
- The Group Risk Management function forms a centralised function to support Senior Management to operationalise the processes and methods, to ensure adequate risk control and oversight are in place.
- The Bank applies risk monitoring and assessment tools to measure trading book positions and market risk factors. Statistical and non–statistical risk assessment tools applied include Value-at-Risk ('VaR'), sensitivity analysis and stress testing.
- Market risk is primarily monitored and controlled via a structure of limits and triggers i.e. cut loss, VaR, trading and notional limit set in accordance with the size of positions and risk tolerance appetites.
- Periodic stress testing are applied to the Bank to ascertain market risk under abnormal market conditions.

38 FINANCIAL RISK MANAGEMENT (CONTINUED)

(a) Financial Risk Management Objectives and Policies (continued)

The Risk Management Framework contains five fundamental principles that drive the philosophy of risk management in the Group. They are (continued):

Liquidity Risk

- The Group ALCO plays a fundamental role in the asset and liability management of the Bank and establishes strategies to assist in controlling and reducing any potential exposures to liquidity risk.
- The liquidity risk management process involves establishing liquidity risk management policies and limits, regular monitoring against liquidity risk limits, regular stress testing, and establishing contingency funding plans. These processes are subject to regular reviews to ensure that they remain relevant in the context of prevailing market conditions.
- Limits on the minimum portion of maturing funds available to meet obligations and the minimum level of inter–bank and other borrowing facilities are set to ensure adequate cover for withdrawals arising from unexpected levels of demand.
- Defined liquidity management ratios are maintained and monitored.
- The Bank has established a Liquidity Incident Management Procedure to manage any potential adverse liquidity incidences, and which can be implemented on a timely basis so that appropriate actions can be taken to mitigate against any unexpected market developments.

Credit Risk

- The Bank abides to the Board approved credit policy which supports the development of a strong credit culture and with the objective of maintaining a well-diversified portfolio that addresses credit risk, and mitigates concern for unexpected losses.
- Industry best practices are incorporated into this policy.
- Group Credit Committee ('GCC') is responsible for ensuring adherence to the Board approved credit risk appetite as well as the effectiveness of credit risk management. GCC is the senior management committee empowered to approve or reject all financial investments, counterparty credit and lending/financing up to the defined threshold limits.
- Group Investment Underwriting Committee ('GIUC') deliberates, approves and rejects stockbroking/equities/futures business related proposals such as equity underwriting, equity derivatives and structured products, and share margin financing.
- GCC and GIUC submit to the Board Credit Committee ('BCC') for affirmation or veto if the financing facilities exceed a pre-defined threshold.
- The Bank also ensures that internal processes and credit underwriting standards are adhered to before credit proposals are approved. All credit proposals are first evaluated by the originating business units before being evaluated prior to submission to the relevant committees for approval. With the exception of credit applications for consumer and approved products under program lending/financing which can be approved by business units' supervisors, all other credit facilities are subject to independent assessment by a team of dedicated and experienced credit evaluators in Head Office. For proper checks and controls, joint approval is required for all discretionary lending between business and independent credit underwriters. Financing which are beyond the delegated lending authority limits will be escalated to the relevant committees for approval.

38 FINANCIAL RISK MANAGEMENT (CONTINUED)

(a) Financial Risk Management Objectives and Policies (continued)

The Risk Management Framework contains five fundamental principles that drive the philosophy of risk management in the Group. They are (continued):

Credit Risk (continued)

- Internal credit rating models are an integral part of the Bank's credit risk management, decision-making process, and regulatory capital calculations.
- Clients' accounts are reviewed at regular intervals and weakening credits are transferred to Loan Recovery for more effective management.
- Counterparty, industry and product exposure limits/directions are set and risk reward relationship are mapped with the aim of maintaining a diverse credit profile and track the changing risk concentrations in response to market changes and external events.
- The Bank has obtained BNM's approval to apply the Internal Ratings-Based ('IRB') approach for credit risk, whereby more advanced Basel II approaches and key program components are implemented, which includes (i) enhancing the returns of the Bank using established credit risk framework and methodologies, (ii) implementing and using empirical credit scoring models for consumer financing and credit grading models for business financing, and (iii) designing and implementing modelling of expected and unexpected losses.
- Plans are underway to migrate other material portfolios to the IRB approach for credit risk.

Operational Risk

- The Group Risk Management function is responsible for the development of group-wide operational risk policies, framework and methodologies, and providing guidance and information to the business units on operational risk areas. The respective business units are primarily responsible for managing operational risk on a day-to-day basis. Some of the operational risk tools used include Risk and Control Self-Assessment, Key Risk Indicators, Incident and Loss Management.
- The Bank's operational risk management system has integrated applications to support the operational risk management process. This system facilitates the Bank' capabilities for the Advanced Measurement Approach of the Basel II Framework in the future.
- The Bank has Business Continuity Planning ('BCP') programmes for the major critical business operations and activities at the Head Office, data centre, and branch locations. The BCP programmes are subject to regular testing to ensure efficacy, reliability and functionality.
- There is continuous refinement of existing policies, procedures and internal control measures; and regular internal review, compliance monitoring, and audits are performed to prevent and/or minimise unexpected losses.
- Regular operational risk reporting is made to senior management, relevant committees and board to facilitate the identification of adverse operational lapses, taking of prompt corrective actions, and ensuring appropriate risk mitigation decision making and action plans.

38 FINANCIAL RISK MANAGEMENT (CONTINUED)

(b) Financial Instruments by Category

2017	Financing and receivables RM'000	Assets at fair value through the profit and loss RM'000	Financial investments AFS RM'000	Financial investments HTM RM'000	Total RM'000
ASSETS					
Cash and short term funds	2,029,860	–	–	–	2,029,860
Securities purchased under resale agreements	1,587,979	–	–	–	1,587,979
Deposits and placements with banks and other financial institutions	447,210	–	–	–	447,210
Financial assets HFT	–	172,536	–	–	172,536
Financial investments AFS	–	–	3,394,493	–	3,394,493
Financial investments HTM	–	–	–	3,820,734	3,820,734
Financing and advances	42,701,794	–	–	–	42,701,794
Derivative assets	–	327,978	–	–	327,978
Other financial assets	7,617	–	–	–	7,617
	46,774,460	500,514	3,394,493	3,820,734	54,490,201

	Liabilities at fair value through the profit and loss RM'000	Other financial liabilities at amortised cost RM'000	Total RM'000
LIABILITIES			
Deposits from customers	–	37,850,205	37,850,205
Deposits and placements of banks and other financial institutions	–	4,394,801	4,394,801
Investment account due to designated financial institutions	–	8,102,698	8,102,698
Obligations on securities sold under repurchase agreements	–	604,163	604,163
Bills and acceptances payable	–	9,216	9,216
Derivative liabilities	327,723	–	327,723
Subordinated obligations	–	755,393	755,393
Other financial liabilities	–	281,991	281,991
	327,723	51,998,467	52,326,190

38 FINANCIAL RISK MANAGEMENT (CONTINUED)

(b) Financial Instruments by Category (continued)

2016	Financing and receivables RM'000	Assets at fair value through the profit and loss RM'000	Financial investments AFS RM'000	Financial investments HTM RM'000	Total RM'000
ASSETS					
Cash and short term funds	3,436,239	–	–	–	3,436,239
Securities purchased under resale agreements	2,353,950	–	–	–	2,353,950
Deposits and placements with banks and other financial institutions	537,141	–	–	–	537,141
Financial assets HFT	–	10,177	–	–	10,177
Financial investments AFS	–	–	3,459,647	–	3,459,647
Financial investments HTM	–	–	–	2,820,123	2,820,123
Financing and advances	33,841,566	–	–	–	33,841,566
Derivative assets	–	402,763	–	–	402,763
Other financial assets	114,720	–	–	–	114,720
	40,283,616	412,940	3,459,647	2,820,123	46,976,326

	Liabilities at fair value through the profit and loss RM'000	Other financial liabilities at amortised cost RM'000	Total RM'000
LIABILITIES			
Deposits from customers	–	29,419,928	29,419,928
Deposits and placements of banks and other financial institutions	–	6,430,194	6,430,194
Investment account due to designated financial institutions	–	6,622,471	6,622,471
Bills and acceptances payable	–	9,050	9,050
Derivative liabilities	400,812	–	400,812
Recourse obligation on financing sold to Cagamas	–	815,243	815,243
Subordinated obligations	–	503,187	503,187
Other financial liabilities	–	814,059	814,059
	400,812	44,614,132	45,014,944

38 FINANCIAL RISK MANAGEMENT (CONTINUED)

(c) Market Risk

Market risk sensitivity assessment is based on the changes in key variables, such as profit rates and foreign currency rates, while all other variables remain unchanged. The sensitivity factors used are assumptions based on parallel shifts in the key variables to project the impact on the assets and liabilities position of the Bank.

The scenarios used are based on the assumption that all key variables for all maturities move at the same time and by the same magnitude and do not incorporate actions that would be otherwise taken by the business units and risk management to mitigate the effect of this movement in key variables. The Bank seeks to ensure that the profit rate risk profile is managed to minimise losses and optimise net revenues.

(i) Profit rate sensitivity analysis

The profit rate sensitivity results below shows the impact on profit after tax and equity of financial assets and financial liabilities bearing floating profit rate and fixed rate financial assets and financial liabilities:

	Impact on profit after tax RM'000	Impact on equity RM'000
2017		
+100 bps	**33,212**	**(102,890)**
–100 bps	**(32,068)**	**109,717**
2016		
+100 bps	(3,498)	(113,332)
–100 bps	3,652	121,600

The results above represent financial assets and liabilities that have been prepared on the following basis:

(i) Impact on the profit after tax is the sum of valuation changes on fixed income instruments held in the trading portfolio and earnings movement for all short term profit rate sensitive assets and liabilities (with maturity or re-pricing tenure of up to one year) that is not held in the trading portfolio. Earnings movement for the short term profit rate sensitive assets and liabilities uses a set of risk weights with its respective time band to simulate the 100 bps (2016: 100 bps) profit rate change impact. For assets and liabilities with non-fixed maturity e.g. current and savings accounts, certain assumptions are made to reflect the actual sensitivity behaviour of these profit bearing assets and liabilities.

(ii) Impact on equity represents the changes in fair values of fixed income instruments held in the AFS portfolio arising from the shift in the profit rate.

38 FINANCIAL RISK MANAGEMENT (CONTINUED)

(c) Market Risk (continued)

(ii) Foreign currency sensitivity analysis

The foreign currency sensitivity represents the effect of the appreciation or depreciation of the foreign currency rates on the currency position, while other variables remain constant.

	Impact on profit after tax RM'000
2017	
+10%	**1,254**
–10%	**(1,254)**
2016	
+10%	(632)
–10%	632

Impact on the profit after tax is estimated on the assumption that foreign exchange move by the same amount and all other variables are held constant and are based on a constant reporting date position.

38 FINANCIAL RISK MANAGEMENT (CONTINUED)

(d) Profit rate risk

The table below summarises the Bank's exposure to profit rate risk. The carrying amount of assets and liabilities (includes non-financial instruments) are categorised by the earlier of contractual re-pricing or maturity dates:

	Non-trading book								
2017	**Up to 1 month RM'000**	**>1 – 3 months RM'000**	**>3 – 6 months RM'000**	**>6 – 12 months RM'000**	**>1 – 3 years RM'000**	**Over 3 years RM'000**	**Non-profit sensitive RM'000**	**Trading book RM'000**	**Total RM'000**
ASSETS									
Cash and short term funds	1,937,560	–	–	–	–	–	92,300	–	2,029,860
Securities purchased under resale agreements	–	968,712	609,921	–	–	–	9,346	–	1,587,979
Deposits and placements with banks and other financial institutions	–	414,627	30,000	–	–	–	2,583	–	447,210
Financial assets HFT	–	–	–	–	–	–	–	172,536	172,536
Financial investments AFS	200,000	15,004	115,363	120,262	600,774	2,309,485	33,605#	–	3,394,493
Financial investments HTM	10,000	1,672,002	218,123	223,468	278,465	1,401,427	17,249	–	3,820,734
Financing and advances:									
– Performing	29,557,681	625,940	344,756	57,303	2,478,619	9,384,282	181,909	–	42,630,490
– Impaired	–	–	–	–	–	–	71,304#	–	71,304
Other assets	–	–	–	–	–	–	90,934	–	90,934
Derivative assets	–	–	35	–	–	–	–	327,943	327,978
Statutory deposits with BNM	–	–	–	–	–	–	1,116,200	–	1,116,200
Deferred tax assets	–	–	–	–	–	–	16,513	–	16,513
Property, plant and equipment	–	–	–	–	–	–	6,193	–	6,193
Intangible assets	–	–	–	–	–	–	5,039	–	5,039
TOTAL ASSETS	31,705,241	3,696,285	1,318,198	401,033	3,357,858	13,095,194	1,643,175	500,479	55,717,463

Included impairment loss.

38 FINANCIAL RISK MANAGEMENT (CONTINUED)

(d) Profit rate risk (continued)

The table below summarises the Bank's exposure to profit rate risk. The carrying amount of assets and liabilities (includes non–financial instruments) are categorised by the earlier of contractual re-pricing or maturity dates: (continued):

2017	Non-trading book: Up to 1 month RM'000	>1 – 3 months RM'000	>3 – 6 months RM'000	>6 – 12 months RM'000	>1 – 3 years RM'000	Over 3 years RM'000	Non-profit sensitive RM'000	Trading book RM'000	Total RM'000
LIABILITIES									
Deposits from customers	8,924,939	4,722,821	10,988,768	7,887,756	4,651	2,061	5,319,209	–	37,850,205
Deposits and placements of banks and other financial institutions	1,446,420	2,768,363	56,652	–	101,859	19,990	1,517	–	4,394,801
Investment account due to designated financial institutions	–	–	–	911,150	2,411,380	4,497,775	282,393	–	8,102,698
Obligations on securities sold under repurchase agreements	603,909	–	–	–	–	–	254	–	604,163
Bills and acceptances payable	–	–	–	–	–	–	9,216	–	9,216
Derivative liabilities	–	–	55	3,217	–	–	–	324,451	327,723
Subordinated obligations	–	–	–	–	500,000	250,000	5,393	–	755,393
Other liabilities	–	–	–	–	–	–	345,792	–	345,792
Provision for tax and zakat	–	–	–	–	–	–	15,623	–	15,623
TOTAL LIABILITIES	10,975,268	7,491,184	11,045,475	8,802,123	3,017,890	4,769,826	5,979,397	324,451	52,405,614
TOTAL EQUITY	–	–	–	–	–	–	3,311,849	–	3,311,849
TOTAL LIABILITIES AND EQUITY	10,975,268	7,491,184	11,045,475	8,802,123	3,017,890	4,769,826	9,291,246	324,451	55,717,463
On-balance sheet profit sensitivity gap	20,729,973	(3,794,899)	(9,727,277)	(8,401,090)	339,968	8,325,368			
Off-balance sheet profit sensitivity gap	–	(220,000)	95,000	(650,000)	(425,000)	–			
TOTAL PROFIT-SENSITIVITY GAP	20,729,973	(4,014,899)	(9,632,277)	(9,051,090)	(85,032)	8,325,368			

38 FINANCIAL RISK MANAGEMENT (CONTINUED)

(d) Profit rate risk (continued)

The table below summarises the Bank's exposure to profit rate risk. The carrying amount of assets and liabilities (includes non–financial instruments) are categorised by the earlier of contractual re-pricing or maturity dates (continued):

	Non-trading book								
2016	**Up to 1 month RM'000**	**>1 – 3 months RM'000**	**>3 – 6 months RM'000**	**>6 – 12 months RM'000**	**>1 – 3 years RM'000**	**Over 3 years RM'000**	**Non-profit sensitive RM'000**	**Trading book RM'000**	**Total RM'000**
ASSETS									
Cash and short term funds	3,414,852	–	–	–	–	–	21,387	–	3,436,239
Securities purchased under resale agreements	665,451	489,273	1,187,178	–	–	–	12,048	–	2,353,950
Deposits and placements with banks and other financial institutions	–	220,632	–	315,738	–	–	771	–	537,141
Financial assets HFT	–	–	–	–	–	–	–	10,177	10,177
Financial investments AFS	–	–	40,001	283,305	384,067	2,719,718	32,556#	–	3,459,647
Financial investments HTM	25,000	1,039,234	50,033	56,224	596,555	1,033,314	19,763	–	2,820,123
Financing and advances:									
– Performing	22,469,539	525,572	336,374	49,219	623,488	9,522,874	173,793	–	33,700,859
– Impaired	–	–	–	–	–	–	140,707#	–	140,707
Other assets	–	–	–	–	–	–	171,730	–	171,730
Derivative assets	–	–	–	–	899	–	–	401,864	402,763
Statutory deposits with BNM	–	–	–	–	–	–	1,051,050	–	1,051,050
Deferred tax assets	–	–	–	–	–	–	20,929	–	20,929
Property, plant and equipment	–	–	–	–	–	–	6,576	–	6,576
Intangible assets	–	–	–	–	–	–	4,750	–	4,750
TOTAL ASSETS	**26,574,842**	**2,274,711**	**1,613,586**	**704,486**	**1,605,009**	**13,275,906**	**1,656,060**	**412,041**	**48,116,641**

Included impairment loss.

38 FINANCIAL RISK MANAGEMENT (CONTINUED)

(d) Profit rate risk (continued)

The table below summarises the Bank's exposure to profit rate risk. The carrying amount of assets and liabilities (includes non-financial instruments) are categorised by the earlier of contractual re-pricing or maturity dates (continued):

	Non-trading book								
2016	**Up to 1 month RM'000**	**>1 – 3 months RM'000**	**>3 – 6 months RM'000**	**>6 – 12 months RM'000**	**>1 – 3 years RM'000**	**Over 3 years RM'000**	**Non-profit sensitive RM'000**	**Trading book RM'000**	**Total RM'000**
LIABILITIES									
Deposits from customers	11,279,431	6,414,917	5,135,151	3,932,822	44,092	432	2,613,083	–	29,419,928
Deposits and placements of banks and other financial institutions	2,812,328	2,640,632	49,337	315,738	400,000	160,874	51,285	–	6,430,194
Investment account due to designated financial institutions	5,662	–	5,839	417,123	1,102,815	4,806,007	285,025	–	6,622,471
Bills and acceptances payable	–	–	–	–	–	–	9,050	–	9,050
Derivative liabilities	–	–	–	678	7,525	666	–	391,943	400,812
Recourse obligation on financing sold to Cagamas	–	–	–	801,342	–	–	13,901	–	815,243
Subordinated obligations	–	–	–	–	–	500,000	3,187	–	503,187
Other liabilities	–	–	–	–	–	–	957,863	–	957,863
Provision for tax and zakat	–	–	–	–	–	–	29,451	–	29,451
TOTAL LIABILITIES	14,097,421	9,055,549	5,190,327	5,467,703	1,554,432	5,467,979	3,962,845	391,943	45,188,199
TOTAL EQUITY	–	–	–	–	–	–	2,928,442	–	2,928,442
TOTAL LIABILITIES AND EQUITY	14,097,421	9,055,549	5,190,327	5,467,703	1,554,432	5,467,979	6,891,287	391,943	48,116,641
On-balance sheet profit sensitivity gap	12,477,421	(6,780,838)	(3,576,741)	(4,763,217)	50,577	7,807,928			
Off-balance sheet profit sensitivity gap	–	–	–	(225,000)	(710,000)	(90,000)			
TOTAL PROFIT-SENSITIVITY GAP	12,477,421	(6,780,838)	(3,576,741)	(4,988,217)	(659,423)	7,717,928			

38 FINANCIAL RISK MANAGEMENT (CONTINUED)

(e) Liquidity risk

Liquidity obligations arise from withdrawals of deposits, repayments of purchased funds upon maturity, extensions of credit and working capital needs.

The Bank has adopted the BNM's liquidity standard on Liquidity Coverage Ratio, to ensure maintenance of adequate stock of unencumbered high-quality liquid assets to survive the liquidity needs for 30 calendar day under liquidity stress condition. The Bank continues to report Net Stable Funding Ratio under the Basel III observation reporting to BNM.

The Bank seeks to project, monitor and manage its liquidity needs under normal as well as adverse circumstances.

The table below analyses the carrying amount of assets and liabilities (includes non-financial instruments) based on the remaining contractual maturity:

2017	Up to 1 week RM'000	1 week to 1 month RM'000	1 to 3 months RM'000	3 to 6 months RM'000	6 to 12 months RM'000	Over 1 year RM'000	No specific maturity RM'000	Total RM'000
ASSETS								
Cash and short term funds	1,757,412	272,448	–	–	–	–	–	2,029,860
Securities purchased under resale agreements	–	–	975,560	612,419	–	–	–	1,587,979
Deposits and placements with banks and other financial institutions	–	–	417,106	30,104	–	–	–	447,210
Financial assets HFT	–	–	–	–	–	172,536	–	172,536
Financial investments AFS	–	–	15,004	115,581	121,694	2,941,594	200,620	3,394,493
Financial investments HTM	10,000	–	1,672,002	223,053	225,335	1,690,344	–	3,820,734
Financing and advances	698,661	3,239,159	627,124	1,950,488	1,198,708	34,987,654	–	42,701,794
Other assets	1	7,808	–	–	–	–	83,125	90,934
Derivative assets	1,571	15,995	73,762	95,894	54,341	86,415	–	327,978
Statutory deposits with BNM	–	–	–	–	–	–	1,116,200	1,116,200
Deferred tax assets	–	–	–	–	–	–	16,513	16,513
Property, plant and equipment	–	–	–	–	–	–	6,193	6,193
Intangible assets	–	–	–	–	–	–	5,039	5,039
TOTAL ASSETS	**2,467,645**	**3,535,410**	**3,780,558**	**3,027,539**	**1,600,078**	**39,878,543**	**1,427,690**	**55,717,463**

38 FINANCIAL RISK MANAGEMENT (CONTINUED)

(e) Liquidity risk (continued)

The table below analyses the carrying amount of assets and liabilities (includes non-financial instruments) based on the remaining contractual maturity (continued):

2017	Up to 1 week RM'000	1 week to 1 month RM'000	1 to 3 months RM'000	3 to 6 months RM'000	6 to 12 months RM'000	Over 1 year RM'000	No specific maturity RM'000	Total RM'000
LIABILITIES								
Deposits from customers	9,758,640	4,126,733	4,795,720	11,195,747	7,966,481	6,884	–	37,850,205
Deposits and placements of banks and other financial institutions	98,613	1,348,628	2,768,375	56,760	–	122,425	–	4,394,801
Investment account due to designated financial institutions	–	–	–	–	937,147	7,165,551	–	8,102,698
Obligations on securities sold under repurchase agreements	604,163	–	–	–	–	–	–	604,163
Bills and acceptances payable	9,216	–	–	–	–	–	–	9,216
Derivative liabilities	1,112	14,039	73,648	95,343	57,120	86,461	–	327,723
Subordinated obligations	–	–	–	5,393	–	750,000	–	755,393
Other liabilities	206,792	29,313	26,460	–	19,425	–	63,802	345,792
Provision for tax and zakat	–	–	–	–	–	–	15,623	15,623
TOTAL LIABILITIES	10,678,536	5,518,713	7,664,203	11,353,243	8,980,173	8,131,321	79,425	52,405,614
TOTAL EQUITY	–	–	–	–	–	–	3,311,849	3,311,849
TOTAL LIABILITIES AND EQUITY	10,678,536	5,518,713	7,664,203	11,353,243	8,980,173	8,131,321	3,391,274	55,717,463

38 FINANCIAL RISK MANAGEMENT (CONTINUED)

(e) Liquidity risk (continued)

The table below analyses the carrying amount of assets and liabilities (includes non–financial instruments) based on the remaining contractual maturity (continued):

2016	Up to 1 week RM'000	1 week to 1 month RM'000	1 to 3 months RM'000	3 to 6 months RM'000	6 to 12 months RM'000	Over 1 year RM'000	No specific maturity RM'000	Total RM'000
ASSETS								
Cash and short term funds	1,333,971	2,102,268	–	–	–	–	–	3,436,239
Securities purchased under resale agreements	670,558	–	490,701	1,192,691	–	–	–	2,353,950
Deposits and placements with banks and other financial institutions	–	–	221,403	–	315,738	–	–	537,141
Financial assets HFT	–	–	–	83	–	10,094	–	10,177
Financial investments AFS	2,215	9,774	10,737	49,212	283,305	2,903,785	200,619	3,459,647
Financial investments HTM	26,387	6,537	1,047,216	53,889	56,224	1,629,870	–	2,820,123
Financing and advances	779,786	1,303,962	527,374	465,980	492,250	30,272,214	–	33,841,566
Other assets	105,825	8,896	–	–	–	–	57,009	171,730
Derivative assets	14,880	12,466	71,771	102,033	125,065	76,548	–	402,763
Statutory deposits with BNM	–	–	–	–	–	–	1,051,050	1,051,050
Deferred tax assets	–	–	–	–	–	–	20,929	20,929
Property, plant and equipment	–	–	–	–	–	–	6,576	6,576
Intangible assets	–	–	–	–	–	–	4,750	4,750
TOTAL ASSETS	2,933,622	3,443,903	2,369,202	1,863,888	1,272,582	34,892,511	1,340,933	48,116,641
LIABILITIES								
Deposits from customers	7,603,799	6,140,298	6,491,690	5,185,878	3,953,480	44,783	–	29,419,928
Deposits and placements of banks and other financial institutions	403,232	2,406,145	2,631,449	49,396	315,738	624,234	–	6,430,194
Investment account due to designated financial institutions	–	6,026	–	6,214	475,786	6,134,445	–	6,622,471
Bills and acceptances payable	9,050	–	–	–	–	–	–	9,050
Derivative liabilities	6,498	14,330	71,263	101,069	125,367	82,285	–	400,812
Recourse obligation on financing sold to Cagamas	–	–	–	–	815,243	–	–	815,243
Subordinated obligations	–	–	–	–	–	503,187	–	503,187
Other liabilities	766,026	12,311	16,652	–	19,070	–	143,804	957,863
Provision for tax and zakat	–	–	–	–	–	–	29,451	29,451
TOTAL LIABILITIES	8,788,605	8,579,110	9,211,054	5,342,557	5,704,684	7,388,934	173,255	45,188,199
TOTAL EQUITY	–	–	–	–	–	–	2,928,442	2,928,442
TOTAL LIABILITIES AND EQUITY	8,788,605	8,579,110	9,211,054	5,342,557	5,704,684	7,388,934	3,101,697	48,116,641

38 FINANCIAL RISK MANAGEMENT (CONTINUED)

(e) Liquidity risk (continued)

The following table presents the cash outflows for the Bank's financial liabilities by remaining contractual maturities on an undiscounted basis. The balances in the table below will not agree to the balances reported in the statement of financial position as the table incorporates all contractual cash flows, on an undiscounted basis, relating to both principal and profit payments.

2017	Up to 1 month RM'000	1 to 6 months RM'000	6 to 12 months RM'000	1 to 3 years RM'000	3 to 5 years RM'000	Over 5 years RM'000	Total RM'000
LIABILITIES							
Deposits from customers	**13,896,522**	**16,185,088**	**8,181,978**	**5,080**	**2,501**	**–**	**38,271,169**
Deposits and placements of banks and other financial institutions	**1,450,382**	**2,840,958**	**–**	**130,188**	**19,906**	**–**	**4,441,434**
Investment account due to designated financial institutions	**–**	**–**	**970,164**	**2,870,324**	**509,259**	**5,333,370**	**9,683,117**
Obligations on securities sold under repurchase agreements	**604,265**	**–**	**–**	**–**	**–**	**–**	**604,265**
Bills and acceptances payable	**9,216**	**–**	**–**	**–**	**–**	**–**	**9,216**
Derivative liabilities:							
– Gross settled derivatives:							
– Inflow	**(253,028)**	**(2,342,420)**	**(1,060,062)**	**(389,394)**	**(345,590)**	**(527,558)**	**(4,918,052)**
– Outflow	**268,389**	**2,525,659**	**1,133,357**	**460,683**	**406,511**	**579,548**	**5,374,147**
– Net settled derivatives	**61**	**969**	**1,675**	**(3,257)**	**(597)**	**–**	**(1,149)**
Subordinated obligations	**–**	**18,475**	**18,475**	**536,775**	**268,300**	**–**	**842,025**
Other financial liabilities	**236,105**	**26,461**	**19,425**	**–**	**–**	**–**	**281,991**
TOTAL FINANCIAL LIABILITIES	**16,211,912**	**19,255,190**	**9,265,012**	**3,610,399**	**860,290**	**5,385,360**	**54,588,163**
2016							
LIABILITIES							
Deposits from customers	13,759,676	11,807,473	4,069,069	46,096	515	–	29,682,829
Deposits and placements of banks and other financial institutions	2,793,494	2,685,562	372,177	500,175	167,961	–	6,519,369
Investment account due to designated financial institutions	–	–	–	702,975	3,475,892	3,798,980	7,977,847
Bills and acceptances payable	9,051	–	–	–	–	–	9,051
Derivative liabilities:							
– Gross settled derivatives:							
– Inflow	(392,366)	(1,954,500)	(1,314,325)	(258,381)	(238,054)	(605,126)	(4,762,752)
– Outflow	414,638	2,131,485	1,411,655	278,096	242,738	603,019	5,081,631
– Net settled derivatives	(91)	1,225	2,064	755	(4,246)	–	(293)
Recourse obligation on financing sold to Cagamas	23,773	139,393	668,841	–	–	–	832,007
Subordinated obligations	–	12,375	512,375	–	–	–	524,750
Other financial liabilities	778,337	16,652	19,070	–	–	–	814,059
TOTAL FINANCIAL LIABILITIES	17,386,512	14,839,665	5,740,926	1,269,716	3,644,806	3,796,873	46,678,498

38 FINANCIAL RISK MANAGEMENT (CONTINUED)

(e) Liquidity risk (continued)

The following table presents the contractual expiry by maturity of the Bank's commitments and contingencies:

	Less than 1 year RM'000	Over 1 year RM'000	Total RM'000
2017			
Transaction-related contingent items	**122,516**	**72,782**	**195,298**
Short term self-liquidating trade-related contingencies	**87,417**	**24,362**	**111,779**
Commitment to buy back the Islamic securities arising from the Sell and Buy Back ('SBBA') transaction	**–**	**629,085**	**629,085**
Irrevocable commitments to extend credit	**–**	**5,800,512**	**5,800,512**
Any commitments that are unconditionally cancelled at any time by the Bank without prior notice or that effectively provide for automatic cancellation due to deterioration in a borrower's creditworthiness	**1,405,272**	**1,108,570**	**2,513,842**
TOTAL COMMITMENTS AND CONTINGENCIES	**1,615,205**	**7,635,311**	**9,250,516**
2016			
Transaction-related contingent items	20,413	106,706	127,119
Short term self-liquidating trade-related contingencies	12,108	62,371	74,479
Obligations under underwriting agreements	–	76,000	76,000
Irrevocable commitments to extend credit	–	4,824,220	4,824,220
Any commitments that are unconditionally cancelled at any time by the Bank without prior notice or that effectively provide for automatic cancellation due to deterioration in a borrower's creditworthiness	3,693	2,179,381	2,183,074
TOTAL COMMITMENTS AND CONTINGENCIES	36,214	7,248,678	7,284,892

Undrawn financing and advances commitments are recognised at activation stage and include commitments which are unconditionally cancellable by the Bank. The Bank expects that not all of the contingent liabilities and undrawn financing commitments will be drawn before expiry.

38 FINANCIAL RISK MANAGEMENT (CONTINUED)

(f) Credit risk

(i) Maximum exposure to credit risk

The maximum exposure to credit risk at the statement of financial position is the amounts on the statement of financial position as well as off-balance sheet financial instruments, without taking into account of any collateral held or other credit enhancements. For contingent liabilities, the maximum exposure to credit risk is the maximum amount that the Bank would have to pay if the obligations of the instruments issued are called upon. For credit commitments, the maximum exposure to credit risk is the full amount of the undrawn credit facilities granted to customers. The table below shows the maximum exposure to credit risk for the Bank:

	2017 RM'000	2016 RM'000
Credit risk exposure relating to on-balance sheet assets:		
Short term funds (exclude cash in hand)	**2,009,202**	3,427,875
Securities purchased under resale agreements	**1,587,979**	2,353,950
Deposits and placements with banks and other financial institutions	**447,210**	537,141
Financial assets and investments portfolios (exclude shares and perpetual sukuk):		
– HFT	**172,536**	10,177
– AFS	**3,193,873**	3,259,028
– HTM	**3,820,734**	2,820,123
Financing and advances	**42,701,794**	33,841,566
Other financial assets	**7,617**	114,720
Derivative assets	**327,978**	402,763
	54,268,923	46,767,343
Credit risk exposure relating to off-balance sheet assets:		
Commitments and contingencies	**9,250,516**	7,284,892
Total maximum credit risk exposure	**63,519,439**	54,052,235

38 FINANCIAL RISK MANAGEMENT (CONTINUED)

(f) Credit risk (continued)

(ii) Collaterals

The main types of collateral obtained by the Bank are as follows:

(a) Fixed deposits, Commodity Murabahah Deposit-i, negotiable instrument of deposits, Islamic negotiable instrument of deposits, foreign currency deposits and cash deposits/margins

(b) Land and/or buildings

(c) Vessels and automobiles

(d) Quoted shares, unit trusts, government bonds and securities and private debt securities

(e) Other tangible business assets, such as inventory and equipment

The Bank also accepts non-tangible securities as support, such as guarantees from individuals, corporates and institutions, bank guarantees, debentures, assignment of contract proceeds, which are subject to internal guidelines on eligibility.

The financial effect of collateral (quantification to the extent to which collateral and other credit enhancements mitigate credit risk) held for financing and advances balances as at 31 December 2017 for the Bank are 66.7% (2016: 68.9%) respectively. The financial effect of collateral held for the remaining on-balance sheet assets are insignificant.

(iii) Credit quality

The Bank assesses credit quality of financing and advances using internal rating techniques tailored to the various categories of products and counterparties. These techniques have been developed internally and combine statistical analysis with credit officer's judgement.

Credit quality description is summarised as follows:

Credit Quality	Description
– Good	Exposures exhibit strong capacity to meet financial commitments with no cause of concern to the Bank
– Fair	Exposures exhibit fairly acceptable capacity to meet financial commitments and may require varying degrees of concern to the Bank
– No Rating	Counterparties which do not satisfy the criteria to be rated based on internal credit grading system

The credit quality of financial assets other than financing and advances are determined based on the ratings of counterparties as defined by Moody's or equivalent ratings of other international rating agencies as defined below:

– AAA to AA3
– A1 to A3
– Baa1 to Baa3
– P1 to P3

38 FINANCIAL RISK MANAGEMENT (CONTINUED)

(f) Credit risk (continued)

(iii) Credit quality (continued)

(a) Financing and advances

Financing and advances are summarised as follows:

	2017 RM'000	2016 RM'000
Neither past due nor impaired	**39,079,609**	29,174,659
Past due but not impaired	**3,550,881**	4,526,200
Individually impaired	**343,961**	393,096
Gross financing and advances	**42,974,451**	34,093,955
Less: Individual impairment allowance	**(42,612)**	(15,864)
Collective impairment allowance	**(230,045)**	(236,525)
Net financing and advances	**42,701,794**	33,841,566

(i) Financing and advances neither past due nor impaired

Analysis of financing and advances that are neither past due nor impaired analysed based on the Bank's internal credit grading system is as follows:

	2017 RM'000	2016 RM'000
Good	**17,998,549**	15,400,194
Fair	**792,436**	123,738
No Rating	**20,288,624**	13,650,727
Neither past due nor impaired	**39,079,609**	29,174,659

Financing and advances classified as non-rated mainly comprise financing under the Standardised Approach for credit risk.

38 FINANCIAL RISK MANAGEMENT (CONTINUED)

(f) Credit risk (continued)

(iii) Credit quality (continued)

(a) Financing and advances (continued)

(ii) Financing and advances past due but not impaired

Analysis of ageing of financing and advances that are past due but not impaired is as follows:

	2017 RM'000	2016 RM'000
Past due up to 30 days	**3,072,249**	3,820,928
Past due 31 to 60 days	**372,076**	536,144
Past due 61 to 90 days	**106,556**	169,128
Past due but not impaired	**3,550,881**	4,526,200

(iii) Impaired financing and advances

Financing and advances that are individually determined to be impaired are as follows:

	2017 RM'000	2016 RM'000
Individually impaired financing	**343,961**	393,096

38 FINANCIAL RISK MANAGEMENT (CONTINUED)

(f) Credit risk (continued)

(iii) Credit quality (continued)

(b) Short term funds, deposits and placements with banks and other financial institutions, securities purchased under resale agreements, financial assets and investments portfolios, other financial assets and derivative assets of the Bank are summarised as follows:

	Short term funds and deposits and placements with banks and other financial institutions RM'000	Securities purchased under resale agreements RM'000	Financial assets HFT RM'000	Financial investments AFS RM'000	Financial investments HTM RM'000	Other financial assets RM'000	Derivative assets RM'000
2017							
Neither past due nor impaired	**2,456,412**	**1,587,979**	**172,536**	**3,193,873**	**3,820,734**	**7,617**	**327,978**
2016							
Neither past due nor impaired	3,965,016	2,353,950	10,177	3,259,028	2,820,123	114,720	402,763

38 FINANCIAL RISK MANAGEMENT (CONTINUED)

(f) Credit risk (continued)

(iii) Credit quality (continued)

(c) Analysis of short term funds, deposits and placements with banks and other financial institutions, securities purchased under resale agreements, financial assets and investments portfolios, other financial assets and derivative assets of the Bank that are neither past due nor impaired by rating agency definition are as follows:

	Short term funds and deposits and placements with banks and other financial institutions RM'000	Securities purchased under resale agreements RM'000	Financial assets HFT RM'000	Financial investments AFS RM'000	Financial investments HTM RM'000	Other financial assets RM'000	Derivative assets RM'000
2017							
AAA to AA3	14,641	1,587,979	–	1,237,955	141,833	–	324,225
A1 to A3	102,717	–	–	20,352	–	–	–
P1 to P3	414,790	–	–	–	–	–	–
Non-rated of which:	1,924,264	–	172,536	1,935,566	3,678,901	7,617	3,753
– Malaysian Government Investment Issues	–	–	172,536	648,592	335,325	–	–
– Bank Negara Malaysia	1,400,849	–	–	–	–	–	–
– Private debt securities	–	–	–	1,277,571	1,473,702	–	–
– Khazanah bonds	–	–	–	9,403	21,799	–	–
– Negotiable Islamic debt certificates	–	–	–	–	1,838,090	–	–
– Others	523,415	–	–	–	9,985	7,617	3,753
	2,456,412	1,587,979	172,536	3,193,873	3,820,734	7,617	327,978

38 FINANCIAL RISK MANAGEMENT (CONTINUED)

(f) Credit risk (continued)

(iii) Credit quality (continued)

(c) Analysis of short term funds, deposits and placements with banks and other financial institutions, securities purchased under resale agreements, financial assets and investments portfolios, other financial assets and derivative assets of the Bank that are neither past due nor impaired by rating agency definition are as follows:

	Short term funds and deposits and placements with banks and other financial institutions RM'000	Securities purchased under resale agreements RM'000	Financial assets HFT RM'000	Financial investments AFS RM'000	Financial investments HTM RM'000	Other financial assets RM'000	Derivative assets RM'000
2016							
AAA to AA3	356,370	2,353,950	–	1,343,937	301,722	–	68,133
A1 to A3	–	–	–	149,447	–	–	–
Non-rated of which:	3,608,646	–	10,177	1,765,644	2,518,401	114,720	334,630
– Malaysian Government Investment Issues	–	–	10,177	691,196	402,619	–	–
– Bank Negara Malaysia	3,071,576	–	–	–	–	–	–
– Private debt securities	–	–	–	1,065,453	309,289	–	–
– Khazanah bonds	–	–	–	8,995	20,872	–	–
– Negotiable Islamic debt certificates	–	–	–	–	895,234	–	–
– Others	537,070	–	–	–	890,387	114,720	334,630
	3,965,016	2,353,950	10,177	3,259,028	2,820,123	114,720	402,763

38 FINANCIAL RISK MANAGEMENT (CONTINUED)

(f) Credit risk (continued)

Credit risk exposure analysed by industry in respect of the Bank's financial assets, including commitments and contingencies, are set out below:

2017	Short term funds and deposits and placements with banks and other financial institutions RM'000	Securities purchased under resale agreements RM'000	Financial assets HFT RM'000	Financial investments AFS@ RM'000	Financial investments HTM RM'000	Financing and advances# RM'000	Other financial assets* RM'000	Commitments and contingencies RM'000	Total RM'000
Agriculture, hunting, forestry and fishing	–	–	–	160,536	120,225	1,122,652	–	289,501	1,692,914
Mining and quarrying	–	–	–	–	–	245,208	426	2,658	248,292
Manufacturing	–	–	–	–	101,157	1,214,436	496	626,629	1,942,718
Electricity, gas and water	–	–	–	352,873	700,029	187,516	–	15,278	1,255,696
Construction	–	–	–	185,917	–	2,981,228	–	1,988,111	5,155,256
Real estate	–	–	–	131,165	126,287	1,274,802	–	–	1,532,254
Purchase of landed property	–	–	–	–	–	11,674,157	–	–	11,674,157
General commerce	–	–	–	10,016	132,766	1,265,732	2,539	309,342	1,720,395
Transport, storage and communication	–	–	–	724,976	107,137	4,870,770	–	195,491	5,898,374
Finance, insurance and business services	1,055,563	1,587,979	–	730,799	1,914,308	3,768,181	324,517	1,981,074	11,362,421
Government and government agencies	1,400,849	–	172,536	897,591	618,825	3,864,895	–	–	6,954,696
Others	–	–	–	–	–	10,462,262	7,617	3,842,432	14,312,311
	2,456,412	1,587,979	172,536	3,193,873	3,820,734	42,931,839	335,595	9,250,516	63,749,484

@ Exclude equity instrument and perpetual sukuk amounting to RM200,620,000.

Excludes collective impairment allowance amounting to RM230,045,000.

* Other financial assets include other assets amounting to RM7,617,000 and derivative assets amounting to RM327,978,000.

38 FINANCIAL RISK MANAGEMENT (CONTINUED)

(f) Credit risk (continued)

Credit risk exposure analysed by industry in respect of the Bank's financial assets, including commitments and contingencies, are set out below (continued):

2016	Short term funds and deposits and placements with banks and other financial institutions RM'000	Securities purchased under resale agreements RM'000	Financial assets HFT RM'000	Financial investments AFS@ RM'000	Financial investments HTM RM'000	Financing and advances# RM'000	Other financial assets* RM'000	Commitments and contingencies RM'000	Total RM'000
Agriculture, hunting, forestry and fishing	–	–	–	204,967	100,076	865,419	–	578,728	1,749,190
Mining and quarrying	–	–	–	–	–	370,536	–	6,697	377,233
Manufacturing	–	–	–	–	–	892,318	–	481,020	1,373,338
Electricity, gas and water	–	–	–	362,654	307,829	165,035	20,685	21,780	877,983
Construction	–	–	–	139,939	200,173	1,415,337	–	1,463,291	3,218,740
Real estate	–	–	–	171,068	29,619	896,869	–	–	1,097,556
Purchase of landed property	–	–	–	–	–	9,006,419	–	806,236	9,812,655
General commerce	–	–	–	–	–	904,735	–	370,530	1,275,265
Transport, storage and communication	–	–	–	355,753	76,636	4,162,512	–	253,258	4,848,159
Finance, insurance and business services	741,886	2,353,950	–	779,403	117,774	3,936,215	68,133	1,005,975	9,003,336
Government and government agencies	3,223,130	–	10,177	799,374	1,532,491	3,018,691	309,198	–	8,893,061
Consumption credit	–	–	–	–	–	–	–	461,216	461,216
Others	–	–	–	445,870	455,525	8,444,005	119,467	1,836,161	11,301,028
	3,965,016	2,353,950	10,177	3,259,028	2,820,123	34,078,091	517,483	7,284,892	54,288,760

@ Exclude equity instrument and perpetual sukuk amounting to RM200,619,000.

Excludes collective impairment allowance amounting to RM236,525,000.

* Other financial assets include other assets amounting to RM114,720,000 and derivative assets amounting to RM402,763,000.

38 FINANCIAL RISK MANAGEMENT (CONTINUED)

(g) Fair Value of Financial Instruments

The Bank analyses its financial instruments measured at fair value into three categories as described below:

Level 1: Quoted prices (unadjusted) in active markets for identical assets or liabilities.

Level 2: Quoted prices for identical or similar instruments in markets that are not active; and model-derived valuations in which inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly.

Level 3: Valuations derived from valuation techniques in which one or more significant inputs are not based on observable market data.

The table below analyses financial instruments carried at fair value analysed by level within the fair value hierarchy:

	Level 1 RM'000	Level 2 RM'000	Level 3 RM'000	Total RM'000
2017				
Financial assets				
Financial assets HFT:				
– Money market instruments	**–**	**172,536**	**–**	**172,536**
Financial investments AFS:	**–**	**3,193,873**	**200,620**	**3,394,493**
– Money market instruments	**–**	**688,480**	**–**	**688,480**
– Unquoted securities	**–**	**2,505,393**	**200,620**	**2,706,013**
Derivative assets	**–**	**327,978**	**–**	**327,978**
	–	**3,694,387**	**200,620**	**3,895,007**
Financial liabilities				
Derivative liabilities	**–**	**327,723**	**–**	**327,723**
2016				
Financial assets				
Financial assets HFT:				
– Money market instruments	–	10,177	–	10,177
Financial investments AFS:	–	3,259,028	200,619	3,459,647
– Money market instruments	–	754,927	–	754,927
– Unquoted securities	–	2,504,101	200,619	2,704,720
Derivative assets	–	402,763	–	402,763
	–	3,671,968	200,619	3,872,587
Financial liabilities				
Derivative liabilities	–	400,812	–	400,812

There were no transfers between Level 1 and 2 during the financial year.

38 FINANCIAL RISK MANAGEMENT (CONTINUED)

(g) Fair Value of Financial Instruments (continued)

(i) Valuation techniques

Financial instruments are classified as Level 1 if their value is observable in an active market. Such instruments are valued by reference to unadjusted quoted prices for identical assets or liabilities in active markets where the quoted prices is readily available, and the price represents actual and regularly occurring market transactions. An active market is one in which transactions occur with sufficient volume and frequency to provide pricing information on an on-going basis. This would include quoted securities and unit trusts.

Where fair value is determined using unquoted market prices in less active markets or quoted prices for similar assets and liabilities, such instruments are generally classified as Level 2. In cases where quoted prices are generally not available, the Bank then determines fair value based upon valuation techniques that use market parameters including but not limited to yield curves, volatilities and foreign exchange rates as inputs. The majority of valuation techniques employ only observable market data. These would include certain bonds, government bonds, corporate debt securities and derivatives.

Financial instruments are classified as Level 3 if their valuation incorporates significant inputs that are not based on observable market date (unobservable inputs). This category includes unquoted shares held for socio-economic reasons, non-transferable and non-tradable perpetual notes/sukuk, impaired securities and unquoted corporate financing stocks. For unquoted corporate financing stocks, discounted cash flow analysis has been performed to determine the recoverability of the instruments.

(ii) Reconciliation of fair value measurements in Level 3:

The following represents the changes in Level 3 instruments for the Bank:

Financial investments AFS

	2017 RM'000	2016 RM'000
Balance as at the beginning of the financial year	**200,619**	201,162
Profit recognised	**11,900**	11,900
Payment received	**(11,899)**	(11,894)
Impairment losses	**–**	(549)
Balance as at the end of the financial year	**200,620**	200,619

39 FAIR VALUES OF FINANCIAL ASSETS AND LIABILITIES

The fair value of each financial assets and liabilities presented on the statement of financial position of the Bank approximates the carrying amount as at the reporting date, except for the following:

	Carrying value RM'000	Fair value RM'000
2017		
Financial assets		
Financial investments HTM	**3,820,734**	**3,822,095**
Financing and advances	**42,701,794**	**42,707,274**
Financial liabilities		
Deposits from customers	**37,850,205**	**37,894,547**
Deposits and placements of banks and other financial institutions	**4,394,801**	**4,384,542**
Investment account due to designated financial institutions	**8,102,698**	**7,873,600**
Subordinated obligations	**755,393**	**759,318**
2016		
Financial assets		
Deposits and placements with banks and other financial institutions	537,141	585,012
Financial investments HTM	2,820,123	2,809,581
Financing and advances	33,841,566	35,217,671
Financial liabilities		
Deposits from customers	29,419,928	29,425,141
Deposits and placements of banks and other financial institutions	6,430,194	6,466,056
Investment account due to designated financial institutions	6,622,471	6,573,820
Recourse obligation on financing sold to Cagamas	815,243	821,965
Subordinated obligations	503,187	505,572

39 FAIR VALUES OF FINANCIAL ASSETS AND LIABILITIES (CONTINUED)

The following table analyses within the fair value hierarchy of the Bank's assets and liabilities not measured at fair value but for which fair value is disclosed:

	Level 1 RM'000	Level 2 RM'000	Level 3 RM'000	Total RM'000
2017				
Financial assets				
Financial investments HTM	**–**	**2,657,421**	**1,164,674**	**3,822,095**
Financing and advances	**–**	**42,707,274**	**–**	**42,707,274**
Financial liabilities				
Deposits from customers	**–**	**37,894,547**	**–**	**37,894,547**
Deposits and placements of banks and other financial institutions	**–**	**4,384,542**	**–**	**4,384,542**
Investment account due to designated financial institutions	**–**	**7,873,600**	**–**	**7,873,600**
Subordinated obligations	**–**	**759,318**	**–**	**759,318**
2016				
Financial assets				
Deposits and placements with banks and other financial institutions	–	585,012	–	585,012
Financial investments HTM	–	1,929,165	880,416	2,809,581
Financing and advances	–	35,217,671	–	35,217,671
Financial liabilities				
Deposits from customers	–	29,425,141	–	29,425,141
Deposits and placements of banks and other financial institutions	–	6,466,056	–	6,466,056
Investment account due to designated financial institutions	–	6,573,820	–	6,573,820
Recourse obligation on financing sold to Cagamas	–	821,965	–	821,965
Subordinated obligations	–	505,572	–	505,572

39 FAIR VALUES OF FINANCIAL ASSETS AND LIABILITIES (CONTINUED)

The fair values are based on the following methodologies and assumptions:

(i) Cash and short term funds and deposits and placements with financial institutions

For cash and short term funds and deposits and placements with financial institutions with maturities of less than six months, the carrying value is a reasonable estimate of fair value. For deposits and placements with maturities of six months and above, estimated fair value is based on discounted cash flows using prevailing money market profit rates at which similar deposits and placements would be made with financial institutions of similar credit risk and remaining period to maturity.

(ii) Securities purchased under resale agreements

The fair values of securities purchased under resale agreements with maturities of less than six months approximate the carrying values. For securities purchased under resale agreements with maturities of six months and above, the estimated fair values are based on discounted cash flows using prevailing market rates for the remaining term to maturity.

(iii) Financial assets HFT, financial investments HTM and AFS

The estimated fair value for financial assets HFT, financial investments HTM and AFS is based on quoted and observable market prices. Where there is no ready market in certain securities, fair values have been assessed by reference to market indicative yield or net tangible asset backing of the investee. Where discounted cash flow technique is used, the estimated future cash flows are discounted using the prevailing market rates for a similar instrument at the date of statement of financial position.

(iv) Financing and advances

For floating rate financing, the carrying value is generally a reasonable estimate of fair value.

For fixed rate financing, the fair value is estimated by discounting the estimated future cash flows using the prevailing market rates of financing with similar credit risk and maturities.

The fair values of impaired financing are represented by their carrying value, net of impairment allowance.

(v) Other assets and liabilities

The carrying value less any estimated impairment allowance for financial assets and liabilities included in 'other assets and liabilities' are assumed to approximate their fair values as these items are not materially sensitive to the shift in market profit rates.

(vi) Deposits from customers

For deposits from customers with maturities of less than six months, the carrying amounts are reasonable estimates of their fair values. For deposits with maturities of six months and above, fair values are estimated using discounted cash flows based on prevailing market rates for similar deposits from customers.

39 FAIR VALUES OF FINANCIAL ASSETS AND LIABILITIES (CONTINUED)

The fair values are based on the following methodologies and assumptions (continued):

(vii) Deposits and placements of banks and other financial institutions, investment account due to designated financial institutions, obligations on securities sold under repurchase agreements and bills and acceptances payable.

The estimated fair values of deposits and placements of banks and other financial institutions, investment account due to designated financial institutions, obligations on securities sold under repurchase agreements and bills and acceptances payable with maturities of less than six months approximate the carrying values. For the items with maturities of six months and above, the fair values are estimated based on discounted cash flows using prevailing money market profit rates with similar remaining period to maturity.

(viii) Recourse obligation on financing sold to Cagamas

For amounts due to Cagamas with maturities of less than one year, the carrying amounts are a reasonable estimate of their fair values. For amounts due to Cagamas with maturities of more than one year, fair value is estimated based on discounted cash flows using prevailing money market profit rates with similar remaining period to maturity.

(ix) Subordinated obligations

The estimated fair value of subordinated obligations is generally based on quoted and observable market prices at the date of statement of financial position.

(x) Credit related commitments and contingencies

The net fair value of these items was not calculated as estimated fair values are not readily ascertainable. These financial instruments generally relate to credit risks and attract fees in line with market prices for similar arrangements. They are not presently sold nor traded. The fair value may be represented by the present value of fees expected to be received, less associated costs.

(xi) Foreign exchange and profit rate related contracts

The fair values of foreign exchange and profit rate related contracts are the estimated amounts the Bank would receive to sell or pay to transfer the contracts at the date of statement of financial position.

40 CAPITAL ADEQUACY

BNM guidelines on capital adequacy requires the Bank to maintain an adequate level of capital to withstand any losses which may result from credit and other risks associated with financing operations. The capital adequacy ratio is computed based on the eligible capital in relation to the total risk weighted assets as determined by BNM.

The capital adequacy ratios of the Bank is as follows:

	2017 RM'000	2016 RM'000
Common Equity Tier I ('CET I') Capital/Tier I Capital		
Share capital	**1,273,424**	1,273,424
Retained profits	**1,787,323**	766,058
Statutory reserve	**–**	762,388
AFS reserve	**(15,929)**	(31,944)
	3,044,818	2,769,926
Less:		
Deferred tax assets	**(17,140)**	(25,748)
Intangible assets (include associated deferred tax liabilities)	**(4,412)**	–
Ageing Reserve and Liquidity Reserve*	**(4,296)**	(2,891)
Total CET I / Total Tier I Capital	**3,018,970**	2,741,287
Tier II Capital		
Subordinated obligations	**750,000**	500,000
Collective impairment allowance and regulatory reserve^	**343,212**	290,408
Total Tier II Capital	**1,093,212**	790,408
Total Capital	**4,112,182**	3,531,695
Capital ratios		
CET I Capital ratio	**10.376%**	10.868%
Tier I Capital ratio	**10.376%**	10.868%
Total Capital ratio	**14.134%**	14.002%

The breakdown of risk-weighted assets in the various categories of risk-weights are as follows:

	2017 RM'000	2016 RM'000
Credit risk-weighted assets	**34,726,152**	29,623,743
Credit risk-weighted assets absorbed by PSIA	**(7,269,199)**	(5,665,344)
Market risk-weighted assets	**240,688**	63,426
Operational risk-weighted assets	**1,397,487**	1,200,381
Total risk-weighted assets	**29,095,128**	25,222,206

40 CAPITAL ADEQUACY (CONTINUED)

In accordance with BNM's "Guidelines on the Recognition and Measurement of Profit Sharing Investment Account ('PSIA') as Risk Absorbent", the credit and market risks of the assets funded by the Restricted Profit Sharing Investment account ('RPSIA') which qualifies as risk absorbent are excluded from the risk-weighted capital ratio (RWCR) calculation. As at 31 December 2017, credit risks relating to RPSIA assets excluded from the RWCR calculation amounted to RM7,269,199,000 (2016: RM5,665,344,000).

^ Excludes collective impairment allowance attributable to financing and advances classified as impaired but not individually assessed for impairment pursuant to BNM's Guideline on "Classification and Impairment Provisions for Financing". Include the qualifying regulatory reserve under the Standardised Approach for non-impaired financing and advances of RM204,312,000 (2016: RM158,516,000).

* Pursuant to the Basel II Market Risk para 5.19 and 5.20 – Valuation Adjustments, the Capital Adequacy Framework (Basel II-RWA) calculation shall account for the ageing, liquidity and holding back adjustments on its trading portfolio.

	2017 RM'000	**2016 RM'000**
Risk-weighted assets by each major risk category are as follows:		
(i) Credit Risk		
0%	**–**	–
20%	**1,046,934**	856,154
35%	**2,257,303**	806,423
50%	**889,206**	867,392
75%	**6,301,341**	8,799,347
100%	**24,096,462**	18,138,791
150%	**134,906**	155,636
	34,726,152	29,623,743
Less: Credit risk-weighted assets absorbed by PSIA	**(7,269,199)**	(5,665,344)
(ii) Market Risk Capital Adequacy Framework	**240,688**	63,426
(iii) Basic Indicator Operational Risk Capital Charge	**1,397,487**	1,200,381
	29,095,128	25,222,206

41 SEGMENT REPORTING

Operating segments are reported in a manner consistent with the internal reporting provided to the chief operating decision-maker, who is the person or group that allocates resources to and assesses the performance of the operating segments of an entity. The Bank has determined RHB Bank's Group Management Committee as its chief operating decision-maker.

The business segment results are prepared based on the Bank's internal management reporting, which reflect the organisation's management structure. Internal allocation of costs has been used in preparing the segmental reporting.

The Bank's business segment can be organised into the following main segments reflecting the Bank's internal reporting structure:

(a) Wholesale Banking

(i) Corporate and Investment Banking

Corporate and Investment Banking caters to financing and managing relationship of corporate customers including public listed corporations and its related entities, multinational corporations, financial institutions, government and state owned entities as well as high net worth individual related to the above. The division also generates fee-based income from private debt securities issuances ('PDS'), financing restructuring and syndication as well as general and project advisory services.

(ii) Treasury

Treasury operation is involved in money market operation and securities trading on behalf of the Bank and also for the Bank's customers. The division also provides solutions to serve investment needs of the Bank and the Bank's customers.

(b) Business Banking

Business Banking caters to funding or lending needs of small and medium sized enterprises. The products and services offered to customers include term financing, revolving financing and hire purchase financing.

(c) Retail Banking

Retail Banking focuses on providing products and services to individual customers. The products and services offered to customers include term financing (house and shop house financing), Islamic automobile financing business with concentration on the financing of high demand and popular passenger motor vehicles, deposit portfolios (savings and current account), credit cards, remittance services, investment products (term deposit/investment account) and bancatakaful products.

41 SEGMENT REPORTING (CONTINUED)

	← Wholesale Banking →				
	Corporate and Investment Banking RM'000	Treasury RM'000	Business Banking RM'000	Retail Banking RM'000	Total RM'000
2017					
External revenue	894,189	449,995	152,300	1,012,025	2,508,509
Inter-segment revenue	(58,290)	519,730	(474)	(460,966)	–
Segment revenue	835,899	969,725	151,826	551,059	2,508,509
Depositors' payout	(626,735)	(783,539)	(38,767)	(190,539)	(1,639,580)
Net income	209,164	186,186	113,059	360,520	868,929
Operating overheads	(44,353)	(21,394)	(46,104)	(206,393)	(318,244)
Depreciation of property, plant and equipment	(353)	(80)	(814)	(1,344)	(2,591)
Amortisation of computer software	(305)	(427)	(212)	(902)	(1,846)
Allowance for impairment on financing and advances	1,159	–	(53,235)	(14,658)	(66,734)
Segmental results	165,312	164,285	12,694	137,223	479,514
Impairment losses written back on other assets					336
Profit before taxation and zakat					479,850
Zakat					(3,500)
Profit after zakat before taxation					476,350
Taxation					(108,958)
Net profit for the financial year					367,392

Note: Total segment revenue comprise of net profit income and other operating income.

41 SEGMENT REPORTING (CONTINUED)

	Wholesale Banking				
	Corporate and Investment Banking RM'000	Treasury RM'000	Business Banking RM'000	Retail Banking RM'000	Total RM'000
2017					
Segment assets	20,487,482	10,411,651	2,875,102	21,827,440	55,601,675
Unallocated assets					99,275
Deferred tax assets					16,513
Total assets					55,717,463
Segment liabilities	20,392,163	19,268,148	2,758,567	9,625,320	52,044,198
Unallocated liabilities					361,416
Total liabilities					52,405,614
Other segment items:					
Capital expenditure	544	–	599	2,868	4,011

41 SEGMENT REPORTING (CONTINUED)

	Wholesale Banking				
	Corporate and Investment Banking RM'000	Treasury RM'000	Business Banking RM'000	Retail Banking RM'000	Total RM'000
2016					
External revenue	781,774	440,380	110,557	905,793	2,238,504
Inter-segment revenue	(161,983)	546,168	22,775	(406,960)	–
Segment revenue	619,791	986,548	133,332	498,833	2,238,504
Depositors' payout	(422,431)	(854,078)	(40,770)	(166,777)	(1,484,056)
Net income	197,360	132,470	92,562	332,056	754,448
Operating overheads	(34,000)	(12,462)	(54,982)	(146,777)	(248,221)
Depreciation of property, plant and equipment	(21)	(17)	40	(1,753)	(1,751)
Amortisation of computer software	(127)	(598)	(140)	(1,237)	(2,102)
Allowance for impairment on financing and advances	(5,621)	–	(27,712)	(36,835)	(70,168)
Segmental results	157,591	119,393	9,768	145,454	432,206
Impairment losses made on other assets					(549)
Profit before taxation and zakat					431,657
Zakat					(3,500)
Profit after zakat before taxation					428,157
Taxation					(103,373)
Net profit for the financial year					324,784

Note: Total segment revenue comprise of net profit income and other operating income.

41 SEGMENT REPORTING (CONTINUED)

	Wholesale Banking				
	Corporate and Investment Banking RM'000	Treasury RM'000	Business Banking RM'000	Retail Banking RM'000	Total RM'000
2016					
Segment assets	16,372,436	11,935,707	2,257,270	17,174,445	47,739,858
Unallocated assets					355,854
Deferred tax assets					20,929
Total assets					48,116,641
Segment liabilities	13,323,951	22,332,000	2,516,061	6,028,874	44,200,886
Unallocated liabilities					987,313
Total liabilities					45,188,199
Other segment items:					
Capital expenditure	69	376	57	1,177	1,679

42 APPROVAL OF FINANCIAL STATEMENTS

The financial statements have been approved for issue in accordance with a resolution of the Board of Directors on 27 February 2018.

STATEMENT BY DIRECTORS

PURSUANT TO SECTION 251(2) OF THE COMPANIES ACT, 2016

We, Dato' Abd Rahman Dato' Md Khalid and Dato' Adissadikin Ali, being two of the Directors of RHB Islamic Bank Berhad, state that, in the opinion of the Directors, the financial statements set out on pages 53 to 150 are drawn up so as to give a true and fair view of the financial position of the Bank as at 31 December 2017 and financial performance of the Bank for the financial year ended on 31 December 2017 in accordance with the Malaysian Financial Reporting Standards, International Financial Reporting Standards and the requirements of the Companies Act, 2016.

Signed on behalf of the Board of Directors in accordance with a resolution of the Directors dated 27 February 2018.

DATO' ABD RAHMAN DATO' MD KHALID
DIRECTOR

DATO' ADISSADIKIN ALI
CHIEF EXECUTIVE OFFICER/MANAGING DIRECTOR

Kuala Lumpur

STATUTORY DECLARATION

PURSUANT TO SECTION 251(1) OF THE COMPANIES ACT, 2016

I, Khairul Hakeem Mohamed Sahari, the Officer primarily responsible for the financial management of RHB Islamic Bank Berhad, do solemnly and sincerely declare that the accompanying financial statements set out on pages 53 to 150 are, to the best of my knowledge and belief, correct and I make this solemn declaration conscientiously believing the same to be true and by virtue of the provisions of the Statutory Declaration Act, 1960.

KHAIRUL HAKEEM MOHAMED SAHARI

Subscribed and solemnly declared by the abovenamed Khairul Hakeem Mohamed Sahari at Kuala Lumpur in Malaysia on 27 February 2018.

COMMISSIONER FOR OATHS
Kuala Lumpur

INDEPENDENT AUDITORS' REPORT

TO THE MEMBER OF RHB ISLAMIC BANK BERHAD

REPORT ON THE AUDIT OF THE FINANCIAL STATEMENTS

Our opinion

In our opinion, the financial statements of RHB Islamic Bank Berhad ("the Bank") give a true and fair view of the financial position of the Bank as at 31 December 2017, and of its financial performance and its cash flows for the year then ended in accordance with Malaysian Financial Reporting Standards, International Financial Reporting Standards and the requirements of the Companies Act 2016 in Malaysia.

What we have audited

We have audited the financial statements of the Bank, which comprise the statement of financial position as at 31 December 2017 and the income statement, statement of comprehensive income, statement of changes in equity and statement of cash flows for the year then ended, and notes to the financial statements, including a summary of significant accounting policies, as set out on pages 53 to 150.

Basis for opinion

We conducted our audit in accordance with approved standards on auditing in Malaysia and International Standards on Auditing. Our responsibilities under those standards are further described in the "Auditors' responsibilities for the audit of the financial statements" section of our report.

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

Independence and other ethical responsibilities

We are independent of the Bank in accordance with the By-Laws (on Professional Ethics, Conduct and Practice) of the Malaysian Institute of Accountants ("By-Laws") and the International Ethics Standards Board for Accountants' Code of Ethics for Professional Accountants ("IESBA Code"), and we have fulfilled our other ethical responsibilities in accordance with the By-Laws and the IESBA Code.

Information other than the financial statements and auditors' report thereon

The Directors of the Bank are responsible for the other information. The other information comprises the Directors' Report which we obtained prior to the date of this auditors' report, and the 2017 Annual Report, which is expected to be made available to us after that date. Other information does not include the financial statements of the Bank and our auditors' report thereon.

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

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

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

REPORT ON THE AUDIT OF THE FINANCIAL STATEMENTS (CONTINUED)

Responsibilities of the Directors for the financial statements

The Directors of the Bank are responsible for the preparation of the financial statements of the Bank that give a true and fair view in accordance with Malaysian Financial Reporting Standards, International Financial Reporting Standards and the requirements of the Companies Act 2016 in Malaysia. The Directors are also responsible for such internal control as the directors determine is necessary to enable the preparation of financial statements of the Bank that are free from material misstatement, whether due to fraud or error.

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

Auditors' responsibilities for the audit of the financial statements

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

As part of an audit in accordance with approved standards on auditing in Malaysia and International Standards on Auditing, we exercise professional judgement and maintain professional scepticism throughout the audit. We also:

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

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

(c) Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the Directors.

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

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

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

OTHER MATTERS

This report is made solely to the member of the Bank, as a body, in accordance with Section 266 of the Companies Act, 2016 in Malaysia and for no other purpose. We do not assume responsibility to any other person for the content of this report.

PRICEWATERHOUSECOOPERS PLT
LLP0014401-LCA & AF 1146
Chartered Accountants

SOO HOO KHOON YEAN
02682/10/2019 J
Chartered Accountant

Kuala Lumpur
27 February 2018

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STATEMENT BY MANAGING DIRECTOR

In accordance with the requirements of Bank Negara Malaysia's Guideline on Capital Adequacy Framework for Islamic Banks (CAFIB) – Disclosure Requirements (Pillar 3), and on behalf of the Board of Directors and Senior Management of RHB Islamic Bank Berhad, I am pleased to provide an attestation that the Basel II Pillar 3 disclosures of RHB Islamic Bank Berhad for the year ended 31 December 2017 are accurate and complete.

DATO' ADISSADIKIN BIN ALI
Managing Director

BASEL II PILLAR 3 DISCLOSURES

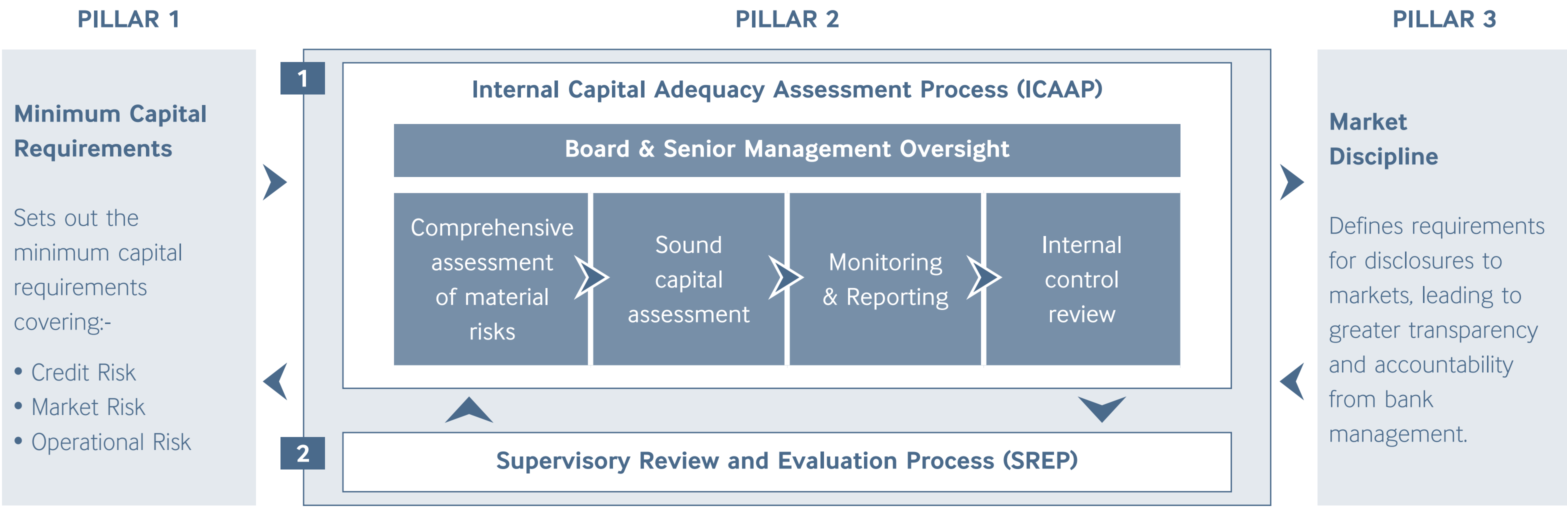
1.0 INTRODUCTION

This document describes RHB Islamic Bank Berhad's risk profile, risk management practices and capital adequacy position in accordance with the disclosure requirements as outlined in the Capital Adequacy Framework for Islamic Banks (CAFIB) – Disclosure Requirements (Pillar 3) issued by Bank Negara Malaysia (BNM's Pillar 3 Guidelines).

BNM's guidelines on Capital Adequacy Framework for Islamic Banks (Risk-Weighted Assets) provide and specify the approaches for quantifying the risk-weighted assets for credit risk, market risk and operational risk.

Basel II introduces a more risk-based approach to regulatory capital with a distinct charge for operational risk in addition to the existing credit and market risk capital charges. Basel II is designed to be a catalyst for more advanced risk management techniques, enterprise-wide culture of risk management and improved corporate governance and public disclosure.

The Basel II approach based on the three pillars can be diagrammatically depicted as below:



Pillar 1 provides guidelines for calculation of risk-weighted assets for credit risk, market risk and operational risk, and the minimum amount of regulatory capital that banks must hold against the risks they assume.

For the purpose of complying with regulatory requirements under Basel II Pillar 1, the approaches adopted by the Bank is as follows:

Entity	Credit Risk	Market Risk	Operational Risk
RHB Islamic Bank Berhad	Standardised Approach	Standardised Approach	Basic Indicator Approach

1.0 INTRODUCTION (CONTINUED)

Pillar 2 comprises two components as follows:

- Placing obligations on banks to develop an Internal Capital Adequacy Assessment Process, and setting capital targets that commensurate with the banking institution's risk profile and control environment; and
- Placing obligations on the supervisory authority to evaluate how well banking institutions are assessing their capital needs relative to their risks and to intervene, where appropriate.

Pillar 3 covers external communication of risk and capital information by banks. The purpose of the Pillar 3 disclosures is to complement the minimum capital requirements under Pillar 1 and the supervisory review process under Pillar 2 by encouraging market efficiency through a set of disclosure requirements that will allow market participants to assess information on banking institutions' capital structures, risk exposures, risk management processes, and hence, their overall capital adequacy.

Basis of Disclosure

The annual Pillar 3 disclosure report is published in accordance with BNM's Pillar 3 Guidelines. This disclosure report has been verified and approved internally in line with the RHB Banking Group: Basel II Pillar 3 Disclosure Policy.

Comparative Information

This document covers the qualitative and quantitative information for financial year ended 31 December 2017 with comparative quantitative information of the preceding financial year 2016.

Frequency of Disclosure

The qualitative disclosures contained herein are updated on an annual basis and more frequently, if there are significant changes in the interim reporting period. The disclosures on capital adequacy and structure are made on a quarterly basis and all other quantitative disclosures are made on a semi-annual basis in accordance to the Group's reporting period.

Medium and Location of Disclosure

RHB Islamic Bank Berhad's Pillar 3 disclosure report is made available under the Investor Relations section of RHB Banking Group's website at www.rhbgroup.com as a separate report in the Bank's Annual Report 2017, after the notes to the Financial Statements.

2.0 SCOPE OF APPLICATION

In this Pillar 3 document, RHB Islamic Bank Berhad's information is presented at entity level and is referred to as the "Bank". The Bank is a wholly owned subsidiary of RHB Bank Berhad as at 31 December 2017.

3.0 CAPITAL MANAGEMENT

The overall capital management objective is to manage capital prudently and to maintain a strong capital position to drive sustainable business growth and seek strategic opportunities to enhance shareholders' value, and be in line with its risk appetite. Capital adequacy is the extent to which capital resources on the Bank's balance sheet are sufficient to cover the business capital requirements now and in the foreseeable future. It also indicates the ability of the Bank to provide financing across the business cycles and in meeting any contingency without compromising the interest of the depositors and investors. The Bank aims to maintain a strong capital position to drive sustainable business growth through an optimal capital structure while meeting regulatory requirements.

With a comprehensive capital management, the Bank aims to have a sound capital management practice that is aligned to BNM's ICAAP requirements.

The management of capital involves capital strategy, capital planning and capital allocation/structuring/optimisation.

- **Capital Strategy**

  Capital strategy includes the determination of target capital under both normal and stressed market conditions and considers the business risk and strategic objectives, external credit ratings, and capital adequacy requirements. A comprehensive capital adequacy assessment is conducted at least annually to ensure that the target capital level is appropriate.

- **Capital Planning**

  Based on strategic direction and regulatory requirements, the Bank formulates a comprehensive and forward looking capital plan to:

  (i) support its overall risk profile and forecast the capital demand for material risks for which capital held is deemed appropriate and aligned with the Bank's risk appetite;

  (ii) provide adequate capital for business growth, changes in asset mix or to cover unanticipated losses.

  The capital plan describes the actions required to raise capital in a timely manner in both normal and stressed conditions as assumed in the stress scenarios. For capital planning purposes, capital adequacy is assessed in the multi-year financial projection under both normal and stressed scenarios, the objective of which is to ensure that the Bank maintains adequate capital on a forward-looking basis. The Bank also establishes a capital contingency funding plan that forms part of the capital plan. The capital plan, together with the analysis and proposed actions, are reviewed by the Group Chief Financial Officer and deliberated at the Group Capital and Risk Committee (GCRC) and for endorsement, and submitted to Islamic Risk Management Committee (IRMC), Board Risk Committee (BRC) and the Board for approval.

- **Capital Allocation/Structuring/Optimisation**

  The Bank determines the amount of capital allocated to each business line based on capital performance target and available funding. An efficient allocation of capital drives returns for the Bank's shareholders.

  Capital structuring affects the Bank through its impact on cash flow and cost of capital. The Bank adopts capital structuring that maximises value and minimises overall cost of capital. In order to achieve optimum capital structure, the Bank determines the levels, mix and structure of internal and regulatory capital in line with its current and planned levels of business activities, risk appetite and desired level of capital adequacy.

  The Bank optimises its capital by integrating risk-based capital into strategy and aligning this with performance measurement.

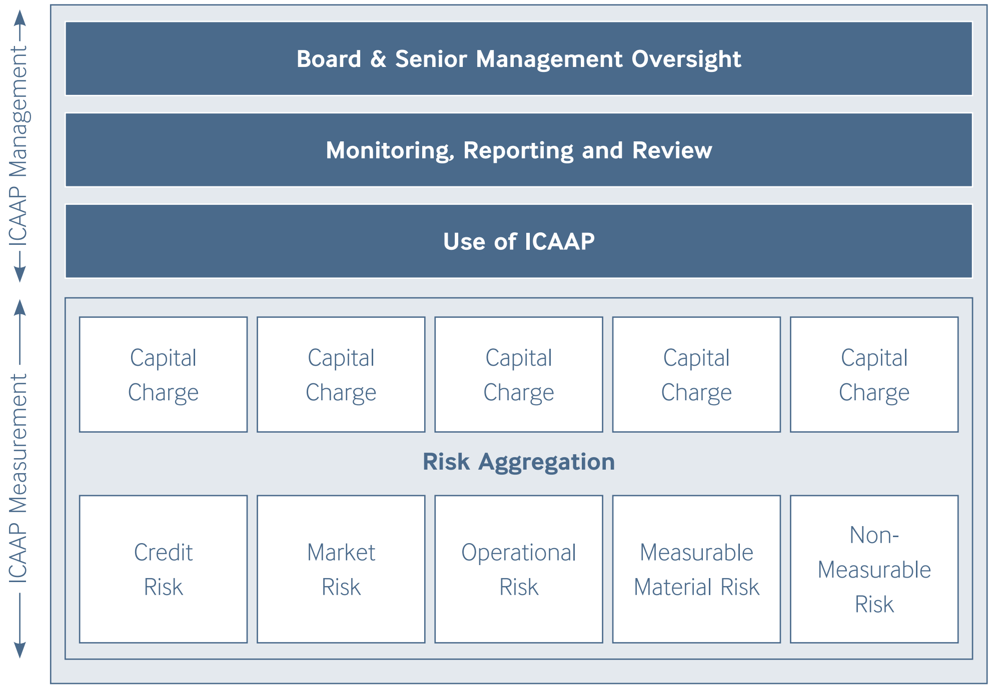
  The Bank also aims to achieve a balance between dividend pay-out and the need to retain earnings in order to be consistent with its capital strength and to support business expansion. The Board reviews the dividend pay-out recommendation on an annual basis.

3.0 CAPITAL MANAGEMENT (CONTINUED)

3.1 Internal Capital Adequacy Assessment Process (ICAAP)

In line with BNM's Guideline on ICAAP under the Capital Adequacy Framework for Islamic Banks (CAFIB) – Internal Capital Adequacy Assessment Process (Pillar 2), the Bank has implemented ICAAP with the objective to forge a strong alignment between risk and capital. Capital adequacy is assessed in relation to the Bank's risk profile, and strategies are in place to maintain appropriate capital levels.

The ICAAP Framework developed and adopted across the Bank summarises the key ICAAP requirements into two functional categories, namely; ICAAP Measurement and ICAAP Management as depicted below:



Key Requirements

- Establish rigorous corporate governance and senior management oversight.
- Establish risk-based strategy including defining and setting the Bank's appetite and tolerance for risk.
- Access and measure all material risks inherent in the Group's business.
- Review, monitor, control and report on all material risks.
- Demonstrate that ICAAP forms an integral part of day-to-day management process and decision making culture of the Group.
- Relate capital to level of risk and ensure capital adequacy using scenario analysis and stress testing methods.

3.2 Basel III Implementation

The implementation of Basel III for capital components by BNM in Malaysia has commenced with effect from 1 January 2013. Under the Basel III rules, banking institutions are required to strengthen the quality of their capital by maintaining higher minimum capital requirements and holding capital buffers namely the capital conservation buffer and the countercyclical capital buffer. However, the requirements are subject to a series of transitional arrangements with a gradual phase-in commencing 2013.

The Bank has implemented BNM's liquidity standards on Liquidity Coverage Ratio (LCR) effective from 1 June 2015 after reporting the LCR under observation since June 2012. BNM has adopted the phased-in arrangement for Malaysian banking institutions to comply with the minimum requirement of 60% in 2015 with incremental of 10% each year thereafter until 100% from 1 January 2019 onwards. The Bank continues to report on Net Stable Funding Ratio (NSFR) under observation. The result produced during the observation period facilitates the Bank's strategy in managing the appropriate balance sheet structure for achieving optimal NSFR.

BASEL II PILLAR 3 DISCLOSURES

3.0 CAPITAL MANAGEMENT (CONTINUED)

3.3 Capital Adequacy Ratios

BNM's Guideline on Capital Adequacy Framework for Islamic Banks (Capital Components) sets out the general requirements concerning regulatory capital adequacy and the components of eligible regulatory capital. As of 1 January 2015, banking institutions are required to maintain, at all times, the following minimum capital adequacy ratios:

Calendar Year	Common Equity Tier I (CET I) Capital Ratio	Tier I Capital Ratio	Total Capital Ratio
2015 onwards	4.5%	6.0%	8.0%

In addition, the Bank is required to maintain additional capital buffers in the form of CET I capital above the minimum CET I, Tier I and total capital ratios set out above. The capital buffers shall comprise of capital conservation buffer (CCB) and countercyclical capital buffer (CCyB). The CCB is intended to enable the banking system to withstand future periods of stress and will be phased-in as follows:

Calendar Year	CCB
2016	0.625%
2017	1.250%
2018	1.875%
2019 onwards	2.500%

CCyB is determined based on the weighted average of the prevailing CCyB rates applied in the jurisdictions in which the Bank has credit exposures. This buffer is intended to protect the banking sector as a whole from the build-up of systemic risk during an economic upswing when aggregate credit growth tends to be excessive. Application of CCyB above the minimum capital ratios is in the range of 0.0% to 2.5%. BNM will communicate any decision on the CCyB rate by up to 12 months before the date from which the rate applies.

3.0 CAPITAL MANAGEMENT (CONTINUED)

3.3 Capital Adequacy Ratios (continued)

The capital ratios of the Bank as at 31 December 2017 and 31 December 2016 are:

Table 1: Capital Adequacy Ratios

	RHB Islamic Bank	
	2017	**2016**
Before Proposed Dividends:		
Common Equity Tier I Capital Ratio	**10.376%**	10.868%
Tier I Capital Ratio	**10.376%**	10.868%
Total Capital Ratio	**14.134%**	14.002%
After Proposed Dividends:		
Common Equity Tier I Capital Ratio	**10.376%**	10.868%
Tier I Capital Ratio	**10.376%**	10.868%
Total Capital Ratio	**14.134%**	14.002%

The above capital ratios are above the minimum level required by BNM.

The following table shows the breakdown of RWA by risk types as at 31 December 2017 and 31 December 2016:

Table 2: Risk-Weighted Assets ('RWA') by Risk Types

	RHB Islamic Bank	
Risk Types	**2017 RM'000**	**2016 RM'000**
Credit RWA	**34,726,152**	29,623,743
Credit RWA Absorbed by Profit Sharing Investment Account ('PSIA')	**(7,269,199)**	(5,665,344)
Market RWA	**240,688**	63,426
Operational RWA	**1,397,487**	1,200,381
Total RWA	**29,095,128**	**25,222,206**

3.0 CAPITAL MANAGEMENT (CONTINUED)

3.3 Capital Adequacy Ratios (continued)

The following table shows the breakdown of RWA by risk types and the corresponding capital requirement as at 31 December 2017 and 31 December 2016:

Table 3: Risk-Weighted Assets by Risk Types and Minimum Capital Requirements

RHB Islamic Bank	RWA		Minimum Capital Requirements	
Risk Types	**2017 RM'000**	**2016 RM'000**	**2017 RM'000**	**2016 RM'000**
Credit Risk	**27,456,953**	23,958,399	**2,196,556**	1,916,672
Under Standardised Approach	**34,726,152**	29,623,743	**2,778,092**	2,369,899
Absorbed by PSIA under Standardised Approach	**(7,269,199)**	(5,665,344)	**(581,536)**	(453,227)
Market Risk				
Under Standardised Approach	**240,688**	63,426	**19,255**	5,074
Operational Risk				
Under Basic Indicator Approach	**1,397,487**	1,200,381	**111,799**	96,030
Total	**29,095,128**	**25,222,206**	**2,327,610**	**2,017,776**

Capital requirement for the three risk types is derived by multiplying the risk-weighted assets by 8%.

The Credit RWA increased by RM3.5 billion in 2017 mainly due to increased exposures in Home Financing and Corporate portfolios.

The Market RWA increase was arising from increase in FX derivatives volume.

4.0 CAPITAL STRUCTURE

The constituents of total eligible capital are set out in BNM's Guideline on Capital Adequacy Framework for Islamic Banks (Capital Components). These include shareholders' funds, after regulatory-related adjustments, and eligible capital instruments issued by the Bank. Tier I capital consists primarily of ordinary share capital, share premium, retained profits, other reserves and hybrid Tier I capital securities. Tier II capital consists of subordinated obligations and collective impairment allowance. Refer to Note 19 to the Financial Statements for the terms of these capital instruments.

BNM had on 3 May 2017, issued a Revised Policy Document on Capital Funds for Islamic Banks (Revised Policy Document) and the revised component of capital funds shall exclude share premium and reserve fund. The Revised Policy Document is only applicable for banking institutions operating in Malaysia.

The following table represents the capital position of the Bank as at 31 December 2017 and 31 December 2016:

4.0 CAPITAL STRUCTURE (CONTINUED)

Table 4: Capital Structure

	RHB Islamic Bank	
	2017 RM'000	2016 RM'000
Common Equity Tier I Capital/Tier I Capital		
Paid up ordinary share capital	**1,273,424**	1,273,424
Retained profits	**1,787,323**	766,058
Other reserves	**–**	762,388
Unrealised losses on AFS financial instruments	**(15,929)**	(31,944)
Less:		
Deferred tax assets	**(17,140)**	(25,748)
Other intangibles	**(4,412)**	–
Ageing Reserves and Liquidity Reserve*	**(4,296)**	(2,891)
Total Common Equity Tier I Capital/Tier I Capital	**3,018,970**	**2,741,287**
Tier II Capital		
Subordinated obligations	**750,000**	500,000
Collective impairment allowances and regulatory reserves^	**343,212**	290,408
Total Tier II Capital	**1,093,212**	**790,408**
Total Capital	**4,112,182**	**3,531,695**

^ Excludes collective assessment impairment allowance attributable to advances and financing classified as impaired but not individually assessed for impairment pursuant to BNM's Guideline on Classification and Impairment Provisions for Loans/Financing.

Includes the qualifying regulatory reserve under the Standardised Approach for non-impaired financing and advances of RM204,312,000 (31 December 2016: RM158,516,000).

* Pursuant to the Basel II Market Risk para 5.19 and 5.20 – Valuation Adjustments, the Capital Adequacy Framework (Basel II-RWA) calculation shall account for the ageing, liquidity and holding back adjustments/reserves on its trading portfolio.

5.0 RISK MANAGEMENT

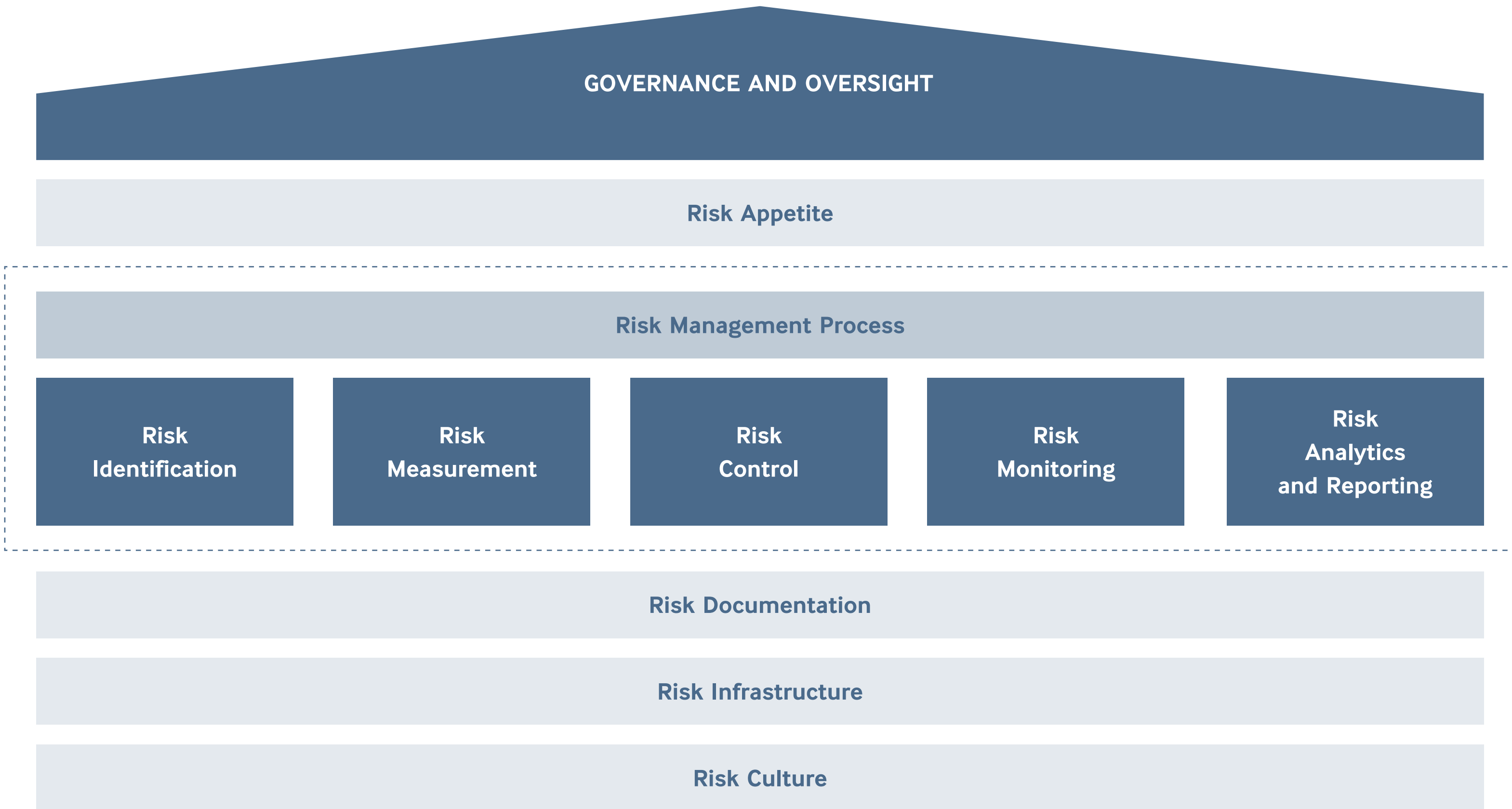
Risk is inherent in the Bank's activities and is managed through a process of on-going identification, measurement and monitoring, subject to limits and other controls. Besides credit risk, the Bank is exposed to a range of other risk types such as market, liquidity, operational, legal, Shariah, strategic and cross-border, as well as other forms of risk inherent to its strategy, product range and geographical coverage.

Effective risk management is fundamental to drive sustainable growth and shareholders' value, while maintaining competitive advantage, and is thus a central part of the proactive risk management of the Bank's operating environment.

The Group Risk Management Framework governs the management of risks in the RHB Banking Group (the Group), as follows:

- It provides a holistic overview of the risk and control environment of the Group, with risk management aimed towards loss minimisation and protection against losses which may occur through, principally, the failure of effective checks and controls in the organisation.
- It sets out the strategic progression of risk management towards becoming a value creation enterprise. This is realised through building up capabilities and infrastructure in risk management sophistication, and enhanced risk quantification to optimise risk-adjusted returns.

The Group Risk Management Framework is represented in the following diagram:



The following sections describe some of these risk management content areas.

5.0 RISK MANAGEMENT (CONTINUED)

OVERARCHING RISK MANAGEMENT PRINCIPLES

The Risk Management Framework contains five fundamental principles that drive the philosophy of risk management in the Group. They are:

- Risk governance from the Boards of Directors of various operating entities within the Group;
- Clear understanding of risk management ownership;
- Institutionalisation of a risk-focused organisation;
- Alignment of risk management to business strategies; and
- Optimisation of risk-adjusted returns.

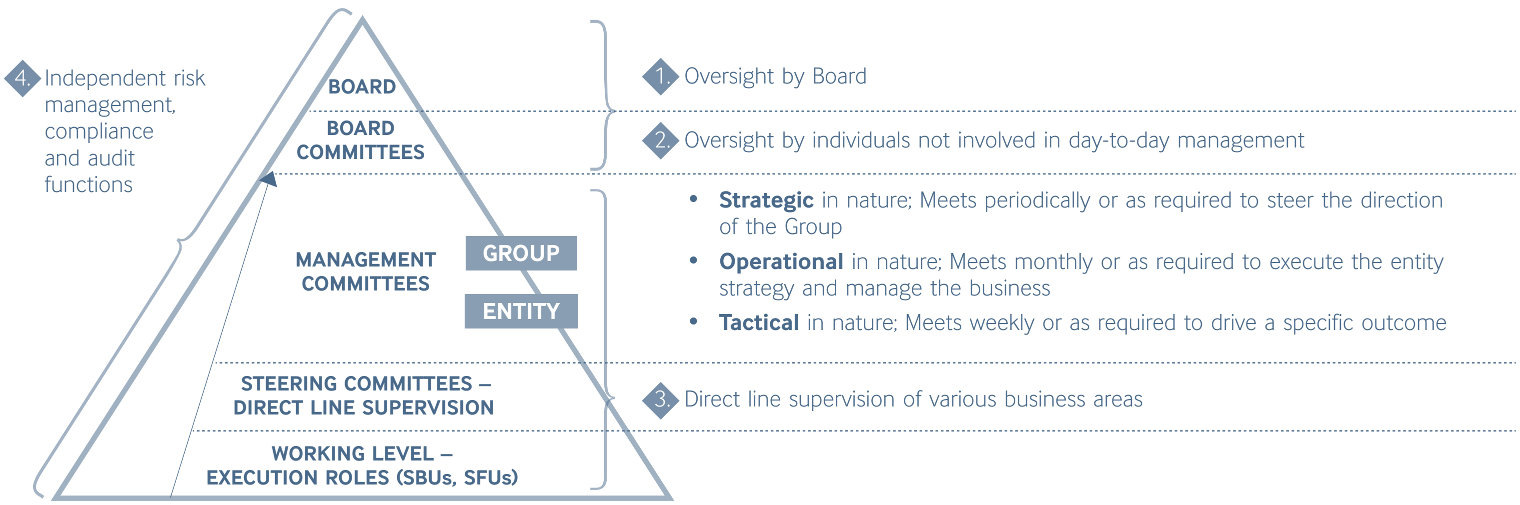
Principle 1: Risk Governance from the Boards of Directors of various operating entities within the Group

The ultimate responsibility of the Boards of Directors in the Group is to ensure that an effective risk management strategy is in place and uniformly understood across the Group. The Group has a structured framework to support the Board's oversight responsibilities.

RISK GOVERNANCE AND ORGANISATION

The Board of Directors (Board), through the BRC/IRMC, GCRC and the Group Risk & Credit Management function, establishes the risk appetite and risk principles for the Group and relevant entities. The BRC is the principal Board Committee that provides oversight over risk management activities for the Group to ensure that the Group's risk management process is in place and functional. The BRC assists the Board to review the Group's overall risk management philosophy, frameworks, policies and models. The IRMC was established to assist the Board of RHB Islamic Bank on risk issues relevant and unique to RHB Islamic Bank.

The responsibility for the supervision of the day-to-day management of enterprise risk and capital matters is delegated to the GCRC comprising Senior Management of the Group and which reports to the BRC/IRMC and the Group Management Committee (GMC). There are other committees set up to manage specific areas of risks in the Group. An overview of this governance framework at Group level is as below:



5.0 RISK MANAGEMENT (CONTINUED)

RISK CULTURE

Principle 2: Clear Understanding of Risk Management Ownership

Proactive risk ownership is important for effective management of risk. This promotes a risk awareness culture throughout the Group. The Group adopts the principle that 'Risk and Compliance is Everyone's Responsibility'.

The strategic business units (SBUs) and strategic functional units (SFUs) of the respective operating entities in the Group are collectively responsible for identifying, managing and reporting risks. The business units manage certain defined risks supported by the services provided by the functional units, including the risk management function. The approach is based on the 'three lines of defence' model as depicted below:

FIRST LINE **Business/Functional Level**	• Responsible for managing day-to-day operational risks and compliance issues • Business Risk and Compliance Officer is to assist business/functional unit in day-to-day risks and compliance matters
SECOND LINE **Group Risk Management & Group Compliance**	• Responsible for oversight, establishing governance and providing support to business/functional unit on risk and compliance matters
THIRD LINE **Group Internal Audit**	• Provide independent assurance to the Board that risk and compliance management functions effectively as designed

RISK ENVIRONMENT AND INFRASTRUCTURE

Principle 3: Institutionalisation of a Risk-Focused Organisation

In addition to risk ownership, a risk-focused culture is promoted throughout the Group through strengthening of the central risk management functions and continuous reinforcement of a risk and control environment within the Group. There is a continuous review of business activities and processes to identify significant risk areas and implement control procedures to operate within established corporate policies and limits.

Central Risk Management Function

Group Risk & Credit Management function is independent of the business function to ensure that the necessary balance in risk/return decisions is not compromised by short-term pressures to generate revenues. The said function is headed by the Group Chief Risk Officer.

The roles and responsibilities of the Group Chief Risk Officer include:

- Facilitating the setting of the strategic direction and overall policy on management and control of risk of the Group;
- Ensuring industry best practices in risk management are adopted across the Group, including the setting of risk management parameters and risk models;
- Developing a pro-active, balanced and risk-attuned culture within the Group;
- Advising Senior Management, the GCRC, BRC/IRMC and the Board on risk issues and their possible impact on the Group in the achievement of its objectives and strategies; and
- Administering the delegation of discretionary powers to Management personnel within the Group.

5.0 RISK MANAGEMENT (CONTINUED)

Central Risk Management Function (continued)

Group Risk & Credit Management consisting of Group Risk Management, Group Credit Management and Group Risk Operations provides independent oversight on business activities and implements the Group Risk Management Framework in order to protect and safeguard the Group's assets, and to prevent and mitigate financial and reputational losses to the Group. Key areas for which Group Risk Management is responsible for include the Group's risk policy and framework, day-to-day risk measurement and monitoring, providing timely risk analysis to management, and ensuring compliance to regulatory risk reporting requirements.

Group Credit Management oversees the Group-wide credit evaluation and assessment, approval and credit monitoring functions by providing credit risk assessment assurance on credit proposals, highlighting key risks and potential problematic accounts, and improving credit process efficiency.

Group Risk Operations is responsible for strategising and implementing a comprehensive enterprise-wide risk governance framework, and managing the development of robust risk management infrastructure and tools, aligned with the Group's strategy for growth and keeping pace with the market requirements and competitive business environment. Group Risk Operations drives the operationalisation of the Group's risk transformation initiatives in establishing risk management as a valuable business partner.

Risk and Control Environment

The business and functional heads are accountable for risk management in their businesses and functions, and for overseas operations where they have governance responsibilities. The business and functional units have clear segregation of duties to ensure that business processes are functioning effectively. There is accountability delegated to the appropriate authority to enable them to execute their respective authorities in meeting the business strategies without compromising the risk management process.

The primary responsibility for managing risks, therefore, rests with the business managers who are best equipped to ensure that risk management and control are continuously focused on the way business is conducted. There is a continuous review of business activities and processes to identify significant risk areas and implement control procedures to operate within established corporate policies and limits.

The risk management processes within the Group seek to identify, measure, monitor and control risk so that risk exposures are adequately managed and the expected returns adequately compensate the risks.

- Identification: The identification and analysis of the existing and potential risks is a continuing process, in order to facilitate and ensure the risks can be managed and controlled within the risk appetite of the Group and specific entity, where necessary.
- Measurement: Risks are measured, assessed and aggregated using comprehensive qualitative and quantitative risk measurement methodologies, and the process also serves as an important tool as it provides an assessment of capital adequacy and solvency.
- Controlling and Monitoring: Controls, triggers and limits are used to manage risk exposures and to facilitate early identification of potential problem on a timely basis.
- Analytics and Reporting: Risk analysis and reports are prepared at the respective entities and consolidated level as well as business level are regularly escalated to the senior management and relevant Boards to ensure that the risks remain within the established appetite and to support an informed decision-making process.

5.0 RISK MANAGEMENT (CONTINUED)

Risk and Control Environment (continued)

The Group recognises that effective implementation of the risk management system and process must be supported by a robust set of documentation and infrastructure. Towards this end, the Group has established frameworks, policies and other relevant control documents to ensure clearly defined practices and processes are implemented consistently across the Group.

In terms of risk infrastructure, the Group has organised its resources and talents into specific functions, and invested into technology, including data management to support the Group's risk management activities.

RISK APPETITE

Principle 4: Alignment of Risk Management to Business Strategies

The Group Risk Management Framework serves to align the Group's business strategy to risk strategy, and vice-versa. This is articulated through the risk appetite setting and the Group's annual business and financial budgetary plan, which is facilitated by the integration of risk measures in capital management.

Risk appetite is set by the Board and reported through various metrics that enable the Group to manage capital constraints and shareholders' expectations. The risk appetite is a key component of the management of risks and describes the types and level of risk that the Group is prepared to accept in delivering its strategy.

Principle 5: Optimisation of Risk-Adjusted Returns

One of the objectives of capital management is to reflect a risk-adjusted return assumed by the businesses throughout the Group. By linking risk to capital, the risk-adjusted return measure contributes to the creation of shareholders' value by facilitating the allocation of capital to the businesses.

The medium to long-term strategy and principle of risk management of the Group is to intensify the integration of capital management within the Group. The Group is progressively implementing a risk-adjusted return based framework for allocation of capital to business units and for performance measurement and management.

6.0 CREDIT RISK

Credit Risk Definition

Credit risk is the risk of loss arising from customers' or counterparties' failure to fulfil their financial and contractual obligations in accordance to the agreed terms. It stems primarily from the Group's financing, trade finance and its funding, investment and trading activities from both on and off-balance sheet transactions.

6.1 Credit Risk Management Oversight and Organisation

The Group Credit Committee (GCC) is the senior management committee empowered to approve or reject all financial investments, counterparty credit and financing up to the defined threshold limits.

GCC will direct, monitor, review and consider such issues as may materially impact on the present and future quality of the Bank's asset book. GCC also acts as the body which, through the BRC, recommends to the respective Boards, on matters pertaining to credit risk (such as credit and underwriting evaluation/approval/procedure, and delegated financing authorities).

The BCC's main functions are (i) affirming, vetoing or imposing more stringent conditions on credits of the Group which are duly approved by the GCC, (ii) overseeing the management of impaired and high risk accounts, and (iii) approving credit transactions to connected parties up to the defined threshold limits. BCC also endorses policy financing and financing required by BNM to be referred to the respective Boards for approval.

The Group Credit Management has the functional responsibility to ensure that internal processes and credit underwriting standards are adhered to before financing proposals are approved. All financing proposals are firstly assessed for its credit worthiness by the originating business units before being evaluated by an independent credit manager and decided upon by the management.

All financing exposure limits are approved within a defined credit approval authority framework. Large financing exposures are further subject to post approval credit review by Group Internal Audit.

With the exception of credit applications for consumer and approved products under programme financing which can be approved by business units' supervisors, all other credit facilities are subject to independent assessment by a team of dedicated and experienced credit evaluators in Head Office. For proper checks and controls, joint approval is required for all discretionary lending between business and independent credit underwriters. Financing which are beyond the delegated financing authority limits will be escalated to the relevant committees for approval.

Within Group Risk Management, the Group Credit Risk Management has the functional responsibility for credit risk management, portfolio risk monitoring, risk reporting and development of credit policies and guidelines. The Group also conducts regular credit stress tests to assess the credit portfolio's vulnerability to adverse credit risk events.

Regular risk reporting is made to the GCRC, IRMC and the Board. These reports include various credit risk aspects such as portfolio quality, expected losses, and concentration risk exposures by business portfolio. Such reporting allows Senior Management to identify adverse credit trends, take prompt corrective actions, and ensure appropriate risk-adjusted decision making.

6.0 CREDIT RISK (CONTINUED)

6.2 Credit Risk Management Approach

The Bank's credit risk management framework is founded upon BNM's Guideline on Best Practices for the Management of Credit Risk. The Bank abides by its Group Credit Policy which supports the development of a strong credit culture with the objective of maintaining a diversified portfolio, and a reliable and satisfactory risk-weighted return. Industry best practices are instilled in the continual updating of the Group Credit Policy.

The Bank's credit risk management process is documented in the Group Credit Guidelines (GCG) and Group Credit Procedures Manual (GCPM) which sets out the operational procedures and guidelines governing the credit processes within the Bank.

The GCG and GCPM have been designed to ensure that:

- The process of credit initiation, administration, supervision and management of financing and advances are carried out consistently and uniformly by the business origination and other credit support functions within the Group.
- Procedures and guidelines governing the credit function are in compliance with the credit policies of the Group.

Financing to Corporate and Institutional Customers

Financing to corporate and institutional customers are individually evaluated and risk-rated. Credit underwriters identify and assess the credit risk of large corporate or institutional customers, or customer groups, taking into consideration their financial and business profiles, industry and economic factors, collateral, or other credit support.

Credit Risk from Investment or Trading Activities

In the course of its trading or investment activities, the Bank is also exposed to credit risks from trading, derivative and debt securities activities. Relevant credit guidelines are established to govern the credit risk via guidance on derivatives, hedging and investment related activities of the different exposures.

Financing to Consumers and Small Businesses

For the consumer and small business sectors, credit risk is managed on a portfolio basis. Such products include home financing, credit cards, auto financing, commercial property financing, personal financing and business financing. Financing are underwritten under product programmes that clearly define the target market, underwriting criteria, terms of financing, maximum exposure, credit origination guidelines and verification process. Scoring models are used in the credit decision process to enable objective risk evaluation and consistent decisions, cost efficient processing, and behavioural score monitoring of expected portfolio performance.

Credit Risk Measurement

Along with judgement and experience, risk measurement or quantification plays a critical role in making informed risk taking and portfolio management decisions. As the nature of credit risk varies by financing type, the Bank applies different credit risk measuring tools, so that the credit risk of each financing type is appropriately reflected.

6.0 CREDIT RISK (CONTINUED)

6.2 Credit Risk Management Approach (continued)

The followings represent the dimensions considered in the credit risk measurement:

1. Probability of Default (PD)

For corporate/non-retail financing, the probability of default is measured from obligor (or customer) rating obtained from the risk rating system to determine obligor's level of default risk. The risk rating of each obligor is regularly reviewed to ensure that it actually reflects the debtor's/customer's updated default risk. For retail exposures/financing, the default risk is measured via different credit scoring or behavioural scoring model.

2. Loss Given Default (LGD)

For corporate financing, LGD is determined via the credit risk mitigation adjustment, in which collateral and security will determine the level of LGD for a specific transaction. For retail financing, LGD is captured at respective segment (or pool) level.

3. Exposure at Default (EAD)

Exposure at default is calculated from the current outstanding balance and availability of committed financing line. In this regard, the key factor is the Bank's obligation related to the available financing line. For corporate financing, the EAD is measured at an individual obligor exposure as per BNM's Guideline on Capital Adequacy Framework for Islamic Banks (Risk-Weighted Assets). For retail financing, the principle of credit risk measurement is similar, but measured on a pooled basis, based on internal models.

6.3 Off-Balance Sheet Exposures and Counterparty Credit Risk (CCR)

The management of the following off-balance sheet exposures of the Bank is in accordance to the credit risk management approach as set out under Section 6.2 of this document:

- Financial guarantees and standby letters of credit, which represent undertakings that the Bank will make payments in the event that its customer cannot meet its obligations to third-parties. These exposures carry the same credit risk as financing even though they are contingent in nature;
- Documentary and commercial letters of credit, which are undertakings by the Bank on behalf of its customers. These exposures are usually collateralised by the underlying shipment of goods to which they relate;
- Commitments to extend financing, which includes the unutilised or undrawn portions of financing facilities;
- Unutilised credit card lines; and
- Principal or notional amount of derivative financial instruments.

6.0 CREDIT RISK (CONTINUED)

6.3 Off-Balance Sheet Exposures and Counterparty Credit Risk (CCR) (continued)

Counterparty Credit Risk

Counterparty Credit Risk is the risk that the entity with whom one has entered into a financial contract (the counterparty to the contract) will fail to fulfil their side of the contractual agreement (eg they default). Counterparty risk is typically defined as arising from two broad classes of financial products:

- Over-the-counter derivatives such as profit rate swaps, FX forwards and credit default swaps.
- Securities financing transactions such as repos and reverse repos; and securities borrowing and financing.

Derivative financial instruments are primarily entered into for hedging purposes. Any financial loss is calculated based on the cost to replace the defaulted derivative financial instruments with another similar contract in the market. The cost of replacement is equivalent to the difference between the original value of the derivatives at the time of contract with the defaulted counterparty and the current fair value of a similar substitute at current market prices. An economic loss would occur if the transactions or portfolio of transactions with the counterparty has a positive economic value at the time of default.

All outstanding financial derivative positions are marked-to-market on a daily basis. The Bank's Treasury Operations Department monitors counterparties' positions and promptly escalates any shortfall in the threshold levels to the relevant parties for next course of action.

6.4 Credit Exposures and Risk-Weighted Assets by Portfolio and Approaches

All credit exposures of the Bank are booked in Malaysia. The following tables show the credit exposures or Exposure at Default (EAD) as at 31 December 2017 compared with 31 December 2016, segregated by:

- the various types of asset classes, showing details of the exposures by type of approaches, before and after credit risk mitigation (CRM), the corresponding RWA and capital requirements;
- disclosure on off-balance sheet and counterparty credit risk;
- industry sector;
- residual maturity; and
- disclosures under the Standardised Approach by risk weights.

6.0 CREDIT RISK (CONTINUED)

6.4 Credit Exposures and Risk-Weighted Assets by Portfolio and Approaches (continued)

Table 5a: Summary of Credit Exposures with Credit Risk Mitigation ('CRM') by Asset Class and Minimum Capital Requirements (On and Off-Balance Sheet Exposures) as at 31 December 2017

RHB Islamic Bank Exposure Class	Gross Exposures/ EAD before CRM RM'000	Net Exposures/ EAD after CRM RM'000	Risk-Weighted Assets RM'000	Risk-Weighted Assets Absorbed by PSIA RM'000	Total Risk-Weighted Assets After Effect of PSIA RM'000	Minimum Capital Requirements RM'000
Exposures under the Standardised Approach						
On-Balance Sheet Exposures						
Sovereigns & Central Banks	5,317,479	5,317,479	65	–	65	5
Public Sector Entities	4,315,960	4,315,960	30,188	–	30,188	2,415
Banks, Development Financial Institutions & MDBs	2,959,428	2,959,428	591,712	–	591,712	47,337
Takaful Cos, Securities Firms & Fund Managers	283,629	281,286	281,286	–	281,286	22,503
Corporates	20,785,998	19,831,636	16,750,555	(6,618,528)	10,132,027	810,562
Regulatory Retail	13,492,830	12,923,049	10,933,236	(527,567)	10,405,669	832,454
Residential Mortgages	8,029,511	8,023,801	3,047,224	(115,179)	2,932,045	234,564
Higher Risk Assets	3,342	3,342	5,012	(305)	4,707	376
Other Assets	112,863	112,863	92,263	–	92,263	7,381
Defaulted Exposures	264,563	256,656	268,490	(6,925)	261,565	20,925
Total On-Balance Sheet Exposures	55,565,603	54,025,500	32,000,031	(7,268,504)	24,731,527	1,978,522
Off-Balance Sheet Exposures						
OTC Derivatives	866,940	866,940	352,011	–	352,011	28,161
Off-balance sheet exposures other than OTC derivatives or credit derivatives	3,987,740	3,865,576	2,371,638	(336)	2,371,302	189,704
Defaulted Exposures	1,794	1,728	2,472	(359)	2,113	169
Total Off-Balance Sheet Exposures	4,856,474	4,734,244	2,726,121	(695)	2,725,426	218,034
Total On and Off-Balance Sheet Exposures	60,422,077	58,759,744	34,726,152	(7,269,199)	27,456,953	2,196,556

6.0 CREDIT RISK (CONTINUED)

6.4 Credit Exposures and Risk-Weighted Assets by Portfolio and Approaches (continued)

Table 5b: Summary of Credit Exposures with Credit Risk Mitigation ('CRM') by Asset Class and Minimum Capital Requirements (On and Off-Balance Sheet Exposures) as at 31 December 2016

RHB Islamic Bank Exposure Class	Gross Exposures/ EAD before CRM RM'000	Net Exposures/ EAD after CRM RM'000	Risk-Weighted Assets RM'000	Risk-Weighted Assets Absorbed by PSIA RM'000	Total Risk-Weighted Assets After Effect of PSIA RM'000	Minimum Capital Requirements RM'000
Exposures under the Standardised Approach						
On-Balance Sheet Exposures						
Sovereigns & Central Banks	7,599,391	7,599,391	2,984	–	2,984	239
Public Sector Entities	3,373,527	3,368,871	15,871	–	15,871	1,270
Banks, Development Financial Institutions & MDBs	1,649,807	1,649,807	328,976	–	328,976	26,318
Takaful Cos, Securities Firms & Fund Managers	279,341	279,341	279,341	–	279,341	22,347
Corporates	17,276,197	16,922,437	13,685,403	(4,833,584)	8,851,819	708,146
Regulatory Retail	13,299,274	13,182,906	10,387,378	(580,493)	9,806,885	784,551
Residential Mortgages	4,060,558	4,055,084	2,100,993	(76,830)	2,024,163	161,933
Higher Risk Assets	–	–	–	–	–	–
Other Assets	195,111	195,111	174,329	–	174,329	13,946
Defaulted Exposures	280,486	276,094	317,861	(6,556)	311,305	24,904
Total On-Balance Sheet Exposures	**48,013,692**	**47,529,042**	**27,293,136**	**(5,497,463)**	**21,795,673**	**1,743,654**
Off-Balance Sheet Exposures						
OTC Derivatives	752,161	752,161	548,880	–	548,880	43,910
Off-balance sheet exposures other than OTC derivatives or credit derivatives	2,618,936	2,594,554	1,778,925	(167,463)	1,611,462	128,917
Defaulted Exposures	1,873	1,873	2,802	(418)	2,384	191
Total Off-Balance Sheet Exposures	**3,372,970**	**3,348,588**	**2,330,607**	**(167,881)**	**2,162,726**	**173,018**
Total On and Off-Balance Sheet Exposures	**51,386,662**	**50,877,630**	**29,623,743**	**(5,665,344)**	**23,958,399**	**1,916,672**

6.0 CREDIT RISK (CONTINUED)

6.4 Credit Exposures and Risk-Weighted Assets by Portfolio and Approaches (continued)

Table 6a: Exposures on Off-Balance Sheet and Counterparty Credit Risk (Before Credit Risk Mitigation) as at 31 December 2017

RHB Islamic Bank Nature of Item	Principal/ Notional Amount RM'000	Positive Fair Value of Derivative Contracts RM'000	Credit Equivalent Amount RM'000	Risk-Weighted Assets RM'000
Transaction related contingent items	195,298		97,649	71,982
Short term self liquidating trade related contingencies	111,779		22,356	8,084
NIFs and obligations under underwriting agreement	–		–	–
Commitment to buy back the Islamic securities arising from the Sell and Buy Back (SBBA) transaction	629,085		629,085	–
Foreign exchange related contracts	10,572,668	324,340	819,299	346,962
1 year or less	*7,910,145*	*241,526*	*387,092*	*131,035*
Over 1 year to 5 years	*1,713,345*	*51,517*	*220,566*	*102,865*
Over 5 years	*949,178*	*31,297*	*211,641*	*113,062*
Profit rate related contracts	4,457,338	28,171	47,641	5,049
1 year or less	*3,690,000*	*24,858*	*28,908*	*817*
Over 1 year to 5 years	*767,338*	*3,313*	*18,733*	*4,232*
Over 5 years	–	–	–	–
Other commitments, such as formal standby facilities and financing lines, with original maturity of over 1 year	5,800,512		3,106,777	2,193,794
Other commitments, such as formal standby facilities and financing lines, with original maturity of up to 1 year	–		–	–
Any commitments that are unconditionally cancellable at any time by the bank without prior notice or that effectively provide for automatic cancellation due to deterioration in a customer's creditworthiness	2,513,842		133,667	100,250
Total	**24,280,522**	**352,511**	**4,856,474**	**2,726,121**

6.0 CREDIT RISK (CONTINUED)

6.4 Credit Exposures and Risk-Weighted Assets by Portfolio and Approaches (continued)

Table 6b: Exposures on Off-Balance Sheet and Counterparty Credit Risk (Before Credit Risk Mitigation) as at 31 December 2016

RHB Islamic Bank Nature of Item	Principal/ Notional Amount RM'000	Positive Fair Value of Derivative Contracts RM'000	Credit Equivalent Amount RM'000	Risk-Weighted Assets RM'000
Transaction related contingent items	127,119		63,560	38,828
Short term self liquidating trade related contingencies	74,479		14,896	4,441
NIFs and obligations under underwriting agreement	76,000		38,000	38,000
Commitment to buy back the Islamic securities arising from the Sell and Buy Back (SBBA) transaction	–		–	–
Foreign exchange related contracts	9,343,242	390,248	706,694	539,070
1 year or less	*7,577,185*	*317,585*	*468,103*	*400,107*
Over 1 year to 5 years	*766,434*	*55,003*	*110,972*	*53,921*
Over 5 years	*999,623*	*17,660*	*127,619*	*85,042*
Profit rate related contracts	4,864,448	3,887	45,467	9,810
1 year or less	*2,585,000*	*–*	*2,253*	*450*
Over 1 year to 5 years	*2,279,448*	*3,887*	*43,214*	*9,360*
Over 5 years	–	–	–	–
Other commitments, such as formal standby facilities and financing lines, with original maturity of over 1 year	4,824,220		2,412,110	1,631,271
Other commitments, such as formal standby facilities and financing lines, with original maturity of up to 1 year	–		–	–
Any commitments that are unconditionally cancellable at any time by the bank without prior notice or that effectively provide for automatic cancellation due to deterioration in a customer's creditworthiness	2,183,074		92,243	69,187
Total	**21,492,582**	**394,135**	**3,372,970**	**2,330,607**

6.0 CREDIT RISK (CONTINUED)

6.4 Credit Exposures and Risk-Weighted Assets by Portfolio and Approaches (continued)

Table 7a: Credit Risk Exposures (Before Credit Risk Mitigation) by Industry Sector as at 31 December 2017

RHB Islamic Bank Exposure Class	Agriculture RM'000	Mining & Quarrying RM'000	Manufacturing RM'000	Electricity, Gas & Water Supply RM'000	Construction RM'000	Wholesale, Retail Trade, Restaurants & Hotels RM'000	Transport, Storage & Communication RM'000	Finance, Takaful, Real Estate & Business RM'000	Education, Health & Others RM'000	Household RM'000	Others RM'000	Total RM'000
Exposures under Standardised Approach												
Sovereigns & Central Banks	–	–	–	–	–	–	–	2,706,406	3,272,768	–	–	5,979,174
Public Sector Entities	–	–	–	–	–	3,007	–	–	4,577,139	–	–	4,580,146
Banks, Development Financial Institutions & MDBs	–	–	–	–	–	–	–	3,569,055	–	–	–	3,569,055
Takaful Cos, Securities Firms & Fund Managers	–	–	–	–	–	–	–	283,629	–	–	–	283,629
Corporates	1,482,616	906,500	1,601,116	372,279	4,656,433	1,278,382	5,221,428	7,232,221	482,234	–	–	23,233,209
Regulatory Retail	9,745	4,019	96,409	1,222	114,450	234,580	27,158	155,724	13,069	13,866,171	–	14,522,547
Residential Mortgages	–	–	–	–	–	–	–	–	–	8,138,037	–	8,138,037
Higher Risk Assets	–	–	–	–	–	–	–	–	–	3,417	–	3,417
Other Assets	–	–	–	–	–	–	–	–	–	–	112,863	112,863
Total	**1,492,361**	**910,519**	**1,697,525**	**373,501**	**4,770,883**	**1,515,969**	**5,248,586**	**13,947,035**	**8,345,210**	**22,007,625**	**112,863**	**60,422,077**

Table 7b: Credit Risk Exposures (Before Credit Risk Mitigation) by Industry Sector as at 31 December 2016

RHB Islamic Bank Exposure Class	Agriculture RM'000	Mining & Quarrying RM'000	Manufacturing RM'000	Electricity, Gas & Water Supply RM'000	Construction RM'000	Wholesale, Retail Trade, Restaurants & Hotels RM'000	Transport, Storage & Communication RM'000	Finance, Takaful, Real Estate & Business RM'000	Education, Health & Others RM'000	Household RM'000	Others RM'000	Total RM'000
Exposures under Standardised Approach												
Sovereigns & Central Banks	–	–	–	–	–	–	–	4,144,313	3,467,552	–	–	7,611,865
Public Sector Entities	–	–	–	–	–	428	–	–	3,764,906	–	–	3,765,334
Banks, Development Financial Institutions & MDBs	–	–	–	–	–	–	–	1,959,624	–	–	–	1,959,624
Takaful Cos, Securities Firms & Fund Managers	–	–	–	–	–	–	–	280,031	–	–	–	280,031
Corporates	1,420,131	572,876	1,035,959	360,607	2,493,970	858,732	4,453,639	7,134,288	1,072,448	–	–	19,402,650
Regulatory Retail	48,491	17,505	141,957	8,349	203,095	272,252	64,950	246,016	25,144	12,990,458	-	14,018,217
Residential Mortgages	–	–	–	–	–	–	–	–	–	4,153,830	–	4,153,830
Higher Risk Assets	–	–	–	–	–	–	–	–	–	–	–	–
Other Assets	–	–	–	–	–	–	–	–	–	–	195,111	195,111
Total	**1,468,622**	**590,381**	**1,177,916**	**368,956**	**2,697,065**	**1,131,412**	**4,518,589**	**13,764,272**	**8,330,050**	**17,144,288**	**195,111**	**51,386,662**

6.0 CREDIT RISK (CONTINUED)

6.4 Credit Exposures and Risk-Weighted Assets by Portfolio and Approaches (continued)

Table 8a: Credit Risk Exposures (Before Credit Risk Mitigation) by Remaining Maturity as at 31 December 2017

RHB Islamic Bank Exposure Class	One year or less RM'000	More than one to five years RM'000	Over five years RM'000	Total RM'000
Exposures under Standardised Approach				
Sovereigns & Central Banks	**1,990,163**	**2,244,359**	**1,744,652**	**5,979,174**
Public Sector Entities	**2,357,171**	**1,893,855**	**329,120**	**4,580,146**
Banks, Development Financial Institutions & MDBs	**3,214,834**	**230,937**	**123,284**	**3,569,055**
Takaful Cos, Securities Firms & Fund Managers	**4,751**	**278,878**	**–**	**283,629**
Corporates	**5,155,607**	**7,682,503**	**10,395,099**	**23,233,209**
Regulatory Retail	**130,406**	**3,053,371**	**11,338,770**	**14,522,547**
Residential Mortgages	**1,527**	**50,040**	**8,086,470**	**8,138,037**
Higher Risk Assets	**–**	**10**	**3,407**	**3,417**
Other Assets	**–**	**–**	**112,863**	**112,863**
Total	**12,854,459**	**15,433,953**	**32,133,665**	**60,422,077**

Table 8b: Credit Risk Exposures (Before Credit Risk Mitigation) by Remaining Maturity as at 31 December 2016

RHB Islamic Bank Exposure Class	One year or less RM'000	More than one to five years RM'000	Over five years RM'000	Total RM'000
Exposures under Standardised Approach				
Sovereigns & Central Banks	3,150,687	2,554,948	1,906,230	7,611,865
Public Sector Entities	403,940	2,941,806	419,588	3,765,334
Banks, Development Financial Institutions & MDBs	1,666,154	133,803	159,667	1,959,624
Takaful Cos, Securities Firms & Fund Managers	1,069	278,962	–	280,031
Corporates	3,752,947	6,732,044	8,917,659	19,402,650
Regulatory Retail	534,487	2,631,420	10,852,310	14,018,217
Residential Mortgages	1,956	41,264	4,110,610	4,153,830
Higher Risk Assets	–	–	–	–
Other Assets	–	–	195,111	195,111
Total	**9,511,240**	**15,314,247**	**26,561,175**	**51,386,662**

6.0 CREDIT RISK (CONTINUED)

6.4 Credit Exposures and Risk-Weighted Assets by Portfolio and Approaches (continued)

Standardised Approach

Under the Standardised Approach, the risk weights are prescribed by BNM based on the asset class to which the exposure is assigned.

The following tables show the Bank's credit exposures for its portfolios with the corresponding risk weights and RWA under the Standardised Approach, after credit risk mitigation (CRM):

Table 9a: Portfolios under the Standardised Approach by Risk Weights as at 31 December 2017

RHB Islamic Bank Exposure Class	Sovereigns & Central Banks RM'000	Public Sector Entities RM'000	Banks, Development Financial Institutions & MDBs RM'000	Takaful Cos, Securities Firms & Fund Managers RM'000	Corporates RM'000	Regulatory Retail RM'000	Residential Mortgages RM'000	Higher Risk Assets RM'000	Other Assets RM'000	Equity Exposures RM'000	Total Exposures after Credit Risk Mitigation RM'000	Total Risk-Weighted Assets RM'000
Supervisory Risk Weights (%)												
0%	5,971,060	4,368,270	25,257	–	2,323,849	–	–	–	20,600	–	12,709,036	–
20%	8,114	207,061	3,527,541	–	1,491,838	118	–	–	–	–	5,234,672	1,046,934
35%	–	–	–	–	–	–	6,449,437	–	–	–	6,449,437	2,257,303
50%	–	–	16,257	–	134,406	5,113	1,622,636	–	–	–	1,778,412	889,206
75%	–	–	–	–	–	8,401,788	–	–	–	–	8,401,788	6,301,341
100%	–	–	–	281,286	18,195,169	5,467,805	59,939	–	92,263	–	24,096,462	24,096,462
150%	–	–	–	–	53,915	32,605	–	3,417	–	–	89,937	134,906
Total Exposures	**5,979,174**	**4,575,331**	**3,569,055**	**281,286**	**22,199,177**	**13,907,429**	**8,132,012**	**3,417**	**112,863**	**–**	**58,759,744**	**34,726,152**

Table 9b: Portfolios under the Standardised Approach by Risk Weights as at 31 December 2016

RHB Islamic Bank Exposure Class	Sovereigns & Central Banks RM'000	Public Sector Entities RM'000	Banks, Development Financial Institutions & MDBs RM'000	Takaful Cos, Securities Firms & Fund Managers RM'000	Corporates RM'000	Regulatory Retail RM'000	Residential Mortgages RM'000	Higher Risk Assets RM'000	Other Assets RM'000	Equity Exposures RM'000	Total Exposures after Credit Risk Mitigation RM'000	Total Risk-Weighted Assets RM'000
Supervisory Risk Weights (%)												
0%	7,584,473	3,589,517	4,926	–	1,383,301	–	–	–	20,782	–	12,582,999	–
20%	27,392	171,162	1,954,698	–	2,123,632	3,887	–	–	–	–	4,280,771	856,154
35%	–	–	–	–	–	–	2,304,065	–	–	–	2,304,065	806,423
50%	–	–	–	–	777,403	39,308	918,073	–	–	–	1,734,784	867,392
75%	–	–	–	–	–	11,704,265	28,198	–	–	–	11,732,463	8,799,347
100%	–	–	–	280,031	14,698,933	2,094,064	891,434	–	174,329	–	18,138,791	18,138,791
150%	–	–	–	–	56,813	40,664	6,280	–	–	–	103,757	155,636
Total Exposures	**7,611,865**	**3,760,679**	**1,959,624**	**280,031**	**19,040,082**	**13,882,188**	**4,148,050**	**–**	**195,111**	**–**	**50,877,630**	**29,623,743**

6.0 CREDIT RISK (CONTINUED)

6.5 Use of External Ratings

For exposures such as sovereigns, corporate and banking institutions, external ratings from approved external credit assessment institutions (ECAIs), where available, are used to calculate the risk-weighted assets and regulatory capital.

The process used to map ECAIs issuer ratings or comparable ECAIs issue ratings, are in accordance to the standards prescribed by BNM. Approved ECAIs are as follows:

- Standard & Poor's (S&P);
- Moody's Investor Services (Moody's);
- Fitch Ratings (Fitch);
- Malaysian Rating Corporation Berhad (MARC);
- RAM Rating Services Berhad; and
- Rating and Investment Information, Inc (R&I).

External ratings for the counterparties are determined as soon as relationship is established and these ratings are tracked and kept updated. Only publicly available credit ratings are used for regulatory risk weighting purpose.

The following tables show the Bank's credit exposures for 31 December 2017 compared with 31 December 2016, according to the ratings by ECAIs:

Table 10a: Rated Exposures According to Ratings by External Credit Assessment Institutions ('ECAIs') as at 31 December 2017

RHB Islamic Bank

Ratings of Corporates by Approved ECAIs	Moody's	Aaa to Aa3	A1 to A3	Baa1 to Ba3	B1 to C	Unrated
	S&P	AAA to AA-	A+ to A-	BBB+ to BB-	B+ to D	Unrated
	Fitch	AAA to AA-	A+ to A-	BBB+ to BB-	B+ to D	Unrated
	RAM	AAA to AA3	A1 to A3	BBB1 to BB3	B to D	Unrated
	MARC	AAA to AA-	A+ to A-	BBB+ to BB-	B1 to D	Unrated
	R&I	AAA to AA-	A+ to A-	BBB+ to BB-	B+ to D	Unrated
Exposure Class		RM'000	RM'000	RM'000	RM'000	RM'000
On and Off-Balance Sheet Exposures						
Public Sector Entities		–	–	–	–	4,575,331
Takaful Cos, Securities Firms & Fund Managers		–	–	–	–	281,286
Corporates		1,450,886	130,716	–	–	20,617,575

6.0 CREDIT RISK (CONTINUED)

6.5 Use of External Ratings (continued)

Table 10a: Rated Exposures According to Ratings by External Credit Assessment Institutions ('ECAIs') as at 31 December 2017 (continued)

Short Term Ratings of Corporates by Approved ECAIs		P-1	P-2	P-3	Others	Unrated
	Moody's S&P	A-1	A-2	A-3	Others	Unrated
	Fitch	F1+, F1	F2	F3	B to D	Unrated
	RAM	P-1	P-2	P-3	NP	Unrated
	MARC	MARC-1	MARC-2	MARC-3	MARC-4	Unrated
	R&I	a-1+, a-1	a-2	a-3	b, c	Unrated
Exposure Class		RM'000	RM'000	RM'000	RM'000	RM'000
On and Off-Balance Sheet Exposures						
Corporates		–	–	–	–	–

Ratings of Sovereigns and Central Banks by Approved ECAIs	Moody's	Aaa to Aa3	A1 to A3	Baa1 to Baa3	Ba1 to B3	Caa1 to C	Unrated
	S&P	AAA to AA-	A+ to A-	BBB+ to BBB-	BB+ to B-	CCC+ to D	Unrated
	Fitch	AAA to AA-	A+ to A-	BBB+ to BBB-	BB+ to B-	CCC+ to D	Unrated
	R&I	AAA to AA-	A+ to A-	BBB+ to BBB-	BB+ to B-	CCC+ to C	Unrated
Exposure Class		RM'000	RM'000	RM'000	RM'000	RM'000	RM'000
On and Off-Balance Sheet Exposures							
Sovereigns & Central Banks		–	5,979,174	–	–	–	–

Ratings of Banking Institutions by Approved ECAIs	Moody's	Aaa to Aa3	A1 to A3	Baa1 to Baa3	Ba1 to B3	Caa1 to C	Unrated
	S&P	AAA to AA-	A+ to A-	BBB+ to BBB-	BB+ to B-	CCC+ to D	Unrated
	Fitch	AAA to AA-	A+ to A-	BBB+ to BBB-	BB+ to B-	CCC+ to D	Unrated
	RAM	AAA to AA3	A1 to A3	BBB1 to BBB3	BB1 to B3	C1 to D	Unrated
	MARC	AAA to AA-	A+ to A-	BBB+ to BBB-	BB+ to B-	C+ to D	Unrated
	R&I	AAA to AA-	A+ to A-	BBB+ to BBB-	BB+ to B-	CCC+ to C	Unrated
Exposure Class		RM'000	RM'000	RM'000	RM'000	RM'000	RM'000
On and Off-Balance Sheet Exposures							
Banks, Development Financial Institutions & MDBs		2,549,740	239,745	1,636	–	–	777,934

6.0 CREDIT RISK (CONTINUED)

6.5 Use of External Ratings (continued)

Table 10b: Rated Exposures According to Ratings by External Credit Assessment Institutions ('ECAIs') as at 31 December 2016

RHB Islamic Bank

Ratings of Corporates by Approved ECAIs	Moody's	Aaa to Aa3	A1 to A3	Baa1 to Ba3	B1 to C	Unrated
	S&P	AAA to AA-	A+ to A-	BBB+ to BB-	B+ to D	Unrated
	Fitch	AAA to AA-	A+ to A-	BBB+ to BB-	B+ to D	Unrated
	RAM	AAA to AA3	A1 to A3	BBB1 to BB3	B to D	Unrated
	MARC	AAA to AA-	A+ to A-	BBB+ to BB-	B1 to D	Unrated
	R&I	AAA to AA-	A+ to A-	BBB+ to BB-	B+ to D	Unrated
Exposure Class		RM'000	RM'000	RM'000	RM'000	RM'000
On and Off-Balance Sheet Exposures						
Public Sector Entities		–	3,303,878	–	–	456,801
Takaful Cos, Securities Firms & Fund Managers		–	–	–	–	280,031
Corporates		1,925,147	934,236	–	–	16,040,630

Short Term Ratings of Corporates		P-1	P-2	P-3	Others	Unrated
by Approved ECAIs	Moody's S&P	A-1	A-2	A-3	Others	Unrated
	Fitch	F1+, F1	F2	F3	B to D	Unrated
	RAM	P-1	P-2	P-3	NP	Unrated
	MARC	MARC-1	MARC-2	MARC-3	MARC-4	Unrated
	R&I	a-1+, a-1	a-2	a-3	b, c	Unrated
Exposure Class		RM'000	RM'000	RM'000	RM'000	RM'000
On and Off-Balance Sheet Exposures						
Corporates		140,069	–	–	–	–

6.0 CREDIT RISK (CONTINUED)

6.5 Use of External Ratings (continued)

Table 10b: Rated Exposures According to Ratings by External Credit Assessment Institutions ('ECAIs') as at 31 December 2016 (continued)

RHB Islamic Bank

Ratings of Sovereigns and Central Banks by Approved ECAIs							
	Moody's	Aaa to Aa3	A1 to A3	Baa1 to Baa3	Ba1 to B3	Caa1 to C	Unrated
	S&P	AAA to AA-	A+ to A-	BBB+ to BBB-	BB+ to B-	CCC+ to D	Unrated
	Fitch	AAA to AA-	A+ to A-	BBB+ to BBB-	BB+ to B-	CCC+ to D	Unrated
	R&I	AAA to AA-	A+ to A-	BBB+ to BBB-	BB+ to B-	CCC+ to C	Unrated
Exposure Class		RM'000	RM'000	RM'000	RM'000	RM'000	RM'000
On and Off-Balance Sheet Exposures							
Sovereigns & Central Banks		–	7,611,865	–	–	–	–

Ratings of Banking Institutions by Approved ECAIs							
	Moody's	Aaa to Aa3	A1 to A3	Baa1 to Baa3	Ba1 to B3	Caa1 to C	Unrated
	S&P	AAA to AA-	A+ to A-	BBB+ to BBB-	BB+ to B-	CCC+ to D	Unrated
	Fitch	AAA to AA-	A+ to A-	BBB+ to BBB-	BB+ to B-	CCC+ to D	Unrated
	RAM	AAA to AA3	A1 to A3	BBB1 to BBB3	BB1 to B3	C1 to D	Unrated
	MARC	AAA to AA-	A+ to A-	BBB+ to BBB-	BB+ to B-	C+ to D	Unrated
	R&I	AAA to AA-	A+ to A-	BBB+ to BBB-	BB+ to B-	CCC+ to C	Unrated
Exposure Class		RM'000	RM'000	RM'000	RM'000	RM'000	RM'000
On and Off-Balance Sheet Exposures							
Banks, Development Financial Institutions & MDBs		1,435,245	427,402	1,426	–	–	95,551

6.0 CREDIT RISK (CONTINUED)

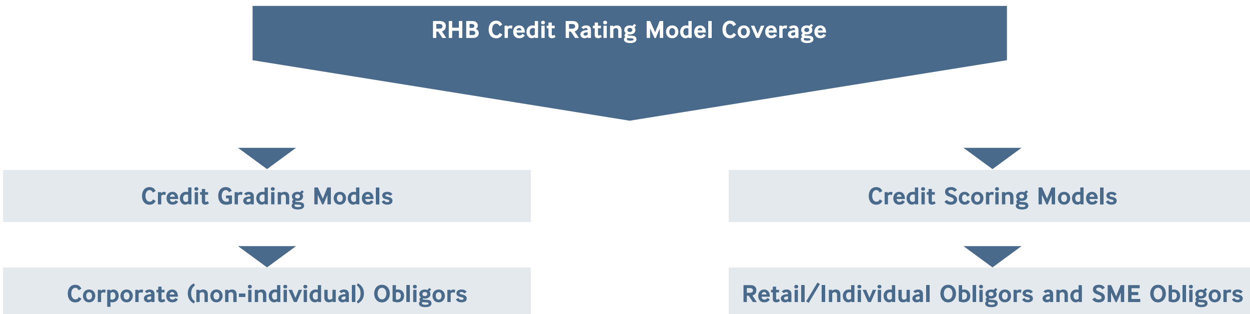
6.6 Internal Credit Rating Models

Internal credit rating models are an integral part of the Bank's credit risk management, decision-making process, and regulatory capital calculations. These internal credit rating models are developed by Group Risk Operations with active participation by the relevant credit experts from the Bank's functional units and/or business units.

Internal rating model development and implementation process have been established to govern the development and validation of rating models and the application of these models. Specifically, all newly developed models prior to implementation, material changes of the rating systems and validation results must be endorsed by GCRC, IRMC and approved by Board. All models are also subject to independent validation by the Model Validation Team before implementation to ensure that all aspects of the model development process have been satisfied. In addition, the models are also subject to annual review and independent validation by the Model Validation Team to ensure that they are performing as expected.

Credit risk/rating models can be broadly classified into:

- Credit Grading Models
- Credit Scoring Models



The credit grading models for corporate (or non-individual) obligors are used to risk rate the creditworthiness of the corporate obligors/guarantors/debt issuers based on their financial standing (such as gearing, expenses and profit) and qualitative aspects (such as management effectiveness and industry environment). Different rating models will be applied subject to the obligor's asset and sales volume to create further risk differentiation.

The credit scoring models are for large volume of exposures that are managed on a portfolio basis, which includes program financing for small and medium-sized enterprises (SMEs). These models are developed through statistical modelling and applied onto the portfolio accordingly. For portfolios where data are readily available or when more granular segmentation is required to support business strategy, more models will be developed and deployed.

6.0 CREDIT RISK (CONTINUED)

6.6 Internal Credit Rating Models (continued)

Application of Internal Ratings

The three components of expected loss, the PD, LGD and EAD are used in variety of applications that measure credit risk across the entire portfolio.

- Credit Approval : PD models are used in the credit approval process in both retail and non-retail portfolios. In high-volume retail portfolios, application scorecard and behaviour scorecard are used as one of the risk management tools.
- Policy : Policies are established to govern the use of ratings in credit decisions and monitoring as well as impairment.
- Reporting : Reports are generated to Senior Management on a monthly basis on the performance of the rating models to show the distribution of the credit exposures by risk rating and monitoring of their performance.
- Capital Management : The capital management and allocation plan takes into consideration the projected RWA computed based on internal rating.
- Risk Limits : The internal ratings are used in establishing the Group's various internal limits (such as industry risk limit).
- Risk Reward and Pricing : PD, EAD and LGD metrics are used to assess profitability of deals to allow for risk-informed pricing considerations and strategic decisions.

6.7 Credit Risk Monitoring and Control

Credit Risk Mitigation

The Bank generally does not grant credit facilities solely on the basis of collateral provided. All credit facilities are granted based on the credit standing of the customer, source of repayment/payment and debt/financing servicing ability.

Collateral is taken whenever possible to mitigate the credit risk assumed, subject to the Bank's policies that govern the eligibility of collateral used for credit risk mitigation. Reliance on collateral when taken is carefully assessed in the light of issues such as legal certainty and enforceability, market valuation and counterparty risk of the guarantor. Recognised collaterals where relevant, include both financial and physical assets. Financial collaterals include cash deposits, shares and unit trusts, while physical collateral includes land and buildings and vehicles. Apart from financial collateral and physical collateral, The Bank has defined standards on the acceptance of guarantors as credit risk mitigants.

Collateral is valued in accordance with the Bank's policy on collateral valuation, which prescribes the frequency of valuation for different collateral/securities types, based on liquidity and volatility of the collateral value and the underlying product or risk exposure. The value of collaterals/securities pledged is monitored periodically, analysed and updated concurrently with the annual/periodic renewal of facilities, as well as updated into the Bank's collateral system.

The Bank also accepts non-tangible securities as support, such as guarantees from individuals, corporates and institutions, bank guarantees, debenture and assignment of contract proceeds, subject to internal guidelines on eligibility. Currently, the Bank does not employ the use of derivative credit instruments and on-balance sheet netting to mitigate its financing exposures. Where possible, the Bank enters into International Swaps and Derivatives Association (ISDA) Master Agreement with its derivative and swap counterparties as the master agreement provides the legal certainty that the credit exposures between counterparties will be netted.

Equity securities or collaterals acquired arising from debt conversions are accounted for as disposal of the financing and acquisition of equity securities or investment properties. Any further impairment of the assets or business acquired is treated as impairment of the relevant asset or business rather than as impairment of the original instrument.

The Bank has established mechanism to monitor credit and market concentration within its credit mitigation.

6.0 CREDIT RISK (CONTINUED)

6.7 Credit Risk Monitoring and Control (continued)

The following tables show the credit risk mitigation of portfolios under the Standardised Approach as at 31 December 2017 compared with 31 December 2016:

Table 11a: Credit Risk Mitigation of Portfolios under the Standardised Approach as at 31 December 2017

RHB Islamic Bank Exposure Class	Gross Exposures Before Credit Risk Mitigation RM'000	Gross Exposures Covered by Guarantees/ Credit Derivatives RM'000	Gross Exposures Covered by Eligible Financial Collateral RM'000
On-Balance Sheet Exposures			
Sovereigns & Central Banks	5,317,479	–	–
Public Sector Entities	4,315,960	4,165,019	–
Banks, Development Financial Institutions & MDBs	2,959,428	25,257	–
Takaful Cos, Securities Firms & Fund Managers	283,629	–	2,342
Corporates	20,785,998	1,919,148	954,363
Regulatory Retail	13,492,830	118	569,780
Residential Mortgages	8,029,511	–	5,710
Higher Risk Assets	3,342	–	–
Other Assets	112,863	–	–
Defaulted Exposures	264,563	20,653	7,907
Total On-Balance Sheet Exposures	55,565,603	6,130,195	1,540,102
Off-Balance Sheet Exposures			
OTC Derivatives	866,940	–	–
Off-balance sheet exposures other than OTC derivatives or credit derivatives	3,987,740	628,250	122,165
Defaulted Exposures	1,794	–	65
Total Off-Balance Sheet Exposures	4,856,474	628,250	122,230
Total On and Off-Balance Sheet Exposures	60,422,077	6,758,445	1,662,332

6.0 CREDIT RISK (CONTINUED)

6.7 Credit Risk Monitoring and Control (continued)

Table 11b: Credit Risk Mitigation of Portfolios under the Standardised Approach as at 31 December 2016

RHB Islamic Bank Exposure Class	Gross Exposures Before Credit Risk Mitigation RM'000	Gross Exposures Covered by Guarantees/ Credit Derivatives RM'000	Gross Exposures Covered by Eligible Financial Collateral RM'000
On-Balance Sheet Exposures			
Sovereigns & Central Banks	7,599,391	–	–
Public Sector Entities	3,373,527	3,289,514	4,655
Banks, Development Financial Institutions & MDBs	1,649,807	4,927	–
Takaful Cos, Securities Firms & Fund Managers	279,341	–	–
Corporates	17,276,197	1,203,945	353,760
Regulatory Retail	13,299,274	3,887	116,368
Residential Mortgages	4,060,558	–	5,474
Higher Risk Assets	–	–	–
Other Assets	195,111	–	–
Defaulted Exposures	280,486	–	4,393
Total On-Balance Sheet Exposures	**48,013,692**	**4,502,273**	**484,650**
Off-Balance Sheet Exposures			
OTC Derivatives	752,161	–	–
Off-balance sheet exposures other than OTC derivatives or credit derivatives	2,618,936	516,667	24,382
Defaulted Exposures	1,873	–	–
Total Off-Balance Sheet Exposures	**3,372,970**	**516,667**	**24,382**
Total On and Off-Balance Sheet Exposures	**51,386,662**	**5,018,940**	**509,032**

6.0 CREDIT RISK (CONTINUED)

6.7 Credit Risk Monitoring and Control (continued)

Credit Concentration Risk

Risk concentration refers to an exposure with the potential to produce losses that are substantial enough to threaten the financial condition of a banking institution. Risk concentrations can materialise from excessive exposures to a single counterparty or group of connected counterparties, a particular instrument or a particular market segment.

The Bank manages the diversification of its portfolio to avoid undue credit concentration risk. Credit concentration risk exists in financing to single customer groups, customers engaged in similar activities, or diverse groups of customers that could be affected by similar economic or other factors. To manage this concentration risk, exposure limits are established for single financing groups and industry segments. Analysis of any single large exposure and group of exposures is regularly conducted and the financing units undertake regular account updates, monitoring and management of these exposures.

Industry and sector-specific analysis are also incorporated within the overall credit risk management regiment. In this respect, the Bank seeks to continually update financing guidelines based on periodic reviews and updates of industry and sector risk factors and economic outlook. This facilitates better management of credit concentration risk.

Credit Monitoring and Annual Reviews

The Bank regularly monitors credit exposures, portfolio performance, and external trends which may impact risk management outcomes. Internal risk management reports are generated for Senior Management, GCRC, IRMC and Board, containing information on key environmental, political and economic trends across portfolios and countries, portfolio delinquency with major credit delinquency, and financing impairment performance.

In addition to the on-going qualitative assessment by the account relationship managers, reviews are conducted at least once a year with updated information on the customer's financial position, market position, industry and economic condition and account conduct. Specific financings may be reviewed more frequently under appropriate circumstances. Such circumstances may arise if, for instance, the Bank believes that heightened risk exists in a particular industry, or the customer exhibits early warning signals such as defaulted on obligations to suppliers or other financial institutions or is facing cash flow or other difficulties.

Within Group Risk & Credit Management, there is a mechanism in place for credit monitoring to flag-out problematic financing (watch list accounts) for intensive monitoring under Enhanced Account Management (EAM). These are accounts which may be exhibiting early distress patterns or in the early stages of delinquency but not yet in default.

For these cases, Watchlist Credit Management department will work closely with the Area Account Relationship Managers (ARMs) to rehabilitate the accounts after discussion with the customer to determine the root cause of the problem and this may result in rescheduling, restructuring or "exit relationship" strategies to be applied. For the larger accounts, regular position update meetings are held with ARMs to review or revise these strategies. The EAM guidelines are refined from time to time, to better identify, monitor and resolve such accounts. Dedicated teams are established (at business units as well as credit evaluation) to conduct independent assessment and to manage the watch list portfolios. These teams are tasked with identifying and implementing strategies to address business relationships under EAM.

Group Internal Audit conducts independent post-approval reviews on a sampling basis to ensure that the quality of credit appraisals and approval standards is in accordance with the credit underwriting standards and financing policies established by the Bank's management, and relevant laws and regulations.

6.0 CREDIT RISK (CONTINUED)

6.8 Impairment Allowances for Financing

The Bank adopts BNM's guidelines on Classification and Impairment Provisions for Financing. The principles in this guidelines are in line with those applicable under the International Financial Reporting Standards compliant framework, the Malaysian Financial Reporting Standards 139.

The customer assessed under Impairment Allowances (IA) shall be classified as impaired under any one of the following situations:

1. When the principal or profit or both, of any facility(s) of the customer is past due for more than 90 days or 3 months.
2. In the case of revolving facilities (eg overdraft facilities), the customer of the facility shall be classified as impaired where the outstanding amount has remained in excess of the approved limit for a period of more than 90 days or 3 months.
3. Where the amount is past due or the outstanding amount has been in excess of the approved limit for 90 days or 3 months or less, the financing exhibits weaknesses (refer to impairment triggers) that would render it to be classified as impaired.
4. Where repayments/payments of the financing are scheduled on intervals of 3 months or longer, the customer is classified as impaired as soon as a default occurs, unless the customer or the financing does not exhibit any weakness (refer to impairment triggers) that would render it to be classified as impaired.
5. Upon occurrence of any one or more Mandatory Status Triggers (MSTs) or any two or more Ancillary Status Triggers (ASTs). These MSTs and ASTs are pre-defined trigger events approved by the Bank to facilitate impairment classification.

Note:

For R&R facilities, the customer shall be classified as impaired in accordance with paras 1 to 4 above based on the revised or restructured terms.

Individual Assessment – Impairment Triggers

For customers (with threshold of RM5 million and above per customer) under individual assessment, the Bank performs impairment assessment when any one of the MSTs or any two of the ASTs events occurred. Consequently, these customers will be classified as impaired even though no impairment allowance may be required after impairment assessment.

Individual Impairment Allowances

Customers under individual assessment and triggered either by any one of the MSTs or any two of the ASTs will be classified as impaired. Consequently, impairment assessment is to be carried out on these impaired customers, based on reasonable and well documented estimates of the future cashflows/realisations of collateral that is expected to be recovered from the impaired customers ie. net present value of future cashflows are discounted based on original effective profit rates and compared against carrying amount. Any impairment on the shortfalls will be provided in full immediately.

Collective Impairment Allowances

Collective impairment applies to all other accounts (impaired and non-impaired) that do not fall within the threshold of individual assessment. The impairment assessment for accounts under collective assessment are as follows:

1. Segmentation is applied to group of financing, both impaired and non-impaired, based on similar credit risk characteristics, for the purpose of assessing impairment and computing historical default rates and loss rates.
2. PD model is established with standard loss identification period (by months) and Point of No Return (by months in arrears). PD model adopted could either be migration analysis model or flow rate model. The approaches to migration analysis model could be either by way of outstanding balances or number of accounts.
3. LGD model establishes loss rate at the point in time when the loss event occurred ie, based on actual incurred loss model.

6.0 CREDIT RISK (CONTINUED)

6.8 Impairment Allowances for Financing (continued)

Re-classification and Recovery of Impaired Customers

An impaired customer may be re-classified as a non-impaired status under the following situations:

1. When the financing repayment/payment of the impaired customer has improved with the principal or profit or both, of its facilities with the Bank being past due by 90 days or 3 months or less.
2. In the case of revolving facilities (eg overdraft facilities), the facility shall be re-classified as non-impaired where the overdue outstanding amount in excess of the approved limit has improved to 90 days or 3 months.
3. Where repayments/payments of the financings are scheduled on intervals of 3 months or longer, the financing is re-classified as non-impaired as soon as the overdue scheduled repayments/payments are settled.

Write-Off of Impaired Financing

All financing that satisfy any one of the following criteria, may be recommended for write-off:

1. Deemed irrecoverable, worthless and with slim prospect of recovery.
2. Waiver/discount already given under approved composite settlement schemes.
3. Abandoned project with no sign of revival. The definition of abandoned project must be in compliance with the definition stated under valuation for abandoned projects.
4. For retail and scored financing, the write off may be expedited for those with ageing of 12 months and above, provided legal action has reached at least writ of summon filed.
5. In the case of credit card and unsecured personal financing, aging is 6 months and above and the write-off is automatic.

Partial write-offs of impaired financing is permitted for the shortfall portion in outstanding balance over the security value which is uncollectible and worthless; and the Bank is in the final stage of realising the security/collateral; or in the case of approved composite settlement arrangement, the waiver portion. Further shortfall if any, arising from the disposal of all securities and upon receipt of the sale proceeds, shall be written off immediately.

This policy of impairment financing write-off is intended to provide a timely and consistent methodology for financing to be written-off and to reflect the true value of assets in the Bank's books.

For year 2017 and 2016 respectively, all impaired, past due and allowances for impaired financing are for credit exposures booked in Malaysia.

6.0 CREDIT RISK (CONTINUED)

6.8 Impairment Allowances for Financing (continued)

The following tables show the Bank's impaired and past due financing and allowances by industry sector as at 31 December 2017 compared with 31 December 2016:

Table 12a: Impaired and Past Due Financing and Allowances for Impairment by Industry Sector as at 31 December 2017

RHB Islamic Bank Industry Sector	Impaired Financing RM'000	Past Due Financing RM'000	Individual Impairment Allowances RM'000	Collective Impairment Allowances RM'000
Agriculture	**304**	**1,644**	**–**	**9,797**
Mining & Quarrying	**530**	**552**	**–**	**875**
Manufacturing	**22,380**	**18,559**	**834**	**20,369**
Electricity, Gas & Water Supply	**29,822**	**39**	**–**	**1,312**
Construction	**40,724**	**16,869**	**13,164**	**22,685**
Wholesale, Retail Trade, Restaurants & Hotels	**54,481**	**10,949**	**28,337**	**38,604**
Transport, Storage & Communication	**9,391**	**1,386**	**–**	**10,534**
Finance, Takaful, Real Estate & Business	**10,072**	**10,065**	**–**	**33,671**
Education, Health & Others	**3,800**	**1,606,926**	**277**	**8,312**
Household	**172,457**	**1,883,891**	**–**	**81,926**
Others	**–**	**1**	**–**	**1,960**
Total	**343,961**	**3,550,881**	**42,612**	**230,045**

Table 12b: Impaired and Past Due Financing and Allowances for Impairment by Industry Sector as at 31 December 2016

RHB Islamic Bank Industry Sector	Impaired Financing RM'000	Past Due Financing RM'000	Individual Impairment Allowances RM'000	Collective Impairment Allowances RM'000
Agriculture	324	1,173	–	8,867
Mining & Quarrying	–	20	–	888
Manufacturing	22,105	12,169	–	24,194
Electricity, Gas & Water Supply	4,771	63	–	1,786
Construction	38,843	14,305	9,362	20,601
Wholesale, Retail Trade, Restaurants & Hotels	48,334	9,614	3,692	30,809
Transport, Storage & Communication	2,094	3,115	–	14,964
Finance, Takaful, Real Estate & Business	42,664	29,502	–	35,169
Education, Health & Others	11,568	1,103,312	2,810	7,178
Household	222,393	3,352,927	–	92,069
Others	–	–	–	–
Total	**393,096**	**4,526,200**	**15,864**	**236,525**

Note: All impaired, past due and allowances for impaired financing are for credit exposures booked in Malaysia.

6.0 CREDIT RISK (CONTINUED)

6.8 Impairment Allowances for Financing (continued)

The following table shows the charges/(write-back) and write-offs for impairment by industry sector as at 31 December 2017 compared with 31 December 2016:

Table 13: Net Charges/(Write-back) and Write-Offs for Impairment by Industry Sector

RHB Islamic Bank	Twelve Months Period Ended 2017		Twelve Months Period Ended 2016	
Industry Sector	Net Charges/ (Write-back) for Individual Impairment Allowances RM'000	Write-Offs RM'000	Net Charges/ (Write-back) for Individual Impairment Allowances RM'000	Write-Offs RM'000
Agriculture	–	–	–	–
Mining & Quarrying	–	–	–	–
Manufacturing	834	5,526	(458)	5,850
Electricity, Gas & Water Supply	–	–	–	–
Construction	3,802	936	(877)	223
Wholesale, Retail Trade, Restaurants & Hotels	27,060	3,975	(1,521)	3,938
Transport, Storage & Communication	–	–	–	–
Finance, Takaful, Real Estate & Business	–	1,560	–	–
Education, Health & Others	(2,492)	150	(582)	–
Household	–	32,715	–	32,132
Others	–	1,636	–	2,234
Total	**29,204**	**46,498**	**(3,438)**	**44,377**

6.0 CREDIT RISK (CONTINUED)

6.8 Impairment Allowances for Financing (continued)

The following tables show the reconciliation of changes to financing impairment allowances as at 31 December 2017 compared with 31 December 2016:

Table 14: Reconciliation of Changes to Financing Impairment Allowances

RHB Islamic Bank	2017 RM'000	2016 RM'000
Individual Impairment Allowance		
Balance as at the beginning of financial year	**15,864**	22,649
Net allowance/(written back) made during the year	**29,204**	(3,438)
Amount written off	**(2,456)**	(3,347)
Balance as at the end of financial year	**42,612**	**15,864**

RHB Islamic Bank	2017 RM'000	2016 RM'000
Collective Impairment Allowance		
Balance as at the beginning of financial year	**236,525**	199,653
Net allowance/(written back) made during the year	**37,562**	77,902
Amount written off	**(44,042)**	(41,030)
Balance as at the end of financial year	**230,045**	**236,525**

7.0 MARKET RISK

Market risk is the risk of loss arising from adverse movements in market indicators, such as profit rates, credit spreads, equity prices, currency exchange rates and commodity prices.

The Bank transacts financial instruments such as debt papers and financial derivative instruments. Derivative instruments are contracts whose characteristics and value are derived from the underlying instruments that can be a reference to profit rates, exchange rates, debt paper, or equity and indices. These include futures, forwards, swaps, and options transactions.

The Bank has an established Group Trading Book Policy Statement as guidance for market risk management. This is reviewed regularly and/or upon change in significant event that has a material impact on policy compliance or regulatory changes.

The Group Asset and Liability Committee (Group ALCO) and GCRC perform a critical role in the management of market risk and supports the IRMC in the overall market risk management. Both committees meet regularly and is the forum where strategic and tactical decisions are made for the management of market risk; this includes the development of the Bank's market risk strategy, market risk management structure and the policies as well as measurement techniques to be put in place.

The Group Market Risk Management within Group Risk Management is the working level that forms a centralised function to support Senior Management to operationalise the processes and methods, to ensure adequate risk control and oversight are in place.

Market Risk Assessment

The Bank applies risk monitoring and assessment tools to measure trading book positions and market risk factors. Statistical and non-statistical risk assessment tools applied include Value-at-Risk (VaR), sensitivity analysis and stress testing.

The Bank adopts a systematic approach in managing these risks by types of instruments and nature of exposure. Market risk is primarily monitored and controlled via a structure of limits and triggers ie cut loss, VaR, trading and notional limit set in accordance with the size of positions and risk tolerance appetites.

In addition, the Bank conducts periodic stress testing of its respective portfolios to ascertain market risk under abnormal market conditions.

Market Risk Monitoring and Reporting

For effective control of market risk, defined management action triggers and risk limits are established and actively monitored. Only authorised trading activities may be undertaken by the specific business units within the allocated limits. All trading positions are monitored independently on a daily basis and in accordance to the established escalation procedures and the key actions to be undertaken.

Hedging Activities

Hedging activities designated for hedge accounting are governed by the Group's Hedging Policy that prescribes the overall hedge activities that can be executed by the Bank and the subsequent control procedures such as effectiveness measurement and reporting to Group ALCO.

Hedging instruments used to mitigate these risks include derivatives such as options, futures, forwards and swaps that are approved by the Board. Execution of the hedging is carried out by the relevant division through the Bank's treasury functions with the approval of Group ALCO.

7.0 MARKET RISK (CONTINUED)

Capital Treatment for Market Risk

The Bank applies the Standardised Approach to calculate market risk capital requirements in accordance with BNM's Guideline. The market risk-weighted assets and the corresponding capital requirements for the Bank as at 31 December 2017 and 31 December 2016 are shown in the tables below:

Table 15a: Market Risk-Weighted Assets and Minimum Capital Requirements as at 31 December 2017

RHB Islamic Bank Market Risk	Long Position RM'000	Short Position RM'000	Risk-Weighted Assets RM'000	Minimum Capital Requirements RM'000
Profit Rate Risk	**9,548,359**	**9,373,985**	**199,064**	**15,925**
Foreign Currency Risk	**41,624**	**25,128**	**41,624**	**3,330**
Total			**240,688**	**19,255**

Table 15b: Market Risk-Weighted Assets and Minimum Capital Requirements as at 31 December 2016

RHB Islamic Bank Market Risk	Long Position RM'000	Short Position RM'000	Risk-Weighted Assets RM'000	Minimum Capital Requirements RM'000
Profit Rate Risk	248,081	238,572	10,793	863
Foreign Currency Risk	44,311	52,633	52,633	4,211
Total			**63,426**	**5,074**

Note:

For year 2017 and year 2016, RHB Islamic Bank did not have any exposure under
- equity risk, commodity risk, inventory risk and options risk, and
- market risk exposure absorbed by PSIA.

8.0 LIQUIDITY RISK

Liquidity risk is the risk of the Group being unable to maintain sufficient liquid assets to meet its financial commitments and obligations when they fall due and transact at a reasonable cost. Liquidity risk also arises from the inability to manage unplanned decreases or changes in funding sources.

There are two types of liquidity risk, namely funding liquidity and market liquidity risk. Funding liquidity risk is the risk that the Group is unable to meet efficiently both expected and unexpected current and future cash flow and collateral needs without affecting either daily operations or the financial condition of the Group. Market liquidity risk is the risk that the Group cannot easily offset or eliminate a position at the market price because of inadequate market depth or market disruption.

The primary role of a bank in terms of financial intermediation is the transformation of short-term deposits into long-term financing. By fulfilling the role of maturity transformation, banks are inherently susceptible to liquidity mismatches and consequently funding and market liquidity risk.

Through the Group's Liquidity Risk Policy, the Bank manages the funding and market liquidity risk to ensure that banking operations continue uninterrupted under normal and stressed conditions. The key objective that underpins the Group's Liquidity Risk Policy includes maintaining financial market confidence at all times, protecting key stakeholders' interests and meeting regulatory liquidity requirements.

The Group ALCO supports the IRMC by performing the critical role in the management of liquidity risk, and is responsible for establishing strategies that assist in controlling and reducing any potential exposure to liquidity risk. The Group ALCO meets regularly and is the forum where strategic and tactical decisions are made for the management of liquidity risk and the Bank's balance sheet profile. Global and domestic economic data, information and events are deliberated at the Group ALCO meetings which enables the Bank to determine its actions and reactions in the capital markets. The Group ALCO is also the governance body which sets profit rates for liabilities products as well as reference rates for financing products and services. Group ALCO is supported by Group Asset and Liability Management (Group ALM) at the working level. Group ALM monitors liquidity risk limits/Management Action Triggers (MATs) and reports to Group ALCO the liquidity risk profile on monthly basis.

The liquidity management process involves establishing liquidity management policies and limits, regular monitoring against liquidity risk limits, regular stress testing, and establishing contingency funding plans. These processes are subject to regular reviews to ensure that they remain relevant in the context of prevailing market conditions. Some of the key liquidity risk management tools are top depositors' mixture, funding source mixture, maturity profile of funding sources, and contingency funding lines.

The Bank has adopted the BNM's liquidity standards on Liquidity Coverage Ratio, to ensure maintenance of adequate stock of unencumbered high-quality liquid assets to survive the liquidity needs for 30 calendar days under liquidity stress condition. The Bank continues to report NSFR under the Basel III observation reporting to BNM.

The Group's Liquidity Incident Management Procedure establishes guidelines for managing liquidity crisis, identifying early warning signs of a possible liquidity event and the need for heightened liquidity risk monitoring and reduced liquidity risk exposure. In addition, it also identifies the individuals responsible for formulating and executing the Bank's response to a liquidity event.

9.0 RATE OF RETURN RISK IN THE BANKING BOOK

Rate of return risk in the banking book refers to the risk of the Group's earnings and economic value of equity due to the adverse movements in benchmark rate. The risk may arise from the mismatches in the timing of repricing of assets and liabilities from both on and off-balance sheet positions in the banking book, changes in slope and shape of the yield curve, basis risk and optionality risk.

Rate of return risk in the banking book comprises:

- Re-pricing risk (mismatch risk) – Arises from timing differences in the maturity (for fixed-rate) and re-pricing (for floating-rate) of bank assets, liabilities, and off-balance sheet positions. While such re-pricing mismatches are fundamental to the business of banking, they can expose a bank's income and underlying economic value to unanticipated fluctuations as benchmark rates vary;
- Basis risk – Arises from imperfect correlation in the adjustment of the rates earned and paid on different instruments with otherwise similar re-pricing characteristics. When benchmark rates change, these differences can give rise to unexpected changes in the cash flows and earnings spread between assets, liabilities and off-balance sheet instruments of similar maturities or re-pricing frequencies;
- Yield curve risk – Arises when unanticipated shifts of the yield curve have adverse effects on the Bank's income or underlying economic value; and
- Embedded optionality risk – Arises primarily from options that are embedded in many banking book positions (eg some fixed rate home financing products give customers the option to prepay the financing early without penalty, call deposit, where customers have the option of withdrawing the deposit funds at any time).

Earnings-at-Risk (EaR) and Economic Value of Equity (EVE) are used to assess rate of return risk in the banking book. They are computed based on the re-pricing gap profile of the banking book using BNM's standard template. Assets and liabilities are bucketed based on their remaining tenure to maturity or next re-price dates. The measurement of EaR and EVE is conducted on a monthly basis.

The Group ALCO supports IRMC in establishing policies, strategies and limits for the management of balance sheet risk exposure. The Group ALM within Group Risk Management supports the Group ALCO in the monthly monitoring and reporting of the rate of return risk profile of the banking book. The primary objective in managing balance sheet risk is to manage the net profit income and economic value of equity, as well as to ensure rate of return risk exposures in the banking book are maintained within defined risk tolerances.

In addition, the Group ALM Policy is established to provide the governance of rate of return risk in the banking book. Benchmark rate sensitivity triggers are applied on earnings for the respective profit centres within the Group. The Group regularly considers the economics and necessity of increasing or reducing its rate of return risk hedges.

In line with the Group ALM Policy to achieve a balance between profitability from banking activities and minimising risk to earnings and capital from changes in benchmark rates, rate of return risk to earnings is controlled using MATs and identified escalation procedures.

Stress testing is also performed regularly to determine the adequacy of capital in meeting the impact of extreme benchmark rate movements on the balance sheet. Such tests are also performed to provide early warnings of potential extreme losses, facilitating proactive management of rate of return risk in the banking book in an environment of rapid financial market changes.

9.0 RATE OF RETURN RISK IN THE BANKING BOOK (CONTINUED)

The impact of changes in benchmark rates to net earnings and economic value as at 31 December 2017 and 31 December 2016 are shown in the following tables:

Table 16a: Rate of Return Risk in the Banking Book as at 31 December 2017

RHB Islamic Bank	Impact on Position as at Reporting Period (100 basis points) Parallel Shift			
	Increase/(Decline) in Earnings		Increase/(Decline) in Economic Value	
Currency	Impact based on +100 basis points RM'000	Impact based on -100 basis points RM'000	Impact based on +100 basis points RM'000	Impact based on -100 basis points RM'000
MYR – Malaysian Ringgit	**51,022**	**(51,022)**	**(229,533)**	**229,533**
USD – US Dollar	**5,859**	**(5,859)**	**1,667**	**(1,667)**
Others[1]	**(945)**	**945**	**177**	**(177)**
Total	**55,936**	**(55,936)**	**(227,689)**	**227,689**

Table 16b: Rate of Return Risk in the Banking Book as at 31 December 2016

RHB Islamic Bank	Impact on Position as at Reporting Period (100 basis points) Parallel Shift			
	Increase/(Decline) in Earnings		Increase/(Decline) in Economic Value	
Currency	Impact based on +100 basis points RM'000	Impact based on -100 basis points RM'000	Impact based on +100 basis points RM'000	Impact based on -100 basis points RM'000
MYR – Malaysian Ringgit	(4,173)	4,173	(335,841)	335,841
USD – US Dollar	1,122	(1,122)	367	(367)
Others[1]	(400)	400	201	(201)
Total	**(3,451)**	**3,451**	**(335,273)**	**335,273**

Note:

1. Inclusive of GBP, EUR, SGD, etc
2. The EaR and EVE exposures are additive and do not take into account any correlation impact in the aggregation.
3. The earnings and economic values were computed based on the standardised approach adopted by BNM.
4. PSIA (Profit Sharing Investment Account) between RHB Islamic and RHB Bank which qualifies as a risk absorbent, is excluded from the computation of rate of return risk.

9.0 RATE OF RETURN RISK IN THE BANKING BOOK (CONTINUED)

The impact to net earnings above represents financial assets and liabilities that have been prepared on the following basis:

- Benchmark rate sensitive assets and liabilities with residual maturity or re-pricing tenure of up to one year that is not captured in the trading portfolio are slotted into time bands based on the maturity or re-pricing tenure whichever is earlier.
- A set of risk weights with its respective time band is used to project the applicable basis point benchmark rate change impact.
- For assets and liabilities with non-fix maturity, eg, current and savings accounts, certain assumptions are made to reflect the actual sensitivity behaviour of benchmark rate bearing items.

Economic value is characterised by the impact of benchmark rates changes on the value of all net cash flows, ie, the effect on the economic value of the Group's assets, liabilities and off-balance sheet positions. This provides a more comprehensive view of the potential long-term effects of changes in benchmark rates than is offered by the earnings perspective. The scenarios used are based on the assumption that all key variables for all maturities move at the same time and by the same magnitude and do not incorporate actions that would be otherwise taken by the business units and risk management to mitigate the effect of this movement in key variables.

10.0 OPERATIONAL RISK

Operational risk is the risk of loss resulting from inadequate or failed internal processes, people, systems and/or external events, which also includes IT, legal and Shariah non-compliance risk but excludes strategic and reputational risk. Operational risk is inherent in the Bank's operations and can never be eliminated entirely. The impact can be in the form of actual financial loss as well as non-financial loss such as loss of reputation, non-compliance and unsatisfactory service level to customers.

One of the Bank's primary safeguards against operational risk is the existence of a sound internal control system, based on the principle of dual control checks and balances, segregation of duties, independent checks and verification processes, and a segmented system access control and authorisation process. These controls are documented through a set of policies and procedures at the respective business and operation level.

The Group's Operational Risk Management Framework comprises a wide range of activities and elements, broadly classified into:

- Analysis and Enhancement – The Group has implemented a Basel II compliant operational risk management system to support its workflow and analytical capabilities.
- Education and Awareness – The Group undertakes change management activities to improve risk management knowledge, culture and practices of the Bank personnel. This is aligned with the principle and requirement that the front-line business and support units of the Group, are by nature of their direct involvement in interfacing with customers and in operating the business, responsible for managing operational risk and acting as the first line of defence.
- Monitoring and Intervention – This is where the principal head office risk control units, including the risk management function, compliance function and the internal audit function, actively manage operational non-compliances and incidences as a second and third line of defence respectively. The second line of defence also undertakes recovery actions, including business continuity measures in cases of incidents causing disruption to business activities.

10.0 OPERATIONAL RISK (CONTINUED)

Operational Risk Management Function and Organisation

The Group Operational Risk Management within Group Risk Management has functional responsibility for the development of operational risk framework, policy and methodologies, and providing guidance and information to the business units on operational risk areas. Its responsibility also includes generating a broader understanding and awareness of operational risk issues at all levels in the Group.

It also ensures that operational risks from new products, processes and systems are adequately managed and mitigated.

The respective business units are primarily responsible for managing operational risk on a day-to-day basis.

Regular operational risk reporting is made to the Senior Management, the GCRC, IRMC and the Board. These reports include various operational risk information such as risk analysis, risk mitigation action plans, risk tools outcomes, risk appetite breaches, significant operational risk events and control failures, and lessons learnt. In addition, key operational risk incidents are reported to senior management daily. Such reporting enables Senior Management to identify adverse operational lapses, take prompt corrective actions, and ensure appropriate risk mitigation decision making and action plans.

Operational Risk Management Processes and Tools

The Bank applies a defined operational risk management process in managing operational risk to enable an institutional and transparent operational risk management practice. The five (5) processes are as follows:

1. Establish the context;
2. Risk identification;
3. Risk analysis;
4. Risk mitigating; and
5. Risk monitoring

The Bank uses relevant operational risk tools and methodologies to support and ensure an effective operational risk management process. The following tools are being used:

- **Risk and Control Self-Assessment (RCSA)**

  RCSA is a methodology to build risk profile for each business and support unit. RCSA sets out a structured process for the identification and assessment of inherent operational risk, the effectiveness of the control environment, and the adequacy of the risk mitigation in place. The RCSA process is facilitated by the business and support units themselves jointly with personnel from Group Operational Risk Management.

- **Key Risk Indicators (KRI)**

  KRI is a measurable indicator utilised to track and monitor key operational risk exposures. KRI serves as an early warning signal; once a risk indicator exceeds the predefined threshold, a warning message is sent to a predefined list of users. Business and support units are required to monitor their risk exposures via KRIs and are required to develop specific and concrete plans to address those where indicators are unfavourable. KRIs are embedded into critical processes to provide early warning signals of increasing risk and/or control failures by flagging up frequencies of events as a mechanism for continuous risk assessment and monitoring.

10.0 OPERATIONAL RISK (CONTINUED)

Operational Risk Management Processes and Tools (continued)

- **Key Control Testing (KCT)**

  KCT is a methodology to assist business/functional units in performing assessments periodically to determine the effectiveness of key controls by evaluating whether the control procedures/activities are adequately designed to achieve the goals of the function and control objectives; and testing whether the key controls are operating as intended in actual practice. Effective KCT can lead to early detection of control weakness and deficiencies which will assist the senior management and business/functional units to quickly focus on control weakness and take concentrated efforts where they are most needed.

- **Incident Management and Loss Data Collection (IMLDC)**

  IMLDC provides structured process for the management of operational risk incidents that have occurred, from the point of discovery until resolution. Business and functional units are required to report all incidences within defined reporting timeline operational losses for further analysis of root cause to avoid further recurrence. This is also useful for reviewing the effectiveness of the RCSA and KRIs.

Risk Mitigation and Controls

Risk mitigation strategies are used to minimise risk to an acceptable level and aim to decrease the likelihood of an undesirable event and the impact on the business, should it occur. The control tools and techniques, amongst others, are as follows:

- **Strengthening internal controls**

  Internal controls are designed to commensurate operational risk exposures faced by the Group. It is mainly categorised into five components, namely:

  a. Control environment – management oversight and risk culture, which sets the tone and serves as a foundation for all other components;

  b. Risk assessment – analyses identified risks to achieve objectives and ensure risks are well managed;

  c. Control activities – policies and procedures implemented manually and/or system-based to ensure management's directives are executed effectively and efficiently;

  d. Information and communication – relevant operational risk information are captured and communicated accordingly for decision making. Such information must be effective for utilisation, delivered timely, confidentiality is preserved, conform integrity needs, comply with relevant law/regulations, sufficient availability and reliable; and

  e. Monitoring – ongoing assessment and correcting deficiencies of internal control to assure it is operating as intended.

- **Business Continuity Management**

  To mitigate the impact of unforeseen operational risk events, the Bank has on-going and actively managed Business Continuity Planning (BCP) programmes for its major critical business operations and activities at the Head Office, data centre, and branches' locations. The BCP programmes are subject to regular testing to ensure efficacy, reliability and functionality, and come under the responsibility of the Group Business Continuity Management Department.

  The Board of Directors has an oversight function through the BRC and GMC. The Group Business Continuity Steering Committee (GBCSC) is the committee that oversees the Bank's business continuity framework, policies, budget and plans. The GBCSC reports to the GCRC.

10.0 OPERATIONAL RISK (CONTINUED)

Risk Mitigation and Controls (continued)

- **Outsourcing**

  With the increasing need to outsource for cost and operational efficiency, the Group's Policy on Outsourcing of Operations and Services ensures that the risk arising from outsourcing activities is adequately identified, assessed and managed prior to entering into any new arrangements and on an on-going basis.

- **Takaful Management**

  The Bank considers risk transfer by means of Takaful to mitigate operational risk. The Bank has a programme of Takaful designed to reduce its exposure to liability and to protect its assets. The Bank purchases Takaful from leading Takaful providers in the market covering fraud, theft, property and casualty, business disruption, liability and other risks for which it may be held responsible. These are provided by third-party Takaful providers and will financially mitigate the economic consequences of risks.

Technology Risk

Technology Risk refers to the business risk associated with the use, ownership, operation, involvement, influence and adoption of IT within an enterprise.

The Bank recognises the risk arising from the advancement and reliance upon information technology to support business operations through the deployment of advance technology and online systems to provide customers with convenient and reliable products and services. The Group's Technology Risk Management Framework ensures that a governance structure is in place for the identification, assessment and management of technology risks within existing IT operations as well as prior to deployment of applications and systems for internal as well as external customers.

New Product and Services Approval Process

The Group has established a Policy on Product Development and Approval and Guidelines on Introduction of New/Variation of Products & Services Lifecycle which governs the risk management of new products, services, or significant changes thereto. The responsible units have a duty to assess the operational risk for new product launches and/or significant changes in product features or related processes and working systems, as well as to ensure that operational risk is at an acceptable level at all times.

Legal Risk

Legal risk is part of operational risk. It can arise from unenforceable, unfavourable, defective or unintended contracts; lawsuits or claims; developments in laws and regulations, or non-compliance with applicable laws and regulations. Business units work together with the Bank's legal counsel and external legal counsel to ensure that legal risk is effectively managed.

Capital Treatment for Operational Risk

Currently, the Bank adopts the Basic Indicator Approach for the calculation of regulatory operational risk capital requirements. The operational risk-weighted assets and the corresponding capital requirements for the Bank as at 31 December 2017 and 31 December 2016, are shown below:

10.0 OPERATIONAL RISK (CONTINUED)

Capital Treatment for Operational Risk (continued)

Table 17: Operational Risk-Weighted Assets and Minimum Capital Requirements

	RHB Islamic Bank	
Operational Risk	**2017 RM'000**	**2016 RM'000**
Risk-Weighted Assets	**1,397,487**	1,200,381
Minimum Capital Requirements	**111,799**	96,030

11.0 COUNTRY CROSS-BORDER RISK

Country cross-border risk is the risk that the Bank will be unable to obtain payment from customers or third-parties on their contractual obligations as a result of certain actions taken by foreign governments.

Cross-border assets comprise financing and advances, profit bearing deposits/placements with other banks, trade and other bills, acceptances, derivatives, certificates of deposit and other negotiable instruments, investment securities and other formal commitments where the counterparty is resident in a country other than where the assets are recorded. Cross-border assets also include exposures to local residents denominated in currencies other than the local currency.

The Bank is guided by the Group Guidance on Cross-Border Business, particularly on ethics in business practices, key success factors in managing such business, and the internal control measures which are essential to provide adequate protection to its customers as well as the Bank's interest, thus reducing the risks associated with business activities.

12.0 REPUTATIONAL RISK

Reputational risk is defined as the risk that negative publicity regarding the conduct of the Bank or any of the entities within the Group, and its business practices or associations, whether true or not, will adversely affect its revenues, operations or customer base, or require costly litigation or other defensive measures. It also undermines public confidence in the Group, affecting the share price.

Reputational risk in the Group is managed and controlled through codes of conduct, governance practices and risk management practices, policies, procedures and training. The Group has developed and implemented a reputational risk management policy. The key elements in the management of reputational risk include:

- Practicing good corporate governance and culture of integrity to promote execution and achievement of corporate strategies and business objective.
- Manage reputational risk within a very low risk appetite with zero tolerance level reporting approach for incident that affects the Group's reputation.
- Adopt sound risk management practices that include the practice of building "reputation capital" and earning the goodwill of key stakeholder.
- Maintaining proper mechanisms to monitor and escalate material lapses/breaches of internal and regulatory policies/guidelines that may place the Group's reputation at risk.
- Maintaining proper channels of communication in dealing with internal and external stakeholders.

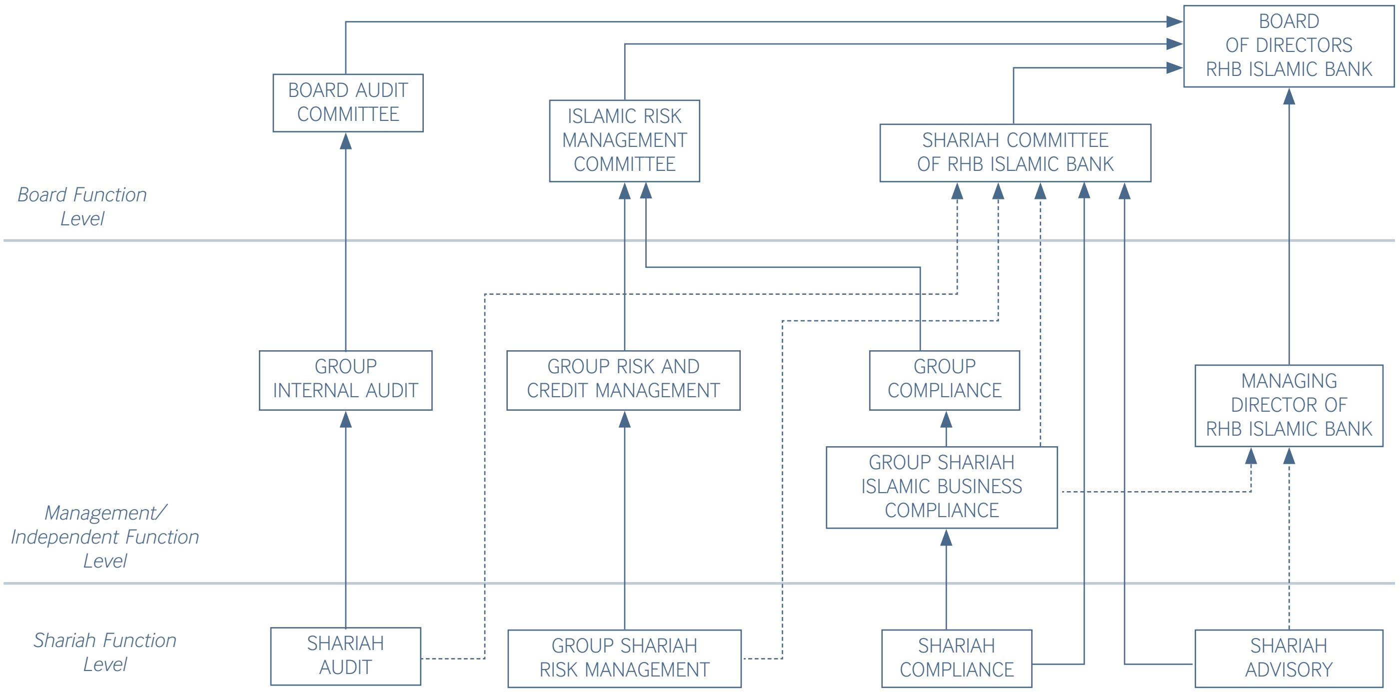
13.0 SHARIAH NON-COMPLIANCE RISK AND GOVERNANCE

Shariah non-compliance risk is the risk of loss arising from the failure to comply with the Shariah rules and principles as determined by the Shariah Committee of RHB Islamic Bank or any other relevant body, such as BNM's Shariah Advisory Council.

A Shariah Governance Framework has been developed with the objective of governing the entire Shariah compliance process within Islamic banking operations, and to:

- Ensure that the planning, development, and implementation of the Islamic Bank's products, services and conduct of business are in accordance with Shariah principles;
- Ensure that the Bank's operations do not contravene any of the Shariah principles and authorities' regulations related to the Shariah; and
- Act as a guide on the Bank's expectations to all personnel engaged in the Bank's activities; to ensure that all such functions are based on the Shariah principles, practices and prudence.

The reporting structure of Shariah governance is as follows:



The Shariah Committee of RHB Islamic Bank (SCR) was established under BNM's Shariah Governance Framework.

The main duties and responsibilities of SCR are to advise the Board of Directors on Shariah matters in relation to Islamic Banking business and operations, to endorse Shariah compliance manuals, to endorse and validate relevant documents as well as to provide written Shariah opinion on new products and RHB Islamic Bank's financial statements.

13.0 SHARIAH NON-COMPLIANCE RISK AND GOVERNANCE (CONTINUED)

On a functional basis, RHB Islamic Bank is supported by Shariah Advisory Division, Group Shariah Risk Management, Group Shariah Business Compliance and Shariah Audit.

The Head of Shariah Advisory Division reports functionally to the SCR and administratively to the Managing Director of RHB Islamic Bank. The key functions of the Shariah Advisory Division are undertaken by two sub-units, ie Shariah Advisory and Research; and Shariah Governance and Management.

The main duties and responsibilities of Shariah Advisory and Research are to conduct reviews on the Islamic products and services, provide internal Shariah advisory support to the management of RHB Islamic Bank in its daily business and operational matters, assist SCR in elaborating and discussing on pertinent Shariah issues, provide in-depth research on competitive analysis in order to help SCR in making decision and to represent RHB Islamic Bank in any Shariah-related matters. Meanwhile, the main duties and responsibilities of Shariah Governance and Management function are to ensure the internal Shariah governance as well as the internal process flow and policies and Shariah approval process is well managed and maintained in an efficient manner, ensure the Bank is in compliance with the highest standard of Shariah governance as set by BNM, serve as the secretariat of SCR and to act as the mediator between the management and the SCR, oversee the computation and distribution of zakat and fund to be channelled to charity, and conduct Shariah-related training.

The key role and responsibilities of Group Shariah Risk Management is to facilitate the identifying, measuring, monitoring and controlling of Shariah non-compliance risks inherent in the Islamic business and operations to mitigate any potential Shariah non-compliance events. Group Shariah Risk Management also performs independent assessment and provides support relating to Shariah non-compliance risk.

Group Shariah Business Compliance conducts review and assists the SCR in providing opinions from Shariah perspective in relation to the status of Shariah compliance of products, services and operations of the Islamic business operations. Shariah Audit provides independent assessment and objective assurance designed to add value and improve the degree of compliance in relation to the Islamic business operations, with the main objective of ensuring a sound and effective internal control system for Shariah compliance.

Any incidences of Shariah non-compliance are reported to the SCR, the GCRC, IRMC, the Board of Directors of RHB Islamic Bank and BNM. Remedial actions may include the immediate termination of the Shariah non-compliant products or services and de-recognition of Shariah non-compliant income.

There is no major Shariah non-compliant event or income arising from the Islamic products or services during the financial year 2017.

14.0 FORWARD LOOKING STATEMENTS

This document could or may contain forward looking statements that are based on current expectations as well as assumptions or anticipation of future events. These forward looking statements can be identified by the fact that they do not relate only to historical or current facts, and often use words such as anticipate, target, expect, estimate, intend, plan, believe, will, may, should, would, could or other words of similar expressions.

Undue reliance should not be placed on any of such statements. By their nature, forward looking statements are subject to risks and uncertainty because they relate to future events and circumstances, including, but not limited to domestic and global economic and business conditions, the effects of continued volatility in the credit markets, market-related risks such as changes in profit rates and exchange rates, changes in regulation, and future business combinations or dispositions. As a result, the Bank's actual future results may differ materially from the plans, goals, and the expectations contained in the forward looking statements.

The Bank undertakes no obligation to revise or update any forward looking statements contained in this document, regardless of whether these statements are affected as a result of new information, future events or otherwise.

14.0 FORWARD LOOKING STATEMENTS (CONTINUED)

Table 18: Glossary of Terms

ARMs	Area Account Relationship Managers
BCC	Board Credit Committee
BCP	Business Continuity Planning
BNM	Bank Negara Malaysia
Board	Board of Directors
BRC	Board Risk Committee
CAFIB	Capital Adequacy Framework for Islamic Banks
CCB	Capital Conservation Buffer
CCR	Counterparty Credit Risk
CCYb	Countercyclical Capital Buffer
CET	Common Equity Tier
CRM	Credit Risk Mitigation
EAD	Exposure at Default
EAM	Enhanced Account Management
EaR	Earnings-at-Risk
ECAIs	External Credit Assessment Institutions
EL	Expected Loss
EUR	Euro Dollar
EVE	Economic Value of Equity
Fitch	Fitch Ratings
GBCSC	Group Business Continuity Steering Committee
GBP	Pound Sterling
GCG	Group Credit Guidelines
GCPM	Group Credit Procedures Manual
GCRC	Group Capital and Risk Committee
GMC	Group Management Committee
Group ALCO	Group Asset and Liability Committee
Group ALM	Group Asset and Liability Management
ICAAP	Internal Capital Adequacy Assessment Process
IMA	Internal Models Approach
IMLDC	Incident Management and Loss Data Collection
IRMC	Islamic Risk Management Committee
ISDA	International Swaps and Derivatives Association
KCT	Key Control Testing
KRI	Key Risk Indicators
LCR	Liquidity Coverage Ratio
LGD	Loss Given Default

14.0 FORWARD LOOKING STATEMENTS (CONTINUED)

Table 18: Glossary of Terms (continued)

MARC	Malaysian Rating Corporation Berhad
MATs	Management Action Triggers
MDBs	Multilateral Development Banks
Moody's	Moody's Investors Service
MYR	Malaysian Ringgit
NIFs	Notes Issuance Facilities
NSFR	Net Stable Funding Ratio
OTC	Over-the-Counter
PD	Probability of Default
PSIA	Profit Sharing Investment Accounts
R&I	Rating and Investment Information, Inc
RAM	RAM Rating Services Berhad
RCSA	Risk and Control Self-Assessment
RM'000	Malaysian Ringgit in nearest thousand
RWA	Risk-Weighted Assets
SA	Standardised Approach
SCR	Shariah Committee of RHB Islamic Bank
SBUs	Strategic Business Units
SFUs	Strategic Functional Units
SGD	Singapore Dollar
S&P	Standard & Poor's
SMEs	Small-and medium-sized enterprises
VaR	Value-at-Risk

ISLAMIC BANKING

MALAYSIA

CAWANGAN UTAMA – KUALA LUMPUR
No. 19A-1-1 & 19A-1-2
Level 1 UOA Centre
No. 19 Jalan Pinang
50450 Kuala Lumpur
Tel : 603 9206 8118
Fax : 603 2161 0599

CAWANGAN AUTO CITY, PRAI
1808-1809B, Jalan Perusahaan Auto-City
North South Highway
Juru Interchange
13600 Prai, Pulau Pinang
Tel : 604 508 0500
Fax : 604 501 6700

CAWANGAN TAMAN FLORA UTAMA, BATU PAHAT
Ground Floor, No. 1 & 2
Jalan Flora Utama 1, Taman Flora Utama
83000 Batu Pahat, Johor
Tel : 607 433 6777
Fax : 607 433 4848

CAWANGAN JALAN RAJA LAUT
Lot G-04, Ground Floor
Bangunan KWSP
No. 5, Jalan Raja Laut
50350 Kuala Lumpur
Tel : 603 9206 8118
Fax : 603 2693 7300

CAWANGAN SUNGAI PETANI
Lot No. 41
Jalan Perdana Heights 2/2
Perdana Heights
08000 Sungai Petani, Kedah
Tel : 604 422 8088
Fax : 604 422 7088

CAWANGAN TAMAN SETIA TROPIKA, JOHOR BAHRU
No. 1, Jalan Setia Tropika 1/30
Taman Setia Tropika
81200 Johor Bahru, Johor
Tel : 607 238 0078
Fax : 607 238 0012

CAWANGAN BANDAR BARU BANGI
No. 39-G-1, Jalan Medan
Pusat Bandar 4
43650 Bandar Baru Bangi
Selangor
Tel : 603 8922 2192
Fax : 603 8926 3343

CAWANGAN KUBANG KERIAN
Lot 1679
Jalan Raja Perempuan Zainab 2
Bandar Baru Kubang, Kerian
16150 Kota Bharu, Kelantan
Tel : 609 764 0221/0222/0223
Fax : 609 764 0700

CAWANGAN JALAN SATOK, KUCHING
Lot 469–471, Ground Floor
Bangunan Al-Idrus Commercial Centre
Section 6, 192I–192K, Jalan Satok
93400 Kuching, Sarawak
Tel : 6082 258 800
Fax : 6082 243 900

CAWANGAN KELANA JAYA
A-G-03A & A-G-05, Jalan SS6/5A
Dataran Glomac
Pusat Bandar Kelana Jaya
47301 Petaling Jaya, Selangor
Tel : 603 9206 8118
Fax : 603 7880 7520

CAWANGAN KUALA TERENGGANU
No. 35451 & 35452
Dataran Austin, Wakaf Tembusu
Kuala Terengganu
23000 Terengganu
Tel : 603 9206 8118
Fax : 609 667 5221

CAWANGAN LAMAN SERI, SHAH ALAM
Lot 17-1 & 17-2
No. 1, Laman Seri Business Park
Seksyen 13
40100 Shah Alam, Selangor
Tel : 603 5510 3491
Fax : 603 5511 2422

www.rhbgroup.com

RHB Islamic Bank Berhad (680329-V)
Level 9, Tower One, RHB Centre, Jalan Tun Razak, 50400 Kuala Lumpur
Tel : 603-9287 8888 Fax : 603-9281 9314

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