United Arab Emirates

مصرف الإمارات العربية المتحدة المركزي

CENTRAL BANK OF THE U.A.E.

Annual Report

2015

President of the United Arab Emirates

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H.E.Saif Hadef Al Shamsi
Assistant Governor for Monetary Policy and Financial Stability

Message from H.E. the Chairman Of the Board of Directors

The oil price dipped further in 2015 on the back of a weakening global economy. The current consensus is that oil prices will remain low for an extended period of time. As a result, the UAE economy was doubly affected. First as a major oil and natural gas exporter, government revenues fell as did liquidity in the economy. Second, as a small open economy, we were affected by the global economic slowdown, which means less FDI and less non-energy export opportunities against the backdrop of continued financial volatility and tighter resources .

The national economy, however, showed remarkable resiliency. Non-oil activities continued growing at a respectable rate, albeit slowing down. Inflation, after a surge in the beginning of the year due to a pickup in non-tradables (mostly housing) prices, moderated due to oversupply, in tandem with contained increase in the price of tradables on account of continued appreciation of the dirham relative to major trading partners.

The Central Bank has been challenged by the continued volatility in the global economy, including the tightening cycle in the country of the peg, and the need to increase its capacity to counter spillovers on the domestic economy. To that end, we have been monitoring development in the banking sector to ensure continued resiliency. Despite a decrease in government deposits, banks have benefited from an increase in non-resident deposits and used their reserves and investments at the Central Bank to accommodate demand for credit, which turned out to be stronger in 2015 in support of continued growth in the non-energy sector. However, with continued volatility in the global economy, the central bank needs to ensure the right balance between efficient intermediation and financial stability.

To that end, the Central Bank continues its close monitoring of the liquidity situation of banks and other indicators of financial prudence which have been robust for the year 2015 as a whole. Going forward, we will maintain this commitment while standing ready to provide liquidity support as deemed necessary to ensure continued healthy growth of the non-energy sector and further diversification of our economy. .

Last but not the least, the Central Bank will continue to join efforts with the Ministry of Finance and other stakeholders to improve statistics collection, processing and publication, and ensure better policy coordination to diversify sources of financing the prospective deficit and reduce pressures on liquid resources available in support of private activity. The Fiscal Coordination Council will continue to play a pivotal role towards attaining these objectives and expediting the issuance of the Public Debt Law to deepen the financial market, benchmark the yield curve in domestic currency and increase options to mobilize domestic savings and attract capital inflows.

Message from H.E. the Governor Of the Central Bank

Against the backdrop of the Dirham peg to the US dollar, 2015 was another year of continued currency appreciation in our country, while interest rates increased last December in line with the Federal Reserve's decision in this respect. Meanwhile, several factors such as dipping oil prices, the slowdown in the global economy, and increasing fiscal vulnerabilities for oil exporting countries, in addition to the Emerging Economies' struggle with weakening currencies, mounting debts and capital outflows, all have added to the challenges that our open economy is facing.

Our banking sector, however, remains resilient, well-capitalized and liquid. Despite some signs of liquidity squeeze, both the ratios of liquid assets to total assets and lending to stable resources remain at prudent levels, while indicators of financial soundness continue to bode well for the ability of banks to support credit while adhering to the guidelines of financial stability.

Small and Medium Enterprises (SMEs) are employing most of the labor force in the UAE. Therefore, we continue to work diligently with major stakeholders to reactivate Federal Law No. 2 of 2014 so that SMEs can have access to financing at affordable costs. Indeed, the recent Central Bank's decision to set up a "Team for Implementation of a Strategy in support of Small and Medium Enterprises" is a clear indication of our continued commitment to contribute significantly to the government strategy, in this respect.

Providing the appropriate prudent financial infrastructure is also a priority for us. Regulations were indeed completed in 2015 regarding bank liquidity and risk management, while a draft was finalized for institutions providing digital payments services, and an engagement process started with banks for the implementation of the new Basel III capital requirements. Moreover, the Central Bank already defined the initial steps of its roadmap to support the UAE Smart Government Initiative, whose full implementation will constitute a priority for us in the coming period.

Our Vision

Leadership and excellence in preserving banking and financial stability

Our Mission

Through application of effective prudential supervision policies, adoption of efficient monetary policy and operation of payment systems compatible with best practices, we maintain a sound banking sector and support stability of the UAE financial system to ensure balanced economic growth.

Our Values

Transparency - Committed to transparency and continuous improvement.

Professionalism - Practice sound governance.

Participation - Achieve excellence through teamwork.

Collaboration - Build and develop integrative partnerships.

Trustworthiness - Maintain the confidence of our stakeholders.

List of Abbreviations

ADSM:	*Abu Dhabi Stock Market*
AED:	*Arab Emirates Dirham*
BRIC:	*Brazil, Russia, India, and China*
CPI:	*Consumer Price Index*
DFM:	*Dubai Financial Market*
ECB:	*European Central Bank*
EIBOR:	*Emirates Inter-Bank Offer Rate*
FATF:	*Financial Action Task Force*
FIU:	*Financial Intelligence Unit*
GREs:	*Government Related Enterprises*
LIBOR:	*London Inter-Bank Offer Rate*
MENAFATF:	*Middle East & North Africa Financial Action Task Force*
PCE	*Private Consumption Expenditure*
PMI:	*Purchasing Managers Index*
RBI:	*Reserve Bank of India*
STRs:	*Suspicious Transaction Reports*
UAE:	*United Arab Emirates*

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Part one: The Economic Report

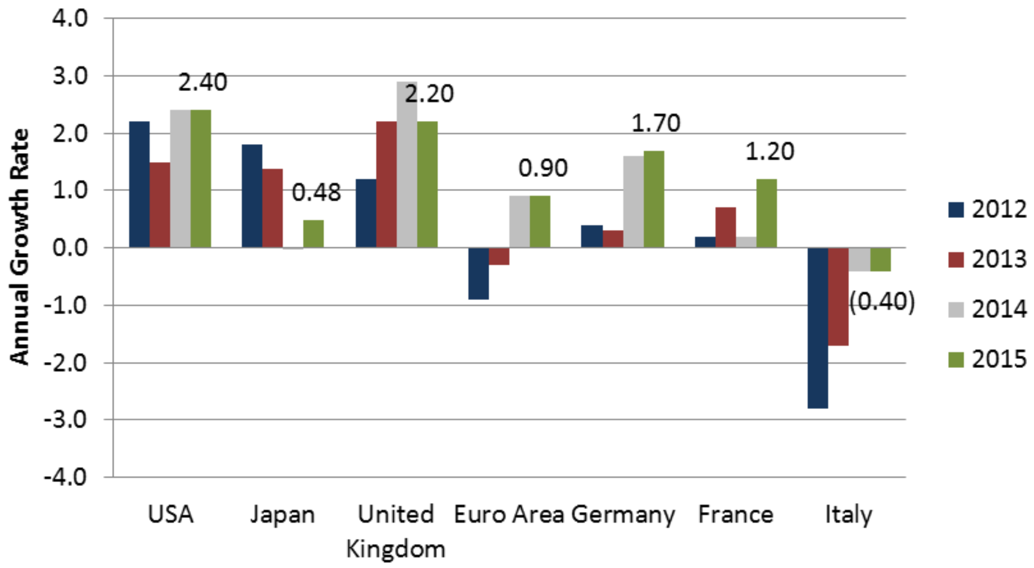
Chapter1. International Economic Developments

Global growth disappointed again in 2015 due to increased uncertainty, slowing to 2.4%, and it is expected to recover at a slower pace than previously envisaged. Negative factors (China's financial gyrations, volatility and low level of oil prices and the further weakening of the US economy) are clouding the outlook, but do not yet signal an imminent global economic recession. Weaker demand from emerging markets made 2015 the worst year for world trade since the aftermath of the global financial crisis, solidifying concerns about the health of the global economy. The largest downward adjustments are seen in emerging markets, of which Brazil and Russia are the most pronounced. In MENA, the oil exporters have been suffering from the low oil prices which triggered fiscal consolidation in these countries, while the oil importers are being hurt by regional and political instability and slow growth in major trading partners.

Global Economy and Capital Markets

Economic activity in the developed world shows a split between the Anglo-Saxon world, such as the US and the UK and the rest of the world. While in the US the growth rate remained the same in 2015 as in 2014, and the UK experienced a deceleration from 2.9% in 2014 to 2.2% in 2015, the Euro area has witnessed an increase in growth, from a negative (-1%) in 2012 to 1.5% in 2015. This picture prevailed for all major Euro area countries. Also, Japan saw acceleration in its GDP growth rate from 0% in 2014 to 0.5% in 2015.

Figure 1.1. Annual Real GDP Growth Rates: Developed World

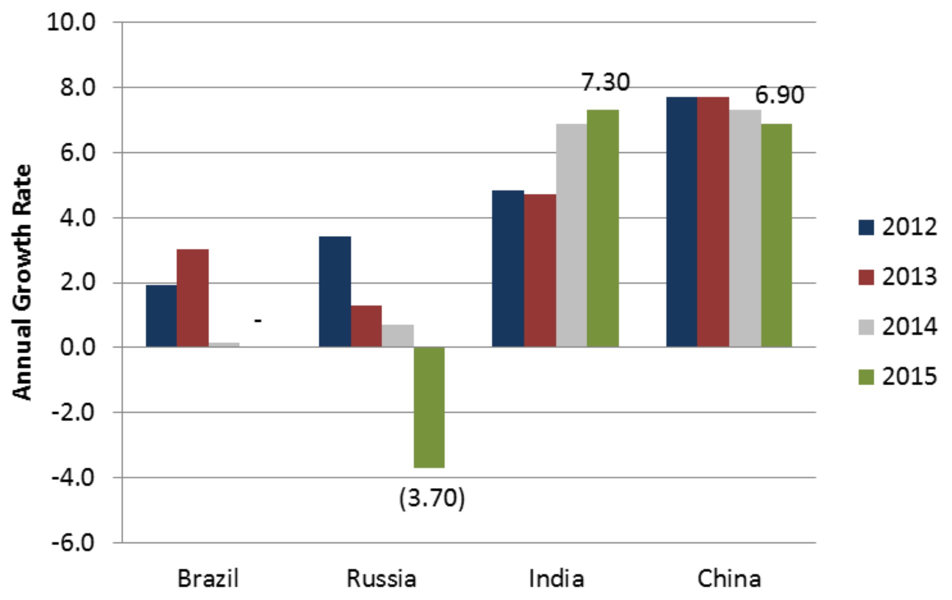


Source: Bloomberg

The growth figures for BRIC countries show clearly the impact of the commodity price decline which continued unabatedly in 2015. Russia and Brazil suffered profoundly in 2015, while China's growth slowed down to 6.9%, and India which benefitted from a lower import bill as the result of lower oil prices, remained an exception with a robust growth of 7.3%.

Financial markets in 2015 focused very much on the weakening growth picture in China whose imports in the past helped many developed countries to overcome domestic demand weaknesses.

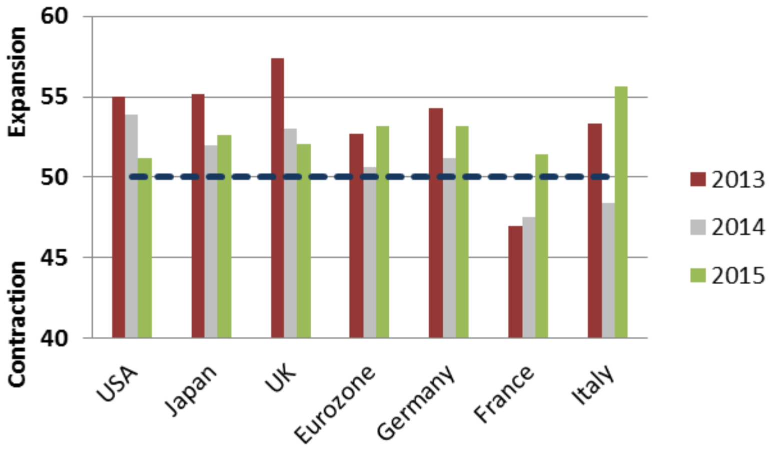
Figure 1.2. Annual Real GDP Growth BRIC Countries



Source: Bloomberg

The difference between Anglo Saxon and Euro area is also visible if one looks at the PMI indicators. The most striking example is the UK which registered a level of almost 60 in 2013 only to find itself at 52.1 by the end of 2015. Contrast that with France whose PMI was in contraction territory in 2013 and whose PMI number reached 51.4 by end of 2015. Italy a laggard in 2014 had the highest PMI reading in 2015 in the sample. The reason can be attributed to the fact that the US – together with the UK – were the first countries to apply vigorously monetary and fiscal support measures after the crisis in 2008 while the ECB was more hesitant.

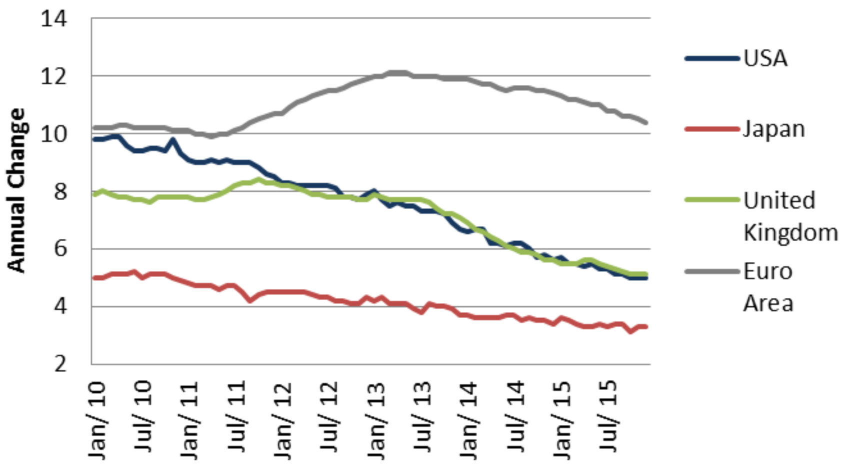
Figure 1.3.a PMI Levels Developed World



Source: Bloomberg

The difference between the Anglo-Saxon bloc and the rest of the developed world becomes also visible when looking at unemployment figures. Since the beginning of 2012, the UK and the US have moved in almost perfect tandem, bringing in both cases the unemployment rate to 5%. The fall in the Euro area unemployment reflects some economic improvement even though it remains at 10.4% at the end of 2015; i.e., more than double of the unemployment rate in the US and the UK. Only Germany with a level of 4.5% at the end of 2015 is getting close to the level in the UK and the US, while Italy and France still hover above the 10% mark in December 2015.

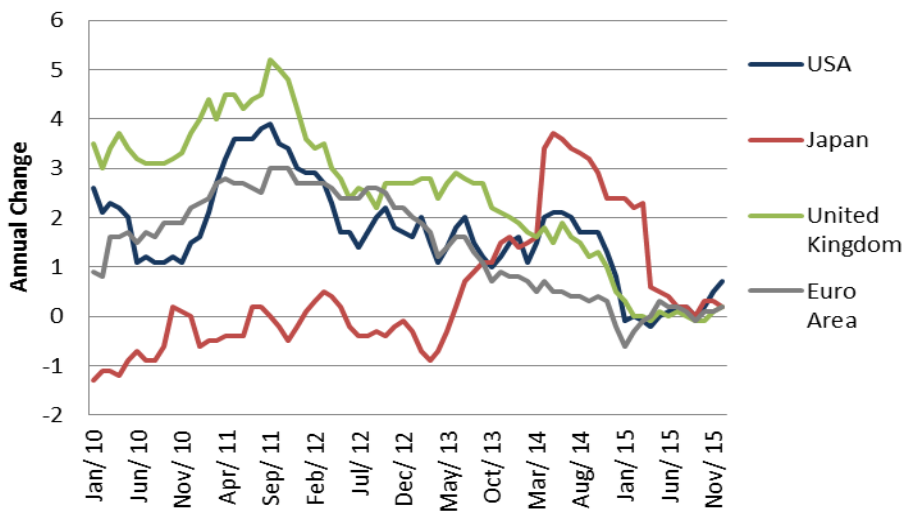
Figure 1.3.b Unemployment Levels Developed World



Source: Bloomberg.

The year 2015 saw a conversion of consumer prices in all major developed economies. This development was spurred by the fall in the oil price by the end of 2014 but as it can be seen, it followed an already well entrenched path since September 2011. The exception is Japan where consumer price inflation edged up in recent years from negative territory to become slightly positive at 0.2%. The low level of inflation is one of the biggest concerns for policy makers as it may reflect sluggish aggregate demand. It may also reflect a heightened competitive situation where price increases are difficult to pass on to consumers.

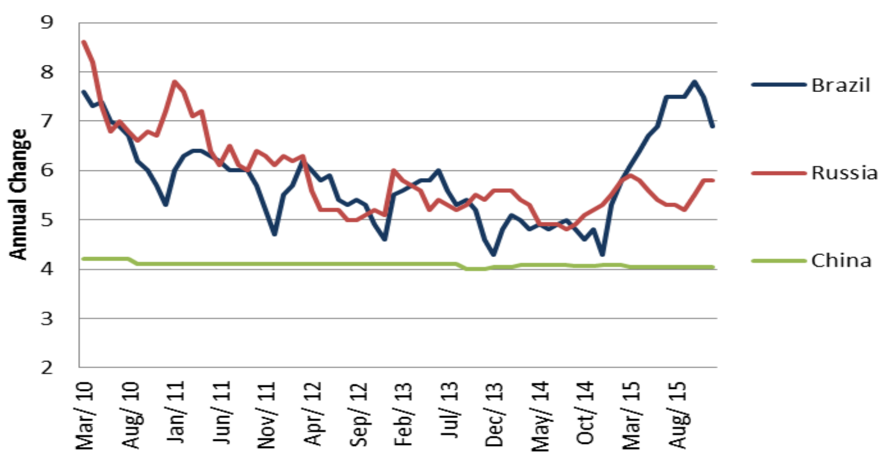
Figure 1.3.c Annual Inflation Rates: Developed World



Source: Bloomberg

In contrast to the developed world, consumer prices in some countries of the developing world gyrate around 4–8% annually, especially in commodity exporting countries. China which reports CPI figures only quarterly has a track record of stable inflation rates at around 4%.

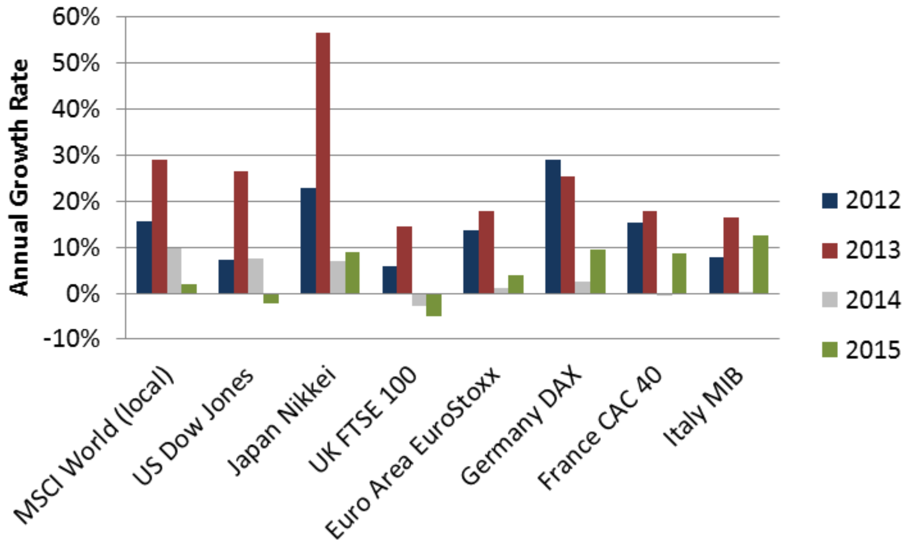
Figure 1.3.d Annual Inflation Rates: Developing World



Source: Bloomberg

All developed equity markets in our analysis, with the exception of Italy, displayed increasing share prices in 2015. While the first quarter was dominated by the European Central Bank and its monthly purchase of securities to support the ailing European economies, the highlight of the fourth quarter was the Federal Reserve Bank which started to raise rates for the first time in almost 10 years and therefore removed an important plank of capital market support.

Figure 1.4.a Annual Stock Market Index Percent Changes: Developed Countries (local)

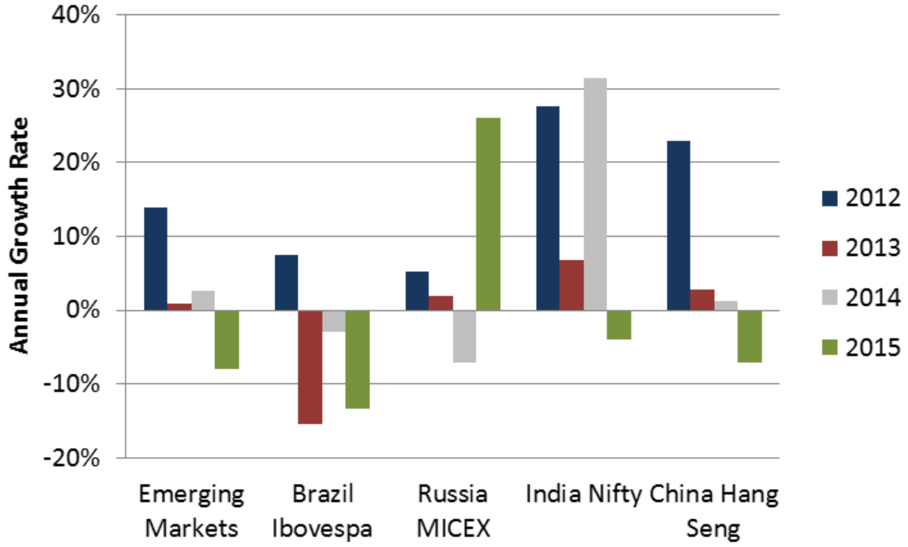


Source: Bloomberg.

Equity markets are discounting future information or at least what market participants expect will be future information. As a consequence, the improvement in economic growth in Europe was already discounted in earlier years. However, the year started with a bonanza in European equities after the announcement of the ECB to pursue an untraditional course of monetary policy by buying various securities in the market. The enthusiasm tapered off however in the last quarter of 2015 when concerns of weaker economic growth in China became widespread. The Fed was certainly the most aggressive central bank when it came to non-traditional stimulus programmes, but in 2015 it became clear that the economy did not need any further assistance. Equity markets took note and the Dow Jones closed with a small loss in 2015.

Emerging markets had a difficult year in 2015, closing with a negative 8%. However, this masks big differences. Interestingly enough, markets pushed up the Russian index by almost 30% in 2015. However, most of the gain happened in the first month of 2015. In USD, Brazil would have lost -42% in 2015, compared to -4.3% for Russia, -8.4% for India and -7.1% for China.

Figure 1.4.b Annual Stock Market Index Percent Change: BRIC Countries (local)



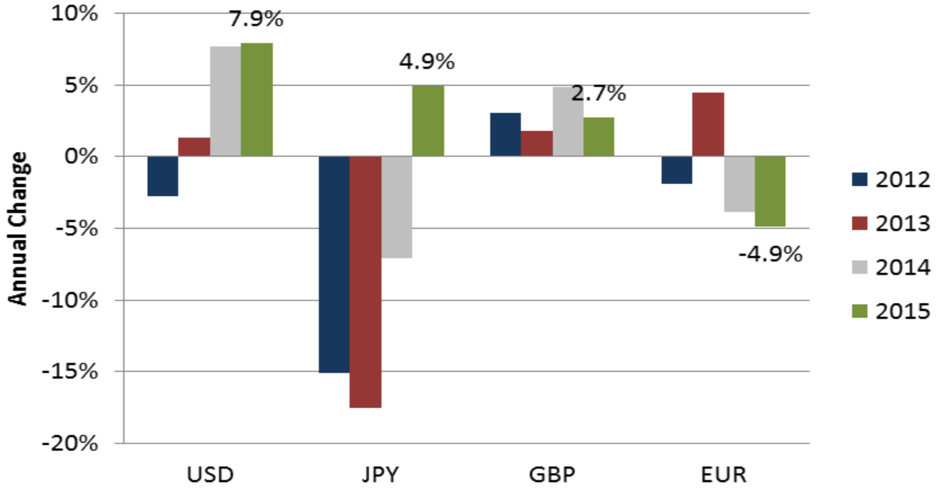
Source: Bloomberg

As regards currency markets, and to the extent that currency movements are a reflection of interest rate differentials, the expectations of a tighter monetary stance in the US led the USD to soar against most currencies. The concept of real effective exchange rates (REER) captures currency movement of the underlying trading partners taking into account the inflation differentials.

The monetary policy divergence can be inferred by the currency movements as well. The USD appreciated against its major trading partners by almost 8% in 2015, almost the same pace of appreciation in 2014. Meanwhile, the Japanese Yen saw a rise in its external value by almost 5% in 2015, certainly not helping the Japanese export industry. As part of the Anglo Saxon bloc, also the British Sterling appreciation mainly reflected the depreciation of the Euro. The Euro lost almost 5% in 2015 after depreciating already by 4% in 2014. This was a clear result of the unconventional policy measures the ECB started in 2015.

The year 2015 will be remembered by currency traders for the decision of the Swiss National Bank to abandon its support for a ceiling of 1.20 against the EUR in January. However, in REER terms, the appreciation of the Swiss Franc by 5% in 2015 was manageable. The introduction of negative interest rates by the Swiss National Bank as a counter measure was certainly dampening any more radical appreciation.

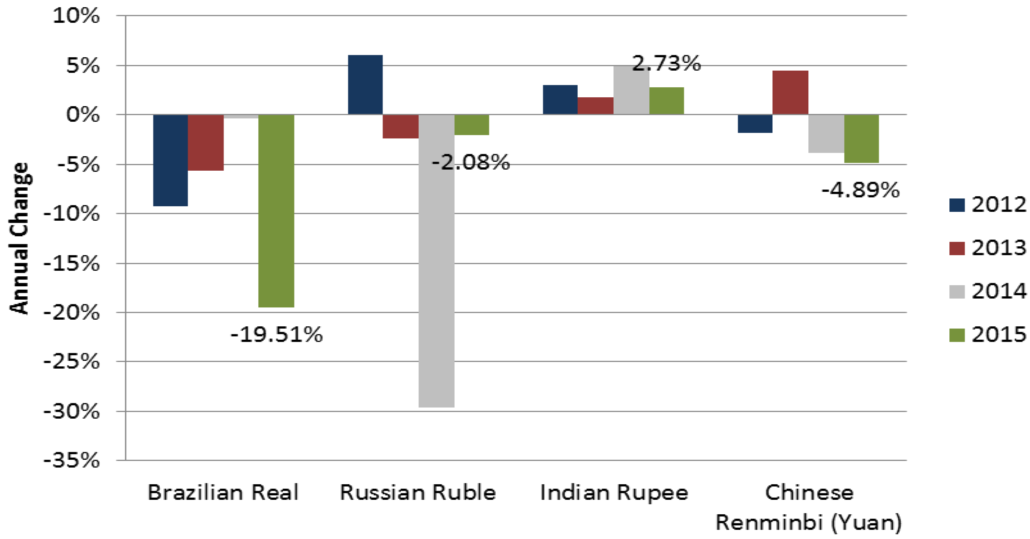
Figure 1.5.a REER Annual Changes Developed Countries



Source: Bloomberg, Barclays

The development of the BRIC currencies also follows the logic of GDP growth. Countries such as Brazil and Russia, which are dependent on commodity exports, have seen the currencies depreciating in nominal and also in real terms. The Russian Rouble fell by almost 13% in nominal effective terms in 2015, compared to a fall of 2% in real terms. However, 2015 was much worse compared to 2014 where the Russian currency depreciated by 30% in real terms and 36% in nominal terms. The country which has seen the best growth rate among the BRIC countries – India – also was the only one which saw a slight appreciation of its currency in nominal terms and also in real terms. The Chinese Renminbi fell by almost 5% in real effective terms but gained in nominal terms by 3.6% in 2015.

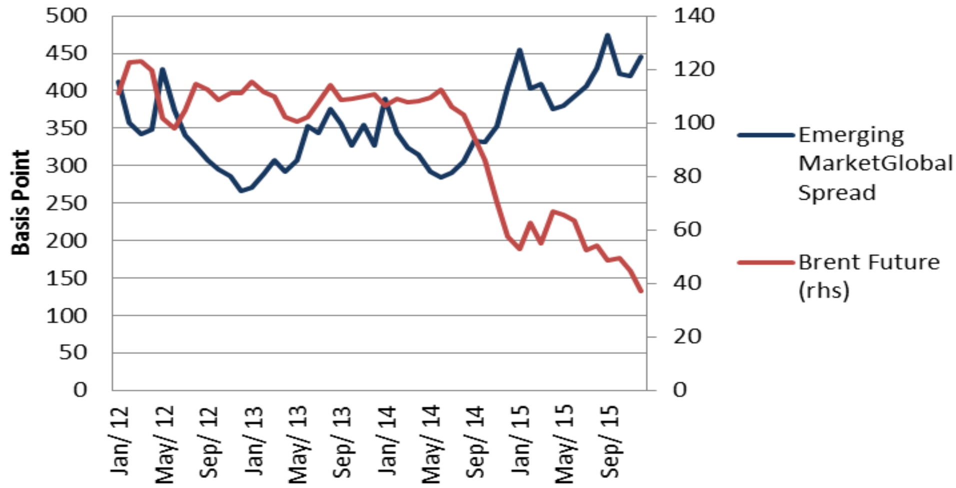
Figure 1.5.b REER Annual Changes: BRIC Countries



Source: Bloomberg, BIS

The credit spreads in the emerging markets underlined the fact that 2015 was a difficult year for most of its members. The spread levels increased by 36% in 2015 from 330 bp to 445 bp by the end of the year. Part of this development can be attributed to the fall of the oil price, but as the chart reveals this negative correlation was non-existing before the summer of 2014 when oil prices collapsed.

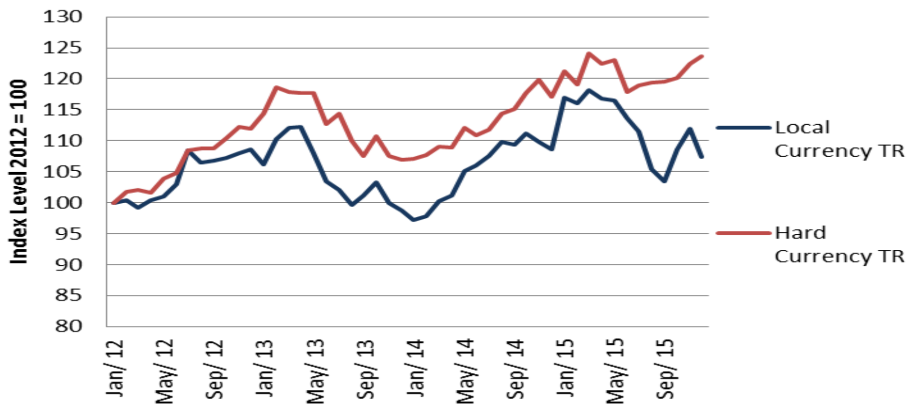
Figure 1.6 Global Emerging Market Spread and Oil Price



Source: Bloomberg.

The tension in emerging markets was particularly visible in the bond market, where local and hard currency denominated issued paper diverged significantly in terms of performance in 2015. The local index lost 1% (total return, including coupon payments) while the hard currency index gained 6% in 2015.

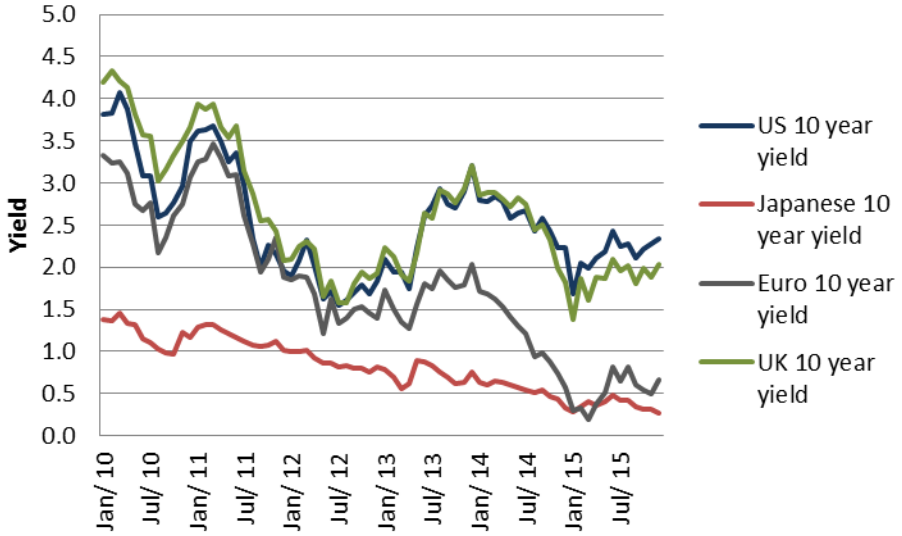
Figure 1.7 Global Emerging Market Indices (Local and Hard Currency Denominated)



Source: Bloomberg, Barclays

The discrepancy in terms of monetary policy between the Anglo-Saxon and the Euro area was already highlighted previously. The divergent development can be also assessed from the perspective of the 10-year government bond yields. While the US, the UK and the Euro area 10 year government yields moved more or less in tandem until end of 2012, the paths diverged in 2013 when markets expected the ECB to engage in its own programme of unconventional policy support. Also, the US and the UK policies diverted by the end of 2015, when it became clear that the Fed is starting in earnest its tightening programme. In the meantime, the Japanese 10-year government yield was heading to a level of 0.2%, which is the more surprising given that the gross debt to GDP ratio in Japan is heading for 250% in contrast to lower debt ratios for other countries, such as Germany, France or Canada, a testament of the impact of divergent monetary policies on sovereign yields.

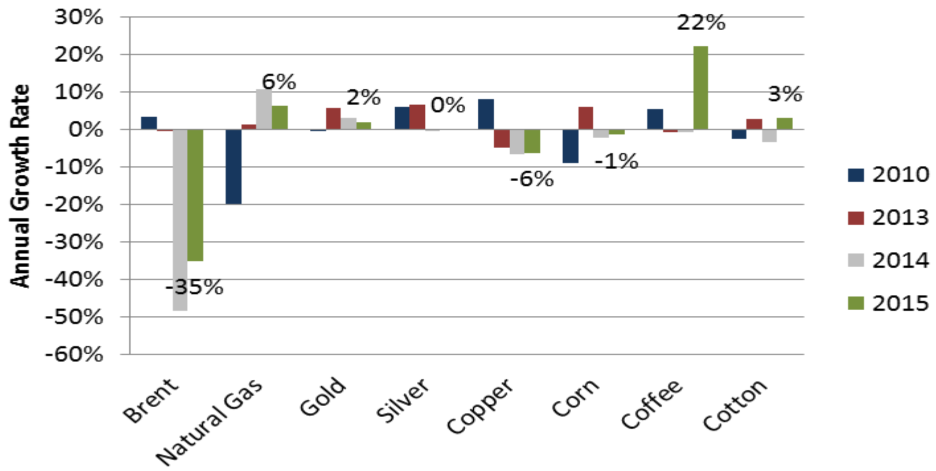
Figure 1.8 a 10-year Government Bond Yields (%)



Source: Bloomberg.

While a fall in commodity prices was mostly seen as beneficial for the world economy, it seems that 2015 reversed this logic. The year 2015 proved to be another ‘annuls horrible’ for commodities in the energy and industrial metals space. Agricultural commodities such as corn, coffee or cotton are equally influenced by weather related factors as by demand patterns.

Figure 1.8.b Commodity Price Developments (front-end futures contract)

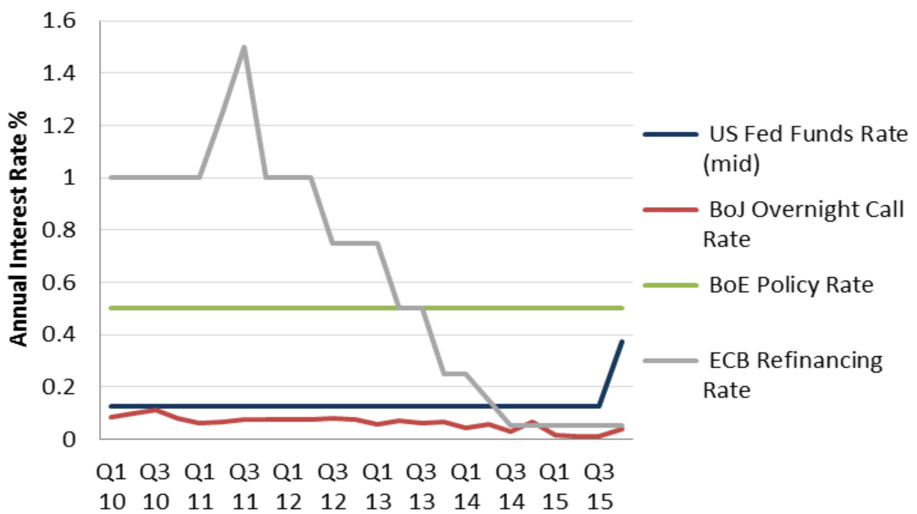


Source: Bloomberg.

In terms of monetary policy, the year 2015 will be remembered by the historic decision of the US Federal Reserve when it finally changed its policy course by raising its policy rate by a quarter of a percentage point in December. It was a difficult decision for the Fed, as even 7 years after the 'Great Recession' not all indicators have been supporting robust economic growth and higher inflation. All the other monetary authorities of the developed world did not change their interest rate policy in 2015, which remained at historically low levels.

Within the BRIC economies, only India and China lowered their policy rates to support growth, while Russia and Brazil kept them steady in order to stem further depreciation risks of their currencies.

Figure 1.9 Policy rates of developed countries

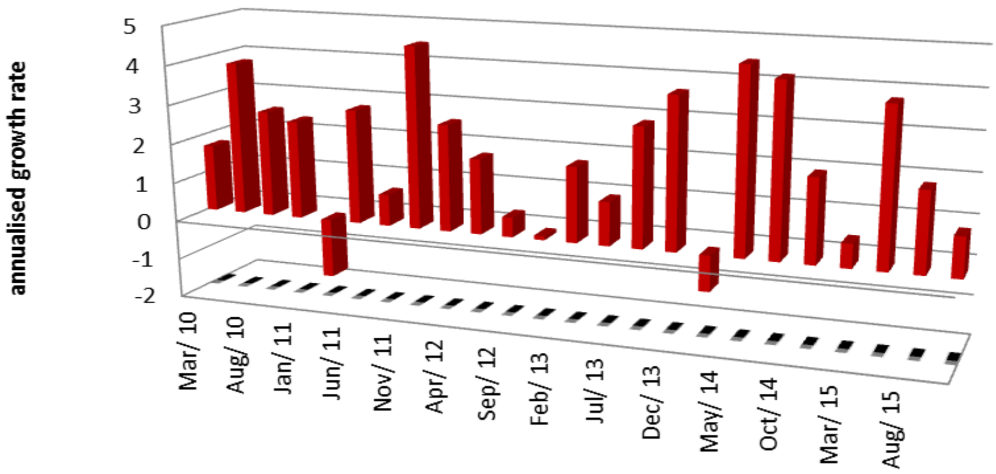


Source: Bloomberg.

1. United States

US growth slowed in the last quarter of 2015 to 1% after running high at 3.9% (annualised) in the second quarter of the year. It appears that the general momentum was slowing in the second half of the year.

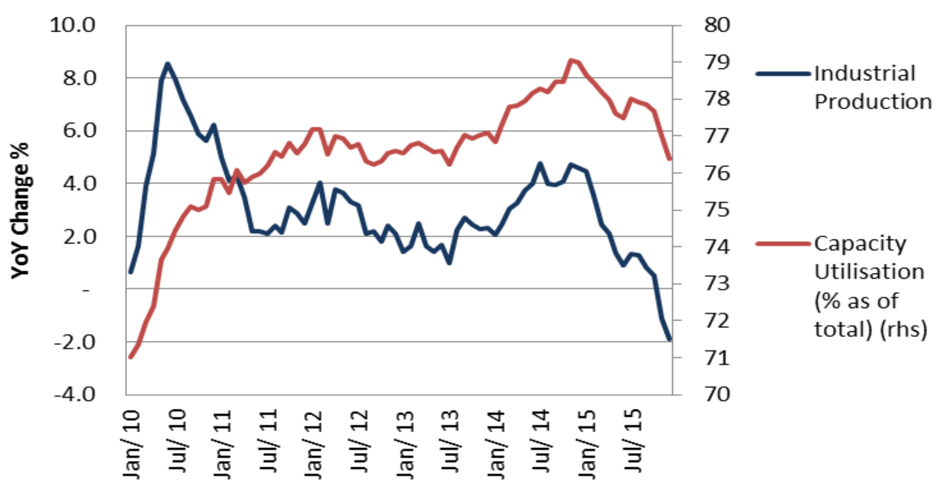
Figure 1.10 US Annualised Quarterly GDP Figures



Source: Bloomberg.

Annual growth rates of industrial production in the U.S. slipped into negative territory in 2015. In line with that development, capacity utilisation which has increased by almost 10% in the last 5 years has slipped throughout 2015.

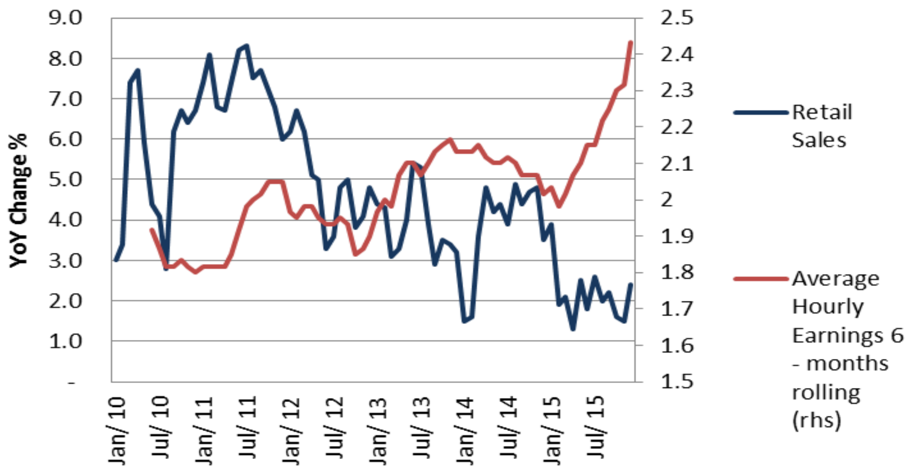
Figure 1.11 US industrial production and Capacity Utilisation



Source: Bloomberg

Also retail sales in the U.S. exhibited a slowdown during the course of 2015 to a level of just around 1%. However, average hourly earnings picked up eventually after languishing around 2% annual increase for years. The low level of earnings growth is partly responsible for the tepid inflation development in the US, considering the fact that US unemployment has been for years on a downward trend.

Figure 1.12 Retail Sales and Average Hourly Earnings



Source: Bloomberg

The fourth quarter of 2015 saw the first increase in the policy rate by the Federal Reserve Bank in years. Apart from the consumer price inflation – whereas the US Fed orients itself on the core PCE (Personal Consumption Expenditure) deflator – the development of unemployment level played a decisive part in the decision by the monetary authorities in December.

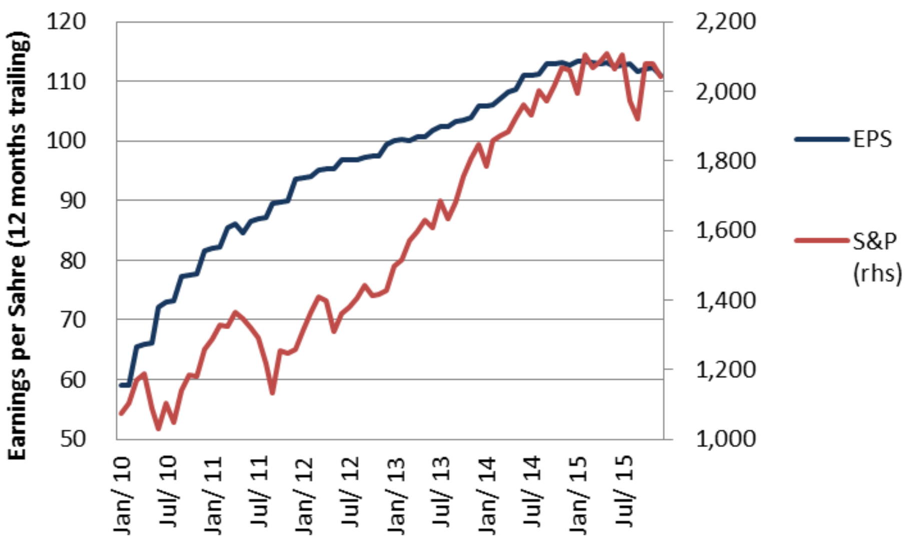
While the unemployment rate fell to levels close to the boom years of 2003 – 2007, labour participation fell steadily over the last few years. The unemployment rate continued its downward slide since the 'Great Recession'. The reduction in the US unemployment figure which has reached 5% by the end of 2015 is an indication that factor markets are getting tighter. However, employment figures are lagging indicators, meaning they represent developments which have occurred already 2-3 quarters ago. More immediate indicators such as PMI figures have deteriorated recently, pointing towards a slowdown of the US economy.

Figure 1.13.a Unemployment Rate and Labour Participation Rate in the US (%)

Source: Bloomberg.

In terms of earnings per share, the slowdown of the US economy was already visible on the corporate level since 2014. The EPS (12 months trailing) retreated in 2015 by 1.6% even when share buy backs continued. Investors took note and the S&P posted a small loss in 2015.

Figure 1.13.b US Stock Market and Earnings per Share (12 months trailing)

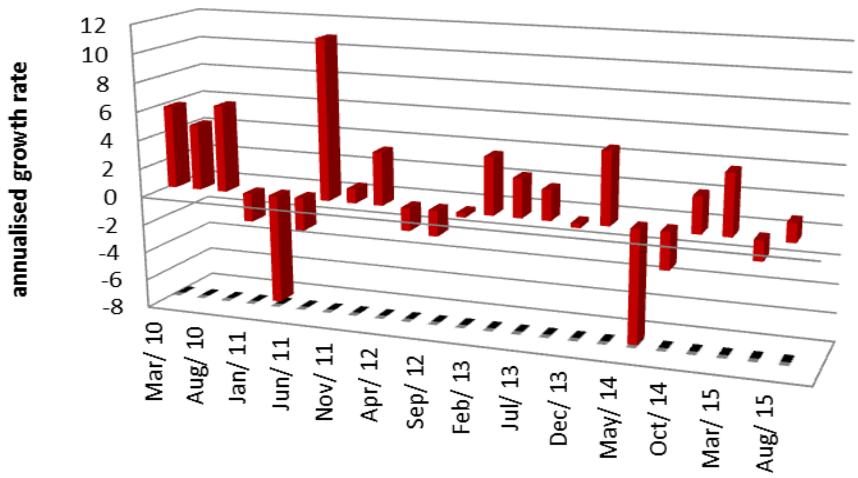


Source: Bloomberg.

2. Japan

Japan's annualised GDP growth went through a rollercoaster in 2015. After having registered a fall of -1.4% in the second quarter, the third quarter posted a gain of 1.3%.

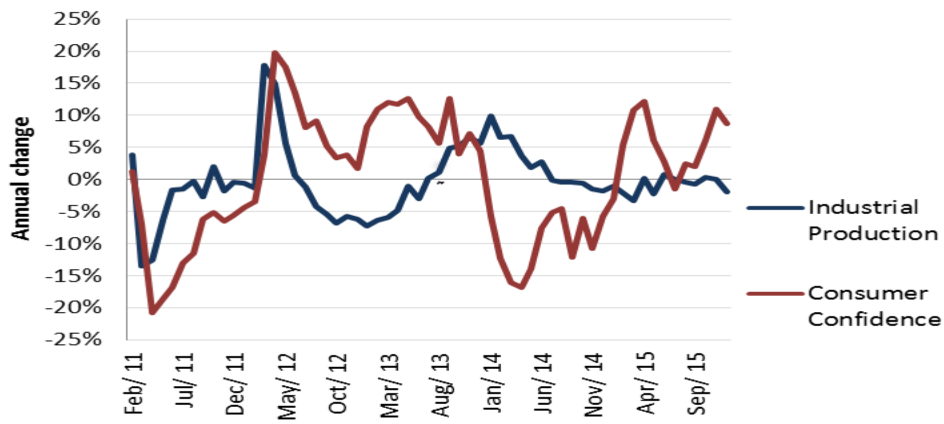
Figure 1.14 Japan Annualised Quarterly GDP Figures



Source: Bloomberg.

During 2011 and 2012, industrial production and consumer confidence grew in tandem in Japan. Since the beginning of 2014, this relationship broke down and industrial production languished at negative annual growth rates. Consumer confidence bounced back sharply in 2015 but lost in the last 2 months of the year some of its momentum. Noteworthy is the sub-index measuring the willingness to buy durable goods which has seen a steady improvement over the course of 2015.

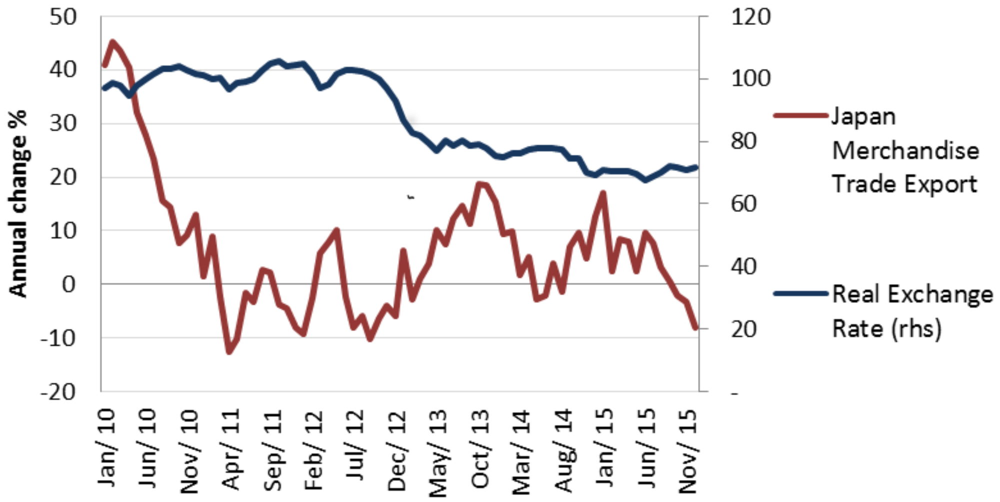
Figure 1.15 Japanese Industrial Production and Consumer Confidence



Source: Bloomberg.

Japanese trade data registered a steep fall in the last few months of 2015. Exports to China, Japan's largest trading partner, were down, driving an overall decline of 8% in the value of overseas shipments in December from a year earlier. The environment for Japanese exports was deteriorating during 2015 as Japanese companies shifted production abroad, the global economy slowed down and the yen strengthened.

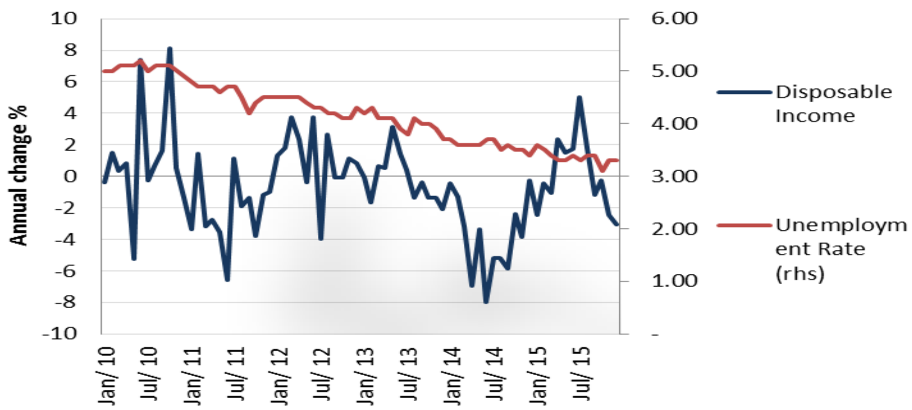
Figure 1.16.a Japanese Trade Export and Real Effective Exchange Rate



Source: Bloomberg.

Unemployment continued its downward trend in the year 2015. However, in 2015 disposable income also fell after having risen steadily during 2014. The decline in household spending was slower than that of disposable income, which registered in December a 3.1% decrease year on year. The average propensity to consume fell to 72.9% in the last month of December. That means people had less income in December and cut spending by less than the reduction in their salaries.

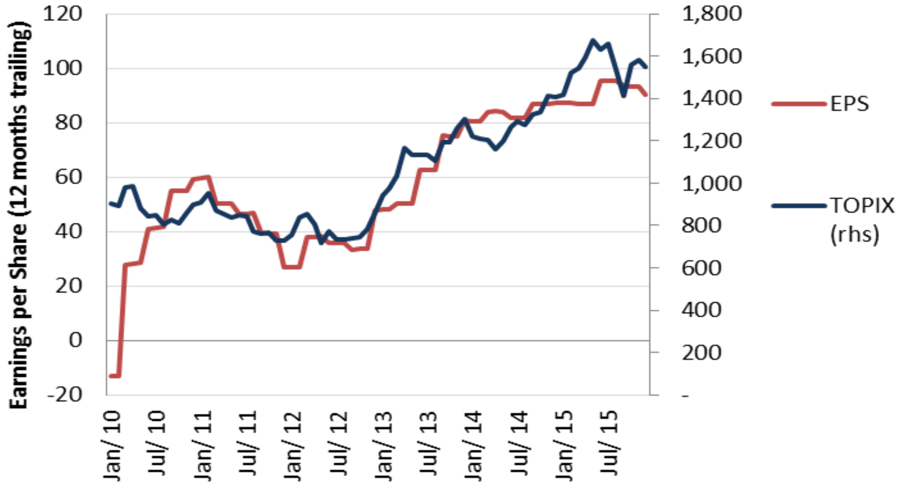
Figure 1.16.b Japanese Disposable Income and Unemployment Rate



Source: Bloomberg.

Earnings per share flattened for Japanese stocks in 2015, partly driven by the strengthening Yen, and partly by the lacklustre demand for Japanese goods overseas and domestically. As a consequence the ascent of the Japanese stock market slowed in 2015

Figure 1.16.c Japanese Stock Market and Earnings per Share (12 months trailing)

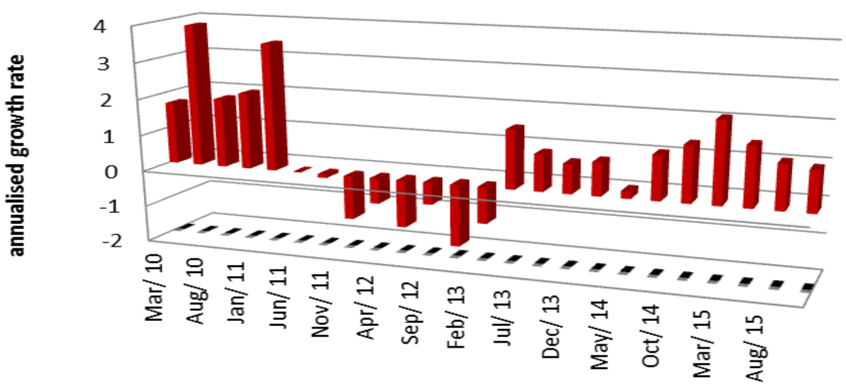


Source: Bloomberg.

3. Euro Area

Euro area GDP growth saw a small slowdown by the end of the year but was in general steady. At least one-third of the growth came from the economies that are smaller than the big four. Germany, France, Italy and Spain, which make up about 78% of total output, together contributed only 0.2 percentage point to the aggregate quarterly growth figure, which was mainly driven by Italy. The services sector played a prominent part in the expansion, while output from industry declined by about 0.1% in the fourth quarter.

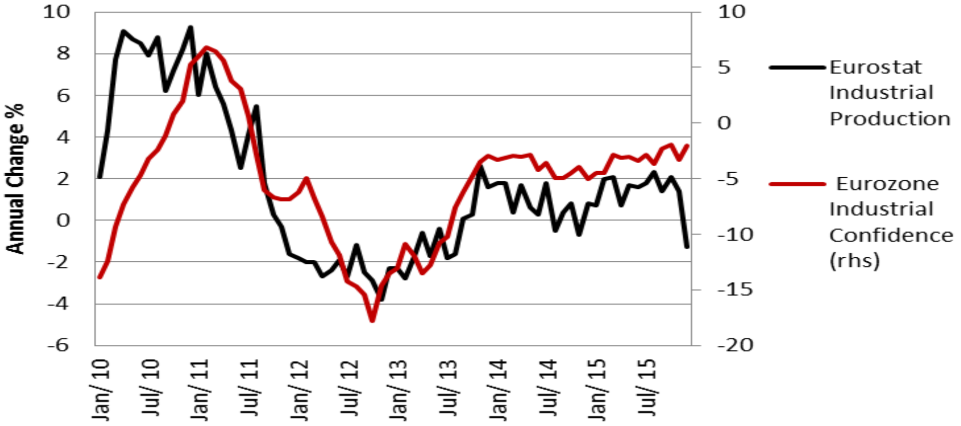
Figure 1.17.a Euro Area Annualized Quarterly GDP Figures



Source: Bloomberg.

Industrial production was falling in the Euro area almost throughout the entire year 2015. Manufacturing confidence which shadows usually industrial production closely, however, has kept steady over the course of 2015, providing some hope that the downturn is temporary. The fall in industrial production happened against a backdrop of a falling Euro, which normally should support the export-oriented European industry. It seems however, that weak demand from emerging markets could not be compensated by a more competitive exchange rate.

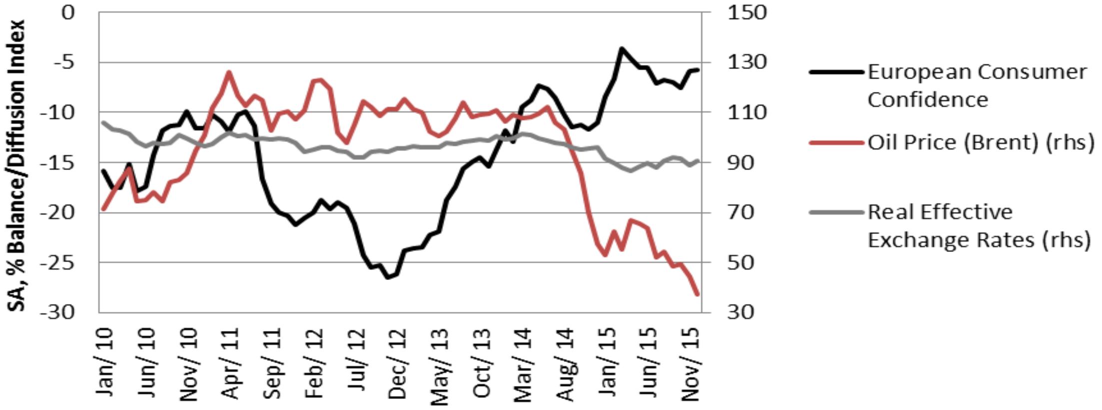
Figure 1.17.b Euro area Industrial Production and Confidence



Source: Bloomberg.

In contrast, European consumer confidence has been on an upward trend since mid-2013, bolstered by lower unemployment and rising disposable income driven partly by the fall in oil prices.

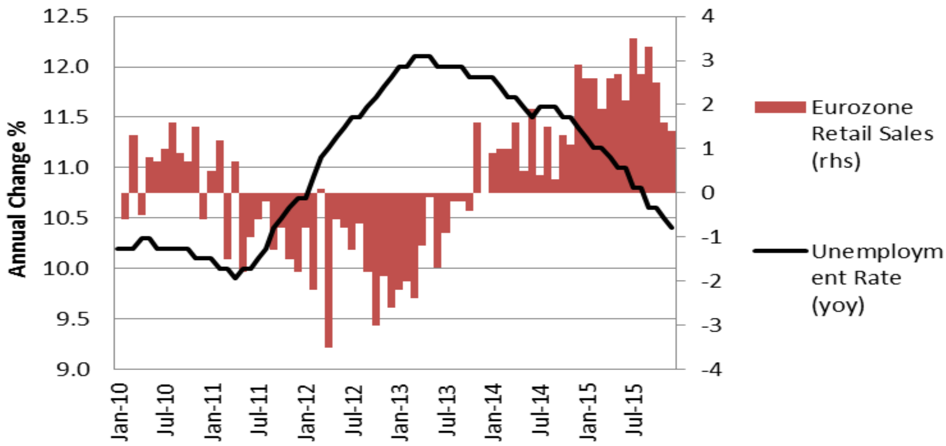
Figure 1.17.c Euro area Consumer Confidence and Real Effective Exchange Rate



Source: Bloomberg.

Retail sales have also recovered since 2013 in line with the fall in unemployment which was closing in to 10% by the end of 2015.

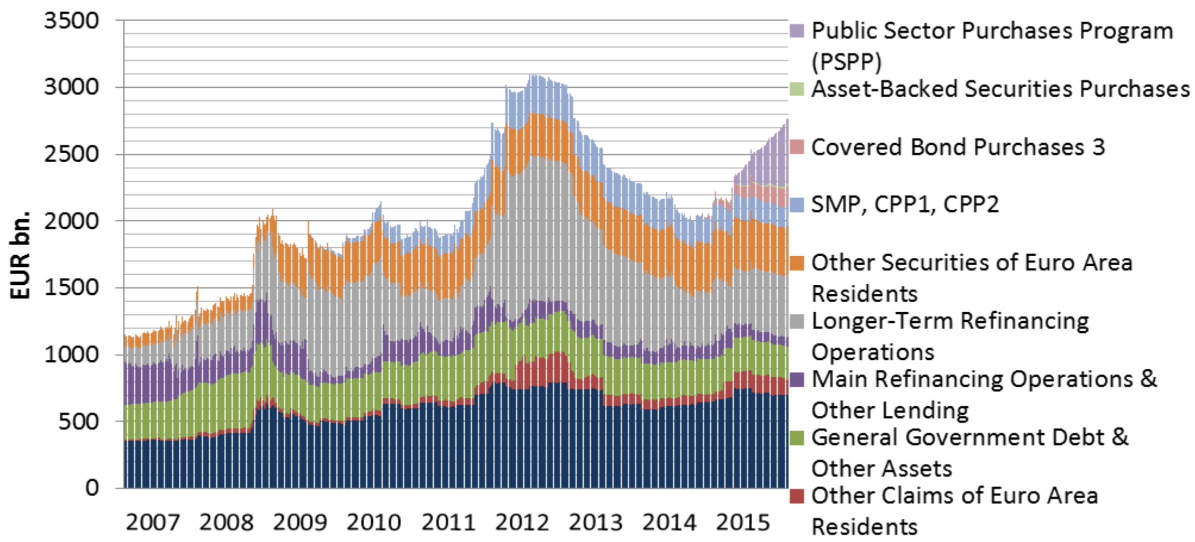
Figure 1.17.d Euro area Retail Sales and Unemployment Rate



Source: Bloomberg.

2015 was the year where the European Central Bank started its unconventional support programme in earnest. Most importantly it started to buy on a monthly basis EUR 60 billion of various securities. About two-thirds of the monthly purchases are government and agency debt, with covered bonds and a small proportion of asset-backed securities making up the rest. The Governing Council agreed in December 2015 to make regional and local government debt eligible, as liquidity in many segments dried up. National central banks, which make the purchases, buy public-sector bonds issued by their own country limited to the size of their economy. They must stick to debt with a yield higher than the deposit rate and a maturity of 2 years to 30 years, and are limited to 33% of any issue.

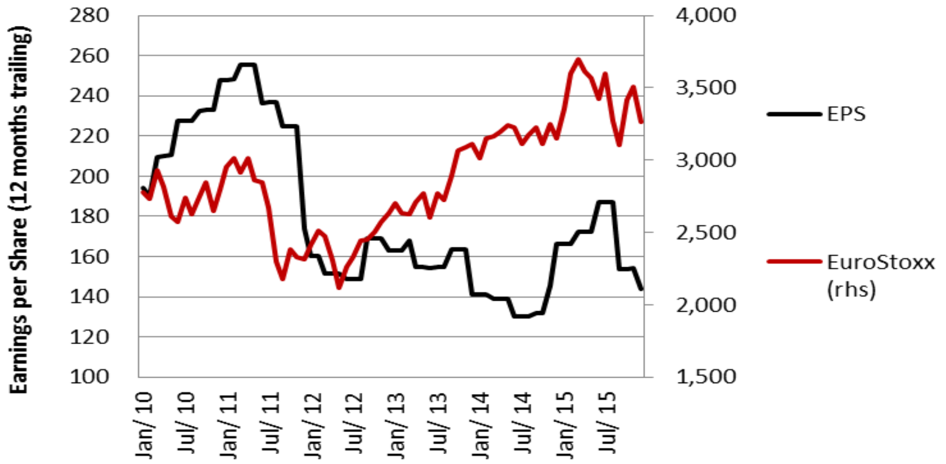
Figure 1.18 ECB Balance Sheet Composition



Source: Bloomberg.

Earnings per share have been accelerating sharply at the beginning of the year 2015 as a result of the depreciation of the Euro against its major trading partners. However, this development went into a reverse by the summer and investors started to sell shares in Euro area companies. The market which has risen in July by 15% in local currency terms settled for a low single digit return for the entire 2015.

Figure 1.19 Euro Area Stock Market and Earnings per Share (12 months trailing)

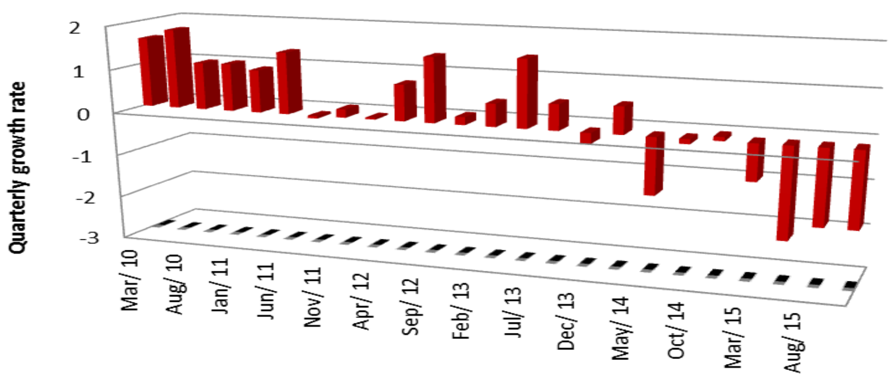


Source: Bloomberg.

4. BRIC (Brazil, Russia, India & China) Economies

The year 2015 was extraordinary for Brazil, marked by the devaluation of the Real, fiscal deterioration, rising inflation and elevated real interest rates. Altogether, this led to plummeting entrepreneurial confidence, an 8.3% contraction in industrial production and a 15% drop in average gross investment for the year. These were the main drivers of the almost 4% contraction in Brazilian GDP in 2015. The fall in commodity prices led to a further deterioration of the situation.

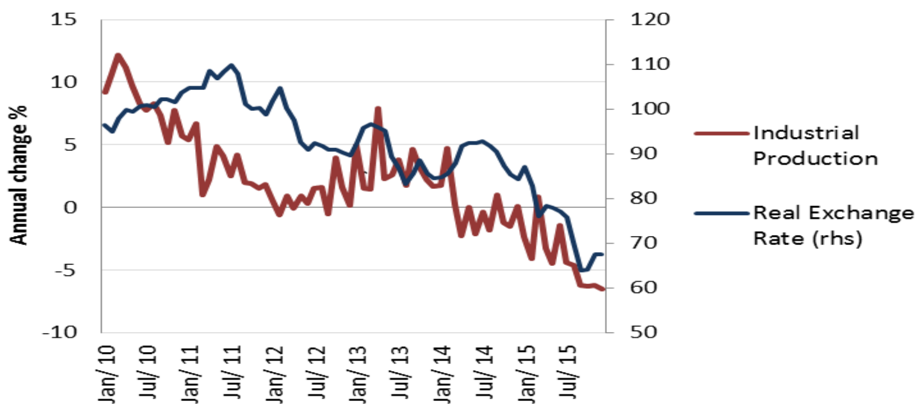
Figure 1.20 Brazil Quarterly GDP Figures (not annualised)



Source: Bloomberg.

Industrial production posted negative growth throughout the year, even if the real effective exchange rate of the Real lost over 30% since its peak in 2011. Activity in the industrial sector has sunk to the average seasonally adjusted level seen in the second quarter of 2004.

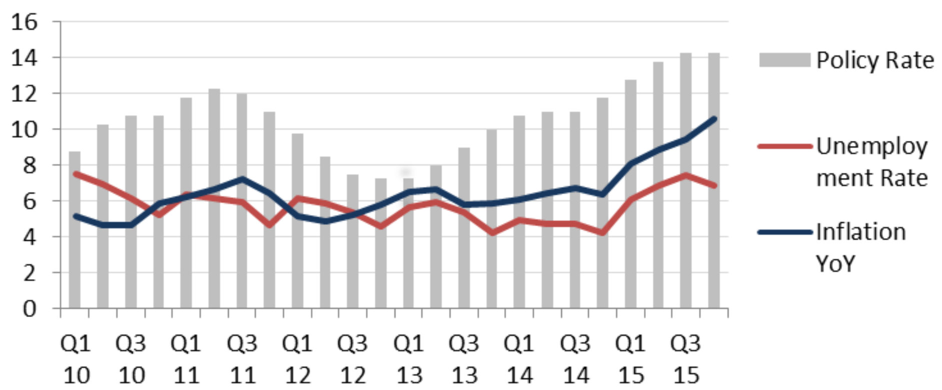
Figure 1.21 Industrial production and real effective exchange rate in Brazil



Source: Bloomberg.

As a consequence, the Brazilian unemployment rate went up in recent years, reaching a high of 7.5% at the end of the third quarter, before edging down to below 7% by the end of the year. Monetary authorities tried to stem the capital outflow which was causing a vicious circle in terms of devaluation by increasing the policy rate (Selic Target Rate) from as low as 7.25% in 2013 to 14.25% in 2015. Inflation accelerated, in spite of the slowdown of the economy, and was mainly driven by the devaluation of the Brazilian currency.

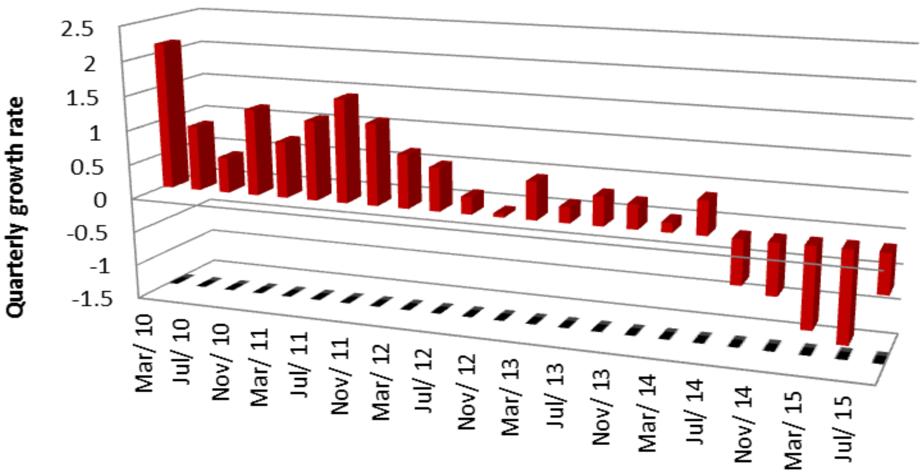
Figure 1.22 Policy rate, unemployment and inflation rate in Brazil (%)



Source: Bloomberg

Since the third quarter of 2014, the Russian economy has suffered from negative growth. In 2015, the slowdown was at least moderated, with a 3rd quarter decline Y-o-Y of 4.1%.

Figure 1.23 Russia Quarterly GDP Figures (not annualised)



Source: Bloomberg

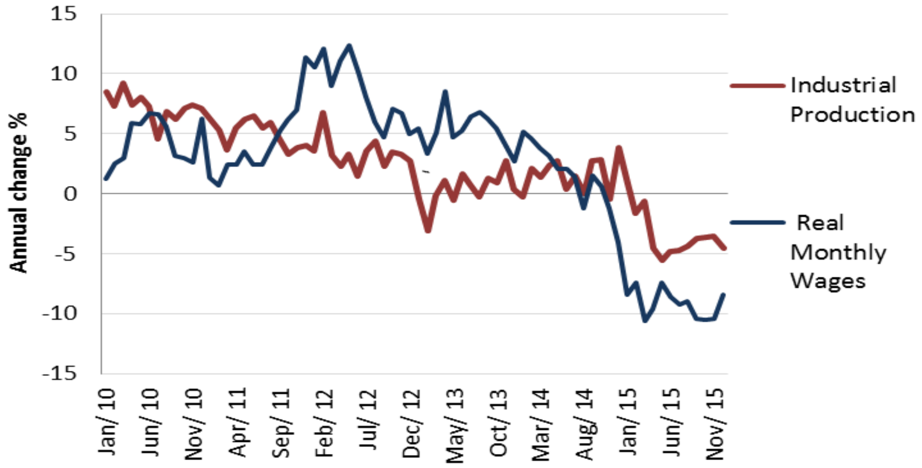
The Russian economy has suffered from the decline in oil prices, as its economy is very much geared towards the energy sector. As a result, retail sales suffered double-digit negative growth rates throughout 2015, equally spread between food and non-food items.

Figure 1.24 Retail sales and oil price

Source: Bloomberg

A similar picture emerges when considering industrial production and wage growth. Both have experienced some sort of consolidation, albeit at a low level throughout 2015.

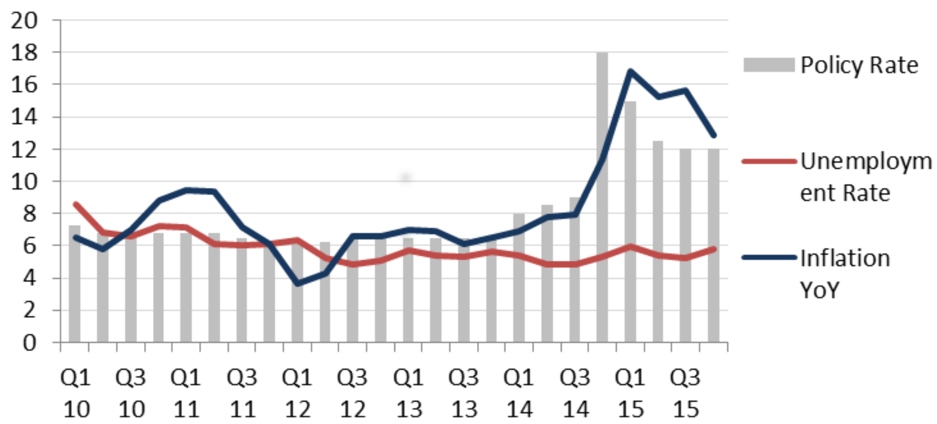
Figure 1.25 Industrial production and real wage growth in Russia



Source: Bloomberg

The only indicator which recorded some improvement over the course of 2015 was inflation which came down from a high of almost 16% to a level below 13% by the end of 2015. Unemployment could be contained below 6% throughout the year. The central bank which started to ease monetary conditions over the course of the year did not change the policy rate though.

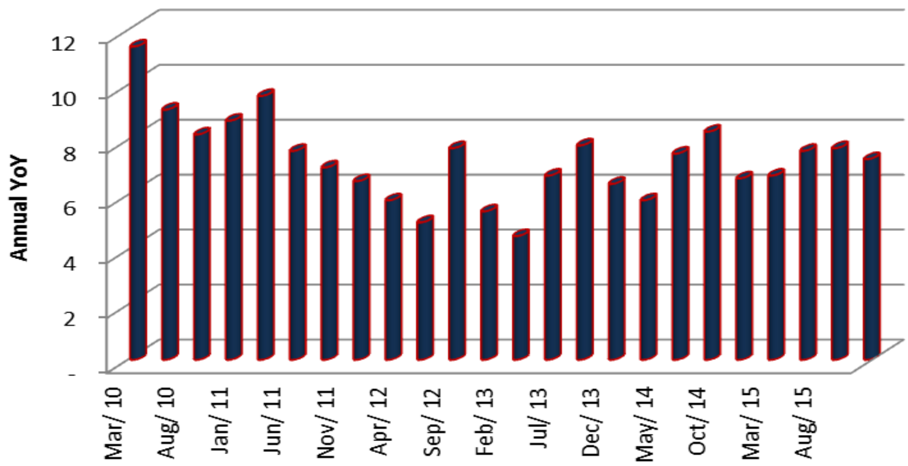
Figure 1.26 Policy, Unemployment & Inflation Rates in Russia (%)



Source: Bloomberg

India has been growing on average at 7.3% in 2015, driven by improved consumer sentiment which was buoyed by lower oil prices.

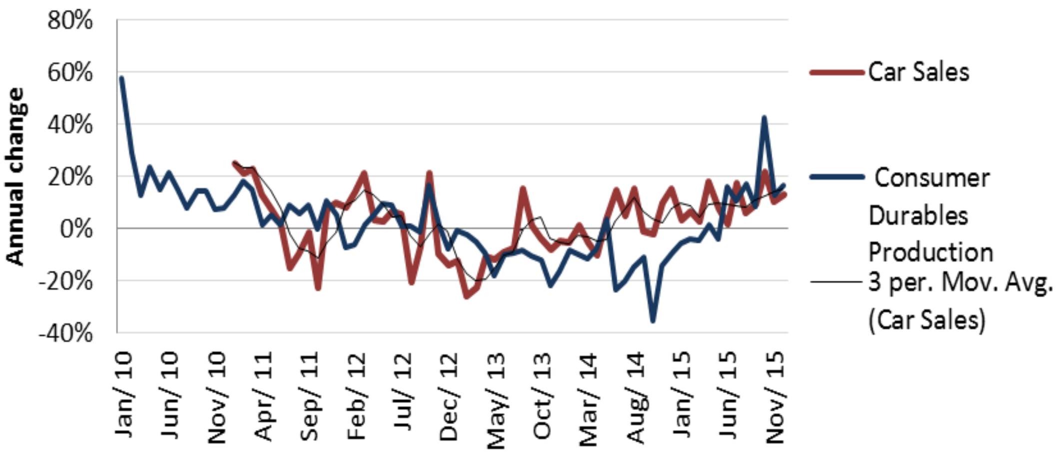
Figure 1.27 India Real GDP Growth (YoY)



Source: Bloomberg

Car sales which are 'big ticket' items for consumers are growing at double digit rates, supporting the notion that India is benefiting from lower oil prices as it increases the spending power. Domestic passenger car sales, which have tracked well with India's GDP, picked up in the first part of the calendar year and have accelerated since September. Low inflation has enhanced the spending power of households. Lower oil prices reduce the cost of operating a vehicle, and lower oil import values reduce the drag on growth from the trade deficit. Consumption accounts for 56% of India's economic activity. This picture is in line with the development of consumer durables production which has grown by an annual 16% by the end of 2015.

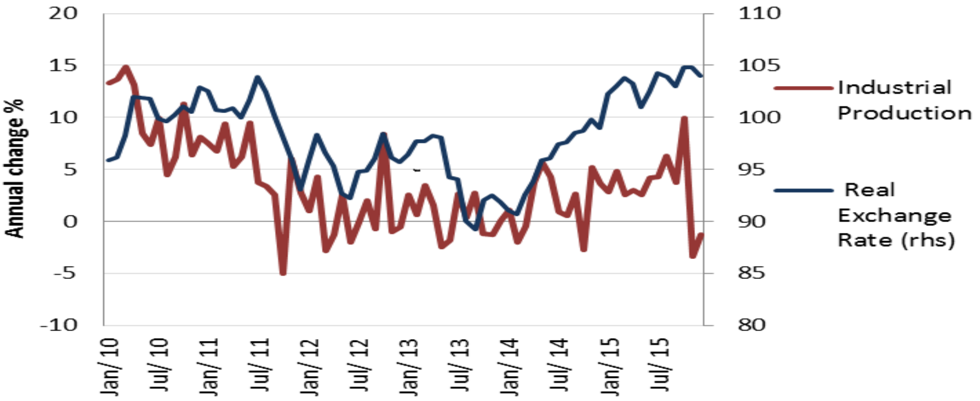
Figure 1.28 Car Sales & Consumer Durables Production in India



Source: Bloomberg

Similar to car sales, industrial production increased steadily in 2015 with the exception of the last 2 months of 2015. But this is partly due to a base effect, as industrial production jumped by over 5% in November and December 2014. The improvement happened against the backdrop of a rising Rupee in real effective terms.

Figure 1.29 Industrial Production and the Real Effective Exchange Rate in India



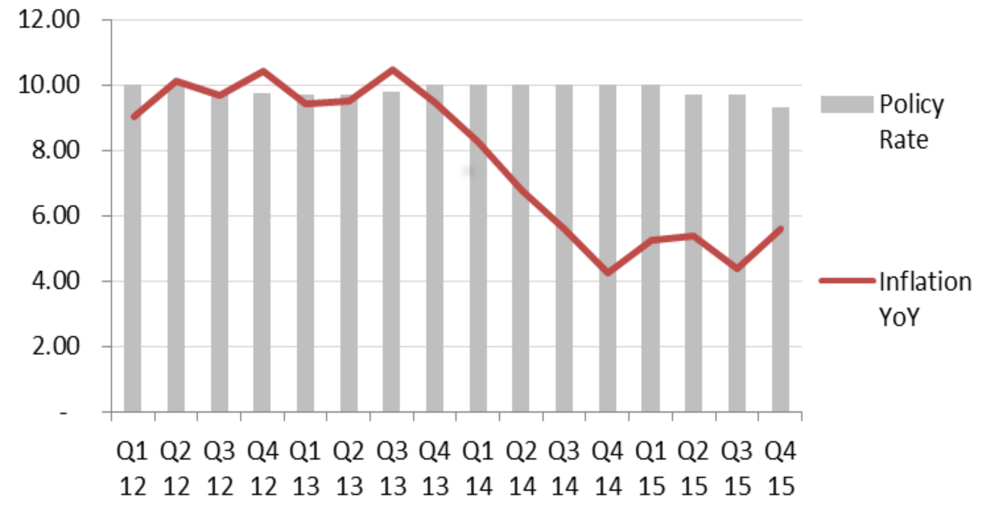
Source: Bloomberg

Earnings at Indian banks are under pressure as they increased provisions for stressed assets to meet a March 2017 deadline set by the Reserve Bank of India to bolster lenders' balance sheets. The central bank is striving to pare the ratio of restructured and soured loans to total advances from a 14-year high and reverse a slowdown in lending.

Over the course of 2015, monetary authorities have reduced the policy rate by 70 bp against the backdrop of an inflation which oscillated around 5% during the course of 2015. Slightly stronger economic activity is also increasing price pressures, and households' inflation expectations have yet to peak.

The RBI's next interim objective is to deliver inflation near 5% by March 2017. Implementation of a national goods and services tax, which will reduce structural inflation, will be critical for meeting this goal unless oil prices continue to languish. In 2015, the central bank adopted a formal target for the consumer price index, after a longstanding focus on the wholesale price index. The goal is to deliver inflation of 4% plus or minus 2%, starting March 2017.

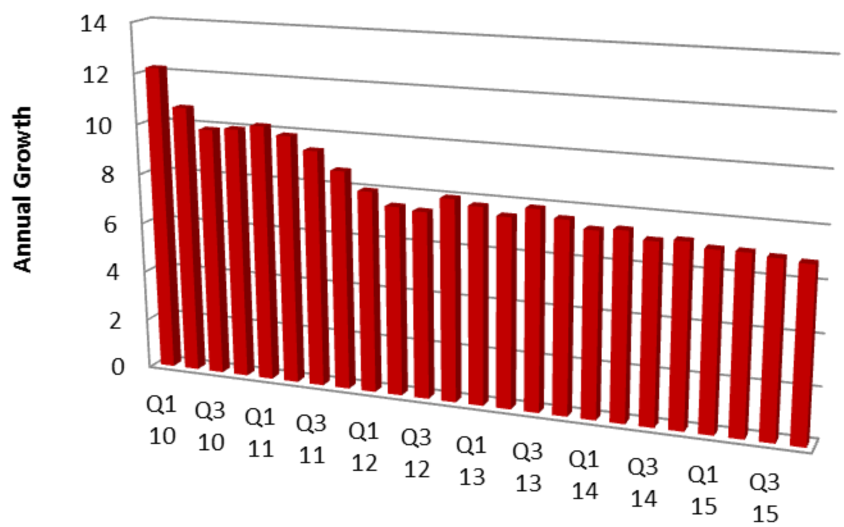
Figure 1.30 Policy and inflation rate in India (%)



Source: Bloomberg.

China managed to grow by 6.9% in 2015, down from 7.3% in 2014; the lowest since 1990, but in line with the government's target for the year. The central bank cut the interest rate, lending accelerated and the Yuan duly depreciated.

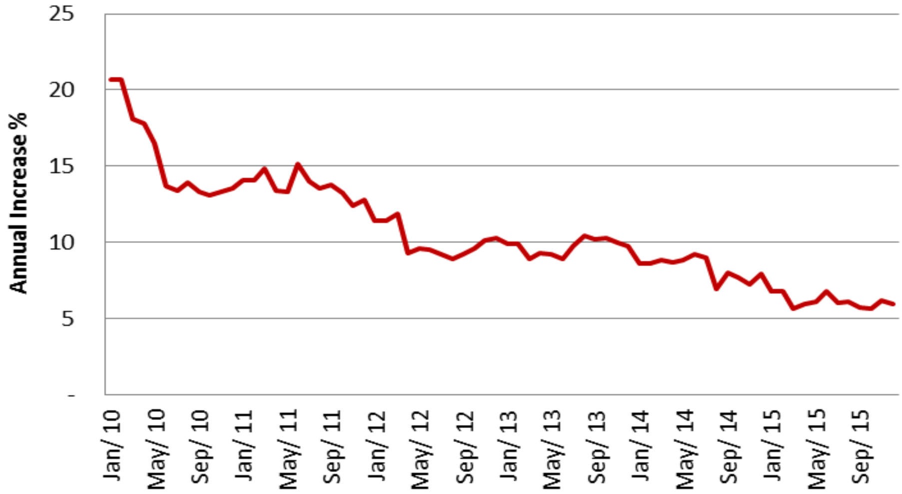
Figure 1.31 Annual GDP growth in China (%)



Source: Bloomberg

Monthly data show the economy losing a little momentum at the end of the year. Industrial output slowed to 5.9% year-on-year in December 2015, down from 6.2% in November. That partly reflected a higher base for comparison as output accelerated at end of 2014.

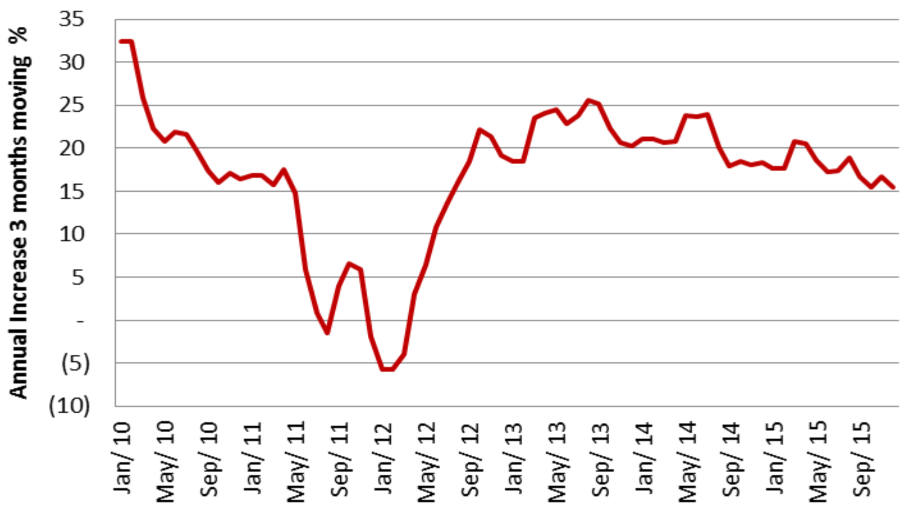
Figure 1.32 Industrial Output



Source: Bloomberg

Also infrastructure investment which is very much supported by government intervention slowed in 2105, but is still growing at a healthy 15% rate in December 2015.

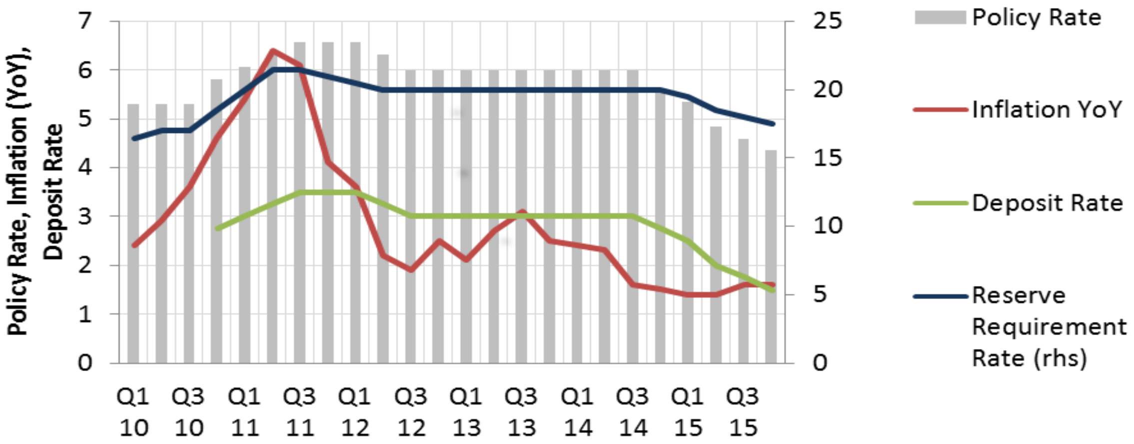
Figure 1.33 Infrastructure Investment YoY (3-months rolling) (%)



Source: Bloomberg

China's authorities have reacted to the slowdown in its economy by lowering their policy rate to 4.35% in the last quarter of 2015 down from 5.6% in the fourth quarter of 2014. Also the deposit rate was lowered by 125bp to 1.5% in the fourth quarter down from 2.75% by the end of 2014. The reduction in the reserve requirement to 17.5% down from 20%, during the same period, was also designed to support slowing economic activities. Inflation stayed its course over the year, ending at 1.6%, barely changed from the 1.5% by the end of 2014.

Figure 1.34 Policy, deposit, inflation and reserve requirement rates in China (%)



Source: Bloomberg

5. MENA Economies

The Middle East and North Africa (MENA) regional outlook is mainly driven by geopolitical consideration and oil price developments. Regional political risks arising from the conflicts in Iraq, Libya, Syria and Yemen are impacting heavily investor confidence in the whole region, while security is impacting the economic situation in post-revolutionary Egypt and Tunisia.

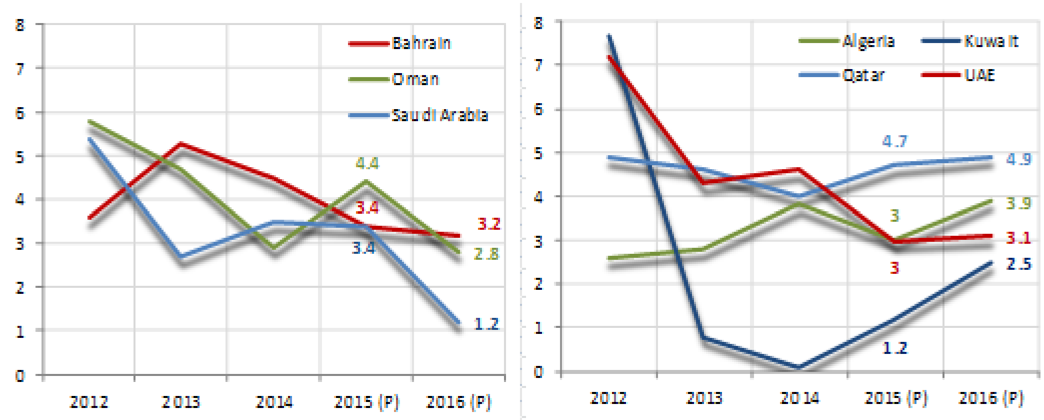
Overall, according to the IMF revised projections of October 2015, the MENA growth was moderate during the year for the GCC countries, while oil importers are benefitting from lower oil prices, but facing shrinking demand, particularly from Europe.

5.1 Oil-exporting countries

Economic Growth

The slowdown in the GCC region is due mainly to the fact that the slump in oil prices turned out to be more pronounced and more persistent in 2015 than previously expected. As a result, the fall in government revenue forced the authorities to initiate fiscal consolidation, which in tandem with tightening liquidity led to decelerated growth, albeit at varying degrees.

Figure 1.35. Real GDP Growth for Oil-exporting countries



Source: IMF, Regional Economic Outlook-October 2015 and CBUAE analysis.

Inflation

Inflation in oil-exporting countries is moderating; due to decelerating prices of food and other imported goods and services on account of the appreciating U.S. dollar to which most of these countries peg their currencies. The exception in the UAE could be explained by the increase in the price of housing and non-tradables in general (see table 1.1.a).

Table 1.1.a. Inflation in the GCC countries (%)

	2014	2015
Saudi Arabia	2.7	2.2
Bahrain	2.7	1.9
Kuwait	2.9	3.3
Oman	1.0	0.0
Qatar	3.3	1.6
UAE	2.3	4.1

Source: Official data, and IMF Regional Economic Outlook-October 2015.

Stock Markets

On the back of persistent low oil prices, diminishing government expenditures, global economic slowdown and market uncertainty, GCC stock markets witnessed a slump in 2015, which was particularly pronounced for Saudi Arabia (-17.1%), Dubai Financial Market and Kuwait Stock Exchange (-16.5%) Qatar (-15.1%), and Oman (-14.8%)

Table 1.1.b. Stock Market Share Prices change in GCC countries (%)

	2014	2015
Saudi Arabia	2.4%	-17.1
Bahrain	-5.0%	-12.3
Kuwait	5.8%	-16.5
Oman	7.7%	-14.8
Qatar	-15.5%	-15.1
UAE		
- ADSM	-5.3%	-4.9
- DFM	-10.7%	-16.5

Source: Bloomberg.

5.2 Oil-importing countries

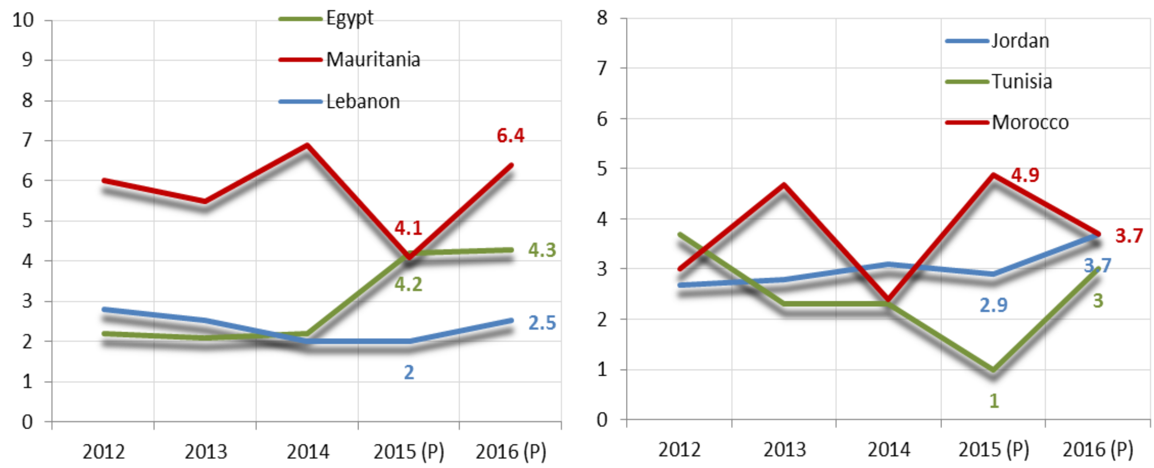
Economic Growth

Recovery in some oil-importing countries is gaining momentum, with average growth expected to rise to 4% in 2015. Low oil prices are beginning to improve the fiscal outlook, and support confidence, investment, and external balances.

However, a stronger rebound in economic activity is being held back by spill overs from the devastating conflicts in Iraq, Libya and Syria that are also intensifying security and social tensions in neighbouring countries, especially Lebanon. In addition, supply-side bottlenecks, restrictions on the business environment and inadequate education and skills, continue to hamper competitiveness and productivity. Therefore, unemployment remains high and large swathes of the population do not benefit from inclusive growth, notably in remote and disadvantaged areas.

Oil-importing countries continue also to suffer in 2015 from reduction in exports, tourism receipts, and remittances due to weak growth in the Euro Area and slowdown in the GCC region. The start of normalization of U.S. monetary policy in December 2015, moreover, sparked more financial market volatility, and tightening financing. In this challenging environment, stepping up the reform momentum is imperative for oil-importers, as they can also take advantage of low inflation and improved fiscal situation to adopt structural changes that would be more difficult in periods of higher prices.

Figure 1.36. Real GDP Growth for Oil-importing countries



Source: IMF, Regional Economic Outlook-October 2015

Inflation

The year 2015 witnessed persistently large negative output gaps and low international food prices, which reduced inflation while energy subsidy phase-outs, currency depreciation, monetization of fiscal deficits, and accommodative monetary policies, were expected to put some upward pressure on prices, especially given the fact that the pass-through of lower international oil and other import prices remains weak, owing to low competition and other hindrances. As a result, the near-term benefits from lower international oil prices for firms' production costs and household incomes in most of the countries remain limited.

Table 1.1.c. Inflation in some Oil-Importing countries (%)

	2014	2015
Oil Importers in MENA	**9.4**	**6.6**
Egypt	10.1	9.5
Jordan	2.9	0.2
Morocco	0.4	1.5
Tunisia	4.9	5.0

Source: IMF, Regional Economic Outlook-October 2015

Stock markets

Share prices continued their decline in most oil importing countries in 2015, consistent with the global capital markets volatility and weak fundamentals. The slump is more pronounced for Egypt (-24.4%) and Morocco (-7.5%).

Table 1.1.d Stock Market Share Prices change for some MENA oil-importing countries (%)

	2014	2015
Egypt	-19.0%	-24.4
Jordan	-4.6%	-1.3
Morocco	-5.4%	-7.5
Tunisia	-13.9%	-0.9

Source: Bloomberg.

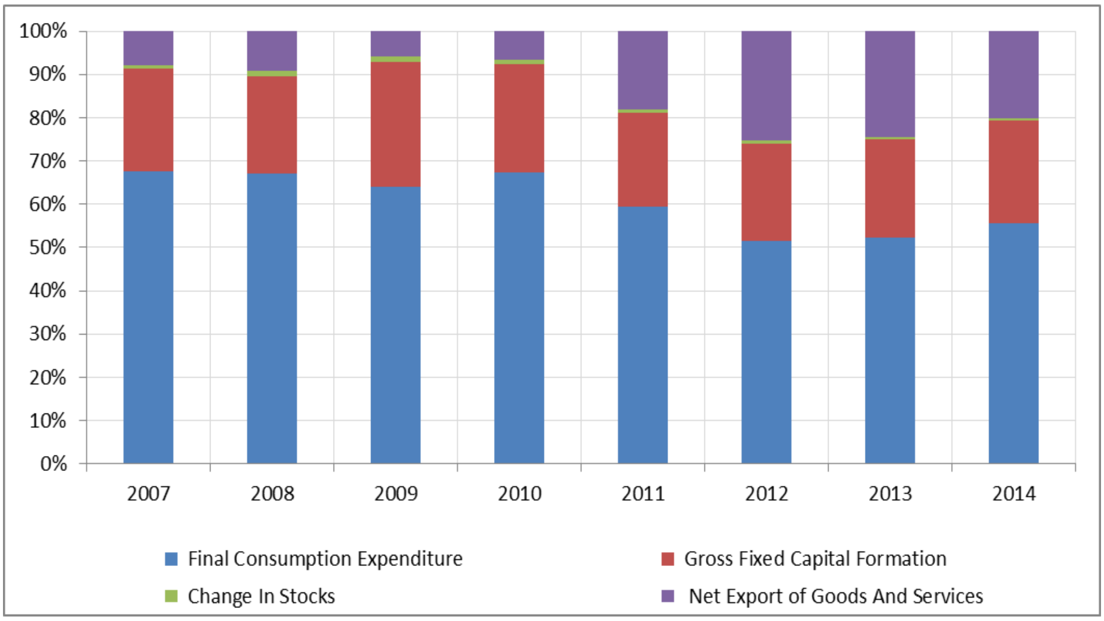
Chapter 2. Domestic Economic Developments

Economic growth has slowed down. However, the diversification of the economy has helped to mitigate the impact of declining oil prices as evident by robust, albeit declining, growth of non-oil activities. The fiscal consolidation started in 2015 by reforming electricity and fuel subsidies. Despite global slowdown and tumbling securities markets, credit growth remained robust, in support of non-oil growth, during the year.

2.1 Economic Growth and the non-hydrocarbon sector

The UAE economy in 2015 was hit by the decline of oil prices as well as the slowdown of the Chinese economy, a major trading partner. The adverse impact of these shocks is partially damped by the increasing diversification of the economy. In testament of more diversified export structure, net exports have had an increasing contribution to economic growth over time, creating a balanced growth picture, alongside the domestic demand. The contribution of net exports of goods and services to the GDP has increased gradually over time from 6.5% in 2010, to reach around 20% in 2014 (see figure 2.1)[1].

Figure 2.1 GDP decomposition 2007-2014 (percent of GDP)



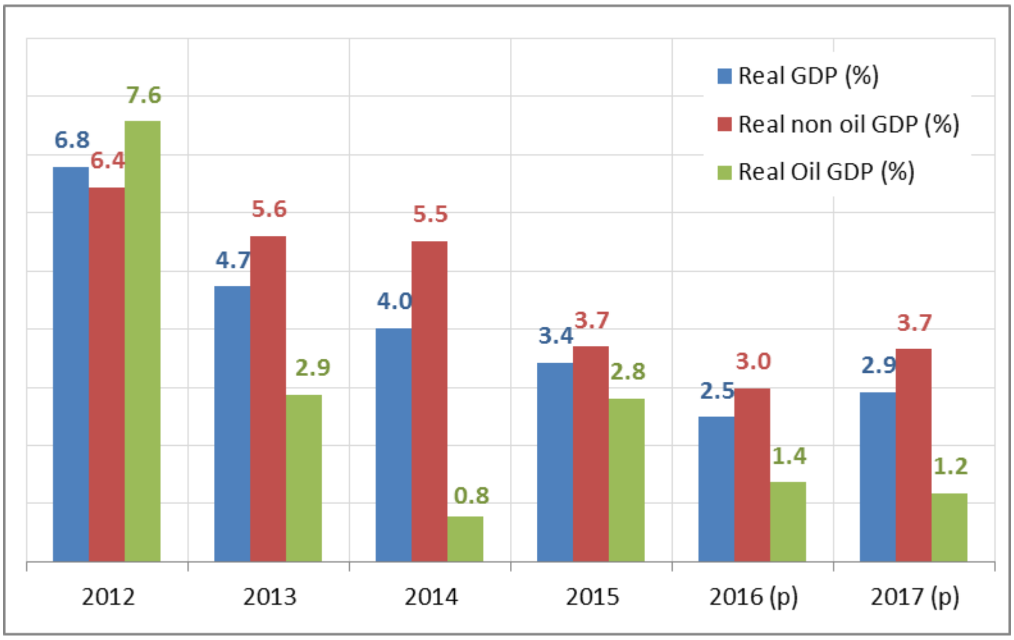
Source: Federal Competitiveness and Statistics Authority - National Accounts Division

Based on the recent data release, the total real GDP grew by 3.4% in 2015, in contrast to 4.0% growth in 2014 (see figure 2.2). This slowdown is due mainly to the decline of real oil GDP growth, which increased by around 2.8% in 2015. Oil prices fell significantly in 2015,

[1] Data for 2015 are not available.

reaching new 11-year lows. Concerning the non-hydrocarbon economic activity, the real non-oil GDP growth slowed down in 2015 to reach a growth rate of 3.7% against 5.5% in 2014. These results are in line with Central Bank estimations for 2015.

Figure 2.2 GDP growth and economic activity in the U.A.E

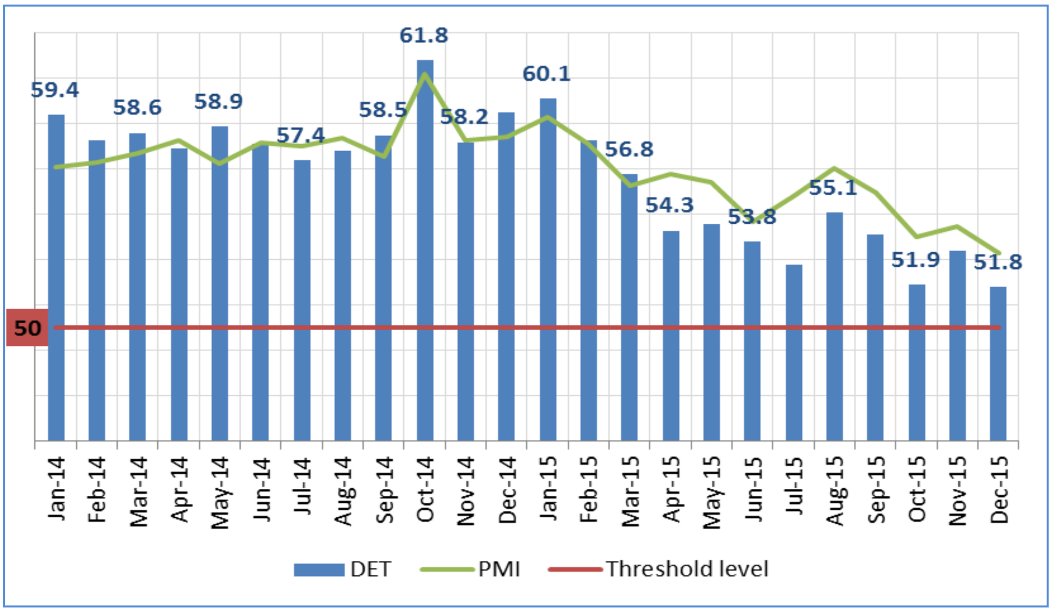


Source: CBUAE

The Purchasing Manager's Index (PMI) and the Dubai Economic Tracker (DET), indicators of the economic activity, based on surveys of the non-oil economic developments in the private sector in the UAE and Dubai, respectively, have decreased significantly in 2015 (see figure 2.3). While the absolute index value remains higher than the 50-threshold during the whole year, the end-of-period PMI declined by 12% in 2015 compared to 2014, signaling slower -but positive- growth in the non-oil private sector. The DET followed a similar path. The end-of-period level declined by around 13% in 2015.

Both the PMI and the DET are derived from individual diffusion indices which measure changes in different economic indicators. The Purchasing Managers Index is based on five individual indices with the following weights: New Orders (30%), Output (25%), Employment (20%), Suppliers' Delivery Times (15%) and Stock of Items Purchased (10%). All sub-indices decreased in 2015. Although firms reduced average output prices by 1.4% in 2015, in a bid to generate new orders, the average New Orders index declined by more than 8% in 2015 compared to 2014. In addition, the average Output and employment sub-indices fell each by 2.2% in 2015, and the backlogs of work index decreased by around 1% reflecting the reduction of new orders and suggesting a downward pressure on production capacity. Overall, the PMI pointed to weaker domestic and external demand in 2015.

Figure 2.3 Non-oil economic activity in the U.A.E



Source: Markit & Emirates NBD

2.2 Consumer Price Index and Inflation

The consumer price index increased on average by 4.1% in 2015 (see figure 2.5). UAE CPI inflation is driven mainly by the housing inflation. Housing prices, covering rental price, electricity, and water and gas prices constitute around 39% of a standard consumption basket in the UAE (see figure 2.4). Average housing prices increased by 8.8% in 2015, with a contribution to the total annual inflation of 3.4%. In contrast, the housing CPI inflation was only around 3.2% in 2014, with a contribution to the total CPI inflation by 1.2%. The most important increase in 2015 was for the electricity price; which increased by more than 23% due to the electricity subsidy reform in 2015. Housing rental prices increased by 8%, in 2015 due mainly to the widening gap between demand and supply. The price of food and transportation which constitute altogether 24% of the consumption basket increased by 1.2% and 2%, contributing to the total inflation by 0.17% and 0.2%, respectively in 2015. Although education accounts only for 4% in the total consumption basket, its contribution to the total inflation equals 0.15%. Education costs increased by more than 3.7% in 2015 because of the increased demand for private schooling and higher quality education.

The textile and clothing, and furniture industries account for 12% of the total consumption basket. The average CPI inflation of the textile and clothing industries decreased in 2015 by 1.6%, while it increased by more than 0.2% in 2014. CPI inflation of the furniture industry increased only by 2.2% in 2015, in contrast to an increase in 2014 of around 4.3%. This result can be attributed to the reduction of imports prices due to the continued Dirham's appreciation with respect to the currencies of major non-dollarized trading partners for imports. Although there is no confirmed evidence on the existence and the degree of the exchange rate pass-through, the lower CPI inflation of most imported goods in 2015 (compared to 2014) provides some evidence to solidify the argument.

Figure 2.4 Standard Consumption basket composition in the U.A.E

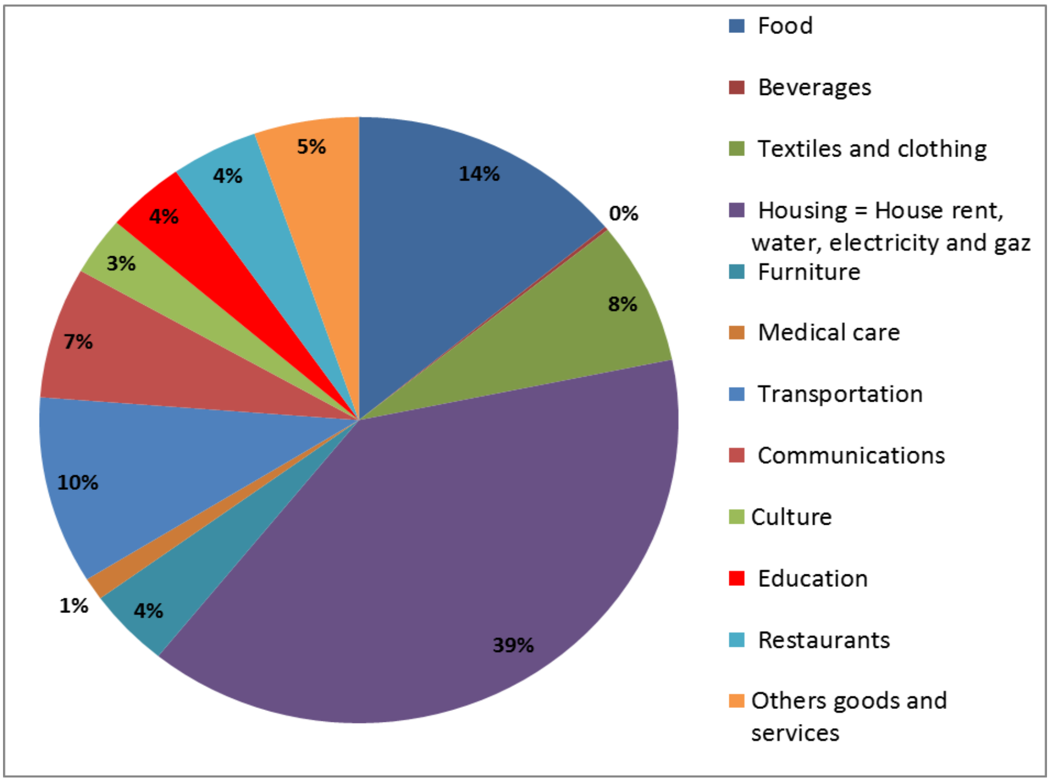
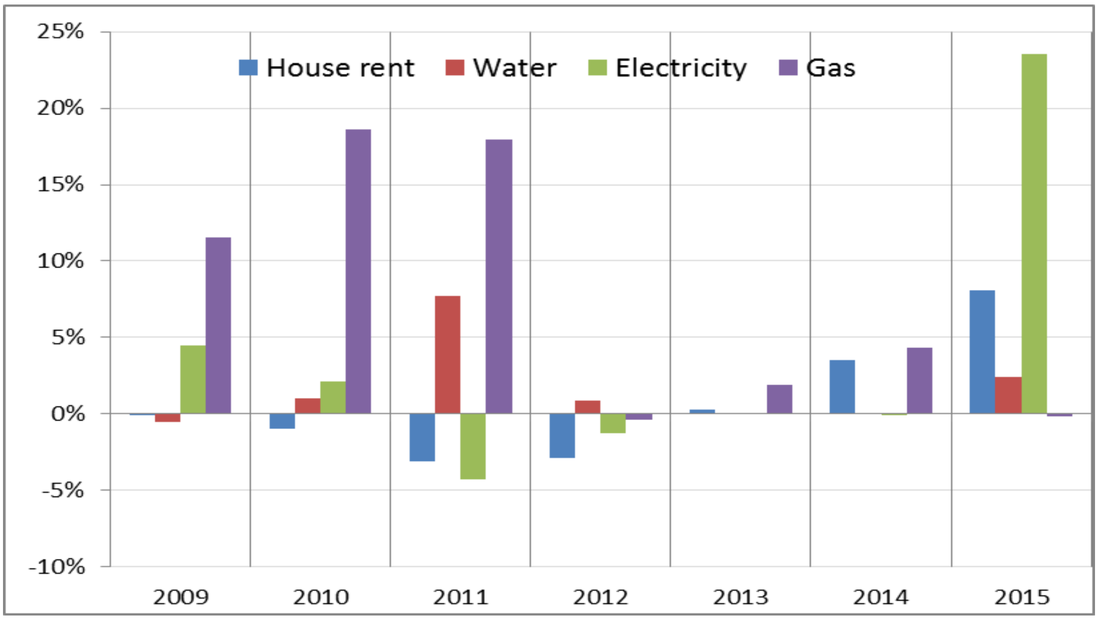
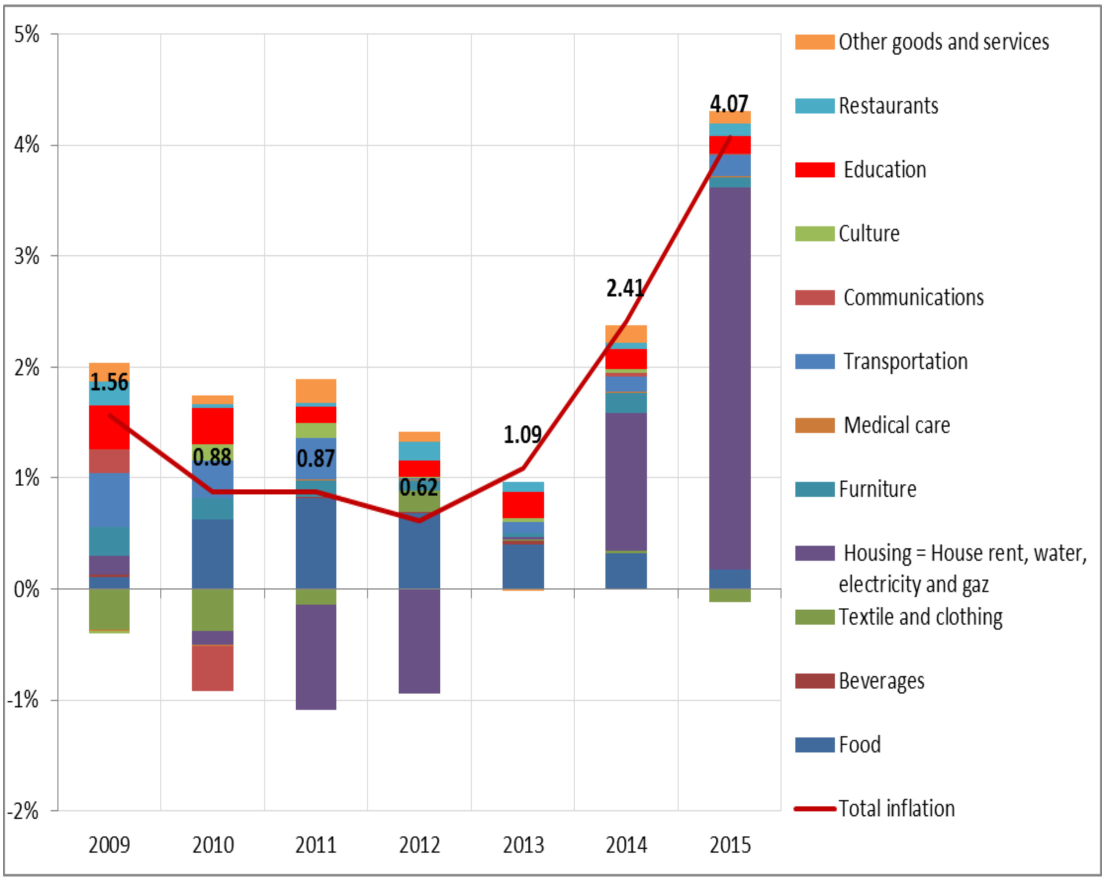


Figure 2.5 CPI inflation of Housing sub-components



Source: Federal Competitiveness and Statistics Authority

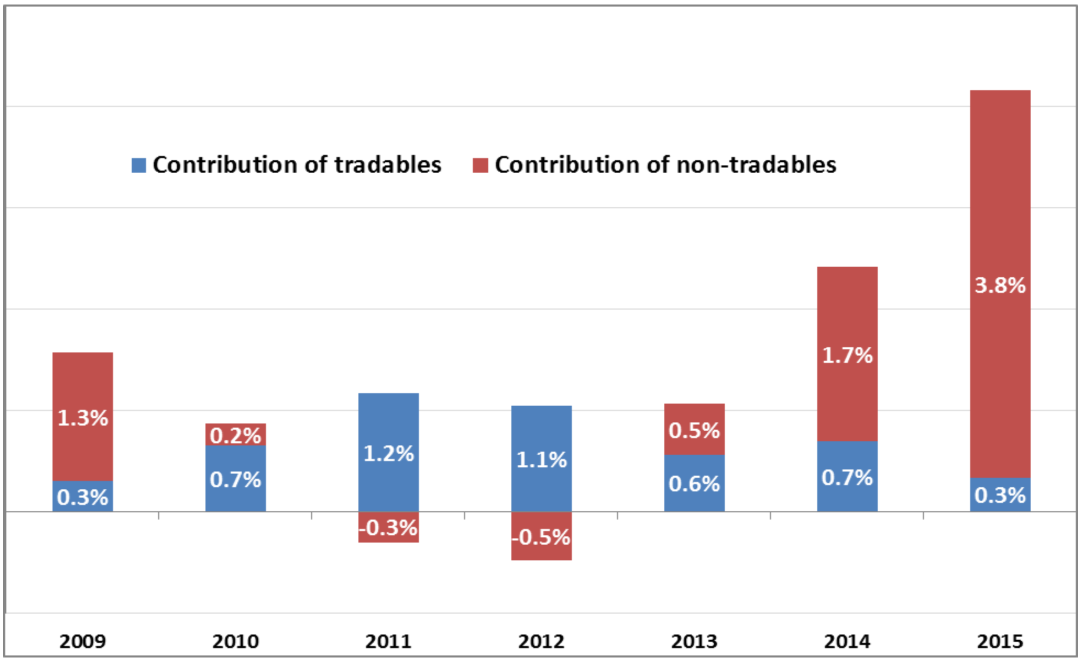
Figure 2.6 Contribution of different sub-components to the total CPI inflation



Source: Federal Competitiveness and Statistics Authority

The development of the CPI inflation of different sub-components summarizes the change of the CPI inflation of two major consumption blocks: tradable goods and non-tradable goods. The tradable goods account for around 34% of the consumption basket, while the non-tradable goods account for 66% where housing prices represent 59% of non-tradables. The CPI inflation of non-tradables was the main driver of the total CPI inflation in 2015. Non-tradable inflation increased by 3.8% in 2015 where the CPI of tradables increased only by 0.3% (see figure 2.7). The contribution of the CPI inflation of non-tradables became dominant and increased significantly during the last three years (0.5% in 2013, 1.7% in 2014). Housing prices are responsible for such increasing trend. The contribution of housing (39% of the CPI basket) to the total CPI inflation increased from 0.02% in 2013 to 1.2% in 2014 and 3.4% in 2015.

Figure 2.7 Contribution of Tradables and Non-tradables components to the total CPI inflation



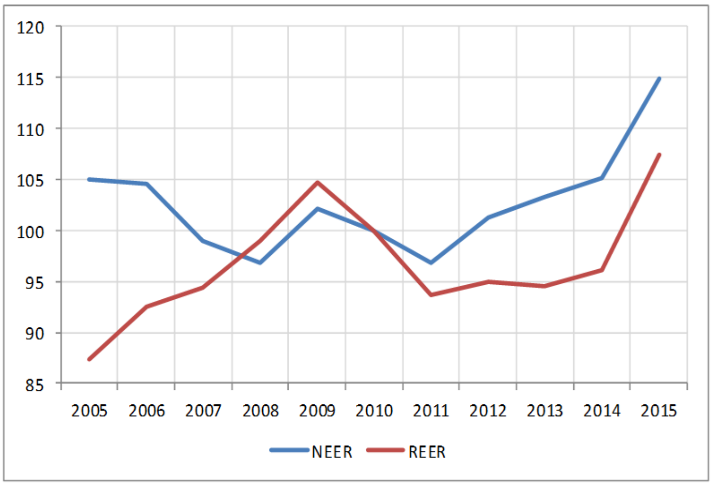
Source: Federal Competitiveness and Statistics Authority

2.3 Exchange Rate appreciation and Competitiveness

Reflecting developments of the US Dollar exchange rate, the effective real exchange rate (REER) of the dirham (based on consumer prices) [2] appreciated by around 12% in 2015 compared to 2014 (see figure 2.8), in contrast to a total appreciation by about 15% during the period 2011-2015.

On the other hand, the analysis of the bilateral exchange rate with main trade partners shows a continuous appreciation of the Dirham against the currencies of both export and import partners.

Figure 2.8. Real and Nominal Effective Exchange rates



Source: BIS

[2] The REER is an average of the bilateral real exchange rates between the country and each of its trading partners, weighted by the respective trade shares of each partner.

Table 2.1.a Dirham appreciation against currencies of top non-dollarized import partners

Currency	Share of UAE imports (%) 2014	Exchange rate 2014	Exchange rate 2015	% Change of Currencies per Dirham 2014	% Change of Currencies per Dirham 2015
Chinese Yuan	11.68	1.6776	1.7110	0.22	1.99
Indian Rupee	9.19	16.6094	17.4621	4.02	5.13
Germany (EUR)	6.09	0.2053	0.2454	0.15	19.53
Japanese Yen	5.55	28.84	32.96	8.50	14.29
UK Pound	3.53	0.1654	0.1782	-5.00	7.74
Swiss Franc	3.38	0.2493	0.2621	-1.19	5.13
Italy (EUR)	3.09	0.2053	0.2454	0.15	19.53
South Korean Won	2.95	286.8252	308.2172	-3.77	7.46
France (EUR)	2.54	0.2053	0.2454	0.15	19.53
Total	**48.00**				
Weighted Appreciation				**0.56**	**4.45**

Source: Federal Competitiveness and Statistics Authority and Bloomberg

Table.2.1.b Dirham appreciation against currencies of top non-dollarized partners for non-oil export

Currency	Share of UAE exports (%) 2014	Exchange rate 2014	Exchange rate 2015	% Change of Currencies per Dirham 2014-2013	% Change of Currencies per Dirham 2015-2014
Indian Rupee	14.85	16.6094	17.4621	4.02	5.13
Saudi Arabian Riyal	8.17	1.0212	1.0213	0.01	0.01
Omani Rial	6.61	0.1048	0.1048	0.01	0.01
Swiss Franc	6.34	0.2493	0.2621	-1.19	5.13
Turkish Lira	5.4	0.5960	0.7424	14.84	24.56
Iraqi Dinar	4.72	318.9919	327.3815	0.51	2.63
Kuwaiti Dinar	4.48	0.0775	0.0820	0.26	5.81
Egyptian Pound	3.65	1.9274	2.0982	2.97	8.86
Chinese Yuan	3	1.6776	1.711	0.22	1.99
Total	**57.20**				
Weighted Appreciation				**1.47**	**3.18**

Source: Federal Competitiveness and Statistics Authority and Bloomberg

The weighted exchange rate with respect to the top 9 non-dollarized import partners, which accounts for 48% of total imports, has appreciated by 4.5% in 2015, against an increase of only 0.56% in 2014 (See table 2.1.a). These developments are a result of a considerable depreciation of all these currencies against the Dirham. The EURO is leading the stream of depreciating currencies against the Dirham. It lost more than 19% in 2015, while it depreciated relative to the dirham only by around 0.2% in 2014. The Japanese Yen lost more than 14% relative to the dirham in 2015. It is worth noting that Germany, Italy, France and Japan represent together a total of 17.3% of the total imports to the UAE. The UK Pound and the South Korean Won lost around 7% each against the Dirham in 2105.

On the non-energy exports side, the weighted average dirham exchange rate variation with respect to the top 9 non-dollarized export partners, which accounts for more than 57% of the total exports, appreciated by around 3.2% in 2015% against a weighted appreciation of the Dirham of 1.5% in 2014 (see figure 2.1.b). This appreciation is driven primarily by the depreciation of the Indian Rupee and the Turkish Lira. The two countries are contributing altogether by more than 20% to the total Emirati non-energy exports. Both currencies depreciated by around 5% and 25%, respectively. The Egyptian Pound lost also around 8.9% during 2015, against the Dirham.

The appreciation of the Dirham against major non-export trading partners raised some concerns about the country's competitiveness. Table 2.2 summarizes a preliminary overview of the developments of real non-hydrocarbon foreign trade (real imports, real exports and real re-exports) during the first 9 month of 2015[3]. The continuous appreciation does not seem to have hindered the country's competitiveness. The real non-oil exports and re-exports experienced a positive growth. During the first 9 months of 2015, they grew by around 7% and 3.4%, respectively. This result can be attributed to the enhancement of the role of the private sector and the continuous diversification process of the economy, capitalizing on the productivity gains. On the other hand, the dirham's appreciation allowed for the real imports to increase by 1%. The cheaper imports are supposed to put some deflationary pressure on consumer prices and reduce the cost of intermediate imports that are used in non-energy exports.

[3] Only data for the first 9 months of 2015 are available.

Table.2.2 Dirham's Appreciation and Foreign Trade

		2014	2015
Real Imports	Dirham's weighted appreciation*	-0.02	4.84
	% change *(with respect to the previous year)*	-13.0	1.0
Real Non-Oil Exports	Dirham's weighted appreciation**	1.51	3.12
	% change *(with respect to the previous year)*	5.5	6.9
Real Re-Exports	Dirham's weighted appreciation**	1.51	3.12
	% change *(with respect to the previous year)*	13.67	3.36

Source: Federal Competitiveness and Statistics Authority and Bloomberg

2.4 Fiscal balance

Based on detailed revenues data available from the Ministry of Finance (see table 2.3), these revenues covered around 80% of the total expenditures in 2015 against a coverage rate of 92% in 2014. This is due mainly to the decrease of these revenue items by 25%, which remains more proportional than the total expenditure decline (15%).

The revenues' decline is generated by the cut in tax revenues by 37%, reflecting reduction in taxes on oil companies in 2015 (see figure 2.9.a). Social contributions decreased by 15% compared to 2014. On the expenditures side, except for the compensation of employees and the consumption of fixed capital, which increased by 24% and 17%, respectively, all expenditure items decreased (2.9.b). Subsidies fell by around 84% because of the subsidy reform pressed by the government in 2015, in addition to decline in transfers to Government Related Enterprises (GREs). The subsidy reform involved electricity and retail fuel subsidies. They were implemented in early 2015 and in August 2015, respectively. Fuel prices were set in accordance with global oil price benchmarks. Although these reforms put an inflationary pressure on housing and transportation prices, they resulted in budget savings of around 3% of total expenditures.

Table.2.3 Consolidated Government Finances

	2014					2015					% change
	Q1	Q2	Q3	Q4	2014	Q1	Q2	Q3	Q4	2015	2015-2014
Revenues (a)	**90.2**	**98.1**	**94.5**	**97.8**	**380.7**	**74.9**	**84.2**	**64.8**	**60.7**	**284.7**	**-25.2**
Taxes	68.1	67.8	75.5	68.4	279.9	54.9	50.6	41.9	28.1	175.4	-37.3
Social contributions	0.9	1.6	0.4	2.4	5.3	1.1	1.1	1.0	1.3	4.5	-14.6
Other revenues	21.2	28.7	18.6	26.9	95.5	19.0	32.5	21.8	31.4	104.7	9.6
Expenditure (b)	**104.0**	**103.7**	**98.9**	**107.9**	**414.6**	**87.0**	**93.1**	**83.9**	**90.3**	**354.4**	**-14.5**
Compensation of employees	10.6	11.4	11.4	14.1	47.5	14.4	15.8	14.5	14.4	59.1	24.4
Use of goods and services	8.9	12.1	13.8	14.7	49.5	10.5	13.5	10.8	16.3	51.0	3.0
Consumption of fixed capital	0.9	0.7	1.0	1.1	3.8	0.9	1.1	0.9	1.5	4.4	16.7
Interest	1.0	1.0	0.9	1.2	4.1	0.5	0.5	0.6	1.3	2.9	-29.5
Subsidies	2.5	3.6	3.4	2.6	12.1	0.2	0.2	1.4	0.1	1.9	-84.4
Grants	9.8	6.2	5.5	0.4	21.9	3.1	2.8	2.5	2.1	10.6	-51.8
Social benefits	12.6	13.8	16.1	18.8	61.4	12.9	15.2	13.5	11.6	53.2	-13.4
Other expense	52.3	41.0	37.2	43.9	174.4	39.9	35.4	33.4	37	145.7	-16.4
Net Acquisition of Nonfinancial Assets	5.5	13.7	9.5	11.2	39.9	4.7	8.7	6.4	5.9	25	-35

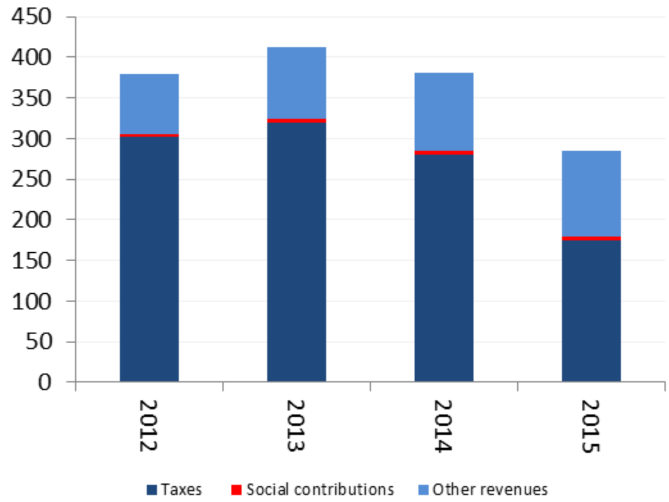
Source: UAE Ministry of Finance

Note: All values are expressed in Billions of Dirhams. 'Other revenues' category covers mainly property income (interest, dividends, rent), Sales of goods and services including administrative fees, fines and penalties.

Government Finance

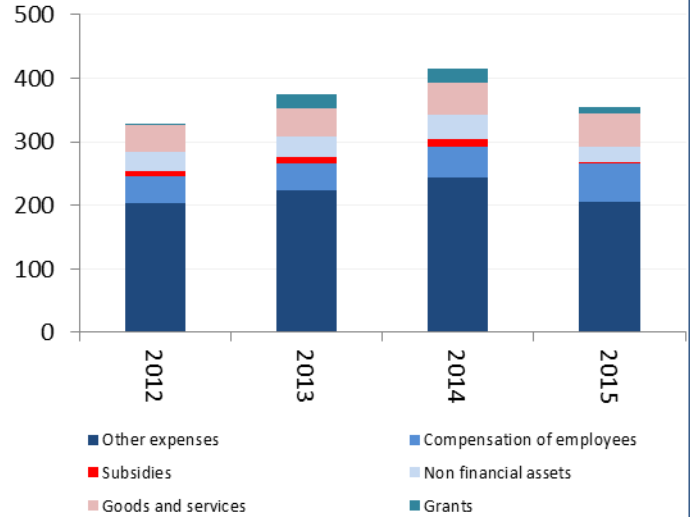
2.9. a General Government Revenues

(Billions of Dirhams)



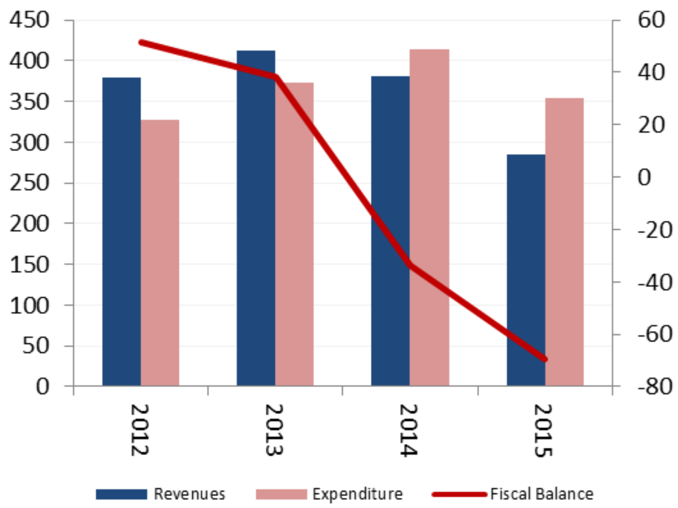
2.9.b General Government Expenditures

(Billions of Dirhams)

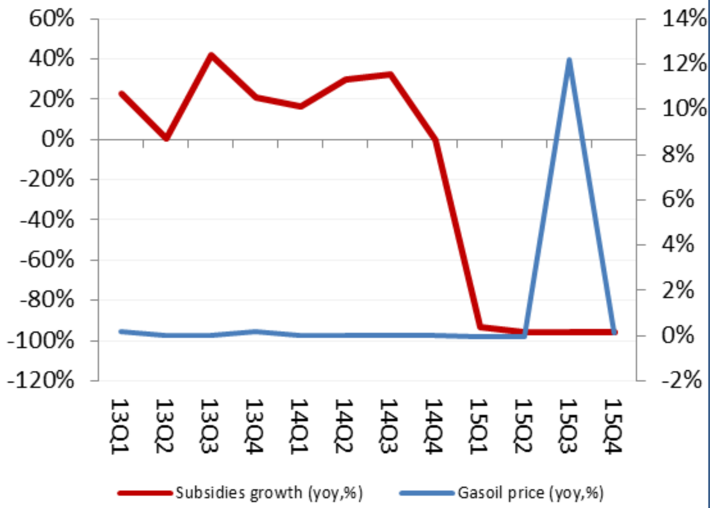


2.9.c Fiscal Stance

(Billions of Dirhams)



2.9.d The total subsidies and Gasoil price development



Source: Ministry of Finance and National Competitiveness and Statistics Authority
Note: Other expenses cover all the payments of Abu Dhabi Government made on behalf of the federal government, including the Armed Forces expenditures.

2.5 Financial developments

2.5.1 Share Price Volatility

The share price index declined by around 7% in 2015 (see table 2.4.1). The global uncertainty accompanied by the huge gyrations in oil prices impacted adversely investors' confidence. This resulted in a decline of the market capitalization by around 5%. The Emirates Securities Market General Index was quite sensitive to economic developments in China. The continued slowdown of the Chinese economy raised concerns about external demand and the futures of the oil.

Table 2.4.1 UAE – Securities Markets

	2012	2013	2014	2015
Change of Share Price Index (%)	9.4	68.4	6.1	-6.6
Change of Market Capitalization (%)	9.5	70.5	12.7	-4.7
Annually Traded Value (AED billions)	58.4	244.5	525.8	209.4

Source: UAE Securities and Commodity Authority and Bloomberg.
Note: Changes computation is based on end-of-period numbers for the share price index and market capitalization.

2.5.2 Credit Default Swaps Premiums

The fall in oil prices had a moderate adverse impact on markets in 2015, leading to only a modest increase in CDS spreads on UAE sovereigns. Spreads have widened from their year lows. In the more oil dependent Abu Dhabi, they increased by 29 bps from 2014 (see table 2.4.2). Meanwhile Dubai CDS spreads have only increased by 7 bps. UAE stock markets declined; reflecting higher cost of raising funds in international markets. On the other hand, the CDS of the GREs increased moderately. The spreads of Dubai Holding rose by around 90 bps in 2015, while the spreads of DP World have decreased by 28 bps.

Table 2.4.2 UAE – Average Credit Default Swaps (CDS)

	2011	2012	2013	2014	2015
Sovereigns					
Abu Dhabi	127.5	84.0	55.0	63.5	92.6
Dubai	445.0	225.0	220.0	226.6	233.7
GREs					
DP World	305.0	193.4	167.5	212.0	183.9
Dubai Holding	1109.4	511.2	325.8	330.7	421.0

Source: Bloomberg.
Note: All data are the observed end-of-quarter values. Premiums are expressed in basis points.

2.6 The Balance of Payments

The surplus of the current account decreased significantly by 63.2% in 2015 due to the fall of oil prices, reaching AED 79.3 billion from AED 215.7 billion in 2014, or 5.8% of GDP, down from 14.6%. The oil price slump during 2015 led to a decrease in hydrocarbon exports by 42.9% (AED 175.7 billion), due mostly to a decrease in crude oil exports which represent 76.9% of hydrocarbon exports. This decrease was partially compensated by a rise in non-hydrocarbon exports by 9% or AED 37.2 billion. Moreover, re-export activities recorded a small increase by AED 12.8 billion. As a result, total exports (FOB), excluding re-exports, decreased by AED 138.5 billion in 2015 and by AED 125.7 billion when re-exports are included.

Meanwhile, total imports (CIF), i.e., including insurance and freight, increased by AED 17.9 billion, in 2015, which led to a reduction in the surplus of the trade balance (CIF) from AED 313.8 billion in 2014 to AED 170.2 billion in 2015 (45.8%). The surplus of the Goods Trade Balance remains however substantial, reaching 12.9% of GDP.

As regards to services, the lower fuel prices boosted the increase in both the credit and debit in travel and transport items. Net travel recorded an inflow of AED 3.3 billion instead of an outflow of AED 1.7 billion in 2014. Inbound tourism in the UAE strengthened during 2015 recording 14.8% increase. The number of overnight international visitors also increased, with 35% originating from GCC and MENA region, 21% from Western Europe and 7% from the U.S. The UAE is also among the top 5 counties with the higher spending per trip worldwide. Net transport increased and reached AED 8.3 billion. Additionally, net government services recorded small increase during 2015. Since the credit of the balance of services increased by more than the decrease in debit, the deficit of the services balance decreased in 2015, reaching AED 145.5 billion.

Net investment income increased and recorded AED 6.4 billion in 2015. The foreign hydrocarbon companies in the enterprises of the public sector recorded the largest reduction in outflows in comparison with the previous year due to the fall of oil prices. Moreover, there are two different trends for transfers where the public transfers, mainly grants and charity abroad, decreased while the outflows conducted by expatriate workers increased, capitalizing on dirham appreciation, thereby widening the net outflow in 2015 by AED 6.6 billion.

The deficit of the financial account decreased by AED 165.1 billion during 2015, reaching AED 37.9 billion or 2.8% of GDP. This was due to recording inflow of AED 71.8 billion in private capital instead of outflow by AED 83.2 billion in 2014. The change in 2015 was mostly driven by a larger size in non-securities inflows, which increased by AED 71 billion, reflecting a surge in non-resident time deposits in non-banking financial institutions (by 92.7%) and a surge in banks' borrowing under repurchase agreements (by 173.8%). The first channel reflects confidence in the stability of the UAE's financial system. The second channel reflects banks' efforts to diversify sources of financing under tighter liquidity conditions. Meanwhile, there was a marginal increase in inward foreign direct investment (FDI) by AED 1.1 billion, reaching AED 38.2 billion, which was mitigated by an increase in the outflow of foreign direct investment abroad in the amount of AED 0.9 billion. Financial outward flows by public sector entities decreased in 2015, reaching AED 109.7 billion in 2015.

On account of less financial outflows and an increase in financial inflows, and notwithstanding the reduction in the current account surplus, the surplus of the overall balance of payments reached AED 55.3 billion in 2015 or 4.1% of GDP, an increase of 66.1% from 2014. As a result net foreign assets of the Central Bank increased during the same period by the equivalent of US dollar 15 billion, notwithstanding the continued decline in energy prices, thanks to the more diversified structure of exports in the UAE and the resilience of its financial sector to attract inflows and mobilize funds from outside the UAE. The foreign assets of the Central Bank reached AED 345.2 billion, as at the end of 2015, against foreign liabilities in the amount of AED 8.9 billion.

Table 2.5 U.A.E Balance of Payments Estimates

In billions of Dirhams

	2013	% change	% GDP	2014	% change	% GDP	2015*	% change	% GDP
Current Account Balance	**272.2**	**0.2**	**19.1**	**215.7**	**-20.8**	**14.6**	**79.3**	**-63.2**	**5.8**
Trade Balance (FOB)	**518.0**	**1.8**	**36.3**	**469.2**	**-9.4**	**31.8**	**328.3**	**-30.0**	**24.1**
Trade Balance (CIF)	**368.9**	**0.4**	**25.9**	**313.8**	**-14.9**	**21.3**	**170.2**	**-45.8**	**12.5**
Total Exports of Hydrocarbon	**475.2**	**2.4**	**33.3**	**409.7**	**-13.8**	**27.8**	**234.0**	**-42.9**	**17.2**
Crude Oil Exports	392.4	3.6	27.5	331.0	-15.6	22.4	179.9	-45.6	13.2
Petroleum Products Exports	35.0	-0.8	2.5	32.2	-8.0	2.2	22.0	-31.7	1.6
Gas Exports	47.8	-4.6	3.3	46.5	-2.7	3.1	32.1	-31.0	2.4
Total Exports of Non-Hydrocarbon	**382.4**	**4.2**	**26.8**	**412.8**	**7.9**	**28.0**	**450.0**	**9.0**	**33.1**
Free Zone Exports	234.2	18.6	16.4	280.6	19.8	19.0	320.0	14.0	23.5
Other Exports [1]	148.2	-12.7	10.4	132.2	-10.8	9.0	130.0	-1.7	9.6
Re Exports [2]	505.0	5.6	35.4	527.5	4.4	35.7	540.3	2.4	39.7
Total Exports & Re Exports (FOB)	**1362.6**	**4.1**	**95.5**	**1350.0**	**-0.9**	**91.5**	**1224.3**	**-9.3**	**90.0**
Total Imports (FOB)	**(844.6)**	**(5.5)**	**(59.2)**	**(880.8)**	**(4.3)**	**(59.7)**	**(896.0)**	**(1.7)**	**(65.9)**
Total Imports (CIF)	**(993.7)**	**(5.5)**	**(69.6)**	**(1036.2)**	**(4.3)**	**(70.2)**	**(1054.1)**	**(1.7)**	**(77.5)**
Other Imports [3]	(685.1)	(2.6)	(48.0)	(696.4)	(1.6)	(47.2)	(703.5)	(1.0)	(51.7)
Free Zone Imports	(286.1)	(13.4)	(20.0)	(318.0)	(11.1)	(21.5)	(335.5)	(5.5)	(24.7)
Imports (gas)	(22.5)	(1.4)	(1.6)	(21.8)	(-3.1)	(1.5)	(15.1)	(-30.7)	(1.1)
Services (NET)	**(150.4)**	**(1.5)**	**(10.5)**	**(150.7)**	**(0.2)**	**(10.2)**	**(145.5)**	**(3.5)**	**(10.7)**
Credits	**78.0**	**12.2**	**5.5**	**87.5**	**12.2**	**5.9**	**100.0**	**14.3**	**7.4**
Travel	45.5	13.5	3.2	51.3	12.7	3.5	58.9	14.8	4.3
Transport	29.5	11.3	2.1	33.1	12.2	2.2	37.9	14.5	2.8
Government Services	3.0	3.4	0.2	3.1	3.3	0.2	3.2	3.2	0.2
Debits	**(228.4)**	**(4.9)**	**(16.0)**	**(238.2)**	**(4.3)**	**(16.1)**	**(245.5)**	**(3.1)**	**(18.0)**
Travel	(50.6)	(4.5)	(3.5)	(53.0)	(4.7)	(3.6)	(55.6)	(4.9)	(4.1)
Transport	(28.3)	(1.8)	(2.0)	(28.9)	(2.1)	(2.0)	(29.6)	(2.4)	(2.2)
Government Services	(3.8)	(8.6)	(0.3)	(4.1)	(7.9)	(0.3)	(4.4)	(7.3)	(0.3)
Freight & Insurance	(145.7)	(5.6)	(10.2)	(152.2)	(4.4)	(10.3)	(155.9)	(2.4)	(11.5)
Investment Income (NET)	**1.7**	**54.5**	**0.1**	**2.4**	**41.2**	**0.2**	**6.4**	**166.7**	**0.5**
Banking System [4]	(5.5)	(5.8)	(0.4)	(5.8)	(5.5)	(0.4)	(6.0)	(3.4)	(0.4)
Private non-banks	(5.7)	(1.8)	(0.4)	(5.6)	(-1.8)	(0.4)	(5.0)	(-10.7)	(0.4)
Enterprises of Public Sector	29.8	10.4	2.1	30.1	1.0	2.0	30.0	0.3	2.2
Official Debt Services (Interest)	(4.8)	(17.1)	(0.3)	(5.0)	(4.2)	(0.3)	(5.1)	(2.0)	(0.4)
Foreign Hydrocarbon Companies in UAE	(12.1)	(10.0)	(0.8)	(11.3)	(-6.6)	(0.8)	(7.5)	(-33.6)	(0.6)
Transfers (NET)	**(97.0)**	**(8.0)**	**(6.8)**	**(105.2)**	**(8.4)**	**(7.1)**	**(110.0)**	**(4.5)**	**(8.1)**
Public	(21.7)	(17.6)	(1.5)	(24.1)	(10.9)	(1.6)	(22.3)	(-7.8)	(1.6)
Private	(75.3)	(5.5)	(5.3)	(81.1)	(7.7)	(5.5)	(87.7)	(8.1)	(6.4)

(Table 2.5 continued)

	2013	% change	% GDP	2014	% change	% GDP	2015*	% change	% GDP
Financial and Capital Account	**(181.7)**	**(7.7)**	**(12.7)**	**(203.0)**	**(11.7)**	**(13.8)**	**(37.9)**	**(-81.3)**	**(2.8)**
Financial Account	**(181.7)**	**(7.7)**	**(12.7)**	**(203.0)**	**(11.7)**	**(13.8)**	**(37.9)**	**(-81.3)**	**(2.8)**
a. Private capital	**(62.8)**	**(16.9)**	**(4.4)**	**(83.2)**	**(32.5)**	**(5.6)**	**71.8**	**(-186.3)**	**5.3**
a-1 Direct Investment	**6.1**	**15.1**	**0.4**	**4.0**	**-34.4**	**0.3**	**4.2**	**5.0**	**0.3**
a-1-1 Outward	(32.4)	(8.0)	(2.3)	(33.1)	(2.2)	(2.2)	(34.0)	(2.7)	(2.5)
a-1-2 Inward	38.5	9.1	2.7	37.1	-3.6	2.5	38.2	3.0	2.8
a-2 Portfolio Investment	**4.1**	**13.9**	**0.3**	**4.6**	**12.2**	**0.3**	**4.0**	**-13.0**	**0.3**
a-3 Banks	**(45.5)**	**(41.7)**	**(3.2)**	**(63.8)**	**(40.2)**	**(4.3)**	**91.6**	**(-243.6)**	**6.7**
a-3-1 Securities	(22.1)	(333.3)	(1.5)	(39.6)	(79.2)	(2.7)	(12.4)	(-68.7)	(0.9)
a-3-2 Other investment (loans, deposits)	14.5	153.7	1.0	33.0	127.6	2.2	104.0	215.2	7.6
a-4 Private nonbanks	**(27.5)**	**9.8**	**(1.9)**	**(28.0)**	**(1.8)**	**(1.9)**	**(28.0)**	**(0.0)**	**(2.1)**
b. Enterprises of Public Sector	**(118.9)**	**(3.4)**	**(8.3)**	**(119.8)**	**(0.8)**	**(8.1)**	**(109.7)**	**(-8.4)**	**(8.1)**
Errors and omissions	(12.8)	80.7	(0.9)	20.6	260.7	1.4	13.9	(32.3)	1.0
Overall balance	**77.8**	**111.9**	**5.4**	**33.3**	**-57.2**	**2.3**	**55.3**	**66.1**	**4.1**
Change in Reserve **	**-77.8**	**-111.9**	**-5.4**	**-33.3**	**57.2**	**-2.3**	**-55.3**	**-66.1**	**-4.1**
UAE Central Bank									
Foreign Assets	**250.6**	**44.9**	**17.6**	**288.6**	**15.2**	**19.5**	**345.2**	**19.6**	**25.4**
Foreign Liabilities	**3.4**	**(0.7)**	**0.2**	**8.1**	**140.7**	**0.6**	**8.9**	**9.0**	**0.7**
Net Foreign Assets	**247.2**	**45.8**	**17.3**	**280.4**	**13.5**	**19.0**	**336.3**	**19.9**	**24.7**
Reserve Position with IMF	1.5	10.1	0.1	1.6	1.6	0.1	1.3	-17.0	0.1
SDR	3.1	-0.6	0.2	3.1	0.6	0.2	2.8	-10.1	0.2
Reserve Position with IMF + SDR	**4.6**	**2.7**	**0.3**	**4.6**	**0.9**	**0.3**	**4.1**	**-12.4**	**0.3**

(1)Including Estimates of other Exports from all Emirates
(2) Including Re-exports of Non-Monetary Gold
(3) Including Estimates of Imports from all Emirates and Imports of Non-Monetary Gold
(4) Central Bank and all Banks
* Preliminary Estimates Subject to Revision
** Negative indicates an increase, positive indicates a decrease

Chapter 3. Monetary & Banking Developments

Government deposits decreased in 2015 as low oil prices persisted, which slowed down the growth of the money supply. Banks, however, capitalizing on improved quality of loan portfolio were able to increase credit albeit at a moderate pace, except for lending to the government which grew more than in previous years. Banks therefore provided the non-energy sectors of the economy with the needed financing. Overall, the banking sector in the UAE remains well capitalized and highly liquid.

3.1. Monetary Aggregates

In 2015, all Money Supply Aggregates witnessed an increase on a yearly basis.

The growth in M1[4] in 2015 could be explained by the increase in monetary deposits by AED 21.5bn (5.7%) to AED 457bn and marginal decrease in currency issued and cash in banks. However, compared to 2013 and 2014 the growth of M1 is much lower, as the pace of growth of monetary deposits was much lower than in the previous two years (29.8% in 2013 and 14.6% in 2014) and currency in circulation increased by 10.5% and 17.5% in 2013 and 2014, respectively.

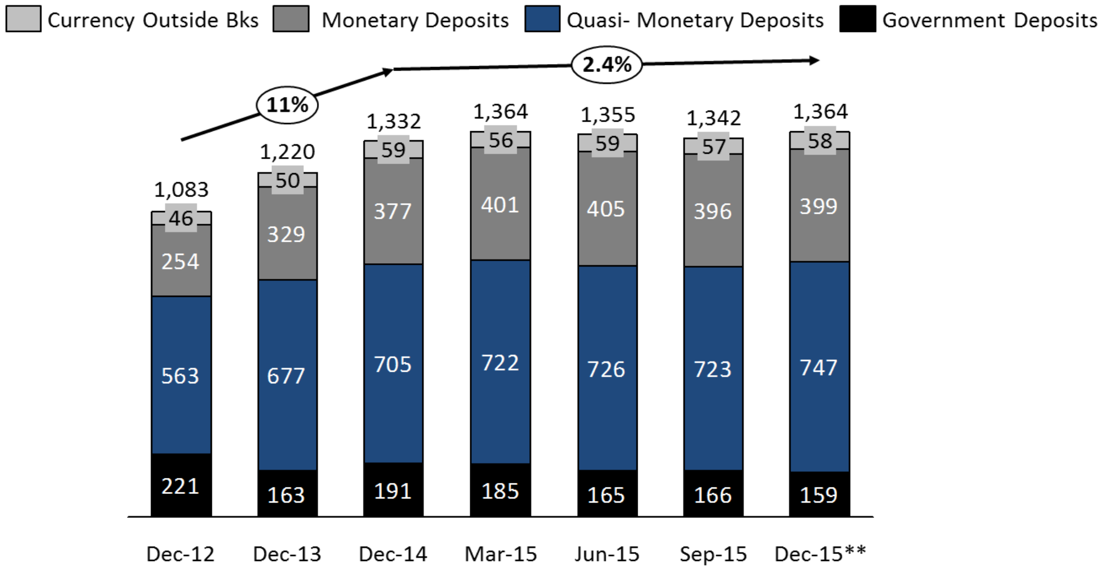
The growth in M2[5] is due to the increase in M1 and the quasi-monetary deposits. The aggregate grew by AED 63.3bn (5.5%) in 2015 to AED 1,204.4bn and the quasi-monetary deposits increased by AED 42.4bn (6%). This growth is much lower than the 2013 figure of 20.2%, but higher than the 4.1% in 2014. This increase could be explained by the fact, that many depositors, especially corporate, are reducing their investment activity on account of less favorable economic environment.

The largest of the monetary aggregates – M3[6], experienced a lower growth - AED 31.6bn (2.4%) because of a contraction of the government deposits[7] during the year, reaching AED 1,363.6bn, having declined by AED 31.7bn (-16.6%) in 2015. In contrast, in 2014 the government deposits grew by 17%. In addition, for the period 2012-2014, the compound annual growth rate (CAGR[8]) of government deposits was 11%.

[4] Currency in Circulation Outside Banks (Currency Issued - Cash at banks) + Monetary Deposits (all short term deposits on which bank customer can withdraw without prior notice)
[5] M1 + Quasi-Monetary Deposits (Resident Time and Savings Deposits in Dirham + Commercial Prepayments in Dirhams + Resident Deposits in Foreign Currencies)
[6] M2 + Government Deposits
[7] This refers to UAE government deposits with commercial banks and the Central Bank of the UAE
[8] The CAGR is the mean annual growth rate (geometric mean) over a specified period of time longer than one year. It is a more precise measure for average growth than the arithmetic mean.

Slower monetary growth indicates moderating economic activity, on account of lower government expenditures, impacting directly and indirectly the private sector.

Figure 3. 1. UAE Monetary aggregates in AED bn



Source: Central Bank of the UAE
Note: All data indicate the end-of-quarter values; data for December 2015 are provisional. Figures in the circles represent the CAGR/annual growth.

3.2. Banking Activity

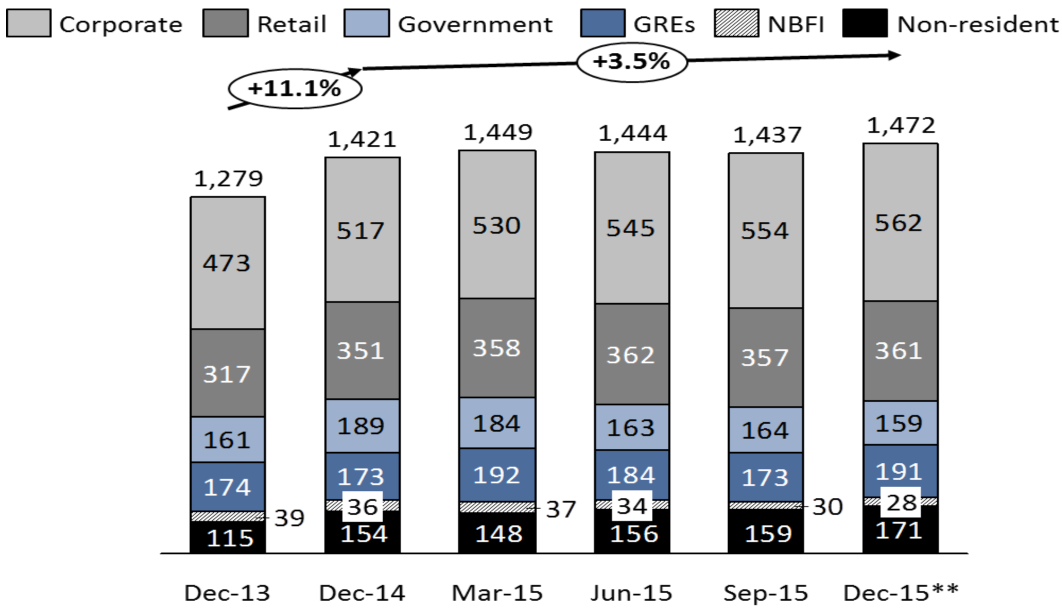
There are 23 locally-incorporated banks in the UAE. Their branches decreased from 869 at the end of 2014 to 856 at the end of 2015, due to the higher cost efficiency requirements from the shareholders, while the 26 foreign banks remained with 86 branches.

Customer Deposits at banks increased in 2015 by AED 50.3bn or 3.5% only, compared to 2014, where the growth was by AED 142.4bn or 11.1%. The slowdown in 2015 was due to the decrease in Government deposits, and despite stable growth in the other asset classes. In 2015, Non-resident Deposits increased by 11.4%, compared to an increase of 33.9% in 2014. The continued growth in 2015 attests to the UAE's ability to maintain its safe haven status in the region.

As regards to UAE Government Deposits in the banking sector, there was a sharp decrease in the middle of the year by 13.7% or AED 25.9bn compared to the end of 2014. The level remained relatively flat for the rest of 2015, reaching AED 158.8bn at end of December.

Government deposits[9] decreased for the whole 2015 by 15.9% or AED 30bn. In 2014, in contrast, the growth of UAE Government Deposits in the banking sector was 14.6% or AED 27.5bn.

Figure 3. 2.a. Deposits in AED bn



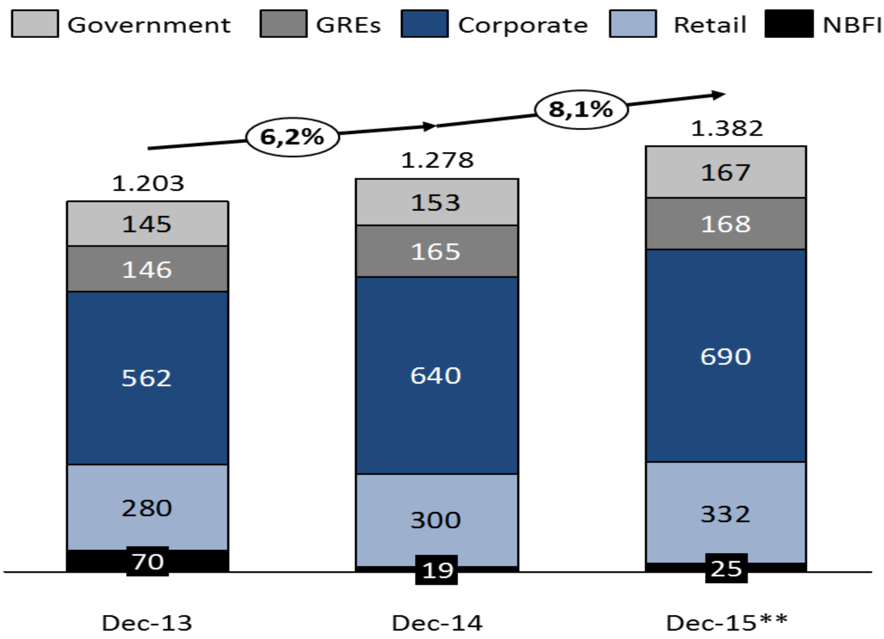
Source: Central Bank of the UAE

Note: All data indicate the end-of-quarter values; data for December 2015 are provisional. Figures in the circles represent the annual growth rate.

Domestic Credit increased in 2015 by 7.5% or AED 104bn, benefiting mainly the Corporate sector by AED 50bn, whereas credit to the Government increased by AED 13.8bn, with the government-related entities (GREs) growing only by AED 2.8bn. Compared with the previous year, however, Domestic Credit growth increased from 6.2% in 2014 to 8.1% in 2015. According to respondents of the Central Bank "Credit Sentiment Survey" in the last quarter of 2015 there may be "a downward trend in credit appetite" going forward across all sectors of economic activity, with the exception of retail and wholesale trade, as well as further tightening in credit standards by banks.

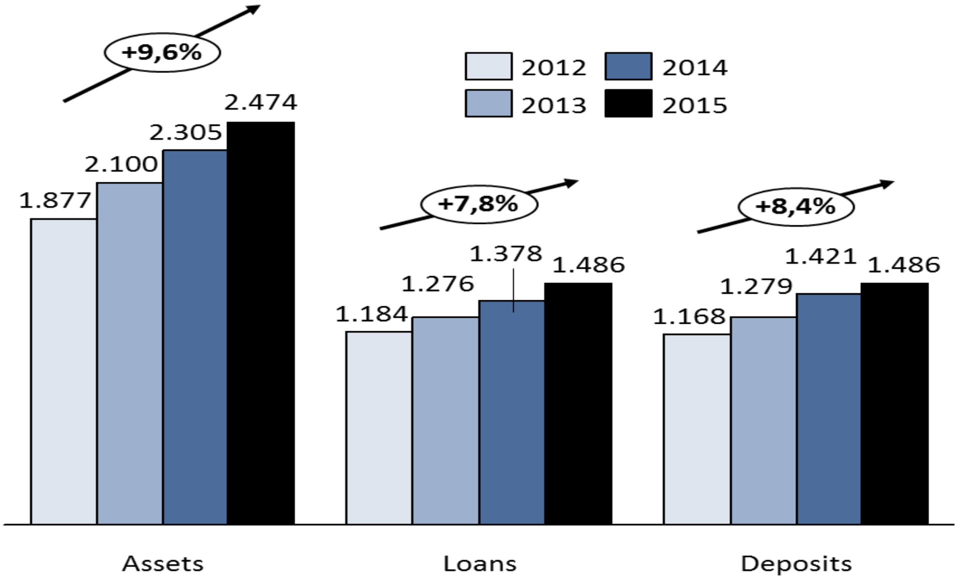
[9] This refers to UAE government deposits with commercial banks only

Figure 3.2.b. Loans per asset classes in AED bn



Source: Central Bank of the UAE
Note: All data indicate the end-of-quarter values; data for December 2015 are provisional. Figures in the circles represent the annual growth rate.

Figure 3. 2.c.UAE Banks' Indicators: Assets and Liabilities in AED bn



Source: Central Bank of the UAE
Note: All data indicate the end-of-quarter values; data for December 2015 are provisional. Values are expressed in billions of Dirhams. Figures in the circles represent the CAGR 2012-2015.

Islamic banks continued to thrive with their assets increasing by 14.6% in 2015, reaching AED 464bn, with their share in total assets increasing from 17.6% at the end of 2014 to 19% at the of 2015. Meanwhile, their financing increased by 15.4%, reaching AED 307 billion, or 22.2% of Domestic Credit, i.e., higher than the average growth rate for banking-wide domestic credit of 8.1%.

Table 3.1.a. Assets and financing of Islamic Banks (2014 – 2015)

	2014	2015			
	Q4	**Q1**	**Q2**	**Q3**	**Q4**
Assets	405	432	445	452	464
Percent of total banking assets	17.6	18.2	18.4	18.7	19.0
Islamic financing	266	280	290	300	307
Percent of Domestic Credit	20.8	21.5	21.7	22.0	22.2

Source: Banking Supervision Department, Central Bank of the UAE

Note: All data indicate the end-of-quarter values. Assets' values are expressed in billions of Dirhams.

3.3. Banking Soundness Indicators

The overall outlook regarding the soundness of the banking sector remains positive during 2015, due to an improved quality of the loan portfolio, while liquidity conditions tightened.

The improved quality of the loan portfolio of banks is evident by the fact that the ratio of non-performing loans (NPLs) remained at 6.3% during the last three quarters of 2015, well below the 7% at the end of 2014. Meanwhile, banks' specific provisions for NPLs remained almost flat in 2015 reaching AED 72.8 billion at the end of December, an increase of 1.7% Y-o-Y, which ensures that NPLs remain fully provisioned.

Banks operating in the UAE remain highly capitalised, with the capital adequacy ratio (CAR) of banks reaching 18.3% (16.6% for Tier1 capital) at the end of 2015, which is well above the regulatory requirements set by the Central Bank (12% and 8%, respectively) with an improvement compared to December 2014, when CAR was at 18.2% (and Tier 1 capital at 16.2%).

Meanwhile, liquid assets which include reserve requirements, certificates of deposit held by banks at the Central Bank, in addition to zero-risk weighted government bonds and public sector debt and cash at banks, as a ratio of total assets increased from 15.7% at the end of 2014 to 17.4% at the end of December 2015. However, during the first three quarters of 2015 the ratio was below 15%. The increase that was observed at the end of the year is attributed to the increase mainly in free and other account balances (excess unremunerated reserves) at the Central Bank, which reached AED 39.3bn at the end of 2015, and banks' investments in Central Bank CDs which increased by 40.5% from AED 99.5bn to AED 139.8bn in December. The increase in both categories is due to some banks opting to increase those two components of assets with the Central Bank, as previously their shares of liquid assets to total assets were lower than the threshold established by the Central Bank at 10%.

To capture the composite effects of changes in loans and deposits, two key ratios related to the funding of the banks are considered: the Loan-to-Deposit[10] (L/D) ratio and the Lending to the Stable Resources Ratio[11] (LSRR).

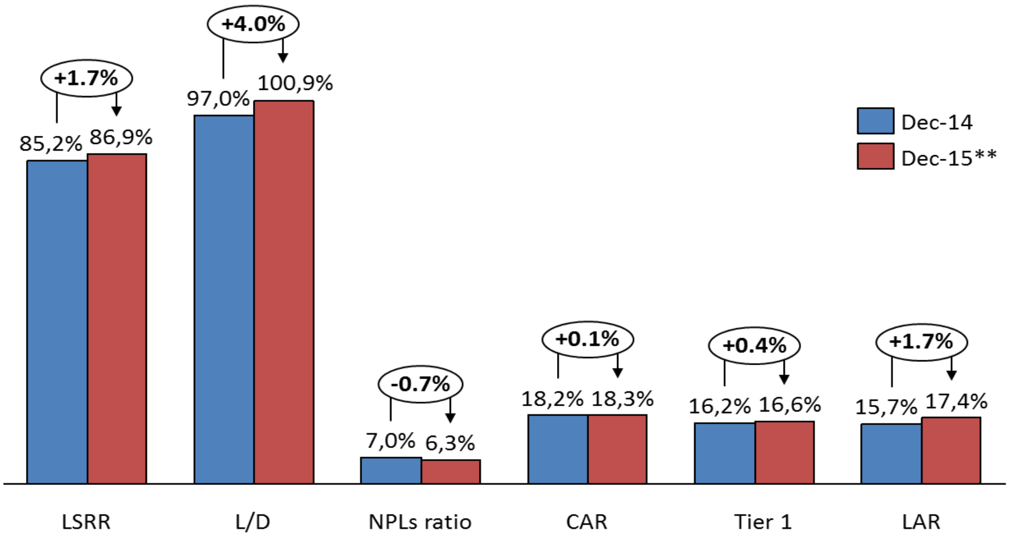
L/D has moved from 97% at end of 2014 to 100.9% in December 2015, surpassing the 100% barrier in June, reaching a peak of 103.2% in October. The percentage increased mainly due to the significant decrease in government deposits and higher than 2014 credit growth. Consistently, LSRR increased by 1.7 percentage points to the level of 86.9% at the end of 2015, compared to 85.2% in 2014. This confirms that the growth of deposits and stable resources was lower than the growth of credit during 2015.

Overall, the banking sector in the UAE, based on indicators in 2015, remains well capitalised with the average CAR largely exceeding the CBUAE minimum requirement of 12%. Even though there were some signs of liquidity squeeze in 2015, the system remains highly liquid, as judged by the ratio of liquid assets to total assets and the share of credit to stable resources as well as banks' assets at the central bank that could be tapped for additional liquidity. Further, indicators of financial soundness continue to bode well for the ability of the banks to support growth of credit while adhering to the guidelines of financial stability, with a very low level of NPLs. Hence, the overall outlook of the banking system remains positive in 2016.

[10] The Ratio of Total Loans to the Total Deposits

[11] The Ratio of the Total Advances (Net Lending + Net Financial Guarantees & Stand -by LC + Interbank Placements more than 3 months) to the sum of (Net Free Capital Funds + Total Other Stable Resources)

Figure 3. 3. Banking soundness indicators



Source: Central Bank of the UAE.

Note: All data indicate the end-of-quarter values; data for December 2015 are provisional. Figures in the circles represent the change in absolute values.
LSRR: Lending to Stable Resources
L/D: Loans to Deposits Ratio
NPL: Non-performing loans
CAR: Capital Adequacy Ratio
Tier 1: Capital Adequacy for Tier 1 Assets
LAR: Liquid Assets Ratio

Chapter 4. Central Bank Financial Results & Reserve Management

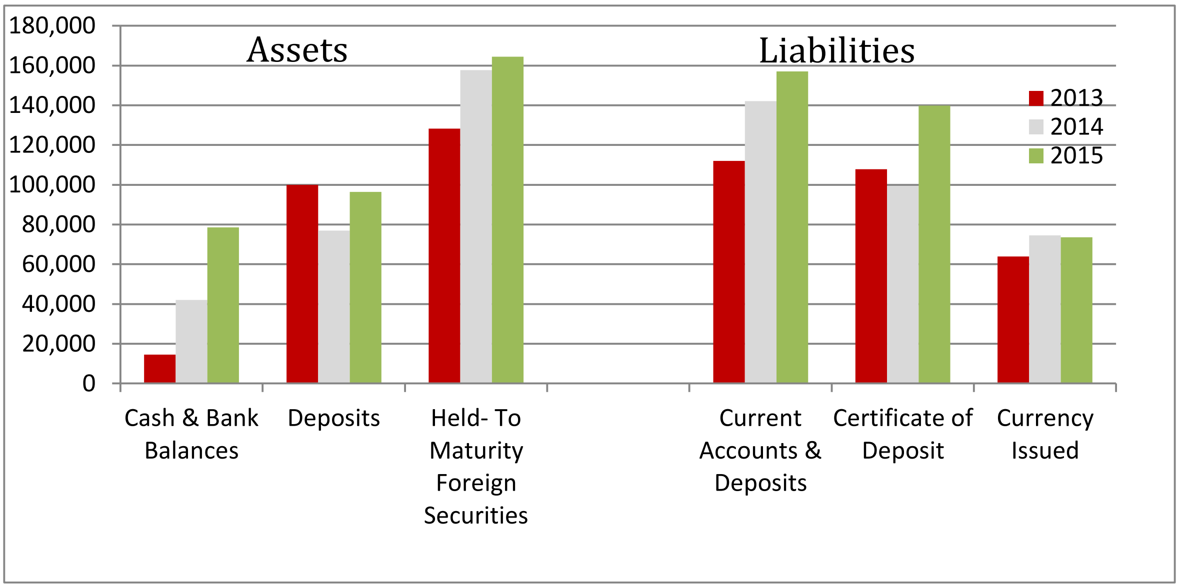
Central Bank assets increased in 2015, triggered by an increase on the liabilities side of the balance sheet, testament to sufficient, albeit tightening liquidity in the banking sector

4.1 Central Bank Balance Sheet

The liabilities side is comprised of reserves of banks at the Central Bank and currency issued. Total liabilities of the balance sheet of the Central Bank continued to increase during the year 2015 despite the negative impact of oil prices on bank liquidity. The Central Bank's total liabilities reached AED 393.7 billion at the end of December 2015, i.e., an increase by 14% compared to December 2014.

The Current Accounts and Deposits of banks at the Central Bank increased in 2015 by 10.5%, reaching AED 157 billion, while banks' holdings of "Certificates of Deposit" issued by the Central Bank increased by 40.4%, reaching AED 139.8 billion. This exceptional increase was due to the fact that some banks decided to increase their holdings of CDs at the end of the year to meet the statutory Liquidity Ratio of 10% required by the Central Bank. Meanwhile, Currency Issued decreased slightly, during the period under review, reaching AED 73.5 billion.

Figure 4.1. Assets and Liabilities of the Central Bank



The total assets of the Central Bank increased in line with the above- indicated increase in liabilities, with the latter constituting the main driver of the said increase. Held-to-Maturity Foreign Securities increased from AED 157.8 billion at the end of December 2014 to AED 164.5 billion at the end of December 2015, as a result of new investments that were made to replace the securities that came to maturity during the year. Cash and Bank Balances increased from AED 42 billion to AED 78.6 billion as a result of the Central Bank's investments in "Bank Balances" which are mostly Nostro Accounts that provide interest. The Central Bank's deposits at banks abroad increased also by AED 19.4 billion in 2015.

Table 4.1. Central Bank Balance Sheet

In Millions of Dirhams

	2013	2014	2015
Assets			
Gold Bullion	-	-	934
Cash & Bank Balances	14,592	42,001	78,611
Deposits	99,927	76,917	96,362
Liquidity Support Facility	513	321	228
Held-To-Maturity Foreign Securities	128,263	157,753	164,495
Held-To-Maturity Bonds Issued by MOF & Dubai Government	55,361	49,443	49,231
Available-for-sale foreign Investments	385	378	361
Advances to Government	-	2,500	2,500
Available-for-sale foreign securities	-	-	74
Derivative Assets	-	7,530	334
Other Assets	6,624	7,996	445
Property and Equipment's	97	79	79
Total Assets	**305,762**	**344,918**	**393,660**
Off Balance Sheet Commitments	**129,367**	**134,105**	**199,681**
Liabilities			
Current Accounts & Deposits	111,973	142,168	157,031
Certificates of Deposit	107,896	99,534	139,773
Currency Issued	63,927	74,472	73,522
Derivative Liabilities	-	-	1,310
Other Liabilities	697	1,683	2,275
Total Liabilities	**284,493**	**317,857**	**373,910**
Authorized Issued & Fully Paid Capital	2,500	2,500	2,500
Fair Value Reserve	-5	-11	-29
Gold Revaluation Reserve	-	-	-60
General Reserve	16,080	16,080	17,339
Retained Earnings	2,694	962	-
Total Liabilities & Capital	**305,762**	**337,388**	**393,660**
Off Balance Sheet Commitments related to foreign exchange fluctuations	**129,367**	**134,105**	**199,681**

Source: Financial Control Division, Central Bank of the UAE.
Note: End-of-year data.

4.2 Foreign Assets

The Central Bank's Foreign Assets, i.e., excluding USD 10 billion Dubai Government bonds, increased by 20.1%, from AED 283.9 billion at the end of December 2014 to AED 341.1 billion at end of December 2015, with the increase in liabilities being the main driver. The investment abroad was mainly in "Held-to-Maturity Securities" (48.1% of total) and "Current Account Balances and Deposits at Banks Abroad" (50.4% of total), which are Nostro Accounts that provide interest.

Table 4.2. Central Bank's Foreign Assets

In billions of Dirhams

	2013	2014	2015
Total Foreign Currency Assets	**246.0**	**283.9**	**341.1**
Current Account Balances and Deposits at Banks Abroad	108.1	115.5	171.8
Held-To-Maturity Securities	128.3	157.8	164.1
Other Foreign Assets	9.6	10.7	4.8

Source: Financial Control Division, Central Bank of the UAE, end of year data

4.3 Interest Rates

The fixed peg of the exchange rate of the Dirham to the US dollar means that the CBUAE has to peg its policy rate to the direction of the interest policy in the U.S. as well. Therefore, following the Federal Open Market Committee decision on 16 December 2015 to increase its target Federal Funds rate by 25 basis points, the Central Bank of the UAE announced its decision on December 17 to raise interest rates applied to the Certificates of Deposits it issues to banks, in line with the increase on the US dollar. Consistent with our commitment to the fixed peg arrangement, and following the FOMC decision in the U.S., the Central Bank increased the targeted cut-off rate on Certificates of Deposit on 17 December 2017 by 25 basis points, thereby reaching a higher bound of 50 basis points.

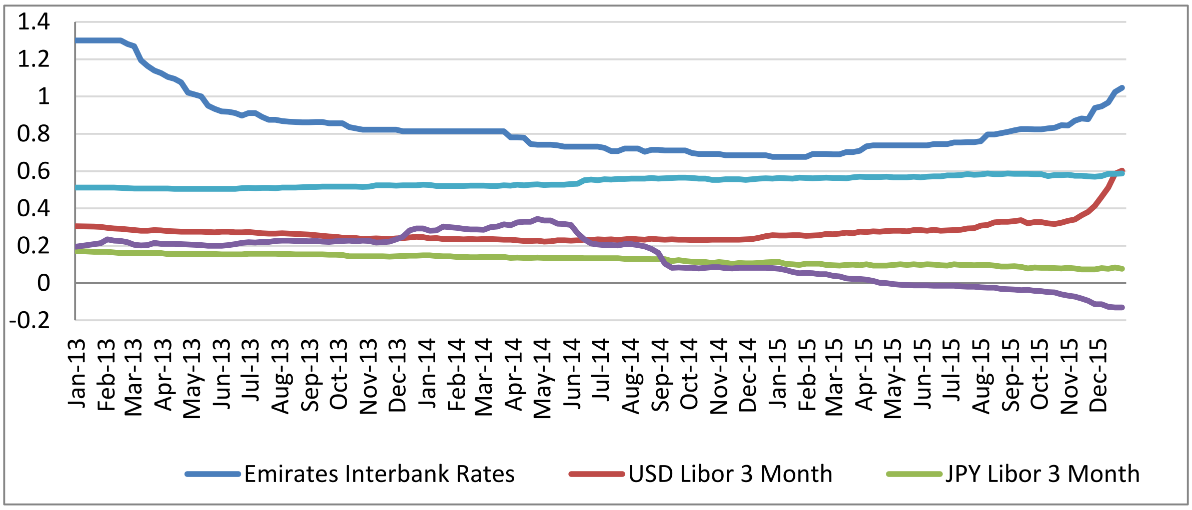
It is also worth-noting in this regard that the CBUAE uses monetary tools at its disposal to manage liquidity in the banking system, with a goal to strike a balance between supporting credit growth and stemming the risks to financial stability, while maintaining its continued commitment to the fixed peg regime.

4.4.1 Short-term interest rates

In line with the expected interest rate increase in the US, the 3-month Emirates Interbank Offer Rate (Eibor), which is calculated by the Central Bank of the UAE, comprising daily quotes of the largest banks operating in the country, increased steadily until July 2015, then it decreased after the Fed failed to increase its policy rate in September. Eibor increased by 12 basis points in December, reaching 1%, with the spread over the 3-month USD Libor rate reduced to 46 basis points.

The 3-month USD Libor increased in line with the expectation of the Fed's decision to increase the targeted Federal Funds rate, with most of the increase taking place in December. The Euro 3-month Libor rate continued its retreat in the fourth quarter, reflecting the tepid economic conditions in the Eurozone and the continued commitment of the European Central Bank (ECB) to quantitative easing to help support sluggish growth in the Euro area.

Figure 4.2. 3-month Libor Rates (%)



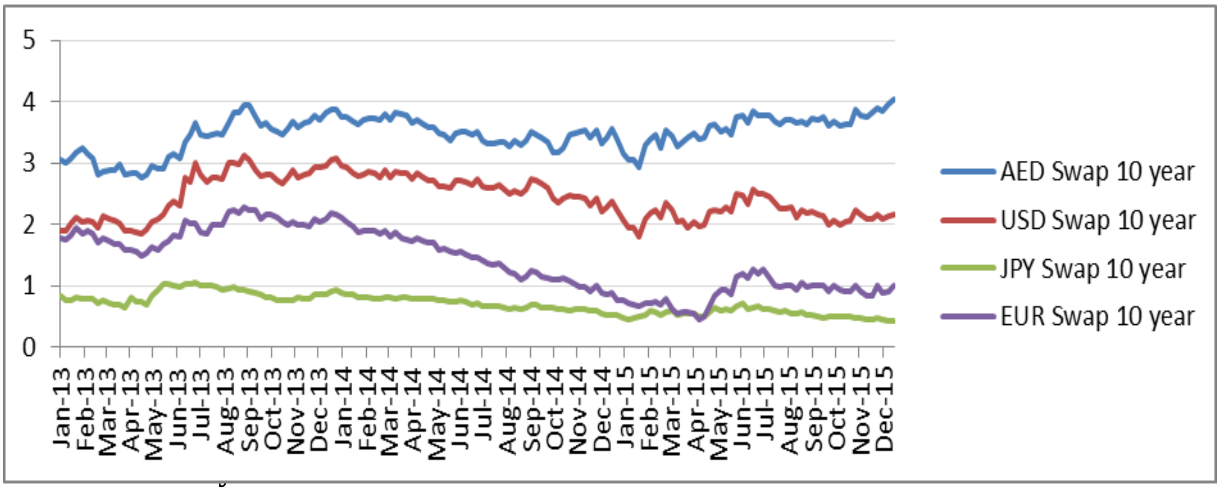
Source: Bloomberg

4.4.2 Long-term swap rates

In the absence of a deep and liquid government bond market in the UAE, the swap market is the only way to get an idea about yields at longer maturities. Interest rate swaps often exchange a fixed payment for a floating payment that is linked to an interest rate, most often the LIBOR. The AED 10-year swap rate increased steadily during the first nine months of 2015, rebounding in December with an increase by 17 bps in consistency with the increase in the policy rate in the U.S. However, the USD 10-year swap rate fluctuated during the year, decreasing by 70 bps from end of July to end of October when the widely expected rise in the Federal Funds rate did not materialize, and then increasing by 10bps in November and 2bps in December, following the historic FOMC's decision taken during that month.

The spread between the AED 10-year swap and the USD 10-year swap increased also steadily during 2015, reaching 1.52 percentage points at the end of September. The spread further increased to 1.61pps at the end of October, to 1.65pps at the end of November, and to 1.80pps at the end of December, reflecting an ever higher risk premium, as investors became averse to the potential adverse impact of low oil prices, particularly falling government revenues and the impending fiscal consolidation.

Figure 4.3. 10-year swap rates



The primary tool for the Central Bank of the UAE is the dollar/dirham spot window which offers banks two-way liquidity, i.e., to exchange dollars against dirhams and vice-versa. This provides confidence to the market in the Central Bank's commitment to defend the exchange rate and enables banks a bigger scope to better manage their liquidity in both currencies.

Certificates of Deposits (CDs) were first issued by the Central Bank in 1988, in tenors varying from 1 month to 6 months. This program offers banks an alternative tool of investing their excess liquidity in dirhams instead of investing it in dollars abroad. The initial program was revamped in 1994 when it was made available for daily issuance, with tenors extended up to 18 months. Banks were also offered the possibility of redeeming their CDs, before maturity, allowing them to get immediate liquidity when needed at a rate set by the Central Bank. The system was revamped in 2007 with the move to a new auction system, where the CBUAE determines issuance by setting a cut-off interest rate for bids posted by banks, while Islamic CDs were introduced in 2010 to allow Islamic banks to better manage their excess liquidity, putting them on equal footing with conventional banks.

4.5 Banks' Excess Liquidity Developments

The main banks' liquidity indicator monitored at the Central Bank is their excess reserves, i.e., their current account at the Central Bank and their holdings of CDs. Banks' current account at the Central Bank decreased during the year before a rebound in December, reaching AED 36.4 billion, i.e., about 23% higher when compared to December 2014, while Certificates of Deposit held by banks increased by AED 40.4%, during the same period.

Total bank liquidity, including reserve requirements and highly-rated government and public sector debt, increased from AED 295 billion at the end of December 2014 to AED 351.2 at the end of December 2015, i.e., 19.1% increase. Notwithstanding the above-indicated exceptional investment in CDs in December, the banking system in general has sufficient liquidity. The few banks that tapped CBUAE's facilities to borrow Dirhams during 2015, namely through the Interim Marginal Lending facility, the Collateralized Murabaha Facility, and the CDs Repo Facility tapped a small amount.

4.6 Reserves Management

Foreign currency reserves are managed by the Reserves Management Division within the Monetary and Reserves Management Department.

CBUAE's reserves are managed with a goal to strike a balance between guaranteeing a reasonable return on investments, while ensuring adequate liquidity buffers. Following the global financial crisis and subsequent adverse effects on the UAE economy, the CBUAE has adopted a more vigilant strategy towards risk management. As a result, the benchmarks for the investment strategy of the Central Bank reserves aim to ensure adequate liquidity, capital preservation and appropriate return, with liquidity being the most important driver to ensure banking stability. Investments are based on the Reserves Management Policy approved by the Board of Directors and in consistency with Union Law 10 of 1980, concerning the Central Bank, The Monetary System and Organization of Banking.

CBUAE's foreign currency assets at the end of December 2015 comprise AED 171.8 billion Deposit Account and Cash with Banks Abroad and AED 164.5 billion Central Banks's Investments Abroad in Highly Rated Securities, Government Bonds and Treasury Bills, in addition to other foreign currency assets, amounting to AED 4.8 billion, which brings total foreign reserves to AED 341.1 billion, excluding USD 10 billion Dubai Government Bonds.

4.7 Risk Management

The management of risks in the Central Bank is coordinated by the Risks Identification and Monitoring Committee, chaired by His Excellency the Governor of the Central Bank and having as members Senior Managers from all relevant business areas. The Committee is assisted in its work by the Risk Management Unit, reporting directly to His Excellency the Governor and, in parallel, to the Risks Identification and Monitoring Committee. The Unit includes specialists in both Financial and Operational Risk.

The use of monetary tools and the management of its reserves expose the Central Bank to financial risks and in particular market, credit and liquidity risks. These risks are, however, limited as a result of the existing restrictions imposed by the Central Bank's policies and the use of appropriate hedging and risk control tools.

Thus, currency risks incurred by holding fixed-income instruments denominated in currencies other than the US dollar are systematically hedged out. Counterparties in all money market instruments are selected among highly creditworthy financial institutions and the exposures towards these counterparties are controlled against established limits. Money market exposures are distributed among a large number of counterparties according to their creditworthiness so that the Gini coefficient[12] of concentration of the exposures was equal to 0.4956 at the end of 2015. Finally, the overall liquidity of the reserves is guaranteed by investing a large part of the reserve management portfolio in very liquid instruments. Liquidity providing operations expose the Central bank to counterparty risk. This risk is, however, limited by the fact that, as a rule, such operations are adequately collateralized.

The Central Bank is also exposed to operational risk, defined by the Basel Committee for Banking Supervision as the risk of loss resulting from inadequate or failed internal processes, people and systems, or from external events. Operational risks identified by the Risk Management Unit, in close cooperation with Risk Coordinators in the relevant business areas, are evaluated by the Risks Identification and Monitoring Committee. Depending on the likelihood and potential impact of such risks, appropriate controls are introduced and the level of the residual risk, after the implementation of the controls, is monitored over time.

[12] *The Gini coefficient is a measure of concentration/dispersion of a variable among a number of entities that ranges from 0 (equal distribution among all entities) to 1 (concentration on one entity).*

Part two: Central Bank Activity

Chapter 5. Banking Supervision and Regulatory Developments

2015 saw consolidation in the supervision process in response to the regulatory changes made during the previous 5 years and saw an increased focus on compliance within the institutions it licenses as well as increasingly robust enforcement actions, when necessary

Banking Supervision's objective is to maintain the safety and soundness of banks and other financial institutions that the Central Bank licenses. It achieves this by introducing, implementing and enforcing regulations and monitoring risks and potential risks within those institutions.

Banking Supervision in its present form was empowered by Chapter 2 of Union Law No. (10) of 1980, which made mandatory the supervision of the financial sector under its jurisdiction and strengthened the Central Bank functions in this regard.

After licensing by the Central Bank, an institution is subject to ongoing supervision to ensure that it is managing its risks prudently and that it is meeting the Central Bank's prudential requirements, this applies to both banks and non-bank financial institutions.

Accordingly, the Banking Supervision Department expanded over the years and a branch opened in Dubai to conduct supervision in Dubai and in the Northern Emirates.

As the financial sector developed, the associated risks from domestic and international developments increased particularly over recent years. To achieve a higher level of efficiency and effectiveness in performing the supervision role, the Banking Supervision Department (BSD) expanded further to meet these new challenges. BSD presently consists of Licensing, On-site and Off-site Examination and Supervision, Regulatory Development, Payment System Oversight, and Consumer Protection and Customer Services.

As at the end of December 2015, the core supervisory functions of BSD are resourced by a team of 64 examiners and 10 reviewers based in both Abu Dhabi and Dubai. The year 2015 saw the introduction of specialist money exchange reviewers and a substantial upgrade in the specialist examination teams assigned to them. This push towards specialization has reinforced a change in a strategy which begun in 2014 with the appointment of a specialist reviewer for non-bank financial institutions. .

The examination schedule during 2015 completed 49 examinations at non-bank financial institutions, and 73 examinations at banks covering full scope as well as thematic reviews.

The teams completed 26 full scope reviews at exchange houses and a significant number of fast track examinations designed to quickly address specific critical issues.

The Supervisory Structure

The Examination and Supervision Division within BSD is broadly delineated along the lines of the requirement to physically verify and report on institutions under the Central Bank's jurisdiction. On-site examination undertakes field inspections, while off-site work focuses on analysis and review of the reports received from bank examiners and follow-up of relevant issues with the concerned institutions. In reality though, both teams are closely linked and there is always significant interaction between the two functions before, during and after the examination itself.

The on-site examination is conducted by examiners whose main tasks are:

1. Prepare a risk based annual examination program for banks and other financial institutions, utilizing the pre-examination notes prepared together with the reviewer offsite that highlight specific areas of supervisory concern.
2. Review and report on compliance with Central Bank regulations as well as the requirements placed on the institution by Union Law 10 of 1980.
3. Assess the adequacy and effectiveness of risk management systems and internal controls at the institution.
4. Carry out a selective, focused review of credit portfolios in order to identify delinquent accounts and check regulatory compliance.
5. Report to the Higher Management of the Central Bank about major findings of the examination exercise.
6. Inform concerned banks and regulated non-bank institutions of all matters that are considered of serious supervisory concerns, such as weaknesses in governance and control, deteriorating asset quality, capital and liquidity concerns, and violations of regulations.

The off-site examination process at theCentral Bank is the responsibility of the reviewers. Their main functions are as follows:

1. Analyze the submitted periodical return forms from banks and other financial institutions, and identify changes in the underlying business and their effect on risk as well as the extent of regulatory compliance.
2. Prepare reports about the concerned institutions that utilize the Central Bank's micro-prudential tools to diagnose potential issues and recommend remedial measures if any, and advice the examination team leader to carry out specific examinations, if needed.

3. Follow up with banks and other financial institutions on the main supervisory concerns.
4. Process banks' and other financial institutions' requests regarding the appointment of external auditors and other ongoing responsibilities such as the 'fit and proper' process for key members of licensed institutions' staff.
5. Review reports of foreign supervisory bodies on branches of local banks operating abroad, and submit examination findings accordingly to the Higher Management of the Central Bank.
6. Participate in the reviewers meetings organized at the head office of the Central Bank in order to identify specific areas of risk in the banking system, share market intelligence and report any unusual/abnormal developments to the Higher Management of the Central Bank.

The increase in complexity of banking and non-banking activities, emergence of new risk factors and continuous change in financial landscape resulted on the need to undertake risk assessments both at individual institution level as well as on a system-wide basis. For this reason, BSD is working to enhance its risk-based supervision processes to ensure that the department continues to support the strategic objectives and the desired outcomes of the Central Bank.

The year 2014 was an important year for BSD and 2015 continued to build on that momentum. The examination process and team structures have been under constant review with the strategic objectives of more efficient resource use, greater regulatory consistency, transparency and escalation and enforcement as a priority. These changes have meant a significant investment in improving the skill levels of all members of the team as well as in the time and effort involved, not only regarding the development of processes and systems but in the implementation of these initiatives.

There has been a significant amount of regulatory change over the last few years and this has required a constant upgrading of rule books to ensure consistency in the way the Central Bank assesses banks. In this respect, 2014 saw the completion of a major project that provided a significant improvement in banks' reporting and the collection and utilization of data. This effort has continued into 2015.

An important element of the enhancement of the risk-based examination process has been the introduction during 2014 of an all-encompassing dashboard for banks designed to quickly assess the strengths and weaknesses of an individual institution, not only in terms of regulatory compliance, but also in terms of the institutions governance, control and risk management capabilities benchmarked against global best practice as well as domestic peer groups. Balance and proportionality are important considerations in assessing the capacity of institutions. This important tool continues to be developed and has become an integral part of our risk based supervision system.

To recap, this important regulatory tool looks in detail at twelve evaluation criteria:

1. The role of the board of directors and governance
2. Management structure and efficiency of systems
3. Large exposures
4. Asset quality
5. Capital Adequacy
6. Real estate loans to deposits ratio
7. Liquidity
8. Lending to deposit ratio
9. Operational and other risks
10. Adequacy of internal controls
11. The role of audit and compliance
12. Conduct of business and complaints

Each of these criteria has further sub-criteria which feed into the result which is then weighted and a score produced. The score triggers a traffic light system for each criteria, red, amber, and green, each of which also contains a high level explanation. Consistency is ensured by the use of scorecards that are detailed as well as granular.

Perhaps even more important, the dashboard drives the regulatory concerns to both the senior management of the Central Bank and the concerned bank, in a concise and easily understandable way. The benchmarking and scoring process, as well as the ability of the system to be proportional allows the senior management of the Central Bank to allocate examination resources effectively, on the basis of risk. It is the key tool used to review and highlight key concerns as well as potential enforcement responses.

This important micro-prudential tool has been complimented by a static information sheet designated as the ‘passport’ which provides supervisors with a snapshot of the institution, its ownership, its management, its important financial highlights, critical exposures and key depositors.

Ensuring Capital Adequacy of Banks

Capital Adequacy is a key pillar for ensuring the safety and soundness of banks. The Central Bank currently requires all banks operating in the UAE to comply with the Basel II Standardized approach in assessing their regulatory capital adequacy. BSD has a team dedicated to ensuring that banks are assessing, planning and reporting their capital requirement in strict accordance with the Basel Committee rules. This includes a thorough review of the Central Bank's pillar II responsibilities as regards the ICAAP (Internal Capital Adequacy Assessment Process) as well as the SREP (Supervisory Review and Evaluation Process) which are prepared by the banks themselves. It is also worth highlighting that having done a significant amount of the preparation work in 2015 the move forward to meet Basel III standards will significantly enhance the quality of banks' core capital as well as banks' holding of liquid assets.

Maintaining Close Relationship with Other Related Institutions

BSD continues to maintain a close relationship with the financial sector, including the UAE Banks Federation, rating agencies, audit and consultancy firms, in addition to the Arab Monetary Fund, the IMF and the World Bank. Regular meetings with these institutions and the Central Bank were held throughout the year.

The Department also continued to be an active participant in the international regulatory development of Islamic finance at the Islamic Financial Services Board and the International Islamic Liquidity Management. This has been instrumental in developing a good understanding of current issues and developments and contributed to the improvement of its supervisory oversight of Sharia compliant finance.

Anti-money laundering

BSD is responsible for implementing anti-money laundering regulations. Examiners are instructed to make sure during their on-site visit that banks comply fully with FATF recommendations in this respect, based on an Examination Manual that contains KYC procedures, record keeping and reporting of Suspicious Transaction Repots (STRs).

After a review at the Central Bank's head office, an Examination Report is forwarded to the Higher Management in this regard, describing bank's degree of compliance, possible violation and recommendations.

The Risk Bureau

In order to provide a sound business environment, which would help banks, finance companies and financial investment companies make informed decisions when extending credit facilities to their respective customers, the Risk Bureau was established in April 1982 at the Central Bank of the UAE.

The Risk Bureau provides available information on total credit facilities extended to one customer, amounting AED 500,000 or more; which was later reduced to AED 250,000 in November 1989, so as to cover the largest possible number of borrowers.

The Risk Bureau also developed a system for blacklisting customers with returned unpaid cheques, in order to encourage a higher sense of commitment amongst bank customers. In addition, a customer rating system and a database of names of bank customers who fail to honor their obligations was introduced at the Bureau in October 1998.

In May 2005, the Central Bank started "live" operations of these systems, enabling financial institutions to disclose data on their borrowing customers through their own terminals linked to the Bureau's database. This allowed continuous updating of borrower data in real time.

The volume of data made available to member financial institutions was further expanded to include, along with the total credit facilities extended to one customer from all financing sources in the UAE, the total number of securities pledged against extended loans, total provisions, and interest in suspense, the lowest classification of extended facilities and a detailed statement of accounts related to the borrower.

Regulatory Developments

Introduction

The Regulatory Development Division was established in December 2012 at the Central Bank of the UAE. The broad mandate of the Division is to continuously review and develop the regulatory framework for financial institutions licensed by the Central Bank, in line with best international practice.

The main objective of the Division is to establish and maintain a regulatory framework for financial institutions in the UAE that is appropriately designed to foster sound and robust financial institutions, provide protection to consumers, and enable the financial sector to develop in a stable and prudent manner.

Developments in 2015

Liquidity

2015 witnessed the introduction of a key regulation by the Central Bank, which is a cornerstone in our new regulatory framework. The regulation regarding liquidity requirements for banks is integral to the prudential management of banks in terms of liquidity portfolio governance, risk management, and practices. This regulation and accompanying guidance manual provides banks with the framework that the Central Bank expects them to implement in order to effectively manage their liquidity risk. It introduces a new requirement that the banks hold eligible liquid assets in case of funding shocks. Equally importantly, it provides a glide path for those banks required to manage their liquidity in accordance with the Basel III liquidity standards (Liquidity Coverage ratio and Net Stable Funding Ratio) to become fully compliant by the effective Basel dates in 2018/2019.

Digital Payments

The Central Bank recognizes that Fintech development will play an important role in shaping the future of the financial services industry in the UAE. In 2015, we worked towards the development of a regulatory framework to help shape the digital payments industry in the UAE. We undertook a significant study of the digital payments landscape and infrastructure in the country and researched digital payments operations and practices in other international jurisdictions. The objective is to create a national vision and associated regulatory framework that enables and supports the development of digital payments services in the UAE, ensures the safety of the payments system, fosters prudent and robust service providers and has built in consumer protections.

We consulted extensively with all of the key stakeholders involved in digital payments and in designing the new regulatory framework and drafting the new regulations we have been guided by best international practice in this area.

Other

A significant amount of ground work has also been undertaken in 2015 aimed at bringing the Central Bank's regulatory environment up to date including the development of new draft regulations covering risk management (for all the major risk types) as well as important industry practices such as outsourcing. A key piece of this effort is also targeted towards drafting regulations on internal and external audit and control. These new regulations are designed to amalgamate, replace and bring up to date existing regulatory requirements into one focused regulatory framework following a rigorous consultation process with the industry.

Regulatory Priorities for 2016

The significant amount of preparation work undertaken during 2015 will bear fruit as 2016 unfolds. This coming year will see the issuance of some important new regulations as well as continued progress on finalizing regulations with the intention to consult on and issue these regulations in 2017.

Amongst the key tasks in 2016 are:

1. Capital

In accordance with Basel III capital requirements, the timeframe for full implementation of the new capital regime is end of 2018. The regime includes new definitions of capital, new capital buffer requirements and better quality of capital in terms of loss absorption. In 2015 Q3, the Central Bank developed an implementation program to begin the engagement process with banks towards implementing the new Basel III capital requirements for banks operating in the UAE from 2016 onwards.

2. Risk management

Five regulations in relation to risk management in banks and 5 supporting standards were completed in 2015 Q3. These 5 documents, namely Risk Management, interest rate risk, operational risk, country and transfer risk and market risk are currently under consultation with the banking sector.

3. Digital Payments

The Central Bank has developed a new vision and blueprint for digital payments services in the UAE. New regulations are in final draft form. We are currently reviewing the responses to the industry consultation and intend to finalize the new regulations by end second quarter 2016.

4. Non-Bank Financial Institutions

The regulatory framework for non-bank financial institutions (NBFIs) is also currently under review with a view to enhance their organization, development, regulation and supervisory oversight. This is now in an advanced stage of readiness and the intention is to engage with the industry on this subject by the end of 2016.

Chapter 6. Financial Market infrastructures and payments

Financial Market infrastructures are the backbone of financial markets as they enable the safe flow of funds and financial assets in the economy. Their smooth operation is crucial to maintaining confidence in the currency and supporting monetary policy operations and the stability of the financial system as a whole.

The Central Bank of the UAE plays a central role in this field. It provides payment and settlement services, oversees financial market infrastructures and payment instruments, and works with market stakeholders to achieve financial market integration. Cooperation and dialogue with other financial institutions and regulatory authorities on policy aspects relating to regional and global developments in the field of market infrastructure and payments are also of a highest importance for the Central Bank.

The public policy objectives of the CBUAE in the area of market infrastructure are targeting the limitation of systemic risk and fostering transparency and financial stability. These objectives are promoted by monitoring existing and planned systems, assessing them against the objectives and, where necessary, inducing change.

The UAE payment services ecosystem is well-established and diversified. It has undergone major reforms under the leadership of the Central Bank of the UAE, and thanks to the effective collaboration between the regulatory authorities and the financial community.

Indeed, and during the past ten years, the Central Bank has undertaken important efforts to bring the UAE into line with best practices in other developed economies. In particular, the reform agenda involved managing the overall risk effectively, promoting the use of electronic payment means (cashless), and increasing efficiency of the settlement arrangements for all type of payment transactions.

At the national level, the CBUAE has also defined the initial steps of its roadmap to support the UAE Smart Government Initiative, particularly with regard to e-Government and m-Government strategies. In this context, the priority was given to the digital payments field with the objective of enhancing the regulatory framework for stored value payment means, as well to the establishment of the enabling infrastructure to support the interoperability of e-payments between all financial institutions in the UAE.

The social dimension is yet an important component of the CBUAE’s agenda in payment systems development. The CBUAE’s support provided to the Wages Protection System (WPS) has enabled the effective implementation of the system to streamline the timely payment of wages to employees; hence meeting the desired objectives of the UAE Government in this field.

From a regional perspective, the CBUAE continues its involvement in the GCC-RTGS project aiming at enabling real-time processing of cross-border payments among GCC countries by using their domestic currencies. The utmost objective of this project is to increase the integration of domestic payment systems across GCC countries and enhance the efficiency of the existing settlement mechanisms.

On the same front, the CBUAE pursues playing a key role towards supporting the UAE's integration in the Arab regional payment ecosystem. To this effect, the CBUAE participates actively in the Arab Regional Payment System project that envisages integrating the clearing and settlement of cross-border payments in the Arab region by enabling the substitution of the existing correspondent banking system by a new system for clearing and settlement of intra-regional cross-border payments.

At the international scene, the CBUAE, in supporting the UAE's sustainable inclusive economic growth objective, is totally committed to the international agenda for "Achieving financial Access by 2020" by improving financial inclusion and access to finance to the various segments of the population.

In this regard, the Central Bank has given a highest priority to the implementation of the digital payment framework, as an important tool that would support the emergence of innovative retail instruments targeting unbanked population. In addition, the Central Bank is also leading the efforts towards establishing the enabling infrastructure and regulatory framework that would promote access to appropriate financing mechanisms and instruments for Micro, Small and Medium Enterprises, being a vulnerable segment of the economic sector.

Non-Cash payments landscape:

According to the latest data available[13], global non-cash transaction volumes reached 357.9 billion in 2013, an overall growth rate of 7.6%, almost similar to the 2012's rate of 7.5%. Among the top ten non-cash markets, China and Russia experienced remarkable growth rates of 37.7% and 33.4% respectively during the period 2012-2013. The fastest rate of growth was recorded in Emerging Asia[14] with 21.6%.

Central Europe, Middle East and North Africa (CEMEA) recorded a growth of 10.6% with economic downturns and political instability slowing growth. Volumes in Latin-America grew by 8.6%. In the mature markets[15], non-cash transactions in Europe and North America outperformed GDP growth at 5.1% and 4.6% respectively, while volumes in mature Asia Pacific countries rose 11.5%.

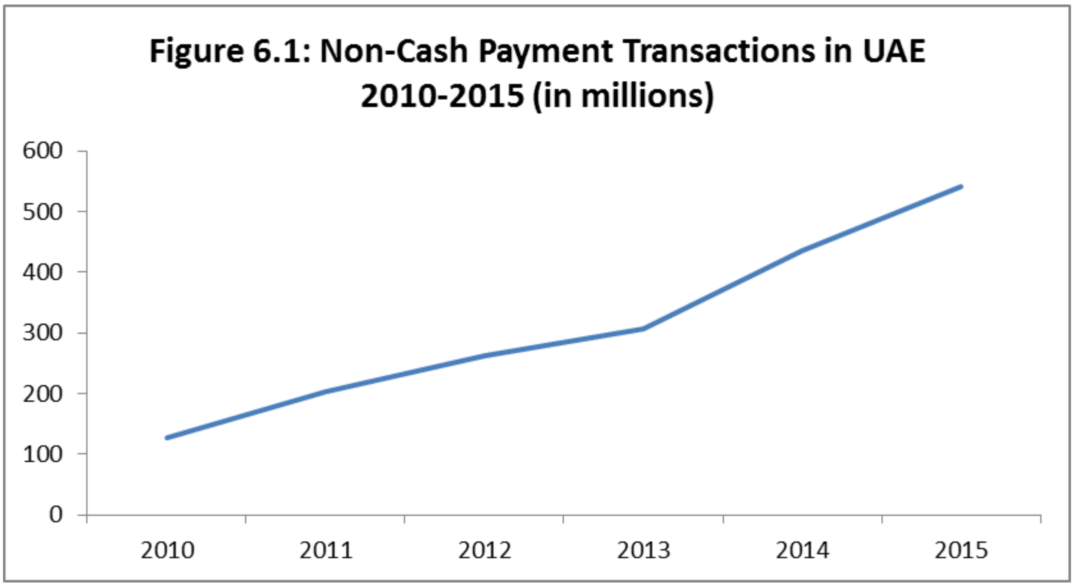
Since the 2008 financial crisis and economic downturn, the U.S market has transformed from a predominantly credit card-based non-cash market into a debit card market. This reflects the overall decrease in consumer credit and a change of purchasing habits.

[13] "The World Payments Report of 2015" that analyses the data of 2013.
[14] Emerging Asia include India and China as well as Honk Kong and other Asian countries
[15] Mature Markets are mature Asia Pacific countries including Australia, Japan, Singapore, and South Korea; Europe, including Eurozone; and North America (the U.S and Canada)

Most of European countries witnessed accelerated growth rates with a faster growth in transaction registered in Germany and the U.K. A combination of revitalized GDP growth and innovations in payment services contributed to an acceleration of non-cash payments growth in the U.K, while in some other markets in Europe, growth of non-cash transactions volume decelerated due to economic stagnation and high unemployment.

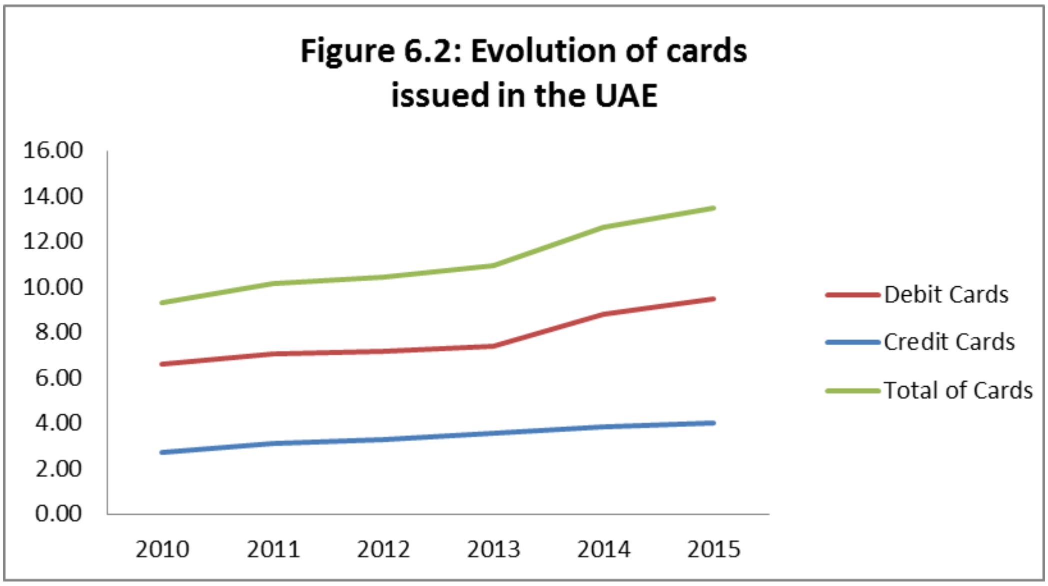
CEMEA also experienced a decline in growth rates from 23.9% in 2011-2012 to 10.6% in 2012-2013, mainly due to geopolitical tension in the Middle East and economic stagnation in Eastern Europe. A marginal decline in growth rates was also experienced in Emerging Asia markets

In the UAE, the volume of non-cash transactions reached 540.25 million transactions in 2015, with a growth rate of 24.22% compared to 434.92 million in 2014. As shown in figure 6.1, non-cash transactions volume has been constantly increasing with a compound annual growth rate during the 6-year period of 34.14%.



Growth in non-cash transaction occurred in the various payment instruments used in the UAE. During the period 2010-2015, POS transactions performed by the overall 13.49 millions of UAE cards grew by a compound annual rate of 45.55%, followed by credit transfers with 33.64%, and far away by cheques with 3.55% during the same period.

As shown in figure 6.2, the number of debit cards registered a relatively slow increase in 2015 with 7.39% compared to the important rise witnessed last year with 18.98%, while the number of credit cards continues a smooth expansion over the past 6 years with a compound rate of 8.26%. This has impacted the growth in the total number of cards issued in the country, with an increase of 6.69% over the 2014's value of 12.64 million cards. The number of point-of-sale terminals reached in 2015 around 141 thousands units, equivalent to an expansion of 26.58%; hence confirming the increasing trend registered over the period 2010-2015.



Similarly to the situation worldwide, the dominance of card transactions in non-cash volume of transactions is notable with a share of 80.30%, equivalent to a volume of 433.82 million transactions in 2015, with 8.11% of this volume done outside the UAE. Customer to Customer credit transfers account for 4.70% of non-cash payments in 2015, cheques 5.78%, and direct debits 0.38%. The remaining share 8.84% represents the volume of salary payments processed in 2015 through the Wages Protection System operated by the Central bank of the UAE (See box 6.1).

It's worth mentioning here that direct debit transactions volume, albeit low in its share, have been growing significantly since the launch of this new functionality in 2013. Indeed, after a modest start with 7930 transactions in 2013, the volume rose to reach around 650 thousands and 2.1 million transactions, respectively in 2014 and 2015. This increase is expected to continue as this instrument will predominantly be used for payment of utility bills.

Box 6.1: Wage Protection System

The Wage Protection System (WPS) was implemented at the CBUAE to meet the desired objectives of the Ministry of Labour (MoL). The objective of UAEWPS is to provide a safe, secure, efficient and robust mechanism to streamline the timely payment of wages to employees. The UAEWPS has been adopted by other authorities in the UAE such as Economic Zones World (EZW).

The model adopted by CBUAE is one where information flows from the employer to one or more of the contracted agents for payment of the wages to their employees. Funds from the employers are secured by CBUAE prior to dispatching the wage information to the agents.

The system empowers CBUAE, and thereby the LRA, with the functionality that would allow effective monitoring of the payment of wages by the employers to their respective employees.

The UAEWPS has been processing salaries since 1st of October 2009. As at the end 2015, a total of 108 Entities participate in the UAEWPS (52 Banks, 4 Non-Banking Finance Companies (NBFCs), 5 Third Party Service Providers and 40+ Exchange Houses).

The payment instruments mix in the UAE is in its way for more balance, similarly to the situation in many countries around the world. Steps taken by regulatory authorities in the UAE and efforts of the banking community to accelerate the deployment of POS devices to merchants, coupled with the domestic card payment market open to competition have increased the volume of non-cash transactions in the country.

Cultural habits in the UAE mean the country still has high levels of cash usage; the growth potential of non-cash transactions remains high, given the number of transactions per inhabitant that reached 56, compared to three-digit values in large mature economies.

The CBUAE, with the cooperation of the other authorities, has put a clear roadmap to narrow the gap in payment transactions per inhabitant in the coming years, thanks to the opportunity offered by the country to support credit-based spending and develop e-commerce and payment innovations.

The adoption and implementation of the digital payments framework by the CBUAE in 2016 is expected to lay the ground for the development of E-money and store value facility schemes, with mass acceptance of this type of instrument in various spaces such as transport and retail payments. In mobile payments, innovations continue as banks and other organizations are developing new apps to create a seamless payments experience for consumers.

Large value payments:

The CBUAE operates the infrastructure for the real-time settlement of large-value AED payments in central bank money. The system UAEFTS[16] settles, among other things, monetary policy operations and interbank transactions, thus fulfilling an important function for the country. It also handles all customer-to-customer fund transfers in the country, no matter the values of the transactions, in addition to other types of transfers.

UAEFTS continued to function smoothly in 2015, reaching 100% availability. It settled a total of approximately 413 thousands bank-to-bank transfers and had a turnover of AED 6.5 trillion, showing a slight increase of 0.65% in volume and 4.42% in value compared with end-2014.

In 2015, work continued to strengthen the role of UAEFTS as the unique real-time settlement system in the UAE by initiating the process of integrating the cash leg settlement of securities into the system. This settlement is currently being performed in commercial bank money, and in cooperation with the Securities and Commodities Authority[17], there is common understanding to move this settlement to the Central Bank of the UAE.

Moreover, progress was made in ensuring that the system achieves full compliance with the Principles on Financial Markets Infrastructure (PFMIs), particularly in the areas of risk assessment and liquidity management. In this regard, the UAEFTS went through the first assessment done by the Payment Systems Oversight Unit at the Central Bank, following the methodology suggested by the Committee on Payment and Market Infrastructures (CPMI)[18]. The overall assessment is positive with the absence of any area of non-compliance. The CBUAE has already defined an action plan to tackle the issues identified to be a source of broadly or partly compliance.

[16] UAE Funds Transfer System
[17] Capital Market Authority of the UAE
[18] CPMI is one of the BIS' committees. It is a global standard setter in the area of payment systems. It promotes the safety and efficiency of payment, clearing, settlement and related arrangements.

Oversight of market infrastructures and payment instruments

Payment systems play an important role in the smooth functioning of an economy and any inefficiency in the payments market can have a devastating effect throughout the economy. The Retail Payments platform witnessed a great deal of innovations in the last few years. Besides usage of payment cards, new products using mobile technologies emerged. The introduction of payment methods using mobile phones, wearable products like smart watches was welcomed by retail users globally due to the convenience and easy to use technologies.

Central Bank of the UAE being the main regulator of the financial sector in the UAE realized the need for regulating latest retail payment systems. With this idea, the Central Bank has embarked on formalizing a comprehensive regulation on Digital Payments. A committee to study the Digital Payments landscape was created in May 2015. This committee worked with the external consultant in studying the digital payments market and a draft regulatory framework has been drawn. The PSOU as one of the main stakeholders significantly contributed to the development of the draft framework. The Central Bank has planned to issue the Digital Payments regulatory framework in 2016.

The main objective of the PSOU is to ensure the safety, soundness and efficiency of payment systems in the country. This is possible by evaluating the payment systems using internationally recognized assessment methods. Therefore the Central Bank as part of its strategy decided to use PFMI-2012 (Principles for Financial Market Infrastructure) and the assessment methodology issued by the BIS in 2012 as a reference document while conducting assessments of payment systems in the UAE. To start with, a detailed assessment of the Central Bank operated systemically important payment systems viz UAEFTS (UAE Funds Transfer System) and ICCS (Image Cheque Clearing System) using the PFMI-2012 assessment methodology was done in Sep/Oct 2015 and a report was issued. Similarly, in 2016 the PSOU has planned to conduct assessments of other retail payment systems viz UAEDDS (UAE Direct Debit System), WPS (Wages Protection System) using the same methodology.

In addition to the above, the PSOU in 2015 studied the impact of risks due to hacking attempts on UAE ATMs (Automated Teller Machines) and issued a regulatory notice to all the ATM providers to install anti-skimming devices and digital cameras to record images while using ATMs. The PSOU is currently studying the fees and charges paid by the card issuers and merchant acquirers in order to identify the impact of such fees and charges levied on the card issuers, acquirers, the merchants which ultimately impact the card users.

PSOU strives to achieve Central Bank of the UAEs goals and mission by securing our current financial infrastructures and policies and paving the way for the future adaptation of upcoming innovations and technologies. By working hand in hand with other government institution and regulating bodies we PSOU and Central Bank can achieve a sound and effective financial infrastructure by the way of Transparency, Professionalism, participation, collaboration and trustworthiness.

Major achievements over the past year:

In 2015, many actions and initiatives have been undertaken toward enhancing the various payment and settlement systems operated by the CBUAE, increasing efficiency of the Non-cash Government payments, and providing the infrastructure to support innovation and diversity in the different payment channels. The most important realizations accomplished in 2015 are as follows:

- Expanding the activity of the UAE national switch for ATM transactions (UAESWITCH) by linking with Union Pay Network: This will allow the transactions performed by cards issued by the majority of banks in China to use the ATMs network of the UAE in a very speedy way.
- Initiating the discussion with the federal ministries and other government agencies to establish an active link to the UAEFTS in order to send automatically their payment orders through the system without any manual processing.
- Initiating the discussion with the various courts in the UAE in order to explore the possibility to have a link with the CBUAE that will support a better transmission, processing and monitoring of the court orders that are currently time-consuming and require an extensive manual processing from the two sides.
- Improving certain payment processing procedures in DDS[19] (recovery of instances for loan/finance), UAEFTS (GPSSA[20] monthly pension contribution), ICCS[21] (explicit payment acknowledgment) for the benefit of their end-users.

Priorities for the coming year 2016:

The CBUAE's priorities in payment systems field for the year ahead build on work undertaken in previous years, and comply with the UAE smart government strategies. Among these priorities, the following remain the major ones:

- **Expand the work on contingency planning to encompass the management of operational risk more broadly, including, importantly, cyber risk**. By their nature, payment systems face significant operational risk. Although such risk cannot be entirely eliminated, systems can take steps to reduce the likelihood of these risks and mitigate their impacts. In 2016, there will be an increased emphasis on cyber risk and the appropriate framework through which it can be evaluated. In common with other areas of critical national infrastructure, payment systems need to ensure they minimize vulnerability to cyber-attack.
- **Create a level-playing field for banks and non-banks as this will foster competition in the payment systems industry**. The CBUAE will pursue its efforts towards the implementation of the appropriate regulation and infrastructure that would support innovation in this field from all the components of the financial sector.

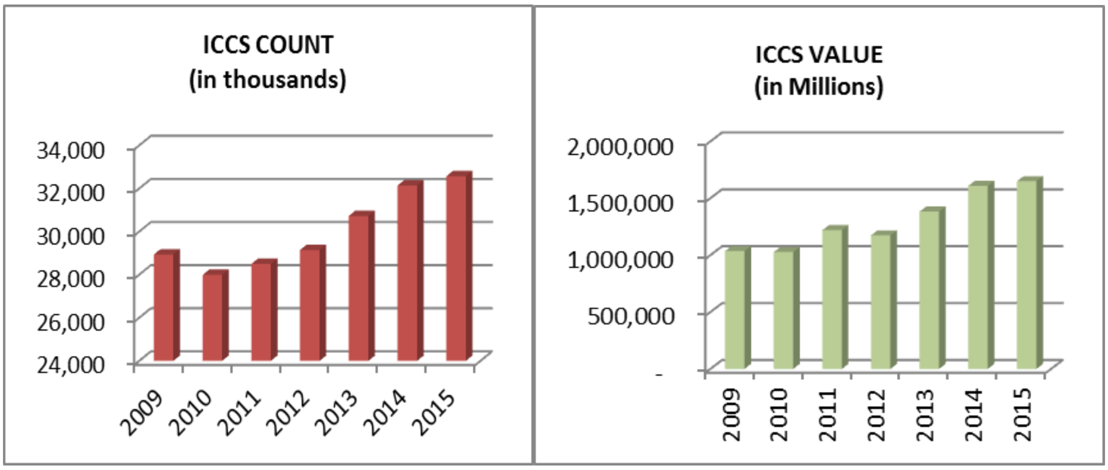
[19] DDS: Direct Debit System
[20] GPSSA: General Pension and Social Security Authority (UAE)
[21] ICCS: Image Cheque Clearing System

The implementation of the digital regulatory payments framework will ensure the digital payments market comes under a well-established regulatory framework.

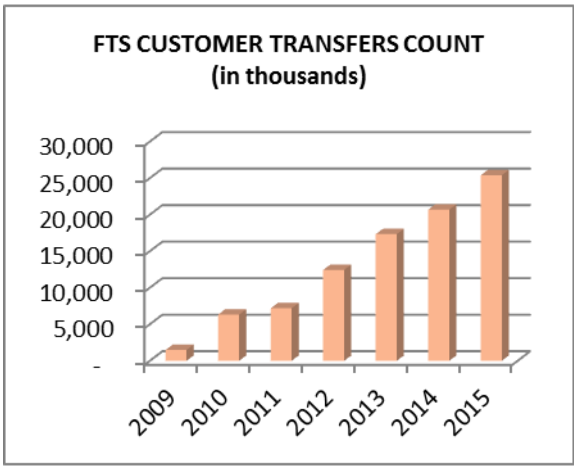
- **Pursue the effort towards strengthening the position of the UAE in the regional payment ecosystem**. The CBUAE will work during 2016 towards achieving the milestones set in the two regional projects at the GCC level and at the Arab regional level.
- **Enhance the integration of the various payment processes in the UAE**. The focus during 2016 will be on the integration of both the POS payments activity in the UAESWITCH system operated by the CBUAE, and the securities settlement as part of the UAEFTS being the RTGS system of the country.

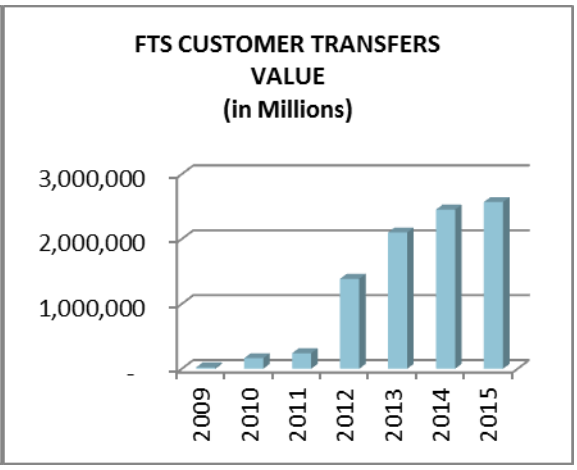
Information on the systems operated by the CBUAE

ICCS		
YEAR	**COUNT(in Thousands)**	**VALUE(in Millions)**
2009	28,939	1,035,517
2010	27,990	1,026,957
2011	28,500	1,219,004
2012	29,148	1,173,429
2013	30,724	1,382,302
2014	32,140	1,608,412
2015	32,570	1,649,654

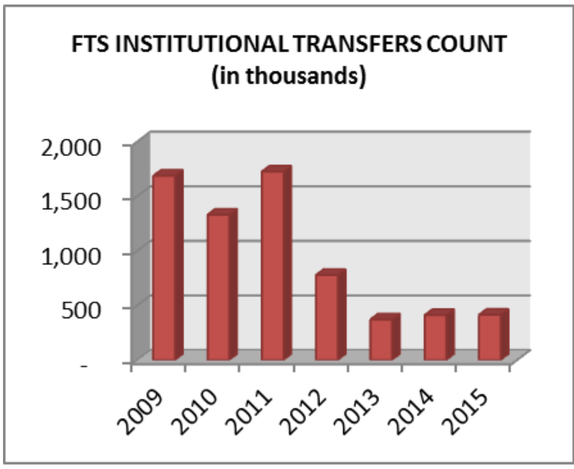


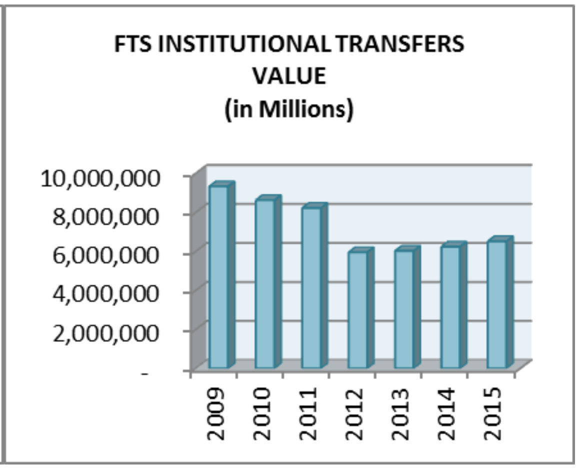
UAEFTS CUSTOMER TRANSFERS		
YEAR	**COUNT(in Thousands)**	**VALUE(in Millions)**
2009	1,481	22,466
2010	6,324	163,634
2011	7,187	240,050
2012	12,435	1,386,489
2013	17,336	2,100,953
2014	20,688	2,453,013
2015	25,407	2,570,712



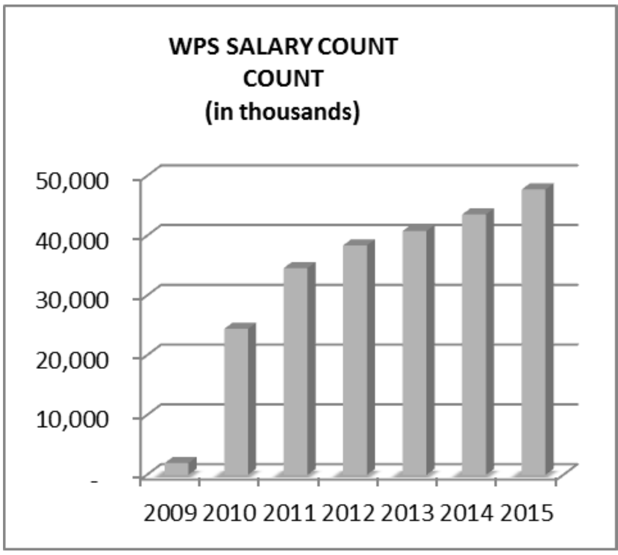


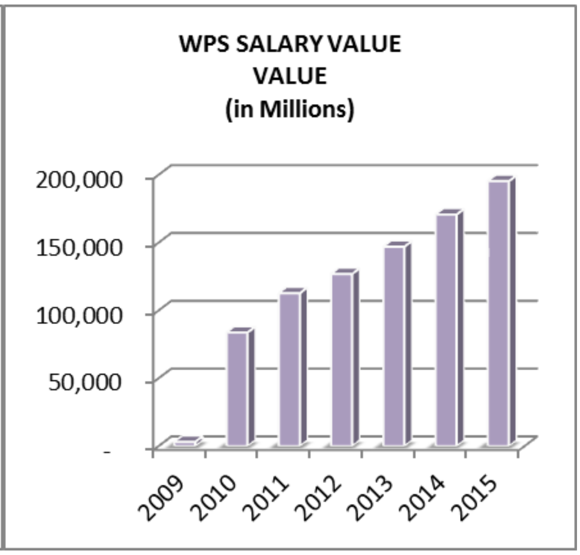
UAEFTS INSTITUTIONAL TRANSFERS		
YEAR	**COUNT(in Thousands)**	**VALUE(in Millions)**
2009	1,687	9,337,134
2010	1,330	8,631,116
2011	1,725	8,226,410
2012	780	5,953,779
2013	371	6,024,287
2014	411	6,242,099
2015	413	6,518,087



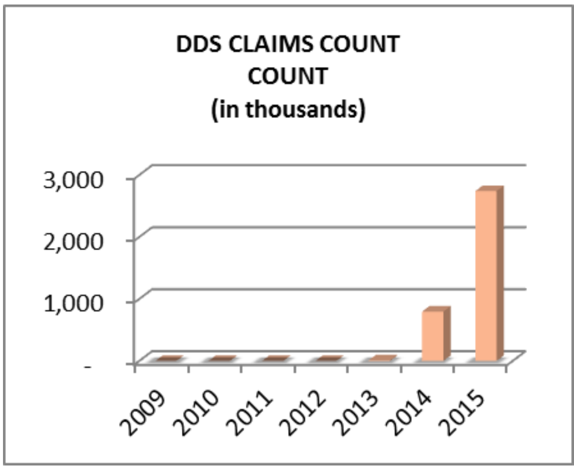


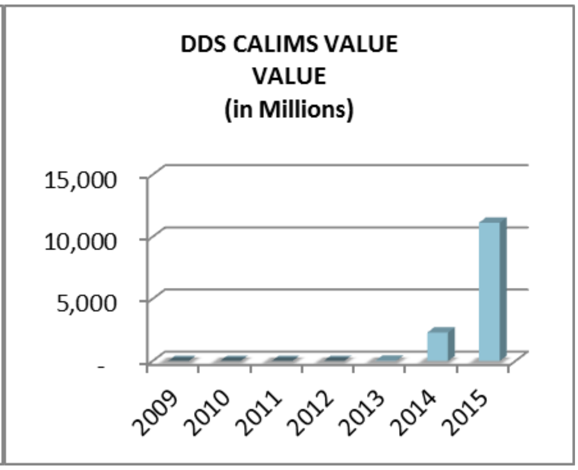
WPS SALARIES		
YEAR	COUNT(in Thousands)	VALUE(in Millions)
2009	1,974	3,039
2010	24,423	83,664
2011	34,597	112,677
2012	38,402	126,791
2013	40,806	146,905
2014	43,572	170,671
2015	47,754	195,254



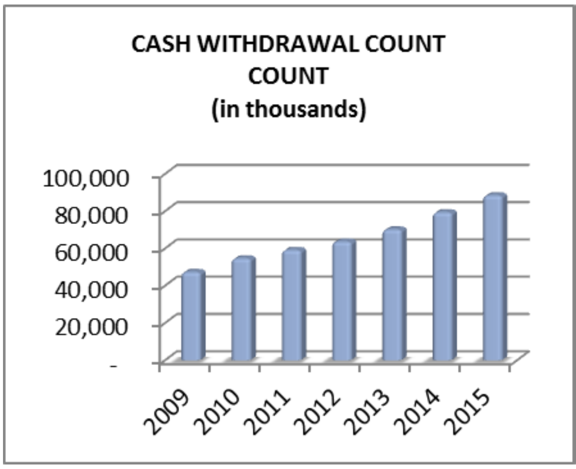


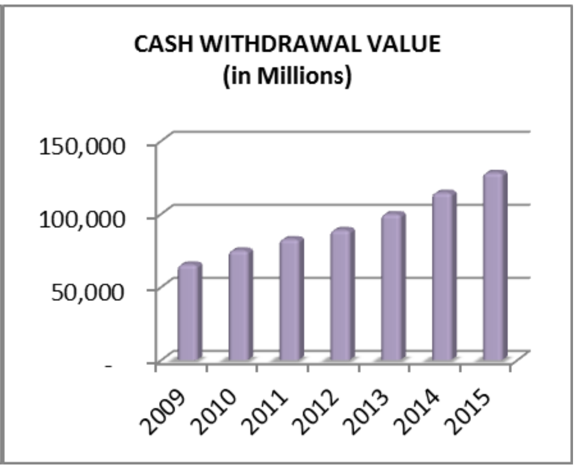
UAE DDS CLAIMS		
YEAR	**COUNT(in Thousands)**	**VALUE(in Millions)**
2009	-	-
2010	-	-
2011	-	-
2012	-	-
2013	9	26
2014	795	2,286
2015	2,740	11,137





UAE SWITCH CASH WITHDRAWAL DOMESTIC		
YEAR	**COUNT(in Thousands)**	**VALUE(in Millions)**
2009	47,361	65,335
2010	54,676	74,993
2011	59,168	82,708
2012	63,698	88,930
2013	70,227	99,867
2014	79,430	114,460
2015	88,532	128,150





Chapter 7. Anti-Money Laundering & Suspicious Cases Unit

Introduction:

The Anti-Money Laundering Suspicious Cases Unit (AMLSCU) at the Central Bank of the UAE is the Financial Intelligence Unit (FIU) of the UAE and the sole national center for receiving, analyzing and disseminating suspicious transaction reports filed by banks, other financial institutions and designated non-financial businesses and professions (DNFBPs) as per the AML/CFT Law, Federal Law No. (9) of 2014 regarding encountering money laundering crimes and combating terrorist financing. It has access to all relevant authorities in the UAE under the aegis of the National Anti-Money Laundering & Combating Financing of Terrorism Committee (NAMLCFTC) and appropriate mechanisms are in place to ensure adequate cooperation and information sharing among different government agencies involved in combating ML/TF and related crimes. AMLSCU links the private and the public sectors in combating money laundering, terrorist financing and proliferation.

AMLSCU is empowered to exchange information on suspicious transactions with its counterpart FIUs and provides training, technical assistance and guidance on evolving standards and best practices to all stakeholders for strengthening the AML/CFT framework in the country.

AMLSCU has an in-house on-line Suspicious Transactions Reporting System and banks and all other financial institutions submit STRs through the said on-line system. AMLSCU has upgraded and enhanced the on-line Suspicious Transaction Reporting System for better exploitation of data and efficient analysis and further improvements are on-going to be at par with global standards. In addition, security has been strengthened to ensure confidentiality of information/documents at AMLSCU in conformity with FATF Recommendation 29 (FIU). At present over 98% of STRs are received on-line and law enforcement authorities are increasingly using STR data in a wide spectrum of criminal investigations leading to arrests of suspected criminals, legal proceedings and subsequent convictions. This demonstrates the effectiveness of UAE's AML/CFT regime.

Major Developments Impacting the AML/CFT Framework in the UAE:

1) Issuance of Ministerial Decision No. (31) of 2015 regarding the Formation of the National Anti-Money Laundering & Combating Financing of Terrorism Committee (NAMLCFTC):

Under the revised AML/CFT Law, Federal law No. (9) of 2014, the scope and the mandate of the National Anti-Money laundering Committee have been expanded to cover terrorist financing among others and the UAE Ministry of Finance has issued a Ministerial Decision No. (31) of 2015 in February 2015 regarding the formation of the said committee named as

"National Anti-Money Laundering & Combating Financing of Terrorism Committee (NAMLCFTC)", to reflect its wider scope.

2) Work Plan for Review/Amendment of UAE AML/CFT Regulatory Framework:

In line with the revised AML/CFT Law and Executive By-Law No. (38) of 2014, AMLSCU is required to coordinate with the supervisory authorities to set/revise all AML/CFT regulations issued by the said authorities to ensure their compliance with the aforementioned laws and FATF Recommendations of 2012 and Methodology of 2013. AMLSCU has drafted a work-plan in this regard which has been placed to the NAMLCFTC for their review and approval thereof.

3) Preparation for the next round of mutual evaluation of UAE:

The National Anti-Money Laundering & Combating Financing of Terrorism Committee (NAMLCFTC) in its meeting on 16/09/2015 decided to establish the following sub-committees as part of the preparation for the next round of mutual evaluation of UAE which is scheduled to be held in 2019:

(i) Sub-committee for UAE National Risk Assessment on money-laundering and Terrorist Financing, as per FATF Recommendations and methodology.

(ii) Sub-committee for reviewing AML/CFT laws and regulations including for gold, precious metal and precious stones as per FATF Recommendations and best practices.

(iii) Sub-committee to evaluate UAE AML/CFT framework in the financial and commercial free zones in line with FATF Recommendations & best practices.

The NAMLCFTC has also decided to engage international experts (legal, financial and law enforcement) to assist the sub-committees to carry-out their mandated tasks.

4) Legal Developments:

Issuance of Anti-Discriminatory Law No. (2) of 2015:

The law criminalizing all forms of discrimination on the grounds of religion, caste, creed, doctrine, race, colour, ethnic origin was issued in July 2015 following a Decree by H.H. the President of UAE. The said law aims to protect its people against commission of acts that promote and spread religious hatred and its intolerance and discrimination in any form; and to safeguard the community at large by providing a sound foundation for the environment of tolerance, broad-mindedness and acceptance in the UAE.

Federal Law No. (8) of 2015 regarding the Federal Customs Authority:

Federal Law No. (8) of 2015 on the Federal Customs Authority (FCA) introduced a number of amendments that come in line with efforts of the UAE Government to streamline the work to safeguard the community, boost the reputation of the country as a hub nurturing businesses and investments, facilitate trade as well as improve the UAE's global competitiveness.

The law aims to improve the competitiveness of customs work by boosting performance and systems. It also seeks to unify all customs procedures, which would facilitate work on the UAE's border checkpoints. This will further strengthen the AML/CFT framework of the UAE.

5) Achievements of AMLSCU during 2015:

- 6077 STRs received from banks and other financial, commercial & economic entities including 1047 STRs on fraudulent activities, an increase of 43% from last year.
- Of which, 3,940 STRs (65%) were reviewed and analyzed during the year.
- 75% of STRs were filed by banks, whereas in 2014 it was 80%.
- 374 STRs were referred to law enforcement authorities in the UAE, for further investigation.
- 306 search and/or freeze requests received from law enforcement, public prosecution and other domestic authorities.
- Instructed financial institutions to repatriate unauthorised transfers amounting to AED 75.88 Mln related to 110 cases.
- Initiated a total of 1,119 Enhanced Customer Due Diligence (ECDD) and Fraud Alerts to Financial Institutions based on STRs.
- Initiated 867 instructions for heightened monitoring of accounts in financial institutions based on Payment Platforms.
- Conducted 174 Due Diligence procedures for pre licencing /renewal of licence of Exchange Houses.
- Conducted 229 Database checks based on requests from Domestic Stakeholders.
- Attended 5 sessions in courts as expert witness for the Public Prosecution in relation to financial crimes.
- AMLSCU as a member of the Bilateral Committees established pursuant to a decision by Dubai Public Prosecution for investigating money laundering and other financial crimes has finalized and submitted 8 Reports in 2015 to them for facilitating judicial proceedings.
- Reviewed details of 217 non-resident customers renting Safe Deposit Lockers from Banks.

- Initiated 11 special examinations of banks & moneychangers on AML/CFT compliance issues and related matters.
- Conducted 87 reviews of nominations to the board of directors of national banks.
- Processed 772 Nostro account applications for exchange companies.
- Processed 134 requests for senior management positions in banks.
- Received 572 requests for information from 84 counterpart FIUs and responded accordingly.
- Initiated 121 requests for information and spontaneous disclosures to 41 foreign FIUs.
- Hosted delegates from counterpart FIU~~s~~ and various other foreign stakeholders.
- Conducted meetings and other AML/CFT outreach programmes which benefited a total of 250 persons, representing public and private sector entities in the UAE.
- Hosted 6th MENAFATF Workshop for Assessors in October 2015.
- Provided Technical Assistance on AML/CFT to the private and public sector entities including foreign authorities which benefited 619 persons.
- Published the AMLSCU Annual Report for 2014.
- IT infrastructure developments are on-going in terms of automating the AMLSCU processes and linking the reporting entities to the STR on-line reporting system.
- Participated in various international, regional and domestic training programmes and other events to build capacity.
- Review of AMLSCU organizational structure and staffing requirements undertaken to enhance operational effectiveness of AMLSCU.

Conclusion:

AMLSCU will continue to focus on capacity building, systems development, and domestic coordination, regional and international cooperation to ensure and maintain financial integrity and counter reputational risks as well as prepare for the next round of mutual evaluation of UAE’s AML/CFT Framework.

Chapter 8. Consumer Protection

The "Consumer Protection Division" was established within the Banking Supervision Department in 2012, in line with the new Organizational Structure of the Central Bank. A subordinate center was established under the name of "Consumer Service Center" which receives customers of Banks & Financial Institutions regulated by the Central Bank who wish to raise complaints or inquire the services offered to them, or make a complaint.

The Central Bank had received **15,118** visitors in 2014 and **24,654** visitors in 2015; this significant increase was due to the availability of consumer service centers in all Central Bank branches operating in UAE.

The Consumer Protection Division aims to ensure that the consumer is treated with transparency and fairness when dealing with Banks / Financial institutions that are regulated by the Central Bank, in addition to access to high quality services at affordable prices and consistent with Central Bank Regulations. It contributes to the development of laws and regulations relating to the tasks entrusted/ assigned to it by analyzing the type of the complaints received and highlight the main issues/ problems raised by the consumers.

The Consumer Protection Division also seeks to raise the level of financial awareness among consumers & the owners of Small and Medium Enterprises to ensure that they know well about their rights and obligations resulting from their financial transactions and other related potential risks.

A comprehensive strategy has been adopted in 2014 to achieve these goals by adopting the following initiatives:

- Participation in awareness campaigns in Abu Dhabi Exhibitions, which are organized annually by government organizations.
- Issuing annually the following awareness leaflets/ brochures:
- Awareness leaflet 2014 titled: Registering a complaint against Banks/ Financial Institutions – General Guideline
- Awareness leaflet 2015 titled: Credit Cards- General Guidelines
- Providing financial education/ awareness by welcoming visits to the Central Bank by students from schools and universities.
- Posting of videos on Central Bank website presenting genuine/ real stories, such as the risks of abusing the use of credit cards and personal loans.

The Consumer Protection Division is currently working on the establishment of a special electronic page for consumer protection on the Central Bank website and developing a phone application in this regard.

The registered complaints have decreased from 6725 complaints in 2014 to 5232 complaints in 2015, i.e. by 22%. This reduction is due to the new "Online Complaint System" developed by Consumer Protection & Consumer Service Center in the third quarter of 2014, which handled / addressed most of the technical problems related to the old system such as the distinction between complaints & requests, avoidance of repeated complaints, accurate classification of complaints according to their types, availability of multiple patterns of reports…

Table 8.1 complaints statistics for 2013-2014

Type of complaints	2013	Share	2014	Share
	Number	(%)	Number	(%)
Request for documents (Liability letter/ Clearance letter/Account statements/Contracts & agreements)	1744	18%	1353	20%
Credit cards (charges & fees/ interest)	1181	12%	946	14%
Personal loans (deferment of payments/ Outstanding balance/ Charges and fees)	884	9%	725	11%
Early settlement fees (outstanding balance/ Islamic banks)	1423	14%	451	7%
Charges and fees	428	4%	342	5%
Sub total	**5660**	**57%**	**3817**	**57%**
Others Examples: (Rescheduling/ Delay in encasing manager cheque /End of service benefits/Opining-closing account/Liabilities consolidation/Top up loan/Credit ratings/ATM/Investments)	4238	43%	2907	43%
Total	**9898**	**100%**	**6724**	**100%**

Type of complaints	2015	%
Request for documents	1798	34
Credit cards	853	16
Personal loans	764	15
Credit ratings	490	9
Remittance	172	3
Housing loan	159	3
ATM	148	3
Car loans	123	2
Investments	102	2
SME’s	86	2
Returned cheques	85	2
Sub total	**4780**	**91**
Others	452	9
Total	**5232**	**100**

Chapter 9. Central Bank Strategy and Operational Plan for 2015

Strategy of the Central Bank of the UAE:

Enhancing and sharpening the focus of the Central Bank of The UAE's strategy was in the fore during 2015. To that end, the current 2014-2016 strategy has been reviewed to link it with the CBUAE's mandate. Further, a comprehensive review of the CBUAE's services took place. , As a result, more initiatives were added to the CBUAE's 2014-2016 the scope of the strategy was broadened to include new initiatives such as the SME, Digital Payments, Islamic Finance, Improving the regulatory framework and some other critical initiatives. Branches and some other business units were included in the CBUAE's strategy to ensure a broad and across the board mandate.

The revamped strategy of the CBUAE was a direct response to the governmental new initiatives, requirements of UAE competitiveness, requirements of UAE national agenda, requirements of the new governmental excellence model G4 and the direction of CBUAE new leadership.

The Central Bank of The UAE started the work on its 2017-2021 Strategy in the middle of 2015. The focus was on coordination of efforts and utilization of the expertise of all relevant stakeholders. Employees from various business units at different managerial levels participated in formulating CBUAE's 2017-2021 Strategy. The CBUAE benefited from the inputs and feedbacks of Strategic Partners, such as the government entities within the financial and economic sector, banks and other financial institutions. A comprehensive questionnaire was shared with all stakeholders asking them about their expectation from the CBUAE 2017-2021 Strategy.

The following Steps were taken in formulating CBUAE's 2017-2021 Strategic Directions:

Analyzing Internal and External Business Environments:

The current status and circumstances were analyzed and brainstormed, with a focus on shaping the future. Brain- storming sessions, comprising staff members and technical experts, have been conducted for the purpose of analyzing factors which affect the Central Bank's business and achievement of its mandate, using PESTEL (Political, Economic, Social, Technical, Environmental and Legal factors), in addition internal factors were integrated into the analysis using SWOT (Strengths, Weaknesses, Opportunities and Threats dimensions).

The outcome of the said analysis was very important input for the CBUAE's Leadership Retreat.

Coordination was established with Strategic Partners (Governmental Entities) regarding the National KPIs included in the National Agenda for the UAE. The expectations of these entities were captured through such coordination.

This stage aimed to integrate governmental work within related sectors, and identify the expectations of strategic partners from CBUAE 2107-2012 strategy. The outcome of this stage formed an important input for the CBUAE higher management retreat, and hence the CBUAE's 2017-2021 strategy.

Capturing Expectations and Inputs of Banks and other Financial Institutions:

A survey was conducted during September 2015 for the Banks and other Financial Institutions. The questionnaire captured the expectations and feedback of Banks and other Financial Institutions.

Capturing CBUAE's Higher Management directions and priorities:

Analyzing expected outcomes of the current the 2014-2016 Strategy:

The outcomes of the current CBUAE's strategy has been analyzed and evaluated.

CBUAE's Leadership Retreat:

The retreat was chaired by H.E. the Governor. The outcomes of all the previous steps were thoroughly discussed and assessed. The outcome of this retreat was the final draft of CBUAE's Strategic Direction for the Strategic Cycle 2017-2021.

The Central Bank of The UAE 2017-2021 Strategic Direction has been approved by the CBUAE Board of Directors including the 2017-2021 new Vision, Mission, Strategic Objectives, in addition to the High-Priority Initiatives. The Prime Minister Office has approved the CBUAE 2017-2021 Strategic Direction before it is officially launched. Following is a part of a quote that the Prime Minister's Office sent back as part of their comments on the strategic direction draft:

"The draft of CBUAE 2017-2021 Strategic Direction reflects the clear efforts by CBUAE in enhancing and improving its strategic direction for the upcoming cycle with the participation and involvement of all teams and leadership. This effort was according to an effective mechanism and in line with best practices".

The new vision for CBUAE is **"Promoting monetary and financial stability towards sustainable economic growth"** and this will be achieved by **enhancing monetary and financial stability through effective supervision, prudent reserve management, and robust financial infrastructure in line with international best practices and standards.**

The main areas on which the CBUAE will focus during its coming 2017-2021 Strategy include:

- Strengthen the systemic risk monitoring tools and develop a crisis management framework and set a framework for the prudential supervision policy.
- Establish a framework for Monetary Policy and operations, while maintaining the CBUAE's high-level monetary policy continued commitment to Peg the dirham to the USD.
- Expand the reserves management and its related risks.
- Improve the regulatory framework and tools that are necessary for effective banking supervision in accordance with the international standards set in this regard, in line with FSAP requirements.
- Focus on supporting the supreme economic policies and directions of the State for projects and initiatives related to the role of the central bank, including growing Islamic finance via the proper regulations that are designed to implement relevant legislations, as well as encouraging the Small and Medium Enterprises by fostering finance to SMEs.
- Implement and promote the procedures necessary for implementing Basel III recommendations.
- Develop governance system for the banking sector.
- Enhance transparency in relation to the policies of the central bank and enhance operational, procedural, and economic transparency, in accordance with the international transparency requirements for the central banks.
- Prepare for the assessment of the UAE in the field of Anti money laundering and suspicious operations which will be held within the time frame of the 4th strategic cycle.
- Make effective contribution to boost Emiratization at varying employment levels in banks and other financial institutions operating in the state and licensed by the Central Bank in line with the government's Emiratization strategy in the banking sector.

- Ensure safe and sound systems for clearing and settlement in the UAE, in addition to setting up a regulatory framework for digital payment.
- Implement initiatives and projects in an innovative way with a focus on government trends in the field of smart government.

The above areas will fall under a five core strategic objectives; **Enhance Financial Stability in the State**, **Strengthen the Monetary & Reserve Management**, **Enhance the regulatory and supervisory framework for licensed Financial Institutions**, **Improve the role of CBUAE in UAE economic management and competitiveness and Improve banking operations services & ensure safe, sound and efficient clearing and settlement systems within UAE**.

In order to achieve all the milestones included in CBUAE 2017-2021 Strategy, the CBUAE will start the implementation of a Change Program focusing on enhancing the capabilities related to its legal and regulatory frameworks This change will lead to a better organization and regulation of CBUAE's way of doing business and its relation with the relevant stakeholders, banks and other Non -Banking financial institutions licensed by the CBUAE.

The targeted change program will include the enhancement of the internal capabilities, Improvement of the existing employees, attraction of new talents and the focus on the satisfaction of staff resources. Also, CBUAE will enhance the internal processes and Organizational Structure. These changes will be positively reflected on the performance of CBUAE and the clarification of the linkage between its strategy and the UAE national agenda and competitiveness.

Appendices

Appendix A: Economic indicators

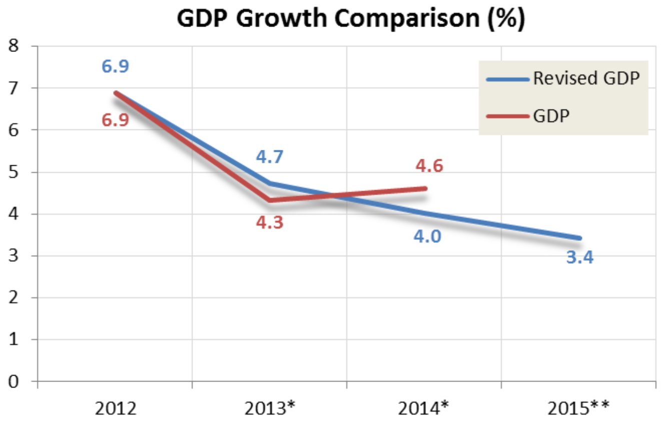
CBUAE : Selected Macroeconomic Indicators 2012 - 2017

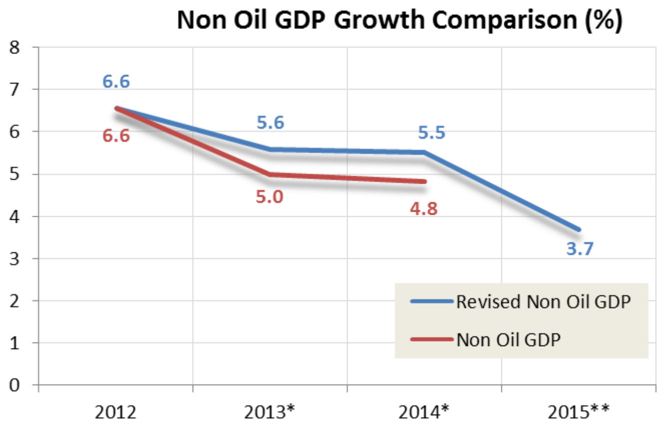
	2012	2013	2014	2015	2016 (P)	2017 (P)
WORLD GDP (%)	3.4	3.3	3.4	3.1	3.4	3.6
US GDP (%)	2.2	1.5	2.4	2.5	2.6	2.6
Oil Price ($/Bl)	112.0	108.9	98.9	52.4	36.1	42.2
Oil production (Million Barrels/day)	2.7	2.8	2.8	3.0	3.1	3.1
	In Billions of AED					
Real GDP	1057.6	1107.6	1152.2	1191.6	1221.2	1256.7
Real Non Oil GDP	718.3	758.6	800.4	830.0	854.7	885.9
Real Oil GDP	339.3	349.1	351.8	361.7	366.6	370.9
Nominal GDP	1371.4	1427.1	1476.2	1359.9	1331.1	1443.4
Nominal Non Oil GDP	832.3	896.2	968.8	1040.7	1108.1	1179.6
Nominal Oil GDP	539.2	530.9	507.4	319.3	223.1	263.8
	Annual percent change (%)					
Real GDP	6.8	4.7	4.0	3.4	2.5	2.9
Real Non Oil GDP	6.4	5.6	5.5	3.7	3.0	3.7
Real Oil GDP	7.6	2.9	0.8	2.8	1.4	1.2
Nominal GDP	7.1	4.1	3.4	-7.9	-2.1	8.4
Nominal Non Oil GDP	7.1	7.7	8.1	7.4	6.5	6.5
Nominal Oil GDP	7.1	-1.5	-4.4	-37.1	-30.1	18.3
CPI	117	118	121	126	130	133
CPI Inflation (%)	0.6	1.1	2.3	4.1	3.2	2.7

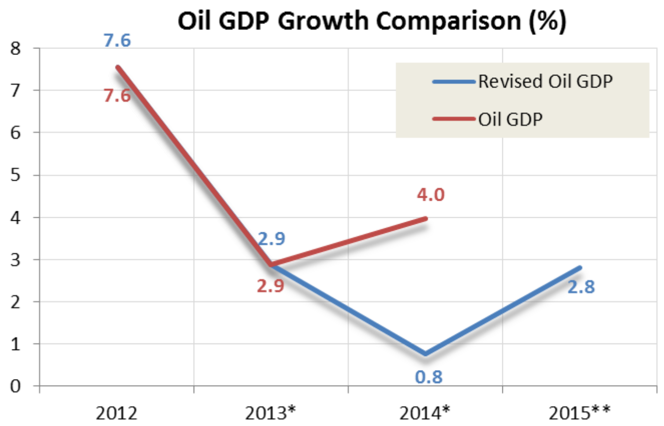
Source: FCSA, Ministry of Finance, IMF & Central Bank of UAE

Appendix B: Revised Official Figures of GDP

The Federal Competitiveness and Statistics Authority (FCSA) has released new GDP figures for 2015 and revised the historical data 2013-2014. The main modification concerned the real Oil GDP for 2014 (from 4% to 0.8%).







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