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   INTRODUCTION

   REVIEW OF LITERATURE

   NEED/IMPORTANCE OF THE STUDY

   STATEMENT OF THE PROBLEM

   OBJECTIVES

   HYPOTHESES

   RESEARCH METHODOLOGY

   RESULTS & DISCUSSION

   FINDINGS

   RECOMMENDATIONS/SUGGESTIONS

   CONCLUSIONS

   SCOPE FOR FURTHER RESEARCH

   ACKNOWLEDGMENTS

   REFERENCES

   APPENDIX/ANNEXURE

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- Bowersox, Donald J., Closs, David J., (1996), "Logistical Management." Tata McGraw, Hill, New Delhi.
- Hunker, H.L. and A.J. Wright (1963), "Factors of Industrial Location in Ohio" Ohio State University, Nigeria.

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- Garg, Sambhav (2011): "Business Ethics" Paper presented at the Annual International Conference for the All India Management Association, New Delhi, India, 19–22 June.

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ONLINE RESOURCES

- Always indicate the date that the source was accessed, as online resources are frequently updated or removed.

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- Garg, Bhavet (2011): Towards a New Natural Gas Policy, Political Weekly, Viewed on January 01, 2012 http://epw.in/user/viewabstract.jsp

MANAGEMENT OF NON-PERFORMING ASSETS: A STUDY ON RAS AL KHAIMAH BANK, UNITED ARAB EMIRATIES

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ABSTRACT
The issue of Non Performing Assets has been discussed at length for financial system all over the world. The problem of NPAs is not only affecting the banks but also the whole economy. In fact high level of NPAs in banks is nothing but a reflection of the state of health of the industry and trade. Weak loan growth and higher levels of non-performing assets (NPAs) are weighing heavily on the future prospects of the UAE's banking sector, with official data showing that provisions for NPAs continues to swell to record numbers despite stability in the country's overall economic situation. The present paper aims to develop a comprehensive understanding of the NPAs and the approach to managing them. The period from 2008 to 2011 saw erratic levels of NPAs in the UAE National Banks. Through this period, the performance of RAK BANK has been commendable in comparison with other banks. The main aim behind this paper is to know how RAK BANK is operating its business and how NPAs play its role to the operations of the bank. The study also focuses upon existing system in the UAE to solve the problem of NPAs and comparative analysis to understand the role that the banks play with concern to NPAs.

KEYWORDS
NPA, RAS AL KHAIMAH Bank

INTRODUCTION
The global crisis exposed the vulnerabilities of the banks in the UAE to varying degrees. The favorable macroeconomics environment in the year preceding the global crisis had been conducive to favorable credit conditions and lower nonperforming loans (NPLs) of banks. In 2009, NPLs increased sharply and credit stagnated, raising worries that the recovery could be slowed down by credit constraints. The banking sector in the UAE is quite fragmented, with the market currently being served by 23 domestic banks and 28 foreign banks. Banks incorporated in Abu Dhabi and Dubai hold the lion's share of total domestic assets. In view of the ambitious outlook of the economy and the expansionist program of the country, the ability of the banking sector to support the pressure is circumspect.

Asset quality deteriorated significantly in 2009 and the trend continued in 2010 with average NPL to gross loans ratio of banks increasing continuously. The troubled debt of Dubai world which have been reported in the 2010 financial statements means these numbers will likely continue to rise. It is worth noting that these ratios may not reflect the real quality of the loans portfolio given the high levels of restructured and rescheduled loans and those past due, but not impaired, reported by banks in accordance with International Financial Reporting standards. These same ratios, reported by foreign banks operating in the UAE, were higher in 2009, which is considered a better indication given the stringent provisioning requirements of those banks. As loan books stagnate in 2010 and into 2011, the ratio of NPL to gross loans is expected to increase for all banks as problematic assets surface in the banking.

The issue of Non Performing Assets has been discussed at length for financial system all over the world. The problem of NPAs is not only affecting the banks but also the whole economy. In fact high level of NPAs in banks is nothing but a reflection of the state of health of the industry and trade. Weak loan growth and higher levels of non-performing assets (NPAs) are weighing heavily on the future prospects of the UAE's banking sector, with official data showing that provisions for NPAs continues to swell to record numbers despite stability in the country's overall economic situation. According to data released by the UAE's Central Bank, total provisioning by banks in the country rose to Dh 67.3 billion in October, up 18.5 per cent in the first 10 months of 2011. Specific provisioning for NPLs up 17.2 per cent in the first 10 months, while general provisions are up 23.2 per cent in the same period, data shows year-on-year, total provisioning is up 24.4 per cent, from Dh 54.1 billion in October 2010 to Dh 67.3 billion in October 2011, while bank deposits are up less than 1 per cent, from Dh 1,053.8 bn to Dh 1,062 bn in the same period. Meanwhile, bank lending remains erratic, with the month of October seeing lending decline by Dh 2 billion, compared with a healthy growth of Dh 18.4 bn in the previous month.

During this time of economic turmoil, Ras Al Khimah Bank (RAK BANK) was amongst the few commercial banks the UAE which posted profit growth in 2009. Due to the Banks's withdrawal in 2006 from lending in the construction and civil engineering segments outside of its base Emirate, it has very little residual exposure in those segments and has no exposure to construction involving high-rise towers. RAK BANK's conservative credit policies and risk management allowed RAKBANK to be less affected by the credit crisis in 2008. With retail losses running at a third of its UAE competitive retail banking peer group.

This papers deals with understanding the concept of NPAs, its magnitude and major causes for an account becoming non-performing analysis of NPAs in RAK BANK over the past few years, the performance of the bank in the recent past and projections and concluding remarks.

STATEMENT OF THE PROBLEM
Non-Performing Asset defines as an asset, including a leased asset, becomes non-performing when it *ceases to generate income* for the bank. A credit facility in respect of which the interest and/or installment of principal has remained "*past due"* for a specified period. Meaning of NPAs an asset is classified as Non-performing Asset (NPA) if due in the form of principal and interest are not paid by the borrower for a period of 180 days. If any advance or credit facilities granted by banks to a borrower become non-performing, then the bank will have to treat all the advances facilities granted to that borrower as non-performing without having any regard to the fact that there may still exits certain advance/credit facilities having performing status. Though the term NPA connotes a financial asset of a commercial bank, which has stopped earning an expected reasonable return, it is also a reflection of the bank, which has stopped earning an reasonable return, it is also a reflection of the productivity of the unit, firm, concern, industry and nation where that asset is idling viewed with this perspective, the NPA is result of an environment that prevents it from performing up to expected levels

RESEARCH METHODOLOGY

The present paper aims to develop a comprehensive understanding of the NPAs and the approach to managing them. The period from 2008 to 2011 saw erratic levels of NPAs in the UAE National Banks. Through this period, the performance of RAK BANK has been commendable in comparison with other banks.

The present paper will aim look at some of the issues leading to the rise of NPAs and the unsustainable performance level of banks in the UAE in comparison with those of RAK BANK in this period. The recommendations and regulations of the Central Bank with increased provision for bank loans and restructurings are predicted to take a toll on earnings of the banks. It is in this context that this paper aims to highlight the management of NPA at the systemic level to improve the performance of the banks. The main aim behind this paper is to know how RAK BANK is operating its business and how NPAs play its role to the operations of the bank. The study also focuses upon existing system in the UAE to solve the problem of NPAs and comparative analysis to understand the role that the banks play with concern to NPAs.

OBJECTIVE THE STUDY

- To understand the meaning and nature of Non Performing Assets
- To identify the underlying reasons for the emergence of the NPAs
- To determine the NPAs of selected banks in the UAE
- To understand the impact of NPAs on the operations of the Banks.
- To provide a comprehensive approach to the management of NPAs in the UAE banks.
- To evaluate the comparative ratios of RAK BANK with other banks in this region.
- To give appropriate recommendations for reducing the NPAs.

This paper is based on the exploratory research method where the data is collected from primary and secondary sources. For secondary data collected from various publications of the Central Bank of the UAE, Websites of National Banks, Annual Report of National Banks, Newspaper and Magazine etc,. Primary Source collected through personal interviews, discussion with the concerned authorities in RAK BANK. The study compares data from the top 9 banks in the country with the performance of RAKBNAK to learn the lessons for sustainable performance in times of crises.

The sample used is for the comparison of the top 9 banks in the period 2008-2010, based on the research by financial institutions. The performance of the banks is compared at the reported level, as well as the new regulations of the central bank in regard to the classification of assets and provisioning for the same. This gives a more uniform picture for the purpose of comparison in line with International standards.

ANALYSIS OF THE DATA

The research paper used simple statistical analysis of data. Charts and comparative tabulations are used for easier and simpler understanding and presentation of data. Ratios and performance indicators recommended by the Central Bank according to the Base II standards are used for analysis of the data

LIMITATIONS OF THE STUDY

Management of NPAs is a highly sensitive area in the banking sector. While banks are being reluctant to divulge information about the NPAs and the steps taken for their management, the only recourse to the information is that available on the public domain.

UNITED ARAB EMIRATES BANKING SYSTEM

Banks have an important role to play in the economic growth of emerging economies, such as the UAE economy. The role of the United Arab Emirate Banking system has undergone a number of changes depending on the requirement of the economy at the material time. In its endeavour to closely monitor the economic developments in UAE, the UAE banking sector is the second largest one after Saudi Arabia among the member states of the Gulf Corporation Council (GCC). The UAE banking sector is not highly concentrated, with the five largest banks accounting for about 44 percent of the total assets of the banking system. Although there are 25 foreign banks compared with 21 local banks, the share of foreign banks in total banking assets and deposits declined from 24.1 and 26.1 per cent at end of 2003 to 21.9 and 24.5 per cent at end of 2006 respectively. The number of banks has been quite stable for a number of years, because of a ban on new foreign entrants and government's desire to avoid mergers in Banking Sector in UAE. The UAE banks ownership structure reflects the prevalent role of the public sector, which is complemented by an active role for the private sector.

IMPACTS OF NPAs ON BANKS

The performance of the public sector banks is the hampered by the increase in the Non- performing Assets. The Non- performing Assets have a drastic effect on the working of the banks. The efficiency of a bank is not always reflected only by the size of its balance sheet but by the level of return on its assets. NPAs do not generate interest income for the banks, but the same time banks are required to make provisions for such NPAs from their current profits.

- They erode current profits through provisioning requirements.
- They result in reduced interest income.
- They require higher provisioning requirements affecting profits and accretion to capital.
- They limit recycling of funds, set in assets-liability mismatches, etc.
- Adverse impact on Capital Adequacy Ratio.
- ROE and ROA goes down because NPAs do not earn.
- Bank's rating gets affected.
- Bank's cost of raising funds goes up.
- Bad effect on Goodwill.
- Bad effect on equity value.

The Central bank has issued guidelines and regulations to introduce checks and controls on the growing NPAs of the banks. To effectively act on the same and to reduce the NPAs, the banks should be motivated to introduce their own precautionary steps. Before lending the banks must evaluate the feasible financial and operational prospective results of the borrowing companies or customer. They must evaluate the borrowing companies by keeping in consideration the overall impact of all the factors that influence the business. A high level of NPAs suggests high probability of a large number of credit defaults that affect the profitability and net-worth of banks and also erodes the value of the asset. The NPA growth involves the necessity of provisions, which reduces the overall profits and shareholders' value.

GROSS NON PERFORMING ASSETS

Gross NPAs are the sum total of all loan assets that are classified as NPAs as per the guidelines of the Central bank as on the date of the Balance Sheet. Gross NPA reflects the quality of the loans made by banks.It consists of all the nonstandard assets like as sub-standard, doubtful, and loss assets. It can be calculated with the help of following ratio:

$$\text{Gross NPAs Ratio} = \frac{\text{Gross NPAs}}{\text{Gross Advances}}$$

NET NPA

Net NPA shows the actual burden of banks. Since the bank balance sheets contain a huge amount of NPAs and the process of recovery and write off of loans is very time consuming, the provisions the banks have to make against the NPAs according to the central bank guidelines, are quite significant. That is why the difference between gross and net NPA is quite high. It can be calculated by following:

$$\text{Net NPAs Ratio} = \frac{\text{Gross NPAs} - \text{Provisions}}{\text{Gross Advances} - \text{Provisions}}$$

CAUSES FOR AN ACCOUNT BECOMING NPA

- **Internal factors**
- **External factors**

INTERNAL FACTORS

- Funds borrowed for a particular purpose but not use for the said purpose.
- Project not completed in time.
- Poor recovery of receivables.
- Excess capacities created on non-economic costs.
- In-ability of the corporate to raise capital through the issue of equity or other debt instrument from capital markets.
- Business failures.
- Diversion of funds for expansion\modernization\setting up new projects\ helping or promoting sister concerns.
- Willful defaults, siphoning of funds, fraud, disputes, management disputes, mis-appropriation etc.
- Deficiencies on the part of the banks viz. in credit appraisal, monitoring and follow-ups, delaying settlement of payments\ subsidiaries by government bodies etc.,

EXTERNAL FACTORS

- Sluggish legal system
- Changes that had taken place in labour laws
- Lack of sincere effort.
- Scarcity of raw material, power and other resources.
- Industrial recession.
- Shortage of raw material, raw material\input price escalation, power shortage, industrial recession, excess capacity, natural calamities like floods, accidents.
- Failures, nonpayment, over dues in other countries, recession in other countries, externalization problems, adverse exchange rates etc.
- Government policies.

EARLY DETECTION OF NPA SYMPTOMS

Symptoms by which one can recognize a performing asset turning in to Non-performing asset are categorized as follows

FINANCIAL

- Non-payment of the very first installment in case of term loan.
- Bouncing of cheques due to insufficient balance in the accounts.
- Irregularity in installment
- Irregularity of operations in the accounts.
- Unpaid overdue bills.
- Declining Current Ratio
- Payment which does not cover the interest and principal amount of that installment
- While monitoring the accounts it is found that partial amount is diverted to sister concern or parent company

OPERATIONAL AND PHYSICAL

- If information is received that the borrower has either initiated the process of winding up or are not doing the business.
- Overdue receivables.
- Stock statement not submitted on time.
- External non-controllable factor like natural calamities in the city where borrower conduct his business.
- Frequent changes in plan
- Nonpayment of wages

ATTITUDINAL CHANGES

- Use for personal comfort, stocks and shares by borrower
- Avoidance of contact with bank
- Problem between partners

OTHERS

- Changes in Government policies
- Death of borrower
- Competition in the market

PREVENTIVE MEASUREMENT FOR NPAs

EARLY RECOGNITION OF THE PROBLEM

Invariably, by the time banks start their efforts to get involved in a revival process, it's too late to retrieve the situation- both in terms of rehabilitation of the project and recovery of bank's dues. Identification of weakness in the very beginning that is : When the account starts showing first signs of weakness regardless of the fact that it may not have become NPA, is imperative. Assessment of the potential of revival may be done on the basis of a techno-economic viability study. Restructuring should be attempted where, after an objective assessment of the promoter's intention, banks are convinced of a turnaround within a scheduled timeframe. In respect of totally unviable units as decided by the bank, it is better to facilitate winding up/ selling of the unit earlier, so as to recover whatever is possible through legal means before the security position becomes worse.

IDENTIFYING BORROWERS WITH GENUINE INTENT

Identifying borrowers with genuine intent from those who are non- serious with no commitment or stake in revival is a challenge confronting bankers. Here the role of frontline officials at the branch level is paramount as they are the ones who have intelligent inputs with regard to promoters' sincerity, and capability to achieve turnaround. Based on this objective assessment, banks should decide as quickly as possible whether it would be worthwhile to commit additional finance. In this regard banks may consider having "Special Investigation" of all financial transactions or business transactions, books of account in order to ascertain real factors that contributed to sickness of the borrower. Banks may have penal of technical experts with proven expertise and track record of preparing techno-economic study of the project of the borrowers. Borrowers having genuine problems due to temporary mismatch in fund flow or sudden requirement of additional fund may be entertained at branch level, and for this purpose a special limit to such type of cases should be decided. This will obviate the need to route the additional funding through the controlling offices in deserving cases, and help avert many accounts slipping into NPA category.

TIMELINESS AND ADEQUACY OF RESPONSE

Longer the delay in response, greater the injury to the account and the asset. Time is a crucial element in any restructuring or rehabilitation activity. The response decided on the basis of techno-economic study and promoter's commitment, has to be adequate in terms of extend of additional funding and relaxations etc. under the restructuring exercise. The package of assistance may be flexible and bank may look at the exit option.

FOCUS ON THE CASH FLOWS

While financing, at the time of restructuring the banks may not be guided by the conventional fund flow analysis only, which could yield a potentially misleading picture. Appraisal for fresh credit requirements may be done by analyzing funds flow in conjunction with the Cash Flow rather than only on the basis of Funds Flow.

MANAGEMENT EFFECTIVENESS

The general perception among borrower is that it is lack of finance that leads to sickness and NPAs. But this may not be the case all the time. Management effectiveness in tackling adverse business conditions is a very important aspect that affects a borrowing unit's fortunes. A bank may commit additional finance to an align unit only after basic viability of the enterprise also in the context of quality of management is examined and confirmed. Where the default is due to deeper malady, viability study or investigative audit should be done – it will be useful to have consultant appointed as early as possible to examine this aspect. A proper techno- economic viability study must thus become the basis on which any future action can be considered.

MULTIPLE FINANCING

A. During the exercise for assessment of viability and restructuring, a Pragmatic and unified approach by all the lending banks/ FIs as also sharing of all relevant information on the borrower would go a long way toward overall success of rehabilitation exercise, given the probability of success/failure.

B. In some default cases, where the unit is still working, the bank should make sure that it captures the cash flows (there is a tendency on part of the borrowers to switch bankers once they default, for fear of getting their cash flows forfeited), and ensure that such cash flows are used for working capital purposes. Toward this end, there should be regular flow of information among consortium members. A bank, which is not part of the consortium, may not be allowed to offer credit facilities to such defaulting clients. Current account facilities may also be denied at non-consortium banks to such clients and violation may attract penal action.

PROFILE OF THE RAK BANK

RAKBANK, the trading name of the National Bank of Ras Al-Khaimah, is a public joint stock company, headquartered in the emirate of Ras Al-Khaimah, in the UAE. The Head Office of the bank is situated in RAKBANK Building, Emirates Rd, Ras Al-Khaimah. The bank is 52.75% owned by the Government of Ras Al-Khaimah. Shares are publicly traded. Board consists of several members of the ruling family of the emirate of Ras-Al Khaimah and businessmen from UAE and Kuwait. The bank is engaged in providing retail and corporate banking services through a network of thirty one branches in the United Arab Emirates. With assets of Dh. 23 billion as at 30 September 2011, it was named the second most profitable bank among GCC top 50 Banks in 2009.

Founded in 1976, the Bank is one of the region's oldest local financial institutions offering a range of personal banking services through its branch network as well as its Telephone, Online and Mobile Banking channels. A major provider of credit cards in the UAE, RAKBANK was the first to launch features such as 'Free for Life' and 'Cashback on Purchase', now adopted by many industry players. RAKBANK was voted the number one Credit Card provider in the Middle East and North Africa region by The Banker Middle East Product Awards 2011. It has also established itself as a leading mortgage and personal loans provider among conventional commercial banks in the UAE, with award-winning customer service. In addition, RAKBANK is one of the most active banks in the area of small to medium enterprise (SME) finance, with a dedicated business unit that offers financial solutions to SME clients.

PERFORMANCE OF RAK BANK

The Financial performance of RAKBANK was remarkable in the recent years considering the economic downturn which has been affecting the bottom lines of most of the other banks in the region. The net profit for the year 2010 amounted to AED 1.0 billion an increase of 38.1% over the previous year. The growth has continued in the current year and the net profit for the nine months ending September 30, 2011 was AED 906,497 compared to AED 729,838 for the same period the previous year, registering a 24.2% growth. On the lending side the problems which were experienced in 2009 extended into the first four months of 2010 but the situation improved as the year continued. Liquidity in 2010 was also significantly tighter in the first half of the year as opposed to the second where improvement has led to reductions in retail deposit rates. However, these rates remained stubbornly higher than similar U.S. Dollar rates notwithstanding the linkage between the two currencies. In the early part of the year this gave rise to substantial arbitrage opportunities but with declining rates this is lessening. RAKBANK has continued to focus on good opportunities in its chosen lending segments, namely personal and auto loans, small and medium enterprises, credit cards and mortgages. Notwithstanding the economic downturn and overall general market conditions RAKBANK has continued to lend. This growth in volume is the primary reason for the improvement in the bank's results, which are a record.

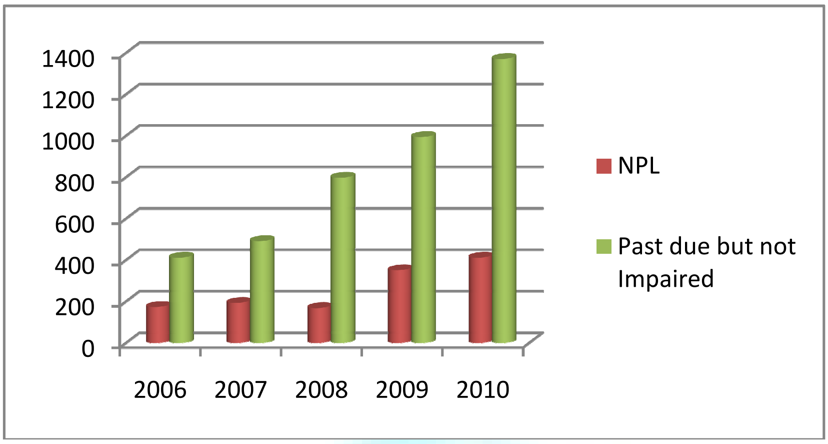
A net profit of AED1 billion was achieved in 2010 compared with AED726.2 million for the previous year. There has been no change in the bank's core business which has maintained its retail and SME focus. As a result of the opportunities which presented themselves in the early part of the year, net interest income rose to AED1.61 billion an increase of 30.9% over 2009. Total advances as at 31st December 2010 stood at AED16.4 billion an increase of 22.1% over 2009 whilst total assets increased by 25% to close at AED21.4 billion. Complementing this growth in assets, other income consisting of fees, commissions, foreign exchange, investment and other operating income grew by 22% to AED 605.0 million. During the year the bank took adequate provisions on its portfolio. Net credit losses increased by 7.1% to AED269.8 million in 2010 from AED251.9 million in 2009, however this was on a larger asset base. Towards the end of the year there was an improving trend in the NCL and the impairment charge for the 4th quarter 2010 were down to AED59.5 million from AED 81.3 million recorded in 1st quarter 2010. The growth in the asset book has been supported by a combination of increases in customer deposits and shareholders equity. The increase in customer deposits was achieved through growth in both fixed term deposits and transaction accounts.

Liquidity ratio stood at 18.2% at year end compared to 16.8% at the end of year 2009. During 2010, AED 1.07 billion of the bank's EMTN programme matured and was repaid by the bank from internal resources. The bank's capital adequacy ratio as per Basel I at end of the year was 15.4% composed entirely of Tier 1 capital against a current minimum of 12% of Tier 1 capital prescribed by the Central Bank of the UAE. With the approval of the Ministry of Finance, the bank has converted its liquidity support loans given in 2008 into 7 year loans dating from 31st December 2009 which because of their term are eligible for Tier 2 status. If that finance is also taken into account then the bank's overall capital adequacy ratio stood at 19.2% a figure which will be further enhanced on approval by the shareholders of the proposed dividend.

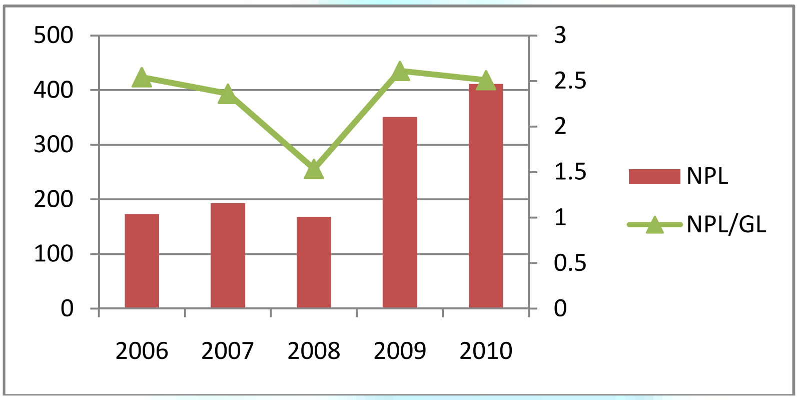
The following table illustrates the bank's ratings by leading rating agencies:

Rating Agency	Deposits	Financial Strength	Outlook
Moody's	Baa1 / P-2	D+	Stable
Fitch	BBB+ / F2	-	Stable
Capital Intelligence	A-/ A2	BBB+	Stable

PROVISIONS FOR NPAs FOR RAKBANK



NPAs for RAKBANK



NPAs of RAKBANK with NPA / Gross Asset Ratio – Years 2006 to 2010

RAKBANK has been on a steady growth mode through the entire period of the study with seemingly no effect of the recession. The period of recession while it was a difficult time for many banks, was an opportunity for RAKBANK to open up new avenues. The current results of the bank, obtained from the interim report from PWC also attest the fact. Below is the consolidated report of the NPA performance of RAKBANK.

Year	Total Provisions	Individual Impaired	Collective Provisions	GL	NPL	Past due but not Impaired	Total Assets	NPL/GL
2006	195.1	126.1	69	6,813.47	173.16	411.52	8,842.29	2.54%
2007	217.82	122.8	95	8,172.48	192.84	491.34	10,973.77	2.36%
2008	225.32	125.32	100	10,950.50	168.05	797.49	13,922.06	1.53%
2009	346.74	241.14	105.6	13,429.70	350.65	993.91	17,117.61	2.61%
2010	307.89	200.29	107.6	16,401.74	411.52	1,370.52	21,379.95	2.51%
September 2011	326.42	253.12	73.3	18,004.86	512.79	-	23,024.42	2.85%

Consolidated NPA report fo RAKBANK from 2006 till September 2011

COMPARISON AND ANALYSIS OF DATA

The data collected from the Reports and research material for the banks can be analyzed using a wide range of Analytical tools and performance indicators. However, the most widely used indicators of performance are as below:

Performance indicators

- Capital Quality
- Asset Quality

CAPITAL QUALITY

The Capital Quality of the banks can be measured using the Capital Adequacy Ratio (CAR) also referred to as the Capital to Risk Weighted Assets Ratio (CRAR). The CAR measures Two types of capital are measured: tier one capital, which can absorb losses without a bank being required to cease trading, and tier two capital, which can absorb losses in the event of a winding-up and so provides a lesser degree of protection to depositors

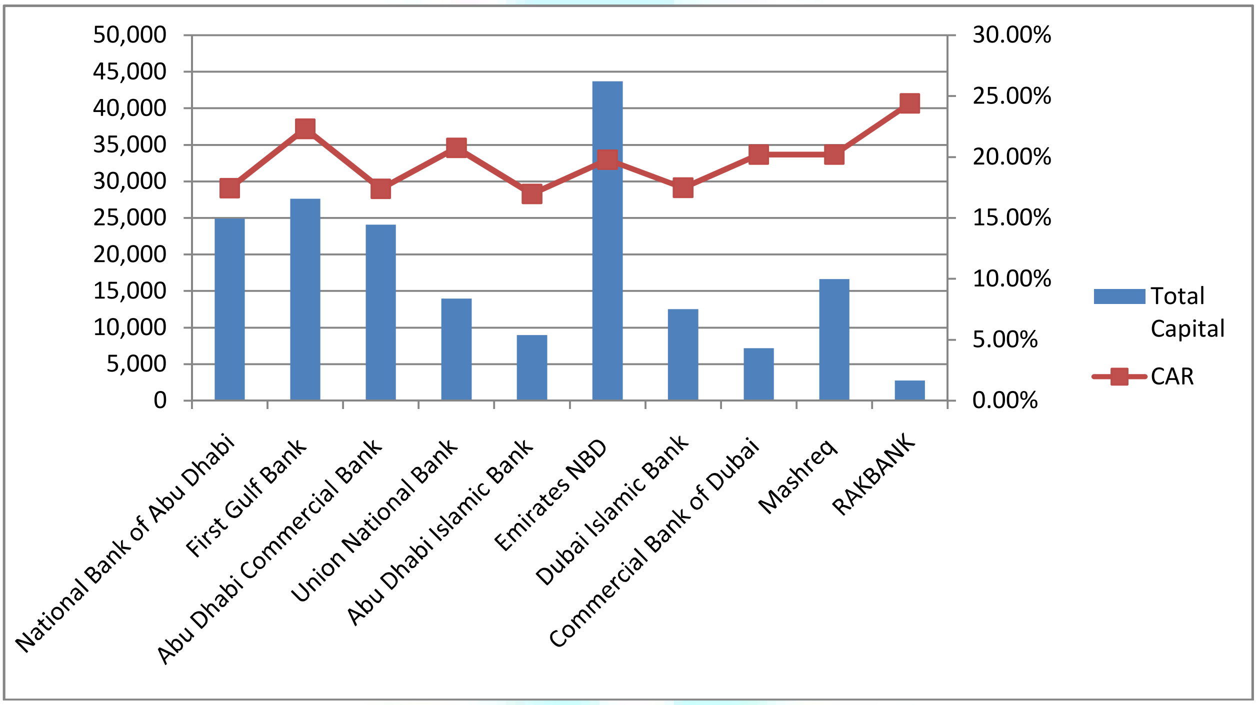
$$CAR = \frac{\text{Tier One Capital + Tier Two Capital}}{\text{Risk Weighted Assets}}$$

The following table shows the CAR for the Top 9 banks in UAE for the year 2009 along with that of RAKBANK.

COMPARATIVE ANALYSIS OF CAPITAL ADEQUACY RATIO OF RAKBANK

UAE BANKS Figures in AED mn.	Total Capital	CAR
National Bank of Abu Dhabi	24,894	17.42%
First Gulf Bank	27,636	22.30%
Abu Dhabi Commercial Bank	24,068	17.38%
Union National Bank	13,958	20.74%
Abu Dhabi Islamic Bank	8,988	16.96%
Emirates NBD	43,690	19.76%
Dubai Islamic Bank	12,503	17.47%
Commercial Bank of Dubai	7,181	20.19%
Mashreq	16,652	20.18%
Cumulative	**179,569**	**19.18%**
RAKBANK	2,755	24.38%

The above comparative with the top 9 banks by Asset value in UAE with RAK bank shows that the CAR ratio of RAKBANK is the highest among the banks for the year 2009 and is more than 5 percentage points of the Cumulative CAR of the top banks in UAE. This reflects the performance of the bank when the outlook of the banks, especially those based in Dubai face bleak prospects in view of the Dubai world and other real estate exposures.



The comprehensive comparison of the Asset Quality has been carried out and the results are presented in a tabulated form below. The Comparison takes into consideration the NPAs and the Provisions as reported and the Coverage ratio. With the new regulations from the Central bank coming into effect, the Coverage ratio for with the new calculation is also presented. While the Cumulative Coverage ratio of the top banks stands at 68.50%, RAKBANK has a reported coverage ratio of 98.88% ensuring that the effect of the NPAs in not felt on the profitability of the bank.

COVERAGE RATIO OF THE UAE BANKS

UAE BANKS - ASSET QUALITY Figures in AED mn.	NPLs as reported	Past due (> 90 days)	NPLs - 90 days	Gross Loans	NPL / G.L. (old)	NPL / G.L. (revised)	Total Provisions	Coverage ratio - reported	Coverage ratio - new calculation
National Bank of Abu Dhabi	1,687	-	1,687	139,971	1.20%	1.20%	2,714	160.90%	160.90%
First Gulf Bank	1,451	1,647	3,098	92,916	1.60%	3.30%	2,530	174.40%	81.70%
Abu Dhabi Commercial Bank	6,242	-	6,242	120,843	5.20%	5.20%	4,232	67.80%	67.80%
Union National Bank	793	252	1,046	51,580	1.50%	2.00%	812	102.30%	77.60%
Abu Dhabi Islamic Bank	2,527	1,767	4,294	42,225	6.00%	10.20%	1,751	69.30%	40.80%
Emirates NBD	5,041	823	5,865	219,679	2.30%	2.70%	5,275	104.60%	89.90%
Dubai Islamic Bank	3,107	1,378	4,485	51,873	6.00%	8.60%	1,948	62.70%	43.40%
Commercial Bank of Dubai	767	339	1,106	29,114	2.60%	3.80%	738	96.20%	66.70%
Mashreq	3,614	643	4,257	47,933	7.50%	8.90%	1,985	54.90%	46.60%
Cumulative	25,229	6,849	32,078	796,134	3.20%	4.00%	21,984	87.10%	68.50%

Effect of the new Regulations on the profitability of the banks can be gauged by the provisioning requirements of the banks as opposed to the actual provisioning done during the fiscal year.

UAE BANKS - PROVISIONS Figures in AED mn.	Total Capital	Total RWA	Credit RWA	CAR	1.5% of CRWA	Reported Collective Provisions	Difference
National Bank of Abu Dhabi	24,894	142,882	128,344	17.42%	1,925	1,604	321
First Gulf Bank	27,636	123,911	114,173	22.30%	1,713	1,946	-233
Abu Dhabi Commercial Bank	24,068	138,475	126,294	17.38%	1,894	1,505	389
Union National Bank	13,958	67,293	63,582	20.74%	954	325	629
Abu Dhabi Islamic Bank	8,988	53,011	50,101	16.96%	752	518	234
Emirates NBD	43,690	221,100	204,800	19.76%	3,072	1,858	1,214
Dubai Islamic Bank	12,503	71,556	64,478	17.47%	967	353	614
Commercial Bank of Dubai	7,181	35,571	32,461	20.19%	487	329	158
Mashreq	16,652	82,507	77,086	20.18%	1,156	513	643
Cumulative	179,569	936,307	861,321	19.18%	12,920	8,950	3,970
RAKBANK	2,755	14,626	10,983	24.38%	165	105.6	59

The above table is the difference in the provision requirements as per the new regulations and reflects upon the effect on the profits due to the new provisioning rules requiring a provisioning of 1.5% of the CRWA.

In comparison to the other banks RAKBANK appears to have done exceedingly well with the management of their NPAs where while the cumulative NPL to Gross Loan ratio stands at 3.2%, RAKBANK's NPL to GL ratio for the same period is 2.61%. However, we believe there is still scope for improvement with a prudent approach to managing the NPAs. The below table shows the performance of RAKBANK in terms of NPAs over the past 5 years along with the Assets, the Gross Loans and other ratios which can be used to gauge the NPAs. Two new ratios suggested as part of this research are also shown in the table wherein the NPL to total Asset ratio in conjunction with the NPL to GL ratio can be used to determine the overall effect the NPLs have on the performance of the bank. Another ratio, the "Past due but not impaired" to the NPL ratio can be used to form the basis for identifying the trends and forecasting the probability of Past due loans turning into non performing loans in the future.

The commendable performance of RAKBANK is possible due to its accounting practices which give a good measure for Management of NPAs. For the purpose of better understanding of the bank's grading and accounting system, a brief about the accounting practices are mentioned here.

Year	Total Provisions	Individual Impaired	Collective Provisions	GL	NPL	Past due but not Impaired	Total Assets	% of Collective	NPL to Asset ratio	Past Due / NPL	NPL/GL
2006	195.1	126.1	69	6,813.47	173.16	411.52	8,842.29	35%	1.96%	2.37653	2.54%
2007	217.82	122.8	95	8,172.48	192.84	491.34	10,973.77	44%	1.76%	2.547915	2.36%
2008	225.32	125.32	100	10,950.50	168.05	797.49	13,922.06	44%	1.21%	4.745552	1.53%
2009	346.74	241.14	105.6	13,429.70	350.65	993.91	17,117.61	30%	2.05%	2.834479	2.61%
2010	307.89	200.29	107.6	16,401.74	411.52	1,370.52	21,379.95	35%	1.92%	3.330385	2.51%
Till Sep 2011	326.42	253.12	73.3	18,004.86	512.79	-	23,024.42	22%	2.23%	-	2.85%

FINDINGS

- Overall NPAs in UAE banks are in an upward trend following the global economic crisis.
- RAKBANK NPAs are currently at an all-time high but it has also got a much larger Asset base and adequate provisioning.
- Banks based in Dubai are most affected by the downturn, while RAKBANK appears to be the least affected.
- NPA management policies and practices in RAKBANK appear to be adequate and the outlook for the bank is quite stable.
- Some banks with more exposure to high-rise constructions are more badly affected in the recent years than those banks with lesser exposure.
- RAKBANK's exposure to the real estate downturn is minimal and the focus is more on the retail sector and SMEs which has insulated it from the effects of the real estate crash and the global downturn.
- Central bank's new regulations appear to be issued to bring UAE banking practices online with International standards as well as to identify the problems with the banks at an earlier stage.
- Central bank's capital infusion has given a new lease of life to 4 of the large national banks which have managed to steer out of troubled waters

SUGGESTIONS

- Banks should keep a stringent check on advances made to Real Estate companies including GREs as this segment contributed heavily to the NPAs in the years 2008 and 2009.
- Banks including RAKBANK should increase their non-interest income, as rise in NPAs due to default in interest income may affect profits adversely
- Uneven scale of repayment with higher interest rates in the initial years should be preferred.
- Ratios of based on asset classification, and past due to NPA should be considered for forecasting the probability of NPAs in the future.
- A forecasting model based on Asset classification can be designed using historic data in the following manner to better prepare for future NPAs.

$$
\begin{array}{ccc}
 & & \text{Time } t+1 \\
 & & \begin{array}{cccc} \text{STD} & \text{SUB} & \text{DOUB} & \text{LOSS} \end{array} \\
\text{Time } t & \begin{array}{c} \text{STD} \\ \text{SUB} \\ \text{DOUB} \\ \text{LOSS} \end{array} & \begin{pmatrix} p_{11} & p_{12} & p_{13} & p_{14} \\ p_{21} & p_{22} & p_{23} & p_{24} \\ p_{31} & p_{32} & p_{33} & p_{34} \\ p_{41}(=0) & p_{42}(=0) & p_{43}(=0) & p_{44}(=1) \end{pmatrix}
\end{array}
$$

Since the probability of a loss asset being converted to any higher asset category is zero, p41 = p42 = p43 = 0 and thus p44 = 1.This transition matrix can be used to assess the loan quality of a firm level borrower by evaluating the financial position. However, this matrix will be difficult to apply to assess individual borrowers because unlike a firm level borrower, financial data of an individual is not available. Therefore, this matrix can be better applied for a firm level or corporate level borrower.

- More focus should be laid on the recovery of doubtful and sub-standard assets ensuring that they do not turn into NPAs

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