

**INDEPENDENT AUDITORS' REVIEW REPORT ON THE
INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**TO: THE SHAREHOLDERS OF
RIYAD BANK
(A Saudi Joint Stock Company)**

Introduction

We have reviewed the accompanying interim condensed consolidated statement of financial position of Riyad Bank (the "Bank") and its subsidiaries (collectively referred to as the "Group") as of 30 June 2018, and the related interim condensed consolidated statements of income and comprehensive income for the three-month and six-month period then ended and interim condensed consolidated statements of changes in shareholders' equity and cash flows for the six-month period then ended and other explanatory notes (the "interim condensed consolidated financial statements").

Management is responsible for the preparation and presentation of these interim condensed consolidated financial statements in accordance with International Accounting Standard 34 "Interim Financial Reporting" ("IAS 34") as modified by the Saudi Arabian Monetary Authority ("SAMA") for the accounting of zakat and income tax. Our responsibility is to express a conclusion on these interim condensed consolidated financial statements based on our review.

Scope of review

We conducted our review in accordance with the International Standard on Review Engagements 2410, "Review of Interim Financial Information Performed by the Independent Auditor of the Entity" as endorsed in the Kingdom of Saudi Arabia. A review of interim financial information consists of making inquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with International Standards on Auditing that are endorsed in the Kingdom of Saudi Arabia, and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

Conclusion

Based on our review, nothing has come to our attention that causes us to believe that the accompanying interim condensed consolidated financial statements are not prepared, in all material respects, in accordance with IAS 34 as modified by SAMA for the accounting of zakat and income tax.

Other regulatory matters

As required by SAMA, certain capital adequacy information has been disclosed in note (17) to the accompanying interim condensed consolidated financial statements. As part of our review, we compared the information in note (17) to the relevant analysis prepared by the Bank for submission to SAMA and found no material inconsistencies.

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4 Dul'qa'dah 1439H
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INTERIM CONDENSED CONSOLIDATED STATEMENT OF FINANCIAL POSITION

		30 June 2018 (Unaudited) SAR'000	31 December 2017 (Audited) SAR'000	30 June 2017 (Unaudited) SAR'000
	Notes			
ASSETS				
Cash and balances with SAMA		14,163,711	18,504,255	18,566,567
Due from banks and other financial institutions		5,208,754	9,372,200	12,442,842
Positive fair value of derivatives	6	239,314	115,890	115,746
Investments, net	7	47,747,599	46,369,903	43,082,109
Loans and advances, net	8	144,311,749	138,837,618	141,180,705
Investment in associates		591,104	564,769	555,236
Other real estate		229,119	235,119	235,057
Property and equipment, net		1,728,862	1,752,408	1,822,041
Other assets		1,256,066	530,009	989,877
Total assets		215,476,278	216,282,171	218,990,180
LIABILITIES AND SHAREHOLDERS' EQUITY				
Liabilities				
Due to banks and other financial institutions		7,471,312	7,056,168	8,449,216
Negative fair value of derivatives	6	269,938	77,923	106,641
Customer deposits	9	153,418,142	154,365,549	156,979,505
Debt securities in issue		8,019,790	8,016,639	8,015,778
Other liabilities		9,362,150	8,142,899	8,811,703
Total liabilities		178,541,332	177,659,178	182,362,843
Shareholders' equity				
Share capital		30,000,000	30,000,000	30,000,000
Statutory reserve		3,922,592	3,922,592	2,936,093
Other reserves		387,988	686,865	681,930
Retained earnings		2,624,366	2,873,536	3,009,314
Proposed dividends		-	1,140,000	-
Total shareholders' equity		36,934,946	38,622,993	36,627,337
Total liabilities and shareholders' equity		215,476,278	216,282,171	218,990,180

The accompanying notes 1 to 18 form an integral part of these interim condensed consolidated financial statements.

INTERIM CONDENSED CONSOLIDATED STATEMENT OF INCOME (Unaudited)

	For the three month period ended 30 June		For the six month period ended 30 June	
	2018 SAR'000	2017 SAR'000	2018 SAR'000	2017 SAR'000
Special commission income	2,022,278	1,821,314	3,890,606	3,658,963
Special commission expense	392,832	348,101	739,817	760,438
Net special commission income	1,629,446	1,473,213	3,150,789	2,898,525
Fee and commission income, net	397,635	348,094	822,487	749,162
Exchange income, net	65,086	70,674	133,720	143,040
Trading income, net	10,500	3,597	42,344	3,440
Dividend income	20,683	17,624	27,253	23,219
Gains on non-trading investments, net	38,724	67,898	107,435	160,483
Other operating income	11,455	2,814	19,047	13,331
Total operating income, net	2,173,529	1,983,914	4,303,075	3,991,200
Salaries and employee-related expenses	444,649	400,481	859,482	798,215
Rent and premises-related expenses	80,905	82,726	163,759	162,876
Depreciation of property and equipment	74,323	67,900	145,590	139,929
Other general and administrative expenses	225,820	212,576	452,899	396,037
Impairment charge for credit losses and other provisions, net (note 8.3)	317,968	371,453	477,652	588,566
Impairment (reversal)/ charge for investments, net	(26,941)	-	18,161	-
Other operating expenses	7,628	6,738	13,702	17,747
Total operating expenses, net	1,124,352	1,141,874	2,131,245	2,103,370
Net operating income	1,049,177	842,040	2,171,830	1,887,830
Share in earnings of associates, net	13,310	5,880	27,490	7,445
Net income for the period	1,062,487	847,920	2,199,320	1,895,275
Basic and diluted earnings per share (in SAR)	0.35	0.28	0.73	0.63

The accompanying notes 1 to 18 form an integral part of these interim condensed consolidated financial statements.

INTERIM CONDENSED CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME (Unaudited)

	For the three month period ended 30 June		For the six month period ended 30 June	
	2018 SAR'000	2017 SAR'000	2018 SAR'000	2017 SAR'000
Net income for the period	1,062,487	847,920	2,199,320	1,895,275
Other comprehensive income:				
Items that will be reclassified to consolidated statement of income in subsequent periods				
- Fair value through other comprehensive income (FVOCI- debt instruments)				
- Net change in fair value	(116,190)	-	(351,566)	-
- Net amounts transferred to interim condensed consolidated statement of income	(25,010)	-	(98,887)	-
- Net changes in allowance for expected credit losses of debt instruments	(26,178)	-	16,688	-
- Available for sale investments				
Net change in fair value	-	150,528	-	300,043
Net amounts transferred to interim condensed consolidated statement of income	-	(62,386)	-	(151,042)
- Gain on sale of investments	-	(62,386)	-	(151,042)
Items that cannot be reclassified back to consolidated statement of income in subsequent periods	-	-	-	-
- Net change on equity instruments at fair value through other comprehensive income (FVOCI- equity instruments)	90,836	-	251,366	-
Other comprehensive income for the period	(76,542)	88,142	(182,399)	149,001
Total comprehensive income for the period	985,945	936,062	2,016,921	2,044,276

The accompanying notes 1 to 18 form an integral part of these interim condensed consolidated financial statements.

INTERIM CONDENSED CONSOLIDATED STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY (Unaudited)

For the six month period ended 30 June 2018 and 2017

<u>SAR'000</u>	Share capital	Statutory reserve	Other reserves	Retained earnings	Proposed dividends	Total
30 June 2018						
Balance at the beginning of the period	30,000,000	3,922,592	686,865	2,873,536	1,140,000	38,622,993
Impact of adopting IFRS 9 at 1 January 2018 (Note 4)	-	-	(116,478)	(2,008,490)	-	(2,124,968)
Restated balance at the beginning of the period	30,000,000	3,922,592	570,387	865,046	1,140,000	36,498,025
Total comprehensive income						
Net changes in fair values of						
- FVOCI equity instruments	-	-	251,366	-	-	251,366
- FVOCI debt instruments	-	-	(351,566)	-	-	(351,566)
Net amount reclassified to the interim condensed consolidated statement of income for debt instruments at FVOCI	-	-	(98,887)	-	-	(98,887)
Net changes in allowance for expected credit losses of debt instruments at FVOCI	-	-	16,688	-	-	16,688
Net income for the period	-	-	-	2,199,320	-	2,199,320
Total comprehensive income	-	-	(182,399)	2,199,320	-	2,016,921
Final dividends - 2017 (note 15)	-	-	-	-	(1,140,000)	(1,140,000)
Provision for zakat	-	-	-	(440,000)	-	(440,000)
Balance at the end of the period	<u>30,000,000</u>	<u>3,922,592</u>	<u>387,988</u>	<u>2,624,366</u>	<u>-</u>	<u>36,934,946</u>
30 June 2017						
Balance at the beginning of the period	30,000,000	2,936,093	532,929	2,604,039	900,000	36,973,061
Total comprehensive income						
Net change in fair value of available for sale investments	-	-	300,043	-	-	300,043
Net amounts relating to available for sale investments transferred to interim condensed consolidated statement of income	-	-	(151,042)	-	-	(151,042)
Net income for the period	-	-	-	1,895,275	-	1,895,275
Total comprehensive income	-	-	149,001	1,895,275	-	2,044,276
Final dividends - 2016	-	-	-	-	(900,000)	(900,000)
Interim dividend - 2017	-	-	-	(1,050,000)	-	(1,050,000)
Provision for zakat	-	-	-	(440,000)	-	(440,000)
Balance at the end of the period	<u>30,000,000</u>	<u>2,936,093</u>	<u>681,930</u>	<u>3,009,314</u>	<u>-</u>	<u>36,627,337</u>

The accompanying notes 1 to 18 form an integral part of these interim condensed consolidated financial statements.

INTERIM CONDENSED CONSOLIDATED STATEMENT OF CASH FLOWS (Unaudited)

	For the six month period ended 30 June	
	2018 SAR'000	2017 SAR'000
OPERATING ACTIVITIES		
Net income for the period	2,199,320	1,895,275
Adjustments to reconcile net income for the period to net cash used in operating activities:		
Accretion of discounts and amortisation of premium, net on non-FVIS instruments, net	(25,524)	(25,322)
Gains on non-trading investments, net	(107,435)	(160,483)
Gains on trading investments, net	(2,598)	(1,583)
Depreciation of property and equipment	145,590	139,929
Share in earnings of associates, net	(27,490)	(7,445)
Impairment charge for investments, net	18,161	-
Impairment charge for credit losses and other provisions, net	477,652	588,566
	<u>2,677,676</u>	<u>2,428,937</u>
Net (increase) decrease in operating assets:		
Statutory deposit with SAMA	(26,994)	90,137
Due from banks and other financial institutions maturing after three months from date of acquisition	1,663,459	(667,727)
Positive fair value of derivatives	(123,424)	73,549
Fair value through income statement (FVIS)	353,523	(300,000)
Loans and advances, net	(7,425,449)	1,140,096
Other real estate	6,000	9,960
Other assets	(726,057)	(112,211)
Net increase (decrease) in operating liabilities:		
Due to banks and other financial institutions	415,144	(387,497)
Negative fair value of derivatives	192,015	(31,997)
Customer deposits	(947,407)	296,368
Other liabilities	233,162	380,677
	<u>233,162</u>	<u>380,677</u>
Net cash (used in) from operating activities	<u>(3,708,352)</u>	<u>2,920,292</u>
INVESTING ACTIVITIES		
Proceeds from sales and maturities of investments not held as FVIS instruments	12,003,692	12,617,455
Purchase of investments not held as FVIS instruments	(13,827,215)	(9,907,586)
Purchase of property and equipment, net	(122,044)	(99,621)
	<u>(1,945,567)</u>	<u>2,610,248</u>
FINANCING ACTIVITIES		
Dividend and zakat paid	(1,205,713)	(928,053)
Cash used in financing activities	<u>(1,205,713)</u>	<u>(928,053)</u>
Net (decrease) increase in cash and cash equivalents	<u>(6,859,632)</u>	<u>4,602,487</u>
Cash and cash equivalents at beginning of the period	16,151,643	16,082,760
Cash and cash equivalents at end of the period	<u>11</u> <u>9,292,011</u>	<u>20,685,247</u>
Special commission received during the period	3,751,094	3,566,571
Special commission paid during the period	873,130	929,966
Supplemental non-cash information		
Net changes in fair value and transfers to interim condensed consolidated statement of income	<u>(182,399)</u>	<u>149,001</u>

The accompanying notes 1 to 18 form an integral part of these interim condensed consolidated financial statements.

NOTES TO THE INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)**For the six months period ended 30 June 2018 and 2017****1. GENERAL**

Riyad Bank (the "Bank") is a Saudi Joint Stock Company incorporated in the Kingdom of Saudi Arabia, formed pursuant to the Royal Decree and the Council of Ministers' Resolution No. 91 dated 1 Jumad Al-Awal 1377H (corresponding to 23 November 1957G). The Bank operates under commercial registration No. 1010001054 dated 25 Rabi Al-Thani 1377H (corresponding to 18 November 1957G) through its 340 branches (30 June 2017: 340) in the Kingdom of Saudi Arabia, a branch in London, United Kingdom, an agency in Houston, United States, and a representative office in Singapore. The registered address of the Bank's Head Office is as follows:

Riyad Bank
King Abdulaziz Road – Al-Murabba District
P.O. Box 22622
Riyadh 11416
Kingdom of Saudi Arabia

The objective of the Bank is to provide a full range of banking services. The Bank also provides to its customers Islamic (non-interest based) banking products which are approved and supervised by an independent Shariah Board established by the Bank.

The interim condensed consolidated financial statements comprise the financial statements of Riyad Bank and its wholly owned subsidiaries, a) Riyad Capital (engaged in investment services and asset management activities related to dealing, managing, arranging, advising and custody of securities regulated by the Capital Market Authority), b) Ithra Al-Riyad Real Estate Company (formed with the objective to hold, manage, sell and purchase real estate assets for owners or third parties for financing activities); c) Riyad Company for Insurance Agency (which acts as an agent for selling insurance products owned and managed by another principal insurance company), incorporated in the Kingdom of Saudi Arabia; d) Curzon Street Properties Limited incorporated in the Isle of Man; and e) Riyad Financial Markets incorporated in the Cayman Islands - a netting and bankruptcy jurisdiction country, to execute derivative transactions with international counterparties on behalf of Riyad Bank. These entities are collectively referred to as "the Group".

2. BASIS OF PREPARATION

The interim condensed consolidated financial statements for the six months ended 30 June 2018 have been prepared in accordance with IAS 34 Interim Financial Reporting as modified by Saudi Arabian Monetary Authority ("SAMA") for the accounting of zakat and income tax. The interim condensed consolidated financial statements do not include all the information and disclosures required in the annual financial statements, and should be read in conjunction with the Group's annual consolidated financial statements as at 31 December 2017. The Group has adopted IFRS 9 Financial Instruments and IFRS 15 Revenue from Contracts with Customers from 1 January 2018 and accounting policies for these new standards are disclosed in note 5 Significant Accounting Policies. The impact of changes in accounting policies due to adoption of these Standards are discussed in note 4. Significant judgments and estimates relating to impairment are disclosed in note 14- Financial Risk Management note considering IFRS 9 first time adoption.

NOTES TO THE INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)**For the six months period ended 30 June 2018 and 2017****3. BASIS OF CONSOLIDATION**

The interim condensed consolidated financial statements include the financial statements of the subsidiaries which are prepared for the same reporting period as that of the Bank, using consistent accounting policies.

Subsidiaries are investees controlled by the Group. The Group controls an investee when it is exposed to, or has rights to, variable returns from its involvement with the investee and has ability to affect those returns through its power over the investee.

The financial statements of the subsidiaries are included in the interim condensed consolidated financial statements from the date that control commences until the date that control ceases.

Balances between the Bank and its subsidiaries, and any unrealised income and expenses arising from intra-group transactions, are eliminated in preparing the interim condensed consolidated financial statements. Unrealised losses are eliminated in the same way as unrealised gains, but only to the extent that there is no evidence of impairment.

The Group acts as a Fund Manager to a number of investment funds. Determining whether the Group controls such an investment fund usually focuses on the assessment of the aggregate economic interests of the Group in the Fund (comprising any carried interests and expected management fees) and the investors' rights to remove the Fund Manager. As a result the Group has concluded that it acts as an agent for the investors in all cases, and therefore has not consolidated these funds.

4. IMPACT OF CHANGES IN ACCOUNTING POLICIES DUE TO ADOPTION OF NEW STANDARDS

Effective 1 January 2018 the Group has adopted two new accounting standards, the impact of the adoption of these standards is explained below:

4.1 IFRS 15 Revenue from Contracts with Customers

The Group adopted IFRS 15 'Revenue from Contracts with Customers' resulting in a change in the revenue recognition policy of the Group in relation to its contracts with customers.

IFRS 15 was issued in May 2014 and is effective for annual periods commencing on or after 1 January 2018. IFRS 15 outlines a single comprehensive model of accounting for revenue arising from contracts with customers and supersedes current revenue guidance, which is found currently across several Standards and Interpretations within IFRS. It established a new five-step model that will apply to revenue arising from contracts with customers. Under IFRS 15, revenue is recognised at an amount that reflects the consideration to which an entity expects to be entitled in exchange for transferring services to a customer.

The Group has opted for the modified retrospective application permitted by IFRS 15 upon adoption of the new standard. Modified retrospective application also requires the recognition of the cumulative impact of adoption of IFRS 15 on all contracts as at 1 January 2018 in equity. The adoption of IFRS 15 did not result in material impact in interim condensed consolidated financial statements.

4.2 IFRS 9 – Financial Instruments

The Group has adopted IFRS 9 - Financial Instruments issued in July 2014 with a date of initial application of 1 January 2018. The requirements of IFRS 9 represent a significant change from IAS 39 Financial Instruments: Recognition and Measurement. The new standard brings fundamental changes to the accounting for financial assets and to certain aspects of the accounting for financial liabilities. As permitted by IFRS 9, the Group has elected to continue to apply the hedge accounting requirements of IAS 39.

NOTES TO THE INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

For the six months period ended 30 June 2018 and 2017

4. IMPACT OF CHANGES IN ACCOUNTING POLICIES DUE TO ADOPTION OF NEW STANDARDS (continued)

4.2 IFRS 9 – Financial Instruments(continued)

The key changes to the Group's accounting policies resulting from its adoption of IFRS 9 are summarized below.

Classification of financial assets and financial liabilities

IFRS 9 contains three principal classification categories for financial assets: measured at amortized cost ("AC"), fair value through other comprehensive income ("FVOCI") and Fair value through income statement ("FVIS"). This classification is generally based, except equity instruments and derivatives, on the business model in which a financial asset is managed and its contractual cash flows. The standard eliminates the existing IAS 39 categories of held-to-maturity, loans and receivables and available-for-sale. Under IFRS 9, derivatives embedded in contracts where the host is a financial asset in the scope of the standard are never bifurcated. Instead, the whole hybrid instrument is assessed for classification. For an explanation of how the Group classifies financial assets under IFRS 9, see respective section of significant accounting policies.

IFRS 9 largely retains the existing requirements in IAS 39 for the classification of financial liabilities. However, although under IAS 39 all fair value changes of liabilities designated under the fair value option were recognized in income statement, under IFRS 9 fair value changes are presented as follows:

- The amount of change in the fair value that is attributable to changes in the credit risk of the issuer is presented in OCI; and
- The remaining amount of change in the fair value is presented in statement of income.

For an explanation of how the Group classifies financial liabilities under IFRS 9, see respective section of significant accounting policies.

Impairment of financial assets

IFRS 9 replaces the 'incurred loss' model in IAS 39 with an 'expected credit loss' model ("ECL"). IFRS 9 requires the Group to record an allowance for ECLs for all loans and other debt financial assets not held at FVIS, together with loan commitments and financial guarantee contracts. The allowance is based on the ECLs associated with the probability of default in the next twelve months unless there has been a significant increase in credit risk since origination. If the financial asset meets the definition of purchased or originated credit impaired (POCI), the allowance is based on the change in the ECLs over the life of the asset.

Under IFRS 9, credit losses are recognized earlier than under IAS 39. For an explanation of how the Group applies the impairment requirements of IFRS 9, see respective section of significant accounting policies.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS - continued

For the six months period ended 30 June 2018 and 2017

4. IMPACT OF CHANGES IN ACCOUNTING POLICIES DUE TO ADOPTION OF NEW STANDARDS (continued)

4.2 IFRS 9 – Financial Instruments(continued)

Transition

Changes in accounting policies resulting from the adoption of IFRS 9 have been applied retrospectively, except as described below.

- Comparative periods have not been restated. A difference in the carrying amounts of financial assets and financial liabilities resulting from the adoption of IFRS 9 are recognized in retained earnings and reserves as at 1 January 2018. Accordingly, the information presented for 2017 does not reflect the requirements of IFRS 9 and therefore is not comparable to the information presented for 2018 under IFRS 9.

- The following assessments have been made on the basis of the facts and circumstances that existed at the date of initial application.

- The determination of the business model within which a financial asset is held.
- The designation and revocation of previous designated financial assets and financial liabilities as measured at FVIS.
- The designation of certain investments in equity instruments not held for trading as FVOCI.

It is assumed that the credit risk has not increased significantly for those debt securities which carry low credit risk at the date of initial application of IFRS 9.

- a) The following table shows the original measurement categories in accordance with IAS 39 and the new measurement categories under IFRS 9 for the Group's financial assets and financial liabilities as at 1 January 2018.

SAR 000s	Original classification under IAS 39	New classification under IFRS 9	Original carrying value under IAS 39	New carrying value under IFRS 9
Financial assets				
Cash and balances with SAMA	Loans and receivables	Amortised Cost	18,504,255	18,501,026
Due from banks and other financial institutions	Loans and receivables	Amortised Cost	9,372,200	9,367,478
Positive fair value derivatives	FVIS	FVIS (mandatory)	115,890	115,890
Loans and advances, net	Loans and receivables	Amortised Cost	138,837,618	137,411,556
Investment securities –debt	Available for sale	FVOCI	12,224,295	12,224,295
Investment securities – debt	Available for sale	FVIS (mandatory)	884,900	884,900
Investment securities – debt	Held at amortised cost	Amortised Cost	31,436,344	31,399,298
Investment securities – equity	Available for sale	FVOCI	1,520,604	1,520,604
Investment securities – equity	Held for Trading	FVIS	303,760	303,760
Other assets – receivables	Held at amortised cost	Amortised Cost	530,009	530,009
			<u>213,729,875</u>	<u>212,258,816</u>
Financial liabilities				
Due to banks and other financial institutions	Held at amortised cost	Amortised Cost	7,056,168	7,056,168
Negative fair value derivatives	FVIS	FVIS	77,923	77,923
Customer deposits	Held at amortised cost	Amortised Cost	154,365,549	154,365,549
Debt securities in issue	Held at amortised cost	Amortised Cost	8,016,639	8,016,639
Other liabilities	Held at amortised cost	Amortised Cost	8,142,899	8,796,808
			<u>177,659,178</u>	<u>178,313,087</u>

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS - continued

For the six months period ended 30 June 2018 and 2017 (continued)

4. IMPACT OF CHANGES IN ACCOUNTING POLICIES DUE TO ADOPTION OF NEW STANDARDS (continued)

4.2 IFRS 9 – Financial Instruments(continued)

b) The following table reconciles the carrying amounts under IAS 39 to the carrying amounts under IFRS 9 on transition to IFRS 9 on 1 January 2018.

<u>SAR 000s</u>	IAS 39 carrying amount as at 31 December 2017	Reclassification	Re-measurement (ECL)	IFRS 9 carrying amount as at 1 January 2018
<u>Financial assets</u>				
<u>Amortised cost</u>				
Cash and balances with SAMA	18,504,255	-	(3,229)	18,501,026
Due from banks and other financial institutions	9,372,200	-	(4,722)	9,367,478
Loans and advances	138,837,618	-	(1,426,062)	137,411,556
Investment securities - Debt	31,436,344	-	(37,046)	31,399,298
Other assets	530,009	-	-	530,009

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS - continued

For the six months period ended 30 June 2018 and 2017

4. IMPACT OF CHANGES IN ACCOUNTING POLICIES DUE TO ADOPTION OF NEW STANDARDS (continued)

4.2 IFRS 9 – Financial Instruments(continued)

- b) The following table reconciles the carrying amounts under IAS 39 to the carrying amounts under IFRS 9 on transition to IFRS 9 on 1 January 2018.

SAR 000s	IAS 39 carrying amount as at 31 December 2017	Reclassification	Re-measurement (ECL)	IFRS 9 carrying amount as at 1 January 2018
Financial assets				
Available for sale				
31 December 2017	14,629,799	-	-	-
Transferred to:	-	-	-	-
FVOCI – equity	-	(1,520,604)	-	-
FVOCI – debt	-	(12,224,295)	-	-
FVIS	-	(884,900)	-	-
1 January 2018				-
FVOCI - equity				
31 December 2017	-	-	-	-
From available for sale	-	1,520,604	-	-
1 January 2018				1,520,604
FVOCI - debt				
31 December 2017	-	-	-	-
From available for sale	-	12,224,295	-	-
1 January 2018				12,224,295
FVIS				
Investment:				
31 December 2017	303,760	-	-	-
From available for sale	-	884,900	-	-
1 January 2018				1,188,660
Positive fair value of derivatives	115,890	-	-	-
1 January 2018				115,890
Financial liabilities				
Amortized cost				
Due to banks and other financial institutions	7,056,168	-	-	-
Customers' deposits	154,365,549	-	-	-
Debt securities in issue	8,016,639	-	-	-
Other liabilities	8,142,899	-	653,909	-
Total amortized cost				178,235,164
FVIS				
Negative fair value of derivatives	77,923	-	-	-
1 January 2018				77,923

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS - (continued)

For the six months period ended 30 June 2018 and 2017

4. IMPACT OF CHANGES IN ACCOUNTING POLICIES DUE TO ADOPTION OF NEW STANDARDS (continued)

4.2 IFRS 9 – Financial Instruments (continued)

c) There were no reclassifications of financial assets and financial liabilities into amortized cost under IFRS 9

d) Impact on retained earnings and other reserves

The following table shows the effects of the reclassification of financial assets and financial liabilities from IAS 39 categories under IFRS 9.

	Retained earnings	Other reserves
Closing balance under IAS 39 (31 December 2017)	2,873,536	686,865
Reclassifications under IFRS 9*	171,761	(171,761)
Recognition of expected credit losses under IFRS 9	(2,180,251)	55,283
Opening balance under IFRS 9 (1 January 2018)	<u>865,046</u>	<u>570,387</u>

* This comprise of reclassification of AFS instruments to FVIS

e) The following table reconciles the opening impairment recorded as per the requirements of IAS 39 to that of IFRS 9:

The closing impairment allowance for financial assets in accordance with IAS 39 and provisions for loan commitments and financial guarantee contracts in accordance with IAS 37 Provisions, Contingent Liabilities and Contingent Assets as at 31 December 2017 to the opening ECL allowance determined in accordance with IFRS 9 as at 1 January 2018.

	31 December 2017 (IAS 39 / IAS 37)	Re classification	Re measurement	1 January 2018 (IFRS 9)
Loans and receivables (IAS 39)/Financial assets at amortised cost (IFRS-9)				
Cash and balances with SAMA	-	-	3,229	3,229
Due from banks and other financial institutions	-	-	4,722	4,722
Investments, net	-	-	37,046	37,046
Loans and advances, net	2,084,926	-	1,426,062	3,510,988
Total	<u>2,084,926</u>	<u>-</u>	<u>1,471,059</u>	<u>3,555,985</u>
Investment, net - FVOCI - Debt (IFRS-9)	-	-	55,283	55,283
Loan commitments and financial guarantee contracts	-	-	653,909	653,909
Total	<u>-</u>	<u>-</u>	<u>709,192</u>	<u>709,192</u>

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS - continued

For the six months period ended 30 June 2018 and 2017

4. IMPACT OF CHANGES IN ACCOUNTING POLICIES DUE TO ADOPTION OF NEW STANDARDS (continued)

4.2 IFRS 9 – Financial Instruments (continued)

f) The following table provides carrying value of financial assets and financial liabilities in the statement of financial position as of 30 June 2018

	Mandatorily at FVIS	FVOCI – debt instruments	FVOCI – equity	Amortized cost	Total carrying amount
Financial assets					
Cash and balances with SAMA	-	-	-	14,163,711	14,163,711
Due from banks and other financial institutions	-	-	-	5,208,754	5,208,754
Positive fair value of derivatives	239,314	-	-	-	239,314
Investments, net	899,007	10,927,871	1,824,568	34,096,153	47,747,599
Loans and advances, net	-	-	-	144,311,749	144,311,749
Other assets	-	-	-	1,256,066	1,256,066
Total financial assets	1,138,321	10,927,871	1,824,568	199,036,433	212,927,193
Financial liabilities					
Due to banks and other financial institutions	-	-	-	7,471,312	7,471,312
Negative fair value of derivatives	269,938	-	-	-	269,938
Customer deposits	-	-	-	153,418,142	153,418,142
Debt securities in issue	-	-	-	8,019,790	8,019,790
Other liabilities	-	-	-	9,362,150	9,362,150
Total financial liabilities	269,938	-	-	178,271,394	178,541,332

The following table provides carrying value of financial assets and financial liabilities in the statement of financial position as of 31 December 2017

	Trading	Loans and receivables	Available for sale	Other amortized cost	Total carrying amount
Financial assets					
Cash and balances with SAMA	-	-	-	18,504,255	18,504,255
Due from banks and other financial institutions	-	-	-	9,372,200	9,372,200
Positive fair value of derivatives	115,890	-	-	-	115,890
Investments, net	303,760	-	14,629,799	31,436,344	46,369,903
Loans and advances, net	-	138,837,618	-	-	138,837,618
Other assets	-	-	-	530,009	530,009
Total financial assets	419,650	138,837,618	14,629,799	59,842,808	213,729,875
Financial liabilities					
Due to banks and other financial institutions	-	-	-	7,056,168	7,056,168
Negative fair value of derivatives	77,923	-	-	-	77,923
Customers' deposits	-	-	-	154,365,549	154,365,549
Debt securities in issue	-	-	-	8,016,639	8,016,639
Other liabilities	-	-	-	8,142,899	8,142,899
Total financial liabilities	77,923	-	-	177,581,255	177,659,178

NOTES TO THE INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)**For the six months period ended 30 June 2018 and 2017****5. SIGNIFICANT ACCOUNTING POLICIES**

The accounting policies, estimates and assumptions used in the preparation of these interim condensed consolidated financial statements are consistent with those used in the preparation of the annual consolidated financial statements for the year ended December 31, 2017 except for the policies explained below. Based on the adoption of new standards explained in note 4, the following accounting policies are applicable effective 1 January 2018 replacing / amending or adding to the corresponding accounting policies set out in 2017 financial statements.

5.1 Classification of financial assets

On initial recognition, the Group classifies all of its financial assets based on the business model for managing the assets and the asset's contractual terms, measured at either:

a) Financial Asset at amortised cost (AC)

A financial asset is measured at amortized cost if it meets both of the following conditions and is not designated as at FVIS:

- the asset is held within a business model whose objective is to hold assets to collect contractual cash flows; and
- the contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding (SPPI test).

b) Financial Asset at FVOCI

A debt instrument is measured at FVOCI only if it meets both of the following conditions and is not designated as at FVIS:

- the asset is held within a business model whose objective is achieved by both collecting contractual cash flows and selling financial assets; and
- the contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

FVOCI debt instruments are subsequently measured at fair value with gains and losses arising due to changes in fair value recognised in OCI. Interest income and foreign exchange gains and losses are recognised in profit or loss.

Equity Instruments: On initial recognition, for an equity investment that is not held for trading, the Group may irrevocably elect to present subsequent changes in fair value in OCI. This election is made on an investment-by-investment basis. Equity instruments at FVOCI are not subject to an impairment assessment.

c) Financial Asset at FVIS

Financial assets at FVIS comprise derivative instruments, quoted equity instruments held for trading and debt securities not classified neither as AC or FVOCI. In addition, on initial recognition, the Group may irrevocably designate a financial asset as FVIS, that otherwise meets the requirements to be measured at amortized cost or at FVOCI, if doing so eliminates or significantly reduces an accounting mismatch that would otherwise arise.

Financial assets are not reclassified subsequent to their initial recognition, except in the period after the Group changes its business model for managing financial assets.

NOTES TO THE INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

For the six months period ended 30 June 2018 and 2017

5. SIGNIFICANT ACCOUNTING POLICIES (continued)

5.1 Classification of financial assets (continued)

The details of business model assessment and SPPI test are explained below.

Business model assessment

The Group assesses the objective of a business model in which an asset is held at a portfolio level because this best reflects the way the business is managed and information is provided to management. The information considered includes:

- the stated policies and objectives for the portfolio and the operation of those policies in practice. In particular, whether management's strategy focuses on earning contractual interest revenue, maintaining a particular interest rate profile, matching the duration of the financial assets to the duration of the liabilities that are funding those assets or realizing cash flows through the sale of the assets;
 - how the performance of the portfolio is evaluated and reported to the Group's management;
 - the risks that affect the performance of the business model (and the financial assets held within that business model) and how those risks are managed;
 - how managers of the business are compensated- e.g. whether compensation is based on the fair value of the assets managed or the contractual cash flows collected; and
 - the frequency, volume and timing of sales in prior periods, the reasons for such sales and its expectations about future sales activity.
- However, information about sales activity is not considered in isolation, but as part of an overall assessment of how the Group's stated objective for managing the financial assets is achieved and how cash flows are realized.

The business model assessment is based on reasonably expected scenarios without taking 'worst case' or 'stress case' scenarios into account. If cash flows after initial recognition are realised in a way that is different from the Group's original expectations, the Group does not change the classification of the remaining financial assets held in that business model, but incorporates such information when assessing newly originated or newly purchased financial assets going forward.

Financial assets that are held for trading and whose performance is evaluated on a fair value basis are measured at FVIS because they are neither held to collect contractual cash flows nor held both to collect contractual cash flows and to sell financial assets.

Assessments whether contractual cash flows are solely payments of principal and interest ("SPPI")

As a second step of its classification process the Group assesses the contractual terms of financial to identify whether they meet the SPPI test.

For the purposes of this assessment, 'principal' is the fair value of the financial asset on initial recognition. 'Interest' is the consideration for the time value of money, the credit and other basic lending risks associated with the principal amount outstanding during a particular period and other basic lending costs (e.g. liquidity risk and administrative costs), along with profit margin.

In assessing whether the contractual cash flows are solely payments of principal and interest, the Group considers the contractual terms of the instrument. This includes assessing whether the financial asset contains a contractual term that could change the timing or amount of contractual cash flows such that it would not meet this condition. In making the assessment, the Group considers:

- contingent events that would change the amount and timing of cash flows;
- leverage features;
- prepayment and extension terms;
- terms that limit the Group's claim to cash flows from specified assets (e.g. non-recourse asset arrangements); and
- features that modify consideration of the time value of money- e.g. periodical reset of interest rates.

Designation at Fair value through income statement

At initial recognition, the Group has designated certain financial assets at FVIS. Before 1 January 2018, the Group also designated certain financial assets as at FVIS because the assets were managed, evaluated and reported internally on a fair value basis.

NOTES TO THE INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

For the six months period ended 30 June 2018 and 2017

5. SIGNIFICANT ACCOUNTING POLICIES (continued)

5.2 Classification of financial liabilities

The Group classifies its financial liabilities, other than financial guarantees and loan commitments, as measured at amortized cost. Amortized cost is calculated by taking into account any discount or premium on issue, and costs that are an integral part of the EIR.

5.3 Derecognition

a- Financial assets

The Group derecognizes a financial asset when the contractual rights to the cash flows from the financial asset expire, or it transfers the rights to receive the contractual cash flows in a transaction in which substantially all of the risks and rewards of ownership of the financial asset are transferred or in which the Group neither transfers nor retains substantially all of the risks and rewards of ownership and it does not retain control of the financial asset.

On derecognition of a financial asset, the difference between the carrying amount of the asset (or the carrying amount allocated to the portion of the asset derecognized) and the sum of (i) the consideration received (including any new asset obtained less any new liability assumed) and (ii) any cumulative gain or loss that had been recognized in OCI is recognized in profit or loss.

From 1 January 2018, any cumulative gain/loss recognized in OCI in respect of equity investment securities designated as at FVOCI is not recognized in profit or loss on derecognition of such securities. Any interest in transferred financial assets that qualify for derecognition that is created or retained by the Group is recognized as a separate asset or liability.

When assets are sold to a third party with a concurrent total rate of return swap on the transferred assets, the transaction is accounted for as a secured financing transaction similar to sale-and-repurchase transactions, as the Group retains all or substantially all of the risks and rewards of ownership of such assets.

NOTES TO THE INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

For the six months period ended 30 June 2018 and 2017

5. SIGNIFICANT ACCOUNTING POLICIES (continued)

5.3 Derecognition (continued)

In transactions in which the Group neither retains nor transfers substantially all of the risks and rewards of ownership of a financial asset and it retains control over the asset, the Group continues to recognize the asset to the extent of its continuing involvement, determined by the extent to which it is exposed to changes in the value of the transferred asset.

In certain transactions, the Group retains the obligation to service the transferred financial asset for a fee. The transferred asset is derecognized if it meets the derecognition criteria. An asset or liability is recognized for the servicing contract if the servicing fee is more than adequate (asset) or is less than adequate (liability) for performing the servicing.

Before 1 January 2018, retained interests were primarily classified as available-for-sale investment securities and measured at fair value.

5.4 Modifications of financial assets and financial liabilities

a) Financial assets

If the terms of a financial asset are modified, the Group evaluates whether the cash flows of the modified asset are substantially different. If the cash flows are substantially different, then the contractual rights to cash flows from the original financial asset are deemed to have expired. In this case, the original financial asset is derecognized with the difference recognized as a de-recognition gain or loss and a new financial asset is recognized at fair value.

If the cash flows of the modified asset carried at amortized cost are not substantially different, then the modification does not result in derecognition of the financial asset. In this case, the Group recalculates the gross carrying amount of the financial asset and recognizes the amount arising from adjusting the gross carrying amount as a modification gain or loss in profit or loss. If such a modification is carried out because of financial difficulties of the borrower, then the gain or loss is presented together with impairment losses. In other cases, it is presented as interest income.

b) Financial liabilities

The Group derecognizes a financial liability when its terms are modified and the cash flows of the modified liability are substantially different. In this case, a new financial liability based on the modified terms is recognized at fair value. The difference between the carrying amount of the financial liability extinguished and the new financial liability with modified terms is recognized in profit or loss.

5.5 Impairment

The Group recognizes loss allowances for ECL on the following financial instruments that are not measured at FVIS:

- financial assets that are debt instruments;
- lease receivables;
- financial guarantee contracts issued; and
- loan commitments issued.

No impairment loss is recognized on equity investments.

The Group measures loss allowances at an amount equal to lifetime ECL, except for the following, for which they are measured as 12-month ECL:

- debt investment securities that are determined to have low credit risk at the reporting date; and
- other financial instruments on which credit risk has not increased significantly since their initial recognition.

NOTES TO THE INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)**For the six months period ended 30 June 2018 and 2017****5. SIGNIFICANT ACCOUNTING POLICIES (continued)****5.5 Impairment (continued)**

The Group considers a debt security to have low credit risk when their credit risk rating is equivalent to the globally understood definition of 'investment grade'.

12-month ECL are the portion of ECL that result from default events on a financial instrument that are possible within the 12 months after the reporting date.

Measurement of ECL

ECL is a probability-weighted estimate of credit losses. They are measured as follows:

- financial assets that are not credit-impaired at the reporting date: as the present value of all cash shortfalls (i.e. the difference between the cash flows due to the entity in accordance with the contract and the cash flows that the Group expects to receive);
- financial assets that are credit-impaired at the reporting date: as the difference between the gross carrying amount and the present value of estimated future cash flows;
- undrawn loan commitments: as the present value of the difference between the contractual cash flows that are due to the Group if the commitment is drawn down and the cash flows that the Group expects to receive; and
- financial guarantee contracts: the expected payments to reimburse the holder less any amounts that the Group expects to recover.

Restructured financial assets

If the terms of a financial asset are renegotiated or modified or an existing financial asset is replaced with a new one due to financial difficulties of the borrower, then an assessment is made of whether the financial asset should be derecognized and ECL are measured as follows:

If the expected restructuring will not result in derecognition of the existing asset, and then the expected cash flows arising from the modified financial asset are included in calculating the cash shortfalls from the existing asset.

If the expected restructuring will result in derecognition of the existing asset, then the expected fair value of the new asset is treated as the final cash flow from the existing financial asset at the time of its derecognition. This amount is included in calculating the cash shortfalls from the existing financial asset that are discounted from the expected date of derecognition to the reporting date using the original effective interest rate of the existing financial asset.

Credit-impaired financial assets

At each reporting date, the Group assesses whether financial assets carried at amortized cost are credit-impaired. A financial asset is 'credit-impaired' when one or more events that have detrimental impact on the estimated future cash flows of the financial asset have occurred.

Evidence that a financial asset is credit-impaired includes the following observable data:

- significant financial difficulty of the borrower or issuer;
- a breach of contract such as a default or past due event;
- the restructuring of a loan or advance by the Group on terms that the Group would not consider otherwise ;
- it is becoming probable that the borrower will enter Groupruptcy or other financial reorganization; or
- the disappearance of an active market for a security because of financial difficulties.

A loan that has been renegotiated due to deterioration in the borrower's condition is usually considered to be credit-impaired unless there is evidence that the risk of not receiving contractual cash flows has reduced significantly and there are no other indicators of impairment. In addition, a retail loan that is overdue for 90 days or more is considered impaired.

NOTES TO THE INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

For the six months period ended 30 June 2018 and 2017

5. SIGNIFICANT ACCOUNTING POLICIES (continued)

5.5 Impairment (continued)

In making an assessment of whether an investment in sovereign debt is credit-impaired, the Group considers the following factors.

- The market's assessment of creditworthiness as reflected in the bond yields.
- The rating agencies' assessments of creditworthiness.
- The country's ability to access the capital markets for new debt issuance.
- The probability of debt being restructured, resulting in holders suffering losses through voluntary or mandatory debt forgiveness.
- The international support mechanisms in place to provide the necessary support as 'lender of last resort' to that country, as well as the intention, reflected in public statements, of governments and agencies to use those mechanisms. This includes an assessment of the depth of those mechanisms and, irrespective of the political intent, whether there is the capacity to fulfil the required criteria.

Presentation of allowance for ECL in the statement of financial position

Loss allowances for ECL are presented in the statement of financial position as follows:

- financial assets measured at amortized cost: as a deduction from the gross carrying amount of the assets;
- loan commitments and financial guarantee contracts: generally, as a provision;
- where a financial instrument includes both a drawn and an undrawn component, and the Group cannot identify the ECL on the loan commitment component separately from those on the drawn component: the Group presents a combined loss allowance for both components. The combined amount is presented as a deduction from the gross carrying amount of the drawn component. Any excess of the loss allowance over the gross amount of the drawn component is presented as a provision; and
- debt instruments measured at FVOCI: no loss allowance is recognized in the consolidated statement of financial position because the carrying amount of these assets is their fair value. However, the loss allowance is disclosed and is recognized in the fair value reserve. Impairment losses are recognised in profit and loss and changes between the amortised cost of the assets and their fair value are recognised in OCI.

Write-off

Loans and debt securities are written off (either partially or in full) when there is no realistic prospect of recovery. However, financial assets that are written off could still be subject to enforcement activities in order to comply with the Group's procedures for recovery of amounts due. If the amount to be written off is greater than the accumulated loss allowance, the difference is first treated as an addition to the allowance that is then applied against the gross carrying amount. Any subsequent recoveries are credited to credit loss expense.

Collateral valuation

To mitigate its credit risks on financial assets, the Group seeks to use collateral, where possible. The collateral comes in various forms, such as cash, securities, letters of credit/guarantees, real estate, receivables, inventories, other non-financial assets and credit enhancements such as netting agreements. The Group's accounting policy for collateral assigned to it through its lending arrangements under IFRS 9 is the same as it was under IAS 39. Collateral, unless repossessed, is not recorded on the Group's consolidated statement of financial position. However, the fair value of collateral affects the calculation of ECLs. It is generally assessed, at a minimum, at inception and re-assessed on a periodic basis. However, some collateral, for example, cash or securities relating to margining requirements, is valued daily.

To the extent possible, the Group uses active market data for valuing financial assets held as collateral. Other financial assets which do not have readily determinable market values are valued using models. Non-financial collateral, such as real estate, is valued based on data provided by third parties such as mortgage brokers, or based on housing price indices.

Collateral repossessed

The Group's accounting policy under IFRS 9 remains the same as it was under IAS 39. The Group's policy is to determine whether a repossessed asset can be best used for its internal operations or should be sold. Assets determined to be useful for the internal operations are transferred to their relevant asset category at the lower of their repossessed value or the carrying value of the original secured asset. Assets for which selling is determined to be a better option are transferred to assets held for sale at their fair value (if financial assets) and fair value less cost to sell for non-financial assets at the repossession date in, line with the Group's policy.

NOTES TO THE INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

For the six months period ended 30 June 2018 and 2017

5. SIGNIFICANT ACCOUNTING POLICIES (continued)

5.5 Impairment (continued)

Collateral repossessed (continued)

In its normal course of business, the Group does not physically repossess properties or other assets in its retail portfolio, but engages external agents to recover funds, generally at auction, to settle outstanding debt. Any surplus funds are returned to the customers/obligors. As a result of this practice, the residential properties under legal repossession processes are not recorded on the consolidated statement of financial position.

5.6 Financial guarantees and loan commitments

Financial guarantees' are contracts that require the Group to make specified payments to reimburse the holder for a loss that it incurs because a specified debtor fails to make payment when it is due in accordance with the terms of a debt instrument. 'Loan commitments' are firm commitments to provide credit under pre-specified terms and conditions.

Financial guarantees issued or commitments to provide a loan at a below-market interest rate are initially measured at fair value and the initial fair value is amortized over the life of the guarantee or the commitment. Subsequently, they are measured as follows:

- from 1 January 2018: at the higher of this unamortized amount and the amount of loss allowance; and
- Before 1 January 2018: at the higher of this unamortized amount and the present value of any expected payment to settle the liability when a payment under the contract has become probable.

The Group has issued no loan commitments that are measured at FVIS. For other loan commitments:

- from 1 January 2018: the Group recognizes loss allowance based on the ECL requirement.
- before 1 January 2018: the Group recognizes a provision in accordance with IAS 37 if the contract was considered to be onerous.

5.7 Foreign currencies

The consolidated financial statements are presented in Saudi Arabian Riyals ("SAR"), which is also the Bank's functional currency. Each entity determines its own functional currency and items included in the financial statements of each entity are measured using that functional currency.

Transactions in foreign currencies are translated into SAR at exchange rates prevailing on the dates of the transactions. Monetary assets and liabilities at the year-end (other than monetary items that form part of the net investment in a foreign operation), denominated in foreign currencies, are translated into SAR at exchange rates prevailing at the reporting date.

The foreign currency gain or loss on monetary items is the difference between amortised cost in the functional currency at the beginning of the year adjusted for the effective profits rate and payments during the year and the amortized cost in foreign currency translated at exchange rate at the end of the year.

Realized and unrealized gains or losses on exchange are credited or charged to the interim condensed consolidated statement of income.

Foreign currency differences arising from the translation of the following items are recognized in OCI:

Available-for-sale equity instruments (before 1 January 2018) or equity investments in respect of which an election has been made to present subsequent changes in fair value in OCI (from 1 January 2018);

Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rates as at the dates of the initial transactions. Non-monetary items measured at fair value in a foreign currency are translated using the exchange rates at the date when the fair value is determined.

As at the reporting date, the assets and liabilities of foreign operations are translated into SAR at the rate of exchange as at the reporting date, and their statement of incomes are translated at the weighted average exchange rates for the year. Exchange differences arising on translation are recognized in other comprehensive income.

When a foreign operation is disposed of such that control, significant influence or joint control is lost, the cumulative amount in the translation reserve related to that foreign operation is reclassified to the statement of income as part of the gain or loss on disposal.

When the Group disposes of only part of its interest in a subsidiary that includes a foreign operation while retaining control, the relevant proportion of the cumulative amount is reattributed to non-controlling interests.

NOTES TO THE INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

For the six months period ended 30 June 2018 and 2017

5. SIGNIFICANT ACCOUNTING POLICIES (continued)

5.8 Revenue / expenses recognition

Special commission income and expenses

Special commission income and expense are recognized in profit or loss using the effective interest method. The 'effective interest rate' is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument to or the amortized cost of the financial instrument.

When calculating the effective interest rate for financial instruments other than credit-impaired assets, the Group estimates future cash flows considering all contractual terms of the financial instrument, but not expected credit losses. For credit-impaired financial assets, a credit-adjusted effective interest rate is calculated using estimated future cash flows including expected credit losses.

The calculation of the effective interest rate includes transaction costs and fees and points paid or received that are an integral part of the effective interest rate. Transaction costs include incremental costs that are directly attributable to the acquisition or issue of a financial asset or financial liability.

Measurement of amortized cost and special commission income

The 'amortized cost' of a financial asset or financial liability is the amount at which the financial asset or financial liability is measured on initial recognition minus the principal repayments, plus or minus the cumulative amortization using the effective interest method of any difference between that initial amount and the maturity amount and, for financial assets, adjusted for any expected credit loss allowance.

The 'gross carrying amount of a financial asset' is the amortized cost of a financial asset before adjusting for any expected credit loss allowance.

In calculating interest income and expense, the effective interest rate is applied to the gross carrying amount of the asset (when the asset is not credit-impaired) or to the amortized cost of the liability.

However, for financial assets that have become credit-impaired subsequent to initial recognition, interest income is calculated by applying the effective interest rate to the amortized cost of the financial asset. If the asset is no longer credit-impaired, then the calculation of interest income reverts to the gross basis.

For financial assets that were credit-impaired on initial recognition, interest income is calculated by applying the credit-adjusted effective interest rate to the amortized cost of the asset. The calculation of interest income does not revert to a gross basis, even if the credit risk of the asset improves.

5.9 Critical accounting judgements, estimates and assumptions

The preparation of the consolidated financial statements in conformity with IFRS as modified by SAMA for accounting of zakat and income tax requires the use of certain critical accounting judgements, estimates and assumptions that affect the reported amounts of assets and liabilities. It also requires management to exercise its judgement in the process of applying the Group's accounting policies. Such judgements, estimates, and assumptions are continually evaluated and are based on historical experience and other factors, including obtaining professional advices and expectations of future events that are believed to be reasonable under the circumstances. Revisions to accounting estimates are recognised in the period in which the estimate is revised, if the revision affects only that period, or in the period of revision and in future periods if the revision affects both current and future periods.

NOTES TO THE INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

For the six months period ended 30 June 2018 and 2017

5. SIGNIFICANT ACCOUNTING POLICIES (continued)

5.9 Critical accounting judgements, estimates and assumptions (continued)

Significant areas where management has used estimates, assumptions or exercised judgements are as follows:

- i. Impairment losses on loans and advances
- ii. Fair value measurement
- iii. Classification of investments as amortised cost, FVOCI and FVIS
- iii. Determination of control over investees
- iv. Depreciation and amortisation
- v. Defined benefit plan

6. DERIVATIVES

The table below sets out the positive and negative fair values of derivative financial instruments, together with their notional amounts. The notional amounts, which provide an indication of the volumes of the transactions outstanding at the end of the period, do not necessarily reflect the amounts of future cash flows involved. These notional amounts, therefore, are neither indicative of the Group's exposure to credit risk, which is generally limited to the positive fair value of the derivatives, nor to market risk.

	30 June 2018 (Unaudited)			31 December 2017 (Audited)			30 June 2017 (Unaudited)		
	Positive fair value SAR'000	Negative fair value SAR'000	Notional amount SAR'000	Positive fair value SAR'000	Negative fair value SAR'000	Notional amount SAR'000	Positive fair value SAR'000	Negative fair value SAR'000	Notional amount SAR'000
Held for trading:									
Special commission rate swaps	193,779	(143,315)	18,089,281	78,724	(45,809)	9,914,179	58,849	(31,897)	8,345,207
Forward foreign exchange contracts	29,279	(114,749)	20,602,953	30,538	(27,886)	19,767,301	48,040	(65,737)	31,146,595
Currency options	3,766	(3,766)	1,580,389	4,228	(4,228)	3,233,155	8,857	(8,857)	5,628,230
Held as fair value hedges:									
Special commission rate swaps	12,490	(8,108)	2,144,247	2,400	-	187,503	-	(150)	187,515
Total	239,314	(269,938)	42,416,870	115,890	(77,923)	33,102,138	115,746	(106,641)	45,307,547

7 INVESTMENTS, NET

	30 June 2018 (Unaudited) SAR'000	31 December 2017 (Audited) SAR'000	30 June 2017 (Unaudited) SAR'000
Investment at Amortized cost	34,096,153	31,436,344	27,126,955
Investments at FVOCI			
- Equity	1,824,568	-	-
- Debt	10,927,871	-	-
Investments at FVOCI	12,752,439	-	-
Available for sale investments (2017)	-	14,629,799	15,653,529
Investment at FVIS	899,007	303,760	301,583
Held to maturity investments (2017)	-	-	42
Total	47,747,599	46,369,903	43,082,109

NOTES TO THE INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

For the six months period ended 30 June 2018 and 2017

8. LOANS AND ADVANCES, NET

Loans and advances held at amortised cost comprise the following:

8.1 Loans and advances held at amortised cost

These comprise the following:

30 June 2018 SAR'000	Overdraft	Credit Cards	Consumer Loans	Commercial Loans	Others	Total
Performing loans and advances-gross	6,224,566	735,017	43,063,924	95,676,107	430,392	146,130,006
Non-performing loans and advances	277,181	-	218,730	989,775	1,259	1,486,945
Total loans and advances	6,501,747	735,017	43,282,654	96,665,882	431,651	147,616,951
Allowance for impairment	(614,055)	(37,039)	(792,884)	(1,857,311)	(3,913)	(3,305,202)
Loans & advances, net	5,887,692	697,978	42,489,770	94,808,571	427,738	144,311,749

31 December 2017 SAR'000	Overdraft	Credit Cards	Consumer Loans	Commercial Loans	Others	Total
Performing loans and advances-gross	6,571,229	733,646	41,611,191	90,329,203	265,118	139,510,387
Non-performing loans and advances	418,781	-	200,318	791,799	1,259	1,412,157
Total loans and advances	6,990,010	733,646	41,811,509	91,121,002	266,377	140,922,544
Allowance for impairment	(284,471)	(16,420)	(386,892)	(1,380,709)	(16,434)	(2,084,926)
Loans & advances, net	6,705,539	717,226	41,424,617	89,740,293	249,943	138,837,618

8.2 The movement in the allowance for impairment of loans and advances to customers for the period ended 30 June 2018 and the year-ended 31 December 2017 is as follows:

	30 June 2018 (Unaudited)
SAR'000	
Closing loss allowance as at 31 December 2017 (calculated under IAS 39)	2,084,926
Amounts restated through opening retained earnings	1,426,062
Opening loss allowance as at 1 January 2018 (calculated under IFRS 9)	3,510,988
Provided during the period	561,221
Bad debts written off against provision	(767,007)
	3,305,202
	31 December 2017
Balance as at 1 Jan 2017	2,577,515
Provided during the year	2,122,460
Bad debts written off	(2,323,641)
Recoveries/ reversals of previously provided amounts	(263,822)
Other movements	(27,586)
Balance at end of the year	2,084,926

8.3 Impairment charges for credit losses and other provisions, net as reflected in the interim consolidated statement of income are detailed as follows:

	For three month period ended		For six month period ended	
	30 June 2018 SAR'000	30 June 2017 SAR'000	30 June 2018 SAR'000	30 June SAR'000
Impairment charge for credit losses, net	328,806	371,453	525,250	588,566
Impairment reversal for other financial assets	(10,838)	-	(47,598)	-
Total	317,968	371,453	477,652	588,566

NOTES TO THE INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

For the six months period ended 30 June 2018 and 2017

9. CUSTOMER DEPOSITS

Customer deposits comprise the following:

	30 June 2018 (Unaudited) SAR'000	31 December 2017 (Audited) SAR'000	30 June 2017 (Unaudited) SAR'000
Current	83,048,491	81,011,365	76,445,458
Saving	414,154	366,380	351,174
Time	56,048,375	61,430,076	68,326,437
Others	13,907,122	11,557,728	11,856,436
Total	153,418,142	154,365,549	156,979,505

10. CREDIT RELATED COMMITMENTS AND CONTINGENCIES AND OTHERS

a) The Group's credit related commitments and contingencies are as follows:

	30 June 2018 (Unaudited) SAR'000	31 December 2017 (Audited) SAR'000	30 June 2017 (Unaudited) SAR'000
Letters of credit	7,764,443	8,328,114	7,786,486
Letters of guarantee	62,005,715	64,588,190	66,111,844
Acceptances	1,514,476	2,026,574	1,928,736
Irrevocable commitments to extend credit	8,987,505	9,889,536	11,023,755
Total	80,272,139	84,832,414	86,850,821

As at 30 June 2018, ECL allowance in respect of above amounted to SAR 148 million.

b) Others

During the period ended 30 June 2018, there has been no change in the status of the Group's Zakat assessments. The Group's position with respect to stance on these assessments, has remained the same as that disclosed in the annual consolidated financial statements for the year ended 31 December 2017.

11. CASH AND CASH EQUIVALENTS

Cash and cash equivalents included in the interim condensed consolidated statement of cash flows comprise the following:

	30 June 2018 (Unaudited) SAR'000	31 December 2017 (Audited) SAR'000	30 June 2017 (Unaudited) SAR'000
Cash and balances with SAMA excluding statutory deposit	6,197,359	10,564,443	10,495,132
Due from banks and other financial institutions maturing within three months from date of acquisition	3,094,652	5,587,200	10,190,115
Total	9,292,011	16,151,643	20,685,247

NOTES TO THE INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

For the six months period ended 30 June 2018 and 2017

12. FAIR VALUES OF FINANCIAL ASSETS AND LIABILITIES

The Group uses the following hierarchy for determining and disclosing the fair value of financial instruments:

Level 1: quoted market price: financial instruments with quoted unadjusted prices for identical instruments in active markets.

Level 2: quoted prices in active markets for similar assets and liabilities or other valuation techniques for which all significant inputs are based on observable market data: and

Level 3: valuation techniques for which any significant input is not based on observable market data.

Following are the financial instruments carried at fair value in the interim condensed consolidated financial statements.

Fair value and fair value hierarchy

30 June 2018 SAR'000 (Unaudited)	Level 1	Level 2	Level 3	Total
Financial assets				
- Derivative financial instruments	-	239,314	-	239,314
- FVIS	899,007	-	-	899,007
- FVOCI	12,436,818	-	315,621	12,752,439
Financial liabilities				
- Derivative financial instruments	-	269,938	-	269,938
31 December 2017 SAR'000 (Audited)	Level 1	Level 2	Level 3	Total
Financial assets				
- Derivative financial instruments	-	115,890	-	115,890
- Held for trading investments	303,760	-	-	303,760
- Available for sale investments	14,313,044	843	315,912	14,629,799
Financial liabilities				
- Derivative financial instruments	-	77,923	-	77,923

NOTES TO THE INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

For the six months period ended 30 June 2018 and 2017

12. FAIR VALUES OF FINANCIAL ASSETS AND LIABILITIES (Continued)

	Six month period ended	
	30 June 2018 (Unaudited) SAR'000S	30 June 2017 (Unaudited) SAR'000
Reconciliation of movement in Level 3 (Unaudited)		
Opening balance	315,912	266,649
Total gains or losses		
- recognised in interim condensed consolidated statement of income	(291)	745
Closing balance	315,621	267,394

There were no transfers between the fair value hierarchy levels during the current or prior period.

The fair values of on-statement of financial position financial instruments, except for loans and advances and other investments held at amortised cost are not significantly different from the carrying values included in the interim condensed consolidated financial statements. The fair values of customer deposits, debt securities in issue, cash and balances with SAMA, due from and due to banks and other financial institutions, other assets and other liabilities which are carried at amortised cost, are not significantly different from the carrying values included in the interim condensed consolidated financial statements, since the current market special commission rates for similar financial instruments are not significantly different from the contracted rates, and for the short duration of due from and due to banks and other financial institutions, other assets and other liabilities.

The management uses discounted cash flow method, using the current yield curve adjusted for credit risk spreads to arrive at the fair value of loans and advances. The estimated fair values of loans and advances was SAR 151.9 billion at 30 June 2018 (31 December 2017: SAR 143.05 billion).

The estimated investments held at amortised cost are based on quoted market prices when available or pricing models when used in the case of certain fixed rate bonds. The estimated fair values of these investments was SAR 34.4 billion at 30 June 2018 (31 December 2017: SAR 31.5 billion).

13. OPERATING SEGMENTS

The Group determines and presents operating segments based on the information that is provided internally to the chief operating decision maker in order to allocate resources to the segments and to assess its performance. The operating segments are managed separately based on the Group's management and internal reporting structure. The Group's primary business is conducted in the Kingdom of Saudi Arabia with one international branch, a representative office and an agency. However, the total assets, liabilities, commitments and results of operations of this branch, representative office and agency are not material to the Group's overall interim condensed consolidated financial statements and as a result have not been separately disclosed. The transactions between the Group's operating segments are recorded as per the Bank's transfer pricing system. There are no other material items of income or expenses between the operating segments.

NOTES TO THE INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

For the six months period ended 30 June 2018 and 2017

13. OPERATING SEGMENTS (continued)

The Group's reportable segments under IFRS 8 are as follows:

Retail banking

Deposits, credit and investment products for individuals and small to medium sized businesses.

Investment banking and brokerage

Investment management services and asset management activities related to dealing, managing, arranging, advising and custody of securities.

Corporate banking

Principally handling corporate customers' current accounts, deposits and providing loans, overdrafts and other credit facilities and derivative products.

Treasury and investment

Principally providing money market, trading and treasury services as well as the management of the Group's investment portfolios.

The Group's total assets and liabilities at 30 June 2018 and 2017 and its total operating income, total operating expenses and net income for the six months periods then ended, by operating segments, are as follows:

30 June 2018	Retail banking	Investment banking and brokerage	Corporate banking	Treasury and investment	Total
SAR'000 (Unaudited)					
Total assets	53,872,757	948,389	106,006,605	54,648,527	215,476,278
Total liabilities	74,165,310	69,729	89,070,772	15,235,521	178,541,332
Total operating income, net of which	1,433,674	173,776	1,719,534	976,091	4,303,075
- Net special commission income	1,269,376	45,934	1,153,296	682,183	3,150,789
- Fee and commission income, net	168,132	116,569	536,828	958	822,487
Inter segment revenues	212,168	45,895	(501,794)	243,731	-
Total operating expenses, net of which	1,126,354	73,382	861,680	69,829	2,131,245
- Depreciation of property and equipment	110,178	82	27,861	7,469	145,590
- Impairment charge for credit losses, net and other provisions	20,290	-	462,853	(5,491)	477,652
- Impairment charge for investments	-	-	-	18,161	18,161
Share in earnings of associates, net	-	-	-	27,490	27,490
Net income	307,320	100,394	857,854	933,752	2,199,320
	-	-	-	-	-
30 June 2017					
SAR'000 (Unaudited)					
Total assets	50,572,683	874,229	107,110,161	60,433,107	218,990,180
Total liabilities	64,088,973	57,115	102,863,983	15,352,772	182,362,843
Total operating income, net of which	1,300,402	147,755	1,729,918	813,125	3,991,200
- Net special commission income	1,149,165	46,096	1,207,979	495,285	2,898,525
- Fee and commission income, net	153,177	99,874	489,999	6,112	749,162
Inter segment revenues	172,258	44,895	(299,049)	81,896	-
Total operating expenses, net of which	915,002	65,037	1,039,955	83,376	2,103,370
- Depreciation of property and equipment	98,809	137	30,198	10,785	139,929
- Impairment charge for credit losses, net	(28,947)	-	617,513	-	588,566
- Impairment charge for investments	-	-	-	-	-
Share in earnings of associates, net	-	-	-	7,445	7,445
Net income	385,400	82,718	689,963	737,194	1,895,275

NOTES TO THE INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

For the six months period ended 30 June 2018 and 2017

14. FINANCIAL RISK MANAGEMENT**14.1 Credit Risk**

Credit exposures arise principally in lending activities that lead to loans and advances, and investment activities. There is also credit risk in off-balance sheet financial instruments, such as loan commitments. The Group uses internal credit rating tools to assess credit standing of its counterparties and assigns credit ratings accordingly. Also the Group uses the external ratings, of the major rating agency, where applicable. A potential credit loss might arise due to lack of proper credit analysis of the borrower's credit worthiness, inability to service the debt, lack of appropriate documentation, etc..

The Group attempts to control credit risk by appropriate credit structuring, credit review process, post-disbursal monitoring of credit exposures, limiting transactions with specific counterparties, and continually assessing the creditworthiness of counterparties. The Group's risk management policies are designed to identify and to set appropriate risk limits and to monitor the risks and adherence to limits. Actual exposures against limits are monitored daily. In addition to monitoring credit limits, the Group manages the credit exposure relating to its trading activities by entering into master netting agreements and collateral arrangements with counterparties in appropriate circumstances, and limiting the duration of exposure. In certain cases, the Group may also close out transactions or assign them to other counterparties to mitigate credit risk.

The Group's credit risk for derivatives, represents the potential cost to replace the derivative contracts if counterparties fail to fulfil their obligation, and to control the level of credit risk taken, the Group assesses counterparties using the same techniques as for its lending activities.

Concentration Risk refers to the risk from an uneven distribution of counterparties in credit or in other business relationship or from concentration in business sectors or geographical regions. Accordingly, concentration risk in the credit portfolios comes into existence through a skewed distribution of financing to (a) individual borrower (name concentration) (b) industry /service sector (sector concentration) and (c) geographical regions (regional concentration). Concentrations of credit risk indicate the relative sensitivity of the Group's performance to developments affecting any particular category of concentration.

The Group seeks to manage its credit risk exposure through diversification of lending activities to ensure that there is no undue concentration of risks with individuals or groups of customers in specific locations or business. It also takes security when appropriate. The Group also seeks additional collateral from the counterparty as soon as impairment indicators are noticed for the relevant individual loans and advances.

Management monitors the market value of collateral recurrently, requests additional collateral in accordance with the underlying agreement and monitors the market value of collateral obtained during its review of the adequacy of the allowance for impairment losses. The Group regularly reviews its risk management policies and systems to reflect changes in markets products and emerging best practice.

NOTES TO THE INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

For the six months period ended 30 June 2018 and 2017

14. FINANCIAL RISK MANAGEMENT

14.2 Credit quality analysis

Amounts arising from ECL – Significant increase in credit risk (continued)

I) Loss allowance

The following table shows reconciliations from the opening to the closing balance of the loss allowance for Loans and advances.

	30 June 2018			Total
	Stage 1	Stage 2	Stage 3	
Balance at 1 January	367,358	662,765	2,480,865	3,510,988
Transfer to 12-month ECL	9,736	(1,624)	(8,112)	-
Transfer to lifetime ECL - not Credit Impaired	(23,268)	29,453	(6,185)	-
Transfer to lifetime ECL - Credit Impaired	(32,846)	(111,449)	144,295	-
Net re-measurement of loss allowance	42,200	(1,354)	520,375	561,221
Write-offs	-	-	(767,007)	(767,007)
Balance as at 30 June	<u>363,180</u>	<u>577,791</u>	<u>2,364,231</u>	<u>3,305,202</u>

viii) Collateral

The Groups in the ordinary course of lending activities hold collaterals as security to mitigate credit risk in the loans and advances. These collaterals mostly include time, demand, and other cash deposits, financial guarantees, local and international equities, real estate and other fixed assets. The collaterals are held mainly against commercial and consumer loans and are managed against relevant exposures at their net realizable values. For financial assets that are credit impaired at the reporting period, quantitative information about the collateral held as security is needed to the extent that such collateral mitigates credit risk

NOTES TO THE INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

For the six months period ended 30 June 2018 and 2017

15. DIVIDENDS

On 26 March 2018, the shareholders in the Ordinary General Assembly meeting approved the distribution of dividends to shareholders for the second half of 2017. The amount of such dividend, net of zakat amounted to SAR 1,140 million (SAR 0.38 per share) and the distribution date for the dividend was 9 April 2018.

The Board of Directors initially approved interim dividend of SAR 1,110 million (2017: SAR 1,050 million), which was finally ratified and announced on 4 July 2018, resulting in dividends of SAR 0.37 per share (2017: SAR 0.35 per share) to the shareholders.

16. BASIC and DILUTED EARNINGS PER SHARE

Basic and diluted earnings per share for the period ended 30 June 2018 and 2017 are calculated by dividing the net income for the period by 3,000 million outstanding shares.

17. CAPITAL ADEQUACY

The Group's objectives when managing capital are to comply with the capital requirements set by SAMA to safeguard the Group's ability to continue as a going concern and to maintain a strong capital base.

The Group monitors the adequacy of its capital using the methodologies and ratios established by the Basel Committee on Banking Supervision and as adopted by SAMA, with a view to maintain a sound capital base to support its business development and meet regulatory capital requirement as defined by SAMA.

The Group management reviews on a periodical basis its capital base and level of risk weighted assets to ensure that capital is adequate for risks inherent in its current business activities and future growth plans. In making such assessments, the management also considers the Group's business plans along with economic conditions which directly and indirectly affects its business environment.

SAMA has issued the framework and guidance regarding implementation of the capital reforms under Basel III - which are effective from 1 January 2013. Accordingly, the Group's consolidated Risk Weighted Assets (RWA), total eligible capital and related ratios on a consolidated group basis are calculated under the Basel III framework.

The following table summarizes the Bank's Pillar-1 Risk Weighted Assets, Tier 1 and Tier 2 capital and capital adequacy ratios.

	30 June 2018 (Unaudited) SAR Millions	31 December 2017 (Audited) SAR Millions	30 June 2017 (Unaudited) SAR Millions
Risk weighted assets			
Credit	196,751	207,783	214,066
Operational	14,063	14,035	13,911
Market	2,770	1,251	2,036
Total Pillar-I Risk Weighted Assets	<u>213,584</u>	<u>223,069</u>	<u>230,013</u>
Eligible capital			
Tier I Capital	36,935	38,623	36,627
Tier II Capital	4,448	5,072	5,072
Total Tier I and II Capital	<u>41,383</u>	<u>43,695</u>	<u>41,699</u>
Tier I Capital Adequacy Ratio %	17.3%	17.3%	15.9%
Total Capital Adequacy Ratio %	19.4%	19.6%	18.1%

18. COMPARATIVE FIGURES

Certain comparative amounts have been reclassified to conform with the current period presentation