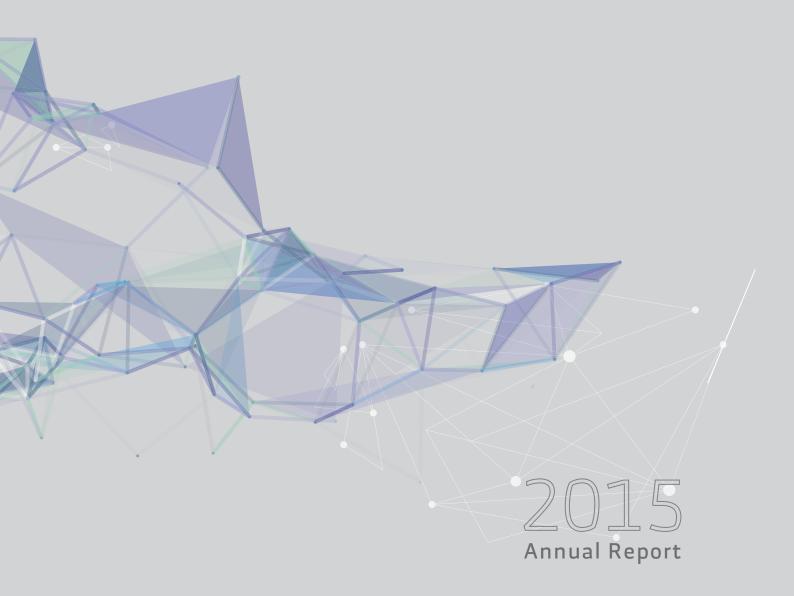
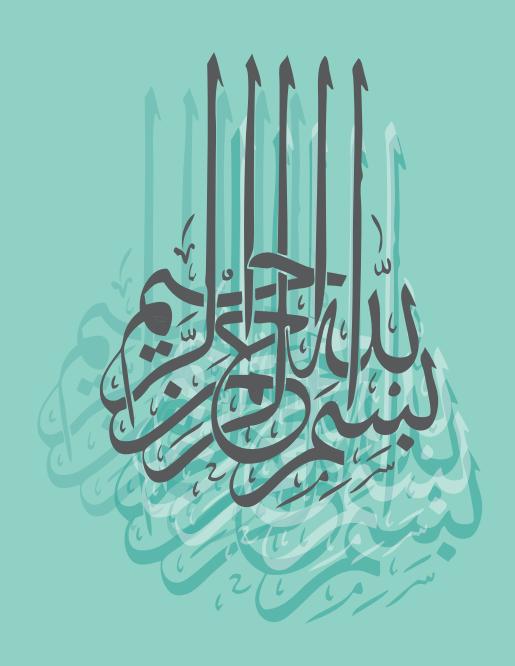
### بنك الرياض rıyad bank









Custodian of the Two Holy Mosques King Salman Bin Abdulaziz Al Saud



HRH Prince Mohammad Bin Nayef Bin Abdulaziz Al Saud Crown Prince, First Deputy Prime Minister and Minister of Interior

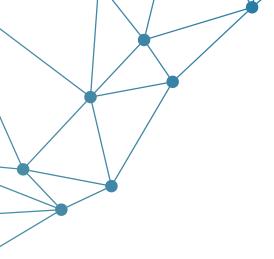


**HRH Mohammad Bin Salman Bin Abdulaziz Al Saud** Second Deputy Prime Minister and Minister of Defence



**Table of Contents** 

Financial Statements Highlights 2015	07	Economic & Financial Outlook	67
		Introduction	68
Board Of Directors	11	Oil Markets	71
The Chairman's Statement	12	The Potential Impact of the Drop in Oil	
Board of Directors	16	Prices on the Global Economy	73
Report of the Board of Directors	18	The Gulf Region	74
Summary of Accomplishments 2015	45	The Saudi Economy	78
Retail Banking Services	46	Financial Markets	80
Ladies Banking	48	Macroeconomic Performance in 2015	
Islamic Banking	48	and Outlook for 2016	81
Private & Golden Banking Services	48		
Overseas Branches	49	Financial Statements 2015	85
Corporate Banking	49	Independent Auditors' Report	86
Treasury & Investment Division	51	Consolidated Statement of Financial	
Investment Portfolio	51	Position	88
Risk Management	51	Consolidated Income Statement	89
Credit Risk	52	Consolidated Statement of	
Market & Liquidity Risks	53	Comprehensive Income	90
Operational Risks	53	Consolidated Statement of Changes in	
Stress Testing	54	Shareholders' Equity	91
Internal Control Department	54	Consolidated Statement of Cash Flows	92
Credit Rating	55	Notes	93
Business Technology	55		
Business Technology Governance	56	Summary of Pillar 3 Qualitative Report	
Compliance Department	56	Disclosure	153
Human Resources	57	Scope Of Application	154
Marketing & Communications	58	Credit Risk	156
Enhancing Customer Experience	59	Market Risk	159
Community Service	60	Operational Risk	160
Riyad Capital	63	Operational Kisk	100
Ajil Financial Services Company	64		
Ithraa Al-Riyad Real Estate Company	64	Executive Management	165
Al- Alamiya Cooperative Insurance Company	65	Executive Management	166
Riyad Company For Insurance Agency	65	Head Office, Regional & Overseas Office	168





We will be the leading Saudi Bank, first in quality, first in value, first in caring for our customers and responding to their needs, by continuously improving our services, while enhancing our shareholders' value.







## Financial Statements Highlights 2015

Total Assets (SAR Billions)

223.316

2015	223		
2014	215		
2013	205		
2012	190		
2011	181		

Loans & Advances, net ( SAR Billions)

144.674

h	2015		1.	45
	2013		Т,	+5
	2014		133	
	2013		131	
	2012	117	1	
	2011	113		

Shareholder's Equity ( SAR Billions)

36.545

2015	37
2014	36
2013	34
2012	32
2011	30

Customer Deposits ( SAR Billions)

167.090

2015	167
2014	164
2013	153
2012	146
2011	140

(SAR' Millions) Financial Statements Highlights	2015	2014	2013	2012	2011
Total Assets	223,316	214,589	205,246	190,181	180,887
Loans & Advances, net	144,674	133,490	131,191	117,471	112,973
Investments, net	44,552	46,963	43,538	36,254	36,616
Customer Deposits	167,090	164,079	153,200	146,215	139,823
Shareholders' Equity	36,545	35,537	33,870	31,964	30,158
Net Special Commission Income	5,183	5,130	4,697	4,381	4,197
Fee & Commission Income, net	1,786	2,020	1,821	1,777	1,589
Total Operating Income *	8,029	8,058	7,131	6,866	6,321
Operating Expenses excluding provisions	2,927	2,806	2,578	2,350	2,510
Provisions	1,052	900	605	1,050	662
Total Operating Expenses	3,980	3,706	3,183	3,400	3,172
Net Income	4,049	4,352	3,947	3,466	3,149
Earnings Per Share (SAR)**	1.35	1.45	1.32	1.16	1.05
Return on Average Assets ***	1.85%	2.07%	2.00%	1.87%	1.78%
Return on Equity	11.08%	12.25%	11.65%	10.84%	10.44%
Number of Branches in KSA	334	318	252	252	248
Number of ATMs	2,777	2,551	2,518	2,591	2,594

<sup>\*</sup> Total Operating Income includes the Share of Income from Associates

<sup>\*\*</sup> Previous year figures are restated since Bonus Issue is made during 2014  $\,$ 

<sup>\*\*\*</sup> Average is Calculated by adding opening and closing balances and dividing it by 2





# **BOARD OF**DIRECTORS



# The Chairman's Statement

### Chairman's Statement - Annual Report 2015

Since its establishment in 1956, Riyad Bank has been considered as one of the leading prestigious banks in the Kingdom with a key role in supporting the national economy and community service as well as being a pioneer in the Saudi banking sector.

Today, as we turn a new page and welcome a new year, coinciding with the Bank's 60 year anniversary, we look back at the many proud accomplishments that successfully translated the vision of its founders and crystalized the aspirations of its shareholders and reflected the dedicated efforts of its staff who gave their energy and talents effortlessly to preserve the Bank's achievements and surpass them, generating increased revenues and enhancing shareholders' value while maintaining leadership position in the banking industry.

Throughout its journey, Riyad Bank has excelled in answering challenges, while continuing to grow and supporting the national economy and growth by embracing innovation as an adopted approach in banking. The Bank has focused on upholding best practices within the industry, supporting its capabilities and strengthening its capital base, thereby projecting the needs of customers and meeting them in order to provide an enriched banking experience.

Despite the turbulent economic winds that surrounded the Kingdom at large, and the financial and economic challenges that encountered the emerging markets which in turn led to fluctuations in oil prices, the Saudi economy was able to minimize the impacts of this due to the Kingdom's strong financial reserves, as well as its robust fiscal and monetary policies. The Saudi economy managed to maintain a steady growth pace throughout the last five years, at the same time that the government is continuing to execute developmental projects

and capital expenditures to reassure the business community in general and private sectors in particular to support fulfilling its role as a vital pillar of the national economy.

Thus, in 2015, Riyad Bank continued to move forward in its approach to implement its strategy to expand the Bank's business and diversify its activities. This included taking the lead in the financing of national infrastructure and developmental projects, confirming its deep confidence in the ability of the national economy to raise its efficiency to absorb the consequences of global markets recession and overcome the surrounding economic circumstances. The Bank has a firm belief in the attractiveness of investment in the local market and its ability to generate further growth opportunities.

Based on that vision, the Bank issued a four billion riyal subordinated Sukuk in mid-2015 with a tenure of ten years and a call option at the end of the Sukuk's fifth year to strengthen its capital base which in turn will enable it to expand its credit business.

Riyad Bank remained a prominent partner to the business and trade sectors, actively involved in the financing field, given its long-standing and substantial banking experience, solid funding base and flexible banking and financing solutions. Furthermore, the Bank continued to provide specially-tailored funding programs for industry, trade, private and corporate sector projects. The Bank also contributed in infrastructure and large developmental projects, while supporting the small and medium-sized enterprises (SMEs) and emerging enterprises (EEU) sector through the "Kafala" program (that funds small and medium enterprises) making the Bank one of the largest contributors to this program that year.

The Bank continued to implement its restructuring strategy and developing its network of branches and business divisions to implement the strategy of





expanding the Bank's business. To this end, the Bank accomplished many achievements in 2015, most notably the opening of new branches, upgrading the ATM network as well as the significant expansion of the Points of Sale network through the introduction of new incentive packages and benefits designed to attract merchants and enhance a growing culture of adopting electronic payments in the Kingdom.

One of the most prominent banking achievements for Riyad Bank in this regard was the announcement of its "contactless payment service", which made the Bank one of the first Saudi Banks to launch such a service as part of the Points of Sale technology, which is considered a new feature added to smart applications to enhance its electronic banking services.

The Bank has established and launched its new main Data Center according to best international standards and specifications in order to achieve top quality and performance as well as provide high level protection to the Bank's databases and clients' information.

Customers are Riyad Bank's core focus and top priority. Accordingly, the Bank has continually reflected this into its adopted initiatives, approved policies, products and programs to solidify its position as the Bank of choice for customers, and a financial partner that is keen to meet their needs and provide exceptional, quick and meticulous services. Thus, 'Enriching Customers' Experience' strategy was actively pursued to affect a significant shift in the quality of service offered to customers, providing them with innovative products and distinguished solutions that furnish them with dimensions of uniqueness, attractiveness and added value to their banking experience.

As the real wealth of the Bank stems from its human resources without a doubt, its source of strength and success, the Bank strategies throughout the years prioritized this key element. Accordingly, the Bank continued to execute initiatives and programs, aimed at developing the skills of its staff, increasing their potential and instilling positive competition between them. No efforts were spared in this respect, as the Bank currently invests in its staff to

prepare a generation of leading Saudi bankers who can carry on its message and open new horizons of prosperity and progress.

Whilst highlighting its vigorous endeavors, the Bank continued to develop its work environment to attract more Saudi professionals utilizing its partnerships with national academic institutions as well as local and international universities which provide first class Saudi graduates. The Bank maintained its top ranking position as one of the biggest institutions in the private sector in employing Saudi staff with high Saudization rates reaching 93%, while 100% of the Bank's leadership positions are held by Saudis. Similarly, Saudi women maintained their significant position occupying 25% of the workforce, as well as holding many leading positions in the Bank.

The Bank has long been considered a hub for all types of charity work serving different segments of society, aiming at reaching the highest levels of community service, continuing its quality initiatives which emerge out of its commitment to its social responsibilities and maintaining the values of giving and social solidarity which all represent one of the pillars of its vision.

The varied charity activities conducted by the Bank spanned different areas across the Kingdom, leaving a marked trail of positivity and success. In fact, the Bank set three cornerstones for its community work: comprehensiveness, development and sustainability.

To mention a few, the Bank focused on people with special needs, providing them with a multitude of courses aimed at developing their skills to compete within the market and further integrate within society. The Bank also provided special care to underprivileged females, empowering them to be more productive members of society and providers for their families. In addition, the Bank maintained

its ongoing sponsorship of the Book of the Year Award and Women of Excellence Award, which are recognized as two of the most prestigious awards within the realm of culture and literature locally.

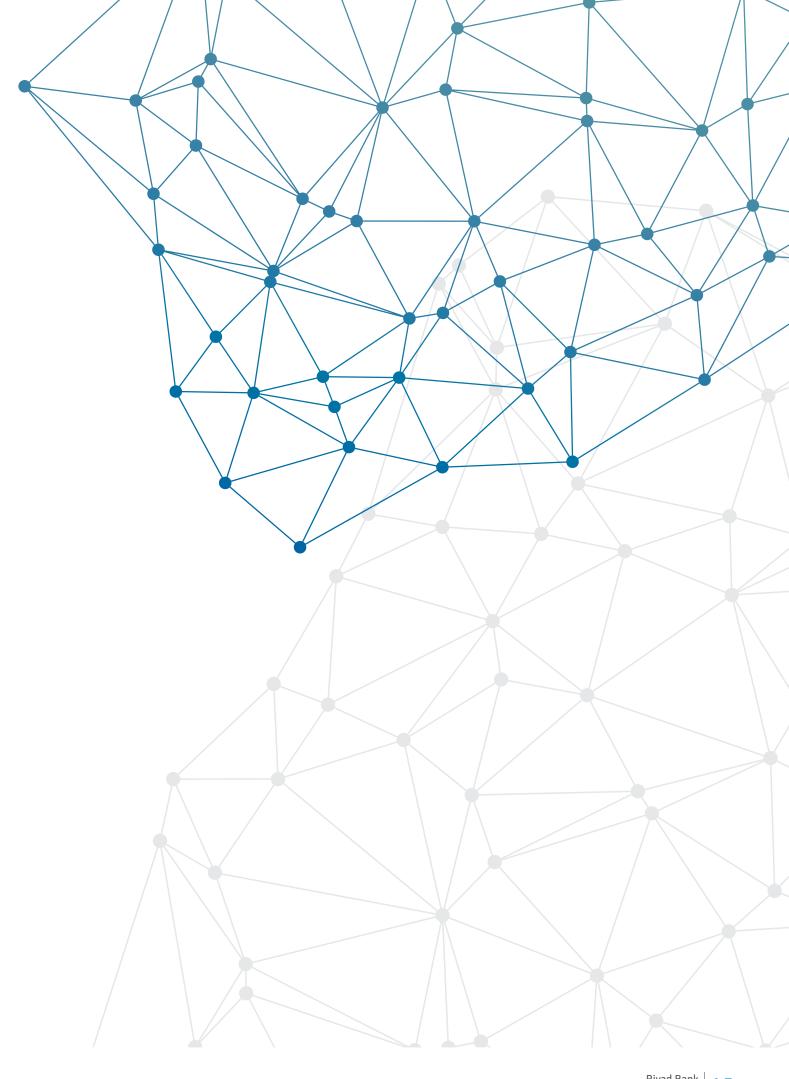
The year also witnessed healthcare related support initiatives. In this respect, the Bank distributed medical equipment and devices to needy patients in cooperation with the Friends of the Patient Committees in the Kingdom, providing charities with the necessary transportation for patients entitled to receive support, arranged visits for inpatient children as well as sponsoring a wide range of programs specialized in raising health awareness which included a number of events, festivals and conferences which was sponsored by the Bank over the past years.

I would like to emphasize that the Bank's progress was first and foremost a result of the dedication and hard work of its employees and I would like to express my gratitude to all of them for their efforts. I would also seize the opportunity to praise the numerous volunteer efforts of our employees including blood donations, visits to inpatients, gifts presented to sick children in hospitals during Eid and the holidays, and visits and donations for the needy families.

In conclusion, and on behalf of the Board of Directors, I would like to express my thanks and gratitude to the shareholders for their precious trust and support, and to the Bank's employees for their devotion and efforts. I hope that the new year will bring with it further success and prosperity for all those associated with the Bank, from its staff to its shareholders

#### Rashed Abdulaziz Al-Rashed

Chairman



### **Board of Directors**

#### **Executive Committee**

Rashed Abdulaziz Al-Rashed (Chairman) Abdullah Ibrahim Al-Ayadhi Faris Adbullah Abaalkhail Mohammed Abdulaziz Al-Afalaq Waleed Abdulrahman Al-Eisa

#### **Audit Committee**

Abdullah Mohammed Al-Eisa (Chairman) Nader Ibrahim Al-Wehibi Ibrahim Al Ali Al-Khudair Abdullah Hasan Al-Abdulqader Abdullah Abdullatif Al-Saif

### The Nomination & Compensation Committee

Abdullah Ibrahim Al-Ayadhi (Chairman) Rashed Abdulaziz Al-Rashed Faris Adbullah Abaalkhail Mohammed Abdulaziz Al-Afalaq Nader Ibrahim Al-Wehibi Waleed Abdulrahman Al-Eisa

Rashed Abdulaziz Al-Rashed
Chairman of the Board of
Directors

Khaled Hamza Nahas Board Director Abdulrahman Hassan Sharbatly Board Director Abdulaziz Saleh Al-Jarbou Board Director Abdullah Ibrahim Al-Ayadhi Board Director

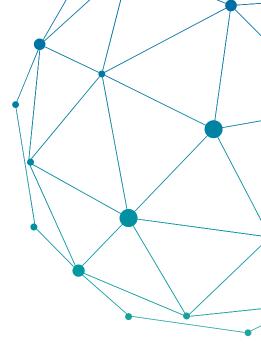












#### Strategic Planning Group

Rashed Abdulaziz Al-Rashed (Chairman) Abdulaziz Saleh Al-Jarbou Abdullah Mohammed Al-Issa Faris Adbullah Abaalkhail Nader Ibrahim Al-Wehibi

#### Risk Committee

Mohammed Abdulaziz Al-Afalaq (Chairman) Abdullah Ibrahim Al-Ayadhi Waleed Abdulrahman Al-Eisa



Abdullah Mohammed Al-Issa Board Director Faris Adbullah Abaalkhail Board Director Mohammed Abdulaziz Al-Afalaq Board Director Nader Ibrahim Al-Wehibi Board Director Waleed Abdulrahman Al-Eisa Board Director











# **Report of**The Board of Directors

The Board of Directors is pleased to announce its annual report on the performance of Riyad Bank and its subsidiaries for the year 2015. This report includes information on the Bank's activities, main achievements, strategies, and financial results, as well as its Board of Directors and various committees, plus other supplementary information in order to meet the requirements of the user of this report.

#### **Primary Activities:**

Riyad Bank's primary activities span the banking and investment sectors both within the Kingdom and abroad. Over the years, the Bank has worked to provide a broad range of banking and commercial services for companies and individuals as well as financing for commercial and industrial activities, enterprises and infrastructure projects through its large network of offices - 334 branches within the Kingdom, a London branch, a Houston agency in the United States and a representative office in Singapore. Through its wholly-owned subsidiary, Riyad Capital, the Bank also offers a variety of asset management services for retail customers including brokerage services in capital markets in addition to a wide range of investment services and funds.

The Income Statement presents the year's results from the Bank's main activities as outlined in Notes 20-21 of the Annual Report while the Bank's business results and divisions are explained in Note 27, which is attached to the financial statement. The assessment of potential risks and vulnerability is an integral element of the Bank's operations and to support the management of potential risks, a number of committees specialise in market, credit, operational, strategic and compliance risk monitoring. These committees complement the Bank's existing Risk Committee, which operates under the Board of Directors. Further information about possible risks, including those what may be encountered by the Bank in the future, is detailed in Notes 28,29,30, 31 of the Annual Report.

#### **Main Achievements:**

Riyad Bank made significant progress during 2015. The Bank had accomplished a number of key strategic objectives, which have supported both the Bank's growth and an expansion of its portfolio of products and services. The Bank's endeavours crystallised through the teams' relentless efforts to meet customer expectations while strengthening its leadership of the Kingdom's banking sector in a number of ways. The Bank's foremost achievements can be examined through a review of the different banking divisions as follows:

#### **Retail Banking Services:**

2015 was marked by a series of successful accomplishments in the retail banking services. This was evident in the Bank's decision to restructure its auto leasing products, by signing new agreements with strategic automobile dealerships and service providers. Accordingly, 8 new after-sale centers were established in key cities across the Kingdom, which reflects the Bank's ambitions towards expansion and pioneering. The Bank also launched a new automated system that enables customers to obtain preliminary financing approval within minutes through its sales agents at automobile dealerships in order to take the customer experience to new levels.

In terms of personal finance, the Bank launched a new Murabaha shares finance product catering to different segments that prefer trading in Shariah compliant equity shares, instead of commodities, for their immediate lending needs. Moreover, the Bank launched a supplementary mortgage product in coordination with Real Estate Development Fund (REDF); becoming one of the first institutions to obtain the approval of SAMA to launch a new mortgage product "Ijara Mousofa Bel-Thema" for off-plan properties through real estate developers.

An achievement for Riyad Bank in 2015 was the issuance of MasterCard Debit Card, in partnership with MasterCard International. The new card is an update of Maestro ATM card and is accepted at over 40 million outlets worldwide. The MasterCard Debit Card comes in four categories: Silver, Titanium, Platinum and World, all of which are tailored to meet the needs of various segments of customers, Private, Gold and Mass, such as access to more than 600 lounges at airports around the world, as well as access to local and international offers and services by MasterCard.

Another accomplishment for the Bank in 2015 was the new 'Contactless' feature added to the MasterCard Debit Cards, whereby the cardholder does not have to swipe or insert the card through any POS machine, all they have to do is pass it near the sensor of the machine. This feature adds flexibility and more protection to the use of the card. To facilitate the process of issuing the new cards, all Riyad Bank branches around the Kingdom were provided with new machines that can print the new Contactless MasterCard Debit Cards.

Part of its innovative bundle of digital products, Riyad Bank issued a new Virtual electronic card. The card can be used for online shopping on any website that accepts Visa cards in an easy, safe manner without the need to issue the conventional plastic card.

The 'Live Chat' service, incorporated to the Bank's website and Riyad Online, is yet another innovative interactive channel added to the Bank's services. Such a service elevates the prompt response to the

questions and queries of customers.

When it comes to ATMs, the Bank added 339 new machines to its network and was present at 11 events with its mobile ATM vehicle.

With the increasing market share in Ladies Banking, and in line with the Bank's strategy for expanding the ladies branches throughout the Kingdom, as a response to the growing size and needs of this important sector, 6 new regions were added to the existing 3, thus bringing the total number of regions for Ladies Banking to 9, comprising of a total of 79 branches, in addition to 2 self-service centers in Jeddah and Khobar.

#### **Private & Golden Banking Services:**

It is all about modernism and elegance when Riyad Bank's Private and Golden Banking services are mentioned. All the Bank's products and services in this area are based on extensive analysis of customers' needs and expectations which have always been the focus of the Bank. The Bank has 4 Private Banking centers and 60 Golden Banking centers which were designed to service this segment through an experienced team to cater to all their needs.

#### **Corporate Banking:**

Corporate Banking has always operated following a clear vision "we will be a reliable and a strategic partner for our customers, offering them a distinct business environment supported by a top quality customer service". The Corporate Finance Department serves as the Bank's center of expertise for syndicated, structured and project finance operations. The department works in close coordination with the Bank's domestic network and with the offices in London, Houston and Singapore to provide products and services to the Saudi corporate community and to a wider network of



global corporations with investment and trading connections in the Kingdom.

The Financial Institutions Department acts as a focal point for managing all aspects of Riyad Bank's relationship with corresponding banks and non-banking financial institutions by providing them with investment and insurance services, and financing solutions in the form of Ijarah, in addition to a broad range of tailored products and services designed to meet the needs of such a sector.

Riyad Bank continued to stand out due to its large network of corresponding banks needed to facilitate the international banking needs of its retail, corporate and institutional customers, while offering competitive rates with emphasis on quality of service.

The Bank maintained its position among the top contributors to KAFALAH program for financing small and medium enterprises. In this respect, the Bank's share was SAR 3.2 billion, equivalent to 25% of the total amount offered through the program. This amount covers 1,764 enterprises, constitutes 26.5% from the total number of enterprises from the beginning of the program until the end of the third quarter in 2015.

Riyad Bank continued to be active in the local market through the selection of notable financing transactions. The Bank therefore was appointed as the global facility agent and mandated lead arranger for the Saudi Aramco USD 10 billion Standby facility, the largest bank facility ever arranged for a KSA company.

Riyad Bank also acted as the agent for syndicated loans and custodian. It was also the holder of a number of local and international accounts of industrial, infrastructure and real estate projects. In this regard, the Bank was the general agent for 27 financing facilities with a value exceeding SAR 63 billion.

In the same year, Riyad Bank was appointed mandated Islamic lead arranger for the Petro Rabigh 2 expansion project, at a value of US\$ 1.87 billion. It

has also succeeded in winning the bid for managing and executing the Investment loan program launched by the Real Estate Development Fund.

Corporate Banking played an integral part in the Bank's overall growth, by activating the role of cash management and trade finance through restructuring the products and dividing them into various categories that resonate with the ever changing customer needs in electronic payments, prepaid cards and cash management and allowing to reach such products via advanced electronic channels.

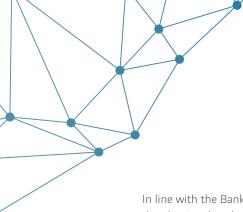
Significant success was achieved by the Bank in prepaid cards, especially cards tailored for staff salaries and student allowances, which offer a number of services such as bill payment, settlement of government fees as well as purchases through Points of Sale (POS). During 2015, Riyad Bank further expanded its Point of Sale (POS) network by adding a large number of retailers, achieving a growth rate of 100%, reaching more than 40,000 POS.

Riyad Mobile Business app is another achievement for the Bank in electronic services. It is the first application in Saudi Arabia designed to help corporate customers manage their business online through smartphones, anytime and anywhere. Two other services especially made for corporate customers were also launched in 2015: SADAD safe payment services and cash deposit machines.

On the trade finance front, the Bank introduced many improvements to its work processes by automating the execution of operations and by developing Riyad Online Corporate, which allowed the customers to execute their transactions in a shorter period of time.

#### **Treasury & Investment Division:**

The Treasury and Investment Division plays a pivotal role in managing the Bank's liquidity and funding requirements, as well as managing the interest rate and foreign exchange risk exposure within the limits approved by the Bank, and managing the investment portfolio and providing financial hedging products and solutions to the Bank's customers.



In line with the Bank's overall cross-selling strategy, the division has been aligned and focused on a cross-selling initiative to widen and diversify its customer reach. The expansion of the cross-selling initiative shall also provide Corporate and Private customers with innovative hedging solutions for interest rate and foreign exchange exposure. During the year, the division's cross-selling initiative was a major success; posting a strong growth rate in deal volumes as well as revenues.

Also during 2015, Treasury and Balance Sheet Management unit under ALCO supervision managed the issuance of SAR 4 billion sub-ordinated Tier II Sukuk to strengthen the capital base of the Bank, to reduce maturity mismatch risk and diversify funding sources. This was received with high interest from investors which reflects the Bank's financial strength and investor's trust.

#### **Investment Portfolio:**

Riyad Bank's investment strategy focuses on the quality, diversity and liquidity of the assets allocation process under the supervision of the Bank's Investment Committee. The Bank's investment portfolio consists of diversified local and international assets with investment in fixed income in government and corporate bonds constituting the majority of the assets. The investment portfolio has generated good returns in 2015.

#### **Islamic Banking:**

Riyad Bank continued its march during 2015 towards developing banking solutions and products that are compliant with Shari'ah and are approved by the Bank's Shari'ah Committee. The Bank's Islamic products and solutions cover the daily transactions, financing and investment solutions for its retail and corporate customers.

The Bank saved no effort in improving human resources involved in the provision of Islamic banking services, raising the efficiency of their performance through more training and regular assessment of the performance of the Islamic banking branches through more than 50 follow-up visits.

2015 also witnessed 8 meetings with the Shari'a Committee for Islamic banking through which a number of financial products and solutions in accordance with the "Murabaha" and "Ijara" (rental) formats were developed. The Bank has also adopted the terms and conditions of issuing Islamic credit cards in addition to hedging products in the Treasury Division. It has further worked on integrating the investment solutions provided by Riyad Capital including Riyad Bank 'Sukuk' and Maaden Phosphate Company 'Sukuk' and Riyad Real Estate Income Fund.

#### **Overseas Branches:**

Through an overseas banking network represented by our branch office in London, the Houston agency, and the Singapore Representative Office, Riyad Bank provides banking solutions to its customers abroad, serving the corporate customer base, and allowing the Bank to provide its customers with tailored services to meet their various needs. In addition, the Bank provides advice on investments and business in the Kingdom of Saudi Arabia. This leads to enhanced trade in the Kingdom and customers' investment interests abroad.

The London Branch plays an active role in supporting the rapid growth of commercial activities carried out by the leading European multinational companies with the Kingdom. This support ranges from providing letters of guarantee and stand-by letters of credit, as well as assisting in the provision of financing for their business in Saudi Arabia. In addition to this, the London Branch also provides tailored banking services to the Bank's customers in the Kingdom and their affiliated companies in order to support their European investments in industry and other sectors.

Riyad Bank is the only window for Saudi banks in the Americas, where the Houston Agency plays an important role in attracting investments to the region, as well as helping U.S. and multinational companies to support their commercial activities in the Kingdom of Saudi Arabia. In addition, the Agency supports Saudi companies doing business in North America.

Riyad Bank is also present in the Far East, where our Singapore Representative Office helps Riyad Bank customers take advantage of investment opportunities in Asia, and to develop relationships with correspondents and Asian corporations who have business activities in Saudi Arabia.

#### **Business Technology Governance:**

The Business Technology Governance has occupied an important position in managing the risks and securing the Bank's business. The Bank has paid special attention to build a well-controlled system, which has witnessed many accomplishments during 2015.

The Bank obtained the ISO Certificate for Information Security Management. The ISO 27001:2013 audit conducted by BSI (British Standards Institution) for Riyad Online services was completed successfully without any non-conformities or observations. Riyad Bank was the first bank in KSA to attain ISO certification. The Bank has further taken action towards assuring that governance and risk management are in line with information security policies. This initiative enhances the Bank's infrastructure to comply with any future requirements, enhancing business management while limiting risks related to information security.

The Business Continuity department continually carried out Business Continuity Assessment for Riyad Bank Business Continuity Process; allowing a 360 degree analysis of the process to boost and enhance the Bank's services in accordance with international standards for banking and financial institutions.

The department also implemented the Business Continuity Lifecycle Automation System (BCLAS), that positions Riyad Bank ahead of its peers locally and internationally. The project has provided the necessary capabilities for the continuity of banking systems and it is now in its final stages. This allows crises management to carry out business in an efficient way while making the Business Continuity Processes more transparent and accountable.

#### **Business Technology:**

During 2015, Riyad Bank carried out significant accomplishments in the area of Information Technology. The most prominent achievement was the Data Center Relocation Project. The data center contained all the Bank's data related to transactions and customers.

The new data center is highly designed and supplied with state-of-the-art equipment to enhance the speed and efficiency of performance. The Centre uses fiber optic communication systems that enhances the effectiveness of Riyad Bank's channels and raise the protection of its databases and its transfer mechanism.

The center is considered a smart and environment friendly venue; having fire protection and multi protection systems to combat any disasters, accidents or breakthroughs. According to Uptime indicator, the new data center building obtained the highest rating in the Saudi market (A+).

Furthermore, the Division successfully migrated Mypay and Alawal customers to the new Card Management System, which is fully compliant with the Saudi Arabian Monetary Agency (SAMA) prepaid cards regulations. This initiative enabled the prepaid cardholders to make bill payments through ATM Channels.

#### **Risk Management:**

The Bank continues to adopt the standards of corporate governance in accordance with local statutory and regularity requirements and also follows the developments internationally in corporate governance codes and practices to support the Bank's policies to manage risk according to accurate and well-founded standards.

Financial crimes constitute a serious threat on financial institutions and their employees, and if arise, might cause damage to the Bank's strength and negatively impact the delivery of its services and weaken the trust it has with the regulatory authorities, customers, business partners alike. This will also keep the Bank exposed to continued threats and might damage its reputation locally and internationally. Thus in 2015, The Financial Crimes Prevention Department was set up under Risk Management as part of its comprehensive program to improve controls and methods to combat money laundering, terrorism financing and fraud.

#### **Credit Risk:**

Financial institutions are facing a multitude of challenges the foremost of which is credit criteria in addition to insufficient assessment of changing economic conditions which could lead to deterioration of the credit standing of customers. Credit risk appears when there are indicators of the inability or failure of borrowers to meet their contractual commitments. Riyad Bank manages these risks by conducting in depth and thorough analysis of the borrower's ability to honor his obligations which would include repayment sources, the nature of underlying collateral and other factors and conditions impacting the borrower's activities.

The Credit Risk Management framework, within which the Bank operates, consists of principles, structures, tools and activities required for managing credit risk at all levels. This framework supports the Bank's efforts in enhancing asset quality while observing the rules and regulations set by the Saudi Arabian Monetary Agency (SAMA), all within clearly designed and regularly monitored risk parameters. In addition, the other related departments supervise the execution of credit strategy and risk appetite levels by setting a clear plan for identifying, establishing risk tolerance parameters, along with monitoring and reporting mechanisms for credit risk at the Bank. The Bank continually assesses and monitors credit exposures to ensure timely identification of potential credit problems.

The Bank utilizes sophisticated credit software systems to ensure management of credit applications, limits management, and collateral management. In addition the Bank uses an advanced internationally recognized credit rating system to assess the viability of corporate credit applications and produce their credit ratings according to the

rating system that is approved by the Board of Directors. The Bank also uses an advanced retail credit system for Retail Risk.

Currently, the Bank is focusing on strengthening its infrastructure and developing an automated system for early warning notification to start reviewing credit portfolios and take the necessary corrective measures before it gets affected.

In accordance with SAMA regulations, the Bank is in compliance with all Basel requirements in respect to capital adequacy calculation to cover credit risk according to the Standardized Approach. Following the success in developing credit rating models as per Basel III requirements, the Bank made further progress in 2015 towards the implementation of Internal Rating Based (IRB) standards as a second alternative.

The Bank established a system for validating these models on regular basis. In 2015, the Bank went through another round of independent periodical tests to validate the outcomes of these credit rating models and its quantitative and qualitative components in line with SAMA expectations. Further, the Bank established the infrastructure to use and operate these models in taking credit related decisions depending on a precise measurement of credit risks and the expected return from these risks. At the same time, the Bank completed the review of approved risk policies to further assure that credit rating systems meet IRB standards.

At the same time, the Retail Risk department has taken final steps in implementing the Advanced Internal Ratings-Based (AIRB) standard that is compatible with the Basel requirement as mandated by Saudi Arabian Monetary Agency (SAMA), which include defining governance structures as well as most updated credit policies.

The department has also undertaken an enterprise level assessment of its existing credit risk systems and tools to better measure risk adjusted return. This assessment will benefit the customer's experience by adopting a digital strategy which provide customers with fast and easy access to e-banking services.

#### **Market and Liquidity Risks:**

The Market and Liquidity Risk Management Department, which is part of the Risk Management Division (RMD), assumes the responsibility of measuring and monitoring market risks, and asset/liability risks resulting from the fluctuation in fair values or future cash flows of financial instruments due to changes in market prices within the Board's approved risk framework and limits. Periodic reports were prepared and submitted to the relevant stakeholders at the Bank.

The primary market risk measure used within Riyad Bank is the Value-at-Risk (VaR) methodology, which incorporates the volatility of relevant market prices and the correlation of their movement. In addition, the Bank implemented a number of standards and other advanced methodologies to enhance its analytical capabilities in managing market risk including stress testing and sensitivity analysis. The Bank also continued to implement its strategy in compliance with Basel's Internal Model (IMA) Approach to measure and manage market risk.

During 2015, the Bank continued to align its market risk management processes to the new guidelines of Saudi Arabian Monetary Agency (SAMA) regarding liquidity risk management and improving mechanisms to gather, analyze and present risk data.

#### **Operational Risks:**

Operational risks play a vital role within financial institutions, especially after the rapid growth of banking services which fully depend nowadays on information technology and communications that cover all aspects of life. Operational risk can be defined as deficiency resulting from inadequate or failed processes, people or systems. Therefore, Operational Risk Management ensures the application of SAMA instructions regarding risks resulting from deficiencies in operations, systems, infrastructure or human errors. During 2015, the department worked on activating a range of precautions to raise the efficiency of the Operational Risk Management department which included the following:

Upgrading and updating essential operational risks management systems as well as increasing

its efficiency through automating the Risk Control Self Assessment (RCSA) as well as risks control. In addition to providing a comprehensive view of the current risks in the form of periodic reports supported with charts and diagrams to evaluate risks of every department and division at the Bank, while ensuring that the risks standards are compliant with Basel (III) requirements.

- Implementing a bank-wide Risk Control Self Assessment (RCSA) methodology across all business lines. The RCSA plays an important role in the detection of control gaps and serves as a strong and effective internal control tool.
- Completing a comprehensive evaluation of the Internal Control framework for its Control Environment, Risk Assessment and Management, Institutional Controls, Accounting, Information and Communication Systems, and Self-Assessment and Monitoring, Reporting and follow-up pursuant to the Bank's internal control guidelines.

During 2015, the capital adequacy ratios were continually monitored to prevent any operational risks. The Bank works in accordance with the standardized approach under the Basel II requirements, and is gradually preparing itself to meet the Advanced Measurement Approach (AMA) requirements for operational risk using the Value at Risk (VaR) model.

#### **Stress Testing:**

The Bank implemented an overarching Stress Testing Framework in 2015, covering all material risks relating to banking activities under the oversight of the Board of Directors and that was after enhancing the policies, frameworks and rules of governance related to it. Under this framework, risk owners reviewed the stress methodologies along with their assumptions to maintain efficacy of the stress models deployed.

#### **Internal Control Department:**

During 2015, the Bank continued to emphasize its commitment to the best standards for

internal control and the full compliance with the requirements of the Saudi Arabian Monetary Agency (SAMA). Riyad Bank has been incessantly improving the elements of governance and internal control in order to integrate the risk management systems into internal control and raise the general awareness. Amongst these efforts came the establishment of the Internal Control Department that reports directly to the Chief Risk Officer .

The Internal Control Department is responsible for collecting the information from different areas, both internal and external, classifying them and analyzing their importance. The Internal Control Department follows up on the necessary plans to reinforce the internal control system. It further defines the criteria upon which the annual attestations, presented by the executive management and control units about the soundness and efficiency of the internal control system.

The department prepares internal control reports to the Audit Committee and executive management and also to the Operational Risk Management and Compliance (ORMSS).

At the executive management level, the internal control indicators were linked with performance standards. The Bank's divisions have also finished the application of control risk self-assessment of risk and internal control procedures by the divisional controllers who were assigned the responsibility of performing continuous tests to adjust, improve and enhance procedures and policies applied inside each division.

#### **Marketing & Communications:**

2015 witnessed the successful launch of several key marketing programs for various Retail and Corporate products and services, like Riyad Mobile Business app, MasterCard debit card, POS solutions, and many other activities, using conventional and modern media, supported by social media. This led to an improvement in the marketing campaigns results in terms of awareness, reach and engagement. The mix of conventional, digital and social media helped in consolidating

## the presence of the Bank and its competitive capabilities within the Saudi banking industry.

In addition, the Marketing Division developed two of its key departments - Digital Marketing and Marketing Intelligence. The evolving market needs and the changes in media scene and the consumption habits of conventional and digital media implied the empowerment of the Digital Marketing Department with necessary tools and resources to face the challenges of the day and the future. There were remarkable improvements in the Bank's presence on various social media platforms in 2015, where fans and followers on Facebook and Twitter doubled in size compared to the previous year. The Bank's page on LinkedIn was activated to help position Riyad Bank as a favored employer of choice. On average, throughout 2015 the Bank managed to maintain a leading position on the list of most socially influential banks in Saudi Arabia.

On the other hand , the Marketing Intelligence Department extended support to all the Bank's divisions by providing them with meaningful market, industry and product insights and learnings to help them with their decision making process. In 2015, the department managed to complete more than 87,000 phone calls with customers to measure their level of satisfaction and loyalty through a scheme known as "Net Promoter Score". The department also conducted 24 focus group discussion sessions with area managers and 240 in-depth interviews with frontline employees to measure, identify and recommend actionable solutions to enhance the quality of service at the branches.

A key objective for the Advertising & Media Relations Department is to support the image of the Bank and its products and services in local and regional media. In this respect, the department released 167 press releases, which were published 1,230 times in newspapers and major websites, in addition to 42 press supplements in 2015. The department shed the light on many retail and corporate banking products and services, and achieved a distinct media exposure for a multitude of community service programs.

One of Riyad Bank's most important objectives is to satisfy the needs of customers and exceed their expectations, which is an area of focus for the Quality Assurance Department. In 2015, the department implemented a series of advanced tactics and techniques to ensure quality and improve performance, and to make sure that quality improvement is a continuous process. In order to do that, the department restructured itself to focus on quality assurance requirements across various operations at the Bank.

#### **Enhancing Customer Experience:**

Following the successful establishment of a Customer Experience Department in 2014, the team begun to design and implement its strategy. Accordingly, the Customer Experience Team was always present to ensure that the design of the Customer Experience is underpinned by deep meaningful customer insights, and that the products, services and processes are designed around customer needs.

During 2015, the Customer Experience Department had key achievements, among which was the implementation of Net Promoter Score methodology that measures customer satisfaction and loyalty.

The team also led a study that focused on the different segments of the market. The study aimed at setting a better understanding of the requirements and behavior of customers upon which the Bank's services and products are designed. The team was a main contributor to the branches' services quality improvement program; developing the procedures of financing requests, issuing ATM cards and updating current accounts.

Early in 2015, the department inaugurated the research lab which is the first of its kind in the Kingdom. The lab is responsible for performing tests on the Bank's services and products in addition to studying their effect on actual customers before introducing them to the market. Moreover, many electronic services were subject to the live experience.

#### **Compliance Department:**

Riyad Bank endeavors to maintain a sound compliance culture and a business

strategy whereby the Bank's values and standards of professional conduct are maintained at every business level and within all its activities. These standards include local, international regulatory obligations, as well as the best practiced business standards and Riyad Bank's own internal regulations and codes of ethics and standards.

Riyad Bank's Compliance Department has been always committed to the betterment of the Bank's Compliance Control Environment, as well as the implementation of an effective compliance program which includes monitoring, advice and regulatory services. The Compliance Department aims at meeting the new requirements for initiatives such as Deposit Protection Fund, the new update of credit card and prepaid card regulations, the consumer protection laws and regulations for financing companies, Saudi Payment Network "MADA" Operating standards, the new amendments to the labor law, in addition to any updates to the SAMA Anti Money Laundering and Counter Terrorism Financing and Account Opening & Operating Regulations.

On the International front, the Bank continued its commitment to meet recommendations of FATF, and abide by the OFAC enforcements in order to combat money laundering and financing terrorism, as well as the financing of proliferation of weapons of mass destruction. The compliance department was also actively engaged with the local specialized authorities in fulfilling the implementation of FATCA requirements and complied by meeting the requirements of 2015 in that respect.

Moreover , the Compliance Department has been committed to following it's ongoing strategy striving to the highest standards and methodologies when it comes to Monitoring Compliance Risk in the Bank, a risk based monitoring plan was further developed and executed for 2015, and the plan was approved and monitored by the Board Audit Committee.

#### **Credit Rating:**

Riyad Bank succeeded in maintaining its distinct credit ratings with world rating agencies. With the Kingdom of Saudi Arabia witnessing a lowering in its ratings from (AA-/A-1+) to (A+/A-1), the Bank had its ratings consequently modified by Standard and Poor's Financial Services from (A+) to (A) for long-term commitments, while maintaining its rating (A-1) for short-term commitments, which is the highest rating there is. The overall outlook also changed from stable to negative in line with the sovereign rating. Having had such slight change in ratings, Fitch Ratings kept its ratings for Rivad Bank as (A+) for long-term commitments and (F1) for short-term commitments, which is the highest rating there is. From its side, Capital Intelligence, affirmed its ratings for the Bank as (AA-) for long-term commitments and (A1+) for short-term commitments, which is the highest rating there is. The last two ratings anticipate a stable future perspective for the Bank which in turn reflects the strength and durability of Riyad Bank's financial position.

#### **Bank Borrowings:**

On 6th November 2013, the Bank completed its primary sukuk offering of SAR 4 billion with a tenure of seven years and a call option at the end of the sukuk's fifth year. The sukuk's yield is three month SAIBOR +0.68%. This was followed on 24th February 2015 by another private secondary sukuk offering of SAR 4 billion with a tenure of ten years and a call option at the end of the sukuk's fifth year. The secondary sukuk yield is priced at +115 basis points over SAIBOR. These sukuk issuances are designed to support the diversification of the Bank's funding sources and maturities as well as the growth of its loan portfolio.

#### **Strategy and Objectives:**

Throughout 2015, the Bank continued implementing the set strategies thus working on the distribution strategy for retail as an organic extension to the enhancement of the customer experience enrichment program with a clear emphasis on digital technology and electronic banking channels. The Bank also focused on Ladies banking as a key pillar of retail banking to become the Bank of choice for this segment and cement its leadership position.

Moreover, the Bank continued to drastically change the quality of services at branches to meet the growing needs of customers of all different segments to be more efficient. The Bank paid special attention to Wealth and Asset management and funding emerging enterprises and SMEs to maintain its position as a key player in this market. The Bank will also continue to spare no effort to become the best Trade Finance bank in the Kingdom in terms of transaction execution and consultation services.

The Bank's strategies for the near future will focus on supporting the basis of key functions and highlighting the importance of the quality and nature of services provided to enhance performance levels, increase income, improve service standards and cross selling to customers. The Bank is also expected to track costs, improve efficiency in operations and execution of banking transactions by supporting asset quality and capital strength to increase the Bank's competitive capacity. In addition, the Bank remains keenly interested in digital and electronic banking as well as retail banking, while it will venture with some targeted initiatives into insurance, foreign currency exchange and mortgage loan markets.

The Bank also plans to expand its network by the optimal utilization and diversification of ATM machines and POS terminals to maintain a leading position in the banking industry. The Bank will also invest in the future to re-empathize its commitment to become the leading bank in offering digital banking services and will continue to execute projects in order to achieve this strategic goal.

#### **Community Service:**

Following in the footsteps of past years, Riyad Bank continued to pursue new horizons and achievements, that reflect the Bank's active role in community service and its contribution in supporting comprehensive growth and sustainable development.

The Bank also focused throughout the year on improving its delivery mechanisms through a process of regular evaluation.

Thus, in the field of healthcare, the Bank distributed medical equipment and supplies to the less fortunate and needy through a partnership with the Patients' Friends Committee and General Directorate of Health Affairs who oversee the distribution of supplies in a professional manner. As a continuation of "the charitable project for transportation", the Bank donated two especially equipped buses to transport patients for the benefit of the Patients' Friends Committee in Jeddah. The other two were donated to the King Fahad National Centre for Children's Cancer and Research in Riyadh.

The Bank also sponsored and participated in numerous activities related to healthcare awareness to educate the public about the importance of maintaining a healthy lifestyle. These activities included sponsoring breast cancer awareness campaign for Zahra Breast Cancer Association for the 8th year in a row, the Saudi Stroke Association awareness campaign, "Naqa" Anti-Smoking Society campaign, as well as "Nebras" the National Committee for Combatting Drugs, in addition to participating in the Saudi-American Healthcare Forum. The Bank staff also showed their support by participating in the blood donation campaign for the benefit of Children's Cancer Support Association "Sanad".

Furthermore, the Bank spearheaded several initiatives aimed at developing the skill set and abilities of special needs individuals. Some of the most notable examples include the "Momken" initiative - a program which aims to stimulate the capabilities of people with special needs, develop their skills and empower them to integrate in society. In partnership with the Ahsa Handicapped Society and the Irrigation and Drainage Authority, the Bank celebrated the graduation of 15 farmers as part of its 4th season of sponsoring this farming training program that focuses on qualifying individuals with simple mental disabilities to enter the job market. Similarly, the Bank partnered with the Riyadh Al-Shabab Club to sponsor the 9th season of the summer training programme for people with special needs. This resulted in establishing two centers in Bahaa and Hai'l with the collaboration of the Handicapped Society in Bahaa and HADCA association for special needs in Hai'l.

Following the success of the "Productive Families Project", Rivad Bank continued to support this initiative by developing and training young females to enable them to live as independent and selfsufficient productive members of society. This included the 'Nabta' programme in Al Jawf region, which was held in cooperation with Albir Society, and resulted in training 100 girls from beneficiary families on how to use computers, learn sewing, embroidery, cooking, baking and cosmetics. Riyad Bank also sponsored the Productive Families Project in Hoya, Taif as well as 'Bawabet Al-Khair' project which was organized by the Charitable Society for Mother and Childcare in the Eastern Province in order to improve the income of productive families by selling their handmade products.

Following its yearly custom, Riyad Bank's charity caravans have spanned the Kingdom's cities and villages with the assistance of staff volunteers. During Ramadan, the caravans distributed food baskets to needy families throughout the Kingdom and partnered with various charitable organizations such as Albir Society in Hoya, Charitable Association in Najran, Albir Society in Wosayta, Aja Women's Charity in Hail. In addition to the endless support Eta'am Charity's drive to spread awareness of food conservation and preservation, as well as Mawada Society's approach to reduce divorce cases.

These caravans undertook a similar mission during the winter season as part of the annual "Winter Clothing Campaign" to provide needy families in remote areas with the necessary supplies and clothing to bear the harsh winter conditions.

The Bank staff also continued with the yearly ritual of visiting ill children in hospitals and getting them gifts to lift up their spirits during the Eid holidays.

Moreover, cultural activities did not escape Riyad Bank's attention. The Bank celebrated the 8<sup>th</sup> Book of the Year Award in partnership with the Riyadh Literary Club. The 2015 award winners were Dr. Abdullah Al-Monef and Dr. Hind Al-Motairy.

Furthermore, in recognition of the integral role of culture in sustainable development, the Bank sponsored the first cultural award for women through the establishment of the Women of Excellence Award in cooperation with Al Qaseem Literary Club. The winners in the 1st season were Dr. Ghada Al-Tareef, Dr. Amina Al-Jibreen and Dr. Wafa Khinkar.

Strengthening its partnership with charities in the Kingdom, Riyad Bank took part in the campaign organized by Al-Nahda Women's Society to spread awareness of the importance of participating in the municipal elections and emphasized the role of women in Saudi society.

These charities organization were supported also by the Bank's electronic channels and portals to spread the campaign messages and raise awareness. In this way, Riyad Bank's community service activities were promoted across a wider audience, while at the same time partner charities and institutions benefited from the increased coverage from using these e-communication tools and social media platforms which has a large number of users and followers.

The Bank also launched the online donation feature for customers to be able to donate directly to specific charity organizations with ease and speed after undertaking an extensive background check of these charities and its activities.

Finally, addressing the needs of deceased employees and their families during the year, Riyad Bank renewed its 'Wafaa' programme with Al-Othaim Markets Company. An initiative specially tailored for the needy families of deceased staff members, the Bank issued prepaid cards for less fortunate families to provide them with the means to a decent life.

#### **Subsidiaries and Associates**

#### 1. Riyad Capital:

Riyad Capital is a Saudi limited liability company wholly owned by Riyad Bank with a paid up capital of SAR 200 million, and is licensed by the Saudi Capital Market Authority for dealing as Principal, Agent, Underwriting, Arranging, Advising and Custody Services.

Riyad Capital continuously innovates and develops investment products that meet the needs of its diverse customer base, through its Assets Management Department, which worked during 2015 on expanding its products by launching new investment fund: the 'Riyad Real Estate Income Fund' represents the 37th fund to be added to Riyad Capital's roster of investment funds. This has reinforced Riyad Capital's leadership in the assets market through its diversified investment products and large customer base. As a result, Riyad Capital boasts the second largest asset volume in the Kingdom.

In relation to Corporate Investment Banking, Riyad Capital is keen on attracting local professional expertise with relevant experience in all areas of investment banking advisory services, such as the management of Sukuk issuing, corporate shares, M&A and structured finance operations. One of the most important achievements of 2015 was the issuance of Riyad Bank's Sukuk with the value of SAR 4 billion, acting as the financial advisor, underwriter and the IPO lead manager for the Middle East Paper Co. worth of SAR 450 million .

To further strengthen Riyad Capital leading role in the local and international trading, in 2015 Riyad Capital launched a new digital channel to the list "Riyad Tadawul Mobile app" that is specially designed for smart phones and tablets . Additionally, Riyad Capital worked on enhancing its services to increase the customer satisfaction level and overall transactions, also executing digital marketing campaigns with unique propositions. Furthermore, Riyad Capital managed to gain a competitive edge by successfully signing an agreement with a specialized broker-dealer for US stock market which reflected positively on the international trading services.

In 2015, the Wealth Management Department promoted an enhanced investment culture among its customers through the value-added Investment Advisory Services that are provided to high-networth clients privately and professionally, through its 3 centers in Riyadh and eastern region, to help identify and tailor their investment options carefully and accurately. Consequently, Riyad Capital continued to implement its program for building

and preparing of an integrated team for wealth management, and provide technical and professional capabilities to enable this team to provide services to the company's high-net-worth clients to the fullest.

Retail Investment Department continued to provide and enhance its services its 19 network of investment centers spread throughout the Kingdom along with advanced electronic channels and call center.

#### 2. Ajil Financial Services Company:

Ajil Financial Services Company is a Saudi closed joint stock company subject to the regulations of the Saudi Arabian Monetary Agency. Ajil, with its headquarters in Jeddah, has a paid up capital of SAR 500 million divided over 50 million shares, with a nominal value of SAR 10 per share. Riyad Bank's contribution to Ajil's paid up capital is 35%, and the balance is held by Mitsubishi Company and a number of Saudi base businesses. Ajil Financial Services Company is a pioneering company in providing financing to capital assets, leasing advantages and many other innovative services to various economic sectors in the Kingdom, such as construction, transportation, manufacturing, trade and commerce.

#### 3. Ithraa Al-Riyad Real Estate Company:

Ithraa Al-Riyad Real Estate Company, registered in the Kingdom of Saudi Arabia, is a limited liability company wholly owned by Riyad Bank. Ithraa Al-Riyad Real Estate Company, headquartered in Riyadh, has a paid up capital of SAR 10 million divided over 1 million shares with a nominal value of SAR 10 per share. The company provides services for the real estate owners, and also buys and sells real estate and similar assets to support various financing solutions.

#### 4. Al-Alamiya Cooperative Insurance Company:

Al-Alamiya Cooperative Insurance Company, a joint stock company, founded by Riyad Bank in partnership with Royal Sun Alliance Insurance

(Middle East) in Bahrain, with a paid up capital of SAR 200 million divided over 20 million shares with a nominal value of SAR 10 per share. Al-Alamiya Cooperative Insurance Company shares are traded on the Saudi Stock Market (Tadawul). The company increased its capital from SAR 200 million to SAR 400 million through a rights issue upon the approval of the Extraordinary General Assembly held on 15/03/1436 A.H. (06/01/2015). The company is regulated by the Saudi Arabian Monetary Agency (SAMA) and its operations are in the Kingdom of Saudi Arabia. Riyad Bank owns 30% of its capital, directly and indirectly; directly owning 19.92% of the company shares and 21.42% of the shares of Royal Sun Alliance Insurance (Middle East). The relationship between Riyad Bank and Royal Sun Alliance Insurance (UK) goes back to over thirty years. 30% of Al-Alamiya Cooperative Insurance Company equity was offered to the Saudi public through an IPO. The Company is engaged in the commercial insurance and reinsurance business in the Kingdom, including general insurance, medical insurance, protection insurance and engineering insurance.

#### 5. Riyad Company for Insurance Agency:

Riyad Company for Insurance Agency is a limited liability company wholly owned by Riyad Bank. Its paid up capital is SAR 500,000. Riyad Company for Insurance Agency is registered in the Kingdom of Saudi Arabia with its headquarters located in Riyadh. The agency focuses on marketing and selling the insurance products of Al-Alamiya Cooperative Insurance Company through Riyad Bank to both corporate and retail customers in the Kingdom.

Riyad Company for Insurance Agency has entered into an insurance agreement with Al-Alamiya Cooperative Insurance Company to distribute insurance products in partnership with Riyad Bank. The company is fully licensed by the Saudi Arabian Monetary Agency and operates in accordance with its rules and regulations.

#### SUMMARY - RESULTS OF THE BANK'S OPERATIONS FOR THE PAST FIVE YEARS

SAR' Million

Description	2015	2014	2013	2012	2011
Assets					
Cash and balances with banks and SAMA	29,839	29,231	25,367	29,462	23,708
Loans and advances, net	144,674	133,490	131,191	117,471	112,973
Investments, net	44,552	46,963	43,538	36,254	36,616
Property, equipment, other real estate					
and investment in associates	2,678	2,566	2,542	2,606	2,588
Other assets	1,572	2,339	2,608	4,388	5,002
Total assets	223,316	214,589	205,246	190,181	180,887
Liabilities					
Balances with banks	4,496	3,790	7,578	6,163	6,242
Customer deposits	167,090	164,079	153,200	146,215	139,823
Other liabilities	15,185	11,183	10,598	5,839	4,664
Shareholders' equity	36,545	35,537	33,870	31,964	30,158

SAR' Million

Description	2015	2014	2013	2012	2011
Total operating income including share in					
earnings of associates	8,029	8,058	7,131	6,866	6,321
Total operating expenses	3,980	3,706	3,183	3,400	3,172
Net income	4,049	4,352	3,947	3,466	3,149
Earnings per share (SAR)	1.35	1.45	1.32	1.16	1.05

#### **Financial Results:**

The Bank achieved a net profit of SAR 4,049 million for the year ended 31st December 2015, a decrease of 6.96% from the previous year. The Bank's net profit was SAR 851 million for the fourth quarter compared to SAR 1,060 million for the corresponding quarter in the previous year, a decrease of 19.72%.

The Bank continued its focus on core banking activities which has further strengthened its financial position. As of 31st December 2015, Loans and Advances increased to SAR 144,674 million compared to last year's result of SAR 133,490 million - an increase of 8.38%. Investments, however, witnessed a decrease by 5.13% to SAR 44,552 million compared to SAR 46,963 million in the previous year. Customer deposits stood at SAR 167,090 million compared to SAR 164,079 million in the previous year, an increase of 1.83%. Total assets grew by 4.07%, reaching a total of SAR 223,316 million compared to SAR 214,589 million in the previous year.

The Bank attained a total operating income achieving SAR 7,989 million for the year 2015 compared to SAR 8,012 million in the previous year.

The diversity of the Bank's financing and investment products led to the growth in net special commissions which reached SAR 5,183 million for the year ended 31st December 2015 compared to

SAR 5,130 million for the previous year, an increase of 1.03%. In 2015, earnings per share reached SAR 1.35. The decrease in the Bank's net profit during the year ended 31st December 2015 is attributed to the decline in net income because of the increase in total operating expenses by 7.4%. This is mainly due to the increase in staff salaries and employee related expenses as well as the rise in the provision for credit losses, other operating expenses, provision for investments which were offset by a decline in other general and administrative expenses. Operating income decreased by 0.3% given the reduction in fee and commission income, and earnings of nontrade investments which were offset by an increase in other operating income, foreign exchange income and trading earnings.

Subsequently in the shareholders' general assembly, the Bank's Board of Directors recommended the distribution of SAR 1,050 million as dividends for the second half of 2015, at a rate of 35 Halalas per share. The total dividends for 2015 reached SAR 2,100 million, representing a rate of 70 Halalas per share. This reflects the Bank's commitment to undertake the approved strategies, in line with shareholders' expectations, as well as its endeavors to raise the yield on the shareholders' shares and preserve the rates of dividends, albeit against the macroeconomic challenges.

#### Geographical Analysis of the Bank's Total Income:

Total income for the year ended 31<sup>st</sup> December 2015 was SAR 8,963 million from domestic operations and SAR 1,137 million from international operations. The following table illustrates the geographical analysis of the total revenues:

SAR' Million

	Do	mestic Operatio	ns		
Year	Western Province	Central Province*	Eastern Province	International Operations	Total **
2015	1,532	6,190	1,241	1,137	10,100

\* The amount allocated for the Central Province includes income from investments related to the Treasury and Investment Division, which totaled SAR 3,293 million. This income is not related to any specific geographic sector domestically. It also includes revenues related to other regions.

\*\* The above mentioned total income is shown in gross amounts. In calculating the net amount, each income item is handled according to its category in the financial statements.

#### Geographical Analysis of the Total Income of the Bank's International Operations:

SAR' Million

Year	GCC & Middle East	Europe	North & Latin America	South East Asia	Other Regions	Total
2015	326	310	395	51	55	1,137

#### Appropriation of Earnings:

The Bank abides by all relevant, applicable rules and regulations and observes the following policies in distributing dividends to its shareholders:

- a) A transfer of 25% of the net profit to statutory reserve. Such transfers may be discontinued when the total statutory reserve is equal to the paid-up capital.
- b) Upon the recommendation of the Board of Directors and approval of the Annual General Assembly, dividends are distributed among shareholders, each in proportion to their shareholdings.
- c) The Bank's strategic direction determines the distribution of the interim and annual dividends. The dividends proposed for the second half of the year are included in the shareholders' equity, and will remain there until the Annual General Assembly approves the Board of Directors' recommendation.

#### The Board of Directors recommended the appropriation of earnings as follows:

SAR' 000

Retained earnings of 2014 at the beginning of the year	2,160,066
Net income of the year 2015	4,049,477
Total	6,209,543
Appropriation as follows:	
Zakat as per the Sharia'	250,000
Cash dividends, distributed to shareholders for the first half of 2015	1,050,000
Cash dividends, proposed for distribution to shareholders for the second half of 2015	1,050,000
Transfer to statutory reserve	1,012,369
Retained earnings at the end of the year 2015	2,847,174

On 27<sup>th</sup> July 2015, the Bank distributed an amount of 35 Halalas per share as an interim half-year dividend. The proposed dividend for the second half of 2015, amounting to 35 Halalas per share, will be distributed upon the approval of the General Assembly. This will bring the total dividends for 2015 to SAR 2,100 million after deducting Zakat, at a rate of 70 Halalas per share.

#### **Board of Directors:**

The Bank is governed by a Board of Directors which is composed of ten members who are elected by the General Assembly every three years and may be re-elected for a similar term at the end of their term. The Board of Directors currently includes six independent members and four non-executive members, as defined in Article II of the Corporate Governance Guidelines issued by the Capital Market Authority (CMA). The Board of Directors held nine meetings in 2015, with 100% quorum in person or by proxy, with an attendance rate of 86%.

The following table depicts the Board of Directors meetings during 2015:

Riyad Bank's Board Members **	Meeting 1	Meeting 2	Meeting 3	Meeting 4	Meeting 5	Meeting 6	Meeting 7	Meeting 8	Meeting 9	Total
Date	7/1/2015	2/2/2015	6/4/2015	6/4/2015	18/5/2015	15/6/2015	19/9/2015	26/10/2015	21/12/2015	
Rashed Abdulaziz Al-Rashed (Independent)	✓	✓	✓	✓	1	✓	✓	✓	1	9
Dr. Khaled Hamza Nahas (Independent)	1	1	✓	1	✓	✓	✓	✓	✓	9
Abdulrahman Hassan Sharbatly (Non-Executive)	By Proxy	By Proxy	By Proxy	By Proxy	1	By Proxy	By Proxy	1	By Proxy	2
Dr. Abdulaziz Saleh Al- Jarbou (Independent)	1	1	1	1	1	✓	1	1	1	9
Abdullah Ibrahim Al-Ayadhi * (Non-Executive)	✓	✓	1	1	By Proxy	By Proxy	1	✓	1	7
Eng. Abdullah Mohammed Al-Issa (Independent)	✓	✓	✓	✓	✓	✓	✓	✓	1	9
Dr. Faris Abdullah Abaalkhail (Independent)	By Proxy	✓	By Proxy	By Proxy	1	1	By Proxy	✓	✓	5
Mohammed Abdulaziz Al- Afaleq (Independent)	1	1	1	1	1	1	1	1	✓	9
Nader Ibrahim Al-Wehibi* (Non-Executive)	1	1	1	1	1	1	1	1	1	9
Waleed Abdulrahman Al- Eisa* (Non-Executive)	1	1	1	1	1	✓	1	1	1	9

<sup>\*</sup> Members representing the Public Investment Fund (PIF), General Organization for Social Insurance (GOSI) and Public Pension Agency (PPA) respectively.

The Board of Directors carries out its responsibilities through several committees which comprise Riyad Bank Board members, except for the Audit Committee, which, in addition to two members from the Board of Directors, includes three external, independent, non-Board members.

#### 1. The Executive Committee:

The Executive Committee is responsible for the credit, banking, financial and administrative functions in the Bank, as determined by the Board of Directors. The Committee held twenty four meetings in 2015, with 100% attendance from all members.

#### 2. The Audit Committee:

The Audit Committee is responsible for the operations related to financial reporting and compliance operations, specifically legal and regulatory compliance. The Audit Committee is also tasked with monitoring the effectiveness and efficiency of the Bank's Internal Control system

<sup>\*\*</sup> All members of the Board of Directors are elected, including the corporate representatives.

and risk management processes. Finally, the Audit Committee also recommends the selection of external auditors. The Committee held six meetings in 2015, with an attendance rate of 97%. The Bank's Audit Committee consists of five members, three of whom are external, non-Board members – Dr. Ibrahim Al Ali Al-Khudair, Dr. Abdullah Hasan Al-Abdulqader and Eng. Abdullah Abdullatif Al-Saif.

### 3. Risk Committee:

The Risk Committee assists the Board of Directors in overseeing the Bank's risk strategy. The Risk Committee continually reviews the Bank's approved risk levels and prepares recommendations to the Board of Directors on the suitability of these risk levels. The Risk Committee also monitors executive management compliance with these risk levels. The Risk Committee consists of three members. The Risk Committee held four meetings in 2015, with an attendance rate of 100%.

### 4. The Nomination & Compensation Committee:

The Nomination & Compensation Committee is responsible for the development, approval and application of the Bank's compensation system on behalf of the Board of Directors. The Nomination & Compensation Committee tasks consist of regularly reviewing and assessing the Bank's compensation policy to ensure its suitability and effectiveness for the Bank. The Committee is responsible for

submitting policy recommendations to the Board of Directors which accordingly updates or amends them. The Committee also evaluates the Bank's compensation payments structure and regularly makes recommendations to the Board of Directors on issues including salary levels and structures, compensation and benefits for the Bank's senior executives. The Committee ensures Riyad Bank's compliance with SAMA regulations regarding compensation policies in the banking sector.

Finally, the Committee oversees all recommendations and nominations to the Board of Directors as per approved policies and standards, to ensure regulatory compliance with the Board membership rules established by the Banking Control regulations, the Capital Market Authority (CMA), and Saudi Corporate Law. The Committee, consisting of six members, held three meetings during 2015, with 100% attendance.

### 5. The Strategic Planning Group:

The Strategic Planning Group is responsible for the preparation of the Bank's strategy. The Group also monitors and evaluates all actions taken to accomplish these objectives. The Group regularly reviews all major projects initiated by the Bank, and benchmarks the Bank's financial and operational performance against the Bank's strategic objectives. The Committee held three meetings in 2015, with 100% attendance.

Dr. Ibrahim Al Ali Al-Khudair External Member of the Audit Committee Dr. Abdullah Hasan Al-Abdulqader
External Member of the
Audit Committee

Eng. Abdullah Abdullatif Al-Saif External Member of the Audit Committee







The following table lists the names of Riyad Bank's Board of Directors, committees and committee members, along with the attendance rate of members at the Board of Director's meetings, as well as permanent and temporary committees, both in person or by proxy. In total, there were 285 meetings, with 99.5% attendance. The table also shows other joint stock companies in which Riyad Bank board members participate in their boards of directors.

The responsibilities of the committees of the Board of Directors are listed below:

Riyad	Bank's Board of Directors		Names of joint stock companies (listed and unlisted) where Board	
' Name	Committee Membership	Attendance %	Members hold membership in their Boards	
Rashed Abdulaziz Al-Rashed	Chairman of The Executive Committee Chairman of The Strategic Planning Group Member of the Nomination & Compensation Committee	100%	Abdulaziz Al-Rashed Al-Humaid Company	
Dr. Khaled Hamza Nahas		100%	National Water Company Hasana Investment Company Saudi Basic Industries Corporation (SABIC)	
Abdulrahman Hassan Sharbatly		100%	Al Sagr Cooperative Insurance Company	
Dr. Abdulaziz Saleh Al-Jarbou	Member of the Strategic Planning Group	100%	Saudi Paper Manufacturing Company (WARAQ) Amiantit Company Gulf Chemicals and Industrial Oils Company	
Abdullah Ibrahim Al- Ayadhi	Chairman of the Nomination & Compensation Committee Member of the Executive Committee Member of the Risk Committee	100%	Saudi Technology Development and Investment Company National Water Company	
Eng. Abdullah Mohammed Al-Issa	Chairman of the Audit Committee Member of the Strategic Planning Group	100%	Arabian Cement Company Saudi Basic Industries Corporation (SABIC) Dur Hospitality Co. Etihad Etisalat	
Dr. Faris Abdullah Abaalkhail	Member of the Executive Committee Member of the Nomination & Compensation Committee Member of the Strategic Planning Group	100%	Fawaz Abdulaziz Alhokair & Company	

Riyad	Bank's Board of Directors	Attendance	Names of joint stock companies (listed and unlisted) where Board Members hold membership in	
Name	Committee Membership	%	their Boards	
Mohammed Abdulaziz Al-Afaleq	Chairman of the Risk Committee Member of the Executive Committee Member of the Nomination & Compensation Committee	100%	None	
Nader Ibrahim Al-Wehibi	Member of the Audit Committee Member of the Nomination & Compensation Committee Member of the Strategic Planning Group	100%	None	
Waleed Abdulrahman Al-Eisa	Member of the Executive Committee Member of the Nomination & Compensation Committee Member of the Risk Committee	100%	Taawuniya Insurance Company	

	k Board's Committee Members Non-Board Members)		Names of joint stock companies (listed and unlisted) where Board	
Name	e Committee Membership		Members hold membership in their Boards	
Dr. Ibrahim Al Ali Al-Khudair	Member of the Audit Committee (Non-Board Member)	100%	None	
Dr. Abdullah Hasan Al- Abdulqader	Member of the Audit Committee (Non-Board Member)	100%	Saudi Telecom Company Saudi Technology Development and Investment Company Saudi Arabian Investment Company Gulf International Bank (Bahrain)	
Eng. Abdullah Abdullatif Al- Saif	Member of the Audit Committee (Non-Board Member)	83%	Qassim Cement Company Herfy Food Services Company Specialized Laboratory Company Hassana Investment Company	

### Remuneration of Directors and Senior Executives during the year 2015:

(SAR' 000)

Description	Members of the Board	Senior Executives *	
Salaries	-	11,580	
Allowances	711	1,494	
Annual and periodic remuneration **	3,600	5,102	
Incentive Plans	-	1,376	
Compensation and Other Benefits	43	458	
End of Service Benefits	-	1,363	

<sup>\*</sup> Represents remuneration for the five senior executives from the Bank's executive management, including the CEO and CFO.

### Changes in major shareholdings:

The following tables detail shareholdings and any change thereof during 2015, for the Bank's Board of Directors, Senior Executives, their spouses and minor children in the shares or credit instruments of the Company and its subsidiaries, in accordance with the provisions of Article 43 of the CMA Listing Rules:

Major Shareholders, Non-Board Members and Senior Executives including their Spouses and Minor Children							
	Beginning of the year			End of Year			
Name	Number of Shares	Credit Instruments	Ownership*	Number of Shares	Credit Instruments	Net Change **	Ownership*
Public Investment Fund (PIF)	652,608,000	-	21.7536%	652,608,000	-	-	21.7536%
General Organization for Social Insurance (GOSI)		_	21.6252%	501,757,200	_	(147,000,000)	16.7252%
Public Pension Agency (PPA)	275,424,674	-	9.1808%	275,424,674	-	-	9.1808%
Al-Nahla Trading and Construction Company	268,778,637	_	8.9593%	268,778,637	-	_	8.9593%
Aseela Investment Co. (MASC Holding Company previously)	240,000,000	_	8.0000%	240,000,000	_		8.0000%

<sup>\*</sup> To the nearest four decimal points.

<sup>\*\*</sup> The annual remuneration for a board member reaches SAR 360 thousand.

	Begini	ning of th			End	d of Year	
Name	Number of Shares	Credit Instruments	Ownership*	Number of Shares	Credit Instruments	Net Change **	Ownership*
Rashed Abdulaziz Al-Rashed **	29,648,653	-	0.9883%	12,396,076	-	(17,252,577)	0.4132%
Dr. Khaled Hamza Nahas	4,800	-	0.0002%	4,800	-	-	0.0002%
Abdulrahman Hassan Sharbatly	283,528,824	-	9.4510%	283,971,984	-	443,160	9.4657%
Dr. Abdulaziz Saleh Al-Jarbou	2,000	-	0.0001%	324,048	-	322,048	0.0108%
Abdullah Ibrahim Al- Ayadhi	-	-	-	-	-	-	-
Eng. Abdullah Mohammed Al-Issa	1,262,000	-	0.0421%	1,262,000	-	_	0.0421%
Dr. Faris Abdullah Abaalkhail	2,460,000	-	0.0820%	2,245,554	-	(214,446)	0.0749%
Mohammed Abdulaziz Al- Afaleq	78,500	_	0.0026%	80,000	_	1,500	0.00279
Nader Ibrahim Al Al-Wehibi	-	_	-	-	_	-	
Waleed Abdulrahman Al-Eisa	_	_	-	_	_	_	
Talal Ibrahim Al-Qudaibi	66,864		0.0022%	66,864		-	0.00229

<sup>\*</sup> To the nearest four decimal points.

<sup>\*\*</sup> Controlled by the Chairman of the Board of Directors, Rashed Abdulaziz Al-Rashed, the shares enlisted in the company shareholders record witnessed a decrease in the last period. Owned and registered under the names of family members, the shares were excluded after their respective owners assumed the management of the shares themselves.

### **Accrued Regulatory Payments:**

There are no accrued regulatory payment(s) due by the Bank for the year 2015, except for those illustrated below:

(SAR' 000)

Description	2015
Zakat – Department of Zakat and Income Tax	250,000
Taxes payable by the Bank on behalf of non-resident bodies (in accordance with the terms and conditions of the contract)	15,056
Taxes payable by the Bank's overseas branches to official bodies outside the Kingdom	16,852

# Penalties, Sanctions and Preventative Provisions:

No regulatory restrictions were imposed on the Bank by the CMA or any other supervisory, regulatory or judicial authority. Total penalties and fines paid by the Bank in conducting its operational activities amounted to SAR 2,369 thousand, which were mainly related to the Bank's ATM operations and other operational fines.

### **Applicable Accounting Standards:**

The consolidated financial statements are prepared in accordance with the Accounting Standards for Financial Institutions promulgated by the Saudi Arabian Monetary Agency (SAMA) and International Financial Reporting Standards (IFRS).

The Bank also prepares its consolidated financial statements in compliance with the Banking Control Law, the provisions of Regulations for Companies in the Kingdom of Saudi Arabia.

In line with its role and responsibility towards safeguarding and protecting the Bank's assets and its customers' deposits, the Board of Directors confirms that:

 The Bank is not a party in any contract that is or was of substantial interest to either the Chairman, the members of the Board of Directors, the Chief Executive Officer, Chief Financial Officer, or any person with a direct relationship with any of them. The following statement explains the transactions of related parties during the Bank's ordinary course of business in 2015:

a) The Board of Directors members, key management personnel, other major shareholders and their affiliated companies:

	SAR' 000
Loans and advances	4,476,342
Customer deposits	51,299,804
Derivatives assets (at fair value)	1,876
Commitments and contingencies (irrevocable)	2,458,247
Executive end of service benefits	47,447

Key management personnel are referred to individuals, including an executive or non-executive director, who have authority and responsibility for planning, directing and controlling the activities of the Bank, directly or indirectly. Other major shareholders represent persons with shareholdings of 5% or more of the Bank's issued share capital.

b) Income and expenses pertaining to transactions with related parties and included in the financial statements are as follows:

	SAR' 000
Special commission income	91,302
Special commission expense	323,886
Fees from banking services, net	156,580
Directors and committees remuneration and expenses	4,705
Executive remuneration and salaries	38,871
Executive end of service	2,584
Other expenses	15,112

- The internal control system is properly developed and is effectively implemented;
- All accounting records are properly prepared and maintained;
- There is no doubt as to the Bank's ability to continue its activities.

In regards to the Internal Control the Board commends the good work of the Internal Control Department and the Bank's Internal Control system. The Bank's Internal Control staff pursues financial best practices. The Bank has a well-established and organized process, both for the design of financially-based internal controls as well as their effective implementation. The essential elements of the Bank's Internal Controls system include: well-defined roles and responsibilities for the Board of Directors and Executive Management; delegated financial and administrative authorities based on seniority, and proper segregation of duties and responsibilities.

Risks are qualitatively and quantitatively analyzed and are controlled by the Bank's Internal Committees, including the committees for market risk, credit, operational, strategic and compliance risks. These Management committees report directly to the Audit and Risk committees under the Board of Directors.

The Board of Directors through the Audit Committee has full access to all internal audit reports, internal control reviews, as well as risk management and other relevant reports. These are reviewed on an annual basis to provide an ongoing assessment of the effectiveness of the Bank's Internal Control system. In addition, the Internal Audit Department is required

to regularly follow up on prior recommendations and file update reports for the Bank's Audit Committee on previous recommendations relating to changes in the Bank's Internal Controls system. The Audit Committee sees no significant gaps or poor performance during 2015 which would have affected the quality or accuracy of the financial statements contained within this report. While both the Audit Committee and the Board of Directors endeavour to ensure a reasonable level of assurance and accuracy in terms of the Bank's internal controls, they also note that no internal control system, no matter how well designed and implemented, can provide an absolute level of assurance.

### **Corporate Governance Regulations:**

The Bank applies the provisions contained in the Corporate Governance Regulations of the Kingdom of Saudi Arabia, issued by the Capital Market Authority (CMA), except as disclosed in Form (8) regarding the extent of compliance to the Corporate Governance Regulations, summarized as follows:

Article 6 – Voting Rights – The Bank has not adopted accumulative voting and will not do so until such voting rights are finally approved by the relevant regulatory bodies, in accordance with the provisions set out by the Saudi Arabian Monetary Agency.

Riyad Bank looks to comply with all governance regulations and will continue to keep abreast of developments in this important area. The Bank is in the process of finalizing all related policies and procedures.

### **Human Resources:**

Building a strong institution like Riyad Bank requires a strong human resources structure. In this context, the Bank has finalized its strategies for restructuring, determining specifications and career paths within its 3-year workforce plan which aims at developing the organizational structure.

As far as the Saudization process is concerned, the Bank is considered a pioneering institution. The ratio of Saudi employees has been steadily increasing over the years and it has now reached 93.5% this year. The Bank is also proud to have 100% Saudi women employees working within its organization, during this year the female workforce has increased to 25% of the total workforce and this positive increase is ongoing.

The Human Resources Department has developed a strategic plan to support the activities needed for skills development. The plan works by determining the requirements for each job and providing the incumbent with the necessary skills through internal and external training.

The Human Resources Department has a vision that underlies all its work - that the Bank is the

prime choice for employees. Working towards this vision, the department develops its structure and the program related to career progression, such as the 'Riyad Bank Program'. The Department has been pursuing international best practices in all the services, procedures and transactions provided for employees, some of which include the 'iRecruitment System' and 'Performance Appraisal System.'

The Human Resources Department is a strategic partner to the Bank's many divisions. To guarantee the success and sustainability of this partnership, the Bank has issued its 'Business Partner Management' program as a medium to improve the services offered to the business sector.

Similarly, the Talent Management department has developed the technical criteria and competencies required to follow the career progress of employees. Talent Management has further executed several program and courses, the most important of which were related to retail banking, credit and risk management. As a result, it provided 16,679 training opportunities in 2015.

During 2015, Riyad Bank Program provided 7 specialized courses tackling the fields of finance, operation , branch services and Golden Banking, business technology and governance, credit, treasury, risk management, internal audit and compliance.

Moreover, 2478 branch employees have been trained to obtain the Professional Certificate in retail banking basics.

The balances of the staff incentive program and movements in 2015 are shown below:

(SAR'000)

	Investment Saving			
Description	Staff's Share	Staff's Share Bank's Share		
Balance at the beginning of the year	39,627	14,798	54,425	
Provided during the year 2015	9,336	3,490	12,826	
Charged during the year 2015	(10,788)	(4,084)	(14, 872)	
Balance at the end of the year	38,175	14,204	52,379	

### **External Auditors:**

The Annual General Assembly of the Bank's Shareholders held on 6<sup>th</sup> April 2015 approved the appointment of KPMG (Al Fozan & Partners) and Pricewaterhousecoopers ME as joint external auditors for the financial year ending 31<sup>st</sup> December 2015. The General Assembly will decide in its upcoming meeting whether to reappoint the current auditors or replace them; the General Assembly will also approve their fees for reviewing the Bank's financial statements for the financial year ending 31<sup>st</sup> December 2016, after reviewing recommendations made by the Audit Committee and the Board of Directors.

### **Acknowledgements:**

We would like to take this opportunity to extend our profound thanks and gratitude to the Custodian of the Two Holy Mosques, His Royal Highness King Salman bin Abdulaziz Al Saud and and His Royal Highness Prince Mohammed Bin Naif Bin Abdulaziz Deputy Prime Minister and Minister of Interior and

His Royal Highness Mohammed bin Salman bin Abdulaziz, Second Deputy Prime Minister, Deputy Crown Prince and Minister of Defense as well as the government. Much is owed to the Ministry of Finance, the Saudi Arabian Monetary Agency (SAMA) and the Capital Market Authority (CMA) for their continued assistance and support to the banking and financial institutions sector.

Our appreciation also goes to our shareholders, customers and correspondents for their valued support and confidence which motivates us to consistently exert more effort and commitment. Finally, we extend our thanks and appreciation to the Bank's staff for their dedication, loyalty and outstanding performance that were, and are, directed to achieve Riyad Bank's goals and objectives.

The Board of Directors

Riyadh, February 1, 2016 Rabi Al Thani 22, 1437H

# INSPIRATION INGENUITY PLANNED VISION ABILITY OBSERVATION THOUGHTFUL EXPERTISE



## SUMMARY OF ACCOMPLISHMENTS IN 2015

### **Retail Banking Services:**

2015 was marked by a series of successful accomplishments in the retail banking services. This was evident in the Bank's decision to restructure its auto leasing products, by signing new agreements with strategic automobile dealerships and service providers. Accordingly, 8 new after-sale centers were established in key cities across the Kingdom, which reflects the Bank's ambitions towards expansion and pioneering. The Bank also launched a new automated system that enables customers to obtain preliminary financing approval within minutes through its sales agents at automobile dealerships in order to take the customer experience to new levels.







In terms of personal finance, the Bank launched a new Murabaha shares finance product catering to different segments that prefer trading in Shariah compliant equity shares, instead of commodities, for their immediate lending needs. Moreover, the Bank launched a supplementary mortgage product in coordination with Real Estate Development Fund (REDF); becoming one of the first institutions to obtain the approval of SAMA to launch a new mortgage product "Ijara Mousofa Bel-Thema" for off-plan properties through real estate developers.

An achievement for Riyad Bank in 2015 was the issuance of MasterCard Debit Card, in partnership with MasterCard International. The new card is an update of Maestro ATM card and is accepted at over 40 million outlets worldwide. The MasterCard Debit Card comes in four categories: Silver, Titanium, Platinum and World, all of which are tailored to meet the needs of various segments of customers, Private, Gold and Mass, such as access to more than 600 lounges at airports around the world, as well as access to local and international offers and services by MasterCard.

Another accomplishment for the Bank in 2015 was the new 'Contactless' feature added to the MasterCard Debit Cards, whereby the cardholder does not have to swipe or insert the card through any POS machine, all they have to do is pass it near the sensor of the machine. This feature adds flexibility and more protection to the use of the card. To facilitate the process of issuing the new cards, all Riyad Bank branches around the Kingdom were provided with new machines that can print the new Contactless MasterCard Debit Cards.

More to 2015, Riyad Bank signed an agreement with Visa International. Such an agreement will incorporate the massive local, regional and international experience of Visa International and shall pave the way for more digital payment options. The agreement will bring Riyad Bank Visa cardholders several offers and advantages provided by Visa around the world.

Part of its innovative bundle of digital products, Riyad Bank issued a new Virtual electronic card. The card can be used for online shopping on any website that accepts Visa cards in an easy, safe manner without the need to issue the conventional plastic card. To further enrich customer experience, the Bank facilitated the process of applying for the new Virtual card through Riyad Online website. This comes in line with the Bank's efforts to leverage its relationship with such experienced partners as Visa International in order to provide the Bank's customers with products and services that add value to their experience in dealing with Riyad Bank.

Electronic Banking at Riyad Bank was characterized by incessant efforts aimed at widening the offering of innovative financial solutions by introducing new electronic channels. The Remote Banking Team launched 'Riyad Token', a fast and secure solution when using Riyad Bank e-channels without the need to connect to internet or a GSM network. The application enables the Bank's customers to authenticate important banking transactions, such as logging in to electronic channels, making financial transfers or paying bills and government fees. Riyad Token app generates a one-time password (OTP) instead of the usual authentication methods through a mobile phone or a separate token. The new app is a friendly option for all smartphones, regardless of





their operating systems, making the authentication of banking transactions easier and safer.

The 'Live Chat' service, incorporated to the Bank's website and Riyad Online, is yet another innovative interactive channel added to the Bank's services. Such a service elevates the prompt response to the questions and queries of customers.

During 2015, Riyad Bank's website, <a href="www.riyadbank.com">www.riyadbank.com</a>, witnessed an increase in interactive services. To mention a few: applying for new products where the visitor is given an order number instantly, 'Call me back' service where the visitor is given the flexibility of choosing the best time to receive a call from one of the Bank's representatives, and 'Send a query' service for visitors who prefer text

communication whereby they receive answers to their queries by email.

When it comes to ATMs, the Bank added 339 new machines to its network and was present at 11 events with its mobile ATM vehicle.

### **Ladies Banking:**

With the increasing market share in Ladies Banking, and in line with the Bank's strategy for expanding the ladies branches throughout the Kingdom, as a response to the growing size and needs of this important sector, 6 new regions were added to the existing 3, thus bringing the total number of regions for Ladies Banking to 9, comprising of a total of 79 branches, in addition to 2 self-service centers in Jeddah and Khobar.





### **Islamic Banking:**

Riyad Bank continued its march during 2015 towards developing banking solutions and products that are compliant with Shari'ah and are approved by the Bank's Shari'ah Committee. The Bank's Islamic products and solutions cover the daily transactions, financing and investment solutions for its retail and corporate customers.

The Bank saved no effort in improving human resources involved in the provision of Islamic banking services, raising the efficiency of their performance through more training and regular assessment of the performance of the Islamic banking branches through more than 50 follow-up visits.

2015 also witnessed 8 meetings with the Shari'a Committee for Islamic banking through which a number of financial products and solutions in accordance with the "Murabaha" and "Ijara" (rental) formats were developed. The Bank has also adopted the terms and conditions of issuing Islamic credit cards in addition to hedging products in the Treasury Division. It has further worked on integrating the investment solutions provided by Riyad Capital including Riyad Bank 'Sukuk' and Maaden Phosphate Company 'Sukuk' and Riyad Real Estate Income Fund.

### **Private & Golden Banking Services:**

It is all about modernism and elegance when Riyad Bank's Private and Golden Banking services are mentioned. All the Bank's products and services in this area are based on extensive analysis of customers' needs and expectations which have always been the focus of the Bank.

The Bank has 4 Private Banking centers and 60 Golden Banking centers which were designed to

service this segment through an experienced team to cater to all their needs.



4 PRIVATE
BANKING
CENTERS

Golden
Banking
Centers

### **Overseas Branches:**

Through an overseas banking network represented by our branch office in London, the Houston agency, and the Singapore Representative Office, Riyad Bank provides banking solutions to its customers abroad, serving the corporate customer base, and allowing the Bank to provide its customers with tailored services to meet their various needs. In addition, the Bank provides advice on investments and business in the Kingdom of Saudi Arabia. This leads to enhanced trade in the Kingdom and customers' investment interests abroad.

The London Branch plays an active role in supporting the rapid growth of commercial activities carried out by the leading European multinational companies with the Kingdom. This support ranges from providing letters of guarantee and stand-by letters of credit, as well as assisting in the provision of financing for their business in Saudi Arabia. In addition to this, the London Branch also provides tailored banking services to the Bank's customers in the Kingdom and their affiliated companies in order to support their European investments in industry and other sectors.

Riyad Bank is the only window for Saudi banks in the Americas, where the Houston Agency plays an important role in attracting investments to the region, as well as helping U.S. and multinational companies to support their commercial activities in the Kingdom of Saudi Arabia. In addition, the Agency supports Saudi companies doing business in North America.

Riyad Bank is also present in the Far East, where our Singapore Representative Office helps Riyad Bank customers take advantage of investment opportunities in Asia, and to develop relationships with correspondents and Asian corporations who have business activities in Saudi Arabia.

### **Corporate Banking:**

Corporate Banking has always operated following a clear vision "we will be a reliable and a strategic partner for our customers, offering them a distinct business environment supported by a top quality customer service". The Corporate Finance Department serves as the Bank's center of expertise for syndicated, structured and project finance operations. The department works in close coordination with the Bank's domestic network and with the offices in London, Houston and Singapore to provide products and services to the Saudi corporate community and to a wider network of global corporations with investment and trading connections in the Kingdom.

The Financial Institutions Department acts as a focal point for managing all aspects of Riyad Bank's relationship with corresponding banks and non-banking financial institutions by providing them with investment and insurance services, and financing solutions in the form of Ijarah, in addition to a broad range of tailored products and services designed to meet the needs of such a sector.

Riyad Bank continued to stand out due to its large network of corresponding banks needed to facilitate the international banking needs of its retail, corporate and institutional customers, while offering competitive rates with emphasis on quality of service.

The Bank maintained its position among the top contributors to KAFALAH program for financing small and medium enterprises. In this respect, the Bank's share was SAR 3.2 billion, equivalent to 25% of the total amount offered through the program. This amount covers 1,764 enterprises, constitutes 26.5% from the total number of enterprises from the beginning of the program until the end of the third quarter in 2015.

Riyad Bank continued to be active in the local market through the selection of notable financing transactions. The Bank therefore was appointed as the global facility agent and mandated lead arranger for the Saudi Aramco USD 10 billion Standby facility, the largest bank facility ever arranged for a KSA company.

Riyad Bank also acted as the agent for syndicated loans and custodian. It was also the holder of a number of local and international accounts of industrial, infrastructure and real estate projects. In this regard, the Bank was the general agent for 27 financing facilities with a value exceeding SAR 63 billion.





In the same year, Riyad Bank was appointed mandated Islamic lead arranger for the Petro Rabigh 2 expansion project, at a value of US\$ 1.87 billion. It has also succeeded in winning the bid for managing and executing the Investment loan program launched by the Real Estate Development Fund.

Given the Bank's keenness to provide its customers with a top notch banking experience, the Bank planned and executed several research assignments with corporate banking customers to better identify their needs and to improve the services offered to them. The results of these surveys were used to launch a new initiative under the Customer Experience program.

Corporate Banking played an integral part in the Bank's overall growth, by activating the role of cash management and trade finance through restructuring the products and dividing them

into various categories that resonate with the ever changing customer needs in electronic payments, prepaid cards and cash management and allowing to reach such products via advanced electronic channels.

Significant success was achieved by the Bank in prepaid cards, especially cards tailored for staff salaries and student allowances, which offer a number of services such as bill payment, settlement of government fees as well as purchases through Points of Sale (POS). During 2015, Riyad Bank further expanded its Point of Sale (POS) network by adding a large number of retailers, achieving a growth rate of 100%, reaching more than 40,000 POS.

Riyad Mobile Business app is another achievement for the Bank in electronic services. It is the first application in Saudi Arabia designed to help corporate customers manage their business online through smartphones, anytime and anywhere. Two other services especially made for corporate customers were also launched in 2015: SADAD safe payment services and cash deposit machines.

On the trade finance front, the Bank introduced many improvements to its work processes by automating the execution of operations and by developing Riyad Online Corporate, which allowed the customers to execute their transactions in a shorter period of time.

### **Treasury & Investment Division:**

The Treasury and Investment Division plays a pivotal role in managing the Bank's liquidity and funding requirements, as well as managing the interest rate and foreign exchange risk exposure within the limits approved by the Bank, and managing the investment portfolio and providing financial hedging products and solutions to the Bank's customers.

In line with the Bank's overall cross-selling strategy, the division has been aligned and focused on a cross-selling initiative to widen and diversify its customer reach. The expansion of the cross-selling initiative shall also provide Corporate and Private customers with innovative hedging solutions for interest rate and foreign exchange exposure. During the year, the division's cross-selling initiative was a major success; posting a strong growth rate in deal volumes as well as revenues.

Also during 2015, Treasury and Balance Sheet Management unit under ALCO supervision managed the issuance of SAR 4 billion sub-ordinated Tier II Sukuk to strengthen the capital base of the Bank, to reduce maturity mismatch risk and diversify funding sources. This was received with high interest from investors which reflects the Bank's financial strength and investor's trust.

### **Investment Portfolio:**

Riyad Bank's investment strategy focuses on the quality, diversity and liquidity of the assets allocation process under the supervision of the Bank's Investment Committee. The Bank's investment portfolio consists of diversified local and international assets with investment in fixed income in government and corporate bonds constituting the majority of the assets. The investment portfolio has generated good returns in 2015.

### **Risk Management:**

The Bank continues to adopt the standards of corporate governance in accordance with local statutory and regularity requirements and also follows the developments internationally in corporate governance codes and practices to support the Bank's policies to manage risk according to accurate and well-founded standards.

Financial crimes constitute a serious threat on financial institutions and their employees, and if arise, might cause damage to the Bank's strength and negatively impact the delivery of its services and weaken the trust it has with the regulatory authorities, customers, business partners alike. This will also keep the Bank exposed to continued threats and might damage its reputation locally and internationally. Thus in 2015, The Financial Crimes Prevention Department was set up under Risk Management as part of its comprehensive program to improve controls and methods to combat money laundering, terrorism financing, and fraud.

### **Credit Risk:**

Financial institutions are facing a multitude of challenges the foremost of which is credit criteria in addition to insufficient assessment of changing economic conditions which could lead to deterioration of the credit standing of customers. Credit risk appears when there are indicators of the inability or failure of borrowers to meet their contractual commitments. Riyad Bank manages these risks by conducting in depth and thorough analysis of the borrower's ability to honor his obligations which would include repayment sources, the nature of underlying collateral and other factors and conditions impacting the borrower's activities.

The Credit Risk Management framework, within which the Bank operates, consists of principles, structures, tools and activities required for managing credit risk at all levels. This framework supports the Bank's efforts in enhancing asset quality while observing the rules and regulations set by the Saudi Arabian Monetary Agency (SAMA), all within clearly designed and regularly monitored risk parameters. In addition, the other related departments supervise the execution of credit strategy and risk appetite levels by setting a clear plan for identifying,

establishing risk tolerance parameters, along with monitoring and reporting mechanisms for credit risk at the Bank. The Bank continually assesses and monitors credit exposures to ensure timely identification of potential credit problems.

The Bank utilizes sophisticated credit software systems to ensure management of credit applications, limits management, and collateral management. In addition the Bank uses an advanced internationally recognized credit rating system to assess the viability of corporate credit applications and produce their credit ratings according to the rating system that is approved by the Board of Directors. The Bank also uses an advanced retail credit system for Retail Risk.

Currently, the Bank is focusing on strengthening its infrastructure and developing an automated system for early warning notification to start reviewing credit portfolios and take the necessary corrective measures before it gets affected.

In accordance with SAMA regulations, the Bank is in compliance with all Basel requirements in respect to capital adequacy calculation to cover credit risk according to the Standardized Approach. Following the success in developing credit rating models as per Basel III requirements, the Bank made further progress in 2015 towards the implementation of Internal Rating Based (IRB) standards as a second alternative.

The Bank established a system for validating these models on regular basis. In 2015, the Bank went through another round of independent periodical tests to validate the outcomes of these credit rating models and its quantitative and qualitative components in line with SAMA expectations. Further, the Bank established the infrastructure to

use and operate these models in taking credit related decisions depending on a precise measurement of credit risks and the expected return from these risks. At the same time, the Bank completed the review of approved risk policies to further assure that credit rating systems meet IRB standards.

At the same time, the Retail Risk department has taken final steps in implementing the Advanced Internal Ratings-Based (AIRB) standard that is compatible with the Basel requirement as mandated by SAMA, which include defining governance structures as well as most updated credit policies. The department has also undertaken an enterprise level assessment of its existing credit risk systems and tools to better measure risk adjusted return. This assessment will benefit the customer's experience by adopting a digital strategy which provide customers with fast and easy access to e-banking services.

### **Market and Liquidity Risks:**

The Market and Liquidity Risk Management Department, which is part of the Risk Management Division (RMD), assumes the responsibility of measuring and monitoring market risks, and asset/liability risks resulting from the fluctuation in fair values or future cash flows of financial instruments due to changes in market prices within the Board's approved risk framework and limits. Periodic reports were prepared and submitted to the relevant stakeholders at the Bank.

The primary market risk measure used within Riyad Bank is the Value-at-Risk (VaR) methodology, which incorporates the volatility of relevant market prices and the correlation of their movement. In addition, the Bank implemented a number of standards

and other advanced methodologies to enhance its analytical capabilities in managing market risk including stress testing and sensitivity analysis. The Bank also continued to implement its strategy in compliance with Basel's Internal Model (IMA) Approach to measure and manage market risk.

During 2015, the Bank continued to align its market risk management processes to the new guidelines of SAMA regarding liquidity risk management and improving mechanisms to gather, analyze and present risk data.



### **Operational Risks:**

Operational risks play a vital role within financial institutions, especially after the rapid growth of banking services which fully depend nowadays on information technology and communications that cover all aspects of life. Operational risk can be defined as deficiency resulting from inadequate or failed processes, people or systems. Therefore, Operational Risk Management ensures the application of SAMA instructions regarding risks resulting from deficiencies in operations, systems, infrastructure or human errors. During 2015, the department worked on activating a range of

precautions to raise the efficiency of the Operational Risk Management department which included the following:

- Upgrading and updating essential operational risks management systems as well as increasing its efficiency through automating the Risk Control Self Assessment (RCSA) as well as risks control. In addition to providing a comprehensive view of the current risks in the form of periodic reports supported with charts and diagrams to evaluate risks of every department and division at the Bank, while ensuring that the risks standards are compliant with Basel (3) requirements.
- Implementing a bank-wide Risk Control Self Assessment (RCSA) methodology across all business lines. The RCSA plays an important role in the detection of control gaps and serves as a strong and effective internal control tool.
- Completing a comprehensive evaluation of the Internal Control framework for its Control Environment, Risk Assessment and Management, Institutional Controls, Accounting, Information and Communication Systems, and Self-Assessment and Monitoring, Reporting and follow-up pursuant to the Bank's internal control quidelines.

During 2015, the capital adequacy ratios were continually monitored to prevent any operational risks. The Bank works in accordance with the standardized approach under the Basel II requirements, and is gradually preparing itself to meet the Advanced Measurement Approach (AMA) requirements for operational risk using the Value at Risk (VaR) model.

### **Stress Testing:**

The Bank implemented an overarching Stress Testing Framework in 2015, covering all material risks relating to banking activities under the oversight of the Board of Directors and that was after enhancing the policies, frameworks and rules of governance related to it. Under this framework, risk owners reviewed the stress methodologies along with their assumptions to maintain efficacy of the stress models deployed.

### **Internal Control Department:**

During 2015, the Bank continued to emphasize its commitment to the best standards for internal control and the full compliance with the requirements of the Saudi Arabian Monetary Agency (SAMA). Riyad Bank has been incessantly improving the elements of governance and internal control in order to integrate the risk management systems into internal control and raise the general awareness. Amongst these efforts came the establishment of the Internal Control Department that reports directly to the Chief Risk Officer .

The Internal Control Department is responsible for collecting the information from different areas, both internal and external, classifying them and analyzing their importance. The Internal Control Department follows up on the necessary plans to reinforce the internal control system. It further defines the criteria upon which the annual attestations , presented by the executive management and control units about the soundness and efficiency of the internal control system.

The department prepares internal control reports to the Audit Committee and executive management and also to the Operational Risk Management and Compliance (ORMSS). At the executive management level, the internal control indicators were linked with performance standards. The Bank's divisions have also finished the application of control risk self-assessment of risk and internal control procedures by the divisional controllers who were assigned the responsibility of performing continuous tests to adjust, improve and enhance procedures and policies applied inside each division.

### **Credit rating:**

Riyad Bank succeeded in maintaining its distinct credit ratings with world rating agencies. With the Kingdom of Saudi Arabia witnessing a lowering in its ratings from (AA-/A-1+) to (A+/A-1), the Bank had its ratings consequently modified by Standard and Poor's Financial Services from (A+) to (A) for long-term commitments, while maintaining its rating (A-1) for short-term commitments, which is the highest rating there is. The overall outlook also changed from stable to negative in line with the sovereign rating. Having had such slight change in ratings, Fitch Ratings kept its ratings for Riyad Bank as (A+) for long-term commitments and (F1) for short-term commitments, which is the highest rating there is. From its side, Capital Intelligence, affirmed its ratings for the Bank as (AA-) for long-term commitments and (A1+) for short-term commitments, which is the highest rating there is. The last two ratings anticipate a stable future perspective for the Bank which in turn reflects the strength and durability of Riyad Bank's financial position.

### **Business Technology:**

During 2015, Riyad Bank carried out significant accomplishments in the area of Information Technology. The most prominent achievement was

the Datacenter Relocation Project. The datacenter contained all the Bank's data related to transactions and customers

The new data center is highly designed and supplied with state-of-the-art equipment to enhance the speed and efficiency of performance. The Centre uses fiber optic communication systems that enhances the effectiveness of Riyad Bank's channels and raise the protection of its databases and its transfer mechanism.

The center is considered a smart and environment friendly venue; having fire protection and multi protection systems to combat any disasters, accidents or breakthroughs. According to Uptime indicator, the new datacenter building obtained the highest rating in the Saudi market (A+).

Furthermore, the Division successfully migrated Mypay and Alawal customers to the new Card Management System, which is fully compliant with the Saudi Arabian Monetary Agency (SAMA) prepaid cards regulations. This initiative enabled the prepaid cardholders to make bill payments through ATM Channels.

Hours

Big Bang execution phase for data centre relocation project



### **Business Technology Governance:**

The Business Technology Governance has occupied an important position in managing the risks and securing the Bank's business. The Bank has paid special attention to build a well-controlled system, which has witnessed many accomplishments during 2015.

The Bank obtained the ISO Certificate for Information Security Management . The ISO 27001:2013 audit conducted by BSI (British Standards Institution) for Riyad Online services was completed successfully without any non-conformities or observations. Riyad Bank was the first bank in KSA to attain ISO certification. The Bank has further taken action towards assuring that governance and risk management are in line with information security policies. This initiative enhances the Bank's infrastructure to comply with any future requirements, enhancing business management while limiting risks related to information security.

The Business Continuity department continually carried out Business Continuity Assessment for Riyad Bank Business Continuity Process; allowing a 360 degree analysis of the process to boost and enhance the Bank's services in accordance with international standers applied by competitors

The department also implemented the Business Continuity Lifecycle Automation System (BCLAS), that positions Riyad Bank ahead of its peers locally and internationally. The project has provided the necessary capabilities for the continuity of banking systems and it is now in its final stages. This allows crises management to carry out business in an efficient way while making the Business Continuity Processes more transparent and accountable.



### **Compliance Department:**

Riyad Bank endeavors to maintain a sound compliance culture and a business strategy whereby the Bank's values and standards of professional conduct are maintained at every business level and within all its activities. These standards include local, international regulatory obligations, as well as the best practiced business standards and Riyad Bank's own internal regulations and codes of ethics and standards.

Riyad Bank's Compliance Department has been always committed to the betterment of the Bank's Compliance Control Environment, as well as the implementation of an effective compliance program

which includes monitoring, advice and regulatory services. The Compliance Department aims at meeting the new requirements for initiatives such as Deposit Protection Fund, the new update of credit card and prepaid card regulations, the consumer protection laws and regulations for financing companies, Saudi Payment Network "MADA" Operating standards, the new amendments to the labor law, in addition to any updates to the SAMA Anti Money Laundering and Counter Terrorism Financing and Account Opening & Operating Regulations.

On the international front, the Bank continued its commitment to meet recommendations of FATF, and abide by the OFAC enforcements in order to combat money laundering and financing terrorism, as well as the financing of proliferation of weapons of mass destruction. The compliance department was also actively engaged with the local specialized authorities in fulfilling the implementation of FATCA requirements and complied by meeting the requirements of 2015 in that respect.

Moreover , the Compliance Department has been committed to following it's ongoing strategy striving to the highest standards and methodologies when it comes to Monitoring Compliance Risk in the Bank, a risk based monitoring plan was further developed and executed for 2015, and the plan was approved and monitored by the Board Audit Committee.

### **Human Resources:**

Building a great organization such as Riyad Bank requires a strong human resources structure. In this context, the Bank finalized restructuring and determining specifications for career paths within its 3 years workforce plan which aims at developing the organizational structure.

As the Saudization process is concerned, Riyad Bank is considered a pioneer. Saudi employees have been increasing over the years until the percentage reached 93.5% in 2015, the Bank aims to increase the percentage in the future. The Bank is also proud to have 100% Saudi women employees as the percentage of female Saudi employees increased to 25% of the total number of employees in the Bank, and the positive increase is ongoing.

Given the importance of human resources development, the Human Resources Division has drawn a strategic plan to support the activities needed for the development of skills. The plan operates by determining the requirements for each job and providing it with the necessary skills through internal and external training.

The Human Resources Division has worked always within its vision which is for the Bank to be 'the prime choice for employees'. Through such vision, the division navigates to develop its structure and set the programs related to succession planning, such as 'Riyad Bank's Program'. The division has been providing latest technological services for its staff services some of which are the 'iRecruitment system' and the 'performance appraisal system'.

The Human Resources is a strategic vital partner to all the Bank's sectors. To guarantee the success and sustainability of such partnership, the Bank has started the 'business partner management' as a medium to support the divisions of the Bank in all the services offered to them.

As part of Talent Management's continuous effort in providing the Bank's employees with their training and development needs, Talent Management has

prepared the technical competencies for all the Bank's divisions and departments linking them to the relevant jobs; hence helping in drawing a career progression chart for all the employees. In addition to that, Talent Management executed several programs and courses in numerous fields providing 16679 training opportunities; focusing on the primary banking business the most important of which were related to retail banking, credit and risk management,.

During 2015, Riyad Bank Program provided 7 specialized courses tackling the fields of finance, operation, branch services and Golden Banking, business technology and governance, credit, treasury, risk management, internal audit and compliance.





Moreover , 2478 branch employees have been trained to obtain the Professional Certificate in retail banking basics.

### **Marketing & Communications:**

2015 witnessed the successful launch of several key marketing programs for various Retail and Corporate products and services, like Riyad Mobile Business app, MasterCard debit card, POS solutions, and many other activities, using conventional and modern media, supported by social media. This lead to an improvement in the marketing campaigns results in terms of awareness, reach and engagement. The mix of conventional, digital and social media helped in consolidating the presence of the Bank and its competitive capabilities within the Saudi banking industry.

In addition, the Marketing Division developed two of its key departments - Digital Marketing and Marketing Intelligence. The evolving market needs and the changes in media scene and the consumption habits of conventional and digital media implied the empowerment of the Digital Marketing Department with necessary tools and resources to face the challenges of the day and the future. There were remarkable improvements in the Bank's presence on various social media platforms in 2015, where fans and followers on Facebook and Twitter doubled in size compared to the previous year. The Bank's page on LinkedIn was activated to help position Riyad Bank as a favored employer of choice. On average, throughout 2015 the Bank managed to maintain a leading position on the list of most socially influential banks in Saudi Arabia.

Another achievement for the Bank was the high level of visibility and accessibility of the public website across search engines, like Google, which

resulted in an increase in traffic to the website (25% growth in number of visitors compared to 2014) and subsequently an increase in leads generated through the website.

On the other hand, the Marketing Intelligence Department extended support to all the Bank's divisions by providing them with meaningful market, industry and product insights and learnings to help them with their decision making process. In 2015, the department managed to complete more than 87,000 phone calls with customers to measure their level of satisfaction and loyalty through a scheme known as "Net Promoter Score". The department also conducted 24 focus group discussion sessions with area managers and 240 in-depth interviews with frontline employees to measure, identify and recommend actionable solutions to enhance the quality of service at the branches.



25% GROWTH IN NUMBER OF VISITORS TO THE WEBSITE

A key objective for the Advertising & Media Relations Department is to support the image of the Bank and its products and services in local and regional media. In this respect, the department released 167 press releases, which were published 1,230 times in newspapers and major websites, in addition to 42 press supplements in 2015. The department shed the light on many retail and corporate banking products and services, and achieved a distinct media exposure for a multitude of community service programs.

One of Riyad Bank's most important objectives is to satisfy the needs of customers and exceed their expectations, which is an area of focus for the Quality Assurance Department. In 2015, the department implemented a series of advanced tactics and techniques to ensure quality and improve performance, and to make sure that quality improvement is a continuous process. In order to do that, the department restructured itself to focus on quality assurance requirements across various operations at the Bank. The Quality Assurance Department undertook several actions in view of cultivating a sustainable quality culture within the Bank, such as developing robust Service Level Agreement (SLA) metrics to cover internal and external stakeholders responsibility with regard to service quality and ensuring its seamless linkage with a cohesive service strategy. Moreover, the department was assigned the responsibility of supervising the quality of service at the branches, ATMs, and the Bank's electronic channels, and preparing internal reports that highlighted areas of improvement with a clear follow up with related stakeholders in order to invest in the identified opportunities.

### **Enhancing Customer Experience:**

Following the successful establishment of a Customer Experience Department in 2014, the

team begun to design and implement its strategy. Accordingly, the Customer Experience Team was always present to ensure that the design of the Customer Experience is underpinned by deep meaningful customer insights, and that the products, services and processes are designed around customer needs.

During 2015, the Customer Experience Department had key achievements, among which was the implementation of Net Promoter Score methodology that measures customer satisfaction and loyalty. The team also led a study that focused on the different segments of the market. The study aimed at setting a better understanding of the requirements and behavior of customers upon which the Bank's services and products are designed. The team was a main contributor to the branches' services quality improvement program; developing the procedures of financing requests, issuing ATM cards and updating current accounts.

Early in 2015, the department inaugurated the research lab which is the first of its kind in the Kingdom. The lab is responsible for performing tests on the Bank's services and products in addition to studying their effect on actual customers before introducing them to the market. Moreover, many electronic services were subject to the live experience.

### **Community Service:**

Following in the footsteps of past years, Riyad Bank continued to pursue new horizons and achievements, that reflect the Bank's active role in community service and its contribution in supporting comprehensive growth and sustainable development.





Ensuring that previous programs and accomplishments in community service initiatives are maintained and built upon, the Bank also focused throughout the year on improving its delivery mechanisms through a process of regular evaluation.

Thus, in the field of healthcare, the Bank distributed medical equipment and supplies to the less fortunate and needy through a partnership with the Patients' Friends Committee and General Directorate of Health Affairs who oversee the distribution of supplies in a professional manner.

As a continuation of "the charitable project for transportation", the Bank donated two especially equipped buses to transport patients for the benefit of the Patients' Friends Committee in Jeddah. The other two were donated to the King Fahad National Centre for Children's Cancer and Research in Riyadh.

The Bank also sponsored and participated in numerous activities related to healthcare awareness to educate the public about the importance of maintaining a healthy lifestyle. These activities included sponsoring breast cancer awareness campaign for Zahra Breast Cancer Association for the 8th year in a row, the Saudi Stroke Association awareness campaign, "Naqa" Anti-Smoking Society campaign, as well as "Nebras" the National Committee for Combatting Drugs, in addition to participating in the Saudi-American Healthcare Forum. The Bank staff also showed their support by participating in the blood donation campaign for the benefit of Children's Cancer Support Association "Sanad".

Furthermore, the Bank spearheaded several initiatives aimed at developing the skill set and abilities of special needs individuals. Some of the most notable examples include the "Momken" initiative - a program which aims to stimulate the capabilities of people with special needs, develop their skills and empower them to integrate in society. In partnership with the Ahsa Handicapped Society and the Irrigation and Drainage Authority, the Bank celebrated the graduation of 15 farmers as part of its 4th season of sponsoring this farming training program that focuses on qualifying individuals with simple mental disabilities to enter the job market.

Similarly, the Bank partnered with the Riyadh Al-Shabab Club to sponsor the 9<sup>th</sup> season of the summer training program for people with special needs. **This resulted in establishing two centers in Bahaa and Hai'l** with the collaboration of the Handicapped Society in Bahaa and HADCA association for special needs in Hai'l.

Supporting the sports achievements of people with special needs, the Bank sponsored the

ceremony recognizing and commemorating the accomplishments of the Kingdom's special needs team in the Eastern Province. Similarly, the Bank launched a special initiative in Najran - under the motto 'to lighten your life' - to teach and train visually





impaired persons on the usage of smart devices. At the same time, the Bank bolstered its partnership with the Disabled Children's Association in Riyadh by sponsoring the publication of the greeting cards booklet of hand drawings done by these children with proceeds going to the Association.

Following the success of the "Productive Families Project", Riyad Bank continued to support this initiative by developing and training young females to enable them to live as independent and self-sufficient productive members of society. This included the 'Nabta' program in Al Jawf region, which was held in cooperation with Albir Society, and resulted in training 100 girls from beneficiary

families on how to use computers, learn sewing, embroidery, cooking, baking and cosmetics. Riyad Bank also sponsored the Productive Families Project in Hoya, Taif as well as 'Bawabet Al-Khair' project which was organized by the Charitable Society for Mother and Childcare in the Eastern Province in order to improve the income of productive families by selling their handmade products.

Following its yearly custom, Riyad Bank's charity caravans have spanned the Kingdom's cities and villages with the assistance of staff volunteers. During Ramadan, the caravans distributed food baskets to needy families throughout the Kingdom and partnered with various charitable organizations such as Albir Society in Hoya, Charitable Association in Najran, Albir Society in Wosayta, Aja Women's Charity in Hail.

These caravans undertook a similar mission during the winter season as part of the annual "Winter Clothing Campaign" to provide needy families in remote areas with the necessary supplies and clothing to bear the harsh winter conditions.

The Bank staff also continued with the yearly ritual of visiting ill children in hospitals and getting them gifts to lift up their spirits during the Eid holidays.

Moreover, cultural activities did not escape Riyad Bank's attention. The Bank celebrated the 8<sup>th</sup> Book of the Year Award in partnership with the Riyadh Literary Club. The 2015 award winners were Dr. Abdullah Al-Monef and Dr. Hind Al-Motairy. Furthermore, in recognition of the integral role of culture in sustainable development, the Bank sponsored the first cultural award for women through the establishment of the Women of Excellence Award in cooperation with Al Qaseem Literary Club. The winners in the 1<sup>st</sup> season were Dr.

Ghada Al-Tareef, Dr. Amina Al-Jibreen and Dr. Wafa Khinkar.

Strengthening its partnership with charities in the Kingdom, Riyad Bank took part in the campaign organized by Al-Nahda Women's Society to spread awareness of the importance of participating in the municipal elections and emphasized the role of women in Saudi society. Two further charity campaigns were supported throughout the year - Eta'am Charity's drive to spread awareness of food conservation and preservation, as well as Mawada Society's approach to reduce divorce cases.

These charities organization were supported also by the Bank's electronic channels and portals to spread the campaign messages and raise awareness. In this way, Riyad Bank's community service activities were promoted across a wider audience, while at the same time partner charities and institutions benefited from the increased coverage from using these e-communication tools and social media platforms which has a large number of users and followers.

The Bank also launched the online donation feature for customers to be able to donate directly to specific charity organizations with ease and speed after undertaking an extensive background check of these charities and its activities.

Riyad Bank sponsored events, forums and exhibitions in the fields of culture, heritage, tourism, education and economy including: the  $10^{\rm th}$  season of the International Mathematics Olympiad, the preparatory meeting for the  $6^{\rm th}$  Scientific Conference held in Princess Nourah Bint Abdulrahman University, active learning strategies forum in Tabouk third primary school, Al Qaseem Heritage Festival, the Loyalty Festival in Saihat, the Economic Forum in Jazan, the Young Merchant

program the GCC Traffic Week, the Riyad Bank Golf Championship at Riyadh's Nova Resort, the annual race held in King Fahd University of Petroleum and Minerals, the CSR Forum in Madinah, the Eastern Shores Festival, an exhibition at Al Imam Mohammed Ibn Saud Islamic University, a Prince Sultan University student initiative, the Audit and Accounting 3rd forum, the Saudi-American Healthcare Forum, the Ernst & Young award for entrepreneurs, the Investors Opportunity Forum, Al Wafaa 4th Festival in Princess Nourah Bint Abdulrahman University, the Global Village in Princess Nourah Bint Abdulrahman University, the 7<sup>th</sup> Anti-Money Laundry Conference, the "Nebras" the National Committee for Combatting Drugs, the Powering Ideas Championship for Football, the 11th Al-Dokhala National Festival, The Good Deed Gate project, the International Conference for Training and Development at Princess Nourah Bint Abdulrahman University, the "Naga" Anti-Smoking association, the Graduation Ceremony for The Disabled in the Eastern Province, the 3rd Annual Summit for Trade Finance, the College of Fine Arts and Design Departments Graduation Projects at Princess Nourah Bint Abdulrahman University, and the Eastern Province Entrepreneur Exhibition.

Finally, addressing the needs of deceased employees and their families during the year, Riyad Bank renewed its 'Wafaa' program with Al-Othaim Markets Company. An initiative specially tailored for the needy families of deceased staff members, the Bank issued prepaid cards for less fortunate families to provide them with the means to a decent life. This year the program was also expanded to address employees' children with special needs and provide them with medical support.

### **Riyad Capital:**

Riyad Capital is a Saudi limited liability company wholly owned by Riyad Bank with a paid up capital of SAR 200 million, and is licensed by the Saudi Capital Market Authority for dealing as Principal, Agent, Underwriting, Arranging, Advising and Custody Services.

Riyad Capital continuously innovates and develops investment products that meet the needs of its diverse customer base, through its Assets Management Department, which worked during 2015 on expanding its products by launching new investment fund: the 'Riyad Real Estate Income Fund' represents the 37th fund to be added to Riyad Capital's roster of investment funds. This has reinforced Riyad Capital's leadership in the assets market through its diversified investment products and large customer base. As a result, Riyad Capital boasts the second largest asset volume in the Kingdom.



SAR 4 Billion Riyad Bank's Sukuk In relation to Corporate Investment Banking, Riyad Capital is keen on attracting local professional expertise with relevant experience in all areas of investment banking advisory services, such as the management of Sukuk issuing, corporate shares, M&A and structured finance operations. One of the most important achievements of 2015 was the issuance of Riyad Bank's Sukuk with the value of SAR 4 billion, acting as the financial advisor, underwriter and the IPO lead manager for the Middle East Paper Co.

To further strengthen Riyad Capital leading role in the local and international trading , in 2015 Riyad Capital launched a new digital channel to the list "Riyad Tadawul Mobile app" that is specially designed for smart phones and tablets . Furthermore, Riyad Capital managed to gain a competitive edge by successfully signing an agreement with a specialized broker-dealer for US stock market which reflected positively on the international trading services.

In 2015, the Wealth Management Department promoted an enhanced investment culture among its customers through the value-added Investment Advisory Services that are provided to high-net-worth clients privately and professionally to help identify and tailor their investment options carefully and accurately. Consequently, Riyad Capital continued

to implement its program for building and preparing of an integrated team for wealth management, and provide technical and professional capabilities to enable this team to provide services to the company's high-net-worth clients to the fullest.

Retail Investment Department continued to provide and enhance its services via a vast network of investment centers spread throughout the Kingdom along with advanced electronic channels and call center.

### **Ajil Financial Services Company:**

Ajil Financial Services Company is a Saudi closed joint stock company subject to the regulations of the Saudi Arabian Monetary Agency. Ajil, with its headquarters in Jeddah, has a paid up capital of SAR 500 million divided over 50 million shares, with a nominal value of SAR 10 per share. Riyad Bank's contribution to Ajil's paid up capital is 35%, and the balance is held by Mitsubishi Company and a number of Saudi base businesses. Ajil Financial Services Company is a pioneering company in providing financing to capital assets, leasing advantages and many other innovative services to various economic sectors in the Kingdom, such as construction, transportation, manufacturing, trade and commerce.

### **Ithraa Al-Riyad Real Estate Company:**

Ithraa Al-Riyad Real Estate Company, registered in the Kingdom of Saudi Arabia, is a limited liability company wholly owned by Riyad Bank. Ithraa Al-Riyad Real Estate Company, headquartered in Riyadh, has a paid up capital of SAR 10 million divided over 1 million shares with a nominal value of SAR 10 per share. The company provides services for the real estate owners, and also buys and sells real estate and similar assets to support various financing solutions.





### **Al-Alamiya Cooperative Insurance Company:**

Al-Alamiya Cooperative Insurance Company, a joint stock company, founded by Riyad Bank in partnership with Royal Sun Alliance Insurance (Middle East) in Bahrain, with a paid up capital of SAR 200 million divided over 20 million shares with a nominal value of SAR 10 per share. Al-Alamiya Cooperative Insurance Company shares are traded on the Saudi Stock Market (Tadawul). The company increased its capital from SAR 200 million to SAR 400 million through a rights issue upon the approval of the Extraordinary General Assembly held on 15/03/1436 A.H. (06/01/2015). The company is regulated by the Saudi Arabian Monetary Agency (SAMA) and its operations are in the Kingdom of Saudi Arabia. Riyad Bank owns 30% of the company, directly and indirectly; directly owning 19.92% of the company shares and 21.42% of the shares of Royal Sun Alliance Insurance (Middle East). The relationship between Riyad Bank and Royal Sun Alliance Insurance (UK) goes back to over thirty years. 30% of Al-Alamiya Cooperative Insurance Company equity was offered to the Saudi public through an IPO. The Company is engaged in the commercial insurance and reinsurance business in the Kingdom, including general insurance, medical insurance, protection insurance and engineering insurance.

### **Riyad Company for Insurance Agency:**

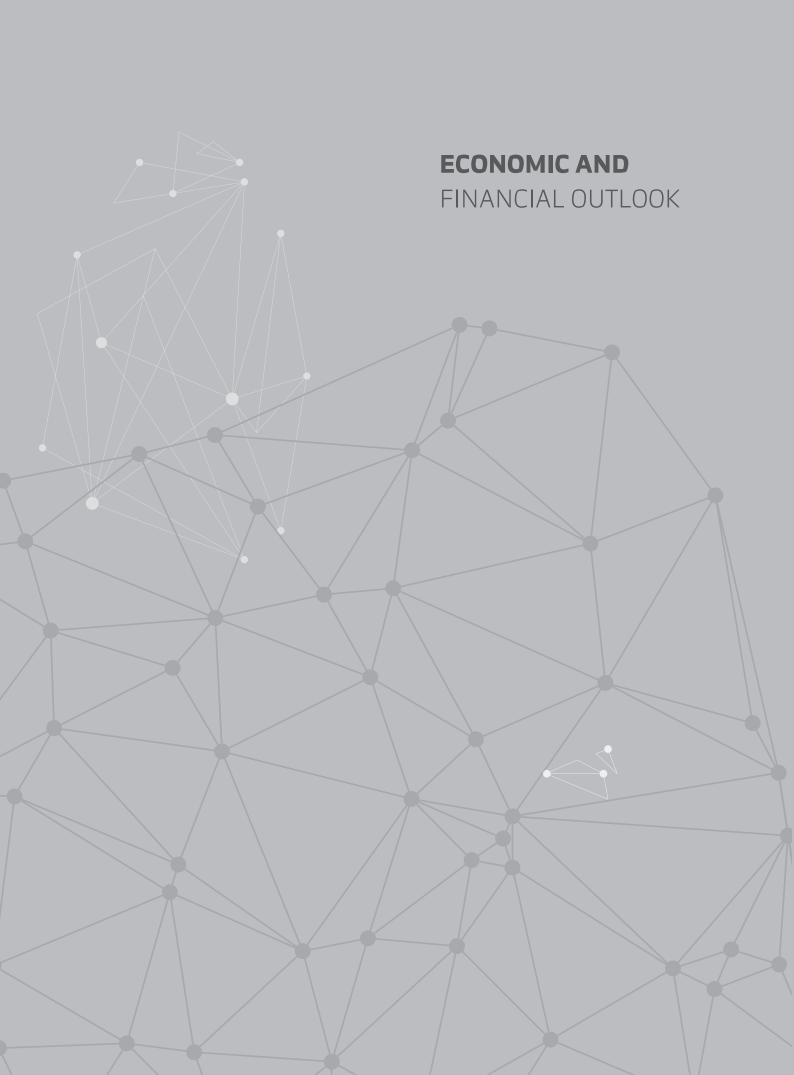
Riyad Company for Insurance Agency is a limited liability company wholly owned by Riyad Bank. Its paid up capital is SAR 500,000. Riyad Company for Insurance Agency is registered in the Kingdom of Saudi Arabia with its headquarters located in Riyadh. The agency focuses on marketing and selling the insurance products of Al-Alamiya Cooperative Insurance Company through Riyad Bank to both corporate and retail customers in the Kingdom.

Riyad Company for Insurance Agency has entered into an insurance agreement with Al-Alamiya Cooperative Insurance Company to distribute insurance products in partnership with Riyad Bank. The company is fully licensed by the Saudi Arabian Monetary Agency and operates in accordance with its rules and regulations.









# **ECONOMIC AND**FINANCIAL OUTLOOK

Growth prospects across major developed economies in 2016 have moderated but should still show some improvement from 2015.

### Introduction

Global growth remained moderate throughout 2015. However, near-term economic growth still looks stronger in advanced economies, compared with the recent past, but weaker in the emerging markets and developing economies. Within advanced economies, receding legacies of recent crises, coupled with protracted monetary policy support and a return to fiscal neutrality, have underpinned accelerating output and falling unemployment, although deflationary pressures remain. Recovery was the most progressive in the United States and the United Kingdom. The Federal Reserve Bank took significant step to normalize the monetary policy by increasing interest rates 25 basis points on December 16th, 2015, and promised a gradual normalization of its monetary policy over the year 2016. The situation in the Euro Area and Japan is still more uncertain. However, deceleration of activities in key emerging and developing economies overshadowed the modest recovery in major advanced economies in 2015. This deceleration was accompanied by further declines in commodity prices, subdued global trade, bouts of financial market volatility, and weakening capital flows.

In a development unprecedented since the 1980s, most of the largest emerging economies in each region have been slowing simultaneously for three consecutive years. The economic rebalancing in China is continuing and accompanied by slowing growth. Brazil and Russia have been going through severe adjustments in the face of external and domestic challenges. On average, activity in emerging and developing commodity exporters stagnated in 2015, as they continued to be hard hit by declining commodity

prices. As a result, the contribution to global growth from these economies has declined substantially. Worsening prospects for developing countries have coincided with a sharp slowdown in global trade, a rise in financial market volatility, and a substantial decrease in capital inflows. With the U.S. tightening monetary policy, currency pressures have intensified and borrowing costs have increased, particularly for a number of commodity exporters. Significant nominal currency depreciations against the U.S. dollar are straining balance sheets in countries with elevated dollar-denominated liabilities, where exports are likely to languish in a weak global trade environment. On the domestic front, major headwinds include deceleration in productivity growth, rising private sector leverage, depleted fiscal buffers, and heightened policy uncertainty.

In contrast to developing countries, the recovery in developed countries gained traction in 2015 and has been increasingly driven by stronger domestic demand as labor markets heal in the United States and improved credit conditions in the Euro Area. In Japan, recovery remains fragile despite substantial policy stimulus. With external demand negatively affected by a slowdown in large emerging market economies, growth prospects across major developed economies in 2016 have moderated but should still show some improvement from 2015. Risk factors include the impact of dollar appreciation in the United States, soft external demand and rising geopolitical concerns in Europe, and the impact on Japan of slowing trade in Asia. In terms of policies, the tightening cycle of the U.S. Federal Reserve is projected to be very gradual, while policy accommodation will likely continue in the Euro Area and Japan. China's gradual slowdown



and rebalancing continued in 2015, as further deceleration in sectors with excess capacity was partially offset by robust growth in services.

Global financial market volatility rose noticeably in 2015 against the backdrop of slowing activity in large emerging economies, diverging monetary policies of major central banks, continued declines in commodity prices, and fragile liquidity conditions. In this context, market adjustments to adverse or unexpected news have been abrupt. Following a correction from overvalued equity prices in China and an unexpected depreciation in its exchange rate during August 2015, the VIX index of stock-market volatility, often considered a proxy of global risk aversion, briefly surged to levels last seen during the 2011-12 Euro Area crisis. While there was no unusual stress in short-term funding markets, nor a credit crunch in any large emerging markets, the summer market turmoil led to a sharp sell-off in developing country assets and a drop in capital inflows to those economies. Additionally, currencies of key commodity exporters fell to multiyear lows both against the U.S. dollar as well as in trade-weighted terms. Since July 2015, sovereign debt spreads have widened by 45 basis points and emerging market corporate debt spreads by 80 basis points. Since October, equity markets have rebounded, and sovereign bond spreads have narrowed, although remaining elevated in many countries. Several emerging market currencies also retraced some of their losses against the U.S. dollar.

According to the World Bank estimations, global investors pulled about \$52 billion from emerging market equity and bond funds in the third quarter of 2015, the

largest quarterly outflow on record. This was mostly driven by institutional investors reducing their exposure in a sign of deteriorating confidence about long-term prospects. Net short-term debt and bank outflows from China, combined with a broadbased retrenchment in the Russian Federation accounted for the bulk of the outflow from emerging markets, but portfolio and short-term capital inflows also dried up elsewhere especially during the third quarter of 2015. Meanwhile, FDI inflows remained generally steady, although they decelerated in some economies. International bond issuance by emerging market corporates slowed significantly, particularly in the oil and gas sector. This has partially reversed the post-crisis doubling of bond issuance by developing country corporates, especially in commodities-related sectors. In consequence, some commodity firms have become highly leveraged, and are now vulnerable to a combination of rising borrowing costs and declining commodity prices.

Capital inflows to developing countries dipped to a post-crisis low relative to GDP in **2015.** They are expected to recover slowly in 2016-2017 as developing-country growth stabilizes. A gradual shift from portfolio to cross-border bank lending flows is likely to continue, supported in particular by a healing European banking sector and ongoing policy accommodation by the ECB. A gradual rise in global interest rates and continued weakness in commodity prices could affect FDI decisions, particularly in mining and exploration, while the cost of infrastructure financing is expected to rise. Based on the last estimation of the World Bank, international capital inflows (foreign direct investment, portfolio investment, and other investment) to developing countries (percent of GDP) will decline to 3.1 percent in 2015, down from 5.3 percent in 2014. It will slightly recover to 3.7 percent in 2016 and to 4.2 percent in 2017. Renewed bouts of volatility, or heightened concerns about developing country growth prospects, represent downside risks to this benign scenario.

Global merchandise trade contracted in the first half of 2015, for the first time since 2009. This was largely driven by a drop in import demand from emerging and developing economies. Growing import

demand from the United States and the Euro Area did not offset the drop in developing countries' import demand, which now accounts for half of global trade. The contraction in import demand from emerging and developing economies reflected three reasons: first, economic contractions in Brazil and the Russian Federation. Recessions in these two countries sharply reduced import demand. Sanctions against the Russian Federation further restricted trade. More generally, sharp declines in commodity prices reduced export revenues and reduced inner-demand among commodity exporters, leading to a significant slowdown in imports from these countries. Second, rebalancing in China. As a result of an increasingly pronounced shift in sources of growth from trade-intensive investment and exports toward less trade-intensive consumption and services, import growth has slowed. Third, currency depreciations. Real effective exchange rate depreciations have been accompanied by a decline in imports in several countries, but have shown so far limited benefits for exports. Estimates for trade flows in 2015 and forecasts for 2016-17 have become more gloomy, in line with the weakened post-crisis relationship between trade and activity. Persistent weakness in global trade not only diminishes export opportunities but also diminishes the scope for productivity gains through increasing specialization and diffusion of technologies. This could continue to put a cap on growth prospects, particularly for smaller and more open developing economies. According to the World Bank latest estimations, world trade volume grew by 3.6 percent in 2015, and it is expected to grow by 3.8 percent in 2016, the estimation is slashed down by 0.8 percentage points and 1.1 percentage points, respectively down from June 2015 estimations.

In light of the above conditions, the World Bank lowered its estimate for the growth of the global economy in 2015 by 0.4 percentage points to 2.4 percent, compared with a growth rate of 2.6 percent in 2014. Within the developed economies, the U.S. economy expanded by 2.5 percent, the economy of the Euro Area grew by 1.5 percent, the U.K. economy advanced by 2.4 percent and the Japanese economy achieved a growth rate of 0.8 percent. For developing countries, the World Bank estimated that China grew at 6.9

percent in 2015, the Russian economy contracted by 3.8 percent, the Brazilian economy have shrunk by 3.7 percent, whereas, the Turkish and the Indian economies grew by 4.2 percent and 7.0 percent, respectively. The instability in commodity prices, the weakness in the world trade and capital flows were the major factors that led the World Bank to update the growth rates in the down side.

In 2016, global activity is expected to slightly strengthen but the risks to the forecast remain on both sides. Global output is expected to expand at a pace of about 2.9 percent in 2016 and 3.1 percent in 2017. Drivers of the projected uptick are the strength of the U.S. economy, the realization of the positive impact of the drop in oil prices and highly accommodative monetary conditions in Europe and Japan. The U.S. economy is expected to grow by 2.1 percent in 2016 and 2017. Growth in the Euro Area will be limited to 1.7 percent in 2016 and 2017. The growth in the block will be held back by the very weak economies in the periphery and low inflation rate. The U.K economy is expected to advance by 2.4 percent in 2016, and 2.2 percent in 2017. Growth in Japan, is expected to speed slightly to 1.3 percent in 2016 in light with the continued quantitative easing and the depreciation of the Yen. Emerging market and developing economies are projected for their growth to moderate in 2016, although the expansion will be faster than in 2015. In Russia, the economy will continue to deteriorate but by 0.7 percent. The Brazilian economy will continue to deteriorate by 2.5 percent in 2016. The growth in China, on the other hand, will slow down to 6.7 percent in 2016. It will slow further in 2017 to 6.5 percent. In India, the economy is expected to speed up to 7.3 percent in 2016, while economy of Turkey will slow down to 3.5 percent. Generally, inflation will remain low in many advanced economies, while unemployment will stay relatively high in various emerging market economies.

Looking ahead, many factors will play significant roles in the growth of the global economy in 2016. The diverging monetary policy stances of major economies will continue to be a key determinant of economic growth and financial conditions in the world. Following

a first hike in December 2015, the pace of interest rate increases in the United States is expected to be gradual and notably slower than in previous tightening cycles, reflecting in part low inflation expectations and U.S. dollar appreciation. Legacies from the crisis, such as elevated household debt and weak productivity growth, also point towards a protracted period of low interest rates. Since the tightening cycle has been widely anticipated, baseline projections assume a benign impact on capital inflows to emerging and developing economies. However, as financial market expectations are susceptible to scares, risks of volatility during the Fed tightening cycle remain significant. In the same time, continued quantitative easing by the ECB and the Bank of Japan should help shore up global liquidity. Negative interest rates in Europe and increasing yield differentials with the United States could contribute to a further appreciation of the U.S. dollar and have mixed effects for developing countries. On the one hand, the increase in crossborder lending from European banks and Eurobond issuance during 2015 is likely to continue as the Euro Area recovery becomes more firmly entrenched and as bank balance sheets improve. On the other hand, continued strengthening of the dollar could contribute to refinancing pressures in countries with significant dollar-denominated liabilities.

Additionally, **continued decline in commodity** prices could also contribute to the pace of economic growth, although, it will have asymmetric impact on different developing countries. Commodity prices fell further in the second half of 2015. By November, the three industrial commodity price indexes-energy, metals, and agricultural raw materials-were down, on average, 45 percent from their 2011 peaks. Abundant supplies, due in part to investment during the decade-long price boom, and softening demand are the main factors behind the continued weakness. The appreciation of the U.S. dollar, the currency in which most commodities are traded, has also contributed to the price weakness. Conditions remain in place for a protracted period of low commodity prices in coming years. In 2016, oil prices are not projected to witness significant support, and any rise will be gradual. Metal and agricultural prices are likely to edge up in the range of 1-2 percent. While

geopolitical risks and adverse weather conditions could lead to a more rapid recovery in prices. In the case of oil, prices may come under renewed downward pressure if weakness in emerging and developing economies persists or if Iran receives substantial foreign investment to expand capacity quickly. These developments suggest continued significant headwinds for the outlook for growth, fiscal positions, and trade of commodity-exporting countries, emphasizing the need to accelerate the diversification of their economies.

#### **Oil Markets**

Oil prices posted a steep annual drop for the second year in a row as global oil supplies exceeded demand and drove down prices in the process. For 2015, the US benchmark dropped 30.5 percent, while Brent dropped 35.0 percent, marking its third straight yearly drop. The crude market is flooded with excess supplies, with US domestic production nearly doubling over the last six years, leading American congressional leaders to pass a bill to lift the country's 40-year-old ban on oil exports, a historic action that reflects economic shifts driven by a boom in U.S. oil drilling. Unconventional Canadian production and exports are also rising year after year. Russia too is producing oil at record levels to maintain its share in the market. There are signs, however, that production is falling in the US and some other oil-producing countries because of the drop in exploration investments. While US output is down from a peak in April, production has fallen more slowly in response to low prices than many investors initially expected. Companies have been able to cut costs and increase efficiency, keeping output high in a low-price environment. On the demand side, the economies of Europe and developing countries are weak, while automobiles are becoming more energy-efficient.

Another key reason for the sharp price drop is the firm decision by OPEC not to intervene to affect market forces and to keep the Cartel's production ceilings. Prices of OPEC's benchmark crude oil have fallen about 50% since the organization declined to cut production at a 2014 meeting in Vienna. On the contrary, Iraq is actually pumping more, and Iran is expected to become a major exporter again under the recent nuclear

deal. According to the Iranian officials, the country will increase the production by 500k bbl/d during the first 6 months of lifting the sanction, and the production will increase by 1.0 million bbl/d after that. Global supply of oil is currently thought to be up to two million barrel a day higher than demand. Traders fear that worsening fiscal conditions in some oil producing countries may lead them to pump more to the market in an attempt to keep market share causing greater glut of crude.

Massive buildup in global inventories and a strong dollar have also weighed on oil prices. Crude supplies in Cushing, Oklahoma, a key storage hub and the delivery point for NYMEX futures, rose to 63 million barrels towards the end of December, reaching a record last seen in April 2004. Concerns earlier in the year, that Cushing could run out of room to store oil also weighed heavily on prices. The decision of hiking interest rates in U.S. and the prospect for additional hikes have led to a higher dollar on foreign exchanges, since oil is priced in dollars that has led to a fall in the cost of crude.

A closer look to crude oil prices throughout 2015 indicates that oil market witnessed higher volatility during the year. The WTI started the year 2015 at \$52.72/bbl, \$0.55 lower than its closing price for 2014. Prices touched a year high at \$61.36 on June 10th, due to tighter global supplies and fears of oil supply disruptions from more sources. In the second half of the year, the appreciation of the US dollar after the Fed first interest hike in 9 years higher sustained increases in crude oil supply, the decision of US to lift 40-year-old ban on oil exports, in addition to lower expected global economic growth in 2015 and in 2016 contributed to a rapid decline in crude oil prices, causing WTI prices tumble to as low as \$34.55 a barrel on December 21st. Brent crude, from its side, started the year 2015 at \$57.33/bbl declining by \$1.95/bbl below its closing price for  $2014.\,Brent\,crude\,price\,touched\,a\,level\,of\,\$66.33/bbl$ on May 13th 2015, spurred by a bullish US gasoline market, output glitches, and expectations of higher global oil demand growth in 2015. However, prices started it downward trend in the second half of the year plunging to its lowest level of \$35.26/bbl also on December 22nd. The level of oil prices through the year of 2015 firmed the forecasts that prices will stay at their current averages for quite significant period of the year 2016.

By the end of the year, WTI prices and Brent crude averaged \$48.74/bbl and \$52.37/bbl respectively in 2015. Going forward, it appears to be no easing off in the supply-demand imbalance during 2016, as the OPEC and the US continue to pump oil. Given the excess supply, the outlook for oil prices in 2016 will largely depend on global demand, which is estimated to stagnate across the biggest consumers such as US, China and Japan. Macro factors like economic growth, investment returns, and geo-political risk could also sway oil prices.

The current values of futures and options contracts suggest high uncertainty in the price outlook. The likelihood of per-barrel prices for WTI falling below \$40 in the next 12 months is about 63 percent, while the likelihood of Brent falling below \$40 is around 56 percent. The probability for the crudes above falling below \$30/bbl over the next 12 months is 24 percent for WTI and around 19 percent for Brent. As an average for the year 2016, the US Energy Information Agency (EIA) expects WTI price to average \$50.89/bbl and Brent to average \$55.78/bbl. The IMF in its most updated reports uses an average price of \$42/bbl for the year 2016, while the World Bank used \$49/bbl.

After more than 18 months since the start of the oil price plunge episode, it became firmly understood that the plunge was caused by changes in underlying supply and demand conditions, amplified in the short term by a sharp appreciation of the U.S. dollar, a shift in OPEC production policy, and abating geopolitical risks. Although the supply capacity of relatively high-cost and flexible producers, such as the shale oil industry in the United States, is already adjusting to this low-price environment, most of the underlying factors point to persisting weakness in oil prices over the medium term. However, any recovery in prices from the current lows in the medium term, if it happens, it will be gradual, with an equilibrium prices remain below recent peaks and could witness more volatility. The pace of the recovery in prices will largely depend on the speed at which supply will adjust to current market conditions. Given that OPEC, for now, appears to have relinquished its role as swing producer, U.S. shale oil producers, with their relatively short production cycles and low sunk costs, may see the greatest adjustments in the short term, but could rapidly restore capacity as prices increase. This response could contribute to more volatility in prices, around a lower equilibrium level.

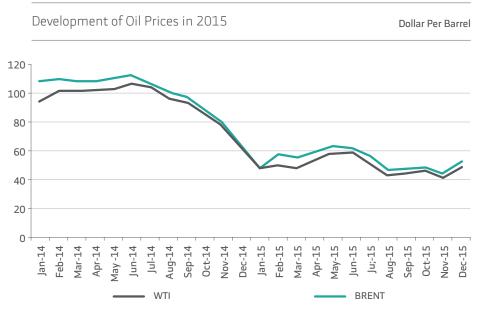
The Potential Impact of the Drop in Oil Prices on the Global Economy

According the many research including the IMF and the World Bank decline in oil prices is expected to leave favorable impact on the global economy. However, the distinction between supply and demand factors is of key importance, as the former has much more positive and lasting effects on activity. Additionally, impact will be asymmetric across countries. Net oil importing countries are expected benefit, while net oil exporting countries are expected to be negatively impacted. Even within each group, there are important differences. Accordingly, drop in oil prices will have significant

impact on policy response by each country, whether it is oil importing or oil exporting country.

The crucial assumptions in quantifying the effects of the decline in oil prices are related to the supply shift factors that impacted the prices; like how large and persistent they are going to be. These assumptions determine not only the price levels and path of adjustment, but also the initial reaction by consumers and firms.

For oil importing countries, there are three main channels through which a decrease in the price of oil affects oil importers. The first is the effect of the increase in real income on consumption. The second is the decrease in the cost of production of final goods, and in turn on profit and investment. The third is the effect on the rate of inflation, both headline and core. The strength of these effects varies across countries: for example, the real income effect is smaller for the United States, which now produces over half of the oil it consumes, than for



the Euro zone or for Japan. The real income benefits also depend on the energy intensity of the country: China and India remain substantially more energy intensive than advanced economies, and thus benefit more from lower energy prices. The share of oil consumption in GDP is on average 3.8 percent for the United States, compared to 5.4 percent for China and 7.5 percent for India.

For oil exporting countries, the impacts are mirror images of what happens in oil importing countries. In those countries, the effect of the decline in the price of oil on GDP depends very much on their degree of dependence on oil exports, and on what proportion of revenues goes to the government. The mechanical impact will be deterioration in the fiscal accounts and current accounts of the balance of payment. The adjustment will imply fiscal tightening, lower output, and a depreciation (mostly for flexible exchange regimes), and depreciation may lead to higher inflation.

The effect on core inflation depends both on the direct effect of lower oil prices on headline inflation, and on the pass-through of oil prices to wages and other prices. The strength of the pass-through depends on real wage rigidities—the way nominal wages respond to CPI inflation—and the anchoring of inflation expectations.

The dominant role of supply factors behind the current drop bodes well for its eventual impact on global activity. IMF and the World Bank estimates suggest that a purely supply-driven decline of 45 percent in oil prices could be associated with a 0.7–0.8 percent increase in global GDP over the medium term, with the effect peaking after two years. For inflation expectations, there will be a decrease in core inflation of 0.2 percentage points while headline inflation decreases by 1 percentage point.

The negative impact of sharply lower prices on exporters has been immediate. In some cases it is accentuated by financial market pressures. On the other hand, the positive impact for importers appears more diffuse across countries and sectors and has not yet fully materialized. Evidence from

past episodes shows that sharply declining oil prices were generally followed by quite diverse global growth outcomes, pointing to other important forces either mitigating or reinforcing the impact of declining oil prices on activity. With a confluence of cyclical and structural forces at work in the global economy, the expected gains for growth from the drop in oil prices could be lower than suggested by the standard estimations. These mitigating factors include current financial vulnerabilities, high indebtedness, limited room for monetary policy in major economies to be loosened further, elevated unemployment, and slowing long-term growth prospects in major oil importing economies. These factors may encourage precautionary savings by households and corporations, particularly in countries still facing important crisis legacies and weak balance sheets.

#### **The Gulf Region**

For decades, the provision of cheap energy has been a main pillar of GCC development strategy aimed at achieving key economic, social and political objectives. These include distributing the rent to the wider population; protecting the income of households, especially those with lower income; enhancing the economy's competitiveness and attractiveness to domestic and foreign investment; promoting industrialization and diversification; and controlling inflation.

While the provision of low energy prices in the past few decades has helped the GCC to achieve key developmental and social objectives, this policy has come at a cost and has resulted in some distortions. Providing energy at low prices resulted in an inefficient allocation of resources that prevent the GCC from maximizing the value of its natural resources. The negative consequences of low energy prices are well known. It result in rapid growth in energy consumption beyond what can be explained by factors such as the rising income levels and population growth. They increase energy intensity of GDP in the economy because low prices distort investment decisions towards energy-intensive projects, hindering economic diversification. It also result in low efficiency as consumers and industries have little incentive to conserve energy. Low energy prices distort energy mix by encouraging reliance on



oil and gas, limiting the penetration of alternative fuels such as renewables and nuclear power, which struggle to compete with hydrocarbons. Differences in energy prices also increase crossborder smuggling. Additionally, low energy prices are not neutral in terms of their distributional effects. Low transport fuel and electricity prices reward higher-income households, which tend to consume more. Similarly, the provision of cheap gas to industry increases profits for the owners of industrial establishments and shareholders in these companies who mostly fall within the high-income groups.

The large and sustained drop in oil prices has increased fiscal vulnerabilities in GCC countries, forcing GCC governments to rationalize their spending and implement long overdue fiscal and economic reforms, including energy prices. The UAE and Saudi Arabia are leading the GCC in raising energy prices and cutting subsidies. In a clear signal of its willingness to implement long overdue fiscal and economic reforms, the Saudi government announced plans in December 2015 to reform prices of water, electricity, natural gas and petroleum products over the next five years, raising the price of various fuels with immediate effect. This followed the UAE's June 2015 announcement to liberalize domestic gasoline and diesel prices. Since the Saudi announcement, other countries in the GCC such as Kuwait, Bahrain and Oman have followed suit, outlining plans to increase energy prices in the near future. While the new prices are still low by international and regional standards, there forms represent a fundamental shift in the GCC's economic and social policies.

The GCC countries are implementing fiscal consolidation gradually over the next five years. This strategy seems reasonable given the size of fiscal buffers which enable the GCC countries to afford maintaining fiscal deficits further into the future, in order to reduce the impact of lower oil prices on growth. According to the IMF, the fiscal buffer for the GCC varies from around five years, as in Bahrain, Oman, and Saudi Arabia to more than 20 years as in Kuwait, Qatar, and the United Arab Emirates. Public debt trajectories and sovereign ratings can provide additional perspective on the ability of the GCC countries to withstand fiscal deficits during the adjustment period toward achieving economic efficiency. Typically, the higher the country's public debt, the lower the sovereign rating and borrowing capacity. Almost all GCC countries (except Bahrain) have ratings similar to those of the bestperforming advanced economies, but their debt ratios are considerably below advanced economy peers by some 20-40 percentage points of GDP. Accordingly, the GCC countries have ample savings, low debt ratios, access to international markets, and developed financial systems which make it feasible for the governments to meet the objectives of economic restructuring at a lower economic cost.

However, the sharp decline in the oil price has altered the economic growth pattern and outlook for the GCC countries. Lower oil revenue has sharply reduced the region's fiscal and external surplus, turning them into a deficit. The budget balance in 2015 in the GCC economies turned into deficit equivalent to 13.2 percent of the GDP for the six countries after a 2.9 percent surplus of the GDP in 2014, and a surplus of 11 percent as an

average for the period 2008-2013. Oil export revenue dropped by more than \$300 billion for the GCC countries as a whole in 2015, and this sharply reduced the region's external surplus, turning it into a deficit. The current account balance for the GCC countries together dwindle from a surplus of 15 percent of GDP in 2014 to a deficit of 0.25 percent in 2015.

Growth in the GCC also slowed in 2015, and it is expected to slow further in the short term as countries initiate fiscal consolidation. GCC economies grew by 3.25 percent 2015. The growth rate is expected to slow down to 2.75 percent next year from 3.5 percent in 2014, and around 5.1 percent during the period 2008-2013. Lower oil prices will result in non-oil growth, through fiscal adjustment and its directions and expectations in the future, although this is partly compensated by higher oil production. Non-oil growth is projected at just below 4 percent in 2016 as in 2015 and lower by 1.75 percent compared with 2014, as fiscal adjustment begins to have effects, notably in Saudi Arabia, the United Arab Emirates and Oman, Over the medium term, continued fiscal consolidation could imply slower overall growth despite anticipated payoffs from structural reforms.

Despite the benefits the reforms can bring to the economy, a move to increase

energy prices can induce negative shocks affecting households, industries, and the wider economy. Higher energy prices can spur inflation, especially if they result in a shift in expectations and wage-price spirals. Energy-pricing reform reduces the welfare of households both directly by raising the price of electricity, water and petroleum products, and indirectly, by increasing the price of other goods and services that use energy as intermediate inputs. Higher energy prices also increase input costs for industries, reducing profits. This is especially true for energy-intensive industries that are not able to pass on the cost increase to end-buyers, either due to the competitive structure of the industry such as petrochemicals or the imposition of price controls like in the cement industry. Thus, in any energy-pricing reform strategy, it is essential that governments put in place measures to mitigate these negative impacts. For instance, the government should design schemes to compensate households, especially those with low incomes. It should establish specialized funds that provide technical assistance and soft loans to help most affected industries to adjust to the higher cost by increasing efficiency through the introduction of new technologies and equipment upgrading.



Actually, the ability of the GCC governments to put in place such schemes and communicate their policies effectively and transparently will determine the success of their energy-pricing reform programs in the longer term.

Beside the domestic factors, represented by the efforts of fiscal reforms, there are many other uncertainties surrounding growth trajectories in the GCC countries, starting from the future path of oil prices and its implications on the GCC economies, to monetary policy normalization in the advanced economies to the growth outlook in emerging markets. Because oil prices are already low and most GCC governments are projected to post budget deficits, a further drop in oil prices would accelerate fiscal adjustment, with adverse implications for growth. Also, the speed to fiscal reforms may differ substantially across the countries. Some governments, especially those with larger initial buffers and/or lower initial debt (Kuwait, Qatar), could decide to continue offsetting the lost oil revenues only partially, and draw down assets or allow additional debt accumulation. Additionally, the economic slowdown could be exacerbated through financial channels-for instance, governments and oil companies may decrease their deposits in the banking system, reducing funding for loans. Also, excessive government borrowing through issuing domestic debt may reduce the amount of liquidity available for the private sector. Also, the pace of fiscal consolidation poses a risk to GCC growth prospects, if the chosen mix of adjustment policies leads to a larger-than-expected decline in domestic demand. Needless to say that sustained conflicts could also have an important impact on region-wide confidence, further dimming growth prospects.

The prospective normalization of monetary conditions in advanced economies, particularly the United States, could be less gradual or orderly than markets currently expect. Higher U.S. interest rates would also raise external borrowing costs. Funding costs could increase and access to markets could tighten for countries in the region, at a time when lower oil prices imply an increased need to tap the markets. Pass-through of higher U.S. interest rates will be strong, given the GCC pegs to the U.S.

dollar, and could slow private investment in non-oil sectors. Improving U.S. economic prospects, relative to the rest of the world, could lead to persistent dollar strength, implying a procyclical tightening of monetary conditions in countries with exchange rates linked to the dollar.

Recent weak data from China have amplified global financial market volatility. Even though non-oil trade between China and the GCC is relatively small, a more slower-than-expected growth in China is likely to put further pressure on oil prices, reflecting China's important role in global oil demand; a slackening of demand in China could cause a further deterioration in fiscal and external balances for the GCC countries, with a negative impact on growth. Financial linkages with China are small and further declines in equity prices, or the value of the Chinese renminbi, are unlikely to have a major impact on the countries in the region, though regional equity markets dropped in response to the emerging market turmoil, especially in Oman, Saudi Arabia, and the United Arab Emirates.

Inflation in most countries of the region has moderated to 2.4 percent in 2015, the decline was driven by the decelerating food price growth and the appreciating U.S. dollar, to which many countries effectively tie their currencies. However, in 2016, reform measures adopted by the government in the region including reviewing subsidies for energy, electricity, and water, will push inflation slightly, but it will still be manageable. Also, jointly imposing the value added tax (VAT) by the GCC countries will also push inflation higher.

One of the major challenges that the GCC countries should work on is the employment structure and the youth unemployment. According to global estimations, more than 2 million nationals are expected to join the workforce by 2020 in the GCC. If private sector job growth were to follow past trends, and public sector employment growth is consistent with the current fiscal projections, more than half a million job market entrants will end up being unemployed. In addition to the 1 million who are already out of work. The aggregate GCC unemployment rate would increase from 12.75 percent to 16 percent. In practice, the increase could

be much higher, as contracted fiscal conditions will not allow the governments to maintain the pace of public sector hiring. Clearly, the private sector will have to take over from the public sector as the main source of job creation. However, the expansion of the private sector and the diversification away from oil that are needed to absorb the growing workforce have not so far proven efficient. Though some progress has been made. The private sector itself is highly reliant on government spending and needs to become self-sustaining through increased competitiveness in other markets. Creating incentives for nationals to move to the private nonhydrocarbon sector, improving skills, and making those skills more relevant to the private sector by improving the quality of education are crucial in this regard.

With respect to the financial sector in the GCC countries, the banking system is seen to be well positioned to withstand the effects of the oil shock and the structural reforms owing to their high capital buffers, low nonperforming loans (NPLs), and generally high liquidity. Though profits could come under pressure. Macroprudential policies have reduced vulnerabilities related to real estate exposure and household indebtedness. The slowdown in deposit growth is affecting credit growth in some countries. The downside risks are likely to increase over time given the strong correlation between non-oil growth and government spending. Second-round effects of lower oil prices on economic activity could weaken asset quality, liquidity, and profitability.

The GCC indices ended the year 2015 on a negative note amid declining oil prices and regional turmoil. A slowdown in China coupled with the hike in US interest rates also fuelled the slide. Additionally, the fiscal consolidation measures that have been taken by most of GCC governments also left significant impact on the markets as government expenditures have been key drivers of corporate earnings. Except Tadawul and The Bahrain Bourse all GCC markets ended the first quarter down. Most regional indices rallied in the second quarter led by a strong performance by the UAE markets supported by

higher oil prices towards mid-June. The downtrend in oil prices weighed on the GCC indices in the third quarter. Weak investor sentiments and expectations of grim corporate earnings led to huge selling pressure resulting in heavy losses in all indices, turning their YTD by the end of guarter into negative. By the end of the year, all the GCC indices continued to head down mainly due to weakness in global equity markets and softer crude oil prices. The Saudi market (Tadawul) posted the biggest losses for the year down by -17.06 percent at 6,911. Dubai Financial Market declined by 16.51 percent to 3,151. Bahrain Bourse retreated by 15.33 percent at 1,205. Qatar Exchange, from its side fell 15.11 percent to 10,429. Muscat Securities Market ended the year down by 14.77 percent at 5,406, and Kuwait Stock Exchange declined by 14.13 percent. Abu Dhabi Securities Exchange managed to limit its losses at 5.58 percent closing at 4,276.

#### The Saudi Economy

According to the latest released numbers by the General Authority of Statistics (GASTAT), the Saudi economy posted a



growth rate of 3.4 percent in 2015, with the private non-oil GDP growing by 3.7 percent following 5.4 percent growth rate in 2014. The growth rates in the private sector during the last two years proved that the benefits from positive development in the oil sector and the expansion in the fiscal programs transmit to the private sector activities within a short lag period. It showed also that this transmission channel seems to be asymmetric. The private sector continued energizing and spurring economic growth even at relatively low oil prices era during the peak of the global financial crisis and global recession in 2009, it also continued to lead growth in 2015, when oil prices dropped by more than 50% from its peaks in June 2014.

The drop in oil prices has led the Saudi Government to undertake comprehensive economic, fiscal, and structural reforms to achieve wide structural reforms in the national economy and to reduce dependence on oil. These measures are planned to be implemented gradually over the period 2016-2020. The measures include: privatizing different economic activities and sectors; overcoming legislative, regulatory and bureaucratic obstacles in the private sector; diversifying revenues away from the hydrocarbon sector, reviewing government subsidies, reforming and developing government performance; improving transparency accountability levels; and enhancing the investment environment. Such reforms are designed in a way to provide strong partnership opportunities between public, private and non-profit sectors, enhance employment and job creation in the private sector and improving the competitiveness and integration of the local economy with the global economy.

Saudi Arabia unveiled the 2016 budget in accordance with the Government Financial Statistics (GFS) of 2001/2014. The Ministry worked on the new methodology as part of its efforts to design and classify the budget according to the best accounting practices. The new classification makes the budget more reactive to transparency and corporate governance requirements. The new

classification also ensures the delivery of the right objectives of the government fiscal policy in order to maximize the overall impact on economy.

Along with announcing the budget, the government also introduced many procedures aiming at enhancing fiscal management through establishing fiscal rules consistent with transparency and corporate governance, enhancing effective coordination between all stakeholders involved in the implementation of fiscal reforms, improving budget policies and implementation, and refining the management style of state assets. For that purpose, the government established a public finance unit within the Ministry of Finance responsible for setting a budget ceiling by adopting a medium-term expenditure framework and ensuring full adherence to this ceiling.

The Government also took significant steps in increasing the efficiency of capital and operating expenditures while compacting growth in recurring spending. In that, the Government established the National Project Management Agency. The Agency will be in charge in reviewing the scope and priorities of government projects to ensure the efficient implementation of these projects with respect to their needs and contribution to development, as well as their funding requirements. The Government will be focusing on investing in development projects and programs that contributes directly to the citizens' quality of life, namely, education, health, security, social and municipal services, water and sanitation, electricity, roads, electronic transactions, and scientific research. In rationalizing and optimizing operating expenditures, the Government will make more for utilization of information technology (IT) for conducting government services, while strengthening control and governance mechanisms through introducing new laws of government's competitiveness and procurement. To compact other recurring expenditures, the government will watch closely the growth of current expenditures items, especially wages, salaries and allowances, that accounts more than 50% of the total expenses. The government also reviewed government subsidies for energy, water, and electricity in order to improve the efficiency of the use of energy and other natural

limited resources. The amendment of subsidies has been started and will progress gradually over the next five years, taking into account any negative effects on low and middle-income class, or any deteriorations in the competitiveness of the business sector.

On the revenue side, the government is in the process of reviewing current structure of fees and fines and introducing new fees and taxes. In particular, completing the necessary arrangements for the application of the value added tax (VAT) approved by the Supreme Council of the GCC countries . Also, imposing additional fees on certain list of goods including tobacco, and soft drinks.

On the financing and debt management side, the government is in the process of establishing the Public Debt Management Unit within the Ministry of Finance. The new unit will be responsible for developing a broader public debt and financing strategy. This includes strengthening the Kingdom's ability to borrow both domestically and internationally, in a way that contributes to the sukuk and local bonds markets.

Taking into account the above developments and principles, the government issued the 2016 budget according to the GFS methodology. The 2016 budget allocates SR 840 billion as a total expenditures for the whole 2016. This allocation implies a decline in total expenditures by SR 20 billion over the 2015 budget, while it shows a decline by 13.8% from actual 2015 expenditures. The budget allocates SR 191.7 billion or 22.8% for "education and manpower training". It allocates SR 104.9 billion for "health services and social developments", and that accounts for 12.5% of the total budget. "Economic resources" got SR 78.1 billion and that accounts for 9.3% of the budget. "Municipalities", infrastructure & transportation" and "public administration" all together, got 8.2% of total allocations of the budget with a value of SR 68.9 billion. The largest allocation went to the "military and security services" that include Ministry of Interior, Ministry of National Guard, Ministry of Defense, General Intelligence Directorate, Saudi Royal Guard Regiment with a value of SR 213 4 hillion

Unlike previous budgets, 2016 budget includes special allocation with a value of SR 183 billion. The necessity for such special provision emerged on the back of the recent excessive volatility in oil prices and the probability of declining revenues compared to the budget estimates. This allocation will offer increased flexibility to redirect capital expenditures and operating expenditures on both ongoing and new projects according to national developmental priorities and to meet any emerging expenditure needs.

The budget expects total revenues to be SR 514 billion in 2016, and that's 28.3% less than the budgeted total revenues in 2015 and less by 15.5% of the actual revenues in 2015. Accordingly the Government expects a deficit of SR 326 billion in 2016. The government could increase it non-oil revenues in 2015 to SR 163.5 billion and this represents an increase by 36.8% over the 2014. Non-oil revenues are expected to grow further in 2016 as the government is expected to increase the fees and fine structure and to introduce additional levies on selected items.

Regarding financing the deficit, the government stated that the deficit will be financed while taking into account the best financing options available, including borrowing from the local and international markets; the scheme will be implemented in a way that will avoid any negative impact on domestic liquidity and to leave a room for the private sector use the needed funding for expansion and growth.

#### **Financial Markets**

During the year of 2015, SAMA continued to implement a balanced monetary policy, in line with domestic and international economic developments. In its policy, SAMA aims at achieving price stability and providing sufficient liquidity for domestic banks to perform their financing role in supporting various economic sectors, to continue growing at a robust and balanced pace, at favorable conditions of stable inflation rate. To keep up with international

development, SAMA took a decision to increase the reverse repo rate by 0.25 basis points to 0.50 percent on December 16, 2015 while keeping the reporate unchanged at 2.0 percent. The step followed the move by the Federal Reserve Bank of increasing the federal fund rate by 25 basis points to range between 0.25 percent - 0.50 percent for the first time since 2006.

The 3-month SIBOR ended the year 2015 at 1.55 percent to average 0.88 percent, 2.0 basis points above its average in 2014 at 0.86 percent. The 12-month SIBOR ended the year at 1.875 percent to average 1.09 percent through the year, the same as its average in 2014. The rates continued to be in the favor of Riyal deposits all over the year. The spread of the 3-month SIBOR over the 3-month LIBOR moved from 60 basis points at the end of December 2014 to 93 basis points at the end of December 2015, but averaged 56 basis points through the 2015 compared with an average of 70 basis points for 2014. Regarding inflation, the data from the Central Department of Statistics and Information indicate that the inflation rate calculated as the percentage change in the consumer price index for the base year 2007, slowed down during 2015 to 2.2 percent compared with 2.7 percent for the year 2014.

Concerning liquidity, latest available weekly data from SAMA shows that broad money supply (M3), reached a SR 1790.6 billion at the end of December 2015 and that is 3.54 percent above its level at the end of December 2014. Total deposits grew by also 3.49 percent with a growth rate in demand deposits reaching 0.61 percent.

Total lending from commercial banks continued to pick up consistently starting from December 2010. By the end of November 2015, total loans extended to the private sector by Saudi banks increased by 8.4 percent reaching SR 1,355.3 billion compared to SR 1,250.6 billion at the end December 2014. As a result, the loan to deposit ratio stabilized at 84.0 percent in November 2015 up from 79.7 percent in December 2014.

The Saudi stock market (TADAWUL) ended the year

sharply down in response to low oil prices throughout the year. During the first quarter, the index ended the guarter up as the Government decided not to alter spending plans in 2015. Additionally, the Capital Market Authority (CMA) announced plans to open the stock market for foreign investors on June 15th 2015. TASI was boosted further after announcing that the government would expedite its housing program. In the second quarter, the index found support after MSCI announced that it would begin consultations with international institutional investors regarding the inclusion of Saudi Arabia in the MSCI Emerging Markets Index. However, TASI moved down in the third quarter below the 9,000 point mark on heavy selling due to falling oil prices and Fitch Rating's decision to cut its outlook for Saudi Arabia's debt. TASI remained volatile towards the year end due to the continued volatility in oil prices and in anticipation of the Government's move to reduce subsidies and spending levels as well as increasing fees to cover the budget deficit amid the low oil price environment. By the end of the year, TASI closed at 6,912 points compared to 8,333 points at the end of 2014, lower by 1,421 points or 17.1 percent. It reached as high as 9,835 points on April 30th, before it bottoms on December 14th to as low as 6,686 points. The P/E ratio increased to 14.24 at the end of 2015 up from 14.00 at the end of 2014, while the market capitalization declined from SR 1,813 billion to SR 1,579 billion, however, its ratio as a percent of GDP stayed at the same level of 2014 at 64.4 percent. "Media and Publishing", "Transport" and "Energy & Utilities" were the best performing sectors through the year. On the other hand, "Cement", "Building and Construction", "Petrochemical Industries" and "Agriculture & Food Industries", were the worst performing sectors respectively. In term of size, "Med Cap" companies were the worst performing on average ending the year with 25 percent losses. Followed by "Small Cap" companies, then declined by 19.9%. "Large Cap" companies, from its side lost 13.5%, while the "Micro Cap" companies, declined by 7.7%.

## Macroeconomic Performance in 2015 and Outlook for 2016

Despite the large drop in oil prices the Saudi economy continued to expand on a relatively strong pace on real terms,

although the size of the GDP shrank on nominal terms. The GDP at current market prices in 2015 deteriorated by 13.35 percent to SR 2,450 billion. This contradiction in the GDP in current prices came as a result of a decline in the oil sector by 42.78 percent, and an increase in the non-oil GDP growth by 8.37 percent, both in nominal terms. The growth in the non-oil GDP resulted from the expansion in the government sector by 14.57 percent and the growth in the non-oil private sector by 5.83 percent.

In real terms, the GDP grew by 3.35 percent in 2015 compared to a growth rate of 3.64 percent in 2014. Estimates show that the oil sector has grown by 3.06 percent in 2015 after an expansion by 2.09 percent in the year before. The government sector, on the other hand, expanded by 3.34 percent, while the private sector expanded by 3.74 percent in 2015. All components of non-oil GDP recorded positive and healthy growth in 2015. Specifically, non-oil manufacturing sector grew by 5.78 percent; construction by 5.60 percent; transport, storage and communication sector by 6.10 percent; wholesale, retail, restaurants, and hotels by 3.86 percent; and finance, insurance and real estate by 2.55 percent.

Concerning the external sector, the total value of exports of goods decreased in 2015 by 40.0 percent to SR 770.5 billion. Non-oil exports of goods dropped by 18.0 percent to SR 178.1 billion, although its share in total exports went up to 23.1 percent up from 16.9 percent in 2014. Exports of services increased by 0.6% in 2015 reaching SR 46.1 billion taking the total value of exports of goods and services to SR 816.6 billion. On the other hand, imports of goods retreated by 3.7 percent to SR 628.1 billion, while imports of services fell by 17.8 percent to SR 251.5 billion. As a result, in 2015, the trade balance registered a surplus of SR 142.4 billion or 5.8 percent of the GDP, while the current account suffered a deficit of SR 227.6 billion or 9.3 percent of the GDP.

Regarding the government budget, total revenues in 2015 declined to SR 608 billion down from SR 1044.4 billion. Oil revenues declined by 51.6 percent to SR 444.5 billion. The non-oil revenues registered significant growth reaching SR 163.5 billion compared to SR 126.8 billion in 2015. Accordingly, the share of non-oil revenues to total revenues surged from 21.1 percent in 2014 to 26.9% in 2015. Total expenditure contained in 2015 by 14.5 percent to SR 975 billion down from SR 1,140.0 billion. The figure for 2015 includes the additional bonus salaries extended to civil and military Saudi employees, beneficiaries of social





security and retirees amounted to SR 88 billion, or nearly 77 percent of the dispersion between actual expenditures and budgeted expenditures for 2015. The difference also includes additional spending on military and security projects of SR 20 billion, which accounts for 17 percent of the divergence from 2015 budget expenditures. As a result, in 2015, the government budget realized a budget deficit of SR 367 billion or 15.0 percent of the GDP. In line with the budget deficit, the government debt increased to SR 142 billion, or 5.8 percent of the GDP in 2015, up from 2.0 percent in 2014. The Government issued bonds with 5, 7 and 10 maturities domestically with a value of SR 98 billion.

Given, the expected mild growth rate in the global economy, and under the assumption that Iran will accelerate oil production by around 1.0 million bbl/d after lifting the sanction, which keeps the supply glut through 2016, we assume oil prices will average within \$40.0 to \$46.0 /bbl. Regarding Saudi oil production, it is expected to stay around 10.3 mb/d. Under these assumptions, oil sector is expected to grow 0.3-0.8 percent in 2016, while the, non-oil sector may grow by a rate which could reach 2.0 percent.

Government sector is expected to slow down significantly through 2016, while the private sector is expected to register a growth rate which range between 1.5-2.4 percent. Accordingly, the overall GDP could grow by a rate which may reach 1.6 percent in 2016. The nominal GDP in 2016 is expected to decline further to SR 2,311 billion. Inflation rate (calculated as the annual percentage change in the consumer price index for the base year 2007) is expected to increase to 3.5 – 4 percent in 2016 as a reflection of the measures adopted by the government to amend the subsidies on energy water and electricity prices. Unemployment rate (among Saudis) is expected to stay around 11.0 percent while continuing efforts boost employments.

Based on the above oil prices and production in 2016, the current account is expected to register a deficit of ranges between SR 484 billion to SR 533 billion (19 – 23) percent of the GDP. The fiscal figures, on the other hand, are expected to register somehow better results than anticipated by the budget. Accordingly, it is expected that the fiscal deficit will range between 10.0 – 14.0 percent of the GDP, as oil revenues are expected to exceed the budgeted figures.





# **FINANCIAL**STATEMENTS







#### **INDEPENDENT AUDITORS' REPORT**

To the Shareholders of Riyad Bank (A Saudi Joint Stock Company)

We have audited the accompanying consolidated financial statements of Riyad Bank ("the Bank") and its subsidiaries (collectively referred to as "the Group"), which comprise the consolidated statement of financial position as at December 31, 2015, and the consolidated income statement, and the consolidated statements of comprehensive income, changes in shareholders' equity and cash flows for the year then ended, and a summary of significant accounting policies and other explanatory notes from 1 to 39. We have not audited note 40, nor the information related to "Basel III Pillar 3 Disclosures" cross referenced therein, which is not required to be within the scope of our audit.

#### Management's Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with Accounting Standards for Financial Institutions issued by the Saudi Arabian Monetary Agency ("SAMA") and International Financial Reporting Standards and to comply with the relevant provisions of the Regulations for Companies, the Banking Control Law in the Kingdom of Saudi Arabia and the Bank's Articles of Association. In addition, management is responsible for such internal controls as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

#### Auditors' Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audit. We conducted our audit in accordance with generally accepted auditing standards in the Kingdom of Saudi Arabia and International Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether these consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the Bank's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Bank's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.



## KPMG Al Fozan & Partners Certified Public Accountants



We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

#### **Opinion**

In our opinion, the consolidated financial statements taken as a whole:

- present fairly, in all material respects, the consolidated financial position of the Group as at December 31, 2015, its consolidated financial performance and consolidated cash flows for the year then ended in accordance with Accounting Standards for Financial Institutions issued by SAMA and with International Financial Reporting Standards; and
- comply with the relevant provisions of the Regulations for Companies, the Banking Control Law in the Kingdom of Saudi Arabia and the Bank's Articles of Association in so far as they affect the preparation and presentation of the consolidated financial statements.

KPMG Al Fozan & Partners Certified Public Accountants

P.O. Box 92876 Riyadh 11663 Kingdom of Saudi Arabia

Abdullah Hamad Al Fozan Certified Public Accountant Registration No. 348 **PricewaterhouseCoopers** 

P.O. Box 13934 Riyadh 11414 Kingdom of Saudi Arabia

Omar M. Al Sagga Certified Public Accountant Registration No. 369

5 Jumada Al-Awwal 1437H 14 February 2016



## CONSOLIDATED STATEMENT OF FINANCIAL POSITION

As at December 31, 2015 and 2014

SAR '000	Notes	2015	2014	
ASSETS				
Cash and balances with SAMA	4	20,569,929	25,315,736	
Due from banks and other financial institutions	5	9,269,380	3,914,504	
Investments, net	6	44,552,383	46,963,269	
Loans and advances, net	7	144,673,830	133,490,274	
Investment in associates	8	525,131	468,535	
Other real estate		258,411	390,802	
Property and equipment, net	9	1,894,701	1,706,731	
Other assets	10	1,572,110	2,339,442	
Total assets		223,315,875	214,589,293	
LIABILITIES AND SHAREHOLDERS' EQUITY				
Liabilities				
Due to banks and other financial institutions	12	4,496,211	3,789,796	
Customer deposits	13	167,089,802	164,079,433	
Debt securities in issue	14	8,000,000	4,000,000	
Other liabilities	15	7,184,750	7,182,959	
Total liabilities		186,770,763	179,052,188	
Shareholders' equity				
Share capital	16	30,000,000	30,000,000	
Statutory reserve	17	2,100,471	1,088,102	
Other reserves	18	297,467	1,038,937	
Retained earnings		2,847,174	2,160,066	
Proposed dividends	25	1,300,000	1,250,000	
Total shareholders' equity		36,545,112	35,537,105	
Total liabilities and shareholders' equity		223,315,875	214,589,293	

## CONSOLIDATED INCOME STATEMENT

For the years ended December 31, 2015 and 2014

SAR '000	Notes	2015	2014
Special commission income	20	5,883,035	5,945,240
Special commission expense	20	700,080	815,001
Net special commission income		5,182,955	5,130,239
Fee and commission income, net	21	1,786,252	2,020,485
Exchange income, net		348,385	280,394
Trading gains (losses), net		33,700	(929)
Dividend income		60,970	58,473
Gains on non-trading investments, net		222,389	376,732
Other operating income	22	354,488	146,372
Total operating income, net		7,989,139	8,011,766
Salaries and employee-related expenses	23	1,613,354	1,471,552
Rent and premises-related expenses		299,585	281,752
Depreciation of property and equipment	9	275,774	257,665
Other general and administrative expenses		650,999	763,815
Impairment charge for credit losses, net		1,030,735	900,063
Impairment charge for investments, net		21,609	-
Other operating expenses		87,525	31,232
Total operating expenses, net		3,979,581	3,706,079
Net operating income		4,009,558	4,305,687
Share in earnings of associates, net		39,919	46,721
Net income for the year		4,049,477	4,352,408
Basic and diluted earnings per share (in SAR)	24	1.35	1.45

## CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

For the years ended December 31, 2015 and 2014

SAR '000	2015	2014
Net income for the year	4,049,477	4,352,408
Other comprehensive income:		
Items that may be recycled back to consolidated income statement in subsequent periods		
- Available for sale investments		
Net change in fair value (note 18)	(582,781)	222,538
Net amounts transferred to consolidated income statement (note 18)	(158,689)	(368,165)
Other comprehensive income for the year	(741,470)	(145,627)
Total comprehensive income for the year	3,308,007	4,206,781

## **CONSOLIDATED STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY**

For the years ended December 31, 2015 and 2014

SAR '000	Notes	Share capital	Statutory reserve	Other reserves	Retained earnings	Proposed dividends	Total
				Available for sale investments			
2015							
Balance at the beginning of the year		30,000,000	1,088,102	1,038,937	2,160,066	1,250,000	35,537,105
Total comprehensive income		-	-	(741,470)	4,049,477	-	3,308,007
Final dividend paid - 2014	25	-	_	-	-	(1,250,000)	(1,250,000)
Interim dividend paid - 2015	25	-	-	-	(1,050,000)	-	(1,050,000)
Transfer to statutory reserve	17	-	1,012,369	-	(1,012,369)	-	-
2015 final proposed dividend	25	-	-	-	(1,300,000)	1,300,000	-
Balance at the end of the year		30,000,000	2,100,471	297,467	2,847,174	1,300,000	36,545,112
2014							
Balance at the beginning of the year		15,000,000	14,328,376	1,184,564	1,957,384	1,400,000	33,870,324
Final dividend paid - 2013	25	-	-	-	-	(1,400,000)	(1,400,000)
Transfer from retained earnings		-	671,624	-	(671,624)	-	-
Issue of bonus shares		15,000,000	(15,000,000)	-	-	-	-
Total comprehensive income		-	-	(145,627)	4,352,408	-	4,206,781
Interim dividend paid - 2014	25	-	-	-	(1,140,000)	-	(1,140,000)
Transfer to statutory reserve	17	-	1,088,102	-	(1,088,102)	-	-
2014 final proposed dividend	25	-	-	-	(1,250,000)	1,250,000	-
Balance at the end of the year		30,000,000	1,088,102	1,038,937	2,160,066	1,250,000	35,537,105

## **CONSOLIDATED STATEMENT OF CASH FLOWS**

For the years ended December 31, 2015 and 2014

SAR '000	Notes	2015	2014
OPERATING ACTIVITIES			
Net income for the year		4,049,477	4,352,408
Adjustments to reconcile net income for the year			
to net cash from (used in) operating activities:			
Accretion of discounts and amortisation of			
premium, net on non-trading investments, net		(80,938)	(125,701)
Gains on non-trading investments, net		(222,389)	(376,732)
Depreciation of property and equipment		275,774	257,665
Share in earnings of associates, net		(39,919)	(46,721)
Impairment charge for investments, net		21,609	-
Impairment charge for credit losses, net		1,030,735	900,063
		5,034,349	4,960,982
Net (increase) decrease in operating assets:			
Statutory deposit with SAMA	4	(527,825)	(695,954)
Due from banks and other financial institutions			
maturing after three months from date of acquisition		187,577	1,596,857
Loans and advances		(12,214,291)	(3,199,780)
Other real estate		132,391	46,566
Other assets		767,332	268,869
Net increase (decrease) in operating liabilities:			
Due to banks and other financial institutions		706,415	(3,788,184)
Customer deposits		3,010,369	10,879,553
Other liabilities		(156,965)	480,484
Net cash (used in) from operating activities		(3,060,648)	10,549,393
INVESTING ACTIVITIES			
Proceeds from sales and maturities of non-trading			
investments		28,340,798	26,178,000
Purchase of non-trading investments		(26,406,341)	(29,225,889)
Purchase of property and equipment, net		(463,744)	(301,746)
Net cash from (used in) investing activities		1,470,713	(3,349,635)
FINANCING ACTIVITIES			
Proceeds from issuance of debt securities in issue	14	4,000,000	-
Dividend and Zakat paid		(2,141,244)	(2,435,820)
Net cash from (used in) from financing activities		1,858,756	(2,435,820)
Net increase in cash and cash equivalents		268,821	4,763,938
Cash and cash equivalents at beginning of the year		20,772,910	16,008,972
Cash and cash equivalents at end of the year	26	21,041,731	20,772,910
Special commission received during the year		5,781,935	5,960,742
Special commission paid during the year		726,753	888,580
Supplemental non-cash information			
Net changes in fair value and transfers to		/	
consolidated income statement		(741,470)	(145,627)

For the years ended December 31, 2015 and 2014

#### 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 November 23, 1957G). The Bank operates under commercial registration No. 1010001054 dated 25 Rabi Al-Thani 1377H (corresponding to November 18, 1957G) through its 334 branches (2014: 318 branches) 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 Bank's Head Office is located at the following address:

Riyad Bank, P.O. Box 22622, Riyadh 11416, Kingdom of Saudi Arabia

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

The consolidated financial statements comprise the financial statements of Riyad Bank and its wholly owned subsidiaries, incorporated in the Kingdom of Saudi Arabia; 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 (with the objective to hold, manage, sell and purchase real estate assets for owners or third parties for financing activities); and c) Riyad Company for Insurance Agency (which acts as an agent for selling insurance products owned and managed by another principal insurance company), and are collectively referred to as "the Group".

#### 2. BASIS OF PREPARATION

#### a) Statement of compliance

The consolidated financial statements are prepared in accordance with the Accounting Standards for Financial Institutions promulgated by the Saudi Arabian Monetary Agency (SAMA) and International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board (IASB). The Bank also prepares its consolidated financial statements to comply with the Banking Control Law, the provisions of Regulations for Companies in the Kingdom of Saudi Arabia and the Bank's Articles of Association.

#### b) Basis of measurement and presentation

The consolidated financial statements are prepared under the historical cost convention except for the measurement at fair value of derivatives and Available for Sale financial assets. In addition, financial assets or liabilities that are hedged in a fair value hedging relationship, and otherwise carried at cost, are carried at fair value to the extent of the risk being hedged.

#### c ) Functional and presentation currency

These consolidated financial statements are presented in Saudi Arabian Riyals (SAR), which is the Bank's functional currency. Except as indicated, financial information presented in SAR has been rounded off to the nearest thousand Saudi Arabian Riyals.

#### d) Critical accounting judgements, estimates and assumptions

The preparation of the consolidated financial statements in conformity with IFRS requires the management to use 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 Bank'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

For the years ended December 31, 2015 and 2014

#### 2. BASIS OF PREPARATION (continued)

#### d) Critical accounting judgements, estimates and assumptions (continued)

of future events that are believed to be reasonable under the circumstances. Significant areas where management has used estimates, assumptions or exercised judgements are as follows:

#### i) Impairment for credit losses on loans and advances

The Bank reviews its loan portfolios to assess specific and collective impairment on a quarterly basis. In determining whether an impairment loss should be recorded, the Bank makes judgements as to whether there is any observable data indicating that there is a measurable decrease in the estimated future cash flows. This evidence may include observable data indicating that there has been an adverse change in the payment status of borrowers in a group. Management uses estimates based on historical loss experience for loans with credit risk characteristics and objective evidence of impairment similar to those in the portfolio, when estimating its cash flows. The methodology and assumptions used for estimating both the amount and the timing of future cash flows are reviewed regularly to reduce any differences between loss estimates and actual loss experience.

#### ii ) Fair value measurement

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The fair value measurement is based on the presumption that the transaction to sell the asset or transfer the liability takes place either:

- In the principal market for the asset or liability, or
- In the absence of a principal market, in the most advantageous market for the asset or liability

The principal or the most advantageous market must be accessible to by the Group.

The fair value of an asset or a liability is measured using the assumptions, that market participants would use, when pricing the asset or liability, assuming that market participants act in their economic best interest. A fair value measurement of a non-financial asset takes into account a market participant's ability to generate economic benefits by using the asset in its highest and best use or by selling it to another market participant that would use the asset in its highest and best use.

The Group uses valuation techniques that are appropriate in the circumstances and for which sufficient data are available to measure fair value, maximising the use of relevant observable inputs and minimising the use of unobservable inputs.

All assets and liabilities for which fair value is measured or disclosed in the consolidated financial statements are categorised within the fair value hierarchy, described as follows, based on the lowest level input that is significant to the fair value measurement as a whole:

- Level 1: Quoted (unadjusted) market prices in active markets for identical assets or liabilities
- Level 2: Valuation techniques for which the lowest level input that is significant to the fair value measurement is directly or indirectly observable
- Level 3: Valuation techniques for which the lowest level input that is significant to the fair value measurement is unobservable

For assets and liabilities that are recognised in the financial statements on a recurring basis, the Group determines whether transfers have occurred between Levels in the hierarchy by re-assessing categorisation

For the years ended December 31, 2015 and 2014

(based on the lowest level input that is significant to the fair value measurement as a whole) at the end of each reporting period.

#### iii ) Impairment of available-for-sale investments

The Bank exercises judgement in considering impairment on the Available for sale equity investments. This includes determination of a significant or prolonged decline in the fair value below its cost. In making this judgement, the Bank evaluates among other factors, the normal volatility in share price. In addition, the Bank considers impairment to be appropriate when there is objective evidence of deterioration in the financial health of the investee, industry and sector performance, changes in technology and operational and financing cash flows.

The Bank reviews its debt securities classified as available for sale at each reporting date to assess whether they are impaired. This requires similar judgement as applied to individual assessment of loans and advances.

#### iv ) Classification of held-to-maturity investments

The Bank follows the guidance of IAS 39 on classifying non-derivative financial assets with fixed or determinable payments and fixed maturity as held-to-maturity. In making this judgement, the Bank evaluates its intention and ability to hold such investments to maturity.

#### v ) Determination of control over investees

#### Investment funds

The Group acts as 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 investor's 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.

#### Special Purpose Entities (SPEs)

The Bank is party to certain SPEs, primarily to facilitate Shariah compliant financing arrangements. The exposures to these entities are included in the Bank's loans and advances portfolio.

#### 3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The significant accounting policies adopted in the preparation of these consolidated financial statements are set out below.

#### a) Changes in accounting policies

The accounting policies used in the preparation of these annual consolidated financial statements are consistent with those used in the preparation of the annual consolidated financial statements for the year ended December 31, 2014 except for the adoption of the following amendments to existing standards and improvements mentioned below which has had an insignificant financial impact on the annual consolidated financial statements of the Group.

a) Amendments to IAS 19 applicable for annual periods beginning on or after July 1, 2014 are applicable to defined benefit plans involving contribution from employees and / or third parties. This provides relief, based on meeting certain criteria, from the requirements proposed in the amendments of 2011 for attributing employee / third party contributions to periods of service under the plan benefit formula or on a straight line basis. The current amendment gives an option, if conditions satisfy, to adjust service cost in the period in which the related service is rendered.

For the years ended December 31, 2015 and 2014

#### 3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

#### a) Changes in accounting policies (continued)

- b) Annual improvements to IFRS 2010-2012 and 2011-2013 cycles, applicable for annual periods beginning on or after July 1, 2014. A summary of the amendments is contained as under:
  - i) IFRS 1 "First time adoption of IFRS" :The amendment clarifies that a first time adopter is permitted but not required to apply a new or revised IFRS that is not yet mandatory but is available for early adoption.
  - ii) IFRS 2 amended to clarify the definition of 'vesting condition' by separately defining 'performance condition' and 'service condition'.
  - iii) IFRS 3 "Business combinations" amended to clarify the classification and measurement of contingent consideration in a business combination. It has been further amended to clarify that the standard does not apply to the accounting for the formation of all types of joint arrangements in IFRS 11
  - iv) IFRS 8 "Operating segments" has been amended to explicitly require disclosure of judgements made by management in applying aggregation criteria.
  - v) IFRS 13 has been amended to clarify measurement of interest free short term receivables and payables at their invoiced amount without discounting, if the effect of discounting is immaterial. It has been further amended to clarify that the portfolio exception potentially applies to contracts in the scope of IAS 39 and IFRS 9 regardless of whether they meet the definition of a financial asset or financial liability under IAS 32.
  - vi) IAS 16 "Property, plant and equipment" and IAS 38 "Intangible assets": The amendments clarify the requirements of revaluation model recognising that the restatement of accumulated depreciation (amortisation) is not always proportionate to the change in the gross carrying amount of the asset.
  - vii) IAS 24 "Related party disclosures" the definition of a related party is extended to include a management entity that provides key management personnel services to the reporting entity, either directly or indirectly.
  - viii) IAS 40 "Investment property" clarifies that an entity should assess whether an acquired property is an investment property under IAS 40 and perform a separate assessment under IFRS 3 to determine whether the acquisition constitutes a business combination.

#### b) Basis of consolidation

The consolidated financial statements comprise the financial statements of Riyad Bank and its subsidiaries drawn up to 31 December each year. The financial statements of the subsidiaries are prepared for the same reporting year 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 the ability to affect those returns through its power over the investee. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases.

Balances between the Bank and its subsidiaries, and any income and expenses arising from intra-group transactions are eliminated in preparing the consolidated financial statements.

The Bank is party to certain special purpose entities (SPEs), primarily for the purpose of facilitation of certain

For the years ended December 31, 2015 and 2014

Shariah compliant financing arrangements. Bank concluded that these entities cannot be consolidated to its financial statements as it could not establish control over these SPEs.

#### c) Settlement date accounting

All regular way purchases and sales of financial assets are recognised and derecognised on the settlement date, i.e. the date the asset is delivered to the counter party. The Bank accounts for any change in fair value between the trade and the settlement date in the same way as it accounts for the acquired assets. Regular way purchases or sales are purchases or sales of financial instruments that require delivery of assets within the time frame generally established by regulation or convention in the market place.

#### d) Investment in associates

An associate is an entity, including an unincorporated entity such as a partnership, over which the investor has significant influence and that is neither a subsidiary nor an interest in a joint venture. Significant influence is the power to participate in the financial and operating policy decisions of the investee, but is not control or joint control over those policies. Investments in associates are accounted for under the equity method of accounting. The equity method is a method of accounting whereby the investment is initially recognised at cost and adjusted thereafter for the post-acquisition change in the investor's share of net assets of the investee. The profit or loss of the investor includes the investor's share of the profit or loss of the investee. Distribution received from the investee reduces the carrying amount of the investment.

#### e) Derivative financial instruments and hedge accounting

Derivative financial instruments, including foreign exchange contracts, special commission rate swaps and currency options (both written and purchased), are initially recognised at fair value on the date on which the derivative contract is entered into and are subsequently re-measured at fair value in the statement of financial position with transaction costs recognised in the income statement. All derivatives are carried at their fair value as assets where the fair value is positive and as liabilities where the fair value is negative. Fair values are obtained by reference to quoted market prices, discounted cash flow models and pricing models, as appropriate. The treatment of changes in their fair value depends on their classification into the following categories:

#### (i) Derivatives held for trading

Any changes in the fair value of derivatives that are held for trading purposes are taken directly to the consolidated income statement and disclosed in trading income/ loss. Derivatives held for trading also include those derivatives, which do not qualify for hedge accounting described below.

#### (ii) Hedge accounting

The Group designates certain derivatives as hedging instruments in qualifying hedging relationships.

For the purpose of hedge accounting, hedges are classified into two categories: (a) fair value hedges which hedge the exposure to changes in the fair value of a recognised asset or liability or an unrecognised firm commitment or an identified portion of such an asset, liability or firm commitment, that is attributable to a particular risk and could affect the reported net gain or loss; and (b) cash flow hedges which hedge exposure to variability in cash flows that is either attributable to a particular risk associated with a recognised asset or liability, or to a highly probable forecasted transaction that will affect the reported net gain or loss.

In order to qualify for hedge accounting, the hedge should be expected to be highly effective, i.e. the changes in fair value or cash flows of the hedging instrument should effectively offset corresponding changes in the hedged item, and should be reliably measurable. At the inception of the hedge, the risk management objective

For the years ended December 31, 2015 and 2014

#### 3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

#### e) Derivative financial instruments and hedge accounting (continued)

and strategy is documented, including the identification of the hedging instrument, the related hedged item, the nature of risk being hedged, and how the Bank will assess the effectiveness of the hedging relationship. Subsequently, the hedge is required to be assessed and determined to be an effective hedge on an ongoing basis.

#### a) Fair value hedges

When a derivative is designated as the hedging instrument in a hedge of the change in fair value of a recognised asset or liability or a firm commitment that could affect income statement, any gain or loss from re-measuring the hedging instruments to fair value is recognised immediately in the consolidated income statement. The related portion of the hedged item is adjusted against the carrying amount of the hedged item and recognised in the consolidated income statement. For hedged items measured at amortised cost, where the fair value hedge of a special commission bearing financial instrument ceases to meet the criteria for hedge accounting or is sold, exercised or terminated, the difference between the carrying value of the hedged item on termination and the face value is amortised over the remaining term of the original hedge using the effective yield basis. If the hedged item is derecognised, the unamortised fair value adjustment is recognised immediately in the consolidated income statement.

#### b) Cash flow hedges

When a derivative is designated as the hedging instrument in a hedge of a variability of cash flows attributable to a particular risk associated with a recognised asset or a liability or a highly probable forecasted transaction that could affect income statement, the portion of the gain or loss on the hedging instrument that is determined to be an effective portion is recognised directly in other comprehensive income and the ineffective portion, if any, is immediately recognised in the consolidated income statement. For cash flow hedges affecting future transactions, the gains or losses recognised in other reserves, are transferred to the consolidated income statement in the same period in which the hedged transaction affects the consolidated income statement. Where the hedged forecasted transaction results in the recognition of a non-financial asset or a non-financial liability, then at the time such asset or liability is recognised the associated gains or losses that had previously been recognised directly in other comprehensive income are included in the initial measurement of the acquisition cost or other carrying amount of such asset or liability.

Hedge accounting is discontinued when the hedging instrument expires or is sold, terminated or exercised, or no longer qualifies for hedge accounting, or the forecast transaction is no longer expected to occur or the Bank revokes the designation. At that point of time, any cumulative gain or loss on the cash flow hedging instrument that was recognised in other comprehensive income is retained until the forecasted transaction occurs. Where the hedged forecasted transaction is no longer expected to occur, the net cumulative gain or loss recognised in other comprehensive income is transferred to the consolidated income statement for the period.

#### f) Foreign currencies

The Group's consolidated financial statements are presented in Saudi Arabian Riyals, which is also the parent company's functional currency. Transactions in foreign currencies are translated into Saudi Arabian Riyals at spot exchange rates prevailing on the transaction dates. Monetary assets and liabilities at the year-end, denominated in foreign currencies, are translated into Saudi Arabian Riyals at the exchange rates prevailing at the reporting date. Foreign exchange gains or losses on translation of monetary assets and liabilities denominated in foreign currencies are recognised in the consolidated income statement. Non-monetary items measured at fair value in a foreign currency are translated using the spot exchange rates at the date

For the years ended December 31, 2015 and 2014

when the fair value is determined. Translation gains or losses on non-monetary items carried at fair value are included as part of the fair value adjustment either in the consolidated income statement or in equity, depending on the underlying financial asset.

Non-monetary assets and liabilities that are measured in terms of historical cost in a foreign currency are translated using the spot exchange rates as at the dates of the initial transactions.

The assets and liabilities of overseas branch are translated at the spot exchange rate at the reporting date. The income and expenses of overseas branch are translated at the average exchange rates for the year. All exchange differences, if significant, are recognised in other comprehensive income. These differences are transferred to consolidated income statement at the time of disposal of foreign operations.

#### g) Offsetting financial instruments

Financial assets and liabilities are offset and reported net in the consolidated statement of financial position when the entity has a legal currently enforceable right to set off the recognised amounts and when the Group intends to settle on a net basis, or to realise the asset and settle the liability simultaneously.

Income and expenses are not offset in the consolidated income statement unless required or permitted by an accounting standard or interpretation, and as specifically disclosed in the accounting policies of the Bank.

#### h) Revenue recognition

#### i) Special commission income and expense

Special commission income and expense for all special commission bearing financial instruments, except for those classified as held for trading or designated at fair value through income statement (FVIS), are recognised in the consolidated income statement using the effective yield basis. The effective yield is the rate that exactly discounts the estimated future cash payments and receipts through the expected life of the financial asset or liability (or, where appropriate, a shorter period) to the carrying amount of the financial asset or liability. When calculating the effective special commission rate, the Bank estimates future cash flows considering all contractual terms of the financial instrument but not future credit losses.

The carrying amount of the financial asset or financial liability is adjusted if the Group revises its estimates of payments or receipts. The adjusted carrying amount is calculated based on the original effective special commission rate and the change in carrying amount is recorded as special commission income or expense.

If the recorded value of a financial asset or a group of similar financial assets has been reduced due to an impairment loss, special commission income continues to be recognised using the original effective yield applied to the new carrying amount.

The calculation of the effective yield includes all fees and points paid or received, transaction costs, and discounts or premiums that are an integral part of the effective special commission rate. Transaction costs are incremental costs that are directly attributable to the acquisition, issue or disposal of financial asset or liability.

#### ii) Fee and commission income

Fee and commissions are recognised when the service has been provided. Loan commitment fees for loans that are likely to be drawn down are deferred, together with the related direct cost, and are recognised as an adjustment to the effective yield on the loan. When a loan commitment is not expected to result in the drawdown of a loan, loan commitment fees are recognised on a straight-line basis over the commitment period. Portfolio and other management advisory and service fees are recognised based on the applicable service

For the years ended December 31, 2015 and 2014

#### 3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

#### h) Revenue recognition (continued)

contracts, usually on a time-proportionate basis. Fee received on asset management, wealth management, financial planning, custody services and other similar services that are provided over an extended period of time, are recognised over the period when the service is being provided.

#### iii) Others

Dividend income is recognised when the right to receive payment is established. Exchange income/ loss are recognised when earned/ incurred. Results arising from trading activities include gains and losses from changes in fair value and related special commission income or expense for financial assets and financial liabilities held for trading.

#### i) Sale and repurchase agreements

Assets sold with a simultaneous commitment to repurchase at a specified future date (repos) continue to be recognised in the consolidated statement of financial position and are measured in accordance with related accounting policies for investments held as FVIS, Available for sale, Held to maturity and Other investments held at amortised cost. The counterparty liability for amounts received under these agreements is included in "Due to banks and other financial institutions" or "Customer deposits", as appropriate. The difference between sale and repurchase prices is treated as special commission expense and is accrued over the life of the repo agreement on an effective special commission rate basis. Assets purchased with a corresponding commitment to resell at a specified future date (reverse repos), are not recognised in the consolidated statement of financial position, as the Bank does not obtain control over the assets.

Amounts paid under these agreements are included in "Cash and balances with SAMA" or "Due from banks and other financial institutions" as appropriate. The difference between purchase and resale prices is treated as special commission income and accrued over the life of the reverse repo agreement on an effective yield basis.

#### j) Investments

All investment securities are initially recognised at fair value, including incremental direct transaction cost except for investments held as Fair Value through Income Statement (FVIS) and are subsequently accounted for depending on their classification as either held to maturity, FVIS, Available for sale or other investments held at amortised cost. Premiums are amortised and discounts accreted using the effective yield basis and are taken to special commission income.

For securities traded in organised financial markets, fair value is determined by reference to exchange quoted market bid prices at the close of business on the reporting date. Fair value of managed assets and investments in mutual funds are determined by reference to declared net asset values.

For securities where there is no quoted market price, a reasonable estimate of the fair value is determined by reference to the current market value of another instrument which is substantially the same, or is based on the expected cash flows of the security. Where the fair values cannot be derived from active markets, they are determined using a variety of valuation techniques that include the use of mathematical models if possible. The input to these models is taken from observable markets where possible, but where this is not feasible, a degree of judgement is required in establishing fair values.

Following recognition, subsequent transfers between the various classes of investments are not ordinarily permissible except in accordance with amendments in IAS 39 (refer note 6). The subsequent period-end reporting values for each class of investment are determined on the basis as set out in the following paragraphs:

For the years ended December 31, 2015 and 2014

#### i) Held as FVIS

Investments in this category are classified at initial recognition as either investment held for trading or those upon initial recognition designated as FVIS. Investments classified as trading are acquired principally for the purpose of selling or repurchasing in short term.

After initial recognition, investments at FVIS are measured at fair value and any change in the fair value is recognised in the consolidated income statement for the period in which it arises. Transaction costs, if any, are not added to the fair value measurement at initial recognition of FVIS investments. Special commission income and dividend income on investment securities held as FVIS are reflected as trading income.

#### ii) Available for sale

Available for sale investments are non-derivative financial instruments and include equity and debt securities that are either designated as Available for sale or not classified as (a) loans and receivables, (b) held-to-maturity investments or (c) financial assets at fair value through profit or loss. Available for sale investments are those equity and debt securities intended to be held for an unspecified period of time, which may be sold in response to needs for liquidity or changes in special commission rates, exchange rates or equity prices. Investments, which are classified as "Available for sale", are subsequently measured at fair value. For an Available for sale investment where the fair value has not been hedged, any gain or loss arising from a change in its fair value is recognised directly in other comprehensive income. On derecognition, any cumulative gain or loss previously recognised in other comprehensive income is included in the consolidated income statement.

#### iii) Other investments held at amortised cost

Investment securities with fixed or determinable payments that are not quoted in an active market are classified as "Other investments held at amortised cost". Such investments whose fair values have not been hedged are stated at amortised cost using effective yield basis, less provision for impairment. Any gain or loss is recognised in the consolidated income statement when the investment is derecognised or impaired.

#### iv) Held to maturity

Investments having fixed or determinable payments and fixed maturity and that the Bank has the positive intention and ability to hold to maturity, are classified as held to maturity. Held to maturity investments are subsequently measured at amortised cost, less provision for impairment in value. Amortised cost is calculated by taking into account any discount or premium on acquisition using an effective yield basis. Any gain or loss on such investments is recognised in the consolidated income statement when the investment is derecognised or impaired.

Investments classified as held to maturity cannot ordinarily be sold or reclassified without impacting the Bank's ability to use this classification and cannot be designated as a hedged item with respect to commission rate or prepayment risk, reflecting the longer-term nature of these investments.

#### k) Loans and advances

Loans and advances are non-derivative financial assets originated or acquired by the Bank with fixed or determinable payments. Loans and advances are recognised when cash is advanced to borrowers. They are derecognised when either borrower repay their obligations, or the loans are sold or written off, or substantially all the risks and rewards of ownership are transferred.

All loans and advances are initially measured at fair value, including directly attributable transaction costs associated with the loans and advances. Loans and advances originated or acquired by the Bank that are not quoted in an active market, are stated at amortised cost. For presentation purposes, allowance for credit losses is deducted from loans and advances.

For the years ended December 31, 2015 and 2014

#### 3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

#### I) Impairment of financial assets

An assessment is made at each reporting date to determine whether there is objective evidence that a financial asset or group of financial assets carried at amortised cost may be impaired. If such evidence exists, the estimated recoverable amount of that asset is determined and any impairment loss, based on the net present value of future anticipated cash flows, is recognised for changes in its carrying amounts.

Objective evidence that financial assets are impaired can include default or delinquency by a borrower, restructuring of a loan or advance by the group on the terms that the Bank would not otherwise consider, indications that a borrower or issuer will enter bankruptcy, the disappearance of active market for a security or other observable data relating to a group of assets such as adverse changes in the payment status of borrowers or issuers.

It may also include instances where Bank considers that the obligor is unlikely to pay its credit obligations to the Bank, in full, without recourse by the Bank to actions such as realizing the security, if held.

When a financial asset is uncollectible, it is written off against the related provision for impairment either directly by a charge to consolidated income statement or through impairment allowance account. Financial assets are written off only in circumstances where effectively all possible means of recovery have been exhausted, and the amount of the loss has been determined

Once a financial asset has been written down to its estimated recoverable amount, special commission income is thereafter recognised based on the rate of special commission that was used to discount the future cash flows for the purpose of measuring the recoverable amount.

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

Loans whose terms have been renegotiated are no longer considered to be past due. Restructuring policies and practices are based on indicators or criteria, which indicate that payments, will most likely continue. The loans continue to be subject to an individual or collective impairment assessment, calculated using the loan's original effective yield rate. Consumer loans are charged off when they become 180 days past due except in the case of secured consumer loans. With effect from April 1, 2015, the Bank individually assesses consumer mortgage loans for impairment when they become 180 days past due and provision is made.

#### i) Impairment of financial assets held at amortised cost

In case of financial instruments held at amortised cost or held to maturity, the Bank assesses individually whether there is objective evidence of impairment based on same criteria as explained above.

A specific provision for credit losses due to impairment of a loan or any other financial asset held at amortised cost is established if there is objective evidence that the Bank will not be able to collect all amounts due. The

amount of the specific provision is the difference between the carrying amount and the estimated recoverable amount. The estimated recoverable amount is the present value of expected cash flows, including amounts estimated to be recoverable from guarantees and collateral, discounted based on the original effective yield rate.

For the years ended December 31, 2015 and 2014

The Bank also considers evidence of impairment at a collective assets level. The collective provision is based on deterioration in the internal grading or external credit ratings, allocated to the borrower or group of borrowers, the current economic climate in which the borrowers operate and the experience and historical default patterns that are embedded in the components of the credit portfolio.

#### ii) Impairment of Available for sale financial assets

In the case of debt instruments classified as Available for sale, the Bank assesses individually whether there is objective evidence of impairment based on the same criteria as explained above. However, the amount recorded for impairment is the cumulative loss measured as the difference between the amortised cost and the current fair value, less any impairment loss on that investment previously recognised in the consolidated income statement.

If, in a subsequent period, the fair value of a debt instrument increases and the increase can be objectively related to credit event occurring after the impairment loss was recognised in the consolidated income statement, the impairment loss is reversed through the consolidated income statement.

For equity investments held as Available for sale, a significant or prolonged decline in fair value below its cost represents objective evidence of impairment. The impairment loss cannot be reversed through consolidated income statement as long as the asset continues to be recognised i.e. any increase in fair value after impairment has been recorded can only be recognised in equity. On derecognition, any cumulative gain or loss previously recognised in shareholders' equity is included in the consolidated income statement for the year.

#### m) Other real estate

The Bank, in the ordinary course of business, acquires certain real estate against settlement of due loans and advances. Such real estate properties are considered as assets held for sale and are initially stated at the lower of net realisable value of due loans and advances or the current fair value of the related properties, less any costs to sell, if material. Rental income from other real estate is recognised in the consolidated income statement. No depreciation is charged on such real estate.

Subsequent to initial recognition, any subsequent write down to fair value, less costs to sell, is charged to the consolidated income statement. Any subsequent gain in the fair value less costs to sell of these assets to the extent this does not exceed the cumulative write down is recognised as income together with any gain/ loss on disposal.

#### n) Property and equipment

Property and equipment is stated at cost and presented net of accumulated depreciation. Freehold land is not depreciated. The cost of other property and equipment is depreciated using the straight-line method over the estimated useful lives of the assets as follows:

Buildings 33 years

Improvements and decoration of premises over the lower of the lease period or 5 years

Furniture, fixtures and equipment 5 to 20 years
Computer hardware 5 years
Software programs and automation projects 3 to 5 years
Motor vehicles 4 years

For the years ended December 31, 2015 and 2014

#### 3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

#### n) Property and equipment (continued)

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at each reporting date. All assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. Any carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount. Gains and losses on disposals are determined by comparing proceeds with carrying amount and are included in consolidated income statement.

#### o) Financial liabilities

All money market deposits, customer deposits and debt securities in issue are initially recognised at fair value less transaction costs. Subsequently, all special commission-bearing financial liabilities other than those held at FVIS or where fair values have been hedged are measured at amortised cost. Amortised cost is calculated by taking into account any discount or premium. Premiums are amortised and discounts accreted on an effective yield basis to maturity and taken to special commission expense.

Financial liabilities in an effective fair value hedge relationship are adjusted for fair value changes to the extent of the risk being hedged. The resultant gain or loss is recognised in the consolidated income statement. For financial liabilities carried at amortised cost, any gain or loss is recognised in the consolidated income statement when derecognised.

#### p) Guarantee contracts

In ordinary course of business, the Bank gives financial guarantees, consisting of letters of credit, guarantees and acceptances. Financial guarantees are initially recognised in the consolidated financial statements at fair value in other liabilities, being the value of the premium received. Subsequent to the initial recognition, the Bank's liability under each guarantee is measured at the higher of the amortised premium and the best estimate of expenditure required to settle any financial obligations arising as a result of guarantees. Any increase in the liability relating to the financial guarantee is taken to the consolidated income statement in 'impairment charge for credit losses'. The premium received is recognised in the consolidated income statement in 'Fee and commission income, net' on a straight line basis over the life of the guarantee.

#### q) Provisions

Provisions are recognised when a reliable estimate can be made by the Bank for a present legal or constructive obligation as a result of past events and it is more likely than not that an outflow of resources will be required to settle the obligation.

#### r) Accounting for leases

Leases entered into by the Group as a lessee, are operating leases. Payments made under operating leases are charged to the consolidated income statement on a straight-line basis over the period of the lease. When an operating lease is terminated before the lease period has expired, any payment required to be made to the lessor by way of penalty is recognised as an expense in the period in which termination takes place.

#### s) Cash and cash equivalents

For the purpose of the consolidated statement of cash flows, cash and cash equivalents are defined as those amounts included in cash, balances with SAMA excluding statutory deposits, and due from banks and other financial institutions maturing within three months from the date of acquisition.

For the years ended December 31, 2015 and 2014

#### t) Derecognition of financial instruments

A financial asset (or a part of a financial asset, or a part of a group of similar financial assets) is derecognised, when the contractual rights to receive the cash flows from the financial asset expires or the asset is transferred and the transfer qualifies for de-recognition.

In instances where the Bank is assessed to have transferred a financial asset, the asset is derecognised if the Bank has transferred substantially all the risks and rewards of ownership. Where the Bank has neither transferred nor retained substantially all the risks and rewards of ownership, the financial asset is derecognised only if the Bank has not retained control of the financial asset. The Bank recognises separately as assets or liabilities any rights and obligations created or retained in the process.

A financial liability (or a part of a financial liability) can only be derecognised when it is extinguished, that is when the obligation specified in the contract is either discharged, cancelled or expires.

#### u) End of service benefits

Benefits payable to the employees of the Bank at the end of their services are accrued in accordance with the guidelines set by the Saudi Arabian Labor Regulations and are included in other liabilities in the consolidated statement of financial position.

#### v) Zakat

Under Saudi Arabian Zakat and Income Tax Laws, Zakat is the liability of shareholders. Zakat is computed on the shareholders' equity or net income using the basis defined under the Zakat regulations. Zakat is not charged to the Group's consolidated income statement as they are deducted from the dividends paid to the shareholders.

#### w) Investment management services

The Group offers investment services to its customers, which include management of certain investment funds. Fees earned are disclosed under related party transactions. Assets held in trust or in a fiduciary capacity are not treated as assets of the Group and accordingly, are not included in the consolidated financial statements.

#### x ) Non-special commission based banking products

In addition to the conventional banking, the Bank offers its customers certain non-special commission based banking products, which are approved by its Shariah Board. These products include Murabaha, Tawaraq and Ijara. These banking products are accounted for using IFRS and are in conformity with the accounting policies described in these consolidated financial statements.

- i) Murabaha is an agreement whereby the Bank sells to a customer a commodity or an asset, which the Bank has purchased and acquired based on a promise received from the customer to buy. The selling price comprises the cost plus an agreed profit margin.
- ii) Ijarah is a an agreement whereby the Bank, acting as a lessor, purchases or constructs an asset for lease according to the customer request (lessee), based on his promise to lease the asset for an agreed rent and specific period that could end by transferring the ownership of the leased asset to the lessee.
- iii) Tawaraq is a form of Murabaha transactions where the Bank purchases a commodity and sells it to the customer. The customer sells the underlying commodity at spot and uses the proceeds for his financing requirements.

For the years ended December 31, 2015 and 2014

#### 3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

#### y) Short term employee benefits

Short term employee benefits are measured on an undiscounted basis and are expensed as the related service is provided. A liability is recognised for the amount expected to be paid under short term cash bonus plans if the Group has a present legal or constructive obligation to pay this amount as a result of past service provided by employees and the obligation can be estimated reliably.

#### **4. CASH AND BALANCES WITH SAMA**

SAR'000	2015	2014
Cash in hand and other balances	4,117,564	3,550,983
Statutory deposit	8,797,578	8,269,753
Reverse repos with SAMA	7,654,787	13,495,000
Total	20,569,929	25,315,736

In accordance with the Banking Control Law and regulations issued by SAMA, the Bank is required to maintain a statutory deposit with SAMA at stipulated percentages of its demand, savings, time and other deposits, calculated at the end of each month. The statutory deposit with SAMA is not available to finance the Bank's day-to-day operations and therefore is not part of cash and cash equivalents (note 26).

#### 5. DUE FROM BANKS AND OTHER FINANCIAL INSTITUTIONS

SAR'000	2015	2014
Current accounts	1,057,450	519,925
Money market placements	8,211,930	3,394,579
Total	9,269,380	3,914,504

For the years ended December 31, 2015 and 2014

#### 6. INVESTMENTS, NET

#### a) Investment securities are classified as follows:

#### i) Held as FVIS

On September 1, 2008, the Group reclassified investments held in trading portfolio reported under its investments at fair value through income statement ("FVIS") category to the available for sale category.

The carrying and fair value of these reclassified investments as at December 31, 2015 was SAR 3,169 million (December 31, 2014: SAR 3,560 million).

Had the reclassification not occurred, the consolidated income statement for the year ended December 31, 2015, would have included fair value gain on such reclassified investments amounting to SAR 3.1 million (December 31, 2014: unrealised fair value gain SAR 133.9 million).

#### ii) Available for sale

	Dome	estic	Interna	itional	Total	
SAR'000	2015	2014	2015	2014	2015	2014
Fixed rate securities	-	-	11,126,714	11,894,298	11,126,714	11,894,298
Floating rate securities	-	-	1,722,234	1,886,466	1,722,234	1,886,466
Mutual funds	184,347	143,307	1,251,877	1,631,785	1,436,224	1,775,092
Equities	1,166,443	1,244,289	150,208	127,985	1,316,651	1,372,274
Available for sale, net	1,350,790	1,387,596	14,251,033	15,540,534	15,601,823	16,928,130

International investments above includes investment portfolios of SAR 11.2 billion (2014: SAR 11.6 billion) which are externally managed.

#### iii) Other investments held at amortised cost

	Dom	estic	Interna	ational	Total		
SAR'000	2015	2014	<b>2015</b> 2014		2015	2014	
Fixed rate securities	22,924,175	23,416,933	1,038,553	1,987,994	23,962,728	25,404,927	
Floating rate securities	4,722,988	4,155,274	220,000	248,856	4,942,988	4,404,130	
Other investments held							
at amortised cost	27,647,163	27,572,207	1,258,553	2,236,850	28,905,716	29,809,057	

#### iv) Held to maturity

	Dom	estic	Intern	ational	Total		
SAR'000	2015	2014	2015	2014	2015	2014	
Fixed rate securities Floating rate securities	44,844	94,743	-	131,339	44,844	226,082	
Held to maturity	44,844	94,743	-	131,339	44,844	226,082	
Investments, net	29,042,797	29,054,546	15,509,586	17,908,723	44,552,383	46,963,269	

For the years ended December 31, 2015 and 2014

## **6. INVESTMENTS, NET** (continued)

b) The analysis of the composition of investments is as follows:

		2015		2014			
SAR'000	Quoted	Unquoted*	Total	Quoted	Unquoted*	Total	
Fixed rate securities	14,281,835	20,852,451	35,134,286	15,895,411	21,629,896	37,525,307	
Floating rate securities	4,392,420	2,272,802	6,665,222	5,436,359	854,237	6,290,596	
Equities	1,071,939	284,630	1,356,569	1,234,513	178,017	1,412,530	
Mutual funds	1,436,225	-	1,436,225	1,775,092	-	1,775,092	
	21,182,419	23,409,883	44,592,302	24,341,375	22,662,150	47,003,525	
Allowance for impairment	-	(39,919)	(39,919)	-	(40,256)	(40,256)	
Investments, net	21,182,419	23,369,964	44,552,383	24,341,375	22,621,894	46,963,269	

<sup>\*</sup>Unquoted fixed rate securities include Treasury Bills of SAR 15.1 billion (2014: SAR 19.9 billion)

# c) The analysis of unrealised gains and losses and the fair values of other investments held at amortised cost, and held to maturity investments, is as follows:

#### i) Other investments held at amortised cost

		20	15		2014			
SAR'000	Carrying value	Gross unrealised gain	Gross unrealised loss	Fair value	Carrying value	Gross unrealised gain	Gross unrealised loss	Fair value
Fixed rate securities	23,962,728	117,739	(240,886)	23,839,581	25,404,927	262,671	(10,622)	25,656,976
Floating rate securities	4,942,988	333,159	-	5,276,147	4,404,130	309,841	-	4,713,971
Total	28,905,716	450,898	(240,886)	29,115,728	29,809,057	572,512	(10,622)	30,370,947

## ii) Held to maturity

		20	15		2014			
SAR'000	Carrying value	Gross unrealised gain	Gross unrealised loss	Fair value	Carrying value	Gross unrealised gain	Gross unrealised loss	Fair value
Fixed rate securities	44,844	428	-	45,272	226,082	3,337	-	229,419
Floating rate securities	-	-	-	-	-	-	-	-
Total	44,844	428	-	45,272	226,082	3,337	-	229,419

For the years ended December 31, 2015 and 2014

## d) Credit quality of investments

		20	15		2014			
SAR'000	Fixed rate securities	Floating rate securities	Others	Total	Fixed rate securities	Floating rate securities	Others	Total
Grade A- and above	29,247,478	1,876,744	-	31,124,222	31,259,439	2,503,509	-	33,762,948
Lower than A-	5,546,819	215,489	-	5,762,308	4,944,176	275,976	-	5,220,152
Unrated	339,989	4,572,989	2,752,875	7,665,853	1,321,692	3,511,111	3,147,366	7,980,169
Total	35,134,286	6,665,222	2,752,875	44,552,383	37,525,307	6,290,596	3,147,366	46,963,269

The above classification is based on Standard & Poor's/ equivalent credit ratings. Lower than A- comprises mainly of bonds rated BBB and BB. The Others in the unrated investments category comprise of mutual funds and equities.

## e) The analysis of investments by counter-party is as follows:

SAR'000	2015	2014
Government and quasi Government	25,753,838	27,425,170
Corporate	9,458,871	9,960,169
Banks and other financial institutions	9,339,674	9,577,930
Total	44,552,383	46,963,269

Investments include SAR 700.3 million (2014: SAR 659.4 million), which have been pledged under repurchase agreements with customers (note 19 d). The market value of such investments is SAR 700.3 million (2014: SAR 659.6 million).

## f) Movements of allowance for impairment on available for sale equity investments:

SAR'000	2015	2014
Balance at beginning of the year	40,256	40,681
Other movements	(337)	(425)
Balance at end of the year	39,919	40,256

For the years ended December 31, 2015 and 2014

## 7. LOANS AND ADVANCES, NET

#### a) Loans and advances held at amortised cost

These comprise the following:

2015 SAR'000	Overdrafts	Credit cards	Consumer loans*	Commercial loans **	Others	Total	
Performing loans and advances, gross	10,008,311	816,905	37,858,884	95,351,580	1,215,294	145,250,974	
Non-performing loans and advances, net	186,692	-	76,212	1,048,943	9,756	1,321,603	
Total Loans and advances	10,195,003	816,905	37,935,096	96,400,523	1,225,050	146,572,577	
Allowance for							
impairment	(109,212)	-	(14,836)	(697,433)	(4,917)	(826,398)	
Total	10,085,791	816,905	37,920,260	95,703,090	1,220,133	145,746,179	
Portfolio provision							
Loans and advances held at amortised cost, net							

		to the second		
Loans and	advances	neid at	amortised	cost, net

2014 SAR'000	Overdrafts	Credit cards	Consumer loans*	Commercial loans**	Others	Total	
Performing loans and advances, gross	8,309,591	979,453	38,430,973	86,417,579	289,345	134,426,941	
Non-performing loans and advances, net	141,462	-	-	898,087	10,378	1,049,927	
Total Loans and advances	8,451,053	979,453	38,430,973	87,315,666	299,723	135,476,868	
Allowance for impairment	(51,093)	-	-	(853,447)	(9,705)	(914,245)	
Total	8,399,960	979,453	38,430,973	86,462,219	290,018	134,562,623	
Portfolio provision							
Loans and advances held at amortised cost, net							

Loans and advances, net, include Islamic products of SAR 71,181 million (2014: SAR 68,205 million).

<sup>\*</sup> Includes consumer mortgage loans

<sup>\*\*</sup>Includes overdrafts and other loans

For the years ended December 31, 2015 and 2014

## b) Movements in allowance for impairment are as follows:

2015		Allowance fo				
SAR'000	Credit cards	Consumer loans*	Commercial loans **	Total	Portfolio provision	Total
Balance at beginning of the year	_		914,245	914,245	1,072,349	1,986,594
Provided during the year	193,827	1,327,698	8,415	1,529,940	-	1,529,940
Bad debts written off	(193,827)	(1,312,862)	(33,199)	(1,539,888)	-	(1,539,888)
Recoveries of previously provided amounts	-	-	(46,306)	(46,306)	-	(46,306)
***Other movements	-	-	(31,593)	(31,593)	-	(31,593)
Balance at end of the year	-	14,836	811,562	826,398	1,072,349	1,898,747

2014	4 Allowance for impairment							
SAR'000	Credit cards	Consumer loans*	Commercial loans **	Total	Portfolio provision	Total		
Balance at beginning of the year	-	-	859,346	859,346	1,072,349	1,931,695		
Provided during the year	76,978	439,133	719,413	1,235,524	-	1,235,524		
Bad debts written off	(76,978)	(439,133)	(600,006)	(1,116,117)	-	(1,116,117)		
Recoveries of previously provided amounts	-	-	(43,054)	(43,054)	-	(43,054)		
***Other movements	-	-	(21,454)	(21,454)	-	(21,454)		
Balance at end of the year	-	-	914,245	914,245	1,072,349	1,986,594		

During the year, the net charge to the consolidated statement of income on account of impairment charge for credit losses, net is SAR 1,031 million (2014: SAR 900 million) representing amounts provided during the year, net of recoveries of SAR 1,484 million (2014: SAR 1,192 million) and recoveries from amounts previously written off of SAR 453 million (2014: SAR 292 million).

<sup>\*</sup> Includes consumer mortgage loans

<sup>\*\*</sup> Includes overdrafts and other loans

<sup>\*\*\*</sup> Represents unwinding of accrued special commission income on impaired financial assets

For the years ended December 31, 2015 and 2014

## 7. LOANS AND ADVANCES, NET (continued)

#### c) Credit quality of loans and advances

i) Neither past due nor impaired

2015 SAR'000	Credit cards	Consumer loans*	Commercial loans**	Total
Standard category	635,489	35,397,068	106,124,814	142,157,371
Special mention category	-	-	384,333	384,333
Total	635,489	35,397,068	106,509,147	142,541,704
2014 SAR'000	Credit cards	Consumer loans*	Commercial loans**	Total
Standard category Special mention category	665,562	34,502,437	94,213,699 594,482	129,381,698 594,482
Total	665,562	34,502,437	94,808,181	129,976,180

The Group uses an internal classification system based on risk ratings for its credit customers. The risk rating system, which is managed by an independent unit, provides a rating at the obligor level. The risk rating system includes twelve grades, of which nine grades relate to the performing portfolio covering Standard and Special Mention category and the rest to non-performing loans.

Standard category: A credit with very strong to satisfactory credit quality and repayment ability, where regular monitoring is carried out.

Special mention category: A credit that requires close monitoring by management due to deterioration in the borrowers' financial condition.

Standard category as at December 31, 2015 includes commercial loans\*\* of very strong quality amounting to SAR 23,472 million (2014: SAR 23,471 million), good quality amounting to SAR 72,345 million (2014: SAR 59,278 million) and satisfactory quality amounting to SAR 10,308 million (2014: SAR 11,465 million).

<sup>\*</sup> Includes consumer mortgage loans

<sup>\*\*</sup>Includes overdrafts and other loans

For the years ended December 31, 2015 and 2014

# ii) Ageing of loans and advances (Past due but not impaired)

2015 SAR'000	Credit cards	Consumer loans*	Commercial loans**	Total
Upto 30 days	93,996	1,603,700	11,762	1,709,458
•	·			
From 31 - 90 days	40,820	528,883	48,494	618,197
From 91 - 180 days	46,600	329,233	5,782	381,615
More than 180 days	-	-	-	-
Total	181,416	2,461,816	66,038	2,709,270
2014	Credit	Consumer	Commercial	
SAR'000	cards	loans*	loans**	Total
Upto 30 days	94,888	1,917,809	204,892	2,217,589
From 31 - 90 days	105,223	944,440	3,442	1,053,105
From 91 - 180 days	113,780	1,066,287	-	1,180,067
More than 180 days	-	-	-	-
Total	313,891	3,928,536	208,334	4,450,761

<sup>\*</sup> Includes consumer mortgage loans

<sup>\*\*</sup> Includes overdrafts and other loans

For the years ended December 31, 2015 and 2014

## 7. LOANS AND ADVANCES, NET (continued)

d) Economic sector risk concentration for the loans and advances and allowance for impairment are as follows

		20	15		2014			
SAR' 000	Performing	Non performing, net	Allowance for impairment	Loans and advances, net	Performing	Non performing, net	Allowance for impairment	Loans and advances, net
Government and quasi Government	-	-	-	-	8,001	-	-	8,001
Banks and other financial institutions	5,902,182	-	-	5,902,182	4,905,740	-	-	4,905,740
Agriculture and fishing	1,642,973	-	-	1,642,973	1,176,122	-	-	1,176,122
Manufacturing	24,541,927	112,337	(77,149)	24,577,115	21,218,208	129,864	(108,372)	21,239,700
Mining and quarrying	8,568,949		-	8,568,949	7,282,877	-	-	7,282,877
Electricity, water, gas and health services	2,393,024	-	-	2,393,024	2,385,184	-	-	2,385,184
Building and construction	15,463,892	514,198	(291,884)	15,686,206	12,869,148	277,470	(222,433)	12,924,185
Commerce	36,597,073	608,646	(435,020)	36,770,699	32,432,248	631,908	(573,486)	32,490,670
Transportation and communication	4,660,778	8,998	(6,953)	4,662,823	5,326,199	10,326	(9,641)	5,326,884
Services	6,696,891	1,212	(556)	6,697,547	6,612,961	359	(313)	6,613,007
Consumer loans and credit cards	38,675,789	76,212	(14,836)	38,737,165	39,410,426	-	-	39,410,426
Other	107,496	-	-	107,496	799,827	-	-	799,827
Total	145,250,974	1,321,603	(826,398)	145,746,179	134,426,941	1,049,927	(914,245)	134,562,623
Portfolio provision				(1,072,349)				(1,072,349)
Loans and advances, net				144,673,830				133,490,274

## e) Collateral

The Bank in the ordinary course of lending activities holds 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 realisable values. Management monitors the market value of the collateral and requests additional collateral in accordance with the underlying agreement when deemed necessary. Fair value of collateral held by Group against financing and advances by each category are as follows:

For the years ended December 31, 2015 and 2014

SAR'000	2015	2014
Neither past due nor impaired	42,437,701	41,076,041
Past due but not impaired	1,466,867	1,927,439
Impaired	693,376	484,437
Total	44,597,944	43,487,917

#### **8. INVESTMENT IN ASSOCIATES**

Investment in associates represents the Bank's share of investment in entities where the Bank has significant influence. These investments are accounted for using the equity method of accounting. Investment in associates represents 35% (2014: 35%) share ownership in Ajil Financial Services Company incorporated in Kingdom of Saudi Arabia, 21.4 % (2014: 21.4%) share in ownership in Royal and Sun Alliance Insurance (Middle East) Limited E.C., incorporated in Bahrain and 19.9% (2014: 19.9%) share ownership and Board representation in Al-Alamiya for Cooperative Insurance Company incorporated in Kingdom of Saudi Arabia.

## 9. PROPERTY AND EQUIPMENT, NET

SAR' 000	Land and buildings	Improve- ments and decoration of premises	Furniture, fixtures and equipment	Computer hardware, software programs and automation projects	Motor vehicles	Total 2015	Total 2014
Cost							
Balance at beginning							
of the year	1,413,529	770,742	421,981	2,294,221	913	4,901,386	4,607,867
Additions	47,281	50,991	19,999	345,526	284	464,081	301,814
Disposals	(310)	(6)	(291)	(222)	(145)	(974)	(8,295)
Balance at end of the year	1,460,500	821,727	441,689	2,639,525	1,052	5,364,493	4,901,386
Accumulated depreciation and amortisation							
Balance at beginning							
of the year	486,226	672,007	338,641	1,696,868	913	3,194,655	2,945,217
Charge for the year	20,699	38,382	25,799	190,846	48	275,774	257,665
Disposals	-	(6)	(291)	(195)	(145)	(637)	(8,227)
Balance at end of the year	506,925	710,383	364,149	1,887,519	816	3,469,792	3,194,655
Net book value							
As at December 31, 2015	953,575	111,344	77,540	752,006	236	1,894,701	
As at December 31, 2014	927,303	98,735	83,340	597,353	-		1,706,731

Land and buildings and improvements and decoration of premises include work in progress as at December 31, 2015 amounting to SAR 2.4 million (2014: SAR 62.7 million) and SAR 0.5 million (2014: SAR 2.1 million), respectively.

For the years ended December 31, 2015 and 2014

#### **10. OTHER ASSETS**

SAR'000	2015	2014
Accrued special commission receivable		
- banks and other financial institutions	121	872
- investments	213,021	184,300
- loans and advances	392,361	329,437
- other	13,312	3,106
Total accrued special commission receivable	618,815	517,715
Accounts receivable	254,250	223,712
Positive fair value of derivatives (note 11)	197,539	419,112
Other	501,506	1,178,903
Total	1,572,110	2,339,442

#### 11. DERIVATIVES

In the ordinary course of business, the Bank utilises the following derivative financial instruments for both trading and hedging purposes:

#### a) Swaps

Swaps are commitments to exchange one set of cash flows for another. For special commission rate swaps, counterparties generally exchange fixed and floating special commission rate payments in a single currency without exchanging principal. For currency swaps, principal, fixed and floating commission payments are exchanged in different currencies.

#### b) Forwards and futures

Forwards and futures are contractual agreements to either buy or sell a specified currency, commodity or financial instrument at a specified price and date in the future. Forwards are customised contracts transacted in the over-the-counter market. Foreign currency and special commission rate futures are transacted in standardised amounts on regulated exchanges and changes in futures contract values are settled daily.

#### c) Options

Options are contractual agreements under which the seller (writer) grants the purchaser (holder) the right, but not the obligation, to either buy or sell at a fixed future date or at any time during a specified period, a specified amount of a currency, commodity or financial instrument at a pre-determined price.

#### Held for trading purposes

Most of the Bank's derivative trading activities relate to sales, positioning and arbitrage. Sales activities involve offering products to customers and banks in order, inter alia, to enable them to transfer, modify or reduce current and future risks. Positioning involves managing market risk positions with the expectation of profiting from favourable movements in prices, rates or indices. Arbitrage involves identifying pricing anomalies in different markets and products, with the expectation of profiting from price differentials between markets or products.

For the years ended December 31, 2015 and 2014

#### Held for hedging purposes

The Bank has adopted a comprehensive system for the measurement and management of risk. Part of the risk management process involves managing the Bank's exposure to fluctuations in foreign exchange rates and special commission rates to reduce its exposure to currency and special commission rate risks to acceptable levels as determined by the Board of Directors within the guidelines issued by SAMA. The Board of Directors has established levels of currency risk by setting limits on counterparty and currency position exposures. Positions are monitored on a daily basis and hedging strategies are used to ensure positions are maintained within the established limits. The Board of Directors have also established the level of special commission rate risk by setting limits on special commission rate gaps for stipulated periods. Asset and liability special commission rate gaps are reviewed on a periodic basis and hedging strategies are used to reduce special commission rate gap within the established limits.

As part of its asset and liability management, the Bank uses derivatives for hedging purposes in order to adjust its own exposure to currency and special commission rate risks. This is generally achieved by hedging specific transactions as well as strategic hedging against overall consolidated statement of financial position exposures. Strategic hedging, other than portfolio hedges for special commission rate risks, does not qualify for special hedge accounting and the related derivatives are accounted for as held for trading.

#### Fair value hedges

The Bank uses special commission rate swaps to hedge against the special commission rate risk arising from specifically identified fixed special commission rate exposures.

#### Cash flow hedges

The Bank is exposed to variability in future special commission cash flows on non-trading assets and liabilities which bear special commission rate at a variable rate. The Bank uses special commission rate swaps as cash flow hedges of these special commission rate risks.

The table below shows the positive and negative fair values of derivative financial instruments held, together with their notional amounts, analysed by the term to maturity and monthly average. The notional amounts, which provide an indication of the volumes of the transactions outstanding at the year end, do not reflect the amounts of future cash flows involved. These notional amounts, therefore, are neither indicative of the Bank's exposure to credit risk, which is generally limited to the positive fair value of the derivatives, nor market risk.

For the years ended December 31, 2015 and 2014

# **11. DERIVATIVES** (continued)

Cash flow hedges (continued)

				Notional am			
2015 SAR'000	Positive fair value	Negative fair value	Notional amount total	Within 3 months	3-12 months	1-5 years	Monthly average
Held for trading:							
Special commission rate swaps	45,071	(15,052)	5,283,833	769,473	1,289,965	3,224,395	3,232,054
Forward foreign exchange contracts	78,572	(96,544)	38,044,211	34,029,932	4,014,279		55,569,243
Currency options	73,399	(73,399)	8,483,383	3,177,030	3,976,204	1,330,149	6,209,352
Commodity options	-497	(497)	1,696	1,696	-	-	11,212
Held as fair value hedges:							
Special commission rate swaps		(1,637)	230,474	68,110	137,501	24,863	230,474
Held as cash flow hedges:							
Special commission rate swaps	-	-	-	-	-	-	_
Total	197,539	(187,129)	52,043,597	38,046,241	9,417,949	4,579,407	65,252,335

				Notional am			
2014 SAR'000	Positive fair value	Negative fair value	Notional amount total	Within 3 months	3-12 months	1-5 years	Monthly average
Held for trading:							
Special commission rate swaps	1,992	(1,996)	1,351,794	413,994	-	937,800	988,383
Forward foreign exchange contracts	401,348	(353,073)	60,955,155	39,327,529	21,439,705	187,921	65,726,344
Currency options	14,794	(14,794)	3,103,235	526,604	1,449,365	1,127,266	2,912,380
Commodity options	978	(978)	18,499	6,937	11,562	-	13,399
Held as fair value hedges:							
Special commission rate swaps	-	-	-	-	-	-	-
Held as cash flow hedges:							
Special commission rate swaps	-	-	-	-	-	-	-
Total	419,112	(370,841)	65,428,683	40,275,064	22,900,632	2,252,987	69,640,506

The table below shows a summary of hedged items, the nature of the risk being hedged, the hedging instrument and its fair value as at December 31, 2015. There were no fair value hedges as at December 31, 2014.

For the years ended December 31, 2015 and 2014

2015 SAR '000	Fair value	Hedge inception value	Risk	Hedging instrument		Negative fair value
Fixed special commission rate deposits	230,854	229,118	Fair value	Special commission rate swaps	-	(1,637)

#### 12. DUE TO BANKS AND OTHER FINANCIAL INSTITUTIONS

SAR'000	2015	2014
Current accounts	606,385	1,081,019
Money market deposits	3,889,826	2,708,777
Total	4,496,211	3,789,796

Deposits against sales of fixed rate bonds with agreement to repurchase the same at fixed future dates were nil as at December 31, 2015 and 2014.

#### **13. CUSTOMER DEPOSITS**

SAR'000	2015	2014
Demand	72,125,704	71,589,238
Saving	291,263	289,033
Time	85,505,918	82,186,503
Other	9,166,917	10,014,659
Total	167,089,802	164,079,433

Time deposits include deposits against sales of bonds of SAR 701 million (2014: SAR 660 million) with agreement to repurchase the same at fixed future dates. Other customers' deposits include SAR 2,963 million (2014: SAR 3,294 million) of margins held for irrevocable commitments.

Time deposits include non-special commission based deposits of SAR 36,412 million (2014: SAR 18,958 million).

The above include foreign currency deposits as follows:

SAR'000	2015	2014
Demand	2,525,169	3,523,832
Saving	352	538
Time	27,550,326	20,937,977
Other	301,307	694,486
Total	30,377,154	25,156,833

For the years ended December 31, 2015 and 2014

#### 14. DEBT SECURITIES IN ISSUE

During June 2015, the Bank issued SAR 4,000 million Subordinated debt (Sukuk). These are SAR denominated and have maturity date of June 24, 2025 and are callable after 5 years, subject to the terms and conditions of the agreement. The notes carry a special commission rate of SAIBOR plus 115 basis points.

During November 2013, the Bank issued SAR 4,000 million Senior debt (Sukuk). These SAR denominated sukuks carry a 3 month SAIBOR plus 68 basis points, have maturity date of November 11, 2020 and are callable after 5 years, subject to the terms and conditions of the agreement.

#### **15. OTHER LIABILITIES**

SAR'000	2015	2014
Accrued special commission payable		
- banks and other financial institutions	3,482	749
– customer deposits	196,596	228,369
- debt securities in issue	11,313	8,946
Total accrued special commission payable	211,391	238,064
Accounts payable	1,693,240	1,894,640
Negative fair value of derivatives (note 11)	187,129	370,841
Other*	5,092,990	4,679,414
Total	7,184,750	7,182,959

<sup>\*</sup>Includes items in transit which are cleared in the normal course of business

Other in 2015, includes a deposit of SAR 20 million under an initial agreement to sell a plot of land in Jeddah at an approximate value of SAR 202.5 million. The completion of this sale is contingent upon receiving the full value of the land and finalisation of ownership transfer procedures. As such the sale has not yet been recognised by the Bank.

#### **16. SHARE CAPITAL**

The authorised, issued and fully-paid share capital of the Bank consist of 3,000 million shares of SAR 10 each (2014: 3,000 million shares of SAR 10 each).

#### **17. STATUTORY RESERVE**

In accordance with Saudi Arabian Banking Control Law and the Articles of Association of the Bank, a minimum of 25% of the annual net income is required to be transferred to the statutory reserve until this reserve equals the paid up capital of the Bank. Accordingly, SAR 1,012.4 million has been transferred from 2015 net income (2014: SAR 1,088.1 million). The statutory reserve is not currently available for distribution.

For the years ended December 31, 2015 and 2014

#### **18. OTHER RESERVES**

2015 SAR'000	Available for sale investments	Total
Delegan at her feeter of the core	1 020 027	1 020 027
Balance at beginning of the year	1,038,937	1,038,937
Net change in fair value	(582,781)	(582,781)
Transfer to consolidated income statement	(158,689)	(158,689)
Net movement during the year	(741,470)	(741,470)
Balance at end of the year	297,467	297,467
2014 SAR'000	Available for sale investments	Total
Balance at beginning of the year	1,184,564	1,184,564
Net change in fair value	222,538	222,538
Transfer to consolidated income statement	(368,165)	(368,165)
Net movement during the year	(145,627)	(145,627)
Balance at end of the year	1,038,937	1,038,937

#### 19. COMMITMENTS AND CONTINGENCIES

#### a) Legal proceedings

As at December 31, 2015, there were legal proceedings of a routine nature outstanding against the Bank. No provision has been made as management and in-house legal adviser believes that it is unlikely that any significant loss will arise.

#### b) Capital commitments

As at December 31, 2015, the Bank had capital commitments of SAR 195.6 million (2014: SAR 89.0 million). This includes computer hardware, software, automation projects, construction and equipment purchases.

#### c) Credit related commitments and contingencies

The primary purpose of these instruments is to ensure that funds are available to a customer as required. Guarantee and standby letters of credit, which represent irrevocable assurances that the Bank will make payments in the event that a customer cannot meet its obligations to third parties, carry the same credit risk as loans and advances. Cash requirements under guarantees and standby letters of credit are considerably less than the amount of the commitment because the Bank does not generally expect the third party to draw funds under the agreement. Documentary letters of credit, which are written undertakings by the Bank on behalf of a customer authorizing a third party to draw drafts on the Bank up to a stipulated amount under specific terms and conditions, are generally collateralised by the underlying shipments of goods to which they relate, and therefore have significantly less risk.

For the years ended December 31, 2015 and 2014

#### 19. COMMITMENTS AND CONTINGENCIES (continued)

#### c) Credit related commitments and contingencies (continued)

Acceptances comprise undertakings by the Bank to pay bills of exchange drawn on customers. The Bank expects most acceptances to be presented before being reimbursed by the customers.

Commitments to extend credit represent the unused portion of authorizations to extend credit, principally in the form of loans and advances, guarantees and letters of credit. With respect to credit risk on commitments to extend credit, the Bank is potentially exposed to a loss in an amount equal to the total unused commitments. However, the likely amount of loss, which cannot readily be quantified, is expected to be considerably less than the total unused commitment as most commitments to extend credit are contingent upon customers maintaining specific credit standards. The total outstanding commitments to extend credit do not necessarily represent future cash requirements, as many of these commitments could expire or terminate without being funded.

#### (i) The contractual maturity structure for the Bank's commitments and contingencies are as follows:

2015 SAR'000	Within 3 months	3-12 months	1-5 years	Over 5 years	Total
Letters of credit	4,375,375	3,982,634	1,052,320	-	9,410,329
Letters of guarantee	17,141,596	33,356,350	30,424,408	638,367	81,560,721
Acceptances	2,036,455	1,579,063	18,347	157	3,634,022
Irrevocable commitments	418,818	902,870	7,321,992	2,589,406	11,233,086
to extend credit					
Total	23,972,244	39,820,917	38,817,067	3,227,930	105,838,158
2014	Within 3	3-12	1-5	Over 5	
SAR'000	months	months	years	years	Total
Letters of credit	5,942,803	5,828,839	655,161	-	12,426,803
Letters of guarantee	16,107,085	27,890,586	34,533,112	2,929,030	81,459,813
Acceptances	2,063,043	545,078	19,520	-	2,627,641
Irrevocable commitments	583,425	2,352,304	2,877,447	3,817,910	9,631,086
to extend credit					
Total	24,696,356	36,616,807	38,085,240	6,746,940	106,145,343

The outstanding unused portion of non-firm commitments as at December 31, 2015 which can be revoked unilaterally at any time by the Bank, amounts to SAR 90,881 million (2014: SAR 92,681 million).

For the years ended December 31, 2015 and 2014

## (ii) The analysis of commitments and contingencies by counterparty is as follows:

SAR'000	2015	2014
Government and quasi government	1,875,000	900,000
Corporate	77,399,983	80,090,809
Banks and other financial institutions	26,563,175	25,154,534
Total	105,838,158	106,145,343

## d) Assets pledged

Assets pledged as collateral with customers are as follows:

	20	15	20	14
SAR'000	Assets	Related liabilities	Assets	Related liabilities
Other investments held at amortised cost (note 6e and 13)	700,287	700,510	659,386	660,000

These transactions are conducted under the terms that are usual and customary to standard lending and securities borrowing and lending activities.

## e) Operating lease commitments

The future minimum lease payments under non-cancellable operating leases where the Bank is the lessee are as follows:

SAR'000	2015	2014
Less than 1 year	33,165	13,555
1 to 5 years	88,557	34,016
Over 5 years	4,623	6,110
Total	126,345	53,681

For the years ended December 31, 2015 and 2014

## **20. SPECIAL COMMISSION INCOME AND EXPENSE**

SAR'000	2015	2014
Special commission income		
Investments - Available for sale	415,423	417,823
- Other investments held at amortised cost	423,841	399,138
- Held to maturity	2,856	6,111
	842,120	823,072
Due from banks and other financial institutions	32,875	30,268
Loans and advances	5,008,040	5,091,900
Total	5,883,035	5,945,240
SAR'000	2015	2014
Special commission expense		
Due to banks and other financial institutions	18,403	54,008
Customer deposits	577,835	695,138
Debt securities in issue	103,842	65,855
Total	700,080	815,001

## 21. FEE AND COMMISSION INCOME, NET

SAR'000	2015	2014
Fee and commission income:		
- Share brokerage and fund management	341,444	416,505
- Trade finance and corporate finance and advisory	1,243,063	1,517,109
- Other banking services	697,368	577,422
Total fee and commission income	2,281,875	2,511,036
Fee and commission expense:		
- Banking cards and share brokerage	384,226	361,111
- Other banking services	111,397	129,440
Total fee and commission expense	495,623	490,551
Fee and commission income, net	1,786,252	2,020,485

## 22. OTHER OPERATING INCOME

During the second quarter of the current year, the Bank sold land with a book value of approximately SAR 80.9 million. The sold properties were initially acquired in settlement of certain loans and advances. The gain on sale of land amounting to SAR 266.6 million is included in Other operating income.

For the years ended December 31, 2015 and 2014

#### 23. SALARIES AND EMPLOYEE-RELATED EXPENSES

The following table summarises the Group's employee categories defined in accordance with SAMA's rules on compensation practices and includes the total amounts of fixed and variable compensation paid to employees during the years ended December 31, 2015 and 2014, and the forms of such payments.

Categories	Numb emplo			Fixed compensation		Variable compensation				al sation
(SAR'000)	2015	2014	2015	2014	2015	2014	2015	2014		
Senior executives requiring SAMA no objection	36	30	38,890	34,020	9,739	10,802	48,629	44,822		
Employees engaged in risk taking activities	328	343	96,474	102,388	21,711	27,714	118,185	130,102		
Employees engaged in control functions	447	427	92,489	84,590	11,749	9,387	104,238	93,977		
Outsourced employees	292	289	25,051	28,337	-	-	25,051	28,337		
Others	5,064	4,700	702,644	633,717	76,537	54,868	779,181	688,585		
Total	6,167	5,789	955,548	883,052	119,736	102,771	1,075,284	985,823		
Variable compensation accrued in 2015 (2014) and other employee related benefits*  Total salaries and employee-related expenses			657,806	588,500						
as per consolidated incom			1,613,354	1,471,552						

<sup>\*</sup>Other employee benefits include; insurance, pension, relocation expenses, recruitment expenses, training and development and other employee benefits.

Compensation policy is based on the job profile requirements, market practices, nature and level of involvement in risk taking process. It applies to the Bank's senior management and all employees and aims to link individual performance to the Bank's overall achievements and soundness. Compensation includes fixed and variable components. Salary revision, performance bonus and other performance linked incentives are decided based on the performance evaluation process outcome as well as the Bank's financial performance and strategic goals.

The Board of Directors has the responsibility to approve and oversee the Bank's compensation policy. The Nomination and Compensation Committee, made up of six non-executive Directors, is in charge of overseeing the compensation system design and effectiveness on behalf of the Board of Directors as well as preparing the Bank's compensation policy and undertaking its periodic assessment and update to ensure achievement of the system objectives and reinforce the Bank's risk management framework. Fixed compensation comprises salaries and wages and other benefits and allowances. The variable compensation includes sales incentives, product related rewards and performance related payments.

For the years ended December 31, 2015 and 2014

#### 24. EARNINGS PER SHARE

Basic and diluted earnings per share for the years ended December 31, 2015 and 2014 are calculated by dividing the net income for the year by 3,000 million shares.

#### 25. PROPOSED GROSS DIVIDENDS AND ZAKAT

The net cash dividend after deduction of zakat amounted to SAR 2,100 million (2014: SAR 2,190 million), resulting in a net dividend to the shareholders of SAR 0.70 per share (2014: SAR 0.73 per share). The gross dividends for 2015 include interim dividends of SAR 1,050 million paid for the first half of 2015 (2014: SAR 1,140 million). Final dividends, net of zakat of SAR 1,050 million have been proposed for 2015 (2014: SAR 1,050 million).

Zakat appropriation for the year amounted to approximately SAR 250 million (2014: SAR 200 million).

The Bank has filed its Zakat returns for the financial years up to and including the year 2014 with the Department of Zakat and Income Tax (the "DZIT"). The Bank has received Zakat assessments for the year(s) up to 2009 raising additional demands aggregating to SAR 896 million. The above additional exposure is mainly on account of disallowance of certain long-term investments by the DZIT. The basis for this additional aggregate Zakat liability is being contested by the Bank in conjunction with all the Banks in Saudi Arabia. The Bank has also formally contested these assessments and is awaiting a response from DZIT.

The zakat assessment for the years 2010 to 2014 have not been finalized by the DZIT and the Bank may not be able to determine reliably the impact of such assessments.

#### **26. CASH AND CASH EQUIVALENTS**

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

SAR'000	2015	2014
Cash and balances with SAMA excluding statutory deposit (note 4)  Due from banks and other financial institutions maturing within three months from the date of acquisition	11,772,351 9,269,380	17,045,983 3,726,927
Total	21,041,731	20,772,910

For the years ended December 31, 2015 and 2014

#### 27. 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 transactions between the Group's operating segments are recorded as per the Group's transfer pricing system. The Group's primary business is conducted in 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 consolidated financial statements and as a result have not been separately disclosed. There are no other material items of income or expense between the operating segments.

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

#### Retail

Deposit, 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

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

#### Treasury and investments

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

#### Other

Includes income on capital and unallocated costs pertaining to head office, finance division, human resources, technology services and other support departments and unallocated assets and liabilities.

For the years ended December 31, 2015 and 2014

# 27. OPERATING SEGMENTS (continued)

a) The Group's total assets and liabilities as at December 31, its total operating income and expense and its net income, for the years then ended by operating segments, are as follows:

2015		Investment banking and		Treasury and		
SAR'000	Retail	brokerage	Corporate	investment	Other	Total
Total assets	42,342,043	97,897	103,708,781	73,909,249	3,257,905	223,315,875
Total liabilities	57,913,288	60,270	109,210,922	16,498,322	3,087,961	186,770,763
Total operating income, net	2,663,961	363,126	3,443,375	1,129,829	388,848	7,989,139
Net special commission income	2,228,963	49,765	2,363,825	506,673	33,729	5,182,955
Fee and commission income,						
net	406,326	313,922	1,074,367	(8,363)	-	1,786,252
Total operating expenses, net	2,239,445	167,630	116,574	65,685	1,390,247	3,979,581
Depreciation of property and equipment	101,755	-	4,658	8,606	160,755	275,774
Impairment charge for credit losses, net	1,231,623		(200,888)	_	_	1,030,735
Impairment charge for investments, net				21,609		21,609
Share in earnings of associates,				21,003		21,005
net	-	-	-	-	39,919	39,919
Net income (loss)	424,516	195,496	3,326,801	1,064,144	(961,480)	4,049,477
2014		Investment		Treasury		
2014 SAR'000	Retail	banking and	Corporate	Treasury and investment	Other	Total
	Retail		Corporate	and	Other	Total
	Retail 41,995,034	banking and	Corporate 92,530,193	and	Other 3,963,078	Total 214,589,293
SAR'000		banking and brokerage	·	and investment		
SAR'000 Total assets	41,995,034	banking and brokerage 94,544	92,530,193	and investment 76,006,444	3,963,078	214,589,293
SAR'000  Total assets  Total liabilities	41,995,034 56,764,324	banking and brokerage 94,544 81,435	92,530,193 106,457,015	and investment 76,006,444 12,584,470	3,963,078 3,164,944	214,589,293 179,052,188
SAR'000  Total assets Total liabilities Total operating income, net	41,995,034 56,764,324 2,502,060	94,544 81,435 408,636	92,530,193 106,457,015 3,621,563 2,369,212	76,006,444 12,584,470 1,196,691	3,963,078 3,164,944 282,816 146,610	214,589,293 179,052,188 8,011,766 5,130,239
SAR'000  Total assets Total liabilities Total operating income, net Net special commission income Fee and commission income, net	41,995,034 56,764,324 2,502,060 2,050,334	94,544 81,435 408,636 41,538	92,530,193 106,457,015 3,621,563	76,006,444 12,584,470 1,196,691 522,545	3,963,078 3,164,944 282,816 146,610	214,589,293 179,052,188 8,011,766
SAR'000  Total assets Total liabilities Total operating income, net Net special commission income Fee and commission income,	41,995,034 56,764,324 2,502,060 2,050,334 438,477	94,544 81,435 408,636 41,538	92,530,193 106,457,015 3,621,563 2,369,212 1,221,575	76,006,444 12,584,470 1,196,691 522,545 (5,931)	3,963,078 3,164,944 282,816 146,610	214,589,293 179,052,188 8,011,766 5,130,239 2,020,485
SAR'000  Total assets Total liabilities Total operating income, net Net special commission income Fee and commission income, net Total operating expenses, net	41,995,034 56,764,324 2,502,060 2,050,334 438,477	94,544 81,435 408,636 41,538	92,530,193 106,457,015 3,621,563 2,369,212 1,221,575	76,006,444 12,584,470 1,196,691 522,545 (5,931)	3,963,078 3,164,944 282,816 146,610	214,589,293 179,052,188 8,011,766 5,130,239 2,020,485
Total assets Total liabilities Total operating income, net Net special commission income Fee and commission income, net Total operating expenses, net Depreciation of property and	41,995,034 56,764,324 2,502,060 2,050,334 438,477 1,238,578	94,544 81,435 408,636 41,538	92,530,193 106,457,015 3,621,563 2,369,212 1,221,575 825,172	76,006,444 12,584,470 1,196,691 522,545 (5,931) 57,589	3,963,078 3,164,944 282,816 146,610 - 1,430,706	214,589,293 179,052,188 8,011,766 5,130,239 2,020,485 3,706,079
Total assets Total liabilities Total operating income, net Net special commission income Fee and commission income, net Total operating expenses, net Depreciation of property and equipment Impairment charge for credit	41,995,034 56,764,324 2,502,060 2,050,334 438,477 1,238,578 88,297	94,544 81,435 408,636 41,538	92,530,193 106,457,015 3,621,563 2,369,212 1,221,575 825,172 4,072	76,006,444 12,584,470 1,196,691 522,545 (5,931) 57,589	3,963,078 3,164,944 282,816 146,610 - 1,430,706	214,589,293 179,052,188 8,011,766 5,130,239 2,020,485 3,706,079
Total assets Total liabilities Total operating income, net Net special commission income Fee and commission income, net Total operating expenses, net Depreciation of property and equipment Impairment charge for credit losses, net Impairment charge for	41,995,034 56,764,324 2,502,060 2,050,334 438,477 1,238,578 88,297	94,544 81,435 408,636 41,538	92,530,193 106,457,015 3,621,563 2,369,212 1,221,575 825,172 4,072	76,006,444 12,584,470 1,196,691 522,545 (5,931) 57,589	3,963,078 3,164,944 282,816 146,610 - 1,430,706	214,589,293 179,052,188 8,011,766 5,130,239 2,020,485 3,706,079 257,665 900,063
Total assets Total liabilities Total operating income, net Net special commission income Fee and commission income, net Total operating expenses, net Depreciation of property and equipment Impairment charge for credit losses, net Impairment charge for investments, net Share in earnings of associates,	41,995,034 56,764,324 2,502,060 2,050,334 438,477 1,238,578 88,297	94,544 81,435 408,636 41,538	92,530,193 106,457,015 3,621,563 2,369,212 1,221,575 825,172 4,072	76,006,444 12,584,470 1,196,691 522,545 (5,931) 57,589	3,963,078 3,164,944 282,816 146,610 - 1,430,706 163,056	214,589,293 179,052,188 8,011,766 5,130,239 2,020,485 3,706,079 257,665 900,063

For the years ended December 31, 2015 and 2014

b) The Group's credit exposure by operating segment is as follows:

2015 SAR'000	Retail	Corporate	Treasury and investment	Total
Consolidated statement of financial position assets  Commitments and contingencies	41,612,332	104,827,263 58,077,683	51,811,696	198,251,291 58,077,683
Derivatives	-	-	1,197,985	1,197,985
2014 SAR'000	Retail	Corporate	Treasury and investment	Total
Consolidated statement of financial position assets  Commitments and contingencies	41,536,611	93,706,329 50,658,451	48,825,182	184,068,122 50,658,451
Derivatives	-	-	1,351,074	1,351,074

Credit exposure comprises the carrying value of consolidated statement of financial position assets excluding, cash, equity investments, investment in associates, property and equipment, other real estate and other assets. The credit equivalent value of commitments, contingencies and derivatives are included in credit exposure.

#### 28. 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 Bank uses internal credit rating tools to assess credit standing of its counterparties and assigns credit ratings accordingly. Also the Bank 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 Bank 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 Bank'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 Bank 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 Bank may also close out transactions or assign them to other counterparties to mitigate credit risk.

The Bank'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 Bank assesses counterparties using the same techniques as for its lending activities.

For the years ended December 31, 2015 and 2014

#### 28. CREDIT RISK (continued)

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 Bank's performance to developments affecting any particular category of concentration.

The Bank 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 Bank 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 Bank regularly reviews its risk management policies and systems to reflect changes in markets products and emerging best practice.

The Group's due from banks and other financial institutions balance of SAR 9,269 million (2014: SAR 3,915 million - refer note 5) are held by banks and other financial institutions which have credit ratings above Investment Grade as per S&P rating equivalent. The debt securities included in the investment portfolio are mainly sovereign risk. Analysis of investments by counterparty is provided in note 6. For details of the composition of loans and advances refer to note 7. Information on credit risk relating to derivative instruments is provided in note 11 and for commitments and contingencies in note 19. The Bank's maximum credit exposure, which best represents its maximum exposure to credit risk at the end of the reporting period, without taking account of any collateral held or other credit enhancements, is not materially different than the credit exposure by business segment given in note 27. The information on maximum credit risk exposure and their relative risk weights is also provided in note 34.

For the years ended December 31, 2015 and 2014

## 29. CONCENTRATION OF RISKS OF FINANCIAL ASSETS WITH CREDIT RISK EXPOSURE **AND FINANCIAL LIABILITIES**

a) The distribution by geographical region for major categories of assets, liabilities, commitments and contingencies and credit exposure are as follows:

2015 SAR'000	Kingdom of Saudi Arabia	Other GCC and Middle East	Europe	North America	Latin America	South East Asia	Other countries	Total
Assets								
Cash and balances with SAMA	20,569,924	-	4	-	-	1	-	20,569,929
Due from banks and other financial								
institutions	1,373,699	96,277	2,940,765	4,716,915	-	138,872	2,852	9,269,380
Investments, net and investment in								
associates	29,430,850	1,136,363	3,723,162	9,261,675	7,041	703,110	815,313	45,077,514
Loans and								
advances, net	142,521,842	1,384,869	176,036	382,740	157	206,672	1,514	144,673,830
Total	193,896,315	2,617,509	6,839,967	14,361,330	7,198	1,048,655	819,679	219,590,653
Liabilities								
Due to banks and other financial								
institutions	662,669	1,782,362	657,074	277,370	_	10,619	1,106,117	4,496,211
Customer deposits	165,644,975	147,754	1,193,669	96,784	100	599	5,921	167,089,802
Debt securities in								
issue	8,000,000	-	-	-	-	-	-	8,000,000
Total	174,307,644	1,930,116	1,850,743	374,154	100	11,218	1,112,038	179,586,013
Commitments and contingencies	80,855,256	974,233	10,813,068	12,964,503	-	231,098	-	105,838,158

Maximum credit exposure (stated at credit equivalent amounts according to SAMA's prescribed methodology)

- Derivatives	588,699	324,978	266,786	12,819	-	-	4,703	1,197,985
- Commitments and								
contingencies	44,638,461	426,169	5,915,448	6,970,531	-	127,074	-	58,077,683

For the years ended December 31, 2015 and 2014

# **29. CONCENTRATION OF RISKS OF FINANCIAL ASSETS WITH CREDIT RISK EXPOSURE AND FINANCIAL LIABILITIES** (continued)

2014 SAR'000	Kingdom of Saudi Arabia	Other GCC and Middle East	Europe	North America	Latin America	South East Asia	Other countries	Total
3/11/ 000	Sadai / Ilabia	Lust	Larope	7111101100	7 tilleried	Lustrisia	countries	Total
Assets								
Cash and balances with SAMA	25,315,724	-	11	-	-	1	-	25,315,736
Due from banks and other financial								
institutions	619,085	266,366	2,489,410	402,565	-	124,728	12,350	3,914,504
Investments, net and investment in associates	29,395,657	2,335,140	4,561,495	10,574,006		214,915	350,591	47,431,804
		2,335,140	4,501,495	10,574,006	-	214,915	350,531	41,431,804
Loans and advances, net	131,530,792	1,156,052	171,781	366,345	_	264,941	363	133,490,274
Total	186,861,258	3,757,558	7,222,697	11,342,916	_	604,585	363,304	210,152,318
						,		
Liabilities								
Due to banks and other financial								
institutions	119,824	1,950,013	1,177,665	283,008	-	148,227	111,059	3,789,796
Customer deposits	162,560,408	204,890	1,209,805	98,060	-	5,108	1,162	164,079,433
Debt securities in								
issue	4,000,000	-	-	-	-	-	-	4,000,000
Total	166,680,232	2,154,903	2,387,470	381,068	-	153,335	112,221	171,869,229
Commitments and contingencies	80,406,350	1,074,059	12,161,903	11,438,889	-	93,814	970,328	106,145,343

Maximum credit exposure (stated at credit equivalent amounts according to SAMA's prescribed methodology)

- Derivatives	608,641	271,555	384,680	13,488	-	-	72,710	1,351,074
- Commitments and								
contingencies	38,310,624	253,662	5,877,830	5,719,444	-	18,763	478,128	50,658,451

For the years ended December 31, 2015 and 2014

b) The distributions by geographical concentration of non-performing loans and advances and specific allowance for credit losses, which is entirely attributable to Saudi Arabia is as follows:

		rming loans inces, net	Allowance for credit losses		
SAR'000	2015	2014	2015	2014	
Kingdom of Saudi Arabia	1,321,603	1,049,927	(826,398)	(914,245)	
Total	1,321,603	1,049,927	(826,398)	(914,245)	

#### **30. MARKET RISK**

Market Risk is the risk that the fair value or future cash flows of the financial instruments will fluctuate due to changes in market variables such as special commission rates, foreign exchange rates, commodity and equity prices. The Bank classifies exposures to market risk into either trading or non-trading/ banking-book. The market risk for the trading book is managed and monitored using a VaR methodology. Market risk for the non-trading book is managed and monitored using a combination of VaR, stress testing and sensitivity analysis.

#### a) Market Risk - Trading Book

The Bank has set limits (both VaR and exposure based limits) for the acceptable level of risks in managing the trading book. In order to manage the market risk in trading book, the Bank applies a VaR methodology to assess the market risk positions held and also to estimate the potential economic loss based on a set of assumptions and changes in market conditions.

A VaR methodology estimates the potential negative change in market value of a portfolio at a given confidence level and over a specified time horizon. The Bank uses variance-covariance approach for calculating VaR for trading book based on historical data (of 1 year). VaR models are usually designed to measure the market risk in a normal market environment and therefore the use of VaR has limitations because it is based on historical correlations and volatilities in market prices and assumes that the future movements will follow a statistical distribution.

The Bank calculates VaR on the basis of the following:

- 1. 10 days holding period at 99% confidence interval for regulatory capital computation (under IMA approach of Basel II Accord that the Bank plans to adopt in the future)
- 2. 1 day holding period at 99% confidence interval for internal reporting and for disclosure purposes.

This means that the VaR that the Bank measures is an estimate (using a confidence level of 99% of the potential loss) that is not expected to be exceeded if the current market positions were to be held unchanged for 1 or 10 days. The use of 99% confidence level depicts that within a 1-day horizon, losses exceeding VaR figure should occur, on average, not more than once every hundred days.

The VaR represents the risk of portfolios at the close of a business day, and it does not account for any losses that may occur beyond the defined confidence interval. The actual trading results however, may differ from the VaR calculations and, in particular, the calculation does not provide a meaningful indication of profits and losses in stressed market conditions.

For the years ended December 31, 2015 and 2014

#### **30. MARKET RISK** (continued)

#### a) Market Risk - Trading Book (continued)

To overcome the VaR limitations mentioned above, the Bank also carries out stress tests of both non-trading and trading portfolios to simulate conditions outside normal confidence intervals using six stress scenarios for the entire Bank. The potential losses occurring under stress test conditions are reported regularly to the Bank's Asset Liability Committee (ALCO) for their review.

The Bank's VaR related information for the year ended December 31, 2015 and 2014 using a 1 day holding period at 99% confidence interval is as under. All the figures are in million SAR:

2015 SAR'000	Foreign exchange rate risk	Special commission rate risk	Equity price risk	Overall risk
VaR as at December 31, 2015	33.19	4.00	-	33.58
Average VaR for 2015	5.72	3.12	-	6.66
Maximum VaR for 2015	42.30	4.48	-	41.38
Minimum VaR for 2015	0.66	1.50	-	2.12

2014 SAR'000	Foreign exchange rate risk	Special commission rate risk	Equity price risk	Overall risk
VaR as at December 31, 2014	2.91	2.36	-	2.98
Average VaR for 2014	7.57	1.60	-	8.04
Maximum VaR for 2014	32.71	2.86	-	31.79
Minimum VaR for 2014	1.45	0.28	-	2.32

## b) Market Risk - Non-trading or Banking Book

#### i) Special commission rate risk

Special commission rate risk arises from the possibility that the changes in special commission rates will affect either the fair values or the future cash flows of the financial instruments. The Bank has established Net special commission Income at Risk and Market Value at Risk (MVaR) limits that are monitored by ALCO. There are gap limits to accommodate Forward FX and Money Market for all currencies. The Bank monitors positions daily and uses hedging strategies to ensure maintenance of positions within the established gap limits.

The following table depicts the sensitivity to a reasonable possible change in special commission rates, with other variables held constant, on the Bank's consolidated income statement or equity.

For the years ended December 31, 2015 and 2014

The sensitivity of the income is the effect of the assumed changes in special commission rates on the net special commission income for one year, on the non-trading financial assets and financial liabilities held as at December 31, 2015 and 2014, including the effect of hedging instruments.

The sensitivity of equity is calculated by revaluing the fixed rate Available for sale financial assets, including the effect of any associated hedges as at December 31, 2015 and 2014 for the effect of assumed changes in special commission rates. The sensitivity of equity is analysed by maturity of the asset or swap. All the banking book exposures are monitored and analysed in currency concentrations and relevant sensitivities are disclosed in SAR million.

2015 Currency	Increase in basis	Sensitivity of special commission income	6 months or less	1 year or less	1-5 years	Over 5 years	Total
SAR	+100	58.4					
USD	+100	(94.1)	(1.37)	(1.21)	(50.60)	(294.58)	(347.76)
EUR	+100	(3.2)	(0.67)	(0.80)	(10.02)	(7.87)	(19.35)
GBP	+100	(9.4)	(0.09)	(0.07)	(3.66)	(0.45)	(4.27)
JPY	+100	3.1	-	(0.15)	(0.42)	(0.01)	(0.59)
Others	+100	(0.6)	-	(0.02)	(0.53)	(0.02)	(0.57)

Currency	Decrease in basis	Sensitivity of special commission income	6 months or less	1 year or less		Over 5 years	Total
SAR	- 100	(59.6)					
USD	- 100	85.5	1.37	1.21	50.60	294.58	347.76
EUR	- 100	0.1	0.67	0.80	10.02	7.87	19.35
GBP	- 100	8.9	0.09	0.07	3.66	0.45	4.27
JPY	- 100	(3.1)	-	0.15	0.42	0.01	0.59
Others	- 100	0.5	-	0.02	0.53	0.02	0.57

For the years ended December 31, 2015 and 2014

#### **30. MARKET RISK** (continued)

## b) Market Risk - Non-trading or Banking Book (continued)

i) Special commission rate risk (continued)

				Sensitivity of equity							
2014 Currency	Increase in basis	Sensitivity of special commission income	6 months or less	/		Over 5 years	Total				
					752.5	,					
SAR	+100	127.9	-	-	-	-	-				
USD	+100	(30.2)	(1.85)	(2.12)	(44.24)	(279.92)	(328.14)				
EUR	+100	0.5	(0.79)	(0.57)	(18.59)	(14.14)	(34.09)				
GBP	+100	(6.1)	(0.03)	(0.09)	(3.07)	(0.78)	(3.97)				
JPY	+100	4.2	(0.02)	-	(0.41)	(0.50)	(0.93)				
Others	+100	(1.6)	(0.01)	(0.06)	(0.25)	(0.24)	(0.56)				

		Sensitivity of special					
	Decrease	commission	6 months	/		Over 5	
Currency	in basis	income	or less	or less	years	years	Total
SAR	- 100	(128.6)	-	-	-	-	-
USD	- 100	(4.5)	1.85	2.12	44.24	279.92	328.14
EUR	- 100	1.6	0.79	0.57	18.59	14.14	34.09
GBP	- 100	5.8	0.03	0.09	3.07	0.78	3.97
JPY	- 100	(1.4)	0.02	-	0.41	0.50	0.93
Others	- 100	0.6	0.01	0.06	0.25	0.24	0.56

Special commission sensitivity of assets, liabilities and off statement of financial position items

The Bank manages exposure to the effects of various risks associated with fluctuations in the prevailing levels of market special commission rates on its financial position and cash flows. The Bank is exposed to special commission rate risk as a result of mismatches or gaps in the amounts of assets and liabilities and off statement of financial position instruments that mature or re-price in a given period. The Bank manages this risk by matching the re-pricing of assets and liabilities through risk management strategies.

For the years ended December 31, 2015 and 2014

The table below summarises the Group's exposure to special commission rate risks. Included in the table are the Group's assets and liabilities at carrying amounts, categorised by the earlier of contractual re-pricing or the maturity dates.

2015	World a	2 42	1.5	0 5	Non special	
2015 SAR'000	Within 3 months	3-12 months	1-5 years	Over 5 years	commission bearing	Total
JAK 000	IIIOIICIIS	months	years	years	bearing	Total
Assets						
Cash and balances with SAMA	7,654,784	-	-	-	12,915,145	20,569,929
Due from banks and other financial						
institutions	8,551,128	-	-	-	718,252	9,269,380
Investments, net and investment						
in associates	14,511,376	8,424,610	9,523,477	9,340,045	3,278,006	45,077,514
Loans and advances, net	53,800,954	42,414,262	32,014,251	16,444,363	-	144,673,830
Other real estate	-	-	-	-	258,411	258,411
Property and equipment, net	-	-	-	-	1,894,701	1,894,701
Other assets	-	-	-	-	1,572,110	1,572,110
Total assets	84,518,242	50,838,872	41,537,728	25,784,408	20,636,625	223,315,875
Liabilities and shareholders' equity						
Due to banks and other financial						
institutions	3,889,826	-	-	-	606,385	4,496,211
Customer deposits	71,131,575	13,160,599	150,335	-	82,647,293	167,089,802
Debt securities in issue	4,000,000	4,000,000	-	-	-	8,000,000
Other liabilities	-	-	-	-	7,184,750	7,184,750
Shareholders' equity	-	-	-	-	36,545,112	36,545,112
Total liabilities and shareholders'						
equity	79,021,401	17,160,599	150,335	-	126,983,540	223,315,875
Special commission rate sensitivity						
-On statement of financial position gap	5,496,841	33,678,273	41,387,393	25,784,408	(106,346,915)	
	3,430,641	33,016,213	41,361,333	23,764,406	(100,540,913)	
Special commission rate sensitivity -Off statement of financial						
position gap	_	_	_	_	_	
Total special commission rate						
sensitivity gap	5,496,841	33,678,273	41,387,393	25,784,408	(106,346,915)	
Cumulative special commission						
rate sensitivity gap	5,496,841	39,175,114	80,562,507	106,346,915	-	

For the years ended December 31, 2015 and 2014

## **30. MARKET RISK** (continued)

## b) Market Risk - Non-trading or Banking Book (continued)

i) Special commission rate risk (continued)

2014 SAR'000	Within 3 months	3-12 months	1-5 years	Over 5 years	Non special commission bearing	Total
Assets						
Cash and balances with SAMA	13,495,000	-	-	-	11,820,736	25,315,736
Due from banks and other financial institutions	3,409,516	112,576	-	-	392,412	3,914,504
Investments, net and investment						
in associates		15,987,510	7,768,532	7,741,261	3,615,901	47,431,804
Loans and advances, net	54,264,851	29,586,022	34,487,935	15,151,466	-	133,490,274
Other real estate	-	-	-	-	390,802	390,802
Property and equipment, net	-	-	-	-	1,706,731	1,706,731
Other assets	-	-	-	-	2,339,442	2,339,442
Total assets	83,487,967	45,686,108	42,256,467	22,892,727	20,266,024	214,589,293
Liabilities and shareholders' equity						
Due to banks and other financial						
institutions	2,477,209	231,568	-	-	1,081,019	3,789,796
Customer deposits	48,018,396	35,516,381	-	-	80,544,656	164,079,433
Debt securities in issue	4,000,000	-	-	-	-	4,000,000
Other liabilities	-	-	-	-	7,182,959	7,182,959
Shareholders' equity	-	-	-	-	35,537,105	35,537,105
Total liabilities and shareholders' equity	54,495,605	35,747,949	-	-	124,345,739	214,589,293
Special commission rate sensitivity -On statement of financial position gap	28,992,362	9,938,159	42,256,467	22,892,727	(104,079,715)	
Special commission rate sensitivity -Off statement of financial position gap	-	-	-	-	-	
Total special commission rate sensitivity gap	28,992,362	9,938,159	42,256,467	22,892,727	(104,079,715)	_
Cumulative special commission rate sensitivity gap	28,992,362	38,930,521	81,186,988	104,079,715	-	_

The off statement of financial position gap represents the net notional amounts of derivative financial instruments, which are used to manage the commission rate risk.

For the years ended December 31, 2015 and 2014

#### ii) Currency risk

Currency risk represents the risk of change in the value of financial instruments due to changes in foreign exchange rates. The Board has set limits on positions by currencies, which are monitored daily, and hedging strategies are also used to ensure that positions are maintained within the limits.

The table below shows the currencies to which the Bank has a significant exposure as at December 31, 2015 and 2014 on its non-trading monetary assets and liabilities and forecasted cash flows. The analysis calculates the effect of reasonable possible movement of the currency rate against SAR, with all other variables held constant, on the consolidated income statement (due to the fair value of the currency sensitive non-trading monetary assets and liabilities) and equity (due to change in fair value of currency swaps and forward foreign exchange contracts used as cash flow hedges). A positive effect shows a potential increase in consolidated income statement or equity; whereas a negative effect shows a potential net reduction in consolidated income statement or equity.

#### **Currency Exposures**

As at December 31, 2015 (SAR million)	Change in currency rate in %	Effect on net income
USD	± 1	± 5.40
EUR	± 1	± 0.46
GBP	± 1	± 0.1
JPY	± 1	± 0.17
Others	± 1	± 0.007
	Change in	Effect
Currency Exposures	currency rate	on net
As at December 31, 2014	in %	income
USD	± 1	± 6.68
EUR	± 1	± 0.62
GBP	± 1	± (0.05)
JPY	± 1	± 0.07
Others	± 1	± 0.00

For the years ended December 31, 2015 and 2014

#### **30. MARKET RISK** (continued)

#### b) Market Risk - Non-trading or Banking Book (continued)

#### iii) Foreign currency risk

The Bank manages exposure to effects of fluctuations in prevailing foreign currency exchange rates on its financial position and cash flows. The Board of Directors sets limits on the level of exposure by currency and in total for overnight positions, which are monitored daily. At the end of the year, the Bank had the following significant net exposures denominated in foreign currencies:

SAR'000	2015 Long (short)	2014 Long (short)
USD	970,636	(487,928)
JPY	329	(786)
EUR	(68)	3,413
GBP	3,872	(313)
Others	18,833	24,541

Long position indicates that assets in a foreign currency are higher than the liabilities in the same currency; the opposite applies to short position.

## iv) Banking Book - Equity Price risk

Equity risk refers to the risk of decrease in fair values of equities in the Bank's non-trading investment portfolio as a result of reasonable possible changes in levels of equity indices and the value of individual stocks.

The effect on the Bank's equity investments held as available for sale due to reasonable possible change in equity indices, with all other variables held constant, is as follows:

	December	31, 2015	December 31, 2014		
Market Index	Change in Effect in equity index % SAR millions		Change in equity index %	Effect in SAR millions	
	+5	49.35	+5	48.59	
Tadawul	+10	98.69	+10	97.18	
rauawur	-5	(49.35)	-5	(48.59)	
	-10	(98.69)	-10	(97.18)	

For the years ended December 31, 2015 and 2014

#### **31. LIQUIDITY RISK**

Liquidity risk is the risk that the Bank will be unable to meet its net funding requirements. Liquidity risk can be caused by market disruptions or credit downgrades, which may cause certain sources of funding to dry up immediately. To mitigate this risk, management has diversified funding sources and assets are managed with liquidity in mind, maintaining an appropriate balance of cash, cash equivalents and readily marketable securities.

Management monitors the maturity profile to ensure that adequate liquidity is maintained. The daily liquidity position is monitored and regular liquidity stress testing is conducted under a variety of scenarios covering both normal and more severe market conditions.

All liquidity policies and procedures are subject to review and approval by ALCO. Daily reports cover the liquidity position of the Group. A summary report, including any exceptions and remedial action taken, is submitted regularly to ALCO.

In accordance with Banking Control Law and the regulations issued by SAMA, the Bank maintains a statutory deposit with SAMA equal to 7% (2014: 7%) of total demand deposits and 4% (2014: 4%) of saving and time deposits. In addition to the statutory deposit, the Bank also maintains liquid reserves of not less than 20% of its deposit liabilities, in the form of cash, gold, Saudi Government Development Bonds or assets which can be converted into cash within a period not exceeding 30 days. The Bank has the ability to raise additional funds through repo facilities with SAMA up to 75 % of the nominal value of bonds held by the Bank.

The table below summarises the maturity profile of the Group's financial liabilities at December 31, 2015 and 2014 based on contractual undiscounted repayment obligations. As special commission payments up to contractual maturity are included in the table, totals do not match with the statement of financial position. The contractual maturities of liabilities have been determined based on the remaining period at the reporting date to the contractual maturity date and do not take into account the effective expected maturities. The Group expects that many customers will not request repayment on the earliest date the Group could be required to pay and the table does not affect the expected cash flows indicated by the Bank's deposit retention history. The undiscounted maturity profile of the financial liabilities is as follows:

For the years ended December 31, 2015 and 2014

## **31. LIQUIDITY RISK** (continued)

2015 SAR'000	Within 3 months	3-12 months	1-5 years	Over 5 years	Total
Financial liabilities					
Due to banks and other financial institutions	4,501,213	-	-	-	4,501,213
Customer deposits	154,122,683	13,206,444	153,380	-	167,482,507
Debt securities in issue	36,775	110,325	4,619,335	4,344,476	9,110,911
Derivative financial instruments (gross contractual amounts payable)	23,863	72,315	237,757	-	333,935
Total undiscounted financial liabilities	158,684,534	13,389,084	5,010,472	4,344,476	181,428,566
2014	Within3	3-12	1-5	Over5	
SAR'000	months	months	years	years	Total
Financial liabilities					
Due to banks and other financial institutions	3,559,900	232,446	-	-	3,792,346
Customer deposits	128,903,007	34,548,016	1,025,748	27,198	164,503,969
Debt securities in issue	26,372	52,279	278,819	4,066,219	4,423,689
Derivative financial instruments (gross contractual amounts payable)	3,438	10,505	40,260	-	54,202
Total undiscounted financial liabilities	132,492,717	34,843,246	1,344,827	4,093,417	172,774,206

The table below summarises the maturity profile of the Group's assets and liabilities. The contractual maturities of assets and liabilities have been determined on the basis of the remaining period at the reporting date to the contractual maturity date and do not take account of the effective maturities as indicated by the Bank's deposit retention history. The amounts disclosed in the table are the contractual undiscounted cash flows, whereas the Bank manages the inherent liquidity risk based on expected undiscounted cash inflows.

For the years ended December 31, 2015 and 2014

2015	Within 3	3-12	1-5	Over 5	No fixed	
SAR'000	months	months	years	years	maturity	Total
Assets						
Cash and balances with SAMA	11,772,351	-	-	-	8,797,578	20,569,929
Due from banks and other financial institutions	9,269,380	_	_	_	_	9,269,380
Investments, net and	0,200,000					5,255,255
investment in associates	8,339,506	8,929,525	11,921,131	12,609,346	3,278,006	45,077,514
Loans and advances, net	39,206,416	25,760,728	44,557,059	35,149,627	-	144,673,830
Other real estate	-	-	-	-	258,411	258,411
Property and equipment, net	-	-	-	-	1,894,701	1,894,701
Other assets	1,099,606	-	-	-	472,504	1,572,110
Total assets	69,687,259	34,690,253	56,478,190	47,758,973	14,701,200	223,315,875
Liabilities and shareholders' equity						
Due to banks and other						
financial institutions	4,496,211	-	-	-	-	4,496,211
Customer deposits	153,778,868	13,160,599	150,335	-	-	167,089,802
Debt securities in issue	-	-	4,000,000	4,000,000	-	8,000,000
Other liabilities	398,525	-	-	-	6,786,225	7,184,750
Shareholders' equity	-	-	-	-	36,545,112	36,545,112
Total liabilities and						
shareholders' equity	158,673,604	13,160,599	4,150,335	4,000,000	43,331,337	223,315,875

For the years ended December 31, 2015 and 2014

# **31. LIQUIDITY RISK** (continued)

2014	Within 3	3-12	1-5	Over 5	No fixed	
SAR'000	months	months	years	years	maturity	Total
Assets						
Cash and balances with SAMA	17,045,983	-	-	-	8,269,753	25,315,736
Due from banks and other financial institutions	3,801,928	112,576	-	-	-	3,914,504
Investments, net and investment in associates	6,694,727	16,556,531	10,169,503	10,395,142	3,615,901	47,431,804
Loans and advances, net	36,811,704	20,720,474	45,001,283	30,956,813	-	133,490,274
Other real estate	-	-	-	-	390,802	390,802
Property and equipment, net	-	-	-	-	1,706,731	1,706,731
Other assets	1,163,259	-	-	-	1,176,183	2,339,442
Total assets	65,517,601	37,389,581	55,170,786	41,351,955	15,159,370	214,589,293
Liabilities and shareholders' equity						
Due to banks and other financial						
institutions	3,558,228	231,568	-	-	-	3,789,796
Customer deposits	128,563,052	34,468,297	1,020,886	27,198	-	164,079,433
Debt securities in issue	-	-	-	4,000,000	-	4,000,000
Other liabilities	608,907	-	-	-	6,574,052	7,182,959
Shareholders' equity	-	-	-	-	35,537,105	35,537,105
Total liabilities and shareholders' equity	132,730,187	34,699,865	1,020,886	4,027,198	42,111,157	214,589,293

Assets available to meet all of the liabilities and to cover outstanding loan commitments include cash, balances with SAMA, items in the course of collection; loans and advances to banks; and loans and advances to customers. The cumulative maturities of commitments and contingencies is given in note  $19 \, c$ ) (i).

For the years ended December 31, 2015 and 2014

#### 32. FAIR VALUE 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.

#### Fair value and fair value hierarchy

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SAR' 000	Level 1	Level 2	Level 3	Total
Financial assets				
Derivative financial instruments	-	197,539	-	197,539
- Commission rate swaps	-	45,071	-	45,071
- Forward foreign exchange contracts	-	78,572	-	78,572
- Currency and Commodity options	-	73,896	-	73,896
Financial investments available for sale	14,589,396	880,062	253,006	15,722,464
- Fixed rate securities	11,247,256	-	-	11,247,256
- Floating rate securities	1,722,333	-	-	1,722,333
- Mutual funds	556,163	880,062	-	1,436,225
- Equities	1,063,644	-	253,006	1,316,650
Financial liabilities				
Derivative financial instruments	-	187,129	-	187,129
- Commission rate swaps	-	16,689	-	16,689
- Forward foreign exchange contracts	-	96,544	-	96,544
- Currency and Commodity options	-	73,896	-	73,896

For the years ended December 31, 2015 and 2014

#### 32. FAIR VALUE OF FINANCIAL ASSETS AND LIABILITIES (continued)

2014				
SAR' 000	Level 1	Level 2	Level 3	Total
Financial assets				
Derivative financial instruments	-	419,112	-	419,112
- Commission rate swaps	-	1,992	-	1,992
- Forward foreign exchange contracts	-	401,348	-	401,348
- Currency and Commodity options	-	15,772	-	15,772
Financial investments available for sale	15,558,937	1,343,429	147,714	17,050,080
Fixed rate securities	11,931,122	85,026	-	12,016,148
Floating rate securities	1,886,566	-	-	1,886,566
Mutual funds	514,468	1,258,403	2,221	1,775,092
Equities	1,226,781	-	145,493	1,372,274
Financial liabilities				
Derivative financial instruments	-	370,841	-	370,841
- Commission rate swaps	-	1,996	-	1,996
- Forward foreign exchange contracts	-	353,073	-	353,073
- Currency and Commodity options	-	15,772	-	15,772

There were no transfers between the fair value hierarchy levels.

Although the Bank believes that its estimates of fair value of Level 3 securities are appropriate, the use of different methodologies or assumptions could lead to different measurements of fair value. Level 3 consists of local and international unquoted equity securities. Bank uses net assets valuation method based on most recent available audited financial statements to fair value these investments. Other methodology that could be used to value the securities is discounted cash flow model based on expected dividend yield for which no data is available. Therefore potential impact of using reasonably possible alternative assumptions for the valuation techniques is not quantified.

#### Reconciliation of movement in Level 3

SAR'000	2015	2014
Opening balance Total gains or losses	147,714	142,931
- recognised in consolidated income statement	(1,955)	(2,940)
- recognised in other comprehensive income	6,881	8,627
Redemptions	(934)	(904)
Purchases	101,300	-
Closing balance	253,006	147,714

For the years ended December 31, 2015 and 2014

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The fair value measurement is based on the presumption that the transaction to sell the asset or transfer the liability takes place either:

- a) In the principal market for the asset or liability, or
- b) In the absence of a principal market, in the most advantageous accessible market for the asset or liability.

The fair values of on-statement of financial position financial instruments, except for other investments held at amortised costs and held-to-maturity investments which are carried at amortised cost, are not significantly different from the carrying values included in the financial statements. The fair values of, special commission bearing customers' deposits, debt securities in issue, due from and due to banks which are carried at amortised cost, are not significantly different from the carrying values included in the 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. The management uses discounted cash flow method using the current yield curve to arrive at the fair value of loans and advances and such fair value is higher than the carrying value included in the financial statements.

The estimated fair values of held-to-maturity investments and other 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 (respectively). The fair values of these investments are disclosed in note 6.

#### 33. RELATED PARTY TRANSACTIONS

In the ordinary course of its activities, the Bank transacts business with related parties. Related party transactions are governed by the limits set by the Banking Control Law and regulations issued by SAMA. The balances at December 31 resulting from such transactions are as follows:

#### a) Directors, key management personnel, other major shareholders' and their affiliates:

SAR'000	2015	2014
Loans and advances	4,476,342	3,564,951
Customer deposits	51,299,804	47,468,205
Derivatives asset (at fair value)	1,876	736
Commitments and contingencies (irrevocable)	2,458,247	3,890,775
Executive end of service	47,447	44,863

Key management personnel are those persons, including a non-executive director, having authority and responsibility for planning, directing and controlling the activities of the Bank, directly or indirectly.

Other major shareholders represent shareholdings of 5% or more of the Bank's issued share capital.

For the years ended December 31, 2015 and 2014

#### **33. RELATED PARTY TRANSACTIONS** (continued)

#### b) Bank's mutual funds:

SAR'000	2015	2014
Customer deposits	169,864	585,721

Income and expenses pertaining to transactions with related parties included in these consolidated financial statements are as follows:

SAR'000	2015	2014
Special commission income	91,302	138,743
Special commission expense	323,886	315,199
Fees from banking services, net	156,580	162,264
Directors and committees remuneration and expenses	4,705	4,740
Executive remuneration and bonus	38,871	33,146
Executive end of service	2,584	12,470
Other expenses	15,112	9,978

#### **34. 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 Group's business plans along with economic conditions which directly and indirectly affects business environment.

SAMA requires holding the minimum level of the regulatory capital of and maintaining a ratio of total regulatory capital to the risk-weighted asset (RWA) at or above the agreed minimum of 8%. SAMA issued the framework and guidance regarding implementation of the capital reforms under Basel III - which was effective from January 1, 2013. Accordingly, the Group's consolidated Risk Weighted Assets (RWA), total capital and related ratios on a consolidated group basis, calculated under the Basel III framework, are as follows:

For the years ended December 31, 2015 and 2014

	2015 Capital SAR'000	I	Ratio %		20: Capi SAR'00	tal	Ratio %
Top consolidated level							
Tier 1 capital	36,545,112	1	6.2%		35,537,10	05	16.8%
Tier 2 capital	5,072,349				1,072,3	49	
Total regulatory capital (Tier 1 + Tier 2)	41,617,461	1	8.4%		36,609,4	54	17.3%
SAR'000				2	015		2014
Risk weighted assets							
Credit risk weighted assets			211,	,467,	649		197,422,773
Operational risk weighted assets			13,	,509,	713		12,816,125
Market risk weighted assets			1,	,034,	413		977,788
Total Pillar 1 Risk Weighted Assets			226,	,011,	775		211,216,686

# **35. STAFF INVESTMENT SAVINGS PLANS**

The Group operates a Staff Savings Investment Plan. Under the terms of the Staff Savings Investment Plan, participating employees of the Bank make monthly contributions by way of a deduction from their salary subject to a maximum of 15% of their basic salaries. The Bank also contributes on a monthly basis a predetermined percentage (subject to a maximum of 6%) of the basic salary of an employee based on the varying service periods. The proceeds are invested in the Bank's existing range of mutual funds for the benefit of the employees.

The cost of the above plan is charged to the consolidated income statement over the term of the plan.

#### **36. INVESTMENT MANAGEMENT SERVICES**

The Group offers investment management services to its customers, which include management of certain investment funds with assets totaling SAR 26.1 billion (2014: SAR 29.2 billion).

The Group's assets under management include non-special commission based funds amounting to SAR 6.8 billion (2014: SAR 7.7 billion).

For the years ended December 31, 2015 and 2014

#### **37. ISSUED IFRS BUT NOT YET EFFECTIVE**

Following is a brief overview on the new IFRS and amendments to IFRS effective for annual periods beginning on or after January 1, 2016, and the Bank is currently assessing their impact.

#### IFRS and Description

#### Effective date

#### IFRS 9 - Financial instruments:

January 1, 2018

In July 2014, the IASB issued the final version of IFRS 9 Financial Instruments which reflects all phases of the financial instruments project and replaces IAS 39 Financial Instruments: Recognition and Measurement and all previous versions of IFRS 9. The standard introduces new requirements for classification and measurement, impairment, and hedge accounting.

#### IFRS 15 - Revenue from contracts with customers:

January 1, 2017

Issued in May 2014, establishes a new five-step model that will apply to revenue earned from a contract with a customer, regardless of the type of revenue or industry. The principles in IFRS 15 provide a more structured approach to measuring and recognising revenue. This new revenue standard, is applicable to all entities and will supersede the current revenue recognition requirements under IFRS.

#### IFRS 14 - Regulatory Deferral Accounts:

January 1, 2016

The aim of this interim Standard is to enhance the comparability of financial reporting by entities that are engaged in rate-regulated activities. Many countries have industry sectors that are subject to rate regulation, whereby governments regulate the supply and pricing of particular types of activity by private entities. This can include utilities such as gas, electricity and water. Rate regulation can have a significant impact on the timing and amount of an entity's revenue.

#### Amendments of IFRS 11 - Accounting for acquisitions of interests in joint operations:

January 1, 2016

The amendments to IFRS 11 require that a joint operator accounting for the acquisition of an interest in a joint operation, in which the activity of the joint operation constitutes a business, must apply the relevant principles for business combinations accounting in IFRS 3 and other standards. The amendment also clarifies that a previously held interest in a joint operation is not re-measured on the acquisition of an additional interest in the same joint operation while joint control is retained.

# $Amendments \ to \ IAS\ 16\ and\ IAS\ 38\ -\ Clarification\ of\ acceptable\ methods\ of\ depreciation\ and\ amortization:$

lanuary 1, 2016

The amendments clarify the principle in IAS 16 and IAS 38 that revenue reflects a pattern of economic benefits that are generated from operating a business (of which the asset is part) rather than the economic benefits that are consumed through use of the asset. As a result, a revenue-based method cannot be used to depreciate property, plant and equipment and may only be used in very limited circumstances to amortise intangible assets.

For the years ended December 31, 2015 and 2014

#### IFRS and Description Effective date

#### Amendments to IAS 27 - Equity Method in Separate Financial Statements:

January 1, 2016

The objective of this narrow-scope project is to restore the option to use the equity method of accounting in separate financial statements.

# Amendments to IFRS 10 and IAS 28 - Sale or Contribution of Assets between an Investor and its Associate or Joint Venture:

January 1, 2016

The amendments address the conflict between IFRS 10 and IAS 28 in dealing with the loss of control of a subsidiary that is sold or contributed to an associate or joint venture. The amendments clarify that the gain or loss resulting from the sale or contribution of assets that constitute a business, as defined in IFRS 3 Business Combinations, between an investor and its associate or joint venture, is recognised in full. Any gain or loss resulting from the sale or contribution of assets that do not constitute a business, however, is recognised only to the extent of unrelated investors' interests in the associate or joint venture.

#### Amendments to IFRSs:

January 1, 2016

Annual improvements to IFRSs 2012- 2014 cycle.

#### Amendments to IFRS 10, IFRS 12 and IAS 28 - Investment Entities:

January 1, 2016

Applying the Consolidation Exception: The amendments to IFRS 10 clarify that the exemption (in IFRS 10.4) from presenting consolidated financial statements applies to a parent entity that is a subsidiary of an investment entity, when the investment entity measures all of its subsidiaries at fair value.

#### Amendments to IAS 1 - Disclosure Initiative:

January 1, 2016

The amendments to IAS 1 Presentation of Financial Statements clarify, rather than significantly change, existing IAS 1 requirements. These amendments are intended to assist entities in applying judgement when meeting the presentation and disclosure requirements in IFRS, and do not affect recognition and measurement.

#### **38. COMPARATIVE FIGURES**

Certain prior year figures have been reclassified to conform to current year presentation.

#### 39. BOARD OF DIRECTORS' APPROVAL

These consolidated financial statements were approved by the Board of Directors on 22 Rabi II 1437H (corresponding to February 1, 2016).

#### **40. BASEL III PILLAR 3 DISCLOSURES**

Under Basel III Pillar 3, certain quantitative and qualitative disclosures (including capital structure related) are required, and these disclosures will be made available on the Bank's website www.riyadbank.com and the annual report, respectively, as required by the SAMA. Such disclosures are not subject to review or audit by the external auditors.





#### Introduction

The Bank's risk and capital disclosures are consistent with the requirements of the Saudi Arabian Monetary Agency (SAMA) and the Basel III Accord capital adequacy requirements, commonly referred to as Pillar 3 Disclosure requirements. The reported disclosures details are available on the Riyad Bank's website at www.riyadbank.com.

Riyad Bank principally deals with all banking and investment businesses, whether for its own account or on behalf of third parties in Saudi Arabia and abroad. It offers an integrated range of banking and commercial services for companies and individuals, as well as financing for commercial and large industrial activities, infrastructure projects, all through its network of branches within the Kingdom as well as through overseas office operating in London Branch (UK), Houston Agency (USA)and a representative office in Singapore

#### **Scope of Application**

The consolidated financial statements comprises of the financial statements of Riyad Bank and its wholly owned subsidiaries; Riyad Capital which is involved in the management of the Bank's investment services and asset management activities related to dealing, managing, arranging, advising and custody of securities controlled by the Capital Market Authority (CMA), Ithraa Al-Riyadh Real Estate Company, This subsidiary is responsible for providing services of keeping and managing the asset title deeds that are transferred to the Bank or to third parties as collaterals as well as buying and selling real estate in pursuit of the financing purposes for which it was

established. Riyad Company for Insurance Agency, act as an agency for selling insurance products managed and owned by AlAlamiya Cooperative Insurance Company (collectively called "the Group").

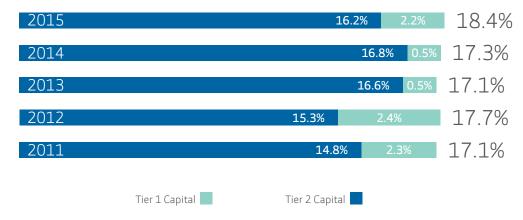
#### **Capital Adequacy and Structure:**

These disclosures are reported in accordance with the requirements of Standardized Approach for risk assessment. Note that the other investments, which have not met the requirements of the deduction of capital, are risk-weighted as 250%.

Riyad Bank provides Saudi Arabian Monetary Agency (SAMA) with quarterly capital adequacy reports, semiannual stress testing report for all kinds of risks and all activities practiced by the Bank under different circumstances, where these reports contain and provide details on the current position of the capital adequacy of the Bank and its subsidiaries, along with the annual performance plan for the future to assess Internal Capital Adequacy Assessment Process (ICAAP). The Bank provides sufficient capital (as represented by the total equity) to face significant risks, such as credit risk, market risk and operational risk, in accordance with the first Pillar of Basel III. The Bank also provides additional capital to meet the other risks that are classified under the second Pillar of Basel III including settlement risk, information technology and strategic risks.

Under the Supervisory Review Process (SRP), the Bank's minimum capital position is the total of Pillar I and Pillar II capital requirements plus any additional capital requirements as determined by the regulator.





For the purposes of the presentation, the tier 1 and tier 2 and total Capital related ratios after 2012 are calculated using the framework and methodologies defined under Basel III requirements. The comparative ratios for 2012 and earlier years are calculated under Basel II and have not been restated.

To enable the Board of Directors to discharge its risk oversight responsibilities, amongst others, a risk committee was formed emanating from the Board of Directors, which includes three members of the Board. The Bank has developed and established the regulatory frameworks, policies, authorities, process and procedures and other control activities which constitute the Bank's control environment and determine the level of their adequacy and effectiveness to ensure the performance of these responsibilities.

To ensure the efficiency and effectiveness of the internal control system, the audit committee, emanating from the Board of Directors, supervise the independence, the efficiency, and the qualifying of the external auditors. As well as the monitoring of internal audit performance level at the Bank, the approval of the annual plans for the audit work, reviewing periodic reports of the control systems, and the work of the Independent review and inspection tasks carried out by the regulatory authorities, verifying the integrity of the financial statements and commitment to regulatory and control requirements, as well as reviewing disclosures in the financial statements with respect to these tasks.

At the Executive Management level, the Bank has the following committees: Credit Risk Policy Committee, Assets and Liabilities Committee, Operational Risk Management and Compliance Committee, which monitors credit risks, market risks, liquidity risks, operational risks, strategic risks and the compliance risk.

The Risk Management function at Riyad Bank is headed by the Chief Risk Officer (CRO) and includes oversight and management of all aspects of the Bank's risk planning, risk modeling, risk measurement, risk methodology development,

and implementation of the capital adequacy rules according to Basel Pillar as per Saudi Arabian Monetary Agency (SAMA) requirements . The Credit Risk management mandate is exercised through the Credit Division, covering all aspects of credit risk. The Risk Management Division covers both financial and operational risks. In addition, the Bank's Capital Management Unit, reporting to the Chief Risk Officer (CRO), is responsible for overseeing and coordinating the preparation of Internal Capital Adequacy Assessment Plan (ICAAP). All of which constitute the Risk Management directly report to the CRO.

The independent Compliance Department, which directly reports to the Bank's Chairman is responsible for assuring the Bank is compliant with all regulations and related by laws.

#### **Internal Control:**

The Bank has established a Control Management Department directly reporting to the Chief Risk Officer (CRO). The Control Management Department works to gather all of the information in this regard from all sectors and control authorities, whether internal or external, classification and analysis of their importance, and follow-up necessary plans to enhance the internal control system. The department also reviews the issuance of the annual attestations made by the executive management and supervisory units for the safety and efficiency of the internal control system.

The Internal Control Department is responsible for reporting on internal control and the various types of risk, based on its importance to the Audit Committee and executive management at all levels, as well as to the Operational Risk Management and Compliance Committee.

The Bank completed linking the internal control system to the performance standards on the executive management level. The Bank's divisions also completed the application of control risk self-assessment of risk and internal control procedures, through Divisional Controllers to perform ongoing tests to evaluate and improve the procedures and policies adopted within each sector.

Set out below is a summary of the major risks, and an explanation of how the Bank manages each risk type:

#### 1- Credit Risk:

Credit risk is the potential that a bank obligor or counterparty will fail to meet its obligations in accordance with agreed terms. Riyad Bank manages these risks by conducting in depth and thorough analysis of the borrower's ability to honor his obligations which would include repayment sources, the nature of underlying collateral and other factors and conditions impacting the borrower's activities. The Bank utilizes sophisticated credit software systems to ensure management of credit applications, limits management and collateral management. The Bank uses an advanced internationally recognized credit rating system to assess the viability of corporate credit applications and produce their credit ratings according to the rating system that is approved by the Board of Directors. The Bank also uses an advanced retail credit system for Retail Risk .Additionally, Riyad Bank uses approved ratings from well recognized rating agencies accepted by Basel Committee to measure risks

In this context, the Bank is currently upgrading its infrastructure by developing an automatic system for early warning notification to start reviewing credit portfolios and take the necessary corrective measures before it gets affected.

#### Strategy and framework for credit risk:

Riyad Bank's Board of Directors approved the framework of Credit Risk Management (CRM), credit risk strategy, and Risk Appetite Statement. This framework includes the principles, structures, tools and activities required for managing credit risk at all levels in the Bank. The CRM Framework and credit risk governance structure are designed to provide comprehensive controls and continuing management of the credit risk inherent in the Bank's business activities in the presence of a clear segregation of roles and tasks assigned to the

entities participated in risk management.

Another purpose of this framework is to support the Bank's efforts to enhance the Bank's asset quality, while observing the rules and regulations set by the Saudi Arabian Monetary Agency (SAMA), all within clearly designed and regularly monitored risk parameters. In addition, the Bank's Credit Strategy and Risk Appetite Statement set out a clear plan for identifying, establishing risk tolerance parameters, along with monitoring and reporting mechanism for credit risk in the Bank, in addition to continually assess and monitor credit exposures to ensure timely identification of potential credit problems. Credit concentration exposures is reviewed and evaluated by industry and geographic areas of customers to ensure that the credit portfolio is adequately diversified according to bank's approved principles and strategies by setting limits to reduce those risks. The Board of Directors and Risk Committee emanating from it have a key and important role in risk-appetite determination, and the approval of credit policy, credit authority delegations, approval of large credits, continuing review of existing credit exposures, and review of status and trends in credit portfolio quality, industry and sector credit concentrations.

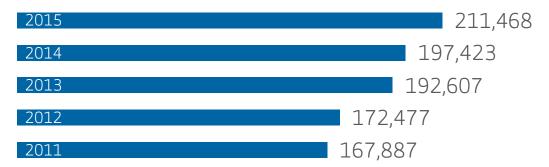
# Credit assets weighted for the purposes of capital adequacy calculation:

As of 1/1/2008, under the approval of the Saudi Arabian Monetary Agency (SAMA), the Bank adopted the Standardized Approach to determine credit assets weighted for the purposes of capital adequacy measurement

Where the relative weights of these assets are calculated according to its kind, and through the automatic system, the required capital values are allocated for each. After the Bank's success in developing the capacities of credit rating models in line with the requirements of the «Basel-III» for measuring the necessary capital adequacy to cover credit risk, we are considered at an advanced stage to start the application of the standard of internal Rating Based (IRB) of credit risk.

The graph below illustrates bank's assets weighted according to credit risk:

#### Credit Risk Weighted Assets (SAR Million)



For the purposes of presentation, the Credit RWAs, after 2012 are calculated using the framework and the methodologies defined under the Basel III framework. The comparative balances for 2012 and earlier years are calculated under Basel II and have not been restated.

During 2015, the Bank has achieved progress towards the application of the Internal Rating Based (IRB). In addition to the design of different models for credit rating, the Bank has developed a system to verify the accuracy and completeness of those models periodically. The year also witnessed another round of independent periodic tests to validate the outcomes of these credit rating models and its quantitative and qualitative components in line with the Saudi Arabian Monetary Agency (SAMA) expectations. The Bank has set up the infrastructure required to use and operate these models in taking the credit related decision depending on a precise measurement of credit risk and the expected return from these risks. At the same time, the Bank completed the review of risk policies to further assure that the credit rating systems meet Internal Rating Based IRB standards.

At the administrative-organizational level, the Credit Risk Policies Committee and Retail Risk Committee are responsible for ensuring of set out and formulate the credit policies and ensure their effective implementation. They are also responsible for following up and monitoring the effectiveness of the role of credit risk management. In Addition,

the Credit Committees, of various compositions and authorities, make the assessment and the adoption of credit exposures of the Bank within the risk limits and required standards for documenting, supervision, and follow-up facilities including the main credit committee, headed by the CEO of the Bank. The Credit Division, independent of the business sectors, manages and controls the credit risks. This is done as a part of a credit risk management framework and credit strategy and Risk Appetite Statement approved by the Bank's Board of Directors under a clear mechanism to monitor and track the department's commitment by the set standards and credit limits identified previously by the Board and reporting on them periodically.

The Internal Audit Department is responsible for reporting to the Audit Committee emanating from the Board of Directors on the ongoing credit portfolio review and the external auditors review and submit their report to the Audit Committee and the Board of Directors on the financial statements of the Bank.

The Investment Committee, chaired by the Chairman of the Board, oversees the Bank's investment portfolio in accordance with Board-approved asset allocation and investment guidelines and mandates. The Investment Committee sets out the policy framework and investment asset allocation. The Portfolio Managers' performances are reviewed by the Investment Department and independent consultants.

The governance framework of the credit Risk Management within the Bank is shown in the diagram below:

#### **Credit Risk Management**



Riyad Bank's credit exposure can be classified in two broad risk categories: Retail Credit Risk and Non-Retail Credit Risk

Retail Credit Risk is the risk of non-payment arising from the consumer finance, mortgage loans, credit cards, and other products offered to individuals. Retail Banking risk acceptance is primarily based on the application of fixed criteria using well-defined scoring methodologies including assessment system. Retail Credit Risk management assesses and develops systems and tools currently used to better measure the risk adjusted returns within the approved risk management frameworks of the Bank . This assessment will benefit the customer's experience by adopting a digital strategy which provide customers with fast and easy access to e-banking services. The Consumer lending risks are mitigated by stipulating a maximum cap on lending activities and the availability of minimum capacity to borrow, in addition to obtaining collaterals and close monitoring of the performance of loan portfolios to avoid the risk of concentration.

Preparing the portfolio allocations based on the allocation policy followed by the Bank as mentioned below.

Non-Retail lending includes corporate facilities/ loans and overdrafts, inter-bank loans, loans to governmental and semi-governmental entities, small and medium-sized enterprise loans, trade finance, structured and project finance, leasing, syndicated loans, corporate guarantees and overdraft. Corporate credit risk is managed by ensuring timely identification, quantification, calibration, monitoring, and credit exposure reporting in line with the Bank's credit risk appetite, and regulatory requirements, corporate strategy, and the Bank's portfolio and sector strategy. Concentration policy and limits exist for single customer exposure, industry concentration, and segment exposure. Credit Risk to related parties are covered by collaterals as per regulatory requirements. Risk is monitored on facility basis, total exposure (single name) basis, portfolio basis. The Bank utilizes sophisticated credit administration and limit management software systems to ensure the full lifecycle management of credit applications, limit management, and financial and non-financial collateral management.

The Bank applies an integrated system for credit rating assessment using two styles of measurement; internal and external qualitative and quantitative measurement. The external, (borrower classification) is assessing the financial analysis by qualitative and quantitative standards, while the internal depends on specific standards for each rating grade / class. Both ratings are validated and presented to the appropriate authority. Note that, any changes in the degree of customer rating are to be adopted by the Credit Risk Rating Committee and the Credit Risk Rating Review Committee and the internal audit department monitors those classifications and their amendments.

Credit risk of the Foreign Financial Institutions and Countries are monitored within the credit limits framework for countries and financial institutions approved by the Board of Directors, additionally there is a dedicated unit in the Bank for evaluating and monitoring the financial institutions credit risk.

The Bank uses Standard & Poor's, Fitch, Moody's, and Capital Intelligence as External Credit Assessment Institutions for ratings of Sovereigns, Central Banks, Banks, Securities Firms and Corporations.

In accordance with the regulator (Saudi Arabian Monetary Agency SAMA), if a given exposure is rated by two External Credit Assessment Agencies, then the lower rating is applied; in case any exposure is rated by three External Credit Assessment Agencies, the highest is discarded, the higher of the residual two ratings is applied.

Collateral is never the principal basis for lending decisions but is viewed as an alternative source of repayment in the event that a business fails. This is controlled by the Bank's policy guidelines on collateral acceptance that determines collateral valuation and liquidity. The collateral risks are monitored on a regular basis.

The Bank has established an effective system of internal controls on credit operations to reduce operational errors risks, fraud and losses that may affect the Bank and its clients. This is done through a clear segregation between business units and rating units, approvals, and implementation at all levels, and through an automatic system documenting all

procedures followed during the credit operations for purposes of control, auditing and documentation.

#### Provision policy:

Provisions of retail loans granted to individuals and commercial loans classified as non-performing debts are calculated on a quarterly basis. The results of a provisions study are presented to the Audit Committee and the Board of Directors for approval, these provisions are reviewed quarterly by the Bank's Internal Audit Department and the External Auditors.

Riyad Bank provisions consist of specific provisions and portfolio reserves. Specific provisions for collateralized defaulted personal loans (against shares and/or Investment Portfolio), mortgage lending for individuals, non-retail loans classified as non-performing, are calculated and reviewed on a periodical basis. This is done through a detailed study for every client classified as non-performing debts. The provision value is the difference between the Net exposure of the client minus the current value of the expected collection net exposure after taking into account the value of collateral related to mortgage lending and collateralized defaulted personal loans.

The general reserve portfolio is calculated for the lending portfolio of commercial performing loan, individuals and credit cards, to cover potential losses in the portfolio in accordance with a specific mechanism which takes into account the debt rating and hedge ratios that reflect the potential loan default levels in each category of the portfolio. For the rest of retail finance products, in case of non-payment for a period of 180 days from the due date, the debt is cancelled and charged to the profit and loss account.

#### 2- Market Risks:

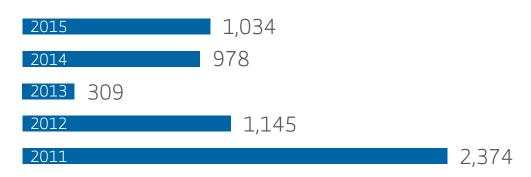
Market risks are the risks related to fluctuations in the fair value or future cash flows of the financial instruments incurred as a result of changes in the market elements prices as special commission rates, foreign exchange rates, or equity prices. The Bank classifies its exposure to market risk into Trading Book and Banking Book risks.

The market risk is managed and monitored using a Value at Risk (VaR) methodology. Market risk for the non-trading book is managed and monitored using a combination of VaR, stress testing and sensitivity analysis.

Market risk of non-trading book includes the fluctuations in special commission rates, foreign exchange rates, or equity prices.

The graph below shows the Bank's Market risk weighted assets:

#### Market Risk Weighted Assets (SAR Million)



For the purposes of presentation, the Market RWAs after 2012 are calculated using the framework and the methodologies defined under the Basel III requirements. The comparative balances for 2012 and earlier years calculated under Basel II and have not been restated.

The Bank monitors its traded market risk positions daily and uses hedging strategies where necessary to ensure maintenance of positions within the established gap limits set and approved by the Board. The Bank manages exposure to the effects of fluctuations in prevailing foreign currency exchange rates on its financial position and cash flows. The Board of Directors sets limits on the level of currency exposure. To mitigate liquidity risk, the Bank has diversified funding sources and retains an appropriate balance of cash, cash equivalents and readily marketable securities as liquid assets.

#### 3- Operational Risk:

Riyad Bank's operational risk strategy is to ensure that the Bank is safeguarded against major operational risks while ensuring that losses incurred as a result of operational risk are minimized. The Bank has updated risk-mitigation strategies supported by risk management frameworks, policies and procedures aimed at detecting and controlling risks. A centralized Operational Risk Management Department monitors and manages all operational risks impacting the Bank and submits monthly reports to the Operational Risk Management & Compliance Committee (ORMCC) which is chaired by the CEO as well as submitting a semi-annual Report to the Risk committee emanating from the Board of Directors.

The graph below shows the Bank's Operational Risk weighted assets:

#### Operational Risk Weighted Assets (SAR Million)



\* For the purposes of presentation, the Operational RWAs and the ratios related after 2012 are calculated using the framework and the methodologies defined under the Basel III . The comparative balances for 2012 and earlier years are calculated under Basel III have not been restated.

Operational risk management also includes:

#### Financial Crimes Prevention Department:

In response to the directions of Saudi Arabian Monetary Agency (SAMA), to adopt the best international practices to combat financial crime risk, a specialized department to combat financial crime risk has been developed. One of the main goals of this department is to prepare and develop policies, procedures and systems that helps the Bank management to identify, assess and manage these risks. Both Anti-Fraud Department and Anti money laundering & Terrorism Financing department reports back to this department.

#### Insurance & Operations Loss Analysis Section:

This section works on recording, analyzing and reporting all operational losses incurred by the Bank, as well as reduce the risks through the work of appropriate insurance documents that cover all expected risks, taking into account their cost. The sections also follows-up the Bank claims to cover the risks / losses that have already occurred from the Insurance Company.

Additionally, the section assesses the accepted risks and evaluates risk management efficiency, which helps business segments to improve the effectiveness of the internal control system through the development of strategies that help in reducing and mitigating the risks.

The Insurance section is responsible in managing all bank-wide insurance policies and claims. It is also responsible for ensuring that appropriate level of cover is maintained for insurable risks across the Bank's business areas, and for the design, placement and administration of the Bank's Insurance Plan through a cost-effective insurance program that provides protection against insurable risks.

The Insurance section tracks & manages all claims as well as settlements with insurers and negotiates with Insurers and Brokers on all terms such as cost, coverage, limitations, exclusions and deductibles, to obtain suitable deals.

#### Investigation and Examination Section:

This section performs examination and investigations in accordance with the approved methodology, including the Bank's branches and administrative units supporting branches in both Retail and Operations, Investment Operations in Riyad Capital, and customer care unit to ensure the effectiveness of the designed procedures and operational policies, and that the acceptable limits of operational risks are not exceeded.

Moreover, this section is also responsible for conducting specific bank-wide investigations in respect of any human, procedure or systems failure or error. Additionally, the section also proposes recommendations to improve the design effectiveness of operational systems, policies and procedures. As such, it follows up on the implementation of these recommendations with the relevant authorities

#### Key Risk Indicators & Process Analysis Section:

The Key Risk Indicators (KRI) and Process Analysis Section is responsible for providing operational risk oversight through the quantification and assessment of operational risks across the Bank's business lines. This is achieved through bank wide deployment and reporting of Key Risk Indicators (KRIs), Risk Control Self-Assessment (RCSA), mandatory risk assessments of all bank products and services and compliance with Basel II requirements for Operational Risk. The major mission of the section is to facilitate operational risk awareness across the Bank via the mitigation and management of bank wide operational risks and to identify control gaps related to all bank processes, products and services.

#### Other Risks:

The Bank follows integrated strategies to manage, monitor, and control other risks such as the following:

#### a-Liquidity Risk:

Liquidity risk is the risk that the Bank will be unable to meet its net funding requirements. Liquidity risk can be caused by market disruptions or credit downgrades, which may cause certain sources of funding to dry up immediately. To mitigate this risk, management has diversified funding sources and assets are managed with liquidity in mind, maintaining an appropriate balance of cash, cash equivalents and readily marketable securities. Management monitors the maturity profile to ensure that adequate liquidity is maintained. The daily liquidity position is monitored. Regular liquidity stress testing is conducted under a variety of scenarios covering both normal and more severe market conditions. All liquidity policies and procedures are subject to review and approval by Assets and Liabilities Committee (ALCO). Daily reports cover the liquidity position of the Bank, a summary report, including any exceptions and remedial action taken, are submitted regularly to ALCO.

#### b- Credit Concentration Risk:

Concentration Risk refers to the risk from an uneven distribution of lending portfolio between customers in business sectors or geographical regions.

The Bank manages 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. The Bank takes suitable collaterals on a regular basis and also seeks additional collateral from the counterparties as soon as impairment indicators are noticed for the relevant individual loans and advances.

#### c- The Volatility Risk of Collateral Market Value:

The section monitors the market value of collateral on a continuous basis and requests additional collaterals in accordance with the concluded agreements, and monitors the market value of collateral obtained during its review in respect of the adequacy of impairment losses. The Bank regularly reviews its risk management policies and systems to reflect changes in market products and best credit practices.

#### d - Banking Rate Risks:

Risk banking rates arise in the banking book as a result of fluctuations in service rates affecting the fair value of the financial instruments cash flows of the Bank's assets portfolio. The Board sets limits for follow-up and control of such fluctuations and their impact on the Bank, as well as precautionary measures to confront, reduce and avoid negative effects, through the adoption of several hedging strategies.

#### e-Information Technology Risks and Strategic Risks:

These risks arise as a result that one or some assumptions that were part of the Bank's business plans did not achieve its goals. The Bank has adopted a clear and integrated framework for the strategic planning process which takes into account macroeconomic risks, business cycle risks, settlement risks, where these strategies focus on reducing their negative effects. The Bank also provides enough capital to cover these risks. The Bank regularly follows up on these plans and monitors their implementation to ensure the achievement of predetermined targets. In this context, the Bank has set a clear policy to establish Business Technology in line with the strategic objectives of the Bank and in accordance with the Saudi Arabian Monetary Agency (SAMA) requirements and includes several major factors such as the technical structure of the Bank with various work units, and, standards of security and safety, absorptive capacity and immediate treatment of accidents.

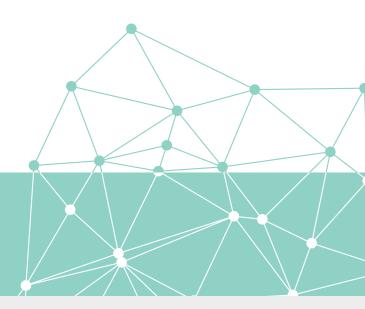
The Bank also performs stress tests following a set of rules and standards to apply these tests for various types of risks in all aspects of banking activities.







# **EXECUTIVE**MANAGEMENT





**Talal I. Al-Qudaibi**President & Chief Executive Officer



**Abdulmajeed A. Al-Mubarak**Deputy Chief Executive Officer



**Thalib A. Al-Shamrani**Senior Executive Vice President,
Chief Risk Officer



**Abdulaziz S. Al-Malki** Executive Vice President, Treasury & Investments



Adel A. Al-Sheikh Senior Executive Vice President, Retail Banking



Ahmed Y. Al-Tayeb Executive Vice President, Risk Management



Ossama A. Bukhari Executive Vice President, Corporate Banking



Adnan S. Al-Joyan Executive Vice President, Human Resources



**Riyadh O. Al-Zahrani** Executive Vice President, Business Support



Mohamad A. Al-Rabeah Executive Vice President, Marketing



**Hani A. Abu Al Naja** Executive Vice President, Branches



**Aiedh M. Al-Zahrani** Executive Vice President, Business Technology



**Mohammed Qureshah**Executive Vice President,
Finance



**Abdulaziz Al-Asker** Executive Vice President, Credit



**Enji Al-Ghazzawi**Executive Vice President,
Operations



Mohammed Abo Al-Naja Executive Vice President, Corporate Services



Nadir S. Al-Koraya Executive Vice President, Treasury

# HEAD OFFICE, REGIONAL AND **OVERSEAS OFFICES**

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#### **Western Region**

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#### **Overseas Branches**

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#### Houston

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# Singapore

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#### **Regional Managers**

#### Ibrahim Fayez Al Shahri

Regional Manager, Eastern Region

#### Yasser A. Al-Babtain

Regional Manager, Central Region

#### **Nayef Mansour Shalabi**

Regional Manager, Western Region