MORE RESILIENT DEPSITE A MAJOR CREDIT CRISIS

- Having released their preliminary Q3 09 results, Saudi banks have continued to show major strengths confirming our optimistic outlook for the sector. In times of such crisis, this sector has managed to report a total profit of SAR 7.14 billion in Q3 09 and SAR 22.35 billion in 9M 09, with none of the individual banks reporting a single loss.

- Compared to the previous quarter, the Saudi banks' net loans and advances grew by a small 1.1% in Q3 09 to SAR 778 billion while customer deposits have declined by 1.8% Q-o-Q to SAR 963 billion. We believe the growth in the industry's loan book will remain muted in the short term, as banks seem to be cautious in their lending activities until the uncertainty surrounding the corporate defaults issues is resolved and the expected global economic recovery stands on solid footings.

- During the first nine month of the year, Saudi banks have reported a YTD rise of 0.7% in their loan book but a larger increase of 4.5% in their customer deposits. This normally translates into lower interest income. However, the higher pricing of risk coupled with a low cost of funding has helped the banks maintain their profitability from core business operations. This has been indicated by the 7% growth in the sector's net special commission income during the first nine month of 2009 as compared to the same period last year.

- Though higher in absolute terms compared to the previous quarter, the credit provisioning for the sector came in less than our forecasts. We estimate total provisions for credit losses at SAR 2.22 billion in Q3 09, up by 19.5% relative to SAR 1.89 billion reported in Q2 09. However, given the lack of transparency regarding the settlement of the Saad Group's debt and the many issues still pending with Al Gosaibi Group, we maintain our cautious stance on the rising NPLs, while lowering our forecasts for the sector's total credit provisioning to around SAR 9 billion from SAR 10.3 billion.

- With real GDP growth expected at 4% in KSA for year 2010, and oil price crossing the USD 80/barrel level, the sector is well positioned to benefit from this positive economic environment supported by its inner operating strengths.

- Capital Adequacy: The positive net income achieved in the past quarters coupled with the largely stable loan portfolio will help further improve the capital adequacy level of Saudi banks.

- Conclusion: Given that the recent quarterly results were broadly in line with our estimates, we maintain the same target prices for the seven banks that we covered in our report dated 26 September, 2009. However, we adjust our recommendations to reflect the recent price developments in the market.

COVERED BANKS

	Current Price (SAR)	Target Price (SAR)	Upside Potential	Recommendation	PB	PE 2009 E	PE 2010 E
Samba Financial Group	57.50	69.75	21.3%	Accumulate	2.63	12.42	9.98
Al Rajhi Bank	77.75	80.72	3.8%	Hold	4.26	18.51	15.25
Riyad Bank	29.50	31.54	6.9%	Hold	1.65	16.48	12.88
Saudi British Bank	49.80	61.47	23.4%	Accumulate	2.85	15.05	11.83
Banque Saudi Fransi	45.80	51.48	12.4%	Accumulate	2.23	14.01	11.93
Arab National Bank	47.00	53.87	14.6%	Accumulate	2.31	12.47	10.51
Saudi Hollandi Bank	33.50	35.61	6.3%	Hold	1.88	16.67	10.91

SECTOR COVERAGE

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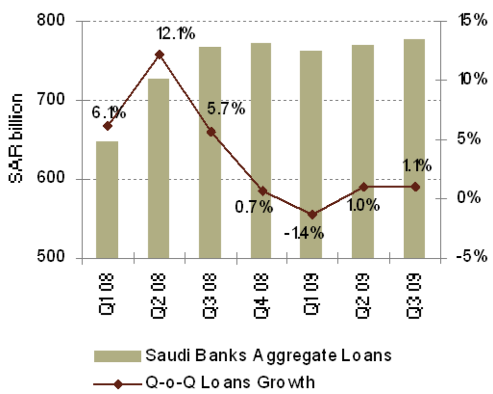
FINANCIAL ANALYSIS FOR 9M 09

Saudi banks reported their preliminary Q3 09 earnings, which came in ahead of market expectations for most of the banks with credit provisioning being the major reason of deviation.

Loan Growth Slightly Revived

Chart 1: Saudi Banks Loan Growth



Source: Saudi Banks Financial Statements

Table 1: Loan Growth across Banks

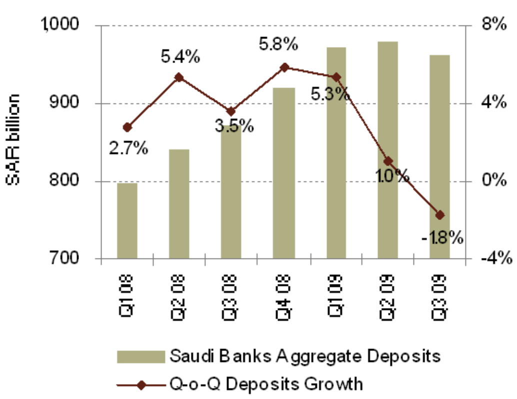
Loans Growth	Q3-o-Q2 09	Q2-o-Q1 09
NCB	10.1%	3.8%
Bilad	2.8%	13.2%
Riyad	1.4%	4.4%
SIB	1.2%	0.1%
Rajhi	0.7%	0.9%
SABB	0.1%	-0.7%
BSF	-0.5%	0.1%
Jazira	-1.4%	3.3%
SHB	-1.7%	0.8%
Samba	-2.2%	-2.4%
ANB	-3.3%	-2.3%

Source: Saudi Banks Financial Statements

Following the increase of 1% in Q2 09 Saudi banks loan book grew by 1.1% Q-o-Q in the third quarter of 2009 to reach SAR 778 billion at the end of September 2009. Among the eleven banks we cover in our analysis, The National Commercial Bank led the way by rising 10.1% Q-o-Q followed by Bank Al Bilad, Riyad Bank and Saudi Investment Bank that displayed a growth of 2.8%, 1.4% and 1.2% respectively. On the negative front, Arab National Bank reported the highest drop in its loan book, down by 3.3% followed by Samba that reported a drop of 2.2% Q-o-Q. We believe the growth in the industry's loan book will remain muted in the short term, as banks seem to be cautious in their lending activities until the uncertainty surrounding the corporate defaults issues is resolved and the expected global economic recovery stands on solid footings.

Deposits Decline

Chart 2: Saudi Banks Deposit Growth



Source: Saudi Banks Financial Statements

Table 2: Deposit Growth across Banks

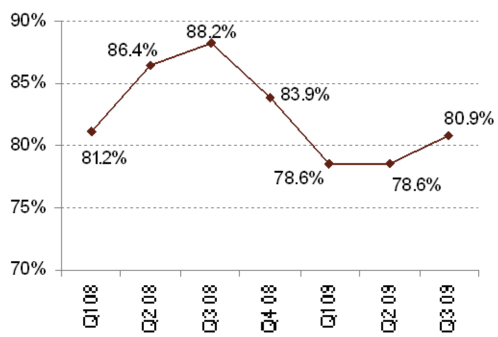
Deposits Growth	Q3-o-Q2 09	Q2-o-Q1 09
SIB	5.6%	-4.4%
Samba	2.8%	11.2%
Jazira	0.2%	-29.4%
Rajhi	0.0%	2.6%
BSF	-0.3%	-1.4%
Riyad	-2.1%	2.4%
SABB	-2.6%	-5.3%
NCB	-4.1%	1.4%
Bilad	-4.5%	-1.5%
ANB	-5.6%	0.8%
SHB	-8.4%	7.4%

Source: Saudi Banks Financial Statements

The Saudi banking system deposits have contracted by 1.8% Q-o-Q and amounted to SAR 963 billion at the end of Q3 09. We believe some banks are letting go of expensive deposits to maintain their spreads and preserve their profitability. Taking a look at the banks individually, we observe that the worst performers were Saudi Hollandi Bank and Arab National Bank that reported a drop of 8.4% and 5.6% respectively while other players such as Saudi Investment Bank and Samba delivered a notable increase of 5.6% and 2.8% respectively. However, as the numbers indicate, we do not see any major migration of deposits outside the system, as some banks are attracting some deposits on the back of others.

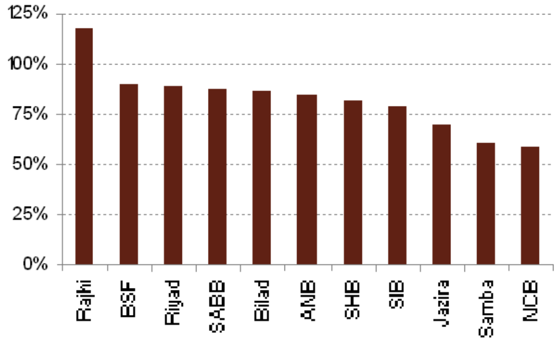
Tightened Liquidity

Chart 3: Saudi Banks Loans to Deposits Ratio



Source: Saudi Banks Financial Statements

Chart 4: Loans to Deposits Ratio across Banks (Q3 09)

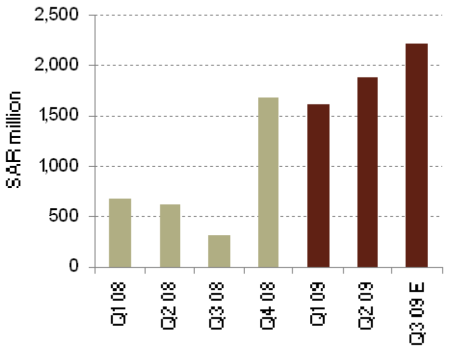


Source: Saudi Banks Financial Statements

Examining the liquidity position of the banks, we notice that the faster growth in loans as compared to deposits resulted in a higher loans-to-deposits ratio of 80.9% in Q3 09, up from 78.6% in Q2 09. However, the overall system liquidity is satisfactory both on an aggregate level and on an individual bank level. It is worth noting that NCB and Samba are the best positioned to benefit from an upturn in the credit cycle as these banks present loans to deposits ratios at the 60% range.

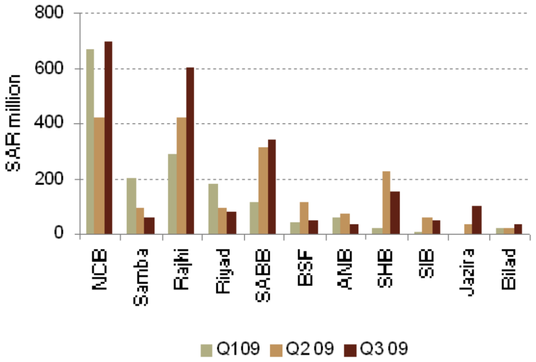
Credit Provisioning Appears Mixed across Banks

Chart 5: Saudi Banks Provisions for Credit Losses



Source: Saudi Banks Financial Statements and Audi Capital Estimates

Chart 6: Provisions for Credit Losses across Banks

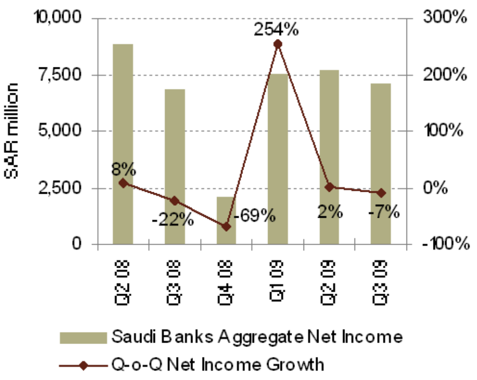


Source: Saudi Banks Financial Statements

In Q3 09, the Saudi Banks' aggregate provisions for credit losses continued their rising trend, escalating by 17.5% Q-o-Q (as per our calculations) following the 17.3% increase in Q2 09. This high level of provisioning is obviously resulting from some deterioration in the asset quality of the banks' loan book and the rising level of NPLs. We note that during the first nine month of the year, banks have booked a total of SAR 5.7 billion as provisions for credit losses and believe that this cost will increase further during the last quarter of the year to reach a total of around SAR 9 billion for year 2009.

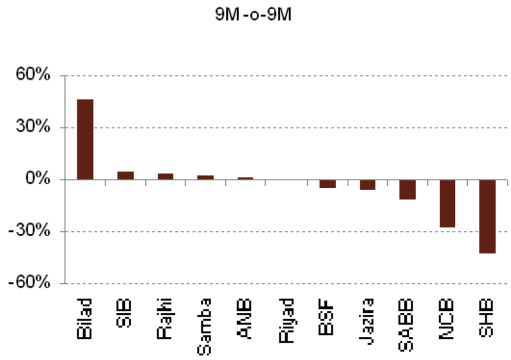
Net Income

Chart 7: Saudi Banks Net Income



Source: Saudi Banks Financial Statements

Chart 8: Net Income Growth across Banks (9M 09)



Source: Saudi Banks Financial Statements

Due to the 17.5% rise in provisions for credit losses in Q3 09 compared to Q2 09, consolidated earnings for Saudi Banks dropped by 7.2% Q-o-Q. During the first nine month of the year, banks' earnings declined by 6.6%, negatively affected by the 255% surge in provisions for credit losses (9M-o-9M), although net special commission income increased by 7% owing to the increase in net interest spreads.

Net Income (SAR million)	Q1 09	Q2 09	Q3 09	Q3-o-Q2 09	Q2-o-Q1 09
SHB	284	91	150	65.9%	-68.2%
SIB	241	188	203	8.1%	-21.9%
BSF	741	692	714	3.2%	-6.6%
Rajhi	1,732	1,771	1,795	1.4%	2.3%
Samba	1,272	1,243	1,211	-2.6%	-2.2%
NCB	1,051	1,192	1,034	-13.2%	13.4%
ANB	695	746	633	-15.2%	7.4%
SABB	760	676	570	-15.7%	-11.0%
Riyad	441	918	759	-17.3%	108.1%
Jazira	102	122	70	-42.8%	19.8%
Bilad	194	27	2	-92.9%	-86.1%

CURRENT PRICE **SAR 57.50**

CREDIT PROVISIONING BELOW THE MARKET'S ESTIMATES

9M 09 earnings increased by 2.7% Y-o-Y

- Samba Financial Group (Samba) reported strong Q3 09 net income of SAR 1,211 million; up 0.6% Y-o-Y but 2.6% lower Q-o-Q. This performance is significantly ahead of market's forecasts and stems mainly from lower than expected credit loss provisioning. 9M 09 net profit reached SAR 3,726 million, rising by 2.7% Y-o-Y from SAR 3,628 million reported in 9M 08.

Further improvement in the liquidity position

- Compared to the previous quarter, net loans and advances fell by 2.2% to SAR 86 billion while customer deposits inched up by 2.8% to SAR 142 billion leading to a further drop in loans to deposit ratio to 60.6% compared to Q2 09 ratio of 63.7%, implying an improved liquidity position. This drop in loans is mainly attributed to the continued cautious lending policies adopted by the bank though it is clear than the severity of the decline is easing. Compared to Q3 08 figures, net loans and advances also decreased by 10.7% while customer deposits grew by 13.6%.

- As of the end of Q3 09, net investments amounted to SAR 52 billion, implying a plunge of 20.7% compared to the same quarter a year earlier and a drop of 9.5% Q-o-Q. Although the overall size of the balance sheet picked up by 3.9% compared to the previous quarter, it continues to be 1.6% lower than Q3 08.

Preserved net special commission income spread

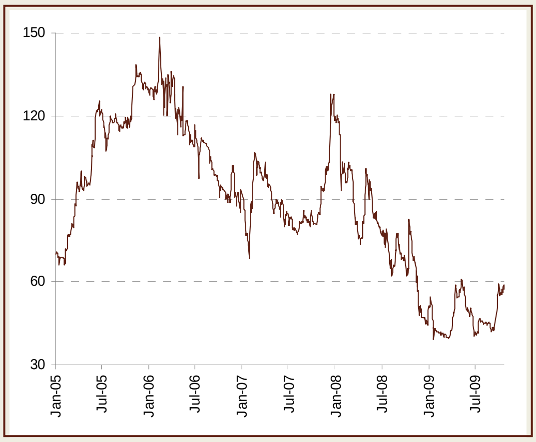
- On the income statement side, the bank reported a drop of 3.6% in its total operating income relative to Q2 09 to reach SAR 1,755 million. This decline is mainly driven by the non-special commission income that slumped by 10.6% Q-o-Q. We attribute this drop in non-special commission income to lower fees and commission and slower growth in the loan book. On the other hand, net special commission income totaled SAR 1,294 million; up by 2.6% Y-o-Y but almost flat Q-o-Q. This indicates a stronger net special commission income spread on the back of sustained higher pricing of risk.

… Higher provisions anticipated for the coming quarter

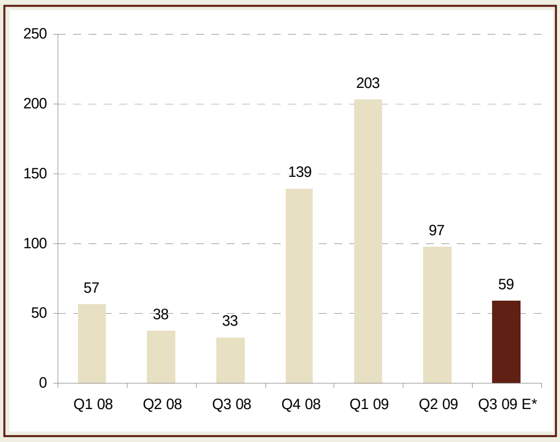
- On the provisioning front, and based on our calculations, we estimate the credit provisioning expense to amount to SAR 59 million in Q3 09, suggesting a drop of 39% Q-o-Q but an increase of 79% Y-o-Y. We expect the credit provisioning to increase in the coming quarter.

PERFORMANCE INDICATORS

Stock Price (SAR)

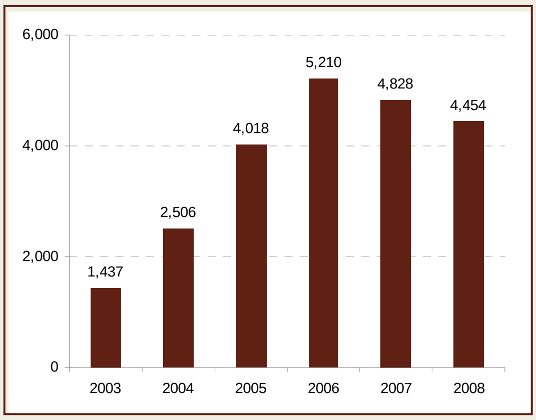


Provision for Credit Losses (SAR million)

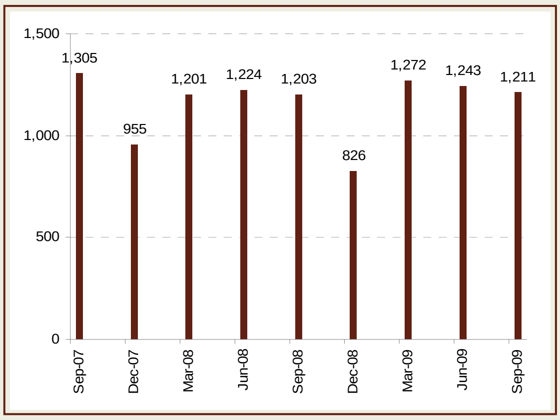


* Audi Capital Estimates

Yearly Earnings (SAR million)



Quarterly Earnings (SAR million)



CURRENT PRICE **SAR 77.75**

OVERALL STRONG RESULTS

9M 09 earnings increased by 3.9% Y-o-Y

- Al Rajhi Bank reported a net profit of SAR 1,795 million in Q3 09; increasing by 1.4% Q-o-Q and by 2.2% Y-o-Y. We believe this performance to be resulting mainly from the rise in operating as well as the non-operating income despite the surge in the provisioning expense "Impairment charge for investments and other".

Balance sheet growth remains stagnant

- The bank's net total investments (net loans and advances) almost remained unchanged compared to the previous quarter reaching SAR 145.5 billion but advancing by a larger 6% Y-o-Y. Also, on the funding side, customer deposits remained stable at SAR123 billion, growing by 4% Y-o-Y. These translated into a slightly weakened liquidity position with net total investments to customer deposits ratio (loans to deposits ratio) rising to 117.15% from 116.8% recorded in Q2 09. Also, the bank's total assets increased by 0.2% Q-o-Q and by 1.1% Y-o-Y.

- For the first nine month of the year, the bank's investment portfolio showed a strong growth of 130% compared to the same quarter last year to reach SAR 1,369 million.

- On the income statement side, total operating income went up by 7.3% Q-o-Q on the back of 8% growth in net income from investments that reached SAR 2,499 million in Q3 09 and 4.8% rise in non-operating income. We attribute this growth in net income from investments to improved interest spreads as balance sheet asset growth remained static.

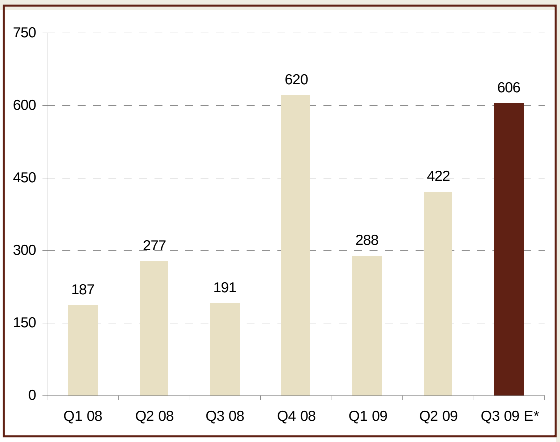
Q3 09 provisions estimated at SAR 606 million

- In Q3 09, we anticipate the provisioning expense to amount to SAR 606 million, translating into a growth of 44% Q-o-Q and more than tripling relative to Q3 08.

PERFORMANCE INDICATORS

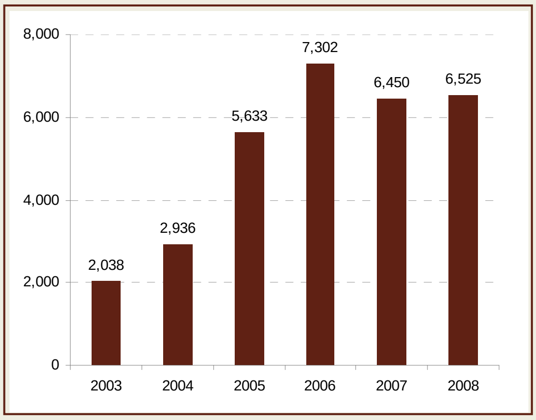
Stock Price (SAR)

Provision for Credit Losses (SAR million)

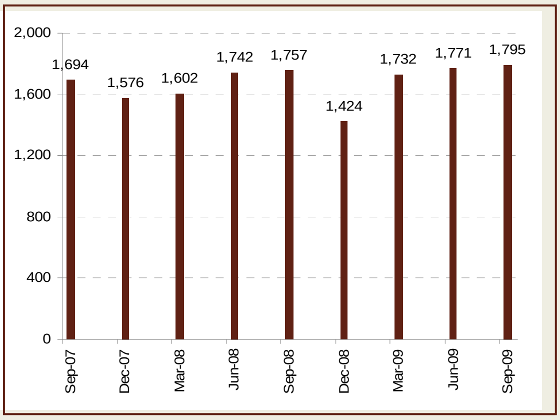


** Audi Capital –KSA- Estimates*

Yearly Earnings (SAR million)



Quarterly Earnings (SAR million)



CURRENT PRICE **SAR 29.50**

WEAK PROFITABILITY ON THE BACK OF LOWER INTEREST SPREADS

9M 09 earnings remained almost flat Y-o-Y

- Riyad Bank generated a net profit of SAR 759 million in Q3 09; up by 48.1% from SAR 513 million reported in Q3 08 but 17.3% lower than Q2 09 results. We believe this performance was due to the 10.5% drop in net special commission income despite lower provisions for credit losses compared to the previous quarter. 9M 09 profits reached SAR 2,118 million, rising by 0.4% Y-o-Y from SAR 2,110 million reported in 9M 08.

Continued balance sheet growth though at a slower pace

- Following an average growth of 4% during the past two quarters, net loans and advances showed a slower increase of 1.4% relative to Q2 09 to reach SAR 106 billion. On the funding side, the bank failed to maintain the high customer deposit growth rates witnessed in the past two quarters with deposits dropping by 2.1% Q-o-Q to reach SAR 119.5 billion and resulting in a loans to deposit ratio of 88.8% compared to 85.7% reported in the preceding quarter.
  It is worth noting that compared to Q3 08 figures, net loans and advances surged by 17.7% and customer deposits presented a stronger growth of 36.3%. Besides, the overall size of the balance sheet advanced by 21% to reach SAR 175.7 billion compared to SAR 145.2 billion reported at the end of September 2008.

- On the income statement side, it is clear that the bank's special commission spreads are contracting Q-o-Q. In fact, the bank reported a drop of 8.1% in its total operating compared to Q2 09. This is mainly attributable to the 10.5% Q-o-Q fall in net special commission income coupled with the 0.7% Q-o-Q drop in the fees and commissions income.

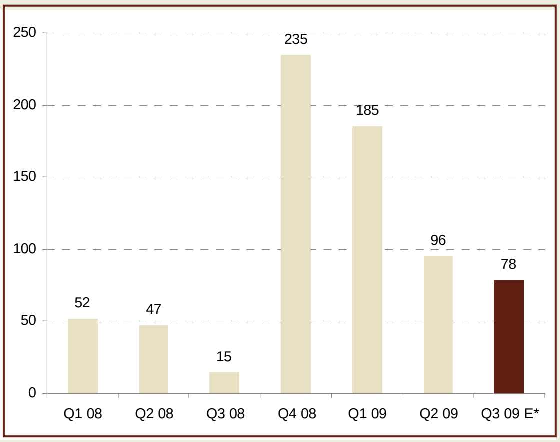
We estimate Q3 09 provisions at SAR 78 million

- On the provisioning front and based on our calculations, we estimate the provisioning charge for credit losses at SAR 78 million, dropping by 18% Q-o-Q but rising by more than five times Y-o-Y.

PERFORMANCE INDICATORS

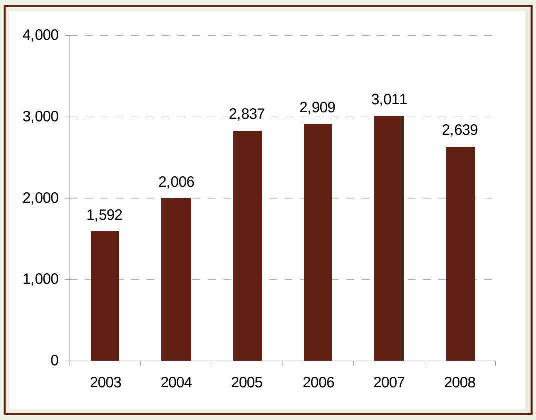
Stock Price (SAR)

Provision for Credit Losses (SAR million)

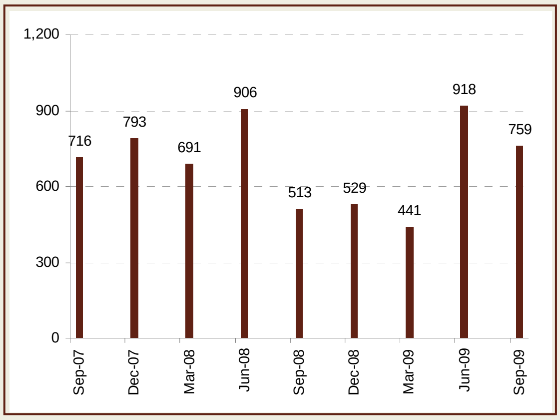


** Audi Capital Estimates*

Yearly Earnings (SAR million)



Quarterly Earnings (SAR million)



CURRENT PRICE **SAR 49.80**

HIGH PROVISIONING CONTINUES TO HIT THE BOTTOM LINE

9M 09 earnings dropped by 11.4% Y-o-Y

- Saudi British Bank (SABB) reported a net profit of SAR 570 million for Q3 09; a drop of 19.8% Y-o-Y and 15.7% lower Q-o-Q. We believe the bottom line was dragged down by the credit provisioning expense estimated at around SAR 342 million for Q3 09. This brings 9M 09 profits to SAR 2,006 million, decreasing by 11.4% Y-o-Y.

Tightened liquidity position

- Lending and deposits: On a Q-o-Q basis, loan growth was flat, increasing by 0.1% to reach SAR 78.8 billion while customer deposits retreated by 2.6% to record SAR 89.2 billion. This has led to a loans to deposits ratio of 88.3% compared to Q2 09 ratio of 86%.
  It is worth noting that compared to Q3 08 figures, net loans and advances dropped by 5.7% and customer deposits was pulled back by 6.8%. As a result, the overall size of the balance sheet shrank by 6.6% Y-o-Y. Besides, this contraction in the balance sheet size resulted from the 33% Y-o-Y fall in net investments that amounted to SAR 24.1 billion at the end of September 09.

Total operating income under pressure

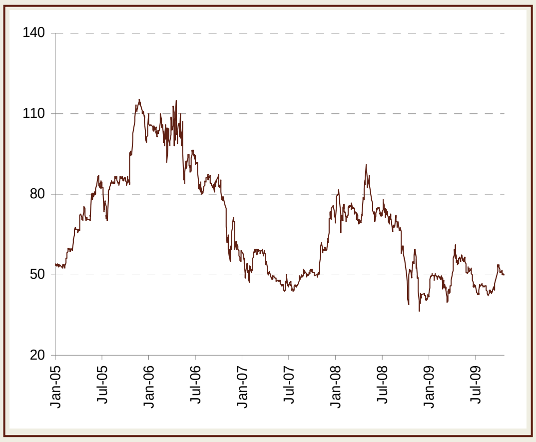
- The bank's total operating income reached SAR 1,304 million, down 7.5% Q-o-Q but up 10.7% Y-o-Y. This decline is driven by both the special commission income that dropped by 4.5% Q-o-Q and the non-special commission income that retreated by 7.9% Q-o-Q owing to lower trading volumes.

High provisioning continues

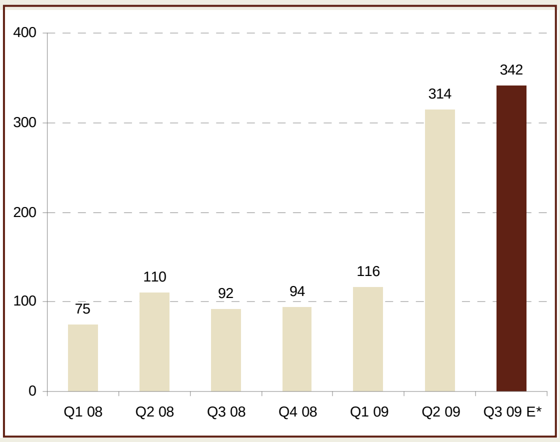
- Based on our calculations, credit provisioning were broadly in line with Q2 09 figure, amounting to SAR 342 million, up by 8.7% Q-o-Q but more than more than tripling Y-o-Y. For SABB, we expect the bank to continue its provisioning cycle, as the bank is building its coverage ratio to reach 100% by year end after falling in the previous quarter probably due to high exposure to defaulting groups.

PERFORMANCE INDICATORS

Stock Price (SAR)

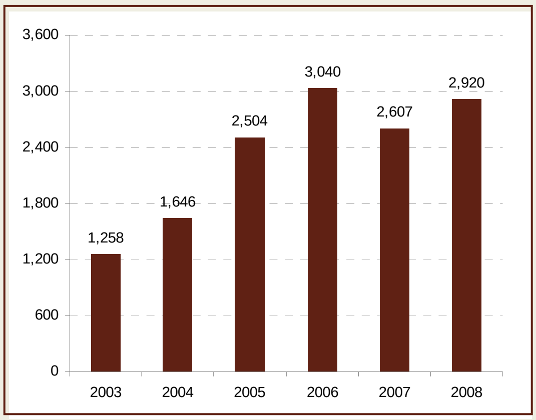


Provision for Credit Losses (SAR million)

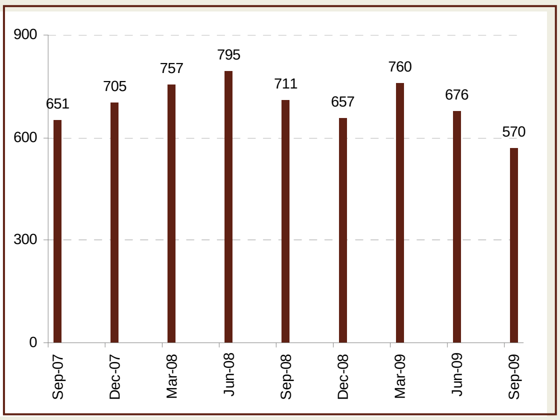


** Audi Capital Estimates*

Yearly Earnings (SAR million)



Quarterly Earnings (SAR million)



CURRENT PRICE **SAR 45.80**

LOWER PROVISIONING LED TO BETTER THAN EXPECTED EARNINGS

9M 09 earnings dropped by 4% Y-o-Y

- Banque Saudi Fransi (BSF) has posted a net profit of SAR 714 million in Q3 09, thus reporting a drop of 1.9% Y-o-Y but a growth of 3.2% Q-o-Q. We believe this quarterly performance is the result of lower "Impairment charge for credit losses" compared to the previous quarter. 9M 09 net earnings reached SAR 2,147 million, declining by 4% Y-o-Y from SAR 2,235 million reported in 9M 08.

Balance sheet size remains unchanged

- Compared to the previous quarter, net loans and advances remained almost unchanged, decreasing by 0.5% Q-o-Q to SAR 81 billion and customer deposits slightly contracted by 0.3% to SAR 90 billion. This has resulted into loans to deposit ratio of 90%, similar to the level recorded in the preceding quarter.
More notably, compared to Q3 08 figures, net loans and advances grew by 2.4 % and customer deposits advanced by 7.2%. However, the overall size of the balance sheet remained unchanged, up by 0.8% Y-o-Y, while contracted by 0.7% Q-o-Q to reach SAR 122 billion.

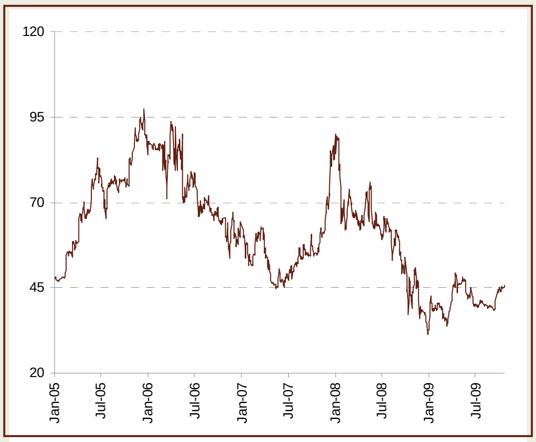
- On the income statement side, total operating income dropped by 3.6% Q-o-Q to SAR 1,057 million mainly driven by the 11.8% decline in non-special commission income. However, net special commission spread remained resilient with net special commission income slightly improving by 0.1% Q-o-Q but more importantly up by 10.8% Y-o-Y.

Provisioning level declines

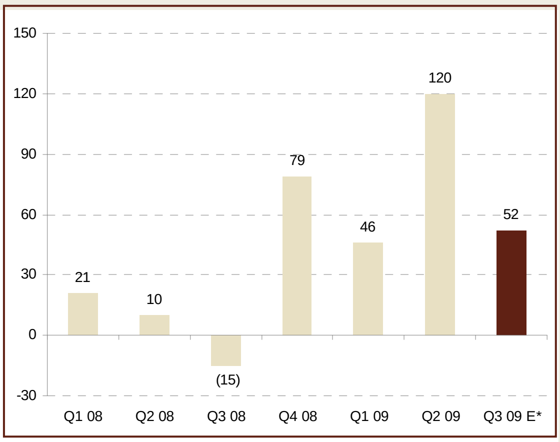
- Based on our estimates, BSF booked an impairment charge for credit losses of SAR 52 million, down by 57% relative to the previous quarter.

PERFORMANCE INDICATORS

Stock Price (SAR)

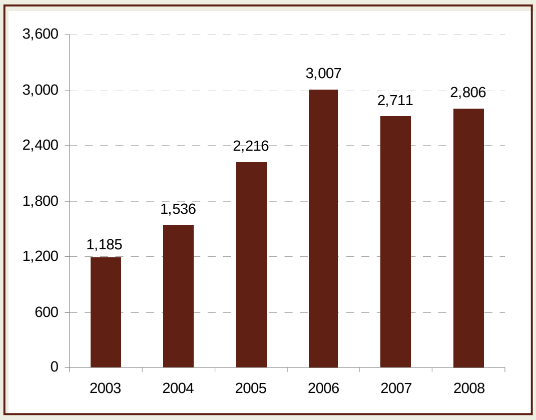


Provision for Credit Losses (SAR million)

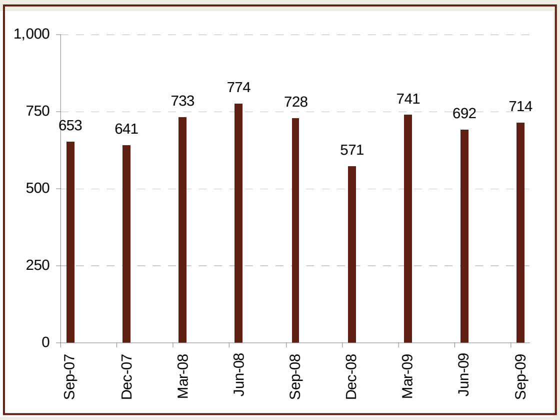


* Audi Capital Estimates

Yearly Earnings (SAR million)



Quarterly Earnings (SAR million)



CURRENT PRICE **SAR 47.00**

WEAKENED EARNINGS ON LOWER OPERATING AND NON-OPERATING INCOME

9M 09 earnings increased by 1.1% Y-o-Y

- Arab National Bank reported a net profit of SAR 633 million in Q3 09; down by 15.1% relative to the preceding quarter net income of SAR 746 million and remaining almost flat compared to Q3 08. This deterioration in the performance compared to the previous quarter is mainly attributed to the 28% plunge in non-special commission income. 9M 09 profits reached SAR 2,074 million, rising by 1.1% Y-o-Y from SAR 2,052 million reported in 9M 08.

Continued contraction in the balance sheet size

- Compared to the previous quarter, net loans and advances continued its sequential drop, declining by 3.3% Q-o-Q following the 2.3% Q-o-Q drop in Q2 09 and the 2.5% fall in Q1 09. On the funding side, customer deposits were pulled back by 5.6% Q-o-Q and 9.1 % Y-o-Y to SAR 80.5 billion. Consequently, the liquidity position of the bank slightly weakened with loans to deposits ratio standing at 85.5% at the end of Q3 09 compared to 83.5% reported in Q2 09.

- Total assets reached SAR 111.9 billion at the end Q3 09 compared to SAR 115.07 billion at the end of Q2 09; down by 2.8% Q-o-Q and by 3.3% Y-o-Y. The negative impact of the slowing loan growth was further intensified by the slowdown in net investments that dropped by 14% Q-o-Q.

Non-special commission income plunged by 28% Q-o-Q

- On the profitability side, total operating income contracted by 11.9% Q-o-Q to SAR 1,067 million owing to the 28% drop in non-special commission income on the back of lower trading volumes coupled with the 6.3% decline in net special commission income.

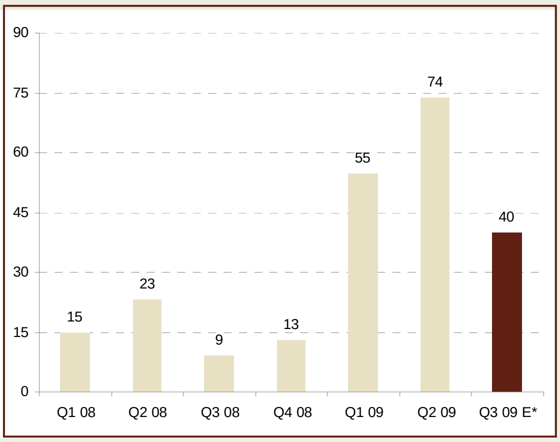
Q3 09 provisions estimated at SAR 40 million

- Based on our calculations, we estimate provisions for credit losses at SAR 40 million, dropping by 46% Q-o-Q but rising by more than four times compared to Q3 08. We believe the bank's high NPL coverage ratios reported in the previous quarters is supportive despite the current low provisioning level.

PERFORMANCE INDICATORS

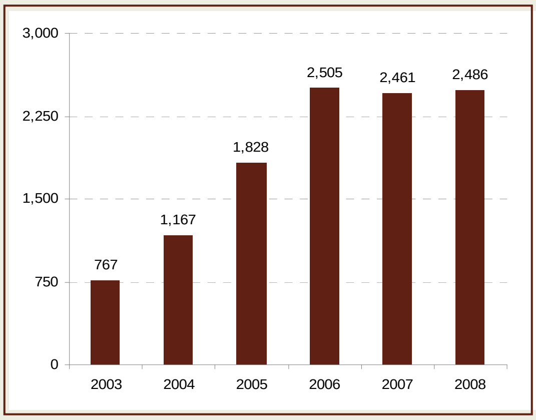
Stock Price (SAR)

Provision for Credit Losses (SAR million)

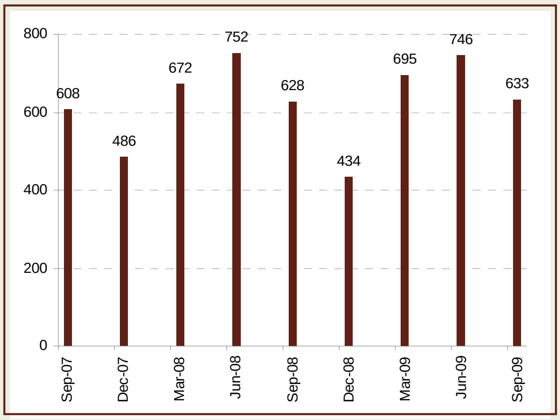


** Audi Capital Estimates*

Yearly Earnings (SAR million)



Quarterly Earnings (SAR million)



CURRENT PRICE **SAR 33.50**

HIGH PROVISIONING LEVEL CONTINUES TO NEGATIVELY AFFTECT THE BOTTOM LINE

9M 09 earnings dropped by 43% Y-o-Y

- Saudi Hollandi Bank has reported a net profit of SAR 150.3 million in Q3 09, down by 51% Y-o-Y but up by 66% Q-o-Q. We believe this negative performance compared to the same quarter last year is stemming mainly from the significantly higher provisions for credit losses that jumped by more than 27 times relative to Q3 08. 9M 09 profit reached SAR 525 million, dropping by 43% Y-o-Y from SAR 915 million reported in 9M 08.

- Compared to the previous quarter, net loans and advances remained almost flat, dropping by 1.7% to SAR 38.95 billion while contrary to what was witnessed in the previous quarter, the bank's customer deposits declined by 8.4%, to reach SAR 47.3 billion, losing all the deposits accumulated in the second quarter of the year. Hence, the loans to deposit ratio stood at 82.3% compared to 76.7% reported in the preceding quarter.
  Besides, the overall size of the balance sheet retreated by 8.5% Q-o-Q to reach SAR 63 billion. This decline has been further amplified by the 11.2% decline in net investments.

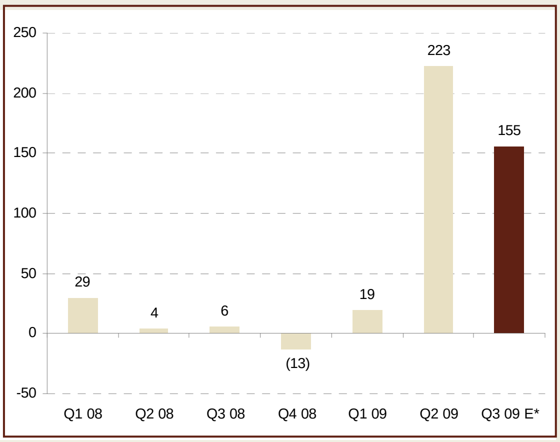
- On the income statement side, Saudi Hollandi Bank reported a drop of 6.6% in its total operating income compared to Q2 09. This has resulted mainly from the 17.8% decline in non-special commission income. However, the net-special commission income remained broadly unchanged helped by the wider spreads despite the decline in the size of interest earning assets.

- Based on our calculations, we estimate credit provisioning at SAR 155 million, dropping by 30% Q-o-Q but rising by more than 27 times Y-o-Y. We believe this high level of provisioning is resulting from a probably high exposure to Al Gosaibi and Al Saad Group coupled with the fact that the bank was under-provisioned relative to its peers at the end of 2008 when the bank reported an NPL coverage ratio of 110% and an NPL ratio of 2.73%.

PERFORMANCE INDICATORS

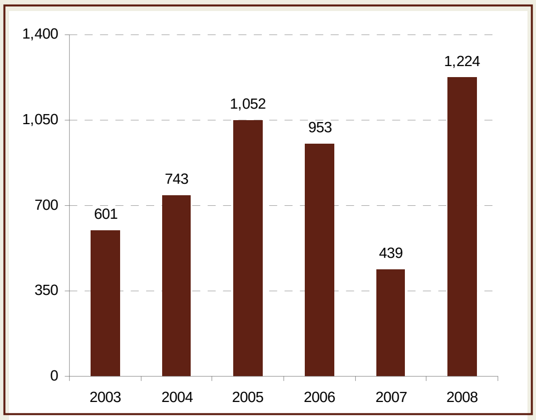
Stock Price (SAR)

Provision for Credit Losses (SAR million)

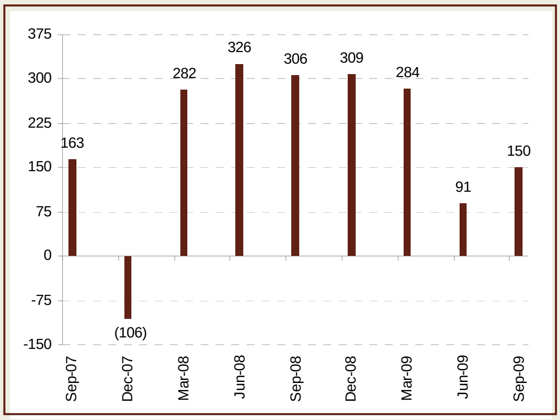


** Audi Capital Estimates*

Yearly Earnings (SAR million)



Quarterly Earnings (SAR million)



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