# AL RAJHI BANKING AND INVESTMENT CORPORATION

## CONSOLIDATED FINANCIAL STATEMENTS
## FOR THE YEAR ENDED DECEMBER 31, 2011
## TOGETHER WITH AUDITORS' REPORT

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# INDEPENDENT AUDITORS' REPORT

**TO: THE SHAREHOLDERS OF
AL RAJHI BANKING AND INVESTMENT CORPORATION
(A Saudi Joint Stock Company)**

We have audited the accompanying consolidated financial statements of Al Rajhi Banking and Investment Corporation (the "Bank") and its subsidiaries (collectively referred to as "the Group"), which comprise the consolidated statement of financial position as at 31 December 2011, 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 the other explanatory notes from (1) to (36). We have not audited note (37), nor the information related to "Basel II-Pillar 3 disclosures" cross-referenced therein, which is not required to be within the scope of our audit.

## Management 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"), International Financial Reporting Standards, the provisions of the Regulations for Companies, the Banking Control Law in the Kingdom of Saudi Arabia and the Bank's By-Laws. This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation 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

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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.

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 financial position of the Group as at 31 December 2011, and of its financial performance and its cash flows for the year then ended in accordance with Accounting Standards for Financial Institutions in the Kingdom of Saudi Arabia issued by the SAMA and with International Financial Reporting Standards; and

- comply with the requirements of the Regulations for Companies, the Banking Control Law in the Kingdom of Saudi Arabia and the Bank's Articles of Association and By-Laws in so far as they affect the preparation and presentation of the consolidated financial statements.

**PricewaterhouseCoopers**

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19 Rabee, 1433H
(11 February, 2012)

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ترخيص مهني رقم ٤٥
PROFESSIONAL LICENCE No. 45
ERNST & YOUNG

**AL RAJHI BANKING AND INVESTMENT CORPORATION**

**CONSOLIDATED STATEMENT OF FINANCIAL POSITION**
**AS AT DECEMBER 31, 2011 AND 2010**
**(SR '000)**

| | Notes | **2011** | 2010 |
|---|---|---|---|
| **ASSETS** | | | |
| Cash and balances with Saudi Arabian Monetary Agency ("SAMA") | 4 | **20,419,467** | 19,475,196 |
| Due from banks and other financial institutions | 5 | **14,599,787** | 11,117,539 |
| Financing, net | 6 | **140,395,619** | 120,064,667 |
| Investments | 7 | **38,802,492** | 28,246,882 |
| Customer debit current accounts, net | 8 | **375,941** | 312,062 |
| Property and equipment, net | 9 | **3,623,522** | 3,394,863 |
| Other assets, net | 10 | **2,596,584** | 2,229,701 |
| **TOTAL ASSETS** | | **220,813,412** | 184,840,910 |
| **LIABILITIES AND SHAREHOLDERS' EQUITY** | | | |
| **LIABILITIES** | | | |
| Due to banks and other financial institutions | 11 | **7,020,781** | 5,414,181 |
| Customer deposits | 12 | **173,429,465** | 143,064,037 |
| Other liabilities | 13 | **7,542,109** | 6,044,903 |
| **TOTAL LIABILITIES** | | **187,992,355** | 154,523,121 |
| **SHAREHOLDERS' EQUITY** | | | |
| Share capital | 14 | **15,000,000** | 15,000,000 |
| Statutory reserve | 15 | **13,956,451** | 12,111,884 |
| Retained earnings | | **114,606** | 205,905 |
| Proposed gross dividends and zakat | 22 | **3,750,000** | 3,000,000 |
| **TOTAL SHAREHOLDERS' EQUITY** | | **32,821,057** | 30,317,789 |
| **TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY** | | **220,813,412** | 184,840,910 |

The accompanying notes from 1 to 37 form an integral part of these consolidated financial statements.

## AL RAJHI BANKING AND INVESTMENT CORPORATION

**CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME**
**FOR THE YEARS ENDED DECEMBER 31, 2011 AND 2010**
**(SR '000)**

| | Notes | 2011 | 2010 |
|---|---|---|---|
| **INCOME:** | | | |
| Gross financing and investments income | | **9,324,397** | 9,352,765 |
| Income paid to customers on time investments | | **(254,454)** | (230,348) |
| **Net financing and investments income** | 17 | **9,069,943** | 9,122,417 |
| Fee from banking services, net | 18 | **2,298,394** | 1,634,384 |
| Exchange income, net | | **798,835** | 636,672 |
| Other operating income | 19 | **334,947** | 267,659 |
| **Total operating income** | | **12,502,119** | 11,661,132 |
| **EXPENSES:** | | | |
| Salaries and employee related benefits | 20 | **1,960,856** | 1,731,529 |
| Rent and premises related expenses | | **174,007** | 154,686 |
| Impairment charge for financing and other | 6-2 | **1,645,142** | 1,908,818 |
| Other general and administrative expenses | | **932,947** | 742,941 |
| Depreciation and amortization | | **407,815** | 349,239 |
| Board of directors' remuneration | 28 | **3,084** | 3,090 |
| **Total operating expenses** | | **5,123,851** | 4,890,303 |
| **Net income** | | **7,378,268** | 6,770,829 |
| **Comprehensive income** | | **-** | - |
| **NET COMPREHENSIVE INCOME** | | **7,378,268** | 6,770,829 |
| Weighted average number of shares outstanding | 14 & 21 | **1,500 million** | 1,500 million |
| **EARNINGS PER SHARE (IN SR)** | 21 | **4.92** | 4.51 |

The accompanying notes from 1 to 37 form an integral part of these consolidated financial statements.

**AL RAJHI BANKING AND INVESTMENT CORPORATION**

**CONSOLIDATED STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY**
**FOR THE YEARS ENDED DECEMBER 31, 2011 AND 2010**
**(SR '000)**

| | Notes | Share capital | Statutory reserve | General reserve | Retained earnings | Proposed gross dividends | Total |
|---|---|---|---|---|---|---|---|
| **2011** | | | | | | | |
| **Balance at January 1, 2011** | | **15,000,000** | **12,111,884** | **-** | **205,905** | **3,000,000** | **30,317,789** |
| Dividends paid for prior year | | **-** | **-** | **-** | **-** | **(2,250,000)** | **(2,250,000)** |
| Transfer to general reserve | 15 | **-** | **-** | **-** | **-** | **-** | **-** |
| Net comprehensive income | | **-** | **-** | **-** | **7,378,268** | **-** | **7,378,268** |
| Transfer to statutory reserve | | **-** | **1,844,567** | **-** | **(1,844,567)** | **-** | **-** |
| Interim dividends paid for the first half of the current year | 22 | **-** | **-** | **-** | **(1,875,000)** | **-** | **(1,875,000)** |
| Proposed gross dividends and zakat | 15&22 | **-** | **-** | **-** | **(3,750,000)** | **3,750,000** | **-** |
| Transfer to accrued zakat | 22 | **-** | **-** | **-** | **-** | **(750,000)** | **(750,000)** |
| **Balance at December 31, 2011** | | **15,000,000** | **13,956,451** | **-** | **114,606** | **3,750,000** | **32,821,057** |
| **2010** | | | | | | | |
| **Balance at January 1, 2010** | | 15,000,000 | 10,419,177 | - | 744,248 | 2,577,459 | 28,740,884 |
| Dividends paid for prior year | | - | - | - | - | (2,250,000) | (2,250,000) |
| Transfer to general reserve | 15 | - | - | 366,465 | (366,465) | - | - |
| Net comprehensive income | | - | - | - | 6,770,829 | - | 6,770,829 |
| Transfer to statutory reserve | | - | 1,692,707 | - | (1,692,707) | - | - |
| Interim dividends paid for the first half of the current year | 22 | - | - | - | (2,250,000) | - | (2,250,000) |
| Proposed gross dividends and zakat | 15&22 | - | - | - | (3,000,000) | 3,000,000 | - |
| Transfer to accrued zakat | 22 | - | - | (366,465) | - | (327,459) | (693,924) |
| **Balance at December 31, 2010** | | 15,000,000 | 12,111,884 | - | 205,905 | 3,000,000 | 30,317,789 |

The accompanying notes from 1 to 37 form an integral part of these consolidated financial statements.

AL RAJHI BANKING AND INVESTMENT CORPORATION

**CONSOLIDATED STATEMENT OF CASH FLOWS**
**FOR THE YEARS ENDED DECEMBER 31, 2011 AND 2010**
**(SR '000)**

| | **2011** | 2010 |
|---|---|---|
| **CASH FLOWS FROM OPERATING ACTIVITIES:** | | |
| Net income | **7,378,268** | 6,770,829 |
| **Adjustments to reconcile net income to net cash provided by operating activities:** | | |
| Depreciation and amortization | **407,815** | 349,239 |
| (Gain) loss on disposal of property and equipment | **(6,444)** | 3,874 |
| Impairment charge for financing and other | **1,645,142** | 1,908,818 |
| **Net (increase) decrease in operating assets:** | | |
| Statutory deposit with SAMA (Note 4) | **(1,317,189)** | (1,397,697) |
| Due from banks and other financial institutions | **(4,711,939)** | (1,006,783) |
| Financing | **(21,925,999)** | (9,825,826) |
| Investments held as FVIS | **(659,262)** | (400,618) |
| Customer debit current accounts | **(83,879)** | 383,729 |
| Other assets | **(366,882)** | 228,145 |
| **Net increase (decrease) in operating liabilities:** | | |
| Due to banks and other financial institutions | **1,606,600** | (687,892) |
| Customer deposits | **30,365,428** | 20,202,197 |
| Other liabilities | **747,206** | (7,673,953) |
| **Net cash provided by operating activities** | **13,078,865** | 8,854,062 |
| | | |
| **CASH FLOWS FROM INVESTING ACTIVITIES:** | | |
| Purchase of property and equipment | **(643,196)** | (572,948) |
| Investments recorded at amortized cost | **(9,926,444)** | (1,347,768) |
| Proceeds from disposal of property and equipment | **13,166** | 7,129 |
| **Net cash used in investing activities** | **(10,556,474)** | (1,913,587) |
| | | |
| **CASH FLOWS FROM FINANCING ACTIVITIES:** | | |
| Dividends paid | **(4,125,000)** | (4,500,000) |
| **Net cash used in financing activities** | **(4,125,000)** | (4,500,000) |
| | | |
| **NET (DECREASE) INCREASE IN CASH AND CASH EQUIVALENTS** | **(1,602,609)** | 2,440,475 |
| | | |
| Cash and cash equivalents at the beginning of year | **20,224,680** | 17,784,205 |
| | | |
| **CASH AND CASH EQUIVALENTS AT THE END OF YEAR (Note 23)** | **18,622,071** | 20,224,680 |

The accompanying notes from 1 to 37 form an integral part of these consolidated financial statements.

## 1. GENERAL

### a) Incorporation and operation

Al Rajhi Banking and Investment Corporation, a Saudi Joint Stock Company, (the "Bank"), was formed and licensed pursuant to Royal Decree No. M/59 dated 3 Dhul Qadah 1407H (corresponding to June 29, 1987) and in accordance with Article 6 of the Council of Ministers' Resolution No. 245, dated 26 Shawal 1407H (corresponding to June 23, 1987).

The Bank operates under Commercial Registration No. 1010000096 and its Head Office is located at the following address:

**Al Rajhi Bank**
**Olaya Street**
**P.O. Box 28**
**Riyadh 11411**
**Kingdom of Saudi Arabia**

The objectives of the Bank are to carry out banking and investment activities in accordance with its Articles of Association and By-Laws, the Banking Control Law and the Council of Ministers' Resolution referred to above. The Bank is engaged in banking and investment activities for its own account and on behalf of others inside and outside the Kingdom of Saudi Arabia through 496 branches including the branches outside the kingdom as at December 31, 2011 (2010: 487 branches) and 9,282 employees as at December 31, 2011 (2010: 8,527 employees). The Bank has established a number of wholly or substantially owned subsidiaries as set out below:

| SUBSIDIARIES | Shareholding % | |
|---|---|---|
| | **2011** | 2010 |
| Al Rajhi Company for Development Limited - Riyadh | **100%** | 99% |
| Al Rajhi Corporation Limited-Malaysia | **100%** | 100% |
| Al Rajhi Capital Company | **99%** | 99% |
| Al Rajhi Bank - Kuwait | **100%** | 100% |
| Al Rajhi Bank – Jordan | **100%** | - |
| Al Rajhi Takaful Agency Company | **99%** | - |

Al Rajhi Bank - Jordan and Al Rajhi Takful Agency Company were formed during the year ended December 31, 2011. All the above-mentioned subsidiaries were consolidated.

### b) Shari'a Authority

As a commitment from the Bank for its activities to be in compliance with Islamic Shari'a legislations, the Bank has, since inception, established a Shari'a Authority to ascertain that the Bank's activities are subject to its approval and control. The Shari'a Authority had reviewed several of the Bank's activities and issued the required decisions thereon.

## 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”). The Bank also prepares its consolidated financial statements to comply with the requirements of Banking Control Law and the provision of Regulations of Companies in the Kingdom of Saudi Arabia and the Bank’s articles of association.

### b) Basis of measurement

The consolidated financial statements are prepared under the historical cost convention as modified for the measurement at fair value of investments held as fair value through income statement (“FVIS”).

### c) Functional and presentation currency

The consolidated financial statements are presented in Saudi Riyal (“SR”), the Bank’s functional currency and are rounded off to the nearest thousand.

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

The preparation of consolidated financial statements in conformity with IFRS requires the use of certain critical accounting estimates and assumptions that affect the reported amounts of assets and liabilities. It also requires management to exercise its judgments in the process of applying the Bank’s accounting policies. Such estimates, assumptions and judgments are continually evaluated and are based on historical experience and other factors, including obtaining professional advice and expectations of future events that are believed to be reasonable under the circumstances. Significant areas where management has used estimates, assumptions or exercised judgements is as follows:

**1. Impairment for credit losses on financing**

The Bank reviews its financing 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 clients in a group. Management uses estimates based on historical loss experience for financing 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.

**2. Fair value of unquoted financial instruments**

The fair values of financial instruments that are not quoted in active markets are determined by using valuation techniques. Where valuation techniques (for example, models) are used to determine fair values, they are validated and periodically reviewed by qualified personnel independent of the area that created them. Models are calibrated to ensure that outputs reflect actual data and comparative market prices. To the extent practical, models use only observable market data, however areas such as credit risk (both own and counter party), volatilities and correlations require management to make estimates. The judgments include considerations of liquidity and model inputs such as volatility for longer dated derivatives and discount rates, prepayment rates and default rate assumptions for asset backed securities. Changes in assumptions about these factors could affect reported fair value of financial instruments.

3. **Going concern**

The Bank's management has made an assessment of the Bank's ability to continue as a going concern and is satisfied that the Bank has the resources to continue in business for the foreseeable future. Furthermore, the management is not aware of any material uncertainties that may cast significant doubt upon the Bank's ability to continue as a going concern. Therefore, the financial statements continue to be prepared on the going concern basis.

## 3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The significant accounting policies used in preparing these consolidated financial statements are set out below. The accounting policies used in preparation of these consolidated financial statements are consistent with those used in the consolidated financial statements for the year ended December 31, 2010, except for the adoption of following amendments and revisions to existing standards mentioned below which has had no financial impact on the consolidated financial statements of the Bank:

- IAS 24 Related Party Disclosures
- Amendments to IFRIC 14 IAS 19
- Improvements to IFRSs 2010 - IFRS 7 Financial Instruments Disclosures
- Improvements to IFRSs 2010 - IAS 1 Presentation of Financial Statements

### a) Basis of the preparation of the consolidated financial statements

These consolidated financial statements include the accounts of Al Rajhi Bank and its subsidiaries (the "Group") in which the Bank's shareholdings exceed 50% of their share capital and the Bank has the power to govern their financial and operational policies. The financial statements of subsidiaries are prepared for the same reporting year as that of the Bank, using consistent accounting policies.

Subsidiaries are all entities over which the Bank has the power to govern the financial and operating policies, so as to obtain benefits from its activities, generally accompanying a shareholding of more than one half of the voting rights. Subsidiaries are consolidated from the date on which control is transferred to the Bank and cease to be consolidated from the date on which the control is transferred from the Bank. The results of subsidiaries acquired or disposed of during the year, if any, are included in the consolidated statement of comprehensive income statement from the date of the acquisition or up to the date of disposal, as appropriate.

Inter-group balances and any income and expenses arising from intra-group transactions, are eliminated in preparing these consolidated financial statements. Unrealised losses are eliminated in the same way as unrealised gains, but only to the extent that there is no evidence of impairment. As of December 31, 2011 and 2010 interests in subsidiaries not directly owned by the Bank are owned by representative shareholders for the beneficial interest of the Bank and hence are not separately disclosed on the consolidated statement of financial position or statement of comprehensive income.

### b) Zakat

Zakat is calculated based on the zakat rules and regulations in the Kingdom of Saudi Arabia and is considered as a liability on the shareholders to be deducted from dividends. Zakat is computed based on equity or net income using the basis defined under the zakat regulations. In case of any differences between the Bank's calculation and the Department of Zakat and Income Tax's ("DZIT") assessment, such differences will be charged to the general reserve.

**c) Trade date**

All regular purchases and sales of financial assets are recognized and derecognized on the trade date (i.e. the date that the Bank commits to purchase or sell the assets). Regular way purchases or sales of financial assets require delivery of those assets within the time frame generally established by regulation or convention in the market place.

**d) Foreign currencies**

Transactions in foreign currencies are translated into Saudi Riyals at exchange rates prevailing on the dates of the transactions. Monetary assets and liabilities at the year-end, denominated in foreign currencies, are translated into Saudi Riyals at exchange rates prevailing at the date of the consolidated statement of financial position.

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

The monetary assets and liabilities of foreign subsidiaries are translated at rates of exchange prevailing at the date of the consolidated statement of financial position. The statements of income of foreign subsidiaries are translated at the average exchange rates for the year.

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

Exchange differences arising on translation are taken directly to a separate component of equity (if material). On disposal of a foreign entity, the deferred cumulative amount recognised in equity relating to that particular foreign operation is recognised in the income statement in 'Other operating expenses' or 'Other operating income'.

**e) Offsetting financial instruments**

Financial assets and liabilities are offset and are reported net in the consolidated statement of financial position when there is a legally enforceable right to set off the recognized amounts, and when the Bank intends to settle on a net basis, or to realize the asset and settle the liability simultaneously.

**f) Revenue recognition**

- Income from Mutajara, Murabaha, investments held at amortized costs, installment sale, Istisnaa financing and visa services is recognized based on effective yield basis on the outstanding balances.

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

- Dividend income is recognised when the right to receive income is established.

- Exchange income / loss is recognized when earned / incurred.

**g) Financing and investment**

The Bank offers non-interest based products including Mutajara, installment sales, Murabaha and Istisna'a to its customers in compliance with Shari'a rules.

The Bank classifies its principal financing and investment as follows:

i. Held at amortized cost - such financing and certain investments which meets the definition of loans and receivable under IAS 39, are measured at amortized cost, and comprise Mutajara, installment sale, Istisnaa, Murabaha and visa operations accounts balances.

ii. Held as FVIS - Investments in this category are classified as either investment held for trading or those designated as FVIS on initial recognition. These investments comprise of mutual funds, and other investments. Such investments are measured at fair value and any change in the fair value is charged to the consolidated statement of comprehensive income.
Financing held at amortized cost are initially recognized at fair value and subsequently measured at amortized cost less any amounts written off, and provision for impairment.

**h) Impairment of financial assets**

An assessment is made at the date of each consolidated statement of financial position to determine whether there is objective evidence that a financial asset or a group of financial assets may be impaired. If such evidence exists, the difference between the assets carrying amount and the present value of estimated future cash flows is calculated and any impairment loss, is recognized for changes in the asset's carrying amount. The carrying amount of the financial assets held at amortized cost, is adjusted either directly or through the use of a provision account, and the amount of the adjustment is included in the consolidated statement of comprehensive income.

Specific provisions are evaluated individually. Considerable judgment by management is required in the estimation of the amount and timing of future cash flows when determining the level of provision required. Such estimates are essentially based on assumptions about several factors involving varying degrees of judgment and uncertainty, and actual results may differ resulting in future changes to such provisions. In addition to the specific provisions described above, the Bank also makes collective impairment provisions, which are evaluated on a group basis and are created for losses, where there is objective evidence that unidentified losses exist at the reporting date. The amount of the provision is estimated based on the historical default patterns of the investment and financing counter-parties as well as their credit ratings, taking into account the current economic climate.

The criteria that the Bank uses to determine that there is objective evidence of an impairment loss include:

- Delinquency in contractual payments of principal or profit.
- Cash flow difficulties experienced by the customer.
- Breach of repayment covenants or conditions.
- Initiation of bankruptcy proceedings against the customer.
- Deterioration of the customer's competitive position.
- Deterioration in the value of collateral.

When financing amount is uncollectible, it is written-off against the related provision for impairment. Such financing is written-off after all necessary procedures have been completed and the amount of the loss has been determined.

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 recognized (such as an improvement in the customer's credit rating), the previously recognized impairment loss is reversed by adjusting the provision account. The amount of the reversal is recognized in the statement of comprehensive income in impairment charge.

Financial assets are written off only in circumstances where effectively all possible means of recovery have been exhausted.

**i) De-recognition of financial assets and liabilities**

A financial asset is derecognized when the contractual rights to the cash flows from the financial asset expire or if the Bank has not retained control on the financial asset.

A financial liability can be only derecognized when it is extinguished, that is when the obligation specified in the contract is either discharged, cancelled or expires.

**j) Customer debit current accounts**

All non-commission bearing customer debit current accounts are stated at amortized cost, less doubtful amounts and provision for impairment, if any.

**k) Property and equipment**

Property and equipment are stated at cost, net of accumulated depreciation and amortization. Land is not depreciated. The cost of other property and equipment is depreciated or amortized using the straight-line method over the estimated useful lives of the assets, as follows:

| | |
|---|---|
| Leasehold land improvements | over the period of the lease |
| Buildings | 33 years |
| Leasehold building improvements | 3 years |
| Equipment and furniture | 3 to 10 years. |

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at each statement of financial position date.

Gains and losses on disposals are determined by comparing proceeds with carrying amount. These are included in consolidated statement of comprehensive income.

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.

**l) Customer deposits**

Non-commission bearing customer deposits are initially recognized at fair value, being the fair value of the consideration received, and are subsequently measured at amortized cost.

**m) Guarantees**

In the ordinary course of business the Bank gives guarantees which include letters of credit, letters of guarantee and acceptances. Initially, the received margins are recognized as liabilities and included in customers' deposits in the consolidated financial statements. The Bank's obligation towards each guarantee is measured through the higher of amortized margin or best estimate for the required payments to meet the financial commitments resulted from the guarantees. Any increase in the financial commitments related to the guarantees is recognized in the consolidated statement of comprehensive income.

**n) Provisions**

Provisions are recognized when the Bank has present legal, or constructive obligation as a result of past events, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation, and a reliable estimate of the amount of the obligation can be made.

**o) Accounting for leases**

Leases entered into by the Bank as a lessee are all operating leases. Accordingly, payments are charged to the consolidated statement of comprehensive income on straight-line basis over the period of the lease. Leases entered into by the Bank as a lessor are all operating leases.

**p) Cash and cash equivalents**

For the purposes of the consolidated statement of cash flows preparation, cash and cash equivalents are defined as those amounts included in cash and balances with SAMA (excluding the statutory deposit) and due from banks maturing within ninety days on acquisition.

**q) Special commission excluded from the consolidated statement of comprehensive income**

In accordance with the Shari'a Authority's resolutions, special commission income received by the Bank is excluded from the determination of income, and is recorded as other liabilities in the consolidated statement of financial position and is paid as charities.

**r) Provisions for employees' end of service benefits**

The provision for employees' end of service benefits is calculated through actuarial basis according to the regulations of Saudi labor law and local regulatory requirements.

**s) Mudaraba funds**

The Group carries out Mudaraba transactions on behalf of its customers, and are treated by the Group as being restricted investments. These are included as off balance sheet items. The Group's share of profits from managing such funds is included in the Group's consolidated statement of comprehensive income.

### t) Investment management services

The Group provides investment management services to its customers, through its subsidiary which include management of certain mutual funds. Assets held in trust or in a fiduciary capacity are not treated as assets of the Group and, accordingly, are not included in the Group's consolidated financial statements. The Group's share of these funds is included under FVIS investments. Fees earned are disclosed under consolidated statement of comprehensive income.

### u) Bank's products definition

The Bank provides its customers with banking products based on interest avoidance concept and in accordance with Shari'a regulations. The following is a description of some of the financing products:

Mutajara financing:
It is financing agreement whereby the Bank purchases a commodity or an asset and sell it to the client based on a purchase promise from the client with a deferred price higher than the cash price, accordingly the client becomes debtor to the Bank with the sale amount and for the period agreed on in the contract.

Installment sales financing:
It is financing agreement whereby the Bank purchases a commodity or an asset and sell it to the client based on a purchase promise from the client with a deferred price higher than the cash price, accordingly the client becomes debtor to the Bank with the sale amount to be paid through installments as agreed in the contract.

Istisnaa financing:
It is a financing agreement whereby the Bank contracts to manufacture a commodity with certain specifications according to the client's request. The client become debtor to the Bank with the manufacturing price of which includes cost plus profit.

Murabaha financing:
It is a financing agreement whereby the Bank purchases a commodity or asset and sell it to the client with a price representing the purchase price plus a profit known and agreed by the client which means that he should be aware of the cost and profit separately.

## 4. CASH AND BALANCES WITH SAMA

Cash and balances with SAMA as of December 31 comprise the following:

| | (SR'000) | |
|---|---|---|
| | **2011** | 2010 |
| Cash in hand | **6,186,518** | 5,329,888 |
| Statutory deposit | **10,678,461** | 9,361,272 |
| Current accounts | **3,554,488** | 4,784,036 |
| **Total** | **20,419,467** | 19,475,196 |

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 customer deposits, customers' time investment and other customers' account calculated at the end of each Gregorian month. The statutory deposit with SAMA is not available to finance the Bank's day-to-day operations and therefore are not part of cash and cash equivalents.

## 5. DUE FROM BANKS AND OTHER FINANCIAL INSTITUTIONS

Due from banks and other financial institutions as of December 31, comprise the following:

| | (SR'000) | |
|---|---|---|
| | **2011** | 2010 |
| Current accounts | **1,285,458** | 1,440,118 |
| Mutajara | **13,314,329** | 9,677,421 |
| **Total** | **14,599,787** | 11,117,539 |

The above due from banks and other financial institutions balance does not include any past due or impaired balances as of December 31, 2011 and 2010.

## 6. FINANCING, NET

### 6 - 1 Financing

**a)** Net financing as of December 31, comprise the following:

| | (SR'000) | | | |
|---|---|---|---|---|
| | **2011** | | | 2010 |
| | **Gross** | **Provision** | **Net** | Net |
| **Financing held at amortized cost** | | | | |
| Corporate Mutajara | 31,441,547 | (1,332,841) | 30,108,706 | 29,614,767 |
| Installment sale | 99,662,914 | (1,444,782) | 98,218,132 | 76,959,797 |
| Murabaha | 12,289,833 | (756,858) | 11,532,975 | 12,326,844 |
| Visa cards | 556,400 | (21,151) | 535,249 | 686,362 |
| Istisnaa | 557 | - | 557 | 476,897 |
| **Total** | **143,951,251** | **(3,555,632)** | **140,395,619** | **120,064,667** |

**b)** The net financing by location, inside and outside the Kingdom, as of December 31 are as follows:

| | (SR'000) | | | | | | |
|---|---|---|---|---|---|---|---|
| | **2011** | | | | | | 2010 |
| **Description** | **Corporate Mutajara** | **Installment sale** | **Murabaha** | **Visa** | **Istisnaa** | **Total** | Total |
| Inside the Kingdom | 31,441,547 | 99,524,825 | 7,674,994 | 551,951 | 557 | 139,193,874 | 116,332,455 |
| Outside the Kingdom | - | 138,089 | 4,614,839 | 4,449 | - | 4,757,377 | 7,348,285 |
| **Total** | 31,441,547 | 99,662,914 | 12,289,833 | 556,400 | 557 | 143,951,251 | 123,680,740 |
| Provision | (1,332,841) | (1,444,782) | (756,858) | (21,151) | - | (3,555,632) | (3,616,073) |
| **Net** | **30,108,706** | **98,218,132** | **11,532,975** | **535,249** | **557** | **140,395,619** | **120,064,667** |

**c)** The net financing concentration risks and the related provision, by major economic sectors at December 31, are as follows:

| **2011** | **(SR'000)** | | | |
|---|---|---|---|---|
| **Description** | **Performing** | **Non-Performing** | **Provision** | **Net financing** |
| Commercial | 20,260,970 | 790,883 | (710,377) | 20,341,476 |
| Industrial | 10,525,218 | - | - | 10,525,218 |
| Building and construction | 14,336,863 | 967,550 | (819,446) | 14,484,967 |
| Personal | 84,968,642 | 637,521 | (279,023) | 85,327,140 |
| Services | 8,551,611 | - | - | 8,551,611 |
| Agriculture and fishing | 109,589 | - | - | 109,589 |
| Other | 2,802,404 | - | - | 2,802,404 |
| **Total** | 141,555,297 | 2,395,954 | (1,808,846) | 142,142,405 |
| Additional portfolio provision | | | (1,746,786) | (1,746,786) |
| **Balance** | | | (3,555,632) | 140,395,619 |

| **2010** | **(SR'000)** | | | |
|---|---|---|---|---|
| **Description** | **Performing** | **Non-Performing** | **Provision** | **Net financing** |
| Commercial | 22,391,211 | 1,904,211 | (802,984) | 23,492,438 |
| Industrial | 7,974,369 | - | - | 7,974,369 |
| Building and construction | 12,151,974 | 41,438 | (15,249) | 12,178,163 |
| Personal | 65,060,527 | 716,521 | (249,728) | 65,527,320 |
| Public (Government) | 512,606 | - | - | 512,606 |
| Services | 9,809,206 | - | - | 9,809,206 |
| Agriculture and fishing | 1,674,734 | - | - | 1,674,734 |
| Other | 1,443,943 | - | - | 1,443,943 |
| **Total** | 121,018,570 | 2,662,170 | (1,067,961) | 122,612,779 |
| Additional portfolio provision | | | (2,548,112) | (2,548,112) |
| **Balance** | | | (3,616,073) | 120,064,667 |

**d)** The table below depicts the categories of financing as shown in the statement of financial position as per main business segments at December 31:

| **2011** | **(SR'000)** | | |
|---|---|---|---|
| | **Retail** | **Corporate** | **Total** |
| Corporate Mutajara | - | 31,441,547 | 31,441,547 |
| Installment sale | 92,087,304 | 7,575,610 | 99,662,914 |
| Murabaha | 2,861,348 | 9,428,485 | 12,289,833 |
| Visa | 556,400 | - | 556,400 |
| Istisnaa | - | 557 | 557 |
| **Total** | **95,505,052** | **48,446,199** | **143,951,251** |
| Less: Provision | (2,198,216) | (1,357,416) | (3,555,632) |
| **Financing, net** | **93,306,836** | **47,088,783** | **140,395,619** |

| **2010** | (SR'000) | | |
|---|---|---|---|
| | **Retail** | **Corporate** | **Total** |
| Corporate Mutajara | - | 31,157,077 | 31,157,077 |
| Installment sale | 71,260,471 | 7,028,572 | 78,289,043 |
| Murabaha | 3,054,799 | 10,015,048 | 13,069,847 |
| Visa | 687,876 | - | 687,876 |
| Istisnaa | - | 476,897 | 476,897 |
| Total | 75,003,146 | 48,677,594 | 123,680,740 |
| Less: Provision | (2,049,188) | (1,566,885) | (3,616,073) |
| Financing, net | 72,953,958 | 47,110,709 | 120,064,667 |

**e)** The table below summarizes financing balances at December 31, that are neither past due nor impaired, past due but not impaired and impaired, as per the main business segments of the Bank:

| **2011** | (SR'000) | | | | | |
|---|---|---|---|---|---|---|
| | **Neither past due nor impaired** | **Past due but not impaired** | **Impaired** | **Total** | **Provision** | **Net** |
| Retail | 93,815,890 | 446,047 | 1,243,115 | 95,505,052 | (2,198,216) | 93,306,836 |
| Corporate | 46,899,025 | 394,335 | 1,152,839 | 48,446,199 | (1,357,416) | 47,088,783 |
| **Total** | **140,714,915** | **840,382** | **2,395,954** | **143,951,251** | **(3,555,632)** | **140,395,619** |

| **2010** | (SR'000) | | | | | |
|---|---|---|---|---|---|---|
| | **Neither past due nor impaired** | **Past due but not impaired** | **Impaired** | **Total** | **Provision** | **Net** |
| Retail | 73,602,616 | 145,098 | 1,255,432 | 75,003,146 | (2,049,188) | 72,953,958 |
| Corporate | 46,626,818 | 644,038 | 1,406,738 | 48,677,594 | (1,566,885) | 47,110,709 |
| Total | 120,229,434 | 789,136 | 2,662,170 | 123,680,740 | (3,616,073) | 120,064,667 |

Financing past due for less than 90 days are not treated as impaired, unless other available information proves otherwise.

Neither past due nor impaired and past due but not impaired comprise the total performing financing.

**f)** The tables below depict the quality of financing past due (up to 90 days) but not impaired at December 31:

| **2011** | (SR'000) | | |
|---|---|---|---|
| | **Retail** | **Corporate** | **Total** |
| Standard | 415,186 | 283,857 | 699,043 |
| Special mention | 30,861 | 110,478 | 141,339 |
| **Total** | **446,047** | **394,335** | **840,382** |

| 2010 | (SR'000) | | |
|---|---|---|---|
| | Retail | Corporate | Total |
| Standard | 130,741 | 640,911 | 771,652 |
| Special mention | 14,357 | 3,127 | 17,484 |
| Total | 145,098 | 644,038 | 789,136 |

Financing under the standard category are performing, have sound fundamental characteristics and include those that exhibit neither actual nor potential weaknesses.

The special mention category includes financing that are also performing, current and up to date in terms of principal and profit payments. However, they require close management attention as they may have potential weaknesses both financial and non-financial that may, at some future date, result in the deterioration of the repayment prospects or either the principal or the profit payments. The special mention financing would not expose the Bank to sufficient risk to warrant a worse classification.

**g)** The tables below set out the aging of financing past due but not impaired as of December 31:

| **2011** | **(SR'000)** | | |
|---|---|---|---|
| **Age** | **Retail** | **Corporate** | **Total** |
| up to 30 days | 243,983 | 244,117 | 488,100 |
| 31-60 days | 171,203 | 39,740 | 210,943 |
| 61-90 days | 30,861 | 110,478 | 141,339 |
| **Total** | **446,047** | **394,335** | **840,382** |
| **Fair value of collateral** | **-** | **1,915,364** | **1,915,364** |

| 2010 | (SR'000) | | |
|---|---|---|---|
| Age | Retail | Corporate | Total |
| up to 30 days | 111,050 | 492,272 | 603,322 |
| 31-60 days | 19,691 | 148,639 | 168,330 |
| 61-90 days | 14,357 | 3,127 | 17,484 |
| Total | 145,098 | 644,038 | 789,136 |
| Fair value of collateral | - | 491,351 | 491,351 |

The fair value of collateral is based on valuation techniques and quoted prices (wherever available).

**h)** The table below sets out gross balances of individually impaired financing, together with the fair value of related collaterals held by the Bank as at December 31:

| **2011** | **(SR'000)** | | |
|---|---|---|---|
| | **Retail** | **Corporate** | **Total** |
| Individually impaired financing | - | 1,152,839 | **1,152,839** |
| Fair value of collateral | - | 1,302,217 | **1,302,217** |

| 2010 | (SR'000) | | |
|---|---|---|---|
| | Retail | Corporate | Total |
| Individually impaired financing | - | 1,406,738 | 1,406,738 |
| Fair value of collateral | - | 582,250 | 582,250 |

The Bank in the ordinary course of financing activities holds collaterals as security to mitigate credit risk in financing. These collaterals mostly include customer deposits and other cash deposits, financial guarantees, local and international equities, real estate and other property and equipment. The collaterals are held mainly against commercial and consumer financing and are managed against relevant exposures at their net realizable values.

**i)** The tables below depict the quality of neither past due nor impaired

| | **(SR'000)** | |
|---|---|---|
| | **2011** | 2010 |
| Risk Rating 1 | **-** | - |
| Risk Rating 2 | **-** | - |
| Risk Rating 3 | **10,437,056** | 9,283,000 |
| Risk Rating 4 | **44,980,424** | 36,062,000 |
| Risk Rating 5 | **57,459,210** | 47,563,000 |
| Risk Rating 6 | **20,850,663** | 20,066,000 |
| Risk Rating 7 | **6,987,562** | 7,255,434 |
| Total | **140,714,915** | 120,229,434 |

Risk Rating 1
Exceptional - Obligors of unquestioned credit standing at the pinnacle of credit quality.

Risk Rating 2
Excellent - Obligors of the highest quality, presently and prospectively. Virtually no risk in lending to this class. Cash flows reflect exceptionally large and stable margins of protection. Projected cash flows including anticipated credit extensions indicate strong liquidity levels and debt service coverage. Balance Sheet parameters are strong, with excellent asset quality in terms of value and liquidity.

Risk Rating 3
Superior - Typically obligors at the lower end of the high quality range with excellent prospects. Very good asset quality and liquidity. Consistently strong debt capacity and coverage. There could however be some elements, which with a low likelihood impair performance in the future.

Risk Rating 4
Good - Typically obligors in the high end of the medium range who are definitely sound with minor risk characteristics. Elements of strength are present in such areas as liquidity, stability of margins, cash flows, diversity of assets, and lack of dependence on one type of business.

Risk Rating 5

Satisfactory - These are obligors with smaller margins of debt service coverage and with some elements of reduced strength. Satisfactory asset quality, liquidity, and good debt capacity and coverage. A loss year or declining earnings trend may occur, but the borrowers have sufficient strength and financial flexibility to offset these issues.

Risk Rating 6

Adequate - Obligors with declining earnings, strained cash flow, increasing leverage and/or weakening market fundamentals that indicate above average risk. Such borrowers have limited additional debt capacity, modest coverage, average or below average asset quality and market share. Present borrower performance is satisfactory, but could be adversely affected by developing collateral quality/adequacy etc.

Risk Rating 7

Very high risk - Generally undesirable business constituting an undue and unwarranted credit risk but not to the point of justifying a substandard classification. No loss of principal or interest has taken place. Potential weakness might include a weakening financial condition, an unrealistic repayment program, inadequate sources of funds, or a lack of adequate collateral, credit information or documentation. The entity is undistinguished and mediocre. No new or incremental credits will generally be considered for this category.

**6 - 2 Impairment charge for financing:**

The movement in the impairment provision for financing for the years ended December 31, is as follows:

| **2011** | **(SR'000)** | | |
|---|---|---|---|
| | **Retail** | **Corporate** | **Total** |
| Balance at the beginning of the year | 2,049,188 | 1,566,885 | 3,616,073 |
| Provided during the year * | 970,045 | 645,002 | 1,615,047 |
| Disposals (bad debts written off) | (821,017) | (854,471) | (1,675,488) |
| **Balance at the end of the year** | **2,198,216** | **1,357,416** | **3,555,632** |

* The amount provided does not include SR 30,095 representing additions to investments provision.

| 2010 | (SR'000) | | |
|---|---|---|---|
| | Retail | Corporate | Total |
| Balance at the beginning of the year | 2,178,601 | 2,013,647 | 4,192,248 |
| Provided during the year | 705,116 | 1,203,702 | 1,908,818 |
| Disposals (bad debts written off) | (834,529) | (1,650,464) | (2,484,993) |
| Balance at the end of the year | 2,049,188 | 1,566,885 | 3,616,073 |

## 7. INVESTMENTS

Net investments comprise the following as of December 31:

| | (SR'000) | |
|---|---|---|
| Investments held at amortized costs | **2011** | 2010 |
| Murabaha with SAMA | **35,524,923** | 25,598,479 |
| **Total investments held at amortized costs** | **35,524,923** | 25,598,479 |
| Investments held as FVIS | | |
| Sukuk | **1,310,097** | 1,007,539 |
| Equity investments | **789,841** | 711,340 |
| Mutual funds | **482,975** | 400,537 |
| Sundry | **694,656** | 528,987 |
| **Total investments held as FVIS** | **3,277,569** | 2,648,403 |
| **Total investments** | **38,802,492** | 28,246,882 |

The designated FVIS investments included above are so designated when the financial instruments are being evaluated on a fair value basis and are in accordance with the documented risk management strategy of the Bank.

Equity investments include traded investments amounting to SR 766 million as of December 31, 2011 (2010: SR 688 million).

Investments do not include balances that are past due or impaired as of December 31, 2011.

The following is analysis of investment according to counterparties:

| | (SR'000) | |
|---|---|---|
| | **2011** | 2010 |
| Government and qausi government | **35,524,923** | 25,598,479 |
| Companies | **766,394** | 674,587 |
| Banks and other financial institutions | **23,447** | 36,753 |
| Others | **2,487,728** | 1,937,063 |
| **Total investments** | **38,802,492** | 28,246,882 |

## 8. CUSTOMER DEBIT CURRENT ACCOUNTS, NET

Customer debit current accounts, net comprise the following as of December 31:

| | (SR'000) | |
|---|---|---|
| | **2011** | 2010 |
| Customer debit current accounts (inside the kingdom) | **397,909** | 362,062 |
| Less: provision | **(21,968)** | (50,000) |
| **Customer debit current accounts, net** | **375,941** | 312,062 |

## 9. PROPERTY AND EQUIPMENT, NET

Property and equipment, net comprise the following as of December 31:

| | (SR'000) | | | | | |
|---|---|---|---|---|---|---|
| | Land | Buildings | Leasehold land & buildings improvements | Equipment and furniture | Total 2011 | Total 2010 |
| **COST** | | | | | | |
| **At January 1** | **1,348,080** | **1,287,152** | **575,892** | **2,012,708** | **5,223,832** | 4,919,362 |
| Additions | **134,682** | **98,448** | **119,387** | **290,679** | **643,196** | 572,948 |
| Disposals | **(6,430)** | **(850)** | **-** | **(6,531)** | **(13,811)** | (268,478) |
| **At December 31** | **1,476,332** | **1,384,750** | **695,279** | **2,296,856** | **5,853,217** | 5,223,832 |
| **ACCUMULATED DEPRECIATION & AMORTIZATION** | | | | | | |
| **At January 1** | **-** | **107,359** | **396,608** | **1,325,002** | **1,828,969** | 1,737,205 |
| Charge for the year | **-** | **35,957** | **119,426** | **252,432** | **407,815** | 349,239 |
| Disposals | **-** | **(850)** | **-** | **(6,239)** | **(7,089)** | (257,475) |
| **At December 31** | **-** | **142,466** | **516,034** | **1,571,195** | **2,229,695** | 1,828,969 |
| **NET BOOK VALUE** | | | | | | |
| **At December 31, 2011** | **1,476,332** | **1,242,284** | **179,245** | **725,661** | **3,623,522** | |
| At December 31, 2010 | 1,348,080 | 1,179,793 | 179,284 | 687,706 | | 3,394,863 |

Buildings include work-in-progress amounting to SR 102 million as at December 31, 2011 (2010: SR 195 million).

## 10. OTHER ASSETS, NET

Other assets, net comprise the following as of December 31:

| | (SR'000) 2011 | 2010 |
|---|---|---|
| Cheques under collection | **844,042** | 311,569 |
| Advances payments | **286,212** | 302,463 |
| Miscellaneous receivables | **922,821** | 834,892 |
| Prepaid expenses | **209,694** | 167,344 |
| Accrued income | **201,193** | 118,911 |
| Others | **152,588** | 514,488 |
| **Total** | **2,616,550** | 2,249,667 |
| Less: provision | **(19,966)** | (19,966) |
| **Other assets, net** | **2,596,584** | 2,229,701 |

## 11. DUE TO BANKS AND OTHER FINANCIAL INSTITUTIONS

Due to banks and other financial institutions comprise the following as of December 31:

| | (SR'000) | |
|---|---|---|
| | **2011** | 2010 |
| Current accounts | **4,565,842** | 3,273,606 |
| Banks' time investments | **2,454,939** | 2,140,575 |
| **Total** | **7,020,781** | 5,414,181 |

Due to banks by location, inside and outside the Kingdom, as of December 31, are as follows:

| | (SR'000) | |
|---|---|---|
| | **2011** | 2010 |
| Inside the Kingdom | **1,709,066** | 1,059,993 |
| Outside the Kingdom | **5,311,715** | 4,354,188 |
| **Total** | **7,020,781** | 5,414,181 |

## 12. CUSTOMER DEPOSITS

Customer deposits by currency comprise the following as of December 31:

| | (SR'000) | |
|---|---|---|
| | **2011** | 2010 |
| Saudi Riyals | **168,647,170** | 139,069,069 |
| Foreign currencies | **4,782,295** | 3,994,968 |
| **Total** | **173,429,465** | 143,064,037 |

Customer deposits by type comprise the following as of December 31:

| | (SR'000) | |
|---|---|---|
| | **2011** | 2010 |
| Demand deposits | **164,817,558** | 130,902,994 |
| Customer time investments | **5,726,461** | 9,527,096 |
| Other customer accounts | **2,885,446** | 2,633,947 |
| **Total** | **173,429,465** | 143,064,037 |

The balance of the other customer accounts includes margins on letters of credit and guarantees, checks under clearance and transfers.

## 13. OTHER LIABILITIES

Other liabilities comprise the following as of December 31:

| | (SR'000) | |
|---|---|---|
| | **2011** | 2010 |
| Accounts payable | **4,435,985** | 3,417,895 |
| Provision for employees' end of service benefits | **533,594** | 477,301 |
| Accrued expenses | **415,949** | 268,193 |
| Charities (see Note 30) | **20,308** | 4,923 |
| Other | **2,136,273** | 1,876,591 |
| **Total** | **7,542,109** | 6,044,903 |

## 14. SHARE CAPITAL

The authorized, issued and fully paid share capital of the Bank as of December 31, 2011 and 2010 consists of 1,500 million shares of SR 10 each.

## 15. STATUTORY AND GENERAL RESERVES

The Banking Control Law in Saudi Arabia and the By-Laws of the Bank require a transfer to statutory reserve at a minimum of 25% of net income for the year. The Bank may discontinue such transfers when the reserve equals the paid up share capital. This reserve is presently not available for distribution.

In addition, the Bank makes an appropriation to general reserve for general banking risks, zakat and others, if any.

At the General Assembly meeting held on 13 Rabie Awal 1431H (corresponding to February 27, 2010), the shareholders approved to transfer SR 366.5 million from the retained earnings to the general reserve. The Bank has utilized this amount to meet zakat commitment.

## 16. COMMITMENTS AND CONTINGENCIES

### a) Legal proceedings

As at December 31, 2011, there were certain legal proceedings outstanding against the Bank. Provisions have been made for some of these legal cases based on the assessment of the Bank's legal advisors.

### b) Capital commitments

As at December 31, 2011, the Bank had capital commitments of SR 116.8 million (2010: SR 119.7 million) relating to contracts for computer software update and development and SR 103.4 million (2010: SR 46 million) relating to development and improvement of branches.

### c) Credit related commitments and contingencies

The primary purpose of these instruments is to ensure that funds are available to customers as required. Credit related commitments and contingencies mainly comprise of letters of guarantee, standby letters of credit, acceptances and unused commitments to extend credit. Guarantees and standby letters of credit, which represent irrevocable assurances that the Bank will make payments in the event that a customer cannot meet his obligations to third parties, carry the same credit risk as financing.

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 collateralized by the underlying shipments of goods to which they relate, and therefore, carry less risk. Acceptances comprise undertakings by the Bank to pay bills of exchange drawn on customers.

Cash requirements under guarantees and letters of credit are considerably less than the amount of the commitment because the Bank does not expect the third party to draw funds under the agreement.

Commitments to extend credit represent unused portions of authorization to extended credit, principally in the form of financing, guarantees and letters of credit. With respect to credit risk relating to commitments to extend unused credit, the Bank is potentially exposed to a loss in an amount which is equal to the total unused commitments. The likely amount of loss, which cannot be reasonably estimated, is expected to be considerably less than the total unused commitments, since 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.

1. The contractual maturities of commitments and contingencies liabilities are as follows at December 31:

| **2011** | **(SR '000)** | | | | |
|---|---|---|---|---|---|
| | **Less than 3 months** | **From 3 to 12 months** | **From 1 to 5 years** | **Over 5 years** | **Total** |
| Letters of credit and acceptances | 1,070,883 | 711,273 | 176,670 | 1,838,933 | 3,797,759 |
| Letters of guarantee | 31,964 | 785,075 | 3,579,411 | 1,483,519 | 5,879,969 |
| Irrevocable commitments to extend credit | 181,402 | 1,488,601 | 3,067,746 | 968,670 | 5,706,419 |
| **Total** | **1,284,249** | **2,984,949** | **6,823,827** | **4,291,122** | **15,384,147** |

| 2010 | (SR '000) | | | | |
|---|---|---|---|---|---|
| | Less than 3 months | From 3 to 12 months | From 1 to 5 years | Over 5 years | Total |
| Letters of credit and acceptances | 3,978,724 | 609,319 | 45,687 | - | 4,633,730 |
| Letters of guarantee | 4,326,727 | 979,001 | 967,392 | 90,474 | 6,363,594 |
| Irrevocable commitments to extend credit | 1,424,075 | 1,502,051 | 2,162,094 | 2,079,649 | 7,167,869 |
| Total | 9,729,526 | 3,090,371 | 3,175,173 | 2,170,123 | 18,165,193 |

2. The analysis of commitments and contingencies by counter-party is as follows as at December 31:

| | (SR'000) | |
|---|---|---|
| | **2011** | 2010 |
| Corporate | **9,282,221** | 13,624,861 |
| Banks and other financial institutions | **6,101,926** | 4,540,332 |
| **Total** | **15,384,147** | 18,165,193 |

**d) Operating lease commitments**

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

| | (SR'000) | |
|---|---|---|
| | **2011** | 2010 |
| Less than one year | **22,548** | 21,845 |
| One year to five years | **102,442** | 86,399 |
| Over five years | **40,740** | 35,459 |
| **Total** | **165,730** | 143,703 |

## 17. NET FINANCING AND INVESTMENTS INCOME

Net financing and investments income for the years ended December 31, comprises the following:

| | (SR'000) | |
|---|---|---|
| | **2011** | 2010 |
| **Financing** | | |
| Corporate Mutajara | **1,317,524** | 1,619,716 |
| Installment sale | **6,942,975** | 6,714,292 |
| Murabaha | **660,758** | 691,929 |
| Istisnaa | **22,685** | 65,413 |
| **Investments and other** | | |
| Murabaha with SAMA | **201,067** | 141,829 |
| Murabaha with banks | **136,412** | 100,945 |
| Income from Sukuk | **42,976** | 18,641 |
| Gross financing and investment income | **9,324,397** | 9,352,765 |
| Income paid to customers on time investments | **(254,454)** | (230,348) |
| **Net financing and investments income** | **9,069,943** | 9,122,417 |

## 18. FEE FROM BANKING SERVICES, NET

Fees from banking services, net for the years ended December 31, comprise the following:

| | (SR'000) | |
|---|---|---|
| | **2011** | 2010 |
| **Fee income** | | |
| Fees from payment service systems | **469,312** | 387,903 |
| Fees from share trading services | **339,169** | 223,052 |
| Fees from remittance business | **311,470** | 273,646 |
| Fees from credit cards | **154,492** | 117,354 |
| Mudaraba fee income | **57,593** | 50,073 |
| Other | **1,611,807** | 1,076,404 |
| **Total fee income** | **2,943,843** | 2,128,432 |
| **Fee expenses** | | |
| Fees for payment service systems | **(557,134)** | (429,432) |
| Fees for share trading services | **(88,315)** | (64,616) |
| **Total fee expense** | **(645,449)** | (494,048) |
| **Fee from banking services, net** | **2,298,394** | 1,634,384 |

## 19. OTHER OPERATING INCOME

Other operating income for the years ended December 31, comprises the following:

| | (SR'000) | |
|---|---|---|
| | **2011** | 2010 |
| Recovery of written-off debts | **169,462** | 155,231 |
| Dividends income | **33,288** | 22,100 |
| Income from sale of investments | **27,168** | 12,364 |
| Other income, net | **105,029** | 77,964 |
| **Total** | **334,947** | 267,659 |

## 20. SALARIES AND EMPLOYEES RELATED BENEFITS

The following tables provide an analysis of the salaries and employee related benefits for the years ended December 31:

| | | **Compensations (SR'000)** | | | |
|---|---|---|---|---|---|
| | | | **Variable** | | |
| **2011** | **Number of employees** | **Fixed** | **Cash** | **Shares** | **Total** |
| Executives | 28 | 36,881 | 11,339 | - | 48,220 |
| Risk department employees | 253 | 64,393 | 1,791 | - | 66,184 |
| Control department employees | 243 | 82,269 | 5,960 | - | 88,229 |
| Other employees | 8,758 | 1,341,785 | 189,337 | - | 1,531,122 |
| External employees | 979 | 111,102 | 30,515 | - | 141,617 |
| **Total** | 10,261 | 1,636,430 | 238,942 | - | 1,875,372 |
| Accrued variable compensations in 2011 | - | 26,431 | 24,407 | - | 50,838 |
| Other employees' bonuses | - | 34,646 | - | - | 34,646 |
| **Gross total** | 10,261 | 1,697,507 | 263,349 | - | 1,960,856 |

As the Kingdom of Saudi Arabia is part of the G-20, instructions were given to all financial institutions in the Kingdom to comply with the standards and principles of Basel II and the financial stability board.

SAMA, as the regulatory for the financial institutions in Saudi Arabia, issued regulations on compensations and bonus in accordance with the standards and principles of Basel II and the financial stability board.

In light of SAMA instructions related to the compensations and bonuses, the Bank issued compensation and bonuses policy which was implemented after the Board of Directors approval.

The scope of this policy is extended to include the Bank and its subsidiary companies (local and international) that are operating in the financial sector. Accordingly it includes all official employees, permanent and temporary contracted employees and service providers (contribution in risk position if SAMA allows the use of external resources).

For consistency with other banking institutions in the Kingdom of Saudi Arabia, the Bank has used a combination of fixed and variable compensation to attract and maintain talents. The fixed compensation is assessed on a yearly basic by comparing it to other local banks in the Kingdom of Saudi Arabia including the basic salaries, allowance and benefits which is related to the employee's ranks. The variable compensation is related to the employees performance and their compatibility to achieve the agreed on objectives. It includes incentives, performance bonus and other. Incentives are mainly paid to branches employees whereby the performance bonuses are paid to head office employees and others who are not qualified for incentives.

These bonuses and compensation should be approved by the board of directors as a percentage of the Bank's income.

## 21. EARNINGS PER SHARE

Earnings per share are calculated by dividing the net income for the year by the weighted average number of shares outstanding during the year (Note 14).

## 22. PAID AND PROPOSED GROSS DIVIDENDS AND ZAKAT

The Bank distributed dividends for the first half of 2011 amounting to SR 1,875,000 thousand (i.e. SR 1.25 per share). Also the Board proposed gross dividends for the second half of 2011 amounting to SR 3,750,000 thousand (2010: SR 3,000,000 thousand) of which SR 750,000 thousand (2010: SR 750,000 thousand) was deducted for zakat from the proposed gross dividends, resulting in a net dividend of SR 3.25 per share for 2011 (2010: SR 3 per share).

The zakat assessments for the years through 1997 have been finalized with the Department of Zakat and Income Tax ("DZIT"). The DZIT issued assessments for the years 1998 through 2006, which were appealed by the Bank.

The Bank submitted the zakat assessment for the years from 2007 till 2010 and paid the zakat due accordingly. The DZIT did not yet issue the final zakat assessments for these years.

## 23. CASH AND CASH EQUIVALENTS

Cash and cash equivalents included in the consolidated statement of cash flows comprise the following as of December 31:

| | (SR'000) | |
|---|---|---|
| | **2011** | 2010 |
| Cash | **6,186,518** | 5,329,888 |
| Due from banks (current accounts and Murabaha) | **8,881,065** | 10,110,756 |
| Balances with SAMA (current accounts) | **3,554,488** | 4,784,036 |
| **Total** | **18,622,071** | 20,224,680 |

## 24. SEGMENTAL INFORMATION

The Bank identifies operating segments on the basis of internal reports about components of the Bank that are regularly reviewed by the chief operating decision maker, principally the Chief Executive Officer, in order to allocate resources to the segments and to assess its performance.

For management purposes, the Bank is organized into the following four main businesses segments:

**Retail segment:** Includes individual customer deposits, credit facilities, customer debit current accounts (overdrafts), fees from banking services and remittance business.

**Corporate segment:** Incorporates deposits of VIP, corporate customer deposits, credit facilities, and debit current accounts (overdrafts).

**Treasury segment:** Incorporates treasury services, Murabaha with SAMA and international Mutajara portfolio.

**Investment services and brokerage segments:** Incorporates investments of individuals and corporate in mutual funds, local and international share trading services and investment portfolios.

Transactions between the above segments are on normal commercial terms and conditions. There are no material items of income or expenses between the above segments. Assets and liabilities for the segments comprise operating assets and liabilities, which represents the majority of the Bank's assets and liabilities.

The Bank carries out its activities principally in the Kingdom of Saudi Arabia, and has six subsidiaries as of December 31, 2011 (2010: four), as listed in Note 1-a, of which three operates outside the Kingdom of Saudi Arabia (2010: Two).

The total assets, liabilities, commitments, contingencies and results of operations of these subsidiaries are not material to the Bank's consolidated financial statements as a whole.

a) The Bank's total assets and liabilities, together with its total operating income and expenses, and net income, for the years ended December 31, for each segment are as follows:

| **2011** | **(SR'000)** | | | | |
|---|---|---|---|---|---|
| | **Retail segment** | **Corporate segment** | **Treasury segment** | **Investment services and brokerage segment** | **Total** |
| **Total assets** | 103,331,875 | 47,548,619 | 69,104,900 | 828,018 | 220,813,412 |
| **Capital expenditures** | 642,904 | 269 | 23 | - | 643,196 |
| **Total liabilities** | 135,608,235 | 45,570,953 | 4,927,886 | 1,885,281 | 187,992,355 |
| **Gross financing & investments income** | 6,692,759 | 2,100,240 | 507,423 | 23,975 | 9,324,397 |
| **Income paid to customers on time investments** | (26,197) | (16,725) | (211,532) | - | (254,454) |
| **Total operating income** | 8,808,241 | 2,181,239 | 1,095,958 | 416,681 | 12,502,119 |
| **Impairment charge for financing and other** | (970,045) | (675,097) | - | - | (1,645,142) |
| **Deprecation and amortization** | (384,190) | (7,460) | (893) | (15,272) | (407,815) |
| **Other operating expenses** | (2,510,756) | (240,064) | (101,301) | (218,773) | (3,070,894) |
| **Total operating expenses** | (3,864,991) | (922,621) | (102,194) | (234,045) | (5,123,851) |
| **Net income** | **4,943,250** | **1,258,618** | **993,764** | **182,636** | **7,378,268** |

| 2010 | (SR'000) | | | | |
|---|---|---|---|---|---|
| | Retail segment | Corporate segment | Treasury segment | Investment services and brokerage segment | Total |
| Total assets | 82,397,368 | 47,568,053 | 54,072,844 | 802,645 | 184,840,910 |
| Capital expenditures | 571,630 | - | 1,318 | - | 572,948 |
| Total liabilities | 106,730,123 | 42,679,043 | 2,993,084 | 2,120,871 | 154,523,121 |
| Gross financing & investments income | 6,525,109 | 2,461,220 | 343,994 | 22,442 | 9,352,765 |
| Income paid to customers on time investments | (38,432) | (9,412) | (182,504) | - | (230,348) |
| Total operating income | 7,881,379 | 2,380,340 | 1,117,325 | 282,088 | 11,661,132 |
| Impairment charge for financing and other | (705,116) | (1,203,702) | - | - | (1,908,818) |
| Depreciation and amortization | (328,154) | (6,515) | (687) | (13,883) | (349,239) |
| Other operating expenses | (2,150,094) | (212,218) | (75,798) | (194,136) | (2,632,246) |
| Total operating expenses | (3,183,364) | (1,422,435) | (76,485) | (208,019) | (4,890,303) |
| Net income | 4,698,015 | 957,905 | 1,040,840 | 74,069 | 6,770,829 |

b) The Bank’s credit exposure by business segments as of December 31, is as follows:

| **2011** | **(SR'000)** | | | | |
|---|---|---|---|---|---|
| | **Retail segment** | **Corporate segment** | **Treasury segment** | **Investment services and brokerage segment** | **Total** |
| Consolidated balance sheet assets | 96,583,128 | 45,599,820 | 51,990,891 | - | 194,173,839 |
| Commitments and contingencies excluding irrevocable commitments to extend credit | 6,098,578 | 3,579,150 | - | - | 9,677,728 |

| 2010 | (SR'000) | | | | |
|---|---|---|---|---|---|
| | Retail segment | Corporate segment | Treasury segment | Investment services and brokerage segment | Total |
| Consolidated balance sheet assets | 72,274,068 | 47,174,521 | 39,732,833 | 559,728 | 159,741,150 |
| Commitments and contingencies excluding irrevocable commitments to extend credit | 2,792,759 | 7,889,348 | 315,217 | - | 10,997,324 |

Credit risks comprise the carrying value of the consolidated statement of financial position, except for cash and balances with SAMA, property and equipment and other assets. The credit equivalent value of commitments and contingencies are included in credit exposure.

## 25. FINANCIAL RISK MANAGEMENT

The Bank's activities expose it to a variety of financial risks and those activities involve the analysis, evaluation, acceptance and management of some degree of risk or combination of risks. Taking risk is core to the banking business, and these risks are an inevitable consequence of participating in financial markets. The Bank's aim is therefore to achieve an appropriate balance between risk and return and minimize potential adverse effects on the Bank's financial performance.

The Bank's risk management policies, procedures and systems are designed to identify and analyze these risks and to set appropriate risk mitigants and controls. The Bank reviews its risk management policies and systems on an ongoing basis to reflect changes in markets, products and emerging best practice.

Risk management is performed by the Credit and Risk Management Group ("CRMG") under policies approved by the Board of Directors. The CRMG identifies and evaluates financial risks in close co-operation with the Bank's operating units. The most important types of risks identified by the Bank are credit risk, operational risk, liquidity risk and market risk. Market risk includes currency risk, profit rate risk and price risk.

### 25-1 Credit risk

Credit risk is considered to be the most significant and pervasive risk for the Bank. The Bank takes on exposure to credit risk, which is the risk that the counter-party to a financial transaction will fail to discharge an obligation causing the Bank to incur a financial loss. Credit risk arises principally from financing (credit facilities provided to customers) and from cash and deposits held with other banks. Further, there is credit risk in certain off-balance sheet financial instruments, including guarantees relating to purchase and sale of foreign currencies, letters of credit, acceptances and commitments to extend credit. Credit risk monitoring and control is performed by the CRMG which sets parameters and thresholds for the Bank's financing activities.

#### a. Credit risk measurement

**Financing**

The Bank has structured a number of financial products which are in accordance with Shariah law in order to meet the customers demand. These products are all classified as financing assets in the Bank's consolidated statement of financial position. In measuring credit risk of financing at a counterparty level, the Bank considers the overall credit worthiness of the customer based on a proprietary risk methodology. This risk rating methodology utilizes a 10 point scale based on quantitative and qualitative factors with seven performing categories (rated 1 to 7) and three non performing categories (rated 8-10). The risk rating process is intended to advise the various independent approval authorities of the inherent risks associated with the counterparty and assist in determining suitable pricing commensurate with the associated risk.

This process also enables the Bank to detect any weakness in the portfolio quality and make appropriate adjustments to credit risk allowances, where credit quality has deteriorated and where losses are likely to arise. The Bank evaluates individual corporate customer balances which are past due to make appropriate allowances against financings. For the remaining (performing) corporate portfolio, the Bank applies a loss rate to determine an appropriate collective allowance. The loss rate is determined based on historical experience of credit losses.

**Settlement risk**

The Bank is also exposed to settlement risk in its dealings with other financial institutions. These risks arise when the Bank pays away its side of the transaction to the other bank or counterparty before receiving payment from the third party. The risk is that the third party may not pay its obligation. While these exposures are short in duration but they can be significant. The risk is mitigated by dealing with highly rated counterparties, holding collateral and limiting the size of the exposures according to the risk rating of the counterparty.

**b. Risk limit control and mitigation policies**

The responsibility for credit risk management is enterprise wide in scope. Strong risk management is integrated into daily processes, decision making and strategy setting, thereby making the understanding and management of credit risk the responsibility of every business segment.

The following business units within the Bank assist in the credit control process:

- Corporate Credit Unit,
- Credit Administration, Monitoring and Control Unit,
- Remedial Unit,
- Credit Policy Unit,
- Retail Credit Unit

The monitoring and management of credit risk associated with these financing are made by setting approved credit limits. The Bank manages limits and controls concentrations of credit risk wherever they are identified - in particular, to individual customers and groups, and to industries and countries.

Concentrations of credit risks arise when a number of customers are engaged in similar business activities, activities in the same geographic region, or have similar economic features that would cause their ability to meet contractual obligations to be similarly affected by changes in economic, political or other conditions. Concentrations of credit risks indicate the relative sensitivity of the Bank's performance to developments affecting a particular industry or geographical location.

The Bank seeks to manage its credit risk exposure through diversification of its financing to ensure there is no undue concentration of risks with to individuals or groups of customers in specific geographical locations or economic sectors.

The Bank manages credit risk by placing limits on the amount of risk accepted in relation to individual customers and groups, and to geographic and economic segments. Such risks are monitored on a regular basis and are subject to an annual or more frequent review, when considered necessary. Limits on the level of credit risk by product, economic sector and by country are reviewed at least annually.

Exposure to credit risk is also managed through regular analysis on the ability of customers and potential customers to meet financial and contractual repayment obligations and by revising credit limits where appropriate.

Some other specific control and mitigation measures are outlined below.

### b-1) Collateral

The Bank implements guidelines on the level and quality of specific classes of collateral. The principal collateral types are:

- Mortgages over residential and commercial properties.
- Cash, shares, and general assets for customer
- Shares for Murabaha (collateralized share trading) transactions

### b-2) Collateralized Credit - related commitments

The primary purpose of these instruments is to ensure that funds are available to a customer as required. Guarantees and standby letters of credit carry the same credit risk as traditional banking products of the Bank.

Documentary and commercial 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 collateralized by the underlying goods to which they relate, and therefore, risk is partially mitigated.

Commitments to extend credit represent unused portions of authorizations to extend credit in the form of further financing products, guarantees or letters of credit. With respect to credit risk on commitments to extend credit, the Bank is potentially exposed to loss in an amount equal to the total unused commitments. However, the likely amount of loss is less than the total unused commitments, as most commitments to extend credit are contingent upon customers maintaining specific credit standards.

## c. Impairment and provisioning policies

Impairment provisions are recognized for financial reporting purposes only for losses that have been incurred at the statement of financial position date based on objective evidence of impairment, and management judgment.

Management determines whether objective evidence of impairment exists under IAS 39, based on the following criteria as defined by the Bank:

- Delinquency in contractual payments of principal or profit.
- Cash flow difficulties experienced by the customer.
- Breach of repayment covenants or conditions.
- Initiation of bankruptcy proceedings against the customer.
- Deterioration of the customer’s competitive position.
- Deterioration in the value of collateral.

The Bank's policy requires the review of each individual corporate customer at least annually or more regularly when individual circumstances require. Impairment allowances on individually assessed accounts are determined by an evaluation of incurred losses at the statement of financial position date on a case-by-case basis, and by using management judgment.

The assessment normally encompasses collateral held (including re-confirmation of its enforceability) and the anticipated receipts for that individual account.

Collectively assessed impairment allowances are provided for:

- Portfolios of homogenous assets mainly relating to the retail financing portfolio that are individually not significant.
- On the corporate portfolio for financing where losses have been incurred but not yet identified, by using historical experience, judgment and statistical techniques.

The table below sets out the maximum exposure to credit risk at the reporting date without considering collateral or other credit enhancements and includes the off-balance sheet financial instruments involving credit risks.

| | (SR'000) | |
|---|---|---|
| | **2011** | 2010 |
| **On-balance sheet items:** | | |
| Due from banks and other financial institutions | **14,599,787** | 11,117,539 |
| **Financing, net:** | | |
| Corporate | **47,088,783** | 47,110,709 |
| Retail | **93,306,836** | 72,953,958 |
| Customer debit current accounts, net | **375,941** | 312,062 |
| Other assets, net | **2,596,584** | 2,229,701 |
| **Total on-balance sheet items** | **157,967,931** | 133,723,969 |
| **Off-balance sheet items:** | | |
| Letters of credit and acceptances | **3,797,759** | 4,633,730 |
| Letters of guarantee | **5,879,969** | 6,363,594 |
| Irrevocable commitments to extend credit | **5,706,419** | 7,167,869 |
| **Total off-balance sheet items** | **15,384,147** | 18,165,193 |
| **Maximum exposure to credit risk** | **173,352,078** | 151,889,162 |

The above table represents a worst case scenario of credit risk exposure to the Bank at December 31, 2011 and 2010, without taking account of any collateral held or other credit enhancements attached. For on-balance-sheet assets, the exposures set out above are based on net carrying amounts as reported in the consolidated statement of financial position.

### 25-2 Liquidity risks

Liquidity risk is the risk that the Bank will be unable to meet its payment obligations associated with its financial liabilities when they fall due and to replace funds when they are withdrawn. The consequence may be the failure to meet obligations to repay deposits and financing parties and fulfill financing commitments. Liquidity risk can be caused by market disruptions or by credit downgrades, which may cause certain sources of funding to become unavailable immediately. Diverse funding sources available to the Bank help mitigate this risk. Assets are managed with liquidity in mind, maintaining a conservative balance of cash and cash equivalents.

**Liquidity risk management process**

The Bank's liquidity management process is as monitored by the Bank's Asset and Liabilities Committee (ALCO), includes:

- Day-to-day funding, managed by Treasury to ensure that requirements can be met and this includes replenishment of funds as they mature or are invested;
- Monitoring balance sheet liquidity ratios against internal and regulatory requirements;
- Managing the concentration and profile of debt maturities;

- Maintain diversified funding sources;
- Liquidity management and asset and liability mismatching.

Monitoring and reporting take the form of analyzing cash flows of items with both contractual and non-contractual maturities. The net cash flows are measured and ensured that they are within acceptable ranges. The Treasury / ALCO also monitors, the level and type of undrawn lending commitments, usage of overdraft facilities and the potential impact contingent liabilities such as standby letters of credit and guarantees may have on the Bank's liquidity position.

The tables below summarize the maturity profile of the Bank's assets and liabilities, on the basis of the remaining maturity as of the consolidated statement of financial position date to the contractual maturity date.

Management monitors the maturity profile to ensure that adequate liquidity is maintained. Assets available to meet all of the liabilities and to cover outstanding financing commitments include cash, balances with SAMA and due from banks. Further, in accordance with the Banking Control Law and Regulations issued by SAMA, the Bank maintains a statutory deposit equal to a sum not less than 7% of total customer deposits, and 4% of total other customer accounts. In addition to the statutory deposit, the Bank maintains a liquid reserve of not less than 20% of the deposit liabilities, in the form of cash, gold or assets which can be converted into cash within a period not exceeding 30 days. Also, the Bank has the ability to raise additional funds through special financing arrangements with SAMA including deferred sales transactions.

The contractual maturities of assets, liabilities and shareholders' equity as of December 31, based on discounted cash flows are as follows:

| **2011** | **(SR'000)** | | | | | |
|---|---|---|---|---|---|---|
| | **Less than 3 months** | **3 to 12 months** | **1 to 5 years** | **Over 5 years** | **No fixed maturity** | **Total** |
| **Assets** | | | | | | |
| Cash and balance with SAMA | 9,741,006 | - | - | - | 10,678,461 | 20,419,467 |
| Due from banks and other financial institutions | 11,035,951 | 3,563,836 | - | - | - | 14,599,787 |
| Financing, net | 17,889,745 | 28,894,769 | 76,232,987 | 17,378,118 | - | 140,395,619 |
| Investments | 17,845,267 | 20,894,740 | - | 62,485 | - | 38,802,492 |
| Customer debit current accounts, net | 162,575 | - | - | 213,366 | - | 375,941 |
| Property and equipment, net | - | - | - | - | 3,623,522 | 3,623,522 |
| Other assets, net | 2,261,517 | - | 335,067 | - | - | 2,596,584 |
| **Total** | **58,936,061** | **53,353,345** | **76,568,054** | **17,653,969** | **14,301,983** | **220,813,412** |
| **Liabilities and Shareholders' equity** | | | | | | |
| Due to banks and other financial institutions | 6,936,470 | 84,311 | - | - | - | 7,020,781 |
| Customer deposits | 173,429,465 | - | - | - | - | 173,429,465 |
| Other liabilities | - | - | - | - | 7,542,109 | 7,542,109 |
| Shareholders' equity | - | - | - | - | 32,821,057 | 32,821,057 |
| **Total** | **180,365,935** | **84,311** | **-** | **-** | **40,363,166** | **220,813,412** |

| 2010 | (SR'000) | | | | | |
|---|---|---|---|---|---|---|
| | Less than 3 months | 3 to 12 months | 1 to 5 years | Over 5 years | No fixed maturity | Total |
| **Assets** | | | | | | |
| Cash and balances with SAMA | 10,113,924 | - | - | - | 9,361,272 | 19,475,196 |
| Due from banks and other financial institutions | 11,117,539 | - | - | - | - | 11,117,539 |
| Financing, net | 18,300,313 | 22,229,443 | 63,541,315 | 15,993,596 | - | 120,064,667 |
| Investments | 17,738,355 | 10,508,527 | - | - | - | 28,246,882 |
| Customer debit current accounts, net | 100,075 | 149,613 | - | 62,374 | - | 312,062 |
| Property and equipment, net | - | - | - | - | 3,394,863 | 3,394,863 |
| Other assets, net | 981,890 | 972,722 | 275,089 | - | - | 2,229,701 |
| **Total** | 58,352,096 | 33,860,305 | 63,816,404 | 16,055,970 | 12,756,135 | 184,840,910 |
| **Liabilities and Shareholders' equity** | | | | | | |
| Due to banks and other financial institutions | 5,414,181 | - | - | - | - | 5,414,181 |
| Customer deposits | 131,322,236 | 9,064,659 | - | 2,677,142 | - | 143,064,037 |
| Other liabilities | - | - | - | - | 6,044,903 | 6,044,903 |
| Shareholders' equity | - | - | - | - | 30,317,789 | 30,317,789 |
| **Total** | 136,736,417 | 9,064,659 | - | 2,677,142 | 36,362,692 | 184,840,910 |

The following tables disclose the maturity of contractual financial liabilities on undiscounted cash flows as at December 31:

| **2011** | **(SR'000)** | | | | | |
|---|---|---|---|---|---|---|
| | **Less than 3 months** | **3 to 12 months** | **1 to 5 years** | **Over 5 years** | **No fixed maturity** | **Total** |
| Due to banks and other financial institutions | 6,945,140 | 84,912 | - | - | - | 7,030,052 |
| Customer deposits | 173,646,252 | - | - | - | - | 173,646,252 |
| Other liabilities | - | - | - | - | 7,542,109 | 7,542,109 |
| **Total** | 180,591,392 | 84,912 | - | - | 7,542,109 | 188,218,413 |

| 2010 | (SR'000) | | | | | |
|---|---|---|---|---|---|---|
| | Less than 3 months | 3 to 12 months | 1 to 5 years | Over 5 years | No fixed maturity | Total |
| Due to banks and other financial institutions | 5,425,897 | - | - | - | - | 5,425,897 |
| Customer deposits | 131,358,236 | 9,067,659 | - | 2,678,492 | - | 143,104,387 |
| Other liabilities | - | - | - | - | 6,044,903 | 6,044,903 |
| Total | 136,784,133 | 9,067,659 | - | 2,678,492 | 6,044,903 | 154,575,187 |

The cumulative maturities of commitments & contingencies are given in note 16-C-1 of the financial statements.

## 25-3 Market risks

The Bank is exposed to market risks, which is the risk that the fair value or future cash flows of a financial instrument will fluctuate due to changes in market prices. Market risks arise on profit rate products, foreign currency and mutual fund products, all of which are exposed to general and specific market movements and changes in the level of volatility of market rates or prices such as profit rates, foreign exchange rates and quoted market prices.

Market risk exposures are monitored by Treasury / Credit & Risk department and reported to ALCO on a monthly basis. ALCO deliberates on the risks taken and ensure that they are appropriate.

### a. Market risks - speculative operations

The Bank is not exposed to market risks from speculative operations. The Bank is committed to Sharia guidelines which does not permit it to enter into contracts or speculative instruments such as hedging, options, forward contracts and derivatives.

### b. Market risks - banking operations

The Bank is exposed to market risks, which is the risk that the fair value or future cash flows of a financial instrument will fluctuate due to changes in market prices. Market risks arise on profit rate products, foreign currency and mutual fund products, all of which are exposed to general and specific market movements and changes in the level of volatility of market rates or prices such as profit rates, foreign exchange rates and quoted market prices.

**- Profit rate risk**

Cash flow profit rate risk is the risk that the future cash flows of a financial instrument will fluctuate due to changes in market profit rates. The Bank does not have any significant exposure to the effects of fluctuations in prevailing level of market profit rates on its future cash flows as a significant portion of profit earning financial assets and profit bearing liabilities are at fixed rates and are carried in the financial statements at amortized cost. In addition to this, a substantial portion of the Bank’s financial liabilities are non-interest bearing.

**- Foreign currency risks**

The Bank is exposed to the effects of fluctuations in foreign currency exchange rates on its financial position, results of operations and cash flows. The Bank’s management sets limits on the level of exposure by currency and in total for both overnight and intraday positions, which are monitored daily.

A substantial portion of the net foreign currency exposure to the Bank is in US Dollars, where the SR is pegged to the US Dollar. The other currency exposures are not considered significant to the Bank’s foreign currency risks and as a result the Bank is not exposed to major foreign currency risks.

The Bank has performed a sensitivity analysis for the reasonably possible changes in foreign exchange rates, other than US Dollars, using historical average exchange rates and has determined that there is no significant impact on its net foreign currency exposures.

The tables below summarize the Bank’s exposure to foreign currency exchange rate risk at December 31, 2011 and 2010 and the concentration of currency risks. Included in the table are the Bank’s financial instruments at carrying amounts, categorized by currency:

**2011**

| | (SR'000) | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| | **UAE DIRHAM** | **BANGLADESH TAKA** | **JAPANESE YEN** | **EURO** | **LEBANESE LIRA** | **MALAYSIAN RINGGIT** | **US DOLLAR** | **POUND STERLING** | **OTHER** | **TOTAL** |
| **ASSETS** | | | | | | | | | | |
| Cash and cash equivalent | 16,937 | 101 | 67 | 44,434 | 179 | 54,654 | 187,324 | 17,341 | 91,550 | 412,587 |
| Due from banks and other financial institutions | 161,417 | 36,205 | 5,761 | 156,715 | 1,041 | 1,547,189 | - | 4,922 | 1,136,211 | 3,049,461 |
| Financing, net | - | - | - | - | - | 5,388,922 | 7,644,754 | - | 138,089 | 13,171,765 |
| Investments | - | - | - | 424 | - | 1,180,353 | 332,901 | - | 509,273 | 2,022,951 |
| Customer debit current account, net | - | - | - | 1,089 | - | 4,450 | - | - | - | 5,539 |
| Other assets, net | - | - | - | - | - | 185,015 | 69,722 | - | 53,250 | 307,987 |
| **Total Assets** | **178,354** | **36,306** | **5,828** | **202,662** | **1,220** | **8,360,583** | **8,234,701** | **22,263** | **1,928,373** | **18,970,290** |
| **LIABILITIES** | | | | | | | | | | |
| Due to banks and other financial institutions | 7,298 | 1,415 | - | 7,246 | - | 3,778,559 | 266,783 | 5,300 | 130,671 | 4,197,272 |
| Customer deposits | 10,224 | - | 3,578 | 174,132 | 11,569 | 2,417,704 | 1,686,263 | 9,491 | 469,334 | 4,782,295 |
| Other liabilities | 5,503 | 60,533 | 1,067 | 11,749 | 1,241 | 97,745 | - | 7,031 | 102,008 | 286,877 |
| **Total Liabilities** | **23,025** | **61,948** | **4,645** | **193,127** | **12,810** | **6,294,008** | **1,953,046** | **21,822** | **702,013** | **9,266,444** |
| **Net** | **155,329** | **(25,642)** | **1,183** | **9,535** | **(11,590)** | **2,066,575** | **6,281,655** | **441** | **1,226,360** | **9,703,846** |

2010

| | (SR'000) | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| | UAE DIRHAM | BANGLADESH TAKA | JAPANESE YEN | EURO | LEBANESE LIRA | MALAYSIAN RINGGIT | US DOLLAR | POUND STERLING | OTHER | TOTAL |
| **ASSETS** | | | | | | | | | | |
| Cash and cash equivalent | 17,779 | - | 26 | 22,745 | 192 | 49,319 | 101,498 | 13,546 | 65,565 | 270,670 |
| Due from banks and other financial institutions | 96,603 | 99,002 | 140,331 | 198,407 | 477 | 1,554,705 | 1,534,148 | 5,419 | 907,230 | 4,536,322 |
| Financing, net | - | - | - | - | - | 4,914,348 | 6,840,211 | - | - | 11,754,559 |
| Investments | - | - | - | 513 | - | 1,561,840 | 902,883 | - | 461,014 | 2,926,250 |
| Customer debit current account, net | 102 | - | - | 1,375 | - | - | 375 | 291 | - | 2,143 |
| Other assets, net | - | - | - | 62 | - | 283,901 | 63,708 | - | 15,972 | 363,643 |
| **Total Assets** | 114,484 | 99,002 | 140,357 | 223,102 | 669 | 8,364,113 | 9,442,823 | 19,256 | 1,449,781 | 19,853,587 |
| **LIABILITIES** | | | | | | | | | | |
| Due to banks and other financial institutions | - | - | - | 729 | - | 2,960,776 | 1,168,444 | 2,832 | 198,138 | 4,330,919 |
| Customer deposits | 6,061 | - | 138,570 | 180,648 | 11,922 | 2,914,271 | 682,332 | 15,546 | 45,618 | 3,994,968 |
| Other liabilities | 3,672 | 74,700 | 1,009 | 7,288 | 1,327 | 272,240 | (115,874) | 6,112 | 408,359 | 658,833 |
| **Total Liabilities** | 9,733 | 74,700 | 139,579 | 188,665 | 13,249 | 6,147,287 | 1,734,902 | 24,490 | 652,115 | 8,984,720 |
| **Net** | 104,751 | 24,302 | 778 | 34,437 | (12,580) | 2,216,826 | 7,707,921 | (5,234) | 797,666 | 10,868,867 |

### c. Price risk

The Bank has certain investments which are carried at fair value through the income statement and includes investments in quoted mutual funds and other investments. Price risk arises due to changes in quoted market prices of these mutual funds.

As these investments are in a limited number of funds and are not significant to the total investment portfolio, the Bank monitors them periodically and determines the risk of holding them based on changes in market prices.

Other investments have little or no risks as these are bought for immediate sales. Investments are made only with a confirmed sale order and therefore involve minimal risk.

### d. Operational risk

Operational risk is the risk of loss resulting from inadequate or failed internal processes, people, systems, and external events.

Operational risk is inherent in most of the Bank's activities this necessitates an integrated approach to the identification, measurement and monitoring of operational risk.

An Operational Risk Management Unit (ORMU) has been established within the Credit and Risk Management Group which facilitates the management of Operational Risk within the Bank. ORMU facilitates the management of Operational Risk by setting policies, developing systems, tools and methodologies, overseeing their implementation and use within the business units and providing ongoing monitoring and guidance across the Bank.

The three primary operational risk management processes in the Bank are Risk Control Self Assessment, Operational Loss Database and eventual implementation of Key Risk Indicators which are designed to function in a mutually reinforcing manner.

## 26. GEOGRAPHICAL CONCENTRATION

a) The distribution by the geographical region of the major categories of assets, liabilities, commitments, contingencies and credit exposure accounts as of December 31, is as follows:

**2011** (SR'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 | 20,360,676 | 4,021 | 652 | - | - | 54,118 | - | 20,419,467 |
| Due from banks and other financial institutions | 8,414,846 | 4,139,008 | 187,454 | 27,687 | - | 1,613,482 | 217,310 | 14,599,787 |
| Financing, net | 135,798,250 | 138,089 | - | - | - | 4,459,280 | - | 140,395,619 |
| Investments | 36,867,520 | 463,233 | 39,224 | 228,096 | - | 1,204,419 | - | 38,802,492 |
| **Total** | **201,441,292** | **4,744,351** | **227,330** | **255,783** | **-** | **7,331,299** | **217,310** | **214,217,365** |
| **Liabilities** | | | | | | | | |
| Due to banks and other financial institutions | 1,709,066 | 1,020,287 | 17,780 | 435,081 | - | 3,792,056 | 46,511 | 7,020,781 |
| Customer deposits | 170,589,595 | 422,166 | - | - | - | 2,417,704 | - | 173,429,465 |
| **Total** | **172,298,661** | **1,442,453** | **17,780** | **435,081** | **-** | **6,209,760** | **46,511** | **180,450,246** |
| **Commitments and contingencies** | **14,958,109** | **222,061** | **29,982** | **71,974** | **-** | **9,872** | **92,149** | **15,384,147** |
| **Credit exposure (stated at credit equivalent value)** | **9,251,690** | **222,061** | **29,982** | **71,974** | **-** | **9,872** | **92,149** | **9,677,728** |

**2010**

| | (SR'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 | 19,425,698 | 1,187 | - | - | - | 48,311 | - | 19,475,196 |
| Due from banks and other financial institutions | 3,420,097 | 5,176,063 | 593,778 | 138,266 | - | 1,409,658 | 379,677 | 11,117,539 |
| Financing, net | 113,025,229 | 999,989 | 187,600 | - | 937,500 | 4,914,349 | - | 120,064,667 |
| Investments | 26,798,019 | 693,037 | 24,345 | 163,768 | - | 567,713 | - | 28,246,882 |
| **Total** | 162,669,043 | 6,870,276 | 805,723 | 302,034 | 937,500 | 6,940,031 | 379,677 | 178,904,284 |
| **Liabilities** | | | | | | | | |
| Due to banks and other financial institutions | 1,059,993 | 1,430,344 | 19,091 | 13,775 | - | 2,871,692 | 19,286 | 5,414,181 |
| Customer deposits | 139,756,491 | 13,949 | - | - | - | 3,293,597 | - | 143,064,037 |
| **Total** | 140,816,484 | 1,444,293 | 19,091 | 13,775 | - | 6,165,289 | 19,286 | 148,478,218 |
| **Commitments and contingencies** | 13,042,613 | 585,232 | 1,621,882 | 192,710 | 21,217 | 395,559 | 2,305,980 | 18,165,193 |
| **Credit exposure (stated at credit equivalent value)** | 5,874,744 | 585,232 | 1,621,882 | 192,710 | 21,217 | 395,559 | 2,305,980 | 10,997,324 |

Credit equivalent amounts reflect the amounts that result from conversion of the Bank's off-balance sheet liabilities relating to commitments and contingencies into the risk equivalent of financing, using credit conversion factors prescribed by SAMA. Credit conversion factor is meant to capture the potential credit risk related to the exercise of that commitment.

b) The distributions by geographical concentration of non-performing financing and provisions for financing losses as of December 31, are as follows:

**2011**

| | (SR'000) | | |
|---|---|---|---|
| | **Non-performing** | **Provisions for financing losses** | **Net non-performing financing** |
| Kingdom of Saudi Arabia | 2,258,805 | (1,699,701) | 559,104 |
| South East of Asia | 137,149 | (109,145) | 28,004 |
| **Total** | **2,395,954** | **(1,808,846)** | **587,108** |

2010

| | (SR'000) | | |
|---|---|---|---|
| | Non-performing | Provisions for financing losses | Net non-performing financing |
| Kingdom of Saudi Arabia | 2,416,464 | (942,512) | 1,473,952 |
| South East of Asia | 245,706 | (125,449) | 120,257 |
| Total | 2,662,170 | (1,067,961) | 1,594,209 |

Refer to Note 6-c for performing financing.

## 27. FAIR VALUE OF FINANCIAL ASSETS AND LIABILITIES

### Determination of fair value and fair value hierarchy

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

Level 1: quoted prices in active markets for the same instrument (i.e., without modification or repacking):

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.

Assets at fair values are as follows:

| 2011 | (SR'000) | | | |
|---|---|---|---|---|
| | **Level 1** | **Level 2** | **Level 3** | **Total** |
| **<u>Financial assets</u>** | | | | |
| Financial assets at FVIS | 1,225,850 | - | 2,051,719 | **3,277,569** |

| 2010 | (SR'000) | | | |
|---|---|---|---|---|
| | **Level 1** | **Level 2** | **Level 3** | **Total** |
| **<u>Financial assets</u>** | | | | |
| Financial assets at FVIS | 1,051,591 | - | 1,596,812 | **2,648,403** |

Fair value is the amount for which an asset could exchanged or a liability settled between knowledgeable, willing parties in an arm's length transaction.

The fair values of on-statement of financial position financial instruments, are not significantly different from the carrying values included in the consolidated financial statements. The fair values of financing due from and due to banks which are carried at amortized cost, are not significantly different from the carrying values included in the financial statements, since the current market 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 value obtained from the relevant valuation model may differ, with the transaction price of a financial instrument. The difference between the transaction price and the model value commonly referred to as 'day one profit and loss' is either amortized over the life of the transaction, deferred until the instrument's fair value can be determined using market observable data, or realized through disposal. Subsequent changes in fair value are recognized immediately in the income statement without reversal of deferred day one profits and losses.

## 28. RELATED PARTY TRANSACTIONS

In the ordinary course of business, the Bank transacts business with related parties. The related party transactions are governed by limits set by the Banking Control Law and the regulations issued by SAMA. The nature and balances resulting from such transactions as at December 31, are as follows:

| | (SR'000) | |
|---|---|---|
| **Related parties** | **2011** | 2010 |
| **Members of the Board of Directors** | | |
| Mutajara | **2,250,598** | 2,087,694 |
| Contingent liabilities* | **974,908** | 1,275,542 |
| **Companies and establishments guaranteed by members of the Board of Directors** | | |
| Mutajara | **1,133,019** | 474,994 |
| Current accounts | **-** | 34,657 |
| Contingent liabilities* | **37,596** | 36,129 |
| **Mudaraba funds (Note 29)** | | |
| Current accounts | **185,845** | 15,919 |
| Mudaraba | **8,166,509** | 10,058,135 |
| Investment in mutual funds | **482,975** | 400,537 |
| **Other major shareholders (above 5% equity share)** | | |
| Mutajara | **-** | 120,597 |
| Direct investment | **-** | 114,388 |
| Current accounts | **-** | 6,184 |
| Investment in mutual funds | **13,731** | 14,103 |
| Other liabilities | **15,666** | 13,523 |

* = off balance sheet items

Income and expenses pertaining to transactions with related parties included in the consolidated financial statements for the years ended December 31, are as follows:

| | (SR'000) | |
|---|---|---|
| | **2011** | 2010 |
| Income from financing and other | **120,703** | 121,382 |
| Employees' salaries and benefits (air tickets) | **10,543** | 10,395 |
| Rent and premises related expenses | **1,936** | 1,526 |
| Board of Directors' remunerations | **3,084** | 3,090 |

The amounts of compensations recorded in favor of or paid to the Board of Directors and the executive management personnel during the years ended December 31, are as follows:

| | (SR'000) | |
|---|---|---|
| | **2011** | 2010 |
| Short-term benefits | **22,465** | 19,656 |
| Provision for end of service benefits | **1,256** | 1,324 |

The executive management personnel are those persons having authority and responsibility for planning, directing and controlling the activities of the Bank directly or indirectly.

## 29. MUDARABA FUNDS

Mudaraba funds as of December 31, comprise the following:

| | (SR'000) | |
|---|---|---|
| | **2011** | 2010 |
| Customers' Mudaraba and investments | **8,166,802** | 10,058,426 |
| Current accounts, metals | **5,642** | 5,678 |
| **Total** | **8,172,444** | 10,064,104 |

## 30. SPECIAL COMMISSIONS EXCLUDED FROM THE CONSOLIDATED STATEMENTS OF INCOME

The following represents the movements in charities account, which is included in other liabilities (see Note 13):

| | (SR'000) | |
|---|---|---|
| | **2011** | 2010 |
| Balance, beginning of the year | **4,923** | 78,206 |
| Additions during the year | **19,216** | 9,550 |
| Payments during the year | **(3,831)** | (82,833) |
| **Balance, end of the year** | **20,308** | 4,923 |

## 31. INVESTMENT MANAGEMENT SERVICES

The Bank offers investment services to its customers. The Bank has established a number of Mudaraba funds in different investment aspects. These funds are managed by the Bank's Investment Department, and a portion of the funds is also invested in participation with the Bank. Mutual funds' financial statements are not included in the consolidated statement of financial position of the Bank. The Bank's share of investments in these funds is included under investments, and is disclosed under related party transactions. Funds invested in participation with the Bank amounted to SR 19,186,249 thousand at December 31, 2011 (2010 SR 17,079,111 thousand).

## 32. CAPITAL ADEQUACY

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

Capital adequacy and the use of regulatory capital are monitored daily by the Bank's management. SAMA requires to hold the minimum level of the regulatory capital of and maintain a ratio is 8% of total regulatory capital to the risk-weighted asset .

The Bank monitors the adequacy of its capital using ratios established by SAMA. These ratios measure capital adequacy by comparing the Bank's eligible capital with its consolidated statement of financial position, commitments and contingencies, to reflect their relative risk as of December 31, 2011 and 2010.

| | (SR'000) | |
|---|---|---|
| | **2011** | 2010 |
| Credit risk weighted assets | **146,884,726** | 127,166,653 |
| Operational risk weighted assets | **19,697,148** | 19,207,023 |
| Market risk weighted assets | **6,435,113** | 8,262,400 |
| **Total Pillar I - risk weighted assets** | **173,016,987** | 154,636,076 |
| Tier I - capital | **25,443,337** | 23,546,960 |
| Tier II capital | **9,214,326** | 8,360,412 |
| **Total tier I & II capital** | **34,657,663** | 31,907,372 |
| **Capital Adequacy Ratio %** | | |
| Tier I ratio | **14.71%** | 15.23% |
| Tier II ratio | **20.03%** | 20.63% |

## 33. COMPARATIVE FIGURES

Certain prior year amounts have been reclassified to conform with the current year presentation.

## 34. EVENTS AFTER THE REPORTING DATE

The Bank's board of directors proposed, in its meeting dated January 17, 2012, a distribution of dividends to the shareholders for the second half of the current fiscal year in the amount of SR 3,000 million amounting to SR 2.00 per share net of zakat.

The board's proposal is subject to the approval of the Extraordinary General Assembly in its next meeting.

## 35. ISSUED IFRS BUT NOT YET EFFECTIVE

The Bank has chosen not to early adopt the updates on standards mentioned below which have been published and are mandatory for compliance for the Bank's fiscal years beginning January 1, 2012 and afterwards.

- Amendments on IAS (1) presentation of Financial Statements
- IFRS 9 - Financial Instruments
- IFRS 15 - Consolidated Financial Statements
- IRRS 13 - Fair Value Measurement

The adoption of the above standards and amendments above will not result in any material change on the consolidated financial statements other than IFRS 9. The Bank is still evaluating the implications of IFRS 9 on the Bank's financial statements.

## 36. APPROVAL OF THE BOARD OF DIRECTORS

The consolidated financial statements were approved by the Board of Directors on 23 Safar 1433H (corresponding to January 17, 2012).

## 37. BASEL II PILLAR 3 DISCLOSURES (UNAUDITED)

Under Basel II pillar 3, certain quantitative and qualitative disclosures are required, and these disclosures will be made available on the Bank's website www.alrajhibank.com.sa and in the Bank's annual report, respectively, as required by the Saudi Arabian Monetary Agency. Such disclosures are not subject to audit by the external auditors of the Bank.