بنك الجزيرة
BANK ALJAZIRA

Annual Report 2008

Custodian of the Two Holy Mosques
King Abdullah Bin Abdulaziz Al-Saud

HRH Prince Sultan Bin Abdulaziz Al-Saud
Crown Prince, Deputy Prime Minister, Minister of Defense and Aviation, and Inspector General

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بسم الله الرحمن الرحيم

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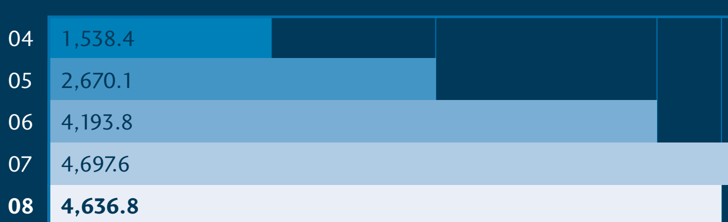
Financial Highlights

(In SR millions, except where noted)	2008	2007	2006	2005	2004
Loans and advances, net	**15,133.1**	9,879.2	6,271.1	6,910.9	5,186.7
Total assets	**27,519.7**	21,563.9	15,712.9	14,168.8	10,721.8
Customer deposits	**20,900.0**	15,647.1	10,917.1	10,816.1	8,141.6
Shareholders' equity	**4,636.8**	4,697.6	4,193.8	2,670.1	1,538.4*
Fee income and others	**562.0**	721.4	1,890.0	925.2	310.4
Net special commission income	**631.4**	595.1	476.6	276.4	187.9
Total operating income	**1,136.5**	1,446.8	2,615.4	1,318.6	600.2
Net income	**222.3**	805.2	1,974.0	874.4	187.7
Net income growth (%)	**(72.4)**	(59.2)	125.8	365.9	100.7
Return on average equity (%)	**4.8**	18.1	57.5	41.6	17.1*
Return on average assets (%)	**0.9**	4.3	13.2	7.0	1.9
Earnings per share (SR)	**0.74**	2.68*	8.77*	7.77*	13.24

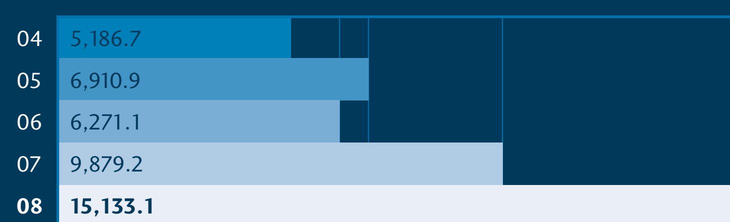
*Restated

OUR MISSION WE ARE A CLIENT-DRIVEN, SERVICE-ORIENTED SAUDI FINANCIAL GROUP WHICH PROVIDES INDIVIDUALS, BUSINESSES AND INSTITUTIONS WITH INNOVATIVE SHARI'AH-COMPLIANT FINANCIAL SERVICES THROUGH PROFESSIONAL AND DEDICATED STAFF.

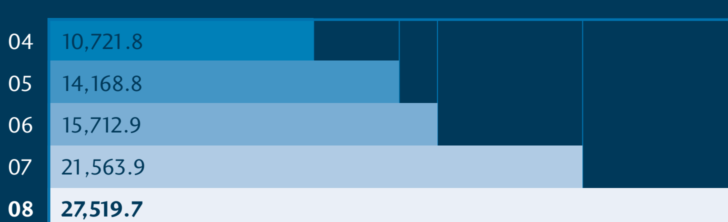
Shareholders' Equity SR millions



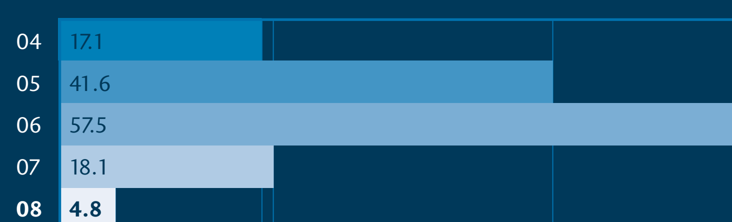
Net Loans and Advances SR millions



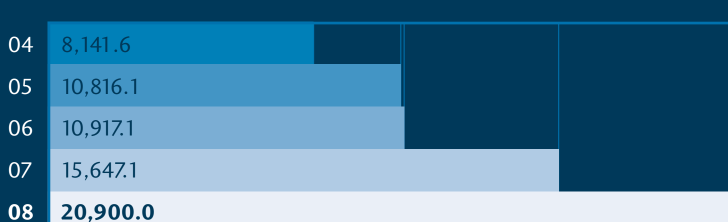
Total Assets SR millions



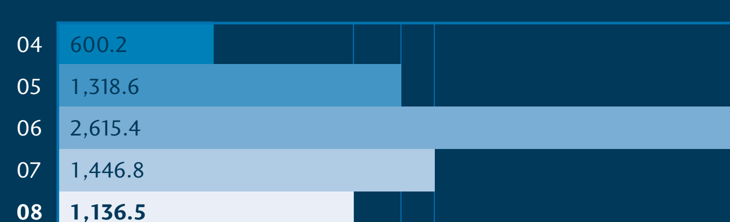
Return on Average Equity Percent



Customer Deposits SR millions



Total Operating Income SR millions



Board of Directors

1 **Taha A. Al-Kuwaiz**
Chairman of the Board

2 **Abdullah S. Kamel**

3 **Tarek O. Al-Kasabi**

4 **Abdul Majeed I. Al-Sultan**

5 **Khalid O. Al-Baltan**

6 **Mohammed A. Al-Madbel**

7 **Mohammed A. Angari**

8 **Khalifa A. Al-Mulhem**

9 **Mishari I. Al-Mishari**

Chairman's Statement

I have great pleasure in presenting Bank Aljazira's annual report and financial statements for the financial year ended 31 December 2008. The year was characterized by a dramatic downturn in global economies, which became especially evident during the third and fourth quarters and negatively affected the Bank's results.

However, I am pleased to report that our Retail Banking, Corporate Banking, Treasury, and Takaful businesses all performed strongly. This helped offset areas that experienced difficulties, particularly Brokerage, which was severely affected by poor trading conditions in the local and regional stock markets.

The degree to which the current economic turmoil has affected the Bank is evidenced by our net income which, at SR 222.3 million, is 72% lower than the previous year's SR 805.2 million. The decline is largely attributable to reduced total operating income (SR 310.3 million) and impairment provisions (SR 123.3 million), as well as increased expenses relating to staff, infrastructural, and administrative costs.

Despite the reduced net income, total assets grew by 28%, from SR 21.5 billion to SR 27.5 billion. Loans and advances increased by 53%, from SR 9.8 billion to SR 15.1 billion. Customer deposits increased at an even faster rate, by 34% from SR 15.6 billion to SR 20.9 billion, reflecting continued consumer confidence in the Bank. Shareholders' equity was largely unchanged at SR 4.63 billion (2007: SR 4.69 billion).

To further enhance the Bank's position leveraging the strong potential of the Saudi economy, we have adopted a new long-term strategy that aims to make Bank Aljazira a multi-specialist Shari'ah-compliant bank. This includes expansion of our branch network, provision of mortgage finance, and project and infrastructure funding.

Implementation of this strategy will be undertaken by world class experts and a highly-competent new management team, enabling the Bank to achieve the sustained growth to which we aspire.

During 2008, we continued to focus on Corporate Social Responsibility through our dedicated 'Khair Aljazira Le Ahl Aljazira' by initiating and sponsoring major social development programs in cooperation with reputable government and non-government philanthropic organizations. These programs are geared to help a vast number of needy families, as well as individuals. In addition, we have offered a variety of vocational training to hundreds of young Saudis giving them real opportunities for employment and more active participation in the development of the national economy.

I would like to thank our shareholders and customers for their trust and support, and thank the management and staff for their outstanding performance during an especially difficult year.

I extend my sincerest gratitude to almighty Allah and prayers upon our beloved messenger Mohammed – may peace be upon him and all his followers.

Taha Abdullah Al-Kuwaiz
Chairman

Chief Executive Officer's Foreword

The global credit crisis, difficult trading conditions, and shrinking liquidity confronted banks across the world during 2008. Similar to all other markets, the Saudi stock market has been affected. The volume of shares traded dropped sharply, resulting in lower revenues from investment brokerage activities. However, Bank Aljazira has successfully maintained its leadership in the brokerage market.

In the meantime, our other activities have experienced significant growth. We believe the Saudi economy is healthy and strong, showing vast growth potential and offering Bank Aljazira significant opportunities to diversify revenue sources.

With this in mind, and to take the Bank to the next level of operation, an ambitious strategy called the 'AFAQ-2012 Transformation Plan' has been developed with the support of first-class consultants. The plan was launched during a major staff convention in November 2008. It defines a list of strategic initiatives that will achieve our long-term vision of becoming a global center of excellence for Shari'ah-compliant finance by setting new standards and by being the crucible of innovative banking products and services. This will enable us to lead in developing Shari'ah-compliant banking solutions to capture the opportunities of today and beyond.

AFAQ-2012 identifies 13 strategic programs and five enablers that will be the cornerstones of our transformation over the next four years. We will expand our network from 24 to 105 branches and increase our sales effort by launching branch task forces and developing our alternative sales channels. We will also move strongly into the Kingdom's mortgage market and grow our consumer finance activities. In corporate banking, we will maintain our strong relations with large corporates by cross-selling multiple products. At the same time, we will seize the opportunity inherent with small to medium companies by developing relations with them and catering to their individual needs. We will also build two new business areas for real estate finance, as well as project and infrastructure finance.

Despite challenges in the brokerage market, we will continue targeting selected investors with tailored customer services, strive to retain existing customers with broader international offers, and expand our presence in the neighboring GCC markets.

We also intend to build a fully-fledged investment fund value proposition that will offer specialized asset management services to specific sectors of the market, and through agency expansion we will aggressively develop further growth in life takaful.

Those ambitious goals will require the building of comprehensive risk management capabilities and processes for the group, enhanced communication to promote Bank Aljazira's image as an innovative multi-faceted Shari'ah-compliant bank, mobilization of people, and selective upgrading of IT applications to support operational excellence and growth. Finally, we need to attract and retain targeted critical talents and mobilize energies through an organizational structure driven by the business units.

We are confident that by setting a clear vision and focused goals, we now have a well-planned strategic roadmap that defines a new organizational structure, sets up new corporate governance controls, enhances our risk management strengths, and identifies potential growth areas for each of our business units.

We have successfully upgraded the quality of our Trade Operations and ATM Services, and the Bank was ISO certified during 2008.

The year's achievements could not have been realized without the dedication of our employees, the support of the Board of Directors, and of course the loyalty of our shareholders and customers, to whom we all extend our grateful thanks.

Khalid Oudghiri
Chief Executive Officer

Executive Management

1 **Khalid Oudghiri**
Chief Executive Officer

2 **Ziad Aba Al-Khail**
Deputy Chief Executive Officer

3 **Sager Nadershah**
Head, Retail Banking Group

4 **Jad Zerouali**
Head, Transformation & Strategy Group

5 **Osama Al Jirafi**
Head, Human Capital Group

6 **Shahid Malik**
Chief Risk Officer

7 **Dr. Mohammed Al-Ghamdi**
Head, Sharia'h Group

8 **Mazen Abdulmajeed**
Senior Adviser to the CEO

9 **Ramiz Ferak**
Head, Treasury Group

10 **Peter Graham**
Head, Financial Services Group

11 **Hisham Al-Nasser**
Head, Corporate Banking Group

Bank Aljazira launches its new strategy AFAQ-2012

Bank Aljazira conducted a major staff convention in November 2008 to present AFAQ-2012, a transformation plan to restructure and become a multi-specialist Shari'ah-compliant bank by 2012, in the process diversifying revenue streams. It is noteworthy that Bank Aljazira converted its activities and operations to comply with Islamic Shari'ah rules in 2007. The convention was attended by the Bank's Chairman, a number of Directors and more than 900 staff from all regions of the Kingdom.

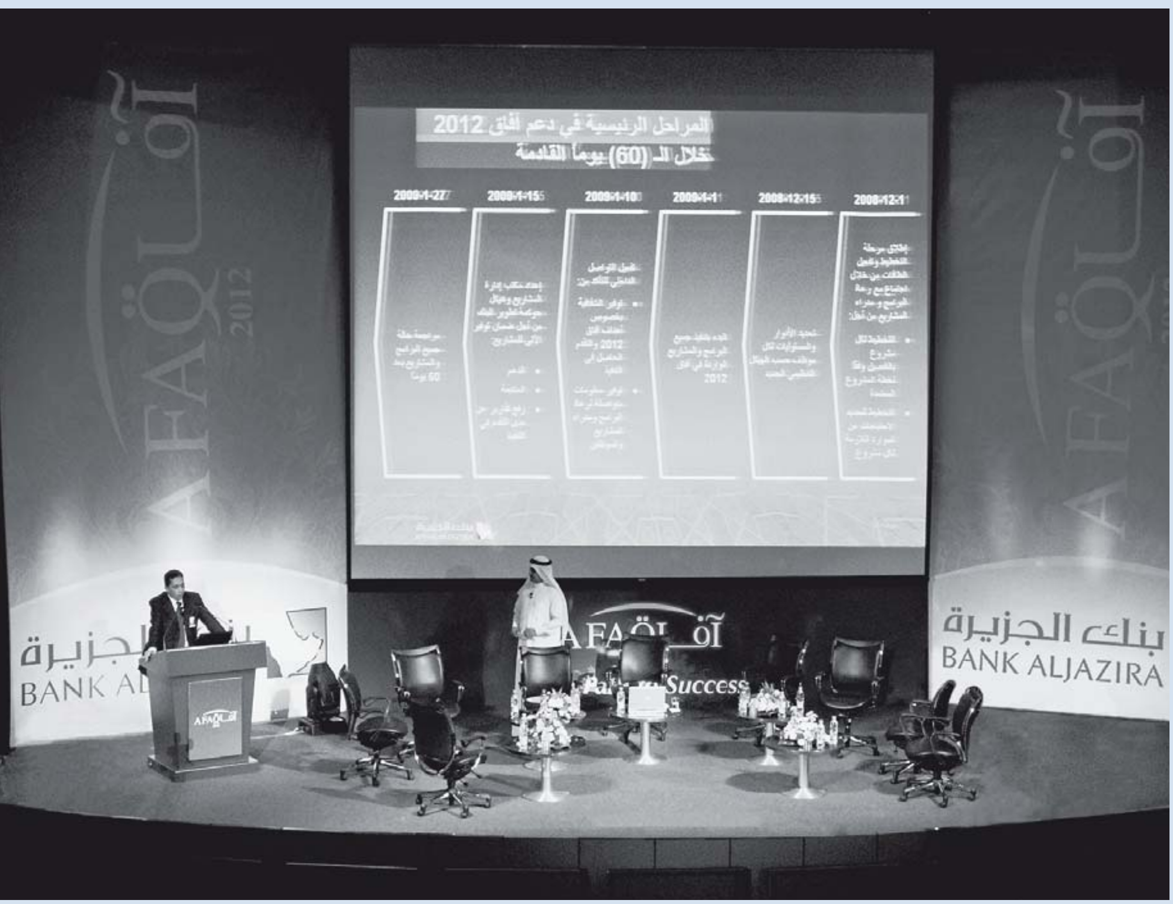
Mr. Taha Abdullah Al-Kuwaiz, Chairman, emphasized the importance of the next phase of the Bank's development and the vital role of human resources in successfully accomplishing the transformation process and achieving outstanding results.

In his presentation, Mr. Khalid Oudghiri, CEO, outlined how Bank Aljazira would focus on certain strategic services: Retail, where the Bank will expand its network and enhance offerings for mass affluent customers and small to medium size companies; Mortgages, where the Bank will seize exciting opportunities through an innovative 'multi channel factory' concept; Corporate, where the Bank will aim to capture an increasing share of the market's dynamic growth; Brokerage, where Aljazira Capital will build on market leadership achieved over recent years and expand its geographic reach; Asset management, where the capabilities will be further enhanced; and Takaful Ta'awuni, gaining full benefit from having been the first entrant into the Saudi market.

Mr. Oudghiri explained that the AFAQ-2012 plan was prepared following a study of the global financial crisis, considering opportunities that will arise in the Saudi market (which has not been significantly impacted) and its needs for products and services. In addition to diversifying revenue streams, the Bank will further strengthen its brand in areas where it excelled over past years.

He also asserted that the international crisis has supported the case for Bank Aljazira to grow into a multi-specialist Shari'ah-compliant bank, presenting a great opportunity for strategic investment and excellence in all banking fields. Mr. Oudghiri concluded his speech by saying "it is important to move forward and establish Bank Aljazira on more solid ground, so we are in a better competitive position to achieve our vision and aspirations, by the will of God".

AFAQ آفاق
2012



Board of Directors' Report

The Board of Directors is pleased to present the thirty second annual report on the Bank's activities for 2008, including the consolidated financial statements for the financial year ending 31 December 2008.

Financial Performance

2008 has proved to be a challenging year for the banking industry with turmoil in the international financial markets that reached to our region. Nonetheless, Bank Aljazira has shown resilience in weathering the global downturn and was successful in continuing its trend in diversifying income, growing its balance sheet, widening its customer base, expanding its market reach through alternative delivery channels, and decreasing its dependency on a single source.

Bank Aljazira continues its focused approach on growing the core banking operation, which has shown concrete results over the past few years as we consistently move away from dependency on one business line. Reflected in monetary terms, total operating income before share trading commissions, capital gains, Takaful fees and trading income from mutual funds increased from SR 237.8 million in 2004 to SR 782.8 million in 2008, as detailed in Table1 (page 11).

2008 has witnessed a 6% increase in net earnings from financing operations, which rose to SR 631.4 million despite the downward pressure on rates. This was a result of balancing the growth in commission earning assets at depressed rates with sources of funds in a competitive market thus having to finance the growth with costly time deposits. Furthermore, loan management fees and trade finance increased by 6% and 36% to reach SR 52 million and SR 21 million respectively. Other fees include mainly span fees which rose by 109%, reflecting the expansion of our ATM network to 314 ATMs. Exchange income had its share of success as it increased by 26% from 2007 to reach SR 22 million.

On the other hand, brokerage fees from local share trading decreased by 41% to reach SR 329 million. Despite the decrease in revenue, Bank Aljazira maintained throughout 2008 the first ranking in local stock market transaction services, in addition to regaining some market share compared to the end of 2007. Furthermore, the Bank posted a capital loss of SR 34 million compared to a capital gain of SR 103 million through divesting part of its direct investments in local equities. The Bank's trading portfolio, mainly mutual funds, posted a net loss of SR 34 million compared to a gain of SR 15 million during 2007.

As a result of the above, the total operating income decreased in 2008 by a net SR 310 million, or 21%, to reach SR 1,137 million.

In order to support the Bank's expansion under the 4-year strategic direction that was finalized during 2008, total operating expenses increased by 18%, only excluding provisions for credit losses, compared to the 27% increase during 2007.

In line with its conservative approach to mitigate and manage credit risks, the Bank booked a provision for credit losses of SR 61 million, compared to a net reversal of SR 26 million during 2007. The coverage against non-performing loans reached 164% during 2008 compared to 161% in 2007. Furthermore, the Bank booked SR 62 million as an impairment charge for its local equity portfolio.

Based on the above, the net income decreased by 72% to reach SR 222 million, compared to SR 805 million, while earnings per share decreased from SR 2.68 in 2007 to SR 0.74 in 2008.

TOTAL OPERATING INCOME BEFORE SHARE TRADING COMMISSIONS, CAPITAL GAINS, TAKAFUL FEES AND TRADING INCOME FROM MUTUAL FUNDS INCREASED FROM SR 237.8 MILLION IN 2004 TO SR 782.8 MILLION IN 2008.

Financial Position

During 2008, the Bank's total assets reached SR 27.5 billion, compared to SR 21.6 billion, representing an increase of 28% over 2007.

Placement with banks & other financial institutions reached SR 3.9 billion, an increase of 7% compared to last year. Investments were maintained at the same level, at SR 5 billion.

Loans and advances ended the year at SR 15.1 billion, a 53% increase over the SR 9.9 billion achieved in 2007, by diversifying the loan portfolio over various economic sectors and broadening the client base, thus lowering the concentration of risk.

Table 2 (opposite) highlights the growth achieved in the loan portfolio over the last five years. It also reflects the Bank's prudent approach in managing the credit risks inherent in the portfolio through the conservative credit monitoring and provisioning policy; whereby the non-performing loans to gross loans have decreased from 3.7% in 2004 to 1.5% in 2008, while the coverage of non-performing loans has developed over the years from below 100% coverage to a healthy 164%.

Client deposits have increased by 34% to a total of SR 20.9 billion, compared to SR 15.6 billion in 2007. Efforts were made to maintain the demand deposits at the level achieved during 2007 and to further grow our retail time deposits which increased between 2004 and 2008, from SR 889 million to SR 4,701 million respectively. Table 3 (opposite) illustrates the positive development in customer deposits between 2004 and 2008.

Shareholders' Equity

Shareholders' equity ended the year at SR 4,637 million and earning per share reached SR 0.74. The capital adequacy ratio calculated under Basel II for Tier 1 and Tier 2 reached 19.34% and 19.92% respectively for Pillar I risk weighted assets, which will enable the Bank to achieve its growth strategy.

Major Business Lines

Bank Aljazira's activities comprise five main lines: Personal Banking, Corporate Banking, Brokerage, Treasury, and Takaful. The Banks' services are conducted through a network of 24 branches in the main cities of the Kingdom. Table 4 (opposite) details information on assets, liabilities, total operating income, total operating expenses, and net profit for each sector.

The geographic distribution of income within the Kingdom is shown in Table 5 (opposite).

Retail Banking Group

As part of Bank Aljazira's program to expand its retail presence in strategic locations across Saudi Arabia, two branches were relocated in Riyadh – in North Olaya and Al-Sweidi as well as opening a ladies' section in Al-Nafl. More new branches are planned to open in 2009. The ATM network also expanded, with 47 machines added, all using the new EMV technology, bringing the total to 314.

To support the Bank's growing network and underpin our customer focus, the Retail Banking Group has been reorganized. This has enhanced marketing capabilities, created a new department for segment management, and merged call centers into a single centralized and multi-functional unit.

During the year, our range of Shari'ah-compliant products and services was expanded with the introduction of the Maysara Visa Card and the launch of a strengthened real estate product branded 'Ejara'.

Our ability to deliver innovative Shari'ah-compliant products was underlined by rapid expansion of our customer base, which increased by about 30% during 2008 with a corresponding growth in deposits and assets.

Corporate Banking Group

Corporate Banking has maintained a stable and growing customer base, evidenced by the 50% growth in corporate lending during 2008. A new exporters' Murabaha product was launched, and account relationships were reorganized, with particular focus on better serving the mid-corporate and large company segments. Cross selling has also been strengthened through joint customer calling activities.

Two new divisions were formed – Real Estate & Project Finance, and E-Banking & Cash Management – to broaden the Bank's range of services.

In other organizational changes, the first of three regional Corporate Centers was established in Jeddah, improving the Bank's distribution capabilities. Facilities at these centers include trade finance, operations, and credit control. Work is under way on two similar centers in Riyadh and Al-Khobar, to be completed in early 2009.

Syndicated facilities were a prime contributor to the increase in corporate transactions. We participated as facility agent in the Hajj terminal project at King Abdul Aziz International Airport, and in recognition received the 2008 Euromoney Project Finance Award.

TABLE 1: **FINANCIAL PERFORMANCE – CORE BANKING PERFORMANCE**

SR'000	2004	2005	2006	2007	2008
Special commission income	317,347	530,911	749,677	908,968	1,114,431
Special commission expenses	(129,421)	(254,499)	(273,030)	(313,847)	(483,010)
Net special commission income	187,926	276,412	476,647	595,121	631,421
Fees from banking services:					
Loan commitment and management fee	10,009	22,341	31,797	48,897	51,617
Trade finance	9,556	12,626	13,733	15,528	21,072
Others	2,628	2,531	8,625	20,371	42,607
Total fees	22,193	37,498	54,155	84,796	115,296
Exchange income	3,132	4,794	6,563	17,232	21,708
Dividend income	16,055	15,026	13,377	12,385	11,532
Other operating income	8,524	379	5,424	5,673	2,806
Total operating income	237,830	334,109	556,166	715,207	782,763
Growth over previous year (%)	19.7%	40.5%	66.5%	28.6%	9.4%

TABLE 2: **FINANCIAL POSITION**

	2004	2005	2006	2007	2008
Loans and advances, net (SR millions)	5,187	6,911	6,271	9,879	15,133
% growth of net loans	11.3%	33.2%	(9.3%)	57.5%	53.2%
Non-performing loans to gross loans (%)	3.7%	2.8%	3.1%	2.0%	1.5%
Provision coverage of non-performing loans (%)	111.8%	176.9%	172.6%	161.1%	163.9%

TABLE 3: **CUSTOMER DEPOSITS**

SR millions	2004	2005	2006	2007	2008
Demand deposits	2,525	4,898	6,394	5,544	5,322
Time deposits					
Time deposits (Corporate)	4,571	4,463	2,019	6,372	10,701
Time deposits (Retail)	889	1,195	2,316	3,126	4,701
Total time deposits	5,460	5,658	4,335	9,498	15,402
Others	157	260	188	605	176
Total customers' deposits	8,142	10,816	10,917	15,647	20,900
% growth of customers' deposits	8.1%	32.8%	0.9%	43.3%	33.6%

TABLE 4: **SUMMARY FINANCIAL STATEMENT**

SR'000	Personal Banking	Corporate Banking	Brokerage	Treasury and others	Total
Total assets	2,562,374	13,119,473	539,620	11,298,238	27,519,705
Total liabilities	9,447,032	2,999,789	31,135	10,303,926	22,781,882
Total operating income	311,507	442,972	334,567	47,498	1,136,544
Charge for provision for credit losses, net	(10,125)	(51,033)	-	-	(61,158)
Impairment of other financial assets	-	-	-	(62,238)	(62,238)
Depreciation	(34,936)	(6,110)	(20,812)	(13,082)	(74,940)
Total operating expenses and minority interests	(287,660)	(180,677)	(242,310)	(203,558)	(914,205)
Net income	23,847	262,295	92,257	(156,060)	222,339

TABLE 5: **DISTRIBUTION OF INCOME WITHIN SAUDI ARABIA**

SR'000	Central	Eastern	Western	Head Office	Total
Total operating income	434,195	250,199	344,511	107,639	1,136,544
Total operating expenses and minority interests	(116,867)	(43,041)	(74,975)	(555,926)	(790,809)
Net operating income	317,328	207,158	269,536	(448,287)	345,735
Charge for provision for credit losses, net	(2,737)	(765)	(25,052)	(32,604)	(61,158)
Impairment of other financial assets	-	-	-	(62,238)	(62,238)
Net income	314,591	206,393	244,484	(543,129)	222,339

Treasury
The year was very challenging as a result of the global credit crisis and tighter liquidity in the market. In these conditions, the challenge was to balance assets and liabilities growth. The Bank succeeded in generating more than 50% of its liabilities as the core source of funding. We grew our market share of fixed-term customer deposits, mainly as a result of strong growth in Shari'ah-compliant deposits. A widening depositor base and successful marketing of long-term funding tools resulted in the average life of customer deposits being extended from 50 to 87 days.

The Bank's investment portfolio yield improved to 4.21%, 105 basis points above the one-month Sibor average. More than 80% of this portfolio is in Murabaha with the Saudi Arabian Monetary Agency (SAMA), with a repo advantage of up to 75% of the volume.

Other highlights included: foreign exchange profitability increasing by 26%; Thrift Saving Plan volume growth of 61%; Naqa'a fixed deposits volume growth of 67%; and Naqa'a long-term volume growth of 410%.

Aljazira Capital
Aljazira Capital formally began operations in April 2008, with a license to engage in all five securities business lines recognized by the Capital Market Authority (CMA): dealing, managing, arranging, advisory, and custody.

The year was pivotal for maintaining Aljazira Capital's leadership in an increasingly competitive market. More than 30 brokers were operational by the year-end, up from 21 a year earlier. Initially the increase in competition had an adverse impact on our market share, dropping to an all-time low of 17% in May. However, this was swiftly addressed with the introduction of a new sales and performance management structure and customer relationship management tools, resulting in steady growth to about 21% by the year-end.

During the year, an institutional trading desk was introduced that provides clients with trading solutions through a dedicated relationship management team and brokers. This contributed to attracting several regional institutional investors.

Other achievements included:

- Issuing our first company report in May,
- Introducing our GCC and US market reports, as well as the new Morning Briefing on global markets,
- Adding Kuwait Stock Exchange to our list of trading markets in the MENA region,
- Upgrading the international brokerage system as part of a plan to enhance, MENA and international brokerage services,
- Implementing an IPO Management solution.

2009 will be a challenging year due to the prevailing global economic conditions. Nevertheless, Aljazira Capital intends to grow and diversify its business, as well as streamlining and optimizing its operations.

Takaful Ta'awuni
Takaful Ta'awuni has focused on maintaining its leadership position in Shari'ah-compliant insurance and financial services, in the midst of heightened competition in the Saudi market. A highlight of 2008 was the progress made, in close liaison with the Saudi Arabian Monetary Agency, to spin-off the division as a separate entity with its own license. In addition, a partnership agreement was signed with one of the world's largest Retakaful companies. This added significant value to the core underwriting function, drawing on the partner company's wealth of experience.

Revenue from agency distribution grew 48% during the year. While this channel continues to be a main driver of the business, we expanded strategically by opening additional sales centers in Madinah, both men's and ladies' branches, and a new ladies' branch in Dammam.

The year also saw 53% growth in annualized premium income, 51% group sales business growth, and 44% growth for Wakalah fee income. Significantly, in 2008 Takaful Ta'awuni crossed the key threshold of 30,000 individual customer contracts.

The continued development of innovative new products is an integral component of Takaful Ta'awuni. During the year a new Takaful Mortgage Protection Plan was developed, offering cover against disability and death, as well as a stand-alone Shari'ah-compliant alternative to conventional personal accident plans.

Takaful Ta'awuni's achievements were recognized when it received the Euromoney Islamic Finance Award for 'Best Life Takaful Provider 2008', and the Middle East Insurance (Insurex) Award for 'Life Insurer of the Year 2008'.

CORPORATE BANKING HAS MAINTAINED A STABLE AND GROWING CUSTOMER BASE, EVIDENCED BY THE 50% GROWTH IN CORPORATE LENDING DURING 2008. A NEW EXPORTERS' MURABAHA PRODUCT WAS LAUNCHED, AND ACCOUNT RELATIONSHIPS WERE REORGANIZED, WITH PARTICULAR FOCUS ON BETTER SERVING THE MID-CORPORATE AND LARGE COMPANY SEGMENTS.

TO TAKE THE BANK TO THE NEXT LEVEL OF OPERATION, MANAGEMENT HAS EMBARKED ON AN AMBITIOUS TRANSFORMATION PLAN CALLED AFAQ-2012, WHICH DEFINES A LIST OF STRATEGIC INITIATIVES DESIGNED TO ACHIEVE OUR LONG-TERM VISION TO BECOME A MULTI-SPECIALIST SHARI'AH-COMPLIANT BANK BY THE YEAR 2012.

Support Group
During 2008, Support Group continued to focus on the Bank's infrastructure upgrade in line with the number of branches, ATMs, products, customers, and transactions.

Upgrading the network, reorganizing stored information, and introducing blade technology have improved the efficiency of the infrastructure. Consolidating internal call centers into a single unit led to better usage of resources and services provided. The MPLS network was implemented, with higher bandwidth reducing communication costs.

During the year, a number of operational excellence initiatives enhanced the quality management system by having all operations activities ISO certified. Certification was completed for the remote ATM network and Trade operations. The remaining activities will achieve certification in line with priorities set under the AFAQ-2012 plan.

The focus on process re-engineering, automation, and paperless initiatives continued. Information systems and security were enhanced during the year, while logistics and procurement procedures were re-engineered to achieve better flexibility and cost effectiveness.

The functionality of the Bank's TadawulCom (online local share trading) portal has been improved, maintaining its market leadership in trading value and volume. Harnessing the latest technology has increased the capacity of all electronic delivery channels, including AlJaziraOnline and ATM Switch.

Risk Management Group
Risk Management plays a key role in supporting the business units in achieving their financial targets within the defined risk appetite. It is also involved in developing new products and ventures that help to strengthen the Bank's franchise. Effective risk control tools and risk mitigation techniques have protected the Bank against various risks and resulted in a relatively low ratio of non-performing loans.

During 2008, Risk Management was reorganized to meet the challenges of the AFAQ-2012 plan. Key objectives were to consolidate key risk functions and take a prudent approach to managing risks; to provide acute focus on key risk areas, especially when they span different products or businesses; to streamline functions and improve response times; and to take a proactive approach to risk origination, risk management, and risk differentiation. The new structure will provide the Bank with enhanced capabilities to identify, evaluate, and manage risks consistent with the Basel II accords and SAMA guidelines.

Internal Audit Group
Internal Audit's role is to assist the Board and senior management by evaluating the processes of risk management, internal control and governance. The group provides analysis, recommendations and information to safeguard the Bank's assets and protect the interests of shareholders, customers, directors and employees.

In 2008, Internal Audit was completely reorganized under a new management team and with additional staff. New audit software was successfully implemented to improve customer account monitoring.

In addition, the number and scope of audits was increased. A Special Fraud Investigation unit was established and its policies defined, while several significant changes to products and policies were reviewed and recommended.

Strategic Management
To take the Bank to the next level of operation, management has embarked on an ambitious transformation plan called AFAQ-2012, which defines a list of strategic initiatives designed to achieve our long-term vision to become a multi-specialist Shari'ah-compliant bank by the year 2012. A Transformation and Strategy Group has been mandated to ensure effective implementation and delivery of all projects, monitor the changing economic environment, and identify potential business opportunities.

The Group consists of:

- The Strategy team, which is in charge of identifying and analyzing business opportunities and recommending appropriate initiatives that will boost the Bank's profitability;
- The Transformation team, which controls and monitors AFAQ-2012 projects through the Program Management Office. It also identifies the processes to be optimized to offer a better quality of services to customers and improve our profitability through the Business Process Re-engineering function. The Transformation team also monitors quality across the Bank through the Quality Management function.

TABLE 6: **CREDIT RATINGS**

	Capital Intelligence	Moody's	Fitch
Foreign Currencies Risk (Short Term)	A2	A3	F2
Foreign Currencies Risk (Long Term)	A-	A3	A-
Financial Strength Rating	A-	D+	C
Support Rating	2		1
Outlook	Stable	Stable	Stable
Sovereign Risks (Short Term)	A1+		A+
Sovereign Risks (Long Term)	AA-		A+

TABLE 7: **STATUTORY APPROPRIATIONS**

	SR millions
Zakat payable by Saudi shareholders	15.3
Income tax payable on non-Saudi shareholdings	2.2

Compliance Group
During 2008, the Anti-Money Laundering division was restructured with redefined staff responsibilities, policies and procedures were updated, and 'Know Your Customer' and customer acceptance policies were enhanced. New systems were also implemented to improve the effectiveness of monitoring customer transactions. All measures were designed to protect the Bank from potential risks arising from unlawful activities.

The Regulatory Compliance function has also been reorganized in line with new guidelines issued by the Saudi Arabian Monetary Agency (SAMA).

Credit Ratings

Table 6 (above) illustrates the credit ratings achieved by the Bank.

Dividend Policy

The Board of Directors has recommended the distribution of a net cash dividend of SR 0.50 per share (after deduction of Zakat) – for a gross total of SR 170.1 million.

Statutory Appropriations

The statutory payables in 2008 are shown in Table 7 (above).

Long-Term Borrowing

There were no long-term borrowings in 2008 and 2007.

Bank Dealings with Board Members, Chief Executive Officer and Chief Financial Officer

Notwithstanding, the information included in Note 34 in the Audited Financial Statements "Related Party Transactions" that have been conducted according to the same terms and conditions as transactions with independent third parties, there are no substantial interests for the Board members, the Chief Executive Officer or Chief Financial Officer.

Corporate Governance

The Bank endeavors to fully comply with corporate governance rules, which ensure strict application of internal controls and transparency policies, as well as rigid adherence to risk management principles. In conducting its business, the Bank ensures comprehensive and consistent compliance with all the rules and regulations promulgated in the Kingdom of Saudi Arabia and all the directives issued by SAMA and the CMA, as well as the Basel II Committee requirements.

In accordance with Article 1 Section (C) and Article 9 Section (A) of the Corporate Governance Regulations in the Kingdom of Saudi Arabia issued by the CMA, Bank Aljazira has implemented all rules and regulations except for Article 6 Section (B) relating to Cumulative Vote, whereby the Bank is in the process of reviewing the possibility of application in the future. All other clauses and sections relating to the rules and regulations of corporate governance have been integrated into the Corporate Governance manual of the Bank.

These policies have been substantially detailed in order to guarantee compliance while allowing for development and adjustments whenever necessary through the Board of Directors. During 2008, the Bank was charged by SAMA and various municipalities' fines totaling SR 71,005.

A) Board of Directors
The Board of Directors consists of nine members, independent/executive, and non-executive, who regularly attend the Board's meetings. During 2008, the Board held three meetings (four meetings during 2007) as detailed in Table 8 (page 16).

In general, the Board monitors the performance and progress of the Bank through regular meetings held throughout the year. The Board establishes general policies, ensures their proper implementation, and regularly reviews the effectiveness of regulations and internal controls. The Board monitors all areas of the Bank's operations to ensure proper application of policies and monitors risk levels to ensure that they are satisfactorily managed.

Through the Review Committee, the Board of Directors reviews the Bank's financial position with the external auditors to ensure sound financial performance and to guarantee full compliance with rules, regulations, and accounting standards of Saudi Arabia. The Board assumes the statutory responsibility for the validity of financial statements and ensures they fairly reflect the Bank's financial position and operational results, and compliance with the Shari'ah Controls as set-up by the Bank's Shari'ah Board.

Bank Aljazira's Board Directors maintain memberships in the Saudi stock companies as listed in Tadawul System on 31 December 2008. See Table 9 (page 16).

Board of Directors' Report continued

TABLE 8: **BOARD OF DIRECTORS – MEETINGS ATTENDANCE**

Name	Functional duties	Category of membership	Meetings attended
Mr. Taha A. Al-Kuwaiz	Chairman of the Board	Independent / executive	3
Mr. Abdullah S. Kamel	Member of the Board	Independent / non-executive	1
Eng. Tarek O. Al-Kasabi	Member of the Board	Independent / non-executive	3
Eng. Abdul Majeed I. Al-Sultan	Member of the Board	Independent / non-executive	3
Mr. Mohammed A. Angari	Member of the Board	Independent / non-executive	3
Mr. Mohammed A. Al-Madbel Representative of the General Organization of Social Insurance	Member of the Board	Independent / non-executive	3
Mr. Khalid O. Al-Baltan	Member of the Board	Independent / non-executive	3
Mr. Khalifa A. Al-Mulhem	Member of the Board	Independent / non-executive	2
Mr. Mishari I. Al-Mishari	Member of the Board	Independent / executive	3

TABLE 9: **BOARD OF DIRECTORS – MEMBERS**

Director's Name	Company Name
Mr. Taha A. Al-Kuwaiz	None
Mr. Abdullah S. Kamel	1. Aseer Company – Board Chairman 2. Saudi Research Group – Board Member 3. Emaar Economic City Company – Board Member 4. Hulwani Ekhwan Company – Board Member
Eng. Tarek O. Al-Kasabi	1. Aseer Company – Board Member
Eng. Abdul Majeed I. Al-Sultan	1. Tabouk Cement Company – Board Member
Mr. Mohammed A. Angari	1. Saudi Hotels Company – Board Member
Mr. Mohammed A. Al-Madbel Representative of the General Organization of Social Insurance	1. National Gas & Industrialization Company – Board Member
Mr. Khalid O. Al-Baltan	1. Ahsa Development Company – Board Chairman
Mr. Khalifa A. Al-Mulhem	1. Advanced Polypropylene Company – Board Chairman 2. Nama Chemical Company – Board Member 3. Wala'a Insurance Company – Board Member
Mr. Mishari I. Al-Mishari	None

TABLE 10: **MAJOR SHAREHOLDERS EXCLUDING BOARD DIRECTORS**

At the beginning of the year		During the year *		At the year end	
No. of shares	% ownership against share capital 225,000,000	Net change in shares	% of change	Total ownership	% ownership against share capital 300,000,000
82,919,570	36.85%	26,375,483	31.81%	109,295,053	36.43%

TABLE 11: **CHANGE IN PERCENTAGE OF BANK SHAREHOLDINGS FOR BOARD DIRECTORS, SENIOR EXECUTIVES, THEIR SPOUSES AND UNDERAGE**

At the beginning of the year		During the year *		At the year end	
No. of shares	% ownership against share capital 225,000,000	Net change in shares	% of change	Total ownership	% ownership against share capital 300,000,000
51,775,368	23.01%	15,212,662	29.38%	66,988,030	22.33%

* The General Assembly held on 10/04/1429H (i.e. 16/04/2008) approved on the recommendation of the Bank's Board of Directors to increase the Bank's capital from SAR 225,000,000 to SAR 300,000,000.

TABLE 12: **THE EXECUTIVE COMMITTEE**

Name	Functional Duties	Meetings Attended
Mr. Taha A. Al-Kuwaiz	Chairman	10
Eng. Tarek O. Al-Kasabi	Member	10
Eng. Abdul Majeed I. Al-Sultan	Member	10
Mr. Khalifa A. Al-Mulhem	Member	7

TABLE 13: **THE AUDIT COMMITTEE**

Name	Functional Duties	Meetings Attended
Eng. Abdul Majeed I. Al-Sultan	Chairman	5
Mr. Salman M. Hassan Al Jishi	Member	4
Dr. Saleh J. Malikah	Member	4
Mr. Faraj M. Abu-Thenian	Member	2

TABLE 14: **THE COMPENSATION COMMITTEE**

Name	Functional Duties	Meetings Attended
Mr. Taha A. Al-Kuwaiz	Chairman	2
Eng. Tarek O. Al-Kasabi	Member	2
Eng. Abdul Majeed I. Al-Sultan	Member	2
Mr. Mohammed A. Al-Angari	Member	2

TABLE 15: **COMPENSATION PAID TO THE BOARD OF DIRECTORS AND TOP 5 EXECUTIVE MANAGEMENT**

SR'000	Executive Board Members	Non-executive Board Members	Top 5 Executive Managers including the CEO & CFO
Salaries	4,500.0	-	11,481.3
Allowances	57.1	340.3	809.3
Bonus	480.0	1,680.0	3,770.0
Incentives	-	-	7,418.2
Total Compensation	5,037.1	2,020.3	23,478.8

B) Board Committees

In response to statutory requirements and to ensure optimum performance and utilization of the expertise of Board members, the following principal supporting committees were established:

1. The Executive Committee

The Executive Committee comprises Directors elected by the Board and is presided over by the Chairman of the Board. The Committee's terms of reference are determined by the Board of Directors. It is responsible for implementing policies laid down by the Board and Risk Management and Performance Control Department. The Committee ensures policies are properly implemented, and that internal controls are effective.

The Board of Directors in their meeting held on 25/11/1427 AH (16 December 2006) established the Executive Committee, which held ten meetings during 2008 (2007: eight meetings) attended as detailed in Table 12 (opposite).

2. The Audit Committee

The Audit Committee plays a vital and important role in assisting the Board of Directors to fulfill their statutory financial and accounting responsibilities. The Committee reviews risk limits and audit duties, and liaises with the Bank's external auditors. On a quarterly basis, the Committee reviews financial statements and assists the Board of Directors in annual assessments of the effectiveness of internal control, in identifying potential risks, and establishing strategic plans to address such risks.

The results of the annual review of the effectiveness of the interim control procedures reflects an excellent level of compliance as the Bank adopts all the requirements set forth by the regulators and the best practices followed internationally.

The Audit Committee comprises a Chairman, selected by the Board of Directors from the non-executive Board members, and three independent members from outside the Bank. Meetings are attended regularly by the Bank's Head of Internal Audit and the Financial Controller, and the Chief Executive Officer and Senior Executives, when required. The Committee was formed on 31 May 2007. During 2008, the Committee held five meetings (2007: seven meetings). These meetings were attended as shown in Table 13 (opposite).

3. The Compensation Committee

Upon the issuance of the Bank's governance rules, this Committee was formed as per the Bank's governance rules Appendix (F) stipulating the Committee's structure and terms of reference based on the CMA's governance rules and regulations.

The General Assembly, in its meeting No. 42 dated 10/01429 AH (16 April 2008), endorsed the selection criteria and functions of the Committee as per Article (15) issued by the CMA and recommendations of the Board of Directors.

During 2008, the Committee held two meetings attended as shown in Table 14 (opposite).

C) Payments to Board Members and Executive Management

The Bank pays meeting attendance expenses and remuneration to Directors and Board Committee members. During 2008, these payments to Board members and the total remunerations paid to the top five Executive Managers including the Chief Executive Officer and the Chief Financial Officer are detailed in Table 15 (above).

D) Internal Controls and Risk Management Procedures

Bank Aljazira constantly reviews and assesses risk exposures including financial, banking operations, investment, credit, liquidity, commission rate and other risks, which are considered inherent in a banking operation. The Bank also ensures the functional separation of risk management. Accordingly, the Bank takes corrective and precautionary actions to minimize potential losses.

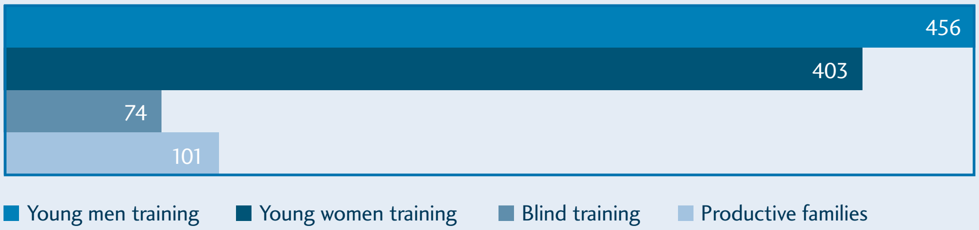
The Bank relies on an integrated system of management organizations, control procedures and administrative reports, as follows:

- Executive Management Committee
- Credit Committee
- Assets and Liabilities Management Committee
- Shari'ah Supervisory Board
- The Schedule of Authorities
- Internal audit programs
- Annual budget and performance benchmarking reports
- Periodic financial reports
- Departmental polices and procedures
- Treasury reports
- Credit oversight controls
- Risk management oversight on business activities
- Automation or work flows

THE FUNCTIONALITY OF THE BANK'S TADAWULCOM (ONLINE LOCAL SHARE TRADING) PORTAL HAS BEEN IMPROVED, MAINTAINING ITS MARKET LEADERSHIP IN TRADING VALUE AND VOLUME. HARNESSING THE LATEST TECHNOLOGY HAS INCREASED THE CAPACITY OF ALL ELECTRONIC DELIVERY CHANNELS, INCLUDING ALJAZIRAONLINE AND ATM SWITCH.

‘KHAIR ALJAZIRA LE AHL ALJAZIRA’ PROGRAM

Number of people benefiting



E) External Auditors
The external auditors are responsible for auditing Bank Aljazira’s final accounts and financial statements. At its 42nd meeting on 10/4/1429 AH (16 April 2008), the General Assembly resolved to appoint Ernst & Young and Al-Juraid and Associates as the official auditors of the Bank’s accounts for 2008.

Social Responsibility

Bank Aljazira pays special attention to the communities that it serves. Through the dedicated ‘Khair Aljazira Le Ahl Aljazira’ program, the Bank implements a range of activities designed to support less advantaged sections of the community.

In 2008 the Bank provided financial assistance to various charitable societies and launched an apprenticeship program to train young Saudi men and women, also providing them with work opportunities following completion of the training. In supporting the handicapped, Bank Aljazira shared in training the blind on computer skills through a program called ‘Tamouh’ and established computer labs to assist them in utilizing advanced technology.

To promote family welfare, the Bank sponsored a number of small projects for productive families, including those that trained girls on computer skills, tailoring, knitting, weaving, and other crafts. In addition, the Bank sponsored a number of cultural events, scientific activities, forums, seminars, and local and international lectures related to Islamic banking and economics.

The ‘Khair Aljazira Le Ahl Aljazira’ program also participated in social and cultural events, as well as various national activities. These included sponsorship of a social event during Ramadan for the Orphans’ charity, ‘Insan’, in addition to supporting the Prince Salman Center for Disability Research, for its vital role in serving disabled people in the Kingdom.

‘Khair Aljazira Le Ahl Aljazira’ is geared to serve all sections of the Saudi community. During the year, 456 young men, 403 young women and 101 families with special needs benefited. Bank Aljazira’s financial commitment to the program exceeded SR 2.3 million during 2008, in addition to SR 590,000 disbursed via other charity channels during the year.

Gratitude

The Board of Directors would like to take this opportunity to express their thanks and gratitude for the wise vision of the government under the leadership of the Custodian of the Two Holy Mosques, King Abdullah Bin Abdulaziz Al-Saud, and to His Royal Highness, Prince Sultan Bin Abdulaziz Al-Saud, the Crown Prince, Deputy Prime Minister, Minister of Defense and Aviation and Inspector General.

We also extend sincere thanks to the Ministry of Finance and National Economy, the Ministry of Commerce and Industry, the Saudi Arabian Monetary Agency and the Saudi Capital Market Authority for their constructive directives, consideration and continued support of the Bank’s progress.

Finally, we take this opportunity to extend our heartfelt thanks and appreciation to our shareholders, customers and associates for their confidence and support. We would also like to reiterate our appreciation of our management and staff for their devotion and dedication, without which we would not have achieved these excellent results.

Board of Directors

Shari'ah Advisory Board Report

Shk. Abdulla Bin Suleiman Al-Mane'e
Chairman

Dr. Mohammed Bin Said Al-Ghamdi
Rappoteur

Dr. Abdulla Bin Mohammed Al-Mutlaq
Member

Dr. Hamza Bin Hussain Al-Fa'ar
Member

Dr. Mohammed Ali Al-Gari
Member

Dr. Abdulsattar Abu Ghuda
Member

Praise be to Allah, and peace be upon his faithful messenger, Mohammed bin Abdullah, and upon his companions.

By the 1st of Muharam 1428H (i.e. 20 January 2007) Bank Aljazira Shari'ah Board met to review whatever arrangements taken to complete the Bank's Conversion into Islamic Banking.

Based on the Board's comprehensive review of the reports presented by the Bank's respective authority and based on the activities performed by the Bank to that extent, the Board is sure that Bank Aljazira has executed the Conversion into Islamic Banking Program as approved by the Shari'ah Board. Thus, all Bank Aljazira's operations and activities are fully converted into practices compliant with the Islamic Shari'ah.

Therefore, the Shari'ah Board declares that as of today Bank Aljazira has completed the Conversion into Islamic Banking Program and deems that Bank Aljazira is becoming an Islamic Bank with all features of Islamic Banking. The Shari'ah Board wishes that Bank Aljazira, by this effort, would present an example for other banks to emulate so as to fully convert into Islamic Banking.

With this declaration, Bank Aljazira's Shari'ah Board is applauding all grateful efforts exerted by the Bank's management and staff, and would like to take this opportunity to appreciate the continuous and on-going support of the Government of The Custodian of The Two Holy Mosques represented by the Saudi Arabian Monetary Agency and other respective authorities, with prayers to ALLAH, the Source of All Good, to grant continuous success and progress to all.

Translated from Arabic

Network

بنك الجزيرة
BANK ALJAZIRA

WESTERN REGION

ATM LOCATIONS: 124

Makkah Mukarama

Makkah Mukarama-Aziziah Branch
Tel: (+966) 2 557 1010
Fax: (+966) 2 553 1655

Makkah Mukarama Branch
Tel: (+966) 2 559 1000
Fax: (+966) 2 559 1142

Madinah Munawara

Madinah Munawara Branch
Tel: (+966) 4 845 1111
Fax: (+966) 4 845 1953

Madinah Munawara Branch (Ladies)
Tel: (+966) 4 845 1956
Fax: (+966) 4 845 1952

Jeddah

Prince Sultan St. Branch
Tel: (+966) 2 607 5450
Fax: (+966) 2 607 5450
Ext. 208

Prince Sultan St. Branch (Ladies)
Tel: (+966) 2 607 0828
Fax: (+966) 2 607 0125

Tahlia St. Branch
Tel: (+966) 2 668 5050
Fax: (+966) 2 663 7084

Tahlia St. Branch (Ladies)
Tel: (+966) 2 669 4469
Fax: (+966) 2 665 3416

Al Musa'adia Branch
Tel: (+966) 2 661 0120
Fax: (+966) 2 661 0108

Al Musa'adia Branch (Ladies)
Tel: (+966) 2 667 3700
Fax: (+966) 2 226 2600

Al Balad Branch
Tel: (+966) 2 648 5533
Fax: (+966) 2 648 4599

Khalid Bin Al-Waleed St. Branch
Tel: (+966) 2 651 8070
Fax: (+966) 2 651 8070
Ext. 1012

Al Nahda Branch
Tel: (+966) 2 609 8500
Fax: (+966) 2 234 6838

Al Nahda Branch (Ladies)
Tel: (+966) 2 609 8520
Fax: (+966) 2 234 7227

CENTRAL REGION

ATM LOCATIONS: 85

Riyadh

Olaya Branch
Tel: (+966) 1 215 7000
Fax: (+966) 1 215 7016

Olaya Branch (Ladies)
Tel: (+966) 1 215 7074
Fax: (+966) 1 215 7052

King Fahd Road Branch
Tel: (+966) 1 225 6000
Fax: (+966) 1 225 6151

King Fahd Road Branch (Ladies)
Tel: (+966) 1 225 6161
Fax: (+966) 1 225 6166

Al-Suwaidi Branch
Tel: (+966) 1 433 8441
Fax: (+966) 1 430 3682

Uqba Bin Nafe'a Branch
Tel: (+966) 1 278 1416
Fax: (+966) 1 278 4616

Uqba Bin Nafe'a Branch (Ladies)
Tel: (+966) 1 278 4387
Fax: (+966) 1 278 4359

Khurais Road Branch
Tel: (+966) 1 225 6399
Fax: (+966) 1 225 6399
Ext. 2021

Al Rayyan Branch
Tel: (+966) 1 208 0166
Fax: (+966) 1 208 0166
Ext. 210

Al Rayyan Branch (Ladies)
Tel: (+966) 1 208 5366
Fax: (+966) 1 208 0166
Ext. 258

Dahrat Al-Badiah Branch
Tel: (+966) 1 428 9269
Fax: (+966) 1 449 3064

Dahrat Al-Badiah Branch (Ladies)
Tel: (+966) 1 428 8309
Fax: (+966) 1 428 8735

King Abdullah St. Branch
Tel: (+966) 1 207 1460
Fax: (+966) 1 207 1362

King Abdullah St. Branch (Ladies)
Tel: (+966) 1 269 6228
Fax: (+966) 1 269 3650

Al-Nafl Branch
Tel: (+966) 1 275 1086
Fax: (+966) 1 274 1507

Al-Nafl Branch (Ladies)
Tel: (+966) 1 275 1086
Fax: (+966) 1 275 1086
Ext. 450

Qasim

Buraidah Branch
Tel: (+966) 6 383 5310
Fax: (+966) 6 383 5306

Onaizah Branch
Tel: (+966) 6 361 7547
Fax: (+966) 6 361 8412

EASTERN REGION

ATM LOCATIONS: 105

Dammam

Dammam Branch
Tel: (+966) 3 832 1272
Fax: (+966) 3 834 3314

Al Khobar

Al-Hada District Branch
Tel: (+966) 3 882 0040
Fax: (+966) 3 887 8653

Al-Hada District Branch (Ladies)
Tel: (+966) 3 882 8848
Fax: (+966) 3 882 8722

King Abdul Aziz Road Branch
Tel: (+966) 3 867 6707
Fax: (+966) 3 867 6923

Jubail

Jubail Industrial City Branch
Tel: (+966) 3 347 1386
Fax: (+966) 3 347 1426

Qateef

Qateef Branch
Tel: (+966) 3 854 5463
Fax: (+966) 3 854 5367

Qateef Branch (Ladies)
Tel: (+966) 3 852 9900
Fax: (+966) 3 852 9877

Al-Ahsa

Al Hofuf Branch
Tel: (+966) 3 586 3555
Fax: (+966) 3 584 3111

الجزيرة كابيتال
ALJAZIRA CAPITAL الجزيرة للأسواق المالية

WESTERN REGION

Makkah Mukarama
Makkah Mukarama-Aziziah Center
Tel: (+966) 2 557 2250

Makkah Mukarama Center
Tel: (+966) 2 559 1000

Madinah Munawara
Madinah Munawara Center
Tel: (+966) 4 845 2345

Madinah Munawara Center (Ladies)
Tel: (+966) 4 845 1956

Jeddah
Prince Sultan St. Center
Tel: (+966) 2 607 1970

Prince Sultan St. Center (Ladies)
Tel: (+966) 2 607 0828

Tahlia St. Center
Tel: (+966) 2 668 2566

Tahlia St. Center (Ladies)
Tel: (+966) 2 669 4469

Al Musa'adia Center
Tel: (+966) 2 668 3600

Al Musa'adia Center (Ladies)
Tel: (+966) 2 668 3600

Al Balad Center
Tel: (+966) 2 648 5533

Khalid Bin Al-Waleed St. Center
Tel: (+966) 2 651 8070

CENTRAL REGION

Riyadh
Olaya Center
Tel: (+966) 1 275 1086

King Fahd Road Center
Tel: (+966) 1 225 6000

King Fahd Road Center (Ladies)
Tel: (+966) 1 205 1838

Al-Suwaidi Center
Tel: (+966) 1 433 4757

Uqba Bin Nafe'a Center
Tel: (+966) 1 278 5390

Uqba Bin Nafe'a Center (Ladies)
Tel: (+966) 1 278 4387

Al Rayyan Center
Tel: (+966) 1 208 3316

Al Rayyan Center (Ladies)
Tel: (+966) 1 208 3316

King Abdullah St. Center
Tel: (+966) 1 207 1460

King Abdullah St. Center (Ladies)
Tel: (+966) 1 207 1406

Al-Nafl Center
Tel: (+966) 1 275 1086

Qasim
Buraidah Center
Tel: (+966) 6 583 5230

Onaizah Center
Tel: (+966) 6 361 8465

EASTERN REGION

Dammam
Dammam Center
Tel: (+966) 3 830 1420

Al Khobar
Al-Hada District Center
Tel: (+966) 3 887 8570

Al-Hada District Center (Ladies)
Tel: (+966) 3 887 8651

King Abdul Aziz Road Center
Tel: (+966) 3 867 6707

Jubail
Jubail Industrial City Center
Tel: (+966) 3 347 1423

Qateef
Qateef Center
Tel: (+966) 3 854 5370

Qateef Center (Ladies)
Tel: (+966) 3 854 5370

Al-Ahsa
Al Hofuf Center
Tel: (+966) 3 586 1590

TAKAFUL TA'AWUNI التكــافــل التعــاوني

WESTERN REGION

Head Office
Level 4, Dahlawi Center
PO Box 6277
Jeddah 21442, KSA
Tel: (+966) 2 683 6364

Jeddah
Dahlawi Center
Tel: (+966) 2 683 6364

Dahlawi Center (Ladies)
Tel: (+966) 2 683 6364

Makkah Mukarama
Al Rajhi Center
Tel: (+966) 2 561 3990

Al Rajhi Center (Ladies)
Tel: (+966) 2 561 3980

Madinah Munawara
Hamza Ghouth Building
Tel: (+966) 4 822 1574

Hamza Ghouth Building (Ladies)
Tel: (+966) 4 822 1572

CENTRAL REGION

Riyadh
Al Mousa Building
Tel: (+966) 1 216 7737

Al-Mousa Building (Ladies)
Tel: (+966) 1 216 7737

EASTERN REGION

Dammam
Al Khuraiji Building
Tel: (+966) 3 831 1717

Al Khuraiji Building (Ladies)
Tel: (+966) 3 833 3696

Al Khobar
Alshaikh Center
Tel: (+966) 3 882 3804

Al Hofuf
Al Mousa Center
Tel: (+966) 3 585 4747

Independent Auditors' Report

ERNST & YOUNG

P.O. Box 1994
Jeddah 21441
Saudi Arabia

PRICEWATERHOUSECOOPERS

P.O. Box 16415
Jeddah 21464
Saudi Arabia

To the Shareholders of Bank AlJazira:

We have audited the accompanying consolidated financial statements of Bank AlJazira (the Bank) and its subsidiaries, which comprise the consolidated balance sheet as at December 31, 2008, and the consolidated statement of income, consolidated statement of changes in equity and consolidated statement of cash flow for the year then ended, and a summary of significant accounting policies and explanatory notes from 1 to 37 for the year then ended. We have not audited Note 38, nor the information related to "Basel II disclosures" cross-referenced therein, which is not required to be within the scope of our audit.

Management's Responsibility for the 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, 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 Articles of Association in so far as they affect the preparation and presentation of the financial statements. This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

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 whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the 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 entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the 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 consolidated financial position of the Bank as at December 31, 2008, and of its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with Accounting Standards for Financial Institutions issued by the Saudi Arabian Monetary Agency and with International Financial Reporting Standards; and
- comply with the requirements of the Regulations for Companies, the Banking Control Law and the Bank's Articles of Association in so far as they affect the preparation and presentation of the financial statements.

For Ernst & Young

Sami Farah
Registration Number 168

February 7, 2009
(Safar 12, 1430H)

PROFESSIONAL LICENCE No. 45
ERNST & YOUNG

PricewaterhouseCoopers Al Juraid

Omar M. Al Sagga
Registration Number 369

PRICEWATERHOUSECOOPERS AL JURAID
CERTIFIED PUBLIC ACCOUNTANTS
LICENSE NO. 25

Financial Statements

December 31, 2008 and 2007

Consolidated Balance Sheets

As at December 31, 2008 and 2007

	Notes	2008 SR'000	2007 SR'000
ASSETS			
Cash and balances with SAMA	3	2,258,459	1,490,783
Due from banks and other financial institutions	4	3,903,582	3,662,768
Investments	5	4,909,368	4,963,619
Loans and advances, net	6	15,133,153	9,879,236
Other real estate, net		75,797	75,797
Property and equipment, net	7	493,503	459,303
Other assets	8	745,843	1,032,482
Total assets		27,519,705	21,563,988
LIABILITIES AND EQUITY			
LIABILITIES			
Due to banks and other financial institutions	10	1,366,645	716,690
Customers' deposits	11	20,900,368	15,647,087
Other liabilities	12	514,869	411,122
Total liabilities		22,781,882	16,774,899
EQUITY ATTRIBUTABLE TO EQUITY HOLDERS OF THE PARENT			
Share capital	13	3,000,000	2,250,000
Statutory reserve	14	1,383,000	1,327,000
General reserve	14	68,000	68,000
Other reserve	15	(3,141)	142,493
Retained earnings		188,943	775,104
Proposed dividend	25	-	135,000
Total equity attributable to equity holders of the parent		4,636,802	4,697,597
Minority interests		101,021	91,492
Total shareholders' equity and minority interests		4,737,823	4,789,089
Total liabilities and equity		27,519,705	21,563,988

The accompanying notes 1 to 38 form an integral part of these consolidated financial statements.

Consolidated Statements of Income

For the years ended December 31, 2008 and 2007

	Notes	2008 SR'000	2007 SR'000
Special commission income	17	1,114,431	908,968
Special commission expense	17	(483,010)	(313,847)
Net special commission income		631,421	595,121
Fees from banking services, net	18	537,515	698,479
Foreign exchange income, net		21,708	17,232
Trading (loss) / income, net	19	(33,940)	15,399
Dividend income	20	11,532	12,385
(Loss) / gain on non-trading investments, net	21	(34,498)	102,503
Other operating income	22	2,806	5,673
Total operating income		1,136,544	1,446,792
Salaries and employee-related expenses		436,340	364,839
Rent and premises-related expenses		64,048	53,292
Depreciation	7	74,940	58,244
Other general and administrative expenses		215,185	191,461
Charge for / (reversal of) provision for credit losses, net	6	61,158	(25,908)
Impairment of other financial assets	5 &15	62,238	-
Other operating expenses	23	830	2,698
Total operating expenses		914,739	644,626
Net income		221,805	802,166
Loss attributable to minority interests		534	3,037
Net income for the year attributable to equity holders of the parent		222,339	805,203
Basic and diluted earnings per share (in SR)	24	0.74	2.68

The accompanying notes 1 to 38 form an integral part of these consolidated financial statements.

Consolidated Statements of Changes in Equity

For the years ended December 31, 2008 and 2007

	Notes	Share capital SR'000	Statutory reserve SR'000	General reserve SR'000	Other reserve SR'000	Retained earnings SR'000	Proposed dividend SR'000	Total equity attributable to equity holders of the parent SR'000	Minority Interests SR'000	Total SR'000
2008										
Balance at January 1, 2008		2,250,000	1,327,000	68,000	142,493	775,104	135,000	4,697,597	91,492	4,789,089
Net changes in fair values of available for sale investments	15	-	-	-	(242,370)	-	-	(242,370)	-	(242,370)
Transfer to consolidated statements of income	15	-	-	-	96,736	-	-	96,736	-	96,736
Net loss directly recognized in equity		-	-	-	(145,634)	-	-	(145,634)	-	(145,634)
Net income for the year		-	-	-	-	222,339	-	222,339	(534)	221,805
Total recognised income and expense for the year		-	-	-	(145,634)	222,339	-	76,705	(534)	76,171
Bonus share issue	13	750,000	-	-	-	(750,000)	-	-	-	-
Transfer to statutory reserve	14	-	56,000	-	-	(56,000)	-	-	-	-
Zakat and income tax relating to a subsidiary		-	-	-	-	(2,500)	-	(2,500)	-	(2,500)
Gross dividend for 2007 (approved)	25	-	-	-	-	-	(135,000)	(135,000)	-	(135,000)
Net changes in minority interests		-	-	-	-	-	-	-	10,063	10,063
Balance at December 31, 2008		3,000,000	1,383,000	68,000	(3,141)	188,943	-	4,636,802	101,021	4,737,823
2007										
Balance at January 1, 2007		1,125,000	1,125,000	68,000	169,444	1,431,901	274,500	4,193,845	56,307	4,250,152
Net changes in fair values of available for sale investments	15	-	-	-	75,552	-	-	75,552	-	75,552
Transfer to consolidated statements of income	15	-	-	-	(102,503)	-	-	(102,503)	-	(102,503)
Net loss directly recognized in equity		-	-	-	(26,951)	-	-	(26,951)	-	(26,951)
Net income for the year		-	-	-	-	805,203	-	805,203	(3,037)	802,166
Total recognised income and expense for the year		-	-	-	(26,951)	805,203	-	778,252	(3,037)	775,215
Bonus share issue	13	1,125,000	-	-	-	(1,125,000)	-	-	-	-
Transfer to statutory reserve	14	-	202,000	-	-	(202,000)	-	-	-	-
Gross dividend for 2006 (approved)		-	-	-	-	-	(274,500)	(274,500)	-	(274,500)
Proposed gross dividend for 2007	25	-	-	-	-	(135,000)	135,000	-	-	-
Net changes in minority interests		-	-	-	-	-	-	-	38,222	38,222
Balance at December 31, 2007		2,250,000	1,327,000	68,000	142,493	775,104	135,000	4,697,597	91,492	4,789,089

The accompanying notes 1 to 38 form an integral part of these consolidated financial statements.

Consolidated Statements of Cash Flows

For the years ended December 31, 2008 and 2007

	Notes	2008 SR'000	2007 SR'000
OPERATING ACTIVITIES			
Net income for the year		222,339	805,203
Adjustments to reconcile net income to net cash from operating activities:			
Trading loss / (income), net	19	33,940	(15,399)
Loss / (gain) on non-trading investments, net	21	34,498	(102,503)
Depreciation	7	74,940	58,244
Loss on disposal of property and equipment, net		20	-
Provision for credit losses	6	61,158	(25,908)
Impairment of other financial assets	15	62,238	-
		489,133	719,637
Net (increase) decrease in operating assets:			
Statutory deposit with SAMA	3	(305,713)	(111,812)
Due from banks and other financial institutions maturing after ninety days of acquisition		(718,716)	(297,504)
Investments held for trading		137,868	85,079
Loans and advances		(5,315,075)	(3,582,208)
Other real estate, net		-	6,930
Other assets		286,639	(696,131)
Net increase (decrease) in operating liabilities:			
Due to banks and other financial institutions		649,955	543,130
Customers' deposits		5,253,281	4,729,999
Other liabilities		112,683	12,173
Net cash from operating activities		590,055	1,409,293
INVESTING ACTIVITIES			
Proceeds from maturity and sale of non-trading investments		3,343,419	175,337
Purchase of non-trading investments		(3,708,125)	(3,904,477)
Purchase of property and equipment	7	(109,178)	(123,444)
Proceeds from sale of property and equipment		18	308
Dividend received		4,779	3,860
Net cash used in investing activities		(469,087)	(3,848,416)
FINANCING ACTIVITIES			
Dividends paid		(146,436)	(247,625)
Net movements in minority interests		9,529	35,185
Net cash used in financing activities		(136,907)	(212,440)
Net decrease in cash and cash equivalents		(15,939)	(2,651,563)
Cash and cash equivalents at the beginning of the year		3,891,962	6,543,525
Cash and cash equivalents at the end of the year	26	3,876,023	3,891,962
Special commission received during the year		1,081,097	744,563
Special commission paid during the year		418,756	305,882
SUPPLEMENTAL NON-CASH INFORMATION			
Net changes in fair values		(145,634)	(26,951)

The accompanying notes 1 to 38 form an integral part of these consolidated financial statements.

Notes to the Consolidated Financial Statements

For the years ended December 31, 2008 and 2007

1. GENERAL

Bank AlJazira (the Bank) is a Joint Stock Company incorporated in the Kingdom of Saudi Arabia and formed pursuant to Royal Decree number 46/M dated Jumad Al-Thani 12, 1395H (June 21, 1975). The Bank commenced its business on Shawwal 16, 1396H (October 9, 1976) with the takeover of The National Bank of Pakistan's branches in the Kingdom of Saudi Arabia and operates under commercial registration number 4030010523 dated Rajab 29, 1396H (July 27, 1976) issued in Jeddah, through its 24 branches (2007: 24 branches) in the Kingdom of Saudi Arabia and employed 2,003 staff (2007: 1,780 staff). The Bank's Head Office is located at the following address:

Bank AlJazira
Khalid Bin Al-Walid Street, P. O. Box 6277
Jeddah 21442, Kingdom of Saudi Arabia

The objective of the Bank is to provide a full range of banking services.

The Bank provides to its customers Shari'ah compliant (non-interest based) banking products comprising of Murabaha, Istisna'a, Ijarah and Tawaraq, which are approved and supervised by an independent Shari'ah Board established by the Bank.

During 2008, the Bank has formed a new capital market company, namely, AlJazira Capital Company, a Saudi Joint Stock Company formed in accordance with Capital Market Authority's Resolution no. 2-38-2007 dated 8 Rajab 1428H (July 22, 2007), and registered in the Kingdom of Saudi Arabia under Commercial Registration No. 4030177603 dated 17 Rabi Awal 1429H (March 26, 2008). The Bank has 99.99% direct ownership interest in the subsidiary, AlJazira Capital Company, and an indirect ownership of 0.01% (the indirect ownership is held on behalf and for the beneficial interest of the Bank by minority shareholders). The activities of Brokerage Division of the Bank have been taken over by the AlJazira Capital Company, with effect from April 5, 2008.

In accordance with new regulatory requirements in Saudi Arabia, the Bank is in the process of completing the legal formalities to transfer asset management activities to AlJazira Capital Company. The actual transfer of the activities / operations is expected to take place during 2009.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The significant accounting policies adopted in the preparation of these consolidated financial statements are consistent with those used in the previous year and are set out below.

a) Basis of presentation

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

The consolidated financial statements are prepared under the historical cost convention except for the measurement at fair value of derivatives, investments held for trading and held at fair value through income statement (FVIS) and available for sale investments.

These consolidated financial statements are expressed in Saudi Arabian Riyals (SR) and are rounded off to the nearest thousands.

b) Basis of consolidation

The consolidated financial statements comprise the financial statements of Bank AlJazira and its subsidiaries drawn up to December 31 each year. 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 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 are included in the consolidated statement of income from the date of the acquisition or up to the date of disposal, as appropriate.

Minority interests represent the portion of net income (loss) and net assets not owned, directly or indirectly, by the Bank in its subsidiaries and are presented separately in the consolidated statement of income and within equity in the consolidated balance sheet, separately from parent shareholders' equity.

All significant inter-company transactions and balances have been eliminated upon consolidation.

The Bank's subsidiaries are as follows:

	Ownership December 31, 2008	Ownership December 31, 2007
Al-Mashareq Japanese Equities Fund	**42.70%**	61.54%
Al-Khair Global Equities Fund	**31.93%**	43.36%
Al-Thoraiya European Equities Fund	**48.74%**	63.61%
AlJazira Capital Company	**100.00%**	-
Aman Real Estate	**98.00%**	98.00%

All the above subsidiaries are incorporated in the Kingdom of Saudi Arabia.

These consolidated financial statements comprise the financial statements of Bank AlJazira and its subsidiaries, namely, AlJazira Capital Company, Al-Mashareq, Al-Khair, Al-Thoraiya and Aman Real Estate (the "Group").

c) Critical accounting judgments and estimates

The preparation of 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 judgment in the process of applying the Group's accounting policies. Such estimates, assumptions and judgments are continually evaluated and are based on historical experience and other factors, including obtaining professional advices and expectations of future events that are believed to be reasonable under the circumstances. Significant areas where management has used estimates, assumptions or exercised judgments are as follows:

i) Impairment losses on loans and advances

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

ii) Impairment of available-for-sale equity investments

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

A significant or prolonged decline, below cost, is recognized in the consolidated statement of income as provision for impairment for other financial assets.

iii) Classification of held-to-maturity investments

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

d) Settlement date accounting

All regular way purchases and sales of financial assets are recognized and derecognized on the settlement date, i.e. the date on which the asset is delivered to the counterparty. Changes in fair value between the trade date and the settlement date are accounted for in the same way as the acquired assets. Regular way purchases or sales are purchases or sales of financial assets that require delivery of assets within the time frame generally established by regulations or convention in the market place.

e) Derivative financial instruments

Derivative financial instruments including foreign exchange contracts, commission rate futures, forward rate agreements, currency and commission rate swaps, currency and commission rate options (both written and purchased) are initially measured at fair value. All derivatives are carried at their fair value as assets, where the fair value is positive, and as liabilities, where the fair value is negative. Fair values are obtained by reference to quoted market prices, discounted cash flow models and pricing models, as appropriate.

Any changes in the fair value of derivatives that are held for trading purposes are taken directly to the consolidated statement of income. Derivatives held for trading also include those derivatives, which do not qualify for hedge accounting. The Group does not have derivatives that qualify for hedge accounting.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES continued

f) Foreign currencies

The consolidated financial statements are denominated and presented in Saudi Arabian Riyals, which is also the functional currency of the Bank.

Transactions in foreign currencies are translated into Saudi Arabian Riyals at exchange rates prevailing at transaction dates. Monetary assets and liabilities at the year end, denominated in foreign currencies, are translated into Saudi Arabian Riyals at the exchange rates prevailing at the consolidated balance sheet date. Foreign exchange gains or losses on translation of monetary assets and liabilities denominated in foreign currencies are recognised in the consolidated statement of income.

The accounting records of the Bank's subsidiaries are maintained in US Dollars or Saudi Riyals. As the rate of exchange of the US Dollar against the Saudi Arabian Riyal was constant throughout the last two years, no exchange difference has arisen on the translation of the subsidiaries' financial statements for the purposes of consolidation.

g) Offsetting

Financial assets and liabilities are offset and reported net in the consolidated balance sheet 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.

h) Revenue recognition

Special commission income and expense including the fees which are considered an integral part of the effective yield of a financial instrument, are recognised in the consolidated statement of income on the effective yield basis and include premiums amortised and discounts accreted during the year.

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

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

Foreign exchange income / loss are recognised when earned / incurred.

Fees and commissions are recognized on an accrual basis when the service has been provided. Loan commitment fees for loans that are likely to be drawn down are deferred and, together with the related direct cost, are recognised if material, as an adjustment to the effective yield on the loan. Portfolio and other management advisory and service fees, including fees for managing investment funds, are recognized based on the applicable service contracts, usually on a time-proportionate basis.

Dividend income is recognised when declared.

i) Sale and repurchase agreements

Assets sold with a simultaneous commitment to repurchase at a specified future date (repos) continue to be recognized in the consolidated balance sheet and are measured in accordance with related accounting policies for investments held for trading and held at FVIS, available for sale, held to maturity and other investments held at amortised costs. The counterparty liability for amounts received under these agreements is included in "due to banks and other financial institutions" or "customers' deposits", as appropriate. The difference between the sale and repurchase price is treated as special commission expense and is accrued over the life of the repo agreement using the effective special commission rate. Assets purchased with a corresponding commitment to resell at a specified future date (reverse repos) are not recognized in the consolidated balance sheet, as the Bank does not obtain control over the assets. Amounts paid under these agreements are included in "cash and balances with SAMA", "due from banks and other financial institutions" or "loans and advances", as appropriate. The difference between the purchase and resale price is treated as special commission income and is accrued over the life of the reverse repo agreement using the effective special commission rate.

j) Investments

All investment securities are initially recognized at fair value, including acquisition charges associated with the investments except for investments held for trading and held as FVIS. Premiums are amortised and discounts are accreted on a systematic basis to their maturity and are taken to special commission income.

For securities that are traded in organized financial markets, fair value is determined by reference to exchange quoted market bid prices at the close of business on the consolidated balance sheet date.

For securities where there is no quoted market price, a reasonable estimate of the fair value is determined by reference to the current market value of another instrument, which is substantially the same, or is based on the expected cash flows or the underlying net asset base of the security.

Following initial recognition, subsequent transfers between the various classes of investments are not ordinarily permissible. The subsequent period-end reporting values for each class of investment is determined on the basis as set out in the following paragraphs:

i) Held for trading and held at fair value through income statement (FVIS)

Investments in this category are classified as either investment held for trading or those designated as FVIS at inception. Investments held for trading are acquired principally for the purpose of selling or repurchasing in short term. An investment may be designated as FVIS by the management if it satisfies the criteria laid down by IAS 39 except for the equity instruments that do not have a quoted market price in an active market and whose fair values cannot be reliably measured.

After initial recognition, investments are measured at fair value and any change in the fair value is recognised in the consolidated statement of income for the period in which it arises. Transaction costs, if any, are not added to the fair value measurement at initial recognition of held for trading and held as FVIS investments. Dividend income received on investment held for trading and held at FVIS are reflected as either trading income or income from FVIS financial instruments in the consolidated statement of income.

ii) Available for sale

Available-for-sale investments are those intended to be held for an unspecified period of time, which may be sold in response to needs for liquidity or changes in interest rates, exchange rates or equity prices.

Investments, which are classified as available for sale, are subsequently measured at fair value. For available for sale investments where the fair value has not been hedged, any gain or loss arising from a change in their fair values is recognized directly in “Other reserve” under shareholders’ equity. On derecognition, any cumulative gain or loss previously recognized in shareholders’ equity is included in the consolidated statement of income for the period.

iii) Held to maturity

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

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

iv) Other investments held at amortised cost

Investments securities with fixed or determinable payments that are not quoted in an active market are classified as “Other investments held at amortised cost”. Such investments whose fair values have not been hedged are stated at amortised cost, less provision for impairment. Amortised cost is calculated by taking into account any discount or premium on acquisition using effective yield method. Any gain or loss is recognized in the consolidated statement of income when the investment is derecognized or impaired.

k) Loans and advances

Loans and advances are non-derivative financial assets originated by the Bank with fixed or determinable payments.

All loans and advances are initially measured at fair value, including acquisition charges associated with the loans and advances except for loans held as FVIS.

Following the initial recognition, loans and advances originated or acquired by the Bank that are not quoted in an active market and for which fair value has not been hedged, are stated at cost less any amount written off and provisions for impairment.

For presentation purposes, provision for credit losses is deducted from loans and advances.

l) Impairment of financial assets

An assessment is made at each consolidated balance sheet date 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 estimated recoverable amount of that asset is determined and any impairment loss, based on the net present value of future anticipated cash flows, is recognized for changes in its carrying amounts as follows:

i) Impairment of financial assets held at amortised cost

A financial asset is classified as impaired when there is an objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the asset and that a loss event(s) has an impact on the estimated future cash flows of the financial asset or group of financial assets that can be reliably estimated.

A specific provision for credit losses due to impairment of a loan or any other financial asset held at amortized cost is established if there is objective evidence that the Bank will not be able to collect all amounts due. The amount of the specific provision is the difference between the carrying amount and the estimated recoverable amount. The estimated recoverable amount is the present value of expected cash flows, including amounts estimated to be recoverable from guarantees and collateral, discounted based on the original effective commission rate.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES continued

l) Impairment of financial assets continued

i) Impairment of financial assets held at amortised cost continued

In addition to specific provision for credit losses, provision for collective impairment is made on a portfolio basis for credit losses where there is an objective evidence that unidentified losses exist at the reporting date. This provision is estimated based on various factors including credit ratings allocated to a borrower or group of borrowers, the current economic conditions, the experience the Bank has had in dealing with a borrower or group of borrowers and available historical default information.

For financial assets at amortised cost, the carrying amount of the asset is adjusted through the use of an allowance account and the amount of the adjustment is included in the consolidated statement of income.

ii) Impairment of financial assets held at fair value

For financial assets held at fair value, where a loss has been recognised directly under shareholders' equity, the cumulative net loss recognised in shareholders' equity is transferred to the consolidated statement of income when the asset is considered to be impaired.

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

The Bank writes off its financial assets when the respective business units determine that the financial assets are uncollectible. This determination is reached after considering information such as the occurrence of significant changes in the borrower/issuer's financial position such that the borrower/issuer can no longer pay the obligations, or that proceeds from collateral will not be sufficient to pay back the entire exposure. The financial assets are, then, written off only in circumstances where effectively all possible means of recovery have been exhausted. For consumer loans, write off decisions are generally based on a product specific past due status. When a financial asset is uncollectible, it is written off against the related provision for impairment, if any, and any amounts in excess of available provision are directly charged to consolidated statement of income.

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

If, in a subsequent period, the amount of the impairment loss on investments other than available for sale equity investments decreases and the decrease can be related objectively to an event occurring after the impairment was recognized (such as an improvement in the issuer's credit rating), the previously recognized impairment loss is reversed by adjusting the provision account. The amount of the reversal is recognized in the consolidated statement of income as reversal of provision for impairment for other financial assets.

Loans whose terms have been renegotiated are no longer considered to be past due but are treated as new loans. Restructuring policies and practices are based on indicators or criteria which, indicate that payment will most likely continue. The loans continue to be subject to an individual or collective impairment assessment.

m) Other real estate

The Bank, in the ordinary course of business, acquires certain real estate against settlement of past due loans and advances. Such real estate are considered as assets held for sale and are initially stated at the lower of the net realizable value of due loans and advances and the current fair value of related properties, less any costs to sell.

Subsequent to the initial recognition, such real estate are revalued on a periodic basis. Any unrealised losses on revaluation, realized losses or gains on disposal and rental income are recognised in the consolidated statement of income.

n) Property and equipment

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

Buildings	33 years
Leasehold improvements	Over the lease period or 10 years, whichever is shorter
Furniture, equipment and vehicles	4 to 10 years

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at each consolidated balance sheet date.

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

All assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. The carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount.

o) Liabilities
All money market deposits and customer deposits are initially recognised at fair value.

Subsequently, all commission-bearing financial liabilities, other than those held for trading and held at FVIS or where fair values have been hedged, are measured at amortised cost. Amortised cost is calculated by taking into account any discount or premium. Premiums are amortised and discounts accreted on a systematic basis to maturity and taken to special commission income or expense.

For financial liabilities carried at amortised cost, any gain or loss is recognized in the consolidated statement of income when derecognized.

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

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

r) Accounting for leases
Leases entered into by the Group as a lessee are all operating leases. Payments made under operating leases are charged to the consolidated statement of income on a straight-line basis over the period of the lease.

When an operating lease is terminated before the lease period has expired, any payment required to be made to the lessor by way of penalty is recognized as an expense in the period in which termination takes place.

s) Cash and cash equivalents
For the purpose of the consolidated statement of cash flows, cash and cash equivalents are defined as those amounts included in cash, balances with SAMA, excluding statutory deposits, and due from banks and other financial institutions with original maturity of ninety days or less.

t) Derecognition of financial instruments
A financial asset (or a part of a financial asset, or a part of a group of similar financial assets) is derecognised, when the contractual rights to the cash flows from the financial asset expires.

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

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

u) Zakat and income tax
Under Saudi Arabian Zakat and Income tax laws, zakat and income tax are the liabilities of Saudi and foreign shareholders, respectively. Zakat is computed on the Saudi shareholders' share of equity or net income using the basis defined under the zakat regulations. Income tax is computed on the foreign shareholder's share of net income for the year.

Zakat and income tax, relating to the shareholders of the Bank, are not charged to the Bank's consolidated statement of income as they are deducted from the dividends paid to the shareholders.

Zakat and income tax relating to AlJazira Capital are included in the consolidated statement of changes in equity.

v) Fiduciary assets
Assets held in trust or in a fiduciary capacity are not treated as assets of the Group and, accordingly, are not included in the accompanying consolidated financial statements.

w) Shari'ah compliant (non-interest based) banking products
The Bank offers its customers Shari'ah compliant (non-interest based) banking products, which are approved by its Shari'ah Board.

All Shari'ah compliant (non-interest based) products are accounted for using International Financial Reporting Standards and in conformity with the accounting policies described in this note.

3. CASH AND BALANCES WITH SAMA

	2008 SR'000	2007 SR'000
Cash in hand	360,407	402,444
Statutory deposit	966,052	660,339
Current account (cash management account)	932,000	428,000
Total	2,258,459	1,490,783

In accordance with the Banking Control Law and regulations issued by Saudi Arabian Monetary Agency (SAMA), the Bank is required to maintain a statutory deposit with SAMA at stipulated percentages of its demand, time and other deposits, calculated at the end of each Gregorian month.

4. DUE FROM BANKS AND OTHER FINANCIAL INSTITUTIONS

	2008 SR'000	2007 SR'000
Current accounts	130,120	48,295
Money market placements	3,773,462	3,614,473
Total	3,903,582	3,662,768

The money market placements represent funds placed on a Shari'ah compliant (non-interest based) Murabaha basis.

5. INVESTMENTS

a) Investments are classified as follows:

i) Held for trading

	Domestic		International		Total	
	2008 SR'000	2007 SR'000	2008 SR'000	2007 SR'000	2008 SR'000	2007 SR'000
Equities	1,484	-	172,706	199,246	174,190	199,246
Mutual fund (Murabaha funds)	350,567	502,098	-	-	350,567	502,098
	352,051	502,098	172,706	199,246	524,757	701,344

ii) Available for sale

	Domestic		International		Total	
	2008 SR'000	2007 SR'000	2008 SR'000	2007 SR'000	2008 SR'000	2007 SR'000
Equities	145,172	399,707	1,319	188	146,491	399,895

iii) Other investments held at amortised cost

	Domestic		International		Total	
	2008 SR'000	2007 SR'000	2008 SR'000	2007 SR'000	2008 SR'000	2007 SR'000
Murabaha investments	3,600,000	3,350,000	-	-	3,600,000	3,350,000
Floating rate notes	619,370	474,880	18,750	18,750	638,120	493,630
Other investments held at amortised cost	4,219,370	3,824,880	18,750	18,750	4,238,120	3,843,630

iv) Held to maturity

	Domestic		International		Total	
	2008 SR'000	2007 SR'000	2008 SR'000	2007 SR'000	2008 SR'000	2007 SR'000
Fixed rate securities	-	-	-	18,750	-	18,750
Held to maturity	-	-	-	18,750	-	18,750
Total investments	4,716,593	4,726,685	192,775	236,934	4,909,368	4,963,619

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

	2008			2007		
	Quoted SR'000	Unquoted SR'000	Total SR'000	Quoted SR'000	Unquoted SR'000	Total SR'000
Murabaha investments	-	3,600,000	3,600,000	-	3,350,000	3,350,000
Fixed rate securities	-	-	-	18,750	-	18,750
Floating rate notes	638,120	-	638,120	493,630	-	493,630
Equities	318,243	2,438	320,681	595,723	3,418	599,141
Mutual fund (Murabaha funds)	350,567	-	350,567	502,098	-	502,098
Investments	1,306,930	3,602,438	4,909,368	1,610,201	3,353,418	4,963,619

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

i) Other investments held at amortised cost

	2008				2007			
	Carrying value SR'000	Gross unrealized gains SR'000	Gross unrealized losses SR'000	Fair value SR'000	Carrying value SR'000	Gross unrealized gains SR'000	Gross unrealized losses SR'000	Fair value SR'000
Murabaha investments	3,600,000	-	-	3,600,000	3,350,000	-	-	3,350,000
Floating rate notes	638,120	1,600	(9,956)	629,764	493,630	1,917	-	495,547
Total	4,238,120	1,600	(9,956)	4,229,764	3,843,630	1,917	-	3,845,547

ii) Held to maturity

	2008				2007			
	Carrying value SR'000	Gross unrealized gains SR'000	Gross unrealized losses SR'000	Fair value SR'000	Carrying value SR'000	Gross unrealized gains SR'000	Gross unrealized losses SR'000	Fair value SR'000
Fixed rate Securities	-	-	-	-	18,750	-	-	18,750

d) The analysis of investments by counterparty is as follows:

	2008 SR'000	2007 SR'000
Government and quasi Government	3,618,750	3,387,500
Corporate	931,665	1,065,071
Banks and other financial institutions	358,953	511,048
Total	4,909,368	4,963,619

Held for trading represents Shari'ah compliant equity and other investments, having a carrying value of SR 524.7 million (2007: SR 701.3 million), which have been measured at fair value.

Available-for-sale (AFS) includes Shari'ah compliant equity investments, having a carrying value of SR 146.5 million (2007: SR 399.9 million) which have been measured at fair value, except for SR 2.4 million (2007: SR 3.4 million) which have been measured at cost as their fair value cannot be reliably measured, due to the absence of an active market and non-availability of observable market prices for a similar instrument.

Other investments held at amortised costs comprise murabaha investments of SR 3,600 million (2007: SR 3,350 million) and Sukuk investments of SR 638.1 million (2007: SR 493.6 million) that are carried at amortised cost. The fair values of these investments are not significantly different from their carrying values.

Held-to-maturity investments at 31 December 2007 include Sukuk investments having a carrying value of SR 18.75 million, which had been measured at amortised cost. The fair values of these investments are not significantly different from their carrying values. During the year, these investments matured.

e) During 2008, the Bank has recorded an impairment loss of SR 62.2 million for available for sale equity investments.

6. LOANS AND ADVANCES, NET

a) Loans and advances, net comprise the following:

2008	Consumer SR'000	Commercial SR'000	Others SR'000	Total SR'000
Performing loans and advances – gross	1,645,776	13,562,617	73,450	15,281,843
Non-performing loans and advances – net	9,449	223,409	-	232,858
Total loans and advances	1,655,225	13,786,026	73,450	15,514,701
Provision for credit losses (specific and portfolio)	(35,616)	(345,932)	-	(381,548)
Loans and advances, net	1,619,609	13,440,094	73,450	15,133,153

2007	Consumer SR'000	Commercial SR'000	Others SR'000	Total SR'000
Performing loans and advances – gross	658,567	9,271,933	70,532	10,001,032
Non-performing loans and advances – net	954	198,234	-	199,188
Total loans and advances	659,521	9,470,167	70,532	10,200,220
Provision for credit losses (specific and portfolio)	(26,111)	(294,873)	-	(320,984)
Loans and advances, net	633,410	9,175,294	70,532	9,879,236

Loans and advances, net represents Shari'ah Compliant (non-interest based) products in respect of Murabaha agreements, Istisna'a and Tawaraq.

b) Movements in provision for credit losses are as follows:

2008	Consumer SR'000	Commercial SR'000	Others SR'000	Total SR'000
Balance at the beginning of the year	26,111	294,873	-	320,984
Provided during the year	10,470	61,394	-	71,864
Bad debts written off	(620)	-	-	(620)
Recoveries of amounts previously provided	(345)	(10,335)	-	(10,680)
Balance at the end of the year	35,616	345,932	-	381,548

2007	Consumer SR'000	Commercial SR'000	Others SR'000	Total SR'000
Balance at the beginning of the year	30,815	325,397	-	356,212
Provided during the year	-	1,577	-	1,577
Bad debts written off	(4,704)	(8,062)	-	(12,766)
Recoveries of amounts previously provided	-	(24,039)	-	(24,039)
Balance at the end of the year	26,111	294,873	-	320,984

c) Net charge for / reversal of provision for credit losses for the year in the consolidated statement of income is as follows:

	2008 SR'000	2007 SR'000
Addition during the year	71,864	1,577
Recoveries of amounts previously provided	(10,680)	(24,039)
Recoveries of debts previously written off	(26)	(3,446)
Charge for provision for credit losses, net	61,158	(25,908)

d) Economic sector risk concentrations for the loans and advances and provision for credit losses are as follows:

2008	Performing SR'000	Non performing, net SR'000	Credit loss provision SR'000	Loans and advances, net SR'000
Banks and other financial institutions	1,081,335	-	-	1,081,335
Agriculture and fishing	40,952	-	-	40,952
Manufacturing	3,551,431	-	-	3,551,431
Mining and quarrying	6,521	-	-	6,521
Electricity, water, gas and health services	30,146	21,928	(21,256)	30,818
Building and construction	2,139,419	85,138	(90,365)	2,134,192
Commerce	2,240,946	19,318	(25,101)	2,235,163
Transportation and communication	383,760	-	-	383,760
Services	100,211	62,617	(62,617)	100,211
Consumer loans and credit cards	1,645,776	9,449	(10,997)	1,644,228
Share trading	422,522	26,558	(23,858)	425,222
Other	3,638,824	7,850	(8,985)	3,637,689
	15,281,843	232,858	(243,179)	15,271,522
Additional portfolio provision	-	-	(138,369)	(138,369)
Total	15,281,843	232,858	(381,548)	15,133,153

2007	Performing SR'000	Non performing, net SR'000	Credit loss provision SR'000	Loans and advances, net SR'000
Banks and other financial institutions	875,242	-	-	875,242
Agriculture and fishing	31,127	-	-	31,127
Manufacturing	2,404,140	-	-	2,404,140
Mining and quarrying	10,018	-	-	10,018
Electricity, water, gas and health services	19,986	-	-	19,986
Building and construction	487,745	80,129	(62,860)	505,014
Commerce	1,937,595	19,789	(23,151)	1,934,233
Transportation and communication	426,030	-	-	426,030
Services	107,765	63,817	(63,817)	107,765
Consumer loans and credit cards	658,567	954	(954)	658,567
Share trading	581,043	26,423	(23,757)	583,709
Other	2,461,774	8,076	(8,076)	2,461,774
	10,001,032	199,188	(182,615)	10,017,605
Additional portfolio provision	-	-	(138,369)	(138,369)
Total	10,001,032	199,188	(320,984)	9,879,236

7. PROPERTY AND EQUIPMENT, NET

	Land and buildings SR'000	Leasehold improvements SR'000	Furniture, equipment and vehicles SR'000	Capital work in progress SR'000	**Total 2008 SR'000**	Total 2007 SR'000
Cost						
Balance at the beginning of the year	149,154	121,416	292,670	79,051	642,291	519,198
Additions	31,080	15,765	36,000	26,333	109,178	123,444
Transfers	-	35,909	18,742	(54,651)	-	-
Disposals	-	(27)	(847)	-	(874)	(351)
Balance at the end of the year	180,234	173,063	346,565	50,733	750,595	642,291
Accumulated depreciation						
Balance at the beginning of the year	3,980	40,775	138,233	-	182,988	124,787
Charge for the year	151	18,199	56,590	-	74,940	58,244
Disposals	-	(3)	(833)	-	(836)	(43)
Balance at the end of the year	4,131	58,971	193,990	-	257,092	182,988
Net book value						
At December 31, 2008	176,103	114,092	152,575	50,733	493,503	
At December 31, 2007	145,174	80,641	154,437	79,051		459,303

8. OTHER ASSETS

	2008 SR'000	2007 SR'000
Accrued commission receivable:		
Banks and other financial institutions	31,737	25,732
Investments	89,885	98,099
Loans and advances	232,955	197,413
Total accrued commission receivable	354,577	321,244
Advances and prepayments	151,400	128,786
Advance for formation of new companies (see note below)	40,000	540,000
Other	199,866	42,452
Total	745,843	1,032,482

Advance for formation of new companies represents capital contributed by the Bank, during 2007, for the formation of two new companies for Brokerage and Investment Management Services. Legal formalities for the formation of one of the companies is in progress.

9. DERIVATIVES

The Bank stopped using derivative financial instruments after its move to Shari'ah complaint (non-interest based) banking and therefore, the Bank did not have any derivative financial instruments at December 31, 2008 and 2007. The Bank is currently evaluating Shari'ah complaint (non-interest based) derivative financial instruments to use in the future.

10. DUE TO BANKS AND OTHER FINANCIAL INSTITUTIONS

	2008 SR'000	2007 SR'000
Current accounts	45,036	29,454
Money market deposits from banks and other financial institutions	1,321,609	687,236
Total	1,366,645	716,690

The money market deposits from banks and other financial institutions comprise deposits received on Murabaha basis.

11. CUSTOMERS' DEPOSITS

	2008 SR'000	2007 SR'000
Demand	5,321,579	5,543,886
Time	15,402,313	9,497,988
Other	176,476	605,213
Total	20,900,368	15,647,087

Time deposits comprise deposits received on Shari'ah Compliant (non-interest based) Murabaha basis.

Other customers' deposits include SR 127 million (2007: SR 111 million) of margins held for irrevocable commitments.

The above include foreign currency deposits as follows:

	2008 SR'000	2007 SR'000
Demand	138,936	53,576
Time	1,553,439	1,411,989
Other	7,354	13,716
Total	1,699,729	1,479,281

12. OTHER LIABILITIES

	2008 SR'000	2007 SR'000
Accrued commission payable:		
Banks and other financial institutions	6,309	2,710
Customers' deposits	133,089	72,434
Total accrued commission payable	139,398	75,144
AlJazira Philanthropic Program (see note below)	95,145	97,500
Accounts payable	152,490	143,680
Provision for indirect facilities	11,245	11,245
Other	116,591	83,553
Total	514,869	411,122

During 2006, the Board of Directors approved the contribution to a philanthropic program to carryout the Bank's social responsibilities towards the Saudi society, through the charitable contributions to various benevolent efforts that promote the general welfare of the society.

For this purpose, the Bank contributed SR 100 million to this program during 2006.

A Social Committee has been established to coordinate this program, consisting of three board members, and it is the intention of the Board of Directors to seek assistance of other independent members' from the business community and the Shari'ah Board of the Bank.

13. SHARE CAPITAL

The authorized, issued and fully paid share capital of the Bank consists of 300 million shares of SR 10 each (2007: 225 million shares of SR 10 each).

During 2008, a bonus issue of 75 million share of SR 10 each (one share for every three shares held) was approved by the shareholders in their extraordinary general assembly meeting held on April 16, 2008 for holders of record as of that date. The Bank obtained the regulatory approval in this respect and the bonus shares were issued on April 19, 2008.

During 2007, a bonus issue of 112.5 million shares of SR 10 each (one share for every one share held) was approved by the shareholders in their extraordinary general assembly meeting held on April 30, 2007 for holders of record as of that date. The Bank obtained the regulatory approval in this respect and the bonus shares were issued on May 5, 2007.

The ownership of the Bank's share capital is as follows:

	2008	2007
Saudi shareholders	**94.17%**	94.17 %
National Bank of Pakistan	**5.83%**	5.83 %

14. STATUTORY AND GENERAL RESERVES

In accordance with Saudi Arabian Banking Control Law and the Articles of Association of the Bank, a minimum of 25% of the annual net income is required to be transferred to a statutory reserve until this reserve equals the paid-up capital of the Bank. Accordingly, SR 56 million has been transferred from net income for 2008 (2007: SR 202 million). The statutory reserve is currently not available for distribution.

In addition, when considered appropriate, the Bank makes an appropriation to a general reserve for general banking risks.

15. OTHER RESERVE

	Available for sale investments 2008 SR'000	Available for sale investments 2007 SR'000
Balance at the beginning of the year	**142,493**	169,444
Net changes in fair values	**(242,370)**	75,552
Transfer to consolidated statement of income		
Loss/ (gain) on non-trading investments, net (see note 21)	**34,498**	(102,503)
Impairment of other financial assets	**62,238**	-
	96,736	(102,503)
Net movements during the year	**(145,634)**	(26,951)
Balance at the end of the year	**(3,141)**	142,493

16. COMMITMENTS AND CONTINGENCIES

a) Legal proceedings

At December 31, 2008, there were legal proceedings of a routine nature outstanding against the Bank. No provision has been made as related professional legal advice indicates that it is unlikely that any significant loss will eventually arise.

b) Capital commitments

At December 31, 2008, the Group had capital commitments of SR 11.16 million (2007: SR 25.8 million) in respect of the construction 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.

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

Documentary letters of credit, which are written undertakings by the Bank on behalf of a customer authorizing a third party to draw drafts on the Bank up to a stipulated amount under specific terms and conditions, are generally collateralized by the underlying shipments of goods to which they relate and, therefore, have significantly less credit risk.

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

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

i) The maturity structure for the Bank's commitments and contingencies is as follows:

2008	Within 3 months SR'000	3-12 months SR'000	1-5 years SR'000	Over 5 years SR'000	Total SR'000
Letters of credit	456,641	161,390	-	-	618,031
Letters of guarantee	495,039	1,102,117	498,416	12,266	2,107,838
Acceptances	281,409	3,915	-	-	285,324
Irrevocable commitments to extend credit	-	-	38,978	1,197,179	1,236,157
Other	-	-	-	-	-
Total	1,233,089	1,267,422	537,394	1,209,445	4,247,350

2007	Within 3 months SR'000	3-12 months SR'000	1-5 years SR'000	Over 5 years SR'000	Total SR'000
Letters of credit	255,296	63,796	742	-	319,834
Letters of guarantee	492,194	420,630	513,290	12,259	1,438,373
Acceptances	118,927	-	-	-	118,927
Irrevocable commitments to extend credit	-	-	334,956	-	334,956
Other	3,931	-	-	-	3,931
Total	870,348	484,426	848,988	12,259	2,216,021

The outstanding unused portion of commitments as at December 31, 2008, which can be revoked unilaterally at any time by the Bank, amounts to SR 3.7 billion (2007: SR 2.8 billion).

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

	2008 SR'000	2007 SR'000
Corporate	4,143,537	2,209,456
Banks and other financial institutions	103,813	2,634
Other	-	3,931
Total	4,247,350	2,216,021

Notes to the Consolidated Financial Statements continued

For the years ended December 31, 2008 and 2007

16. COMMITMENTS AND CONTINGENCIES continued

d) Operating lease commitments

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

	2008 SR'000	2007 SR'000
Less than 1 year	15,526	24,009
1 to 5 years	11,469	32,583
Over 5 years	225	3,045
Total	27,220	59,637

17. NET SPECIAL COMMISSION INCOME

	2008 SR'000	2007 SR'000
Special commission income		
Investments:		
Other investments held at amortised costs	168,565	113,091
Held to maturity	176	1,430
	168,741	114,521
Due from banks and other financial institutions	126,515	222,039
Loans and advances	819,175	572,408
Total	1,114,431	908,968
Special commission expense		
Due to banks and other financial institutions	42,475	12,309
Customers' deposits	434,111	297,641
Other	6,424	3,897
Total	483,010	313,847
Net special commission income	631,421	595,121

18. FEES FROM BANKING SERVICES, NET

	2008 SR'000	2007 SR'000
Fee and commission income		
Local share trading, net	328,815	554,467
Takaful Ta'awuni (insurance) wakala fee	112,919	68,508
Loan commitment and management fee	51,616	48,897
Trade finance	21,072	15,527
International share trading, net	3,874	3,785
Mutual funds fee	1,274	1,067
Others	42,607	20,371
Total fee and commission income	562,177	712,622
Fee and commission expense		
Takaful Ta'awuni – sales commission	(24,662)	(14,143)
Net	537,515	698,479

19. TRADING (LOSS) / INCOME, NET

	2008 SR'000	2007 SR'000
Equities	(46,188)	7,302
Mutual fund (Murabaha)	7,469	4,237
Dividends on equity investments held for trading	4,779	3,860
Total	(33,940)	15,399

20. DIVIDEND INCOME

	2008 SR'000	2007 SR'000
Available for sale investments	11,532	12,385

21. (LOSS) / GAIN ON NON-TRADING INVESTMENTS, NET

	2008 SR'000	2007 SR'000
Available for sale	(34,498)	102,503

22. OTHER OPERATING INCOME

	2008 SR'000	2007 SR'000
Rental income	98	292
Gain on sale of other real estate	-	877
Other	2,708	4,504
Total	2,806	5,673

23. OTHER OPERATING EXPENSES

	2008 SR'000	2007 SR'000
Other operating expenses	830	2,698

24. EARNINGS PER SHARE

Basic earnings per share are calculated by dividing the net income attributable to equity holders of the Bank by the weighted average number of ordinary shares in issue during the year. The weighted average number of ordinary shares outstanding during 2008 was 300 million (2007: 225 million). As required by International Accounting Standard 33, earning per share for last year has been retrospectively adjusted to reflect the issue of bonus shares during 2008.

The calculations of basic and diluted earnings per share are the same for the Bank.

25. PROPOSED GROSS DIVIDEND, ZAKAT AND INCOME TAX

On January 6, 2009, the Board of Directors approved a proposed gross dividend for the year 2008 of SR 17.1 million.

For 2007, a proposed gross dividend of SR 135 million was approved by the Board of Directors on December 10, 2007.

The dividends are paid to the Saudi and non-Saudi shareholders after deduction of zakat and income tax, respectively, as follows:

a) Saudi shareholders:

Zakat attributable to Saudi shareholders amounted to approximately SR 15.3 million (2007: SR 20.6 million), which will be deducted from their share of dividend, resulting in a net dividend to the Saudi shareholders of SR 0.50 per share (2007: SR 0.5 per share).

25. PROPOSED GROSS DIVIDEND, ZAKAT AND INCOME TAX continued

b) Non-Saudi shareholder:

Income tax payable on the current year's share of income of Non-Saudi shareholder is approximately SR 2.2 million (2007: SR 9.7 million).

During 2007, deferred tax of SR 54.3 million relating to Non-Saudi shareholder's earlier years profits was settled in accordance with subsequent SAMA directives. The Non-Saudi shareholder is however contesting a delay fine of SR 1.6 million imposed by the Department of Zakat and Income Tax.

26. CASH AND CASH EQUIVALENTS

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

	2008 SR'000	2007 SR'000
Cash and balances with SAMA, excluding statutory deposit (note 3)	1,292,407	830,444
Due from banks and other financial institutions with an original maturity of ninety days or less	2,583,616	3,061,518
Total	3,876,023	3,891,962

27. BUSINESS SEGMENTS

The Bank's primary segment reporting format is determined to be business segment. A business segment is a group of assets and operations engaged in providing products or services that are subject to risks and returns that are distinct from those of other business segments.

All of the Bank's operations are based in the Kingdom of Saudi Arabia.

Transactions between the business segments are recorded based on the Bank's transfer pricing methodologies. Segment assets and liabilities mainly comprise operating assets and liabilities.

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

Personal banking
Deposit, credit and investment products for individuals.

Corporate banking
Loans, deposits and other credit products for corporate, small to medium sized businesses and institutional customers.

Brokerage
Provides shares brokerage services to customers (this segment includes the activities of the Bank's subsidiary AlJazira Capital Company).

Treasury banking
Money market, trading and treasury services. Commission is charged to business segments based on a pool rate, which approximates the marginal cost of funds.

Other
Other operations of the Bank comprise funds management and other residual businesses, none of which constitutes a separately reportable segment.

a) The Bank's total assets and liabilities and its income from operations and net income for the year by business segment are as follows:

2008	Personal banking SR'000	Corporate banking SR'000	Brokerage SR'000	Treasury and other SR'000	Total SR'000
Total assets	2,562,374	13,119,473	539,620	11,298,238	27,519,705
Total liabilities	9,447,032	2,999,789	31,135	10,303,926	22,781,882
Total operating income	311,507	442,972	334,567	47,498	1,136,544
Charge for provision for credit losses, net	10,125	51,033	-	-	61,158
Impairment of other financial assets	-	-	-	62,238	62,238
Depreciation	34,936	6,110	20,812	13,082	74,940
Total operating expenses and minority interests	287,660	180,677	242,310	203,558	914,205
Net income	23,847	262,295	92,257	(156,060)	222,339

2007	Personal banking SR'000	Corporate banking SR'000	Treasury and other SR'000	Total SR'000
Total assets	1,876,146	8,780,373	10,907,469	21,563,988
Total liabilities	8,153,525	2,104,860	6,516,514	16,774,899
Total operating income	958,804	249,268	238,720	1,446,792
Reversal of provision for credit losses, net	-	(25,908)	-	(25,908)
Depreciation	46,841	4,988	6,415	58,244
Total operating expenses and minority interests	483,497	65,693	92,399	641,589
Net income	475,307	183,575	146,321	805,203

b) The Bank's credit exposure by business segment is as follows:

2008	**Personal banking SR'000**	**Corporate banking SR'000**	**Brokerage SR'000**	**Treasury and other SR'000**	**Total SR'000**
Consolidated balance sheet assets	2,216,639	13,112,544	2,724	8,406,517	23,738,424
Commitments and contingencies	-	2,302,945	-	52,802	2,355,747

2007	Personal banking SR'000	Corporate banking SR'000	Treasury and other SR'000	Total SR'000
Consolidated balance sheet assets	1,441,726	8,772,823	8,685,472	18,900,021
Commitments and contingencies	-	1,120,152	51,966	1,172,118

Credit exposure comprises the carrying value of consolidated balance sheet assets excluding cash, property and equipment, other real estate, investment in equities and mutual fund, certain other assets and the credit equivalent values of commitments, contingencies and derivatives.

28. CREDIT RISK

The Bank manages exposure to credit risk, which is the risk that one party to a financial instrument will fail to discharge an obligation and will cause the other party to incur a financial loss. Credit exposures arise principally in credit-related risk that is embedded in loans and advances and investments. There is also credit risk in off-balance sheet financial instruments, such as loan commitments.

For loans and advances and off-balance sheet financing to borrowers, the bank assesses the probability of default of counterparties using internal rating models. For investments, due from banks and off balance sheet financial instruments with international counterparties, the Bank uses external ratings of the major rating agencies.

The Bank attempts to control credit risk by monitoring credit exposures, limiting transactions with specific counterparties, and continually assessing the creditworthiness of counterparties. The Bank's risk management policies are designed to identify and to set appropriate risk limits and to monitor the risks and adherence to limits. Actual exposures against limits are monitored daily.

The Bank manages the credit exposure relating to its trading activities by monitoring credit limits, entering into master netting agreements and collateral arrangements with counterparties in appropriate circumstances, and limiting the duration of exposure. In certain cases, the Bank may also close out transactions or assign them to other counterparties to mitigate credit risk.

Concentrations of credit risk arise when a number of counterparties are engaged in similar business activities, or 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 risk indicate the relative sensitivity of the Bank's performance to developments affecting a particular industry or geographical location.

The debt securities included in the investment portfolio are mainly sovereign risk. Analysis of investments by counter-party is provided in note 5. For details of the composition of loans and advances refer to note 6. Information on credit risk relating to commitments and contingencies is provided in note 16. The information on banks maximum credit exposure by business segment is given in note 27.

The Bank in the ordinary course of lending activities holds collaterals as security to mitigate credit risk in the loans and advances. These collaterals mostly include time and other cash deposits, financial guarantees from other banks, local and international equities, real estate and other property and equipment. The collaterals are held mainly against commercial and individual loans and are managed against relevant exposures at their net realizable values. The Bank holds real estate collateral against transfer of title deed as collateral. Collateral generally is not held over due from banks & other financial institutions, except when securities are held as part of reverse repurchase. Collateral usually is not held against investment securities, and no such collateral was held at December 31, 2008 and 2007.

28. CREDIT RISK continued

The Bank uses an internal credit classification and review system to manage the credit risk within its loans portfolio. The classification system includes ten grades, of which seven grades relate to the performing portfolio (standard-low risk: risk ratings 1 to 3; standard-medium risk: risk ratings 4 to 6 and special mention; risk rating 7) and three grades relate to the non-performing portfolio (substandard, doubtful and loss; risk ratings 8 to 10). Loans and advances under the standard category are performing, have sound fundamental characteristics and include those that exhibit neither actual nor potential weaknesses. Specific provisions for impairment are maintained in respect of the non performing portfolio based on each borrower's grade, which is determined by the Bank's Credit Control Division using specific criteria such as activities, cash flows, capital structure, securities and delinquency. Additional portfolio provisions are created for losses, where there is objective evidence that unidentified losses are present at the consolidated balance sheet date. These are estimated based upon credit gradings allocated to the borrower or group of borrowers as well as the current economic climate in which the borrowers operate together with the experience and the historical default patterns that are embedded in the components of the credit portfolio. The Bank's Internal Audit Division independently reviews the overall system on a regular basis.

The Bank seeks to manage its credit risk exposure through the diversification of lending activities to ensure that there is no undue concentration of risks with individuals or groups of customers in specific locations or business. It also takes collateral as security when appropriate.

Management monitors the market value of collateral, requests additional collateral in accordance with the underlying agreement and monitors the market value of collateral obtained during its review of the adequacy of the allowance for impairment losses.

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

a) Credit quality of financial assets (Loans and advances and Due from banks and other financial institutions)

The credit quality of loans and advances is managed using internal credit ratings and for due from banks and financial institutions is managed using external credit ratings of internationally recognised rating agency. The table below shows the credit quality by class of asset.

	Loans and advances				Due from Banks and Other Financial Institutions	
2008	Consumer SR'000	Commercial SR'000	Others SR'000	Subtotal SR'000	SR'000	Total SR'000
Performing						
Neither past due nor impaired (performing)						
Standard – low risk	-	2,142,553	-	2,142,553	3,903,582	6,046,135
Standard – medium risk	-	10,092,067	-	10,092,067	-	10,092,067
Standard – unclassified	1,616,098	492,868	73,450	2,182,416	-	2,182,416
Sub total – standard	1,616,098	12,727,488	73,450	14,417,036	3,903,582	18,320,618
Special mention	-	430,873	-	430,873	-	430,873
Sub total	1,616,098	13,158,361	73,450	14,847,909	3,903,582	18,751,491
Past due but not impaired						
Less than 30 days	18,279	235,400	-	253,679	-	253,679
30-60 days	8,198	123,143	-	131,341	-	131,341
60-90 days	2,165	43,614	-	45,779	-	45,779
Over 90 days	1,036	2,099	-	3,135	-	3,135
Total	1,645,776	13,562,617	73,450	15,281,843	3,903,582	19,185,425
Less: portfolio provision	(24,619)	(113,750)	-	(138,369)	-	(138,369)
Net performing	1,621,157	13,448,867	73,450	15,143,474	3,903,582	19,047,056
Non Performing						
Total non Performing	9,449	223,409	-	232,858	-	232,858
Less: Specific provision	(10,997)	(232,182)	-	(243,179)	-	(243,179)
Less: Collateral	-	-	-	-	-	-
Net non performing	(1,548)	(8,773)	-	(10,321)	-	(10,321)

2007	Loans and advances Consumer SR'000	Commercial SR'000	Others SR'000	Subtotal SR'000	Due from Banks and Other Financial Institutions SR'000	Total SR'000
Performing						
Neither past due nor impaired (performing)						
Standard	638,670	8,785,553	70,532	9,494,755	3,662,768	13,157,523
Special mention	-	210,198	-	210,198	-	210,198
Sub total	638,670	8,995,751	70,532	9,704,953	3,662,768	13,367,721
Past due but not impaired						
Less than 30 days	12,521	274,325	-	286,846	-	286,846
30-60 days	1,123	693	-	1,816	-	1,816
60-90 days	237	14	-	251	-	251
Over 90 days	6,016	1,150	-	7,166	-	7,166
Total	658,567	9,271,933	70,532	10,001,032	3,662,768	13,663,800
Less: portfolio provision	(25,157)	(113,212)	-	(138,369)	-	(138,369)
Net performing	633,410	9,158,721	70,532	9,862,663	3,662,768	13,525,431
Non Performing						
Total non Performing	954	198,234	-	199,188	-	199,188
Less: Specific provision	(954)	(181,661)	-	(182,615)	-	(182,615)
Less: Collateral	-	(16,573)	-	(16,573)	-	(16,573)
Net non performing	-	-	-	-	-	-

Standard unclassified mainly comprise consumer, credit cards, small business, employee and share trading loans.

Performing loans as at December 31, 2008 include renegotiated loans of SR 719 million (2007: Nil).

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

28. CREDIT RISK continued

b) Credit quality of financial assets (Investments)

The credit quality of investments (excluding investment in equities and mutual fund) is managed using external credit ratings of international rating agencies. The table below shows the credit quality by class of asset.

	2008 SR'000	2007 SR'000
Performing		
High grade (AAA – BBB)	4,219,370	3,862,380
Standard grade (BA1 – B2)	-	-
Sub-standard grade (BA3 – C)	18,750	-
Unrated	-	-
Sub total	4,238,120	3,862,380
Past due but not impaired (accrued special commission receivable)		
0 – 30 days	-	-
30 – 60 days	-	-
60 – 90 days	-	-
Sub total	-	-
Total performing	4,238,120	3,862,380
Less: portfolio provision	-	-
Net performing	4,238,120	3,862,380
Overall Investments (excluding equities and mutual fund), net	4,238,120	3,862,380

As at December 31, 2008 and 2007, no provision was required for the impairment in the value of investments (excluding investment in equities and mutual fund).

c) An economic sector analysis of Bank's loans and advances

The tables below show an economic sector analysis of the Bank's loans and advances, net of specific and portfolio provisions; after taking into account total collateral held for both performing and non-performing loans and advances.

2008	Maximum exposure On-balance sheet, net of provisions SR'000	Off balance sheet credit – related commitments and contingencies, net of provisions SR'000	Total SR'000
Banks and other financial institutions	1,072,303	210,521	1,282,824
Agriculture and fishing	40,611	23,175	63,786
Manufacturing	3,521,788	820,907	4,342,695
Mining and quarrying	6,464	676,478	682,942
Electricity, water, gas and health services	30,556	26,060	56,616
Building and construction	2,116,360	920,903	3,037,263
Commerce	2,216,527	361,826	2,578,353
Transportation and communication	380,552	47,410	427,962
Services	99,369	98,225	197,594
Consumer loans and credit cards	1,619,609	-	1,619,609
Share trading	421,673	-	421,673
Other	3,607,341	1,050,600	4,657,941
Maximum exposure	15,133,153	4,236,105	19,369,258
Less: collateral for performing and non performing	(4,900,796)	(881,431)	(5,782,227)
Net maximum exposure	10,232,357	3,354,674	13,587,031

2007	Maximum exposure On-balance sheet, net of provisions SR'000	Off balance sheet credit – related commitments and contingencies, net of provisions SR'000	Total SR'000
Banks and other financial institutions	864,656	30,711	895,367
Agriculture and fishing	30,750	3,793	34,543
Manufacturing	2,375,058	436,483	2,811,541
Mining and quarrying	9,897	2,982	12,879
Electricity, water, gas and health services	19,744	269	20,013
Building and construction	498,905	778,765	1,277,670
Commerce	1,910,835	177,436	2,088,271
Transportation and communication	420,877	43,546	464,423
Services	106,461	87,912	194,373
Consumer loans and credit cards	633,410	3,931	637,341
Share trading	576,648	-	576,648
Other	2,431,995	638,948	3,070,943
Maximum exposure	9,879,236	2,204,776	12,084,012
Less: collateral for performing and non performing	(4,070,096)	(598,270)	(4,668,366)
Net maximum exposure	5,809,140	1,606,506	7,415,646

29. GEOGRAPHICAL CONCENTRATION

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

2008	Kingdom of Saudi Arabia SR'000	Other GCC and Middle East SR'000	Europe SR'000	North America SR'000	South East Asia SR'000	Other countries SR'000	Total SR'000
Assets							
Cash and balances with SAMA	2,249,578	-	-	-	8,881	-	2,258,459
Due from banks and other financial institutions	2,439,197	1,415,296	29,402	18,929	149	609	3,903,582
Investments	4,717,912	-	72,895	33,773	63,526	21,262	4,909,368
Loans and advances, net	15,012,130	97,417	-	-	-	23,606	15,133,153
Total	24,418,817	1,512,713	102,297	52,702	72,556	45,477	26,204,562
Liabilities							
Due to banks and other financial institutions	1,245,876	89,594	5,370	25,435	-	370	1,366,645
Customers' deposits	20,900,368	-	-	-	-	-	20,900,368
Total	22,146,244	89,594	5,370	25,435	-	370	22,267,013
Commitments and Contingencies	3,763,781	12,403	197,409	10,472	123,447	139,838	4,247,350
Credit exposure (credit equivalent)							
Commitments and contingencies	1,941,768	8,440	137,002	10,472	123,447	134,618	2,355,747

2007	Kingdom of Saudi Arabia SR'000	Other GCC and Middle East SR'000	Europe SR'000	North America SR'000	South East Asia SR'000	Other countries SR'000	Total SR'000
Assets							
Cash and balances with SAMA	1,476,903	-	-	-	13,880	-	1,490,783
Due from banks and other financial institutions	1,262,500	2,384,809	10,223	4,111	1,105	20	3,662,768
Investments	4,726,685	18,750	100,004	42,820	74,856	504	4,963,619
Loans and advances, net	9,740,615	101,121	-	-	37,500	-	9,879,236
Total	17,206,703	2,504,680	110,227	46,931	127,341	524	19,996,406
Liabilities							
Due to banks and other financial institutions	486,377	213,041	6,124	10,241	907	-	716,690
Customers' deposits	15,647,087	-	-	-	-	-	15,647,087
Total	16,133,464	213,041	6,124	10,241	907	-	16,363,777
Commitments and Contingencies	2,026,088	3,944	65,828	7,116	111,894	1,151	2,216,021
Credit exposure (credit equivalent)							
Commitments and contingencies	984,335	3,760	65,828	5,150	111,894	1,151	1,172,118

Credit equivalent of commitments and contingencies is calculated according to SAMA's prescribed methodology.

b) The distributions by geographical concentration of non-performing loans and advances and provision for credit losses are as follows:

	Non performing loans, net		Provision for credit losses	
	2008 SR'000	2007 SR'000	**2008 SR'000**	2007 SR'000
Kingdom of Saudi Arabia	238,888	199,188	381,548	320,984

30. MARKET RISK

Market risk is the risk that changes in market prices, such as special commission rate, credit spreads (not relating to changes in the obligor's / issuer's credit standing), equity prices and foreign exchange rates, will affect the Bank's income or the value of its holdings of financial instruments. The objective of market risk management is to manage and control market risk exposures within acceptable parameters, while optimising the return on risk.

The Bank separates its exposure to market risk between trading and non-trading portfolios. Trading portfolios mainly are held by the Treasury division and include equity investments and mutual fund that are managed on a fair value basis.

Overall authority for market risk is vested in the Board of Directors. The Bank's Board of Directors sets limits for the acceptable level of risk in trading book.

The market risk for the trading book and non-trading book is managed and monitored using sensitivity analysis.

a) Market risk trading book

Market risk on trading mainly arises from the foreign currency exposures and changes in equity prices and net asset value of mutual fund.

i) Currency risk

Currency risk is the risk that the value of a financial instrument will fluctuate due to changes in foreign exchange rates. The Bank manages exposure to the effects of fluctuations in prevailing foreign currency exchange rates on its financial position and cash flows. The Board has set limits on positions by currency. Positions are monitored twice daily to ensure positions are maintained within established limits.

At the end of the year, the Bank has the following significant exposure, net of minority interest, in its trading book, denominated in foreign currencies as at December 31:

Currency	2008 SR'000	2007 SR'000
USD	13,977	24,581
EUR	14,458	28,531
GBP	9,650	18,952
YEN	24,666	32,566

The table below indicates the extent to which the Bank was exposed to currency risk at December 31, 2008 on its foreign currency positions. The analysis is performed for a reasonable possible movement of the currency rate against the Saudi riyal with all other variable held constant on the consolidated statement of income. A negative amount in the table reflects a potential net reduction in consolidated statement of income, while a positive amount reflects a net potential increase. The sensitivity analysis does not take account of actions that might be taken by the Bank to mitigate the effect of such changes.

	2008		2007	
Currency	Increase in currency rate in %	Effect on profit SR'000	Increase in currency rate in %	Effect on profit SR'000
USD	+3.0	419	+5.0	1,229
EUR	+17.7	2,559	+3.2	912
GBP	+18.8	1,814	+3.8	720
YEN	+16.8	4,144	+1.1	358

ii) Equity price risk

Equity price risk is the risk that the fair value of equities decreases as a result of changes in the levels of equity index and the value of individual stocks.

The financial instruments included in the trading portfolio are equity securities held by three mutual funds that are subsidiaries of the bank, murabaha investments (mutual fund) and equity securities held by AlJazira Capital Company. The bank manages the risk relating to the murabaha investment by monitoring changes in net asset value of the murabaha investments. The investments in equity securities held by the subsidiaries of the bank are managed by the bank in conjunction with professional investment advisors, and the equity price risk is monitored by the bank on a portfolio basis for each mutual fund. The effect on the consolidated statement of income as a result of a change in the fair value of equity instruments held for trading at December 31, 2008 and 2007 due to reasonably possible changes in the underlying respective fund's net asset value, with all other variables held constant, is as follows:

30. MARKET RISK continued

a) Market risk trading book continued

ii) Equity price risk continued

Portfolio	2008 Increase / decrease in equity price %	2008 Effect on consolidated income statement SR'000	2007 Increase / decrease in equity price %	2007 Effect on consolidated income statement SR'000
Al Thoraiya	-35.2	(10,726)	-14.9	(7,951)
Al Khair	-34.1	(5,877)	-12.5	(3,797)
Al Mashareq	-37.0	(8,913)	-14.9	(4,963)

The effect on the consolidated statement of income as a result of a change in the fair value of murabaha investments held for trading at December 31, 2008 and 2007 due to reasonably possible change in the net asset value (NAV) of the fund, with all other variables held constant, is as follows:

Portfolio	2008 Increase / decrease in NAV %	2008 Effect on consolidated income statement SR'000	2007 Increase / decrease in NAV %	2007 Effect on consolidated income statement SR'000
Murabaha investments	+0.50	1,753	+0.50	2,510
Murabaha investments	-1.25	(4,382)	-0.75	(3,765)

b) Market risk – non trading or banking book

Market risk on non-trading or banking positions mainly arises from the special commission rate, foreign currency exposures and equity price changes.

i) Special commission rate risk

Special commission rate risk arises from the possibility that changes in special commission rates will affect future cash flows or the fair values of financial instruments. The Bank's Assets Liabilities Committee (ALCO) has established limits on the special commission rate gap. Positions are monitored on a daily basis and reported on a monthly basis to ALCO to ensure positions are maintained within the established limits. In case of stressed market conditions, the asset-liability gap may be reported to ALCO more frequently.

The following table depicts the sensitivity due to reasonably possible changes in special commission rates, with other variables held constant, on the Bank's consolidated statement of income. The sensitivity of the income is the effect of the assumed changes in special commission rates on the net special commission income for one year, based on the special commission bearing non-trading financial assets and financial liabilities held as at December 31, 2008. All the non-trading book exposures are monitored and analyzed in currency concentrations and relevant sensitivities are disclosed in local currency. The sensitivity analysis does not take account of actions that might be taken by the Bank to mitigate the effect of such changes.

Currency	2008 Increase / decrease in basis point	2008 Sensitivity of special commission income SR'000	2007 Increase / decrease in basis point	2007 Sensitivity of special commission income SR'000
SR	+50	1,000	+50	14,723
SR	-125	(2,500)	-75	(22,085)
USD	+50	(4,025)	+50	(1,106)
USD	-125	10,061	-75	1,659

Commission rate sensitivity of assets, liabilities and off-balance sheet items

The Bank manages exposure to the effects of various risks associated with fluctuations in the prevailing levels of market commission rates on its financial position and cash flows.

The table below summarizes the Bank's exposure to commission rate risks. Included in the table are the Bank's assets and liabilities at carrying amounts, categorized by the earlier of the contractual re-pricing or the maturity dates. The Bank is exposed to commission rate risk as a result of mismatches or gaps in the amounts of assets and liabilities and off-balance sheet instruments that mature or re-price in a given period. The Bank manages this risk by matching the re-pricing of assets and liabilities through risk management strategies.

2008	Within 3 months SR'000	3-12 months SR'000	1-5 years SR'000	Over 5 years SR'000	Non commission bearing SR'000	Total SR'000	Effective commission rate
Assets							
Cash and balances with SAMA	-	-	-	-	2,258,459	2,258,459	-
Due from banks and other financial institutions	2,532,450	1,241,012	-	-	130,120	3,903,582	3.72%
Investments	1,638,120	2,350,000	250,000	-	671,248	4,909,368	4.30%
Loans and advances, net	10,153,809	3,427,969	909,234	598,494	43,647	15,133,153	5.94%
Other real estate, net	-	-	-	-	75,797	75,797	-
Property and equipment, net	-	-	-	-	493,503	493,503	-
Other assets	-	-	-	-	745,843	745,843	-
Total assets	14,324,379	7,018,981	1,159,234	598,494	4,418,617	27,519,705	-
Liabilities and equity							
Due to banks and other financial institutions	1,363,228	-	-	-	3,417	1,366,645	2.97%
Customers' deposits	11,470,671	3,849,519	79,563	-	5,500,615	20,900,368	2.52%
Other liabilities	-	-	-	-	514,869	514,869	-
Shareholders' equity including minority interests	-	-	-	-	4,737,823	4,737,823	-
Total liabilities and Equity	12,833,899	3,849,519	79,563	-	10,756,724	27,519,705	-
On balance sheet gap	1,490,480	3,169,462	1,079,671	598,494	(6,338,107)	-	-
Total commission ratesensitivity gap	1,490,480	3,169,462	1,079,671	598,494	(6,338,107)	-	-
Cumulative commission rate sensitivity gap	1,490,480	4,659,942	5,739,613	6,338,107	-	-	-

2007	Within 3 months SR'000	3-12 months SR'000	1-5 years SR'000	Over 5 years SR'000	Non commission bearing SR'000	Total SR'000	Effective commission rate
Assets							
Cash and balances with SAMA	-	-	-	-	1,490,783	1,490,783	-
Due from banks and other financial institutions	3,013,223	601,250	-	-	48,295	3,662,768	4.67%
Investments	2,476,978	1,537,500	350,000	-	599,141	4,963,619	5.12%
Loans and advances, net	5,471,187	3,320,273	501,518	389,812	196,446	9,879,236	6.97%
Other real estate, net	-	-	-	-	75,797	75,797	-
Property and equipment, net	-	-	-	-	459,303	459,303	-
Other assets	-	-	-	-	1,032,482	1,032,482	-
Total assets	10,961,388	5,459,023	851,518	389,812	3,902,247	21,563,988	-
Liabilities and equity							
Due to banks and other financial institutions	587,235	-	-	-	129,455	716,690	4.45%
Customers' deposits	7,636,292	1,830,696	31,000	-	6,149,099	15,647,087	2.97%
Other liabilities	-	-	-	-	411,122	411,122	-
Shareholders' equity including minority interests	-	-	-	-	4,789,089	4,789,089	-
Total liabilities and Equity	8,223,527	1,830,696	31,000	-	11,478,765	21,563,988	-
On balance sheet gap	2,737,861	3,628,327	820,518	389,812	(7,576,518)	-	-
Total commission ratesensitivity gap	2,737,861	3,628,327	820,518	389,812	(7,576,518)	-	-
Cumulative commission rate sensitivity gap	2,737,861	6,366,188	7,186,706	7,576,518	-	-	-

The effective commission rate (effective yield) of a monetary financial instrument is the rate that, when used in a present value calculation, results in the carrying amount of the instrument. The rate is a historical rate for a fixed rate instrument carried at amortised cost and a current market rate for a floating rate instrument or an instrument carried at fair value.

30. MARKET RISK continued

b) Market risk – non trading or banking book continued

ii) Currency risk

Currency risk is the risk that the value of a financial instrument will fluctuate due to changes in foreign exchange rates. The Bank manages exposure to the effects of fluctuations in prevailing foreign currency exchange rates on its financial position and cash flows. The Board has set limits on positions by currency. Positions are monitored on a daily basis to ensure positions are maintained within established limits.

At the end of the year, the Bank has the following significant net exposures denominated in foreign currencies as at December 31:

Currency	2008 SR'000 Long (short)	2007 SR'000 Long (short)
USD	17,662	95,430

The table below indicates the extent to which the Bank was exposed to currency risk at 31 December 2008 on its foreign currency positions. The analysis is performed for a reasonable possible movement of the currency rate against the Saudi riyal with all other variable held constant on the consolidated statement of income. A negative amount in the table reflects a potential net reduction in consolidated statement of income, while a positive amount reflects a net potential increase. The sensitivity analysis does not take account of actions that might be taken by the Bank to mitigate the effect of such changes.

	2008		2007	
Currency	Increase in currency rate in %	Effect on profit SR'000	Increase in currency rate in %	Effect on profit SR'000
USD	+3	530	+5	4,771

iii) Equity price risk

Equity price risk is the risk that the fair value of equities decreases as a result of changes in the levels of equity index and the value of individual stocks.

The effect on shareholders' equity (other reserves) as a result of a change in the fair value of equity instruments held as available-for-sale at 31 December 2008 and 2007 due to reasonably possible changes in the following market index, with all other variables held constant, is as follows:

	2008		2007	
Market Index	Increase / decrease in index %	Effect on shareholders' equity (other reserve) SR'000	Increase / decrease in index %	Effect on shareholders' equity (other reserve) SR'000
Tadawul	24.22	34,614	22.14	87,821

31. LIQUIDITY RISK

Liquidity risk is the risk that the Bank will be unable to meet its payment obligations when they fall due under normal and stress circumstances. Liquidity risk can be caused by market disruptions or credit downgrades, which may cause certain sources of funding to be less readily available. To mitigate this risk, management has diversified funding sources in addition to its core deposit base, manages assets with liquidity in mind, maintaining an appropriate balance of cash, cash equivalents and readily marketable securities and monitors future cash flows and liquidity gaps on a daily basis. The Bank also has committed lines of credit that it can access to meet liquidity needs.

In accordance with the Banking Control Law and the regulations issued by SAMA, the Bank maintains a statutory deposit with SAMA of 7% of total demand deposits and 4% of savings and time deposits. In addition to the statutory deposit, the Bank also maintains liquid reserves of not less than 20% of the deposit liabilities, in the form of cash or assets that can be converted into cash within a period not exceeding 30 days. The Bank has the ability to raise additional funds through repo facilities available with SAMA up to 75% of the value of Murabaha placements with SAMA.

The liquidity position is assessed and managed under a variety of scenarios, giving due consideration to stress factors relating to both the market in general and specifically to the Bank. One of these methods is to maintain limits on the ratio of liquid assets to deposit liabilities, set to reflect market conditions. Liquid assets consist of cash, short term bank deposits, Murabaha placements with SAMA and liquid debt securities available for immediate sale. Deposits liabilities include both customers and Banks, excluding non-resident Bank deposits in foreign currency. The Bank also monitors the loan to deposit ratio. The liquidity ratio during the year was as follows:

	2008 %	2007 %
As at 31 December	**42**	55
Average during the period	**43**	53
Highest	**50**	59
Lowest	**36**	47

a) Analysis of financial liabilities by remaining contractual maturities

The table below summarises the maturity profile of the Bank's financial liabilities at 31 December 2008 and 2007 based on contractual undiscounted repayment obligations; as special commission payments up to contractual maturity are included in the table, totals do not match with the balance sheet. The contractual maturities of liabilities have been determined on the basis of the remaining period at the consolidated balance sheet date to the contractual maturity date and do not take into account the effective expected maturities as shown on note (b) below (Maturity analysis of assets and liabilities for the expected maturities). Repayments which are subject to notice are treated as if notice were to be given immediately. However, the Bank expects that many customers will not request repayment on the earliest date the Bank could be required to pay and the table does not reflect the expected cash flows indicated by the Bank's deposit retention history.

	On demand SR'000	**Less than 3 months SR'000**	**3-12 months SR'000**	**1-5 years SR'000**	**Over 5 years SR'000**	**Total SR'000**
Financial liabilities						
As at 31 December 2008						
Due to banks and other financial institutions	**45,036**	**1,332,616**	**-**	**-**	**-**	**1,377,652**
Customers' deposits	**5,500,615**	**11,248,813**	**4,131,575**	**318,320**	**-**	**21,199,323**
Total undiscounted financial liabilities 2008	**5,545,651**	**12,581,429**	**4,131,575**	**318,320**	**-**	**22,576,975**
Financial liabilities						
As at 31 December 2007						
Due to banks and other financial institutions	29,455	691,956	-	-	-	721,411
Customers' deposits	6,149,099	7,706,268	1,899,091	37,595	-	15,792,053
Total undiscounted financial liabilities 2008	6,178,554	8,398,224	1,899,091	37,595	-	16,513,464

The contractual maturity structure of the Bank's credit-related contingencies and commitments are shown under note 16.

31. LIQUIDITY RISK continued

b) Maturity analysis of assets and liabilities

The table below shows an analysis of assets and liabilities analysed according to when they are expected to be recovered or settled. See note (a) above for the Bank's contractual undiscounted financial liabilities. For presentation purposes demand deposits are included in "No fixed maturity" category.

2008	Within 3 months SR'000	3-12 months SR'000	1-5 years SR'000	Over 5 years SR'000	No fixed maturity SR'000	Total SR'000
Assets						
Cash and balances with SAMA	-	-	-	-	2,258,459	2,258,459
Due from banks and other financial institutions	1,033,446	2,078,156	791,980	-	-	3,903,582
Investments	1,000,000	470,000	2,768,120	-	671,248	4,909,368
Loans and advances, net	3,060,954	7,207,188	2,974,274	1,449,513	441,224	15,133,153
Other real estate, net	-	-	-	-	75,797	75,797
Property and equipment, net	-	-	-	-	493,503	493,503
Other assets	388,419	244,717	107,666	4,649	392	745,843
Total assets	5,482,819	10,000,061	6,642,040	1,454,162	3,940,623	27,519,705
Liabilities and equity						
Due to banks and other financial institutions	1,024,984	341,661	-	-	-	1,366,645
Customers' deposits	3,341,815	8,984,611	3,073,326	-	5,500,616	20,900,368
Other liabilities	83,180	55,064	1,154	-	375,471	514,869
Shareholders' equity including minority interests	-	-	-	-	4,737,823	4,737,823
Total liabilities and equity	4,449,979	9,381,336	3,074,480	-	10,613,910	27,519,705

2007	Within 3 months SR'000	3-12 months SR'000	1-5 years SR'000	Over 5 years SR'000	No fixed maturity SR'000	Total SR'000
Assets						
Cash and balances with SAMA	-	-	-	-	1,490,783	1,490,783
Due from banks and other financial institutions	903,967	2,289,631	420,875	-	48,295	3,662,768
Investments	975,000	980,625	1,906,755	-	1,101,239	4,963,619
Loans and advances, net	2,735,868	5,392,354	1,165,699	389,861	195,454	9,879,236
Other real estate, net	-	-	-	-	75,797	75,797
Property and equipment, net	-	-	-	-	459,303	459,303
Other assets	689,840	209,306	22,322	65,919	45,095	1,032,482
Total assets	5,304,675	8,871,916	3,515,651	455,780	3,415,966	21,563,988
Liabilities and equity						
Due to banks and other financial institutions	343,618	343,617	-	-	29,455	716,690
Customers' deposits	2,290,888	5,894,613	1,312,487	-	6,149,099	15,647,087
Other liabilities	47,285	23,869	3,990	-	335,978	411,122
Shareholders' equity including minority interests	-	-	-	-	4,789,089	4,789,089
Total liabilities and equity	2,681,791	6,262,099	1,316,477	-	11,303,621	21,563,988

32. FAIR VALUES OF FINANCIAL ASSETS AND LIABILITIES

Fair value is the amount for which an asset could be exchanged or a liability settled between knowledgeable, willing parties in an arm's length transaction. Consequently, differences can arise between carrying values and fair value estimates.

The fair values of on balance sheet financial instruments are not significantly different from the carrying values included in the consolidated financial statements. The estimated fair values of other investment held at amortised costs are based on quoted market prices, when available. The fair values of these investments are disclosed in note 5.

33. RELATED PARTY TRANSACTIONS

In the ordinary course of its activities, the Bank transacts business with related parties. In the opinion of management and the Board of Directors, the related party transactions are conducted at market rates. The related party transactions are governed by the limits set by the Banking Control Law and regulations issued by SAMA. The balances as at December 31 resulting from such transactions included in the consolidated financial statements are as follows:

	2008 SR'000	2007 SR'000
National Bank of Pakistan (shareholder)		
Due from banks and other financial institutions	203	364
Due to banks and other financial institutions	376	108,828
Other liability	-	16
Directors, key management personnel, other major shareholders and their affiliates		
Loans and advances	1,214,244	568,668
Customers' deposits	913,658	683,480
Other assets	-	867
Commitments	21,410	38,785

Other major shareholders represent shareholdings of more than 5% of the Bank's issued share capital.

Income, expenses and other transactions with related parties included in the consolidated financial statements are as follows:

	2008 SR'000	2007 SR'000
Special commission income	67,902	38,507
Special commission expense	43,791	31,292
Fees from banking services	1,615	740
Other expenses	4	307

The total amount of compensation paid to directors and key management personnel during the year is as follows:

	2008 SR'000	2007 SR'000
Short-term employee benefits	47,437	32,633
Termination benefits	26,011	32,550

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

34. 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.

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 balance sheet assets, commitments and notional amount of derivatives at a weighted amount to reflect their relative risk. SAMA requires to hold the minimum level of the regulatory capital and maintain a ratio of total eligible capital to the risk-weighted assets at or above the agreed minimum of 8%.

	2008	
	Eligible Capital SR'000	Capital Adequacy Ratio %
Core capital (Tier 1)	4,633,827	19.34
Supplementary capital (Tier 2)	138,369	-
Core and supplementary capital (Tier 1 + Tier 2)	4,772,196	19.92

Tier 1 capital of the Bank at the year end comprises share capital, statutory, other reserves, retained earnings, proposed dividend and minority interest less other prescribed deductions. Tier 2 capital comprises a prescribed amount of eligible portfolio provisions (collective provisions) less prescribed deductions.

The Bank has implemented Basel II effective January 1, 2008 as stipulated by SAMA. The Bank uses the Standardized approach of Basel II to calculate the risk weighted assets and required Regulatory Capital for Pillar -1 (including credit risk, market risk and operational risk). The Bank's Risk Management Division is responsible for ensuring that minimum required Regulatory Capital calculated is compliant with Basel II requirements. Quarterly prudential returns are submitted to SAMA showing the Capital Adequacy Ratio.

	2008 SR'000
Credit risk	20,865,998
Operational risk	2,959,409
Market risk	129,538
Total pillar-1 – risk weighted assets	23,954,945

35. INVESTMENT MANAGEMENT SERVICES

The Bank offers investment management and advisory services to its customers, compliant with the principle of Shari'ah (avoiding interest). These services include portfolio management on discretionary and non discretionary bases and management of investment funds in conjunction with professional investment advisors. Five such funds for which the Bank acts as the manager are Al-Khair Global Equities Fund, Al-Thoraiya European Equities Fund, Al-Mashareq Japanese Equities Fund, Al-Taiyebat Saudi Equities Fund and Al-Qawafel Fund. All are open-ended mutual funds for Saudi and foreign nationals. Al-Khair, Al-Thoraiya and Al-Mashareq funds invest in foreign equities, while Al-Taiyebat fund invests in local equities. Al-Qawafel fund trades in commodities through Murabaha. The financial statements of Al-Khair, Al-Thoraiya, and Al-Mashareq funds are consolidated with these financial statements.

The Bank also provides investment management and other services to the policyholders of its Takaful Ta'awuni program.

36. PROSPECTIVE CHANGES IN ACCOUNTING STANDARDS

IFRS 8 "Operating Segments" has been published in its final form and is mandatory for compliance for the accounting year beginning 1 January 2009. It replaces IAS 14 on segment reporting. IAS 1 "Presentation of financial statements" has been revised and is mandatory for compliance for the accounting year beginning from 1 January 2009. The application of revised IAS 1 will result in amendments to the presentation of the financial statements. The Bank will apply the revised IAS 1 and IFRS 8 in 2009.

37. BOARD OF DIRECTORS' APPROVAL

The consolidated financial statements were approved by the Board of Directors on February 7, 2009 (Safar 12, 1430H).

38. BASEL II PILLAR 3 DISCLOSURES

Under Basel II pillar 3, certain quantitative and qualitative disclosures are required, and these disclosures, which are not required to be audited, will be made available on the Bank's website www.baj.com.sa and the annual report, respectively as required by the Saudi Arabian Monetary Agency (SAMA).

Basel II – Pillar 3 Qualitative Disclosures

For the year ended December 31, 2008

SCOPE OF APPLICATION

A. The name of the top corporate entity in the group, to which these regulations apply, is Bank Al Jazira.

B. The following table lists the entities that are consolidated in the group financial statements, where control exists, for accounting and regulatory purposes:

Entity Name	Consolidation	
	Accounting	Regulatory
AlJazira Capital Company	Yes	Yes
Aman Real Estate	Yes	Yes
Al-Mashareq Japanese Equity Fund	Yes	No
Al-Khair Global Equity Fund	Yes	No
Al-Thoraiya European Equity Fund	Yes	No

i. Entities that are fully consolidated for regulatory purposes are:

1. AlJazira Capital Company (JAZC):

JAZC is incorporated in Saudi Arabia as a capital market company to carryout the investment banking activities of the group including; brokerage, asset management, arranging, advisory and custody. The company commenced its operations during 2008.

2. Aman Real Estate:

Aman is incorporated in Saudi Arabia as a custodian of title deeds for real estate pledged to the Bank as collateral against credit facilities or/and mortgage lending. The company commenced its operations during 2006.

ii. Entities that are not consolidated for regulatory purposes are:

The other three entities namely Al-Mashareq, Al-Khair and Al-Thoraiya are the international mutual funds operated by the Bank; all are incorporated in Saudi Arabia. The Bank consolidates the funds for accounting purposes due to holding a significant portion of the units outstanding (seed capital) and due to being a manager of these funds thus having control.

Due to the nature of the funds business of units being subscribed to or/and redeemed on a daily basis and since the risk associated with the third parties units do not affect the financial position of the Bank; these funds are not consolidated for regulatory purposes. Furthermore, the Bank's own units held are part of the Held for Trading Investments and are considered for the purpose of calculating capital adequacy under Pillar I.

C. There are no restrictions, or other major impediments, on transfer of funds or regulatory capital within the group.

CAPITAL STRUCTURE

The components of the regulatory capital for Bank Al Jazira are as follows:

	SR'000
Tier One Capital:	
Share capital	3,000,000
Eligible reserve	1,451,000
Retained earnings	188,943
IAS type adjustments	(3,141)
Deductions from Tier I:	
Reciprocal holding of bank capital at 50% deduction	(2,973)
Total Tier One Capital	**4,633,829**
Tier Two Capital:	
Portfolio provision	138,369
Total Tier One and Tier Two Capital	**4,772,198**

CAPITAL STRUCTURE continued

The major components of Tier One & Tier Two Capital of the Bank are:

1. Eligible share capital
The issued and outstanding share capital of the Bank consists of 300 million ordinary shares at SR 10 each. These shares carry equal voting rights.

2. Eligible reserve
Eligible reserves are created by accumulated appropriations of profits and are maintained for future growth. In accordance with Saudi Arabian Banking Control Law and the Articles of Association of the Bank, a minimum of 25% of the annual net income is required to be transferred to a statutory reserve until this reserve equals the paid-up capital of the Bank.

3. Eligible retained earnings
This represents the accumulated undistributed profits that are available for future dividend distributions as recommended by the Board and approved by the General Assembly.

4. Portfolio provision
This is the portfolio provision created under IAS 39 to cover the incurred but not reported losses in the loan portfolio.

CAPITAL ADEQUACY

When assessing the adequacy of its capital BAJ takes the following objectives into consideration:

A Primary Capital Objectives

- **Core Capital Purpose**

i. The directors' objective is to expand the BAJ proposition in Saudi Arabia with a future intention of expansion in the high growth region of the Gulf for Shari'ah compliant Financial Services. The directors' present program is one of expansion and building on success for long term growth, with the majority of capital held to support the expansion.

ii. Capital is held with the purpose to generate the required expected shareholders returns from the successful provision of innovative Shari'ah compliant banking services to individuals, businesses and institutions.

iii. Capital is held to safeguard the Bank's ability to continue as a going concern and to maintain an adequate capital base in order to preserve the rights of all stakeholders including; shareholders, depositors, the community and its' employees.

iv. Capital is held with the purpose to meet the assessed Capital Adequacy Requirements, for Pillar I and II, so that the actual Tier 1 and Tier 2 capital meets regulatory targets, by the greater of the:
   a. minimum regulatory capital requirements (Directors ICAAP); or
   b. Minimum Supervisory ICAAP Guidance (SAMA's ICAAP assessment).

   The directors hold an additional haircut cushion, the Internal Management Buffer, of 1% of the ICAAP Pillar I assessment above the 1) and 2) assessments for core capital purposes.

- **External Credit Rating**
  BAJ's second objective is to achieve a longer term "steady" rating in the A+ to A- range for credit rating to:

i. Facilitate short term transactions in the inter-bank deposit market with tenors up to 2 years for funding and balance sheet management; and

ii. Support the issue of medium term, 3 – 7 year, Sukuks, Shari'ah compliant commercial paper and Musharaka programmes supporting funding and balance sheet growth strategies. Underlying portfolios for these programmes are proposed to consist of sound ring-fenced income generating assets.

B Specific Capital Objectives

- **Investment Capital**

BAJ specific strategy is to grow and expand the investment in financial services in range and service offering with investment opportunities. The directors holding in the investment capital is to support the risk uncertainty and price volatility on exposures [Foreign Exchange, Property Exposures, Mutual Funds, Equities & etc] providing a level of comfort for depositors.

- **Trading Services**

BAJ has a specific objective of holding capital to engage in trading through identifiable channels:

i. Credit Risk Capital for Shari'ah compliant financing services are:
   a. Tawaraq and Murabaha contracts. Product descriptions are Dinar, Naqa'a and Taman;
   b. Trade financing advances – Letters of Credit/Guarantees;
   c. Istinsa'a contracts; and
   d. Ijarah transactions;

ii. Market Risk Capital for Shari'ah compliant Trading are:
   a. Treasury Trading;
   b. Musharaka.

iii. Operational Risk Capital
   The specific objective of providing payment, transaction and professional services exposing BAJ to operational risk failures.

RISK EXPOSURE AND ASSESSMENT
GENERAL QUALITATIVE DISCLOSURE REQUIREMENTS

A. Risk Management

The bank's business operations require identification, measurement, aggregation and effective management of risks and efficient allocation of capital to derive an optimal risk and return ratio. The bank manages its risks in a structured, systematic and transparent manner through a risk policy that embeds risk management into the organizational structure, risk measurement and monitoring processes. The key features of the bank's comprehensive risk management policy are:

- The Board of Directors provides overall risk management direction and oversight.
- The bank's risk appetite is determined by the senior management and approved by the Board of Directors.
- Risk management is embedded in the bank as an intrinsic process and is a core competency of all its employees.
- The bank manages its credit, market, operational and liquidity risks in a centralized manner within the organization.
- The bank risk management function is independent of the business divisions.
- The bank's internal audit function reports to the Board Audit Committee and provides independent validation of the business unit's compliance with risk policies and procedures and the adequacy and effectiveness of the risk management framework on a bank wide basis.

Due to their non-compliance with Shari'ah, the bank does not currently use derivatives and other similar instruments to manage exposures resulting from changes in commission rate, foreign exchange rate, equity risks and credit risks. Collateral are used to reduce the bank's credit risk. The bank is in the process of developing derivative instruments that will be Shari'ah compliant.

The risk management function assists senior management in controlling and actively managing the bank's overall risk. The function also ensures that:

- The bank's overall business strategy is consistent with its risk appetite approved by the Board of Directors and allocated by senior management.
- Risk policies, procedures and methodologies are consistent with the bank risk appetite.
- Appropriate risk management architecture and systems are developed and implemented.
- The portfolio of risks and limits are monitored throughout the bank.

i. Risk Management Organization

The risk management activities are predominantly organized out of the business units' function by Group Risk Management and various committees that deal with the different risk categories. The Group Risk Management carries out the daily and monitoring activities, and also prepares and implements review and control policies on all risk portfolios. Therefore, responsibility of Group Risk Management is to identify, measure, evaluate and report on all risks to which the bank is exposed. Subsidiaries have assigned risk managers who report its risk status to Group Risk Management Head.

ii. Scope and nature of risk reporting tools

The comprehensive risk management framework enables the bank to identify, assess, limit and monitor risks using a comprehensive range of quantitative and qualitative tools. Some of these tools are common to a number of risk categories, while others are tailored to the particular features of specific risk categories and enable generation of information such as:

- Credit risk in commercial and consumer lending and other asset exposures such as collateral coverage ratio, limit utilization, past-due alerts, etc.
- Quantification of the susceptibility of the market value of single positions or portfolios to changes in market parameters (commonly referred to as sensitivity analysis).
- Quantification of exposure to losses due to extreme movements in market prices or rates.

The bank continuously assesses the adequacy and effectiveness of its reporting tools in light of the changing risk environment.

iii. Risk management processes

Through the comprehensive risk management framework, transactions and outstanding risk exposures are quantified and compared against authorized limits, whereas non-quantifiable risks are monitored against policy guidelines and key risk and control indicators. Any discrepancies, excesses or deviations are escalated to senior management for appropriate action.

RISK EXPOSURE AND ASSESSMENT
GENERAL QUALITATIVE DISCLOSURE REQUIREMENTS continued

B. Methodology and Assumptions

i. Current Methodology and Assumptions

The current methodology adopted by the bank on the implementation of SAMA requirements for implementation of BASEL II is structured in two phases. The bank elected Internal Capital Adequacy Assessment Plan (ICAAP) methodology for the implementation program is to calculate Pillar I capital requirements and then add the Pillar 2 assessments.

The Pillar 1 risks (Credit, Market and Operational) have been assessed under the following approaches:

- Credit Risk – Standardized Approach,
- Market Risk – Standardized Approach , and
- Operational Risk – Basic Indicator Approach.

The Bank is in compliance with Basel II since January 2008.

ii. Future Methodology

The Bank's methodology for Phase II is to build and develop the risk management capabilities, processes, records and testing to support implementation of:

- Credit Risk – IRB Foundation Approach, and
- Market and Operational Risk – Standardized Approach

The development and implementation of the infrastructure and resources are expected to enhance the risk management capabilities and capacity.

The key risks assumed by the bank in its daily operations are outlined below:

1. Credit risk

Credit risk is defined as the likelihood that a customer or counterparty is unable to meet the contracted financial obligations resulting in a default situation and/or financial loss. Credit risk arises in the bank's normal course of business.

The bank utilizes the standardized approach for Pillar I credit risk. The parameters used for risk weighted assets represent the rates approved by the supervisory authority.

The bank uses external rating (where available) from Fitch and Moody's to supplement internal rating during the process of determining the credit limits of the counterparties. Unrated exposures are risk weighted as supervisory authority guidelines for capital adequacy purposes. The bank uses the guidelines issued by supervisory authority to map the credit assessment ratings provided by eligible external credit assessment institutions (ECAL's) to determine risk weighted exposures.

Credit risk management strategy

The approach to credit risk management is based on the foundation to preserve the independence and integrity of the credit risk assessment, management and reporting processes combined with clear policies, limits and approval structures which guide the day to day initiation and management of the bank's credit risk exposure. This approach comprises credit limits that are established for all customers or credit and product programs after a careful assessment of their creditworthiness.

Standing procedures, outlined in the bank's credit policy manual, require that all credit proposals be subjected to detailed screening by the credit group pending submission to Management Credit Committee and/or Credit Executive Committee. Whenever necessary, credit facilities are secured by acceptable forms of collateral to mitigate the related credit risks. The Board of Directors defines the bank's credit risk management strategy and approves significant credit risk policies to ensure alignment of the bank's exposure with their risk appetite.

In addition, all credit facilities are continually monitored based on periodical review of the credit performance and obligor rating.

Key features of corporate credit risk management

- Credit facilities are granted based on detailed credit risk assessments which include prevailing and potential macro-economic factors, industry trends and the customer's positioning within its industry.
- In compliance with SAMA regulations, lending to connected parties is secured as per the requirements specified in Banking Control Law and supervisory authority rules and monitored by Credit Executive Committee. Such transactions are made on substantially the same terms, including commission rates and collateral, as those prevailing at the time for comparable transactions with other parties. All such facilities are approved by the Board of Directors through Credit Executive Committee of the Board. The bank limits its exposure per connected party group to 10% of the bank's capital and reserves.
- The corporate proprietary internal-rating model has been successfully rolled out and is regularly reviewed by the bank's risk management function to enhance in line with industry credit risk management "best practices". The bank is in the process to roll out facility rating model for Corporate Banking Group. Due from banks and financial institutions is managed using external credit ratings of internationally recognized rating agencies.

- All new proposals and or material changes to existing credit facilities are reviewed and approved by the appropriate credit committee outlined below:

    1. Credit Executive Committee
    2. Management Credit Committee
    3. Retail Credit Committee

- The credit facility administration process is undertaken by a segregated function to ensure proper execution of all credit approvals and maintenance of documentation, and proactive control over maturities, expiry of limits, collateral valuation and legal covenants.

- Country limits are determined based on the outlook of economic and political factors, along with the review of reports by rating agencies on the country (where available).

- Cross-border exposures are committed after obtaining supervisory authority prior approval and monitored by credit risk management function.

Key features of consumer credit risk management

- Credit-scoring models are used to facilitate underwriting and monitoring of credit facilities to customers and certain small businesses.

- Applicant "scoring" is used for underwriting purposes. Scoring is used in tandem with assessment of the applicant's "Ability to Repay" such as debt-to-income ratio, minimum income and caps on advances by product type.

- Bank applies its lending policy which incorporates supervisory authority guidelines and policies related to consumer credit facilities.

Bank credit risk monitoring

The bank's exposures are continuously monitored through a system of triggers and early-warning signals aimed at detecting adverse symptoms that could result in deterioration of credit risk quality. The triggers and early-warning systems are supplemented by facility utilization and collateral valuation monitoring together with a review of upcoming credit facility expiration and market intelligence to enable timely corrective action by management. The results of the monitoring process are reflected in the internal rating process.

Credit risk is monitored on an ongoing basis with formal quarterly reporting to ensure senior management awareness of shifts in credit quality and portfolio performance.

A specialized team handles the management and collection of problem credit facilities.

Credit Risk – Impairment

In managing its portfolio, the bank utilizes ratings and other measures and techniques which seek to take account of all aspects of perceived risk. Credit exposures classified as 'High' quality are those where the ultimate risk of financial loss from the obligor's failure to discharge its obligation is assessed to be low. These include facilities to corporate entities with financial condition, risk indicators and capacity to repay which are considered to be good to excellent. Credit exposures classified as 'Standard' quality comprise all other facilities whose payment performance is fully compliant with contractual conditions and which are not impaired. The ultimate risk of possible financial loss on 'Standard' quality is assessed to be higher than that for the exposures classified within the 'High' quality range.

The bank classifies its exposure into ten risk categories. Of these, seven categories are for performing and three for non-performing. Each borrower is rated on an internally developed objective risk rating model that evaluates risk based on financial as well as qualitative factors such as management strength, industry characteristics and account conduct. An independent credit unit reviews the assigned ratings periodically. Exposures falling below a certain classification threshold (8 to 10) are considered to be impaired and appropriate specific provisions are made against them by comparing the present value of expected future cash flows for each such exposure with its carrying amount based of the criteria prescribed by IAS 39. Collective impairment is also measured and recognized on portfolio basis for group of similar credits that are not individually identified as impaired.

Past-due and impairment provisions

Credit facilities are classified as "past due" when a payment has not been received on its contractual payment date, or if the facility is in excess of pre-approved limits.

A credit facility is considered as "impaired" if the profit or principal installments are past due for more than 90 days, or if the carrying amount of the facility is greater than its estimated recoverable value. The principle of *materiality* should be taken into consideration when determining an event of default.

Past-due and impaired facilities are managed and monitored as "irregular facilities" and are classified into the following four categories which are then used to guide the provisioning process:

Category	Criteria	Grades	Provision %
Watch list	Irregular for a period up to 90 days		
Substandard	Irregular for a period between 91 and 180 days	8	25%
Doubtful	Irregular for a period between 181 days and 365 days	9	50%
Loss	Irregular for a period exceeding 365 days	10	100%

The bank may also include a credit facility in one of the above categories based on management's judgment of a customer's financial and/or non-financial circumstances.

Basel II – Pillar 3 Qualitative Disclosures continued

For the year ended December 31, 2008

RISK EXPOSURE AND ASSESSMENT
GENERAL QUALITATIVE DISCLOSURE REQUIREMENTS continued

1. Credit risk continued

Standardized Approach and Supervisory Risk Weights

The External Credit Assessment Institutions (ECAIs) that the bank utilizes for the purpose of assessing the credit under the Standardized Approach are Fitch and Moody's.

Credit Risk Mitigation

The bank uses a wide variety of techniques to reduce credit risk on it is lending, one important credit risk mitigation technique is accepting guarantee and collateral with appropriate coverage. The bank ensures that the collateral held is sufficiently liquid, legally effective and regularly valued. The method and frequency of revaluation depends on the nature of the collateral involved.

Collateral provided by the customer shall not be considered as a primary source for repayment. The bank requests collateral in order to protect its claims. The type and quality of collateral depends on the type of transaction, the counterparty and risks involved.

Concentration of credit risk arise from exposure to customers having similar characteristics in terms of the industry and business sector in which they are engaged, such that their ability to discharge contractual obligations may be similarly affected by change in political, economic or other conditions.

The bank's comprehensive risk management framework has specific guidelines that focus on maintaining a diversified portfolio to avoid excessive concentration of risk which is implemented through customer and economic sector limit structures. This risk is managed by diversification of the portfolio which is implemented through client, industry, geographic and product.

Risk transfer in the form of syndicated loans or risk participation arrangements with other banks is common practices to limit the banks exposures.

The bank pledge agreement give another mitigation technique through allowing the bank to net credit and debit balances in the event of default of the counter party.

All interrelated companies controlled by the same management and/or ownership structure are treated as one entity/group. The bank limits its credit concentration per entity/group to 15% of the bank's capital and reserves. In some cases, it is possible to extend an entity/group up to 25% of the bank's capital and reserves provided it enjoys outstanding credit worthiness.

As Shari'ah compliant bank, the nature of the Islamic product entitled the bank with other mitigation techniques such as the ownership of the goods in Murabaha product and the possession of the leased assets in Ijara product.

Management of credit collateral and valuation

The main types of collateral accepted by the bank are:

1. Real estate
2. Quoted shares
3. Cash collateral
4. Bank guarantees
5. Acknowledge assignment of contracts

In accordance with the bank's credit policies, banks, creditworthy companies and individuals with high net worth are accepted as guarantor counterparties, subject to credit risk assessment. Furthermore, in accordance with SAMA / Basel II framework, from the above collateral only cash collateral and banks guarantees are recognized for capital adequacy purposes.

The method and frequency of revaluation depends on the nature of the collateral involved. The amount, type and valuation of collateral are based on guidelines specified in the risk management policies. The custody and revaluation of collateral are performed independent of the business units.

2. Market Risk – Standardized Approach

"Market" risk is defined as the potential loss in value of financial instruments caused by adverse movements in market variables such as commission rates, foreign exchange rates and equity prices.

Market-risk management framework

All instruments and exposures that were subject to market risk were assessed using standardized approach for Pillar I market risk.

The market risk management framework governs the bank's trading and non-trading related market risk. Market risk stemming from trading activities is managed by the relevant group. The management and oversight of market risk inherent within the bank's non-trading activities is the primary responsibility of the bank Asset and liability Committee. All activities giving rise to market risk are conducted within a structure of approved credit and position limits.

Monitoring of "market" risk from "trading" activities
The bank risk management function independently monitors the trading market risk exposure to derive quantitative measures specifically for market risk under normal market conditions.

Monitoring of non-trading market risk in the "banking" book
The bank's key non-trading market risk is the sensitivity of its net commission income to movements in commission rates. Commission rate risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market commission rates.

Currently, the bank uses the following risk measures and limits to identify, measure and monitor the market risk in the trading and banking book:

- Cut-loss limits;
- Commission rate sensitivity;
- Commission rate gaps;
- Maturity gaps; and
- Liquidity ratios limit.

These limits and exposures are reviewed in ALCO meetings.

The commission rate risk in the "banking" book is managed through a "gap" limit structure which is supplemented by periodic analysis of scenarios to capture the extreme indicative measure of exposure to commission rate changes. The analysis of scenarios showed an impact in the banking book as follows:

31 December, 2008	+50bp	-125bp
31 December, 2007	+50bp	-75bp

The bank is exposed to commission rate risk as a result of mismatches or gaps in the amounts of assets and liabilities that mature or re-price in a given period. The bank manages this risk by matching the re-pricing of assets and liabilities through risk management strategies.

Liquidity Risk
Liquidity risk is defined as the inability to generate sufficient financial resources to meet all obligations and commitments as they fall due, or having to access funds to meet payment obligations at an excessive cost. It is the policy of the group to maintain adequate liquidity at all times.

The bank applies a prudent mix of liquidity controls which provide security of access to funds without undue exposure to increased costs of funds from the liquidation of assets, or aggressive bidding for deposits. Liquidity risk is monitored and evaluated daily by Treasury to ensure that, over the short term and by major currency, the profile of projected future cash inflows is adequately matched to the maturity of the liabilities.

The bank uses a mixed approach of cash flow match approach and liquid assets approach. Under the cash flow approach the Bank attempts to match the cash outflow against the contractual cash inflow leaving around one month cash requirements at all times to absorb unexpected cash movement. Whereas the excess liquidity for over one month is managed on the basis of liquid asset approach and as per SAMA guidelines.

To address these risks, management seeks to diversify funding sources to match the growth of its assets with funding.

The bank has to maintain liquid assets of at least 20% of deposit liabilities in the form of cash or assets that can be converted into cash within a period not exceeding 30 days.

The maturity of assets and liabilities is disclosed to determine the sensitivity to commission rate risk.

In accordance with Banking Control Law and the regulations issued by SAMA, the bank maintains a statutory deposit with SAMA. The bank has the ability to raise additional funds through repo facilities with SAMA.

The market risk department is in the process of implementing an advanced financial risk management system that will enable the Bank to measure and monitor the risk more effectively and frequently. It will provide tools to enable sophisticated what-if analyses at various levels of the Bank's portfolios and its trading and banking book. Further, it will allow dynamic simulation, scenario analysis, back and stress test at various levels of granularities of portfolio.

Foreign exchange risk
Foreign exchange risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in foreign exchange rates.

Foreign exchange risks are controlled through limits pre-established by the Board of Directors on currency position exposures and in total for both over night and intra-day positions which are monitored daily. Assets are typically funded in the same currency to minimize exchange exposures. Appropriate segregation of duties exists between the front and back office functions, while compliance with position limits is monitored on an ongoing basis.

RISK EXPOSURE AND ASSESSMENT
GENERAL QUALITATIVE DISCLOSURE REQUIREMENTS continued

3. Operational Risk

Operational risk is defined as the risk of loss resulting from inadequate or failed internal processes, people and systems, or from external events. The operational risk arises largely as a result of unauthorized activities such as frauds, human errors, inefficiencies, system failure or other external factors. Currently, the bank is utilizing the basic indicator approach for operational risk capital charge under Pillar I.

Operational risk management framework

The Bank has adopted a dynamic enterprise risk management approach to comply with sound practices of operational risk management as mandated by Basel Committee and SAMA. The risk management policies, methodologies and processes are aimed to comply with Basic Indicator Approach. Operational risk capital is assessed at 15% of average gross revenue for recent three years as per guidelines for BIA approach.

An independent operational risk management function has been established, reporting to the Chief Risk Officer, to manage operational risks. This department is responsible to identify, assess, quantify, control and report on the status of operational risk management. The bank has acquired a technology system (Control and Risk Environment system) to keep data base of all risks, mitigating controls and losses / errors. The risk assessment of major activities of the bank was performed with the help of an independent consultant and participation of operational experts from the relevant Department, Internal Audit and Risk Management. Any risk not adequately mitigated, is targeted for enhancement of procedures and systems. For every entity, a risk profile is prepared showing major weaknesses and recommended action for enhancement of controls.

As per the Bank's operational risk policy, the risk profile for major entities will be reassessed annually to ensure the risk assessment is current and any changes in the products and organizational structure are taken into account.

Compliance self assessment guidelines have been developed for all key controls to check that the controls are deployed as required. All key controls are tested at least 3 times a year by the Unit Head and reports are sent to Risk Management to update CARE data base. Going forward, Internal Audit will also be required to independently verify during annual audits that all controls are working as desired.

Periodically, a risk summary report is generated that shows progress on risk assessment, gaps in the control environment, controls not working as desired, risks not fully mitigated and recommendations pending for enhancement of systems and controls. This report is used by the management to evaluate operational risk governance and provide guidance on the strategy and approach.

The Bank's business processes are closely monitored to identify, assess, control and prevent potentially illicit use of the Bank's services for laundering money and/or financing terrorism. The bank's "anti money laundering" and "combating terrorism financing" initiatives are regularly reviewed to ensure compliance with local regulatory requirements and international best practices.

The bank has established a frauds investigation committee to investigate any internal and external fraudulent activity, its causes and recommend preventive actions to the executive management.

Business Continuity: The bank has a business continuity management planning process under which critical activities of the bank have been identified as well as resources required to continue those activities in case of disaster. A review will be done to realign the plans to reorganization and bank's disaster recovery management to ensure plans are operational. Bank has also established a disaster recovery centre where most major IT systems have been set up as back up to the main data centre.

Equities in the Banking Book

The bank is also exposed to market risk as a result of changes in the "fair value" of its strategic equity and investment positions held as Available for Sale Investments.

Equity price risk is the risk that the fair values of equities will fluctuate as a result of changes in the level of equity indices or the value of individual share prices. The bank manages the risk through diversification of investments.

The bank conducts periodic scenario analysis in the banking book to gauge changes in economic value under extreme market conditions and provides timely inputs to senior management.