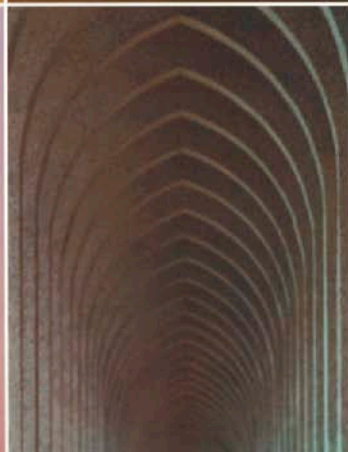


# Annual Report 1994

بنك الأهلي التجاري  
THE NATIONAL COMMERCIAL BANK



# 1994



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الهيئة العامة للغذاء والدواء  
THE NATIONAL COORDINATING BODY



King Fahad Bin Abdulaziz Al Saud  
*The Custodian of the two Holy Mosques*



His Royal Highness Prince Abdullah  
Bin Abdulaziz Al Saud  
*Crown Prince and First Deputy Prime Minister  
Commander of the National Guard*



His Royal Highness Prince Sultan  
Bin Abdulaziz Al Saud  
*Second Deputy Premier  
Minister of Defence and Aviation  
and Inspector General*

## A Tribute

*In opening this Annual Report, The National Commercial Bank pays tribute to the life of the Bank's founder, Sheikh Salim Bin Ahmed Bin Mahfouz, who died towards the end of the year.*



Sheikh Salim was truly the founder of banking in the Kingdom of Saudi Arabia, an incredible feat considering his lack of formal education and a cultural environment hostile to the most fundamental banking practices until the 1950s.

Born in the province of Hadramout, Yemen, Salim Mahfouz left home with one of his brothers when only six years old in order to find work to support his impoverished family.

After a series of travel adventures that took him many thousands of kilometres by foot and even across the Red Sea to Africa, the young Mahfouz arrived in the Holy City of Mecca in 1916. Here he tried a number of menial jobs and travelled the long journey home twice before settling in Mecca in 1922.

After working in a shop with his brother, Abdullah, Salim was sent to work in the household of the Kaaki family, an encounter that was to shape his future. Stubbornly refusing the offered job as a household help, Salim insisted that he should be put into the Kaaki's moneychanging business.

To test the cheeky youth, the Kaakis sent him into the Mecca souk with a gold sovereign to change. He came back with more than they expected and became their leading currency exchanger.

Such was his financial success for the family that the Kaakis astutely took Salim into a new financial partnership under his management that was to continue, almost without alteration, for the next half century.

From a starting capital of 2,000 gold sovereigns, by 1949 the Mahfouz-Kaaki venture had grown into a major financial services company with a value of 400,000 gold sovereigns—equivalent at that time to SR8 million.

A new partnership agreement gave Sheikh Salim absolute control and the company provided services to clients which included the Ministry of Finance. It also was the receiver of the government's oil revenues and the paymaster of government employees. But the business could not carry the title of 'Bank' since banks were still not permitted in the Kingdom.

However, Sheikh Salim had a vision of founding Saudi Arabia's first officially recognised bank and lobbied hard for royal acceptance. At the same time, and supported by his customers, he wanted it to be a 'national bank' to respond to the needs of the whole Saudi economy.

His efforts were eventually rewarded when, in 1951, King Abdul Aziz Ibn Saud relented and The National Commercial Bank was empowered by Royal Decree a year before the foundation of the Saudi Arabian Monetary Agency.

Sheikh Salim Bin Mahfouz steered the growth of NCB as its General Manager for the next three decades before retiring from executive duties. Thereafter he continued to be closely involved in major policy decisions of the Bank.

During his time at the helm of NCB, he introduced many 'firsts' to the Kingdom, including a national housing scheme for low income families and bank-funded irrigation systems for impoverished rural areas. He also played a major part in the structuring of government borrowings and in the successful development of Saudi Arabia's commercial and industrial base. Other family interests included hospitals, health clinics, property and insurance.

A modest man of great personal integrity, Sheikh Salim was universally known in the Kingdom and beyond for his unchallenged reputation for honesty and trust alongside his unrivalled financial acumen.

Sheikh Salim realised within his lifetime a dream far removed from his humble beginnings. He created the first, and still the leading, modern financial institution in the Kingdom and he did so while earning the confidence, respect and friendship of his colleagues, his customers, his international counterparties and his country.

The legacy of Sheikh Salim's sons is felt by everyone who comes into contact with various interests the family is pursuing, including The National Commercial Bank.

## Vision Statement



*The National Commercial Bank is the leading bank in Saudi Arabia.*

- NCB's dual purpose is to enhance the value of the firm and to serve society;
- NCB is the first choice for customers and for talented employees;
- NCB is primarily a commercial bank providing deposit, investment and innovatively tailored products to retail, middle income and high net worth customers;
- NCB engages selectively in corporate business with a full range of financial services for the commercial sector and specialist financial services for large corporate clients. NCB is building a diversified portfolio with returns commensurate with the risks;
- NCB's core values are customer service and reward for performance and teamwork.



# Financial Highlights

## 1994 Performance

SR Millions	1994	1993	Change	%
Total Assets	69,468	66,715	2,753	4.1
Total Customer Deposits	52,794	51,439	1,355	2.6
Total Liabilities	62,371	59,763	2,608	4.4
Total Partners' Equity	7,097	6,952	145	2.1
Contra Accounts	57,095	45,746	11,349	24.8
Operating Income	3,569	3,108	461	14.8
Operating Expenses	2,873	2,751	122	4.4
Net Operating Income	696	357	339	95.0
Other Income (Expense)	(117)	146	(263)	180.1
Net Income	579	503	76	15.1

## Selected Ratios %

Return on partners' equity	8.2	7.2
BIS total ratio	20.9	21.8
Partners' equity as % of total assets	10.2	10.4
Loans & Advances as % of total assets	47.6	41.0
Securities as % of total assets	26.3	23.6
Liquid assets ratio	45.5	51.8
Deposits to Loans & Advances	1.6	1.9

## Key Facts about NCB



*The National Commercial Bank has:*

- The largest Capital Base in Saudi Arabia
- 240 Branches – the most comprehensive network in Saudi Arabia
- 30 Dedicated Islamic Banking Branches
- 5,200 Staff
- The latest, 'state-of-the-art' Banking Technology
- 161 Automatic Teller Machines – 16% of the market
- 1,800 Electronic Point of Sale Terminals – 18% of the market
- Visa and MasterCard with 'Revolving Credit'
- 'NCB Private Banking' with offices in the Kingdom, and representation in London and Geneva
- Overseas Branches in Bahrain and Beirut
- Representative Offices in Major Financial Centres
- Over 570 International Correspondent Banks
- Saudi Arabia's leading Investment Services business; with a range of 24 Open and Closed-End Investment Funds
- In excess of SR11 billion funds under Investment Management
- Over 20,000 Investment Account Holders

## Chairman's Statement

*For The National Commercial Bank, 1994 represented a healthy continuation of our return to financial and strategic strength.*

I am pleased on behalf of everyone working with NCB, to describe several of the most notable features of an eventful year.

Net income increased 15% over 1993 to SR580 million. Difficult market conditions, including abrupt and volatile movements in financial asset values, render this year's result a creditable achievement.

Net income from operations, before provisions, rose by 95% over 1993 to nearly SR700 million, indicating the continued momentum of our earnings power.

The Bank's risk-weighted Tier 1 capital adequacy ratio, as defined by the 'Basle Guidelines' for G10 countries, rose to 17%, well in excess of internationally required levels.

A 10% reduction in our operating expenditures is evidence of an aggressive cost management programme.

Staff levels have been reduced by 2,200 from their peak in 1993. Annual saving in personnel costs of more than SR200 million will be realised as a result. Redundancies were handled sympathetically and involved generous end-of-service payments. The process ensured fair treatment for everyone affected. We disliked losing friends and colleagues but we also accepted that the future must be faced with staff levels that meet our needs.

As part of the same strategy, we have been substantially upgrading our cadre of seasoned professionals. More than 200 professionals joined NCB during the year, providing experience and expertise to key areas such as technology, treasury, corporate finance, marketing, communications and auditing.

To enhance our talent pool and to build for a challenging future, expatriate supervisors have been charged with the development of Saudi nationals as a fundamental responsibility. In a global industry, we will always benefit from international personnel bringing specialised skills. At the same time, NCB is committed to the development of young Saudi talent; creating opportunities for them to strengthen our future together.

Recognising the need for sharing benefit with those who do the most to help NCB achieve its targets, we introduced in 1994 a performance bonus programme. This SR45 million investment will yield rich dividends. This programme is one of many ways in which NCB is being transformed into a market-driven, performance culture.

Helping this process, a major structural change to how NCB manages itself took place during the year. From June 1st, 1994, our traditional, regionalised structure was replaced by eleven highly focused divisions. These divisions have been designed to target distinct

markets, such as Retail, Corporate Banking, Private Banking, etc. and to thereby serve specific customer needs effectively. Already, there are clear signs that this new focus has been well received. Increased levels of commercial deposits and loans are pleasing aspects of the year's performance and the trend is expected to continue.

With regard to overall asset management, we took essential steps in adopting risk asset policies reflective of today's banking environment. We are installing a sophisticated portfolio management system and credit control process which are designed to maintain the integrity of our loan portfolio under all market conditions.

Last year we further increased NCB's investment in technology. By the end of 1994, almost 65% of our customer transactions were being processed by a 'state-of-the-art', on-line, real-time system. A year earlier less than 10% of transactional volume was automated. This system provides access to a central database for customers, wherever they choose to transact their banking. The effect has been to reduce transaction times for most counter services to a fraction of their pre-automation levels – something that research shows all our customers appreciate. NCB plans to have virtually all of its volume transactions converted to this system by mid-1995.



In a separate project, labelled 'Al Sagr' (The Falcon Project) inside the Bank, we have redesigned our transaction flows on a phased basis. Operations previously handled in branch 'back offices', are being removed to regional operations centres where we can concentrate and leverage expertise and technology. This leaves the branches free to concentrate energy on delivering the highest standards of customer contact and the effective distribution of our products and services.

Despite the many advances that have been made so far, we know that there is no room for complacency in the intensely competitive Saudi banking marketplace. Certain current initiatives will take several years of hard work to complete but with a clear vision, determined will and adequate resources, NCB will assert itself as the leader of the banking industry in Saudi Arabia and the Middle East.

The Ministry of Finance and National Economy and the Saudi Arabian Monetary Agency have again provided a sound banking environment which balances regulation and control with freedom for new ideas to flourish. They have our gratitude for this and their continued guidance.

On behalf of The National Commercial Bank and its staff, I take this opportunity to express our gratitude to our customers and our banking friends at home and abroad for their continuing support. We are forever conscious that it was their goodwill and trust upon which this great institution was founded and upon which it will always depend.

We celebrate the memory of Sheikh Salim Ahmed Bin Mahfouz as a visionary in the development of banking in the Kingdom. We also remember his personal commitment to fulfilling his responsibilities to society as a whole. We recognise how great is our responsibility to sustain, in the years ahead, his integrity, independence and initiative in shaping our future.

At a time when a great deal of change is having to be embraced, the Bank's staff deserve our gratitude for showing great loyalty and dedication in securing our future success through serving our customers so well today.



Mohamed Salim Bin Mahfouz  
Chairman

# *Depth*

Because our roots are deep within the community we serve, we are able to see opportunities that other might miss.



## Review of Activities



*On June 1st, 1994, The National Commercial Bank undertook a radical reorganisation of its management structure with the aim of better serving its target markets.*

This move from a traditional, regionally based structure to a market and function based one has enabled NCB to streamline its operations while enhancing its service potential.

The eleven divisions were: Retail Banking, Corporate & Institutional Banking, Treasury, Investment Services, Private Banking, Islamic Banking, Systems & Operations, International Banking, Audit Finance & Accounting and Support Services. Since the year end we have added Corporate Communications.

### Retail Banking

Retail banking underwent a year of purposeful change in 1994 that has further equipped NCB to set new standards of customer service.

It was a year for new ground rules, new faces and new ways of doing almost everything.

Until the middle of 1994, the NCB branch network had served all segments of the banking market and much of the its primary operations took place at branch level.

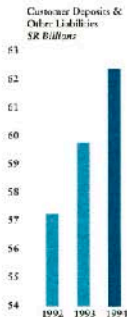
In June 1994, however, the branch network was freed to concentrate on better delivery of Retail Banking's range of consumer orientated products and services to individual customers.

This was achieved by removing to separate business units those product groups best managed as discreet profit centres, such as Corporate & Institutional Banking, and by focusing, wherever possible, the operations

activities not suited to branch network delivery into specialist operations centres.

It is much to its credit that Retail Banking managed such an immense programme of internal change while holding down costs, launching competitive new services and attracting increased levels of business. Most important, detailed market research indicates that customer loyalty has been sustained while the benefits to the consumer are beginning to be recognised.

A pilot 'model' branch was launched in November 1994 at Khalidia, Jeddah, setting new standards for retail banking in the Middle East with its streamlined operations, consumer friendly technology and emphasis on personal contact between the customer and NCB. Armed with this successful developmental experience, a roll out plan for more model branches will be introduced in 1995.



## Review of Activities



### Retail Banking continued

Much of the new technology that went into the model branch is also on offer to clients across the Kingdom as NCB Electronic Banking Services continued its rapid expansion and product development programme.

By the end of 1994, NCB had installed 161 Automatic Teller Machines (ATMs), representing 16% of all ATMs in Saudi Arabia and increasing our transaction volumes by 20% over 1993. The aim for 1995 is to increase the level to 300 ATMs, with emphasis on sites away from existing NCB branches, thereby improving customer accessibility.

We start 1995 with 1,800 point of sale terminals across the Kingdom, approximately 18% of the total installed base. We ended 1994 by introducing the facility for customers to use both Visa and MasterCard on our terminals, in addition to their ATM cards. We were one of only four banks to offer this flexibility.

In the last quarter of 1994, the addition of Visa as well as MasterCard to our product offer was one of the highlights of an active year for Electronic Banking. The Visa agreement allows us to be the Visa Transaction Acquirer Bank for merchants, while we also added the 'revolving credit card' for both Visa and MasterCard. This means we can give our customers the choice of clearing balances outstanding by either full monthly payment or by instalments.

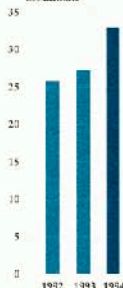
With the introduction of Visa and the continued successful marketing of MasterCard, our overall card base increased in 1994 by nearly 40% and we have ambitious targets for 1995.

NCB's business principles call for a sustained performance culture within the Bank that transmits into an outward-looking, market-orientated

dedication to our customers. Retail Banking and Electronic Banking Services, as elsewhere in NCB, considerably expanded their training programmes in 1994 with the objective of increasing awareness of new systems and procedures, enhancing skill levels and, where necessary, changing internal cultures.

In all this activity, the needs of the customer and the quality of NCB's products and delivery to the customer, have been paramount.

Loans & Advances  
S.R. Billions



### Corporate & Institutional Banking

The division continues to assist the development of the Kingdom's basic industries through project finance and the provision of working capital facilities. During the year, NCB provided facilities packages of SR570 million to United Sugar Company for the first sugar refinery in the Kingdom and of SR156 million for the completion of the first dedicated grain storage and rice processing facility at Jeddah International Seaport.

One of the most exciting capital project developments in the Kingdom at present



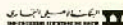
# *Commitment*

We are committed to provide our customers with quality of service that exceeds their expectations.





## Review of Activities

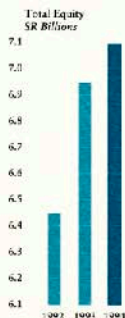


### Corporate & Institutional Banking *continued*

is the construction of a 'state-of-the-art' pharmaceutical production plant for Glaxo Saudi Arabia at South Jeddah. NCB assisted in this major Al-Yamamah Offset Project by making available facilities of SR140 million.

A detailed understanding of the needs of the petrochemical industry has long been a strength of NCB. We were pleased to be the Agent Bank and one of three arrangers and underwriters for a US\$225 million Term Loan Facility for the Al-Jubail Fertilizer Company (SAMAD) to part finance construction of a 2-Ethyl Hexanol plant at Jubail.

Another major financing in this sector involved NCB as principal coordinator and member of a six bank group that arranged and underwrote a US\$500 million Term Loan facility for Saudi Petroleum Company (SADAF), covering almost half of its US\$1,081 million refinery expansion. At the year end, we arranged for two more international banks to join the group, increasing the total sum underwritten to US\$700 million, with syndication in January 1995.



The cement industry is one of the Kingdom's most active sectors, with three companies launching substantial expansions of their production facilities in 1994. In all three cases, NCB supported the appointed contractor, Klockner-Humboldt-Deutz AG of Germany, by providing working capital finance and guarantees in excess of SR1.4 billion. Some of these facilities were successfully syndicated in the region and we further directly supported the three cement companies, Arabian Cement, Saudi Cement and Yanbu Cement, with letters of credit and working capital facilities that totalled more than SR1.5 billion.

In another contribution to the development of the Kingdom's infrastructure, NCB has become closely involved with the financing of the US\$3.9 billion telephone system expansion contract, awarded to AT&T by the Ministry of Post Telegraphs and Telephones. So far, the Bank has provided facilities of US\$75 million to finance housing and offices and we are in discussions with contractors over a further US\$544 million of related projects.

Commercial enterprise in our national and regional markets continues to grow and NCB has assisted the Savola Group by providing a SR250 million term loan facility to support its future growth plans. We also underwrote the construction financing of three McDonald's outlets in the Eastern Province, with negotiations continuing on three more.

NCB Corporate & Institutional Banking extended its product range with cash management services to clients such as Mawarid Group and Savola Group. The division made available SR33 million of acquisition financing to Conversion Industries Limited – which included NCB taking an equity stake in the company. Another first was a SR413 million automobile receivable securitisation programme for Abdul

## Review of Activities



### Corporate & Institutional Banking *continued*

Latif Jameel Company Ltd., part of which was offered to the local market through NCB Investment Services. These transactions were generated by NCB's recently established Corporate Finance unit which engineers sophisticated solutions to complex client problems.

### Treasury

Last year was notable as the year in which NCB Treasury really began to meet the needs of our customers for Treasury products and services.

Greater efficiency, improved service levels, creativity in providing new products and services and a better understanding of the needs of customers has also brought increased activity.

The size of the Treasury operation was increased significantly, with a number of top-flight professionals joining the division from outside the Bank or from elsewhere in NCB. A new office was opened in Riyadh to serve customers in the Central and Eastern provinces and the decision was taken to re-open the Treasury in our Bahrain branch.

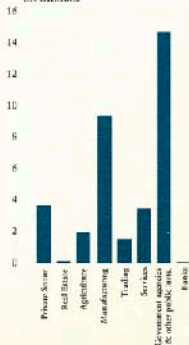
All customer-related activities have been focused into one group in the Treasury called the Client Services Desk. Its dealers have the mission: "To profitably service the market information, balance sheet and cash flow risk management and treasury product needs of our NCB clients". Teamwork and training are taken seriously and practised daily on the Client Services Desk as the team delivers ever higher standards of client service.

Recognising the link between strong Money Market and Trading operations and a robust client business, NCB Treasury strengthened both functions in 1994, giving further power to the client servicing package.

### Investment Services

In 1994, NCB Investment Services reaffirmed its place as leader of the Kingdom's mutual fund market. Providing investors with a broad range of innovative, high-quality funds and investment opportunities combined with professional advice in a friendly, professional atmosphere has become the hallmark of NCB's investment arm.

Loans and Advances by Sector - Domestic (Net)  
SR Millions



NCB Investment Services now offers a range of 24 open and closed-end funds and is involved in raising capital for corporate clients through private placements.

Funds launched in the year included the NCB South East Asia Equity Fund, a fund specialising in the fast-growing markets in the region other than Japan. This fund proved to be highly popular, as did the limited period re-opening of the NCB International Real Estate Fund III. The range of products will be extended by new funds to be launched in 1995, including a number that fully conform to Shariah principles.

# *Vitality*

A new spirit is driving us to find  
imaginative solutions for the  
changing needs of our customers.



## Review of Activities



### Investment Services *continued*

NCB Investment Services developed an intensive programme to accelerate its investment in advanced technology. This will further enhance customer service as well as facilitate the introduction of new products that are specifically tailored to individual customer needs.

As part of its commitment to maintain its leadership position, NCB Investment Services recruits the best international advisors and ensures that its team of professional managers is equipped and trained to produce superior performance.

### Private Banking

The Private Banking division, launched in 1993, developed healthily and to expectations in 1994 with the opening of three offices in the Kingdom, in Riyadh, Jeddah and AlKhobar, and two in Europe, in London and Geneva.

Well positioned to be the Bank of choice for Saudi High Net Worth Individuals, NCB Private Banking offers independently-managed, discreet services under stringent conditions of confidentiality. While everyone throughout NCB is dedicated to customer confidentiality, this basic banking philosophy by definition needs to be most scrupulously observed within the private banking environment.

NCB's relationship managers, called 'Private Bankers' in the marketplace, offer clients a blend of local and international financial products and services, both from within NCB's product range and from other providers. Extensive and continuing research and training keeps NCB's Private Bankers ahead in this highly competitive marketplace.

NCB Private Banking is proving popular with wealthy Saudi women who appreciate the division's home visit

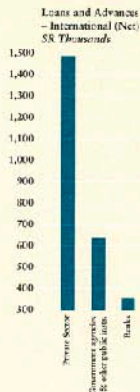
service by Private Banking's female relationship managers.

The unit is also, in co-operation with NCB Corporate & Institutional Banking and other NCB divisions, identifying on behalf of its clients new local and regional investment and project financing opportunities.

### Islamic Banking

There has been a rapid rise over the past decade in the number of financial institutions offering products and services that conform to Islamic principles. The worldwide acceptance of Islamic Banking, which has really evolved only since the mid-70s, now has an estimated global market value of over US\$80 billion with a growth rate of 15%.

NCB is committed to supporting and promoting its own Islamic Banking services alongside, and complementary to, its other Banking streams. The number of dedicated branches operated by the division rose to 27 at the end of





## Review of Activities



### Islamic Banking continued

1994, from 19 at the end of 1993, and this level of growth will be maintained in 1995.

NCB Islamic Banking attracted a total of invested funds of SR1.35 billion across the different categories and sectors of Islamic investment including Murabaha, Musharaka and Mudaraba.

NCB is pleased to be the underwriter and lead sponsor of a unique study into the current practices and future of Islamic financing being conducted by Harvard University in association with the Jeddah-based, Islamic Development Bank.

The 'Harvard University Islamic Investment Study' is bringing together, it is believed for the first time, the combined expertise of Harvard's Business School, Law School and its Center for Middle Eastern Studies. In all, over 20 Harvard academics and researchers, working with NCB, the IDB and other sponsors, are involved in the project.

The initial findings of this two year study are expected to be collated towards the end of 1995, with publication by Harvard the following year. As a leader in the development of modern financial services that adhere to Islamic principles, NCB has given every encouragement to this study as it will benefit the whole Islamic financial community.

### Systems & Operations

A core determining factor for the advance of change at NCB is the ability to provide the operational structure, technology and systems to support the new demands of the marketplace.

Unseen by our customers, this division has played a pivotal role in enabling beneficial change to happen, on time and with minimal service disruption. This makes the division very much the engine room of our business.

Alongside the introduction of new systems and new technology that have



significantly reduced transaction process times, the division has been at the centre of a massive education and training drive. This is equipping existing and new NCB staff with the latest skills in order to complement our investment in new ways of providing service.

Of particular note was the speed at which Systems & Operations converted our branches to the necessary enhanced level of automation. The plan for 1994 gave the division a target of 14 branches to be converted. In fact, an impressive total of 95 branches were completed by the year end.

The 'Al Sage' (The Falcon) project, which moves the back office out of the branches and into regional centres, has got off to an impressive start. Three regional processing centres were set up – in Riyadh, Jeddah and Dammam – and are proving measurably more efficient than the system they replace. This programme continues, bringing considerable improvements in the time it takes us efficiently to service the needs of our customers, while freeing up the branches to concentrate upon the delivery of our products and services direct to their customers.



*rust*

Enduring relationships are built on trust, providing the foundations on which to grow our future.



## Review of Activities



### International Banking

The International Division, based in Jeddah, is responsible for monitoring all the international aspects of the Bank's operations, most of which are channelled through an extensive correspondent banking network of some 570 financial institutions in 89 countries. To ensure the efficient conduct of these activities, NCB has established experienced Representatives in the world's major financial centres, continuously engaged in facilitating the flow of trade finance business, following up project finance enquiries and marketing opportunities.

The Division's principal role is to act as an effective extension of the Bank's successful domestic banking operations, working in close harmony with the other divisions of the Bank by providing experienced support abroad and keeping in constant touch with the Bank's overseas customers, many of whom have been associated with NCB for a number of years.

In Bahrain, branch activities recorded strong growth and NCB Bahrain participated as an underwriter, arranger and lead manager in a US\$300 million loan to Investcorp and as co-Modarab in various Morahaha transactions for Pakistan.

NCB's Beirut branch was relocated to a prime site and its systems upgraded in order to be able to play a greater part in the country's reconstruction and in financing the increasing volume of trade between Saudi Arabia and Lebanon.

### Audit

The Audit Division has seen a substantial expansion of its activities over the past year, under the direction of David Allars, who joined NCB from Citibank at the end of 1993. This year, the division added specialist units covering the Credit



and Treasury functions as well as a Risk Assessment & Fraud Investigation unit. The cadre of professional staff has been enhanced by the recruitment of highly qualified and experienced staff for the new sections and the existing Technology Audit unit.

A Risk Model has been installed that identifies and quantifies the major risk elements of NCB's businesses while maximising the division's own efficiency. Alongside this, audit rating and new reporting procedures have brought consistency of coverage, assessment, treatment and control.

During the year, the Audit Division brought into review a number of areas not previously subject to its formal scrutiny and made significant advances in achieving a heightened awareness of the role and importance of its activities. 1995 will see an increase in automation and a number of pathfinding professional initiatives.

### Support Services

A special mention must be given, when reporting this year of great change for NCB, to the improvements achieved in

## Review of Activities



### Support Services *continued*

Support Services, the division that keeps the Bank's human resources policies, facilities management, administrative and legal affairs on track. Unless these functions improve as fast as, if not faster, than the parts of NCB interfacing the customer, our ability to deliver will not match our promises.

A benchmark survey of the Bank's branch property assets is underway, with the aim of creating a database of building specifications, systems and materials to be used in modernising our facilities management and maintenance.

We have a mission to attract and keep the very best talent to be found in the Kingdom. We want to grow our own future with less reliance upon buying in expatriate skills, while recognising that we will always need to have the best professional input, whatever the source.

Investment in information technology will help us manage our skills base better; graduate traineeships and training programmes will help accelerate the development of young Saudis of talent into management, and we are taking steps to modify structures of pay and conditions to meet tomorrow's staffing needs.

Training ratios were substantially up, with an increase in courses tailored to the needs of each division. Training Saudis for tomorrow's challenges remains a primary commitment of all managers and is the priority task given to all of the non-Saudi professionals who we have brought in to help us with their specialist expertise.

values of the Bank were founded in respect for our fellow citizens, their rights and their needs.

All staff, in their business lives and in the community, are expected to embrace the principles of service and conduct that define NCB as the Bank both for and of all parts of our society.

The National Commercial Bank gave in 1994 both time and financial assistance in aid of many worthy causes, large and small, local and national, from promoting road safety to protecting the national culture. In so doing, the Bank represents its shareholders, its employees and its customers in the finest of Saudi traditions.

### Social Responsibility

NCB continues to play an active part in the communities in which it operates, the societies which it serves. The core

# Auditors' Report



## To the Partners of The National Commercial Bank:

We have audited the balance sheet of The National Commercial Bank (a general partnership) (the "Bank") as of 31 December 1994 and the related statements of income, changes in partners' equity, and cash flows for the year then ended, including the related notes 1 to 23 which form part of these financial statements. These financial statements, which have been derived from computerised accounting records maintained in Arabic in the Kingdom of Saudi Arabia, are the responsibility of the Bank's management and have been prepared in accordance with the provisions of the Banking Control Regulations and submitted to us together with all the information and explanations which we required. Our responsibility is to express an opinion on these financial statements based on our audit.

Our audit was conducted in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance that the financial statements are free of material

misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable degree of assurance to enable us to express our opinion on the financial statements.

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

- present fairly, in all material respects, the financial position of the Bank as of 31 December 1994 and the results of its operations and its cash flows for the year then ended in accordance with Accounting Standards for Commercial Banks issued by the Saudi Arabian Monetary Agency; and
- comply with the provisions of the Banking Control Regulations and the Bank's partnership deed in so far as they affect the preparation and presentation of the financial statements.

**FOR WHINNEY MURRAY & CO**  
Dr. Abdullah Abdulcalman Baeshen,  
Registration No. 66

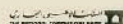
**FOR ISSA EL AYOUTY & CO**  
Accountants and Auditors,  
El Sayed El-Ayouty,  
Registration No. 36

27 February 1995

28 Ramadan 1415 H

# Balance sheet

at 31 December 1994 (in thousands of Saudi Riyals)



Assets	Notes	1994	1993
Cash and balances with SAMA	3	2,958,100	3,474,469
Due from banks	4	10,378,640	15,328,154
Trading securities	5	357,591	11,959,438
Loans and advances, net	6	33,043,538	27,325,814
Investment securities, net	7	17,887,967	3,819,576
Fixed assets, net	8	1,475,736	1,414,583
Other real estate, net	9	1,850,507	1,881,679
Other assets	10	1,515,756	1,511,809
<b>Total assets</b>		<b>69,467,835</b>	<b>66,715,522</b>
<b>Liabilities and partners' equity</b>			
<b>Liabilities</b>			
Customers' deposits	11	52,794,449	51,438,509
Due to banks	12	7,449,931	6,703,790
Other liabilities	13	2,126,407	1,620,921
<b>Total liabilities</b>		<b>62,370,787</b>	<b>59,763,220</b>
<b>Partners' equity</b>			
Capital	14	6,000,000	6,000,000
Statutory reserve	15	1,097,048	952,302
<b>Total partners' equity</b>		<b>7,097,048</b>	<b>6,952,302</b>
<b>Total liabilities and partners' equity</b>		<b>69,467,835</b>	<b>66,715,522</b>
<b>Contra accounts</b>	16	<b>57,094,747</b>	<b>45,746,433</b>

See attached notes 1 to 23 form part of these financial statements.

Mohamed Bin Salim Bin Mahfouz

Chairman General Management Committee



# Statement of Income

for the year ended 31 December 1994 (in thousands of Saudi Riyals)

البنك الأهلي التجاري  
THE NATIONAL COMMERCIAL BANK

Operating income	Notes	1994	1993
Special commissions on loans, advances and deposits		2,434,863	2,609,094
Foreign exchange		77,140	67,472
(Losses) gains on trading securities		(263,772)	374,728
Income from investment securities		868,161	208,875
Gains (losses) on other real estate	17	231,385	(588,411)
Banking services		174,905	164,587
Other		45,635	70,968
<b>Total operating income</b>		<b>3,568,317</b>	<b>3,107,313</b>
<b>Operating expenses</b>			
Cost of funds		1,452,123	1,174,581
Provision for loan losses	6	93,763	193,400
Salaries and other staff-related costs		811,299	845,181
Depreciation of fixed assets and other real estate	8 & 9	86,932	89,138
Other general and administrative expenses		428,579	448,328
<b>Total operating expenses</b>		<b>2,872,696</b>	<b>2,750,628</b>
<b>Net income from operations</b>		<b>695,621</b>	<b>356,685</b>
<b>Other income (expense)</b>			
(Losses) gains on investment securities	18	(209,233)	32,274
Gains (losses) on disposal of fixed assets		5,080	(133)
Income from trading securities		49,472	120,820
Other income		79,197	34,115
Donations and charitable contributions		(31,150)	(40,578)
Zakat	21	(10,000)	-
		(116,634)	146,498
<b>Net income</b>		<b>578,987</b>	<b>503,183</b>

The attached notes 1 to 23 form part of these financial statements.

# Statement of Cash Flows

for the year ended 31 December 1994 (in thousands of Saudi Riyals)



	1994	1993
<b>Cash flows from operating activities</b>		
Net income	578,987	593,183
Adjustment of net income to net cash flow from operating activities:		
Provision for loan losses	93,763	193,400
Loss on valuation of investments securities	226,779	170,000
Loss on valuation of other real estate	-	410,632
Depreciation of fixed assets and other real estate	86,932	89,138
(Gain) loss on sale of fixed assets	(5,080)	133
	981,381	1,366,486
<b>Net (increase) decrease in operating assets:</b>		
Due from banks	4,949,514	462,956
Trading securities	1,552,884	(300,853)
Loans and advances	(5,811,487)	(1,749,710)
Other real estate	23,834	(73,361)
Other assets	(3,947)	(424,426)
<b>Net increase (decrease) in operating liabilities:</b>		
Customers' deposits	1,355,940	(465,795)
Due to banks	746,141	2,841,986
Other liabilities	71,245	259,999
<b>Net cash flow generated from operating activities</b>	<b>3,865,505</b>	<b>1,917,282</b>
<b>Cash flows from investing activities:</b>		
Net increase in investment securities	(4,246,207)	(1,425,647)
Purchase of fixed assets	(156,644)	(61,347)
Proceeds from sale of fixed assets	20,977	931
<b>Net cash flow absorbed in investing activities</b>	<b>(4,381,874)</b>	<b>(1,486,063)</b>
<b>Net (decrease) increase in cash and balance with SAMA</b>	<b>(516,369)</b>	<b>431,219</b>
<b>Cash and balances with SAMA at beginning of the year</b>	<b>3,474,469</b>	<b>3,043,250</b>
<b>Cash and balances with SAMA at end of the year</b>	<b>2,958,100</b>	<b>3,474,469</b>
<b>Supplementary information on non cash activities:</b>		
Operating activities: transfer from trading securities to investment securities	10,048,963	-
Financing activities: profit for distribution	434,241	-

The attached notes 1 to 23 form part of these financial statements.

# Notes to the Financial Statements



for the year ended 31 December 1994

## 1. General

The National Commercial Bank (the "Bank") was established as a general partnership by a Royal Decree in Rajah 1369 H (corresponding to May 1950) and was registered in the commercial register under No. 1588 in Dhul Hijja 1376 H (corresponding to July 1957). Due to the death of the partners and sales of shares between their heirs, the partnership deed needs to be amended. The legal formalities relating to the amendment of the partnership deed, in accordance with the Regulations for Companies, have not been completed.

The objectives of the Bank are to provide all types of banking services. The Bank operates through 241 branches (1993: 238 branches) in the Kingdom of Saudi Arabia and two branches overseas.

## 2. Summary of significant accounting policies

### A) REGULATORY

The Bank is subject to the Companies Regulations and the Banking Control Regulation in the Kingdom of Saudi Arabia. The financial statements are prepared in accordance with Accounting Standards for Commercial Banks issued by the Saudi Arabian Monetary Agency (SAMA) and the requirements of the General Disclosure Standard issued by the Ministry of Commerce.

### B) ACCOUNTING CONVENTION

The financial statements are prepared under the historical cost convention.

### C) SECURITIES PORTFOLIOS

The Bank maintains two separate and distinct securities portfolios, namely "investment securities" and "trading securities". The designation is made by the Bank's management between the two portfolios at the time of purchase and no transfers are made between them after such date unless the management has justifications for such transfers.

On 1 January 1994, the Bank's management transferred domestic quoted shares amounting to SR883 million from the trading securities to the investment securities at the prevailing market value at that date. The transfer was made in line with the management intention to hold these shares for the purpose of long-term investment.

The Bank's management also transferred its international bonds and domestic treasury bills amounting to SR5,166 million from the trading securities to the investment securities at the prevailing market value at that date. The transfer was made in line with the management intention to hold these securities to maturity.

### (i) Trading securities

Securities purchased for trading purposes are initially recorded at acquisition cost. Thereafter, they are carried at market value.

The realised and unrealised gains and losses are included in income from operations. Income from these securities is credited to other income.

### (ii) Investment securities

Securities acquired by the Bank for the purpose of investment are recorded at actual cost. Those transferred from the trading securities are stated at market value at the date of transfer.

The value of bonds is adjusted for amortisation of premiums and accretion of discounts.

Amortisation and accretion are computed using the straight-line method over the remaining maturity period.

The amortised premium and discount and the income earned by the Bank on these securities is included under operating income.

In case of a permanent diminution in the value of any of the securities, or if management expects that its value cannot be redeemed in full, a provision is made for the amount of diminution. Such provision together with the gains and losses arising on disposal of investment securities, is included in other income.

### D) PROVISION FOR LOAN LOSSES

Provision for loan losses is made against loans and advances determined following a review of the portfolio that takes into account the recoverability of outstanding loans and advances and the general economic condition. The provision amount is charged to operating expenses.

The provision for loan losses is reduced by the loans written off, the amounts of which are determined after management's review of recoverability and any related collateral. In addition, the provision for loan losses is reduced on reclassification of non-performing loans to performing loans. The amounts of write back are credited to operating income.

Provision for loan losses is deducted from loans and advances in the balance sheet.

## Notes to the Financial Statements *continued*

for the year ended 31 December 1994



### E) FIXED ASSETS

Fixed assets are stated at cost. Freehold land is not depreciated. The cost of other fixed assets is depreciated using the straight-line method over their expected useful lives, based on the following percentage rates:

Buildings	2.5%
Furniture, fixtures and equipment	10% to 25%

### F) OTHER REAL ESTATE

The Bank acquires certain real estate against settlement of overdue loans and advances. Such real estate is recorded at the lower of net realisable value of due loans and advances and their fair value at the settlement date.

The loss in value arising on periodical valuation of other real estate and gains or losses on disposal are included in income from operations.

The cost of buildings is depreciated using the straight-line method at an annual rate of 2.5%.

Other real estate is stated in the balance sheet net of accumulated depreciation and provision for decline in book value.

### G) CONTRA ACCOUNTS

Contingencies and commitments incurred in the Bank's ordinary course of business are recorded as contra accounts and disclosed as off balance sheet items. These include letters of credit, letters of guarantee, commitments to purchase and sell foreign currencies, interest rate and foreign currencies related swaps and other miscellaneous contingent liabilities.

Commitments for purchase and sale of foreign currencies, interest rate and foreign currencies related swaps are recorded at gross values.

### H) INCOME RECOGNITION

Income and expenses are recognised on an accrual basis. However, income on loans and advances classified as non-performing is recognised on a cash basis until the loan or advance is reclassified as performing whereupon the recognition of income reverts to an accrual basis. Income from Musharaka and Mudaraba transactions is recognised on a cash basis, whereas income from Murabaha is recognised on a straight-line basis over the period of the transaction.

Accumulated special commissions in suspense are deducted from loans and advances in the balance sheet.

### I) FOREIGN CURRENCIES

Transaction in foreign currencies are translated to Saudi Riyals at the exchange rates prevailing on the dates of the transactions. Assets and liabilities denominated in foreign currencies at the balance sheet date are translated to Saudi Riyals at the rates of exchange prevailing at that date.

Forward foreign exchange contracts are recorded in Saudi Riyals at the spot rates prevailing at the deal date. Premiums and discounts relating to the forward foreign exchange contracts are amortised over the period of the contract. Contracts outstanding at the balance sheet date are valued at the spot exchange rates prevailing at that date.

Realised and unrealised gains and losses on exchange are credited or charged to operating income.

### J) END OF SERVICE BENEFITS

Benefits payable to the employees of the Bank are provided for in accordance with the guidelines set by the Saudi Arabian Labor Law and the balance is included in other liabilities.

### K) ZAKAT

Zakat is computed based on the balance sheet at the year end and charged to the statement of income as a provision against non-operating income.



## Notes to the Financial Statements *continued*

for the year ended 31 December 1994



### 3. Cash and Balances with SAMA

	1994	1993
a) Cash in hand	829,511	1,086,222
b) Balances with SAMA		
Statutory deposit	1,933,386	2,049,208
Current accounts	195,203	339,039
	2,958,100	3,474,469

In accordance with Article (7) of the Banking Control Regulations, the Bank is required to maintain a statutory deposit with SAMA at stipulated percentages of its call, time, savings and other deposits calculated at the end of each Gregorian month.

### 4. Due from banks

	1994	1993
a) Domestic		
Call accounts	73,421	53,717
Time deposits	1,058,158	2,242,530
	1,131,579	2,296,247
b) Foreign branches of domestic banks		
Time deposits	125,000	468,750
c) International		
Call accounts	1,605,396	1,142,362
Time deposits	7,516,665	11,420,825
	9,122,061	12,563,187
	10,378,640	15,328,154

### 5. Trading securities

	1994	1993
a) Domestic		
Shares	-	882,966
Fixed rate bonds	-	50,500
Fixed rate treasury bills	-	3,662,246
Units in investment funds managed by the Bank	94,450	300,000
	94,450	4,895,712
b) International		
Externally-managed portfolios (shares, bonds and others)	263,141	7,063,726
	357,591	11,959,438

Notes to the Financial Statements *continued*


for the year ended 31 December 1994

## 6. Loans and advances, net

	1994	1993
<b>a) Domestic</b>		
<i>Private sector</i>		
Real estate	3,704,036	3,591,349
Agriculture	140,690	218,522
Manufacturing	1,978,667	1,864,780
Trading	9,391,257	7,494,205
Services	1,549,059	1,558,935
Other	3,504,284	3,177,196
<i>Government, government agencies, quasi government and other public institutions</i>		
Banks	14,740,099	9,525,548
	82,674	106,026
	35,090,766	29,536,561
<b>b) International</b>		
<i>Private sector</i>		
Other	1,490,286	1,511,116
<i>Government, government agencies, quasi government and other public institutions</i>		
Banks	638,995	679,297
	359,915	395,502
	2,489,196	2,585,915
	37,579,962	32,122,476
Provision for loan losses and accumulated commissions in suspense	(4,536,424)	(4,796,662)
	33,043,538	27,325,814

Total non-performing loans and advances on which no income was recognised amounted to SR6,915 million (1993: SR7,751 million).

Loans extended to the private sector include accounts receivable from certain partners and members of the General Management Committee amounting to SR900 million (1993: SR1,117 million). However, these parties have deposits with the Bank that exceed the amounts of their loans.

The movement on the provision for loan losses and accumulated special commissions in suspense is as follows:

	1994	1993
Balance at beginning of the year	4,796,662	5,403,253
Bad debts written off in settlement for:		
– real estate	(94,151)	(133,892)
– other	(486,154)	(853,905)
Provided during the year:		
– provisions for loan losses	150,000	293,400
– special commissions suspended	226,304	197,806
Recoveries	(56,237)	(100,000)
Balance at end of the year	4,536,424	4,796,662
The net amount charged to operating expenses is comprised as follows:		
Provided during the year	150,000	293,400
Recoveries	(56,237)	(100,000)
	93,763	193,400

# Notes to the Financial Statements *continued*

for the year ended 31 December 1994

بنك الأهلي التجاري  
THE NATIONAL COMMERCIAL BANK

## 7. Investment securities, net

	1994	1993
<b>a) Domestic</b>		
Shares	934,454	91,927
Fixed rate bonds	5,064,577	2,995,909
Fixed rate treasury bills	2,943,230	—
	8,942,261	3,087,836
<b>b) International</b>		
Shares — different currencies	71,747	88,268
Fixed rate treasury bonds (US Dollar)	3,432,713	—
Fixed rate government bonds (different currencies)	1,179,759	441,343
Fixed rate commercial bonds (different currencies)	4,261,487	202,129
	8,945,706	731,740
	<b>17,887,967</b>	<b>3,819,576</b>

The market fair value of investment securities as at the balance sheet date amounted to \$8,170,017 million (1993: \$93,653 million).

## 8. Fixed assets, net

	Land	Buildings	Furniture, cars and fixtures	Total
<b>Cost</b>				
Balance at beginning of the year	261,797	1,358,682	416,594	2,037,073
Additions	6,955	19,030	130,639	156,644
Disposals	—	—	(63,948)	(63,948)
	268,752	1,377,712	483,305	2,129,769
<b>Accumulated depreciation</b>				
Balance at beginning of the year	—	326,572	295,918	622,490
Additions	—	34,780	44,814	79,594
Disposals	—	—	(48,051)	(48,051)
	—	361,352	292,681	654,033
<b>Net book values</b>				
1994	268,752	1,016,360	190,624	1,475,736
1993	261,797	1,032,110	120,676	1,414,583

## 9. Other real estate, net

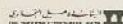
	1994	1993
Balance at beginning of the year, net	1,881,679	2,225,956
Additions	68,591	133,891
Disposals	(92,425)	(60,530)
Loss on valuation during the year	—	(410,632)
Depreciation on buildings during the year	(7,338)	(7,006)
<b>Balance at end of the year, net</b>	<b>1,850,507</b>	<b>1,881,679</b>

## 10. Other assets

	1994	1993
Customers' liabilities on acceptances	493,025	712,589
Accrued commissions receivable	484,100	148,677
Other	538,631	650,543
	<b>1,515,756</b>	<b>1,511,809</b>

Notes to the Financial Statements *continued*

for the year ended 31 December 1994



	1994	1993
<b>11. Customers' deposits</b>		
<b>a) Domestic</b>		
Call accounts	22,024,626	22,966,952
Notice accounts	1,922,926	600,256
Saving	823,220	926,425
Time deposits	25,224,872	24,105,818
Other	2,528,105	2,584,333
	52,523,758	51,183,814
<b>b) International – foreign currencies</b>		
Call accounts	46,699	23,881
Savings	23,624	52,662
Time deposits	15,433	11,337
Other	1,919	1,972
	87,675	89,852
<b>c) Accrued commissions</b>	183,016	164,843
	52,794,449	51,438,599

Customers' deposits include an amount of SR457 million (1993: SR50 million) against sales of fixed rate bonds under repurchase agreements.

	1994	1993
<b>12. Due to banks</b>		
<b>a) Domestic</b>		
Call accounts	47,324	14,842
Notice accounts	597,000	2,770,000
Time deposits	3,522,087	2,363,557
	4,166,411	5,148,379
<b>b) Foreign branches of domestic banks</b>		
Time deposits	155,000	25,000
<b>c) International</b>		
Call accounts	1,772,620	620,742
Time deposits	1,355,900	909,669
	3,128,520	1,530,411
	7,449,931	6,703,790

	1994	1993
<b>13. Other liabilities</b>		
Acceptances outstanding	493,025	712,589
Profit for distribution	434,241	–
Other (note 21)	1,199,141	908,332
	2,126,407	1,620,921

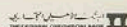
**14. Capital**

During 1992 the Bank's capital was increased to SR6,000 million. The legal formalities relating to the amendment of the partnership deed in accordance with the provisions of the Regulations for Companies in respect of the increase in capital have not been completed.



Notes to the Financial Statements *continued*

for the year ended 31 December 1994

**15. Statutory reserve**

In accordance with the Banking Control Regulations, 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. This reserve is not available for distribution.

**16. Contra accounts**

	1994	1993
Letters of credit	5,643,028	3,635,599
Letters of guarantee	6,942,615	7,480,340
Forward contracts to purchase foreign currencies	17,813,794	19,438,104
Forward contracts to sell foreign currencies	25,680,259	14,720,478
Swap contracts	360,250	348,375
Other	654,801	123,537
	<b>57,094,747</b>	<b>45,746,433</b>

The Bank's management does not anticipate any material loss as a result of these contingencies and commitments.

**17. Gains (losses) on other real estate**

	1994	1993
Gain on sale of other real estate	217,955	8,050
Loss on valuation of other real estate	-	(410,652)
Rental income	13,430	14,191
	<b>231,385</b>	<b>(388,411)</b>

**18. (Losses) gains on investment securities**

	1994	1993
Gain on sale of investments	17,546	202,274
Loss on valuation of investments	(226,779)	(170,090)
	<b>(209,233)</b>	<b>32,274</b>

**19. Investment services**

The Bank provides certain investment management services to its customers. These services include the management of a variety of investment funds in association with professional investment managers. The assets of these funds do not form part of the Bank's assets and, accordingly, are not included in the financial statements of the Bank.

The other defendants involved in the settlement have agreed to bear any damages arising from the settlement. Accordingly, no provision for any contingent liabilities has been made.

**21. Zakat**

The Bank's management made a provision of SR10 million for Zakat charges (1993: nil). The balance of accrued Zakat is included under other liabilities (note 13).

**20. Contingent liabilities**

Certain lawsuits were filed outside the Kingdom of Saudi Arabia against the Bank and other parties for substantial amounts. These lawsuits are on the point of settlement. The terms of settlement have been agreed with the plaintiff. Foreign court approval of the terms of the settlement is required and the matter will be heard before the court in the near future. Once the court approval has been obtained, the settlement will result in all the said lawsuits being terminated. Accordingly, adequate provision has been made against the expected loss of the Bank's assets subject to the settlement.

**22. Statement of cash flows**

The Bank has changed the presentation of the financial statements for 1994 to include a statement of cash flows instead of a statement of source and application of funds prepared by the Bank in 1993.

**23. Comparative figures**

Certain of the comparative figures for 1993 have been reclassified to conform with the classification of the financial statements in 1994.

## Saudi Arabia's Capital Market

*Saudi Arabia had the largest stock market in the region in terms of capitalisation at SR141 billion (\$38 billion) by the end of 1994.*

This represents around 50% of the value of all shares traded on the Arab exchanges. Even though there is no official exchange in the Kingdom, shares are heavily traded via a very sophisticated screen-based system, ESIS (Electronic Securities Information System), developed by the Saudi Arabian Monetary Agency (SAMA). The top five Saudi shareholding companies ranked by market value are: Saudi Basic Industries Corporation (SABIC), the Saudi American Bank, Al Rajhi Banking Investment Corporation, Riyadh Bank, and the electricity company SCECO Central.

The paid up capital of the listed companies amounted to SR69.4 billion (\$18.5 billion) by the end of 1994, compared to SR65 billion (\$17.3 billion) in 1993, an increase of 6.8%. As a percentage of GDP, market capitalisation reached 31% last year. Electricity companies account for the biggest share, with 44.1% of total market capitalisation; followed by industry firms, including cement companies (33%), services (12.3%), banks (7.9%), and agricultural companies (2.7%).

There are 78 companies listed on the exchange, but only 68 are publicly tradeable. The total number of shares outstanding by the end of 1994 was around 755 million, compared with 698 million the year before. This means close to 57 million shares were issued last year as three new companies (The Saudi Industrial Export Company, Al Riyadh Development Company and Tabuk Cement Company) have entered the market and five others boosted their capital by issuing new shares.

Only shares of Saudi companies may be traded in the Kingdom and these are normally acquired by Saudi citizens. In special circumstances (e.g. 1984 Saudi Basic Industries Corporation (SABIC) issue and more recently the Tabuk Cement Company among 13 other Saudi companies) specified portions of the shares floated were made available to other Gulf Co-operation Council Citizens. Following the last GCC summit held in Bahrain in December 1994, a decision was made to allow GCC nationals to own up to 25% of all Saudi shares.

Close to 296 million shares, or 39.2% of the total shares issued are held by the Saudi government, while foreign entities hold 29 million shares or 3.8% of the total. Most of the shares held by the government and by foreigners are not traded in the market. This means only 438 million shares, or 57% of the total shares outstanding, are actually available for trading. Even among those shares available for trading, we find a concentration of large blocks in the hands of investors who are holding them for the annual earnings they generate. Furthermore several large investors are less likely to sell their holdings because they do not wish to lose board representation or voting influence.

The depth of the Saudi stock market, i.e. the value of shares traded as a percentage of total market value of shares outstanding, has generally been small. In 1994, total number of shares traded reached 152 million, or 35% of the number of shares available for trading and constituted around 20% of total shares issued.

Table 1 Saudi Arabia, official stock market indices and % change by sector and total

End of Period	Banking		Industry		Services		Agriculture		Electricity		Cement		Total	
	Index	% Change	Index	% Change	Index	% Change	Index	% Change	Index	% Change	Index	% Change	Index	% Change
1991	436.92	129.55	291.41	104.05	118.43	105.63	138.13	36.63	58.63	3.71	133.67	47.46	187.77	91.64
1992	498.72	14.14	259.01	11.12	137.75	16.31	154.97	12.19	60.36	2.92	210.02	50.37	188.87	0.59
1993	497.30	(1.49)	222.11	(14.25)	124.32	(9.75)	110.19	(28.92)	62.62	3.74	193.34	(7.94)	179.33	(5.05)
1994														
Q1*	388.50	(20.92)	159.53	(10.17)	106.92	(14.00)	88.05	(20.08)	55.76	(10.95)	183.36	(5.16)	152.48	(16.97)
Q2*	361.70	(26.38)	130.93	(18.54)	91.21	(26.63)	81.40	(26.53)	55.00	(12.17)	135.11	(30.12)	138.01	(23.04)
Q3*	370.75	(24.54)	159.08	(10.37)	97.17	(21.84)	92.03	(16.48)	51.63	(12.55)	159.96	(12.25)	144.74	(19.29)
Q4*	305.83	(37.75)	190.15	(14.39)	85.08	(31.56)	76.96	(30.16)	47.69	(23.84)	141.92	(26.60)	127.81	(28.73)

\*Percentage change from end 1993

Source: Ministry of Finance, Official Share Market Indices.



The official stock market index was down 28.7% in 1994 following a drop of 5.05% in 1993, a rise of less than 1% in 1992 and a 91% increase in 1991 (table 1). Most world markets moved downward or sideways last year. The world benchmark, the MSCI world index was up by a meagre 3%. The US market was up by 2.1% and only Japan's stock market recorded an increase in dollar terms of 19%. After falling by 23% in the first two quarters to a low of 138.01, the official Saudi stock market index rose by 4.9% on its mid year level to reach 144.74 by the end of the third quarter. The fourth quarter, however, witnessed a return of bearish sentiment leading to a further decline. By the end of the year the index declined by 11.7% compared to its level at the end of September.

Indices of all sectors of the Saudi market registered declines last year. Shares of industrial sector companies recorded the smallest percentage decline in 1994, dropping 14.3% from 264.80 at the end of 1993 to 222.11 at the end of 1994. Bank shares registered the largest decline, with the index there dropping from 491.30 at the end of 1993 to 305.83 by the end of 1994, a decrease of 37.8%. The decline in share values of banks coincided with the return of banks' profits to more sustainable levels in 1994 compared to the exceptional levels recorded in 1993. The index of electricity companies lost 23.8% last year dropping from 62.62 at the end of 1993 to 47.6% at the end of 1994. The indices of cement, agriculture and services sector companies declined by 26%, 30.2% and 31.6% respectively.

The slowdown in overall economic activities, the tight liquidity conditions in the country and the rising SR interest rates in 1994 all contributed in varying degrees to the slump in stock prices. The policy of the banks to cut down on their financing of speculative share

buying added to the stampede. With share prices on the decline and in an effort to salvage the value of the collateral they hold in the form of stocks, banks sold shares whenever there was a buyer at a reasonable price. The decline in share prices in the last two years has rendered many stocks undervalued at current levels. Furthermore, the share prices of many companies have now dropped below their book value.

While share prices trended lower last year, the number and total value of shares traded rose reaching their highest level since 1985. The surge in trading activity and the sizeable increase in the value and volume of shares traded point to a market that has gained ample depth and maturity in the last few years. The total value of shares traded rose by 43% in 1994 and the quantity by 152% (table 2).

In 1985, 300,000 shares per month were traded. The figure ballooned to 12.5 million shares per month in 1994, with an average daily value of SR100 million. The main reason behind this large growth is the ability of the ESIS (electronic settlement system) to settle all buy/sell transactions on a next day of trade basis.

The total value of shares traded in 1994 was SR24.9 billion, up from SR17.4 billion in 1993, an increase of 43%. This followed increases of 27% and 61% in 1993 and 1992 respectively. The most actively traded shares last year were those of services and industrial sector companies, these accounted for 35.9% and 32.4% of total value of shares traded respectively. Banks, Cement, Agriculture and Electricity followed with 24.9%, 3.9%, 2.3% and 0.5% respectively. A total of 152 million shares were traded during the year, up from 60.3 million in 1993, out of which 48.2% were of service sector companies and 31.4% were of industrial sector companies. The year witnessed the execution of 357,180 transactions, up 12% on the year before, out of which 70% were for shares of companies in the services and the industrial sectors.

The head offices of the twelve Saudi banks are now connected to the ESIS network host computer located at SAMAs headquarters in Riyadh. The banks have extended the communications capability further, connecting their designated branches throughout the Kingdom. The banks' head offices also have direct simultaneous communication links with

**Table 2** Value and volume of shares trades in the Saudi Stock market

	Value of shares traded (SR million)	% change on the year before	Quantity of shares traded (millions)	% change on the year before
1985	759.9	—	3.9	—
1986	830.7	9%	5.3	34%
1987	1,685.5	103%	12.0	128%
1988	2,036.8	21%	14.6	22%
1989	3,363.7	65%	15.3	4%
1990	4,403.2	31%	16.9	11%
1991	8,527.3	94%	30.8	82%
1992	13,695.8	61%	35.2	14%
1993	17,360.0	27%	60.3	71%
1994	24,871.1	43%	152.1	152%



## Saudi Arabia's Capital Market *continued*

the Saudi Shares Registration Company (SSRC). The SSRC is a centralised agency responsible for holding records of stock ownership and transfers after the successful execution of buy or sell orders.

ESIS processes share transactions from entry of the buy or sell order to final share registration and printing of share certificates (a kind of ownership note used for trading purposes).

Within the integrated electronic system, ESIS provides electronic handling, including maintenance of accurate client information; release of bids and offers into the share market and execution of share transactions; delivery of sold shares and money payments through SAMA clearings; and price dissemination to the central trading units of all participating banks and their branches.

A recently issued royal decree amending the companies' law in the Kingdom has made it possible for corporations to issue preferred stocks, after the approval of the commerce minister. Such non-voting preferred stocks give the shareholder the right to receive a certain

percentage of the company's net profit of not less than 5% of the nominal value of the shares before distributing the profits of the corporation to other shareholders. It also gives the shareholder of preferred stocks priority in the recovery of share capital upon liquidation. No company issued preferred shares in 1994.

Yields on 3 months Saudi Riyal Treasury Bills and Saudi Government Development Bonds followed an upward trend in 1994 in line with those of the US.

The rising trend started in January and continued throughout the year. Yields on the 3-month Saudi Riyal Treasury Bills rose from a monthly average of 3.95% in January to 4.84% by mid-year and ended the year at a monthly average of 7.10%, a yearly rise of 80%. Yields on the 3-year Saudi Government Development Bonds (SGDB) rose from a monthly average of 4.90% in January to 7.80% in December, an annual increase of 59%. The yield differential between 3-month Saudi Riyal Treasury Bills and the 3-year SGDBs rose from 95 basis points in January to 287

basis points in May, before declining to 70 basis points in December. Yields on longer maturities also assumed an up trend during the year with those on 5-year SGDBs rising from a monthly average of 5.7% in January to 8.16% in December, the year on year increase being 2.46% (table 3).

There is no private bond market to speak of in Saudi Arabia. A domestic Saudi Riyal bond market existed till 1978, when SAMA imposed a moratorium on Saudi Riyal issues.

In the mid 1980s, few dollar denominated floating rate notes were arranged for local borrowers in the Kingdom by Saudi banks and the Offshore Banking Units in Bahrain. The moratorium imposed by SAMA on Riyal issues has effectively been applied to dollar denominated issues as well.

The lack of a corporate bond market is probably the most serious deficiency in Saudi capital markets at the moment. The loans to deposits ratios of the commercial banks have been rising to the extent that some banks now have to take a much more selective approach to term lending than they did in recent years. Besides, several industrial companies have medium-term financing requirements and would not like to take the interest rate exposure associated with bank loans. Some of them are exploring the possibility of issuing dollar denominated bonds out of Bahrain.

Another novelty last year was the issuance in August 1994 of \$280 million in floating rate notes in the name of the Government of the Kingdom of Saudi Arabia. This was welcomed as an indication that the Kingdom's financial authorities are willing to start considering new options. The notes were well received and a further issue of \$270 million came to the market in December last year.

**Table 3** Yields on Saudi Treasury Bills and Development Bonds (%)

Actual	3-months Treasury Bills	3-years Development Bonds	5-years Development Bonds
Jan. 1994	3.95	4.90	5.70
Feb. 1994	3.60	3.17	5.84
Mar. 1994	4.00	3.76	6.48
Apr. 1994	4.35	6.19	6.55
May 1994	4.57	6.44	7.14
Jun. 1994	4.84	6.67	7.23
Jul. 1994	5.16	6.92	7.54
Aug. 1994	5.10	6.86	7.43
Sep. 1994	5.21	7.03	7.62
Oct. 1994	6.39	7.21	7.75
Nov. 1994	7.16	7.39	7.98
Dec. 1994	7.10	7.80	8.16

Source: NCB Treasury



## The Management Committee



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Ahmed Banaja, Abdulhadi Ali Shayif, Sheikh Mohamed Bin Salim Bin Mahfouz, Abdullah Salim Bahamdan, Mohamed Salim Al-Batati and Omar Abdul Qader Bajamal

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