

## Pillar 3 Disclosures

### Qualitative and Quantitative

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## 1.0 Scope of Application

### 1.1 Introduction

The Pillar 3 disclosures and the related regulations apply to the National Commercial Bank (the Bank) at a consolidated level. Please refer to note 1.1 of the *Audited Financial Statements for the year ended 31 December 2015* for details on the incorporation and activities of the Bank.

### 1.2 Basis of Consolidation

The Bank does not have any subsidiaries other than banking, securities and financial entities, accordingly, there is no difference in the basis of consolidation used in the *Audited Financial Statements for the year ended 31 December 2015* and that used for regulatory purposes.

SCOPE OF APPLICATION (SAMA reference table 1)	
Capital Deficiencies (Table 1, (e))	
Particulars	Amount (SR '000)
The aggregate amount of capital deficiencies in subsidiaries not included in the consolidation i.e. that are deducted:	<b>Nil</b>

### ***(i) Entities (within the group) fully consolidated for regulatory purposes***

Following is a list of the consolidated subsidiaries of the Bank.

*(1) NCB Capital Company (NCBC)*

*(1.1) Eastgate Capital Holdings Inc. (Eastgate)*

*(1.2) NCBC Investment Management Umbrella Company Plc*

*(2) Türkiye Finans Katılım Bankası A.Ş.(TFK) and its special purpose entities*

*(3) Real Estate Development Company (Redco)*

*(4) Alahli Insurance Services Marketing Company*

*(5) Saudi NCB Markets Limited*

Please refer to note 1.2 of the *Audited Financial Statements for the year ended 31 December 2015* for details on the incorporation and activities of the subsidiaries of the Bank.

### ***(ii) Significant investments in banking, financial and insurance entities that are outside the scope of regulatory consolidation***

Capital investment in banking, financial and insurance entities where NCB owns more than 10% of its issued common share capital are subject to certain thresholds of both NCB and the entities' capital set by Basel III. Thus the aggregate of all NCB's investments does not trigger any deduction adjustment; and therefore they are risk weighted at 250%. Following is a list of significant investments in banking, financial and insurance entities that are outside the scope of regulatory consolidation:

(1) Al-Ahali Takaful Company

The Bank has a 30% ownership in Al-Ahali Takaful Company. Al-Ahali Takaful Company (the Company) is a Saudi Joint Stock Company registered in the Kingdom of Saudi Arabia under Commercial Registration No. 4030171573 dated 21 Rajab 1428H, corresponding to 4 August 2007. The object of the Company is to transact cooperative insurance operations and related activities in the Kingdom of Saudi Arabia. The Company was listed on the Saudi stock market on 18 August 2007. The Company commenced its commercial operations on 4 February 2008.

(2) Arabian Financial Services Company

The Bank has 13% ownership in Arabian Financial Services (AFS) company. It is the region's leading provider of electronic-payments and consumer-finance outsourcing services.

(3) Saudi Traveler Cheques Company

The Bank has 25% ownership in the Saudi Travelers Cheques Company (STCC). Saudi Riyal Travelers Cheques are issued by the company which was jointly established by the banks of Saudi Arabia.

(4) The Saudi Credit Bureau

The Bank has 11% ownership in the Saudi Credit Bureau (SIMAH). It is the first and sole licensed national credit bureau offering consumer and commercial credit information services to respective members in the Kingdom of Saudi Arabia.

**(iii) Entities (within the group) neither consolidated nor deducted**

All other equity investments are risk weighted at 100%.

**1.3 Transferability of Capital**

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

## 2.0 Capital Structure

The capital of the bank consists of the following:

### (1) Eligible paid-up share capital

The authorized, issued and fully paid share capital of the Bank excluding Treasury shares<sup>1</sup> consists of 1,995 million shares of SR 10 each. All these shares carry equal voting rights and are not redeemable. These shares rank junior to all other claims on the Bank.

### (2) Eligible reserves

Eligible reserves comprise statutory reserves, other reserves, retained earnings, minority interest and eligible portfolio (collective) allowances. Eligible reserves are mainly created by accumulated appropriations of profit and are maintained for future growth.

Goodwill, intangible assets and other prescribed deductions are deducted from eligible capital.

### (3) Debt Securities Issued

#### Tier 1

The National Commercial Bank through a Shari'a compliant arrangement issued Tier 1 Sukuks , aggregating to SR 5.7 billion. The arrangement was approved by the regulatory authorities and the shareholders of the Bank. These Sukuks are perpetual securities in respect of which there is no fixed redemption. However, the Bank shall have the exclusive right to redeem or call the Sukuks in a specific period of time, subject to the terms and conditions stipulated in the Sukuk Agreement.

#### Tier 2

The National Commercial Bank issued Non- convertible unlisted Sukuk in February 2014. The tenure is 10 years, callable on the 5th anniversary of the issue date and carrying profit payable semi-annually.

<sup>1</sup> The bank acquired its own equity shares from a customer as a result of partial set-off of debt. Treasury shares are deducted from equity and accounted for at cost, being the value of set-off.

Following tables give the balance sheet and capital structure of the Bank.

TABLE 2: CAPITAL STRUCTURE			
Balance sheet - Step 1 (Table 2(b))	All figures are in SAR'000		
	Balance sheet in Published financial statements ( C )	Adjustment of banking associates / other entities (*) ( D )	Under regulatory scope of consolidation ( E )
<b>Assets</b>			
Cash and balances at central banks	27,559,154		27,559,154
Due from banks and other financial institutions	20,102,519		20,102,519
Investments, net	132,997,549		132,997,549
Financing and advances, net	251,531,030		251,531,030
Investment in associates, net	423,740		423,740
Other real estate, net	876,264		876,264
Goodwill	393,513		393,513
Other intangible assets	76,769		76,769
Property and equipment, net	3,716,091		3,716,091
Other assets	11,663,800		11,663,800
<b>Total assets</b>	<b>449,340,429</b>		<b>449,340,429</b>
<b>Liabilities</b>			
Due to Banks and other financial institutions	47,719,572		47,719,572
Customer deposits	323,282,273		323,282,273
Debt securities in issue	9,862,828		9,862,828
Other liabilities	12,930,199		12,930,199
<b>Subtotal</b>	<b>393,794,872</b>		<b>393,794,872</b>
Paid up share capital	20,000,000		20,000,000
Treasury Shares	(190,510)		(190,510)
Statutory reserves	19,383,697		19,383,697
Other reserves	726,547		726,547
Retained earnings	9,833,777		9,833,777
Minority Interest	1,383,071		1,383,071
Proposed dividends	1,495,975		1,495,975
Foreign currency translation reserve	(2,787,000)		(2,787,000)
Tier 1 Sukuk	5,700,000		5,700,000
<b>Total liabilities and equity</b>	<b>449,340,429</b>		<b>449,340,429</b>

TABLE 2: CAPITAL STRUCTURE				
Balance sheet - Step 2 (Table 2(c))		All figures are in SAR'000		
	Balance sheet in Published financial statements  ( C )	Adjustment of banking associates / other entities  ( D )	Under regulatory scope of consolidation  ( E )	Reference*
<b>Assets</b>				
Cash and balances at central banks	27,559,154		27,559,154	
Due from banks and other financial institutions	20,102,519		20,102,519	
Investments, net	132,997,549		132,997,549	
Financing and advances, net	251,531,030		251,531,030	
of which Collective provisions	(2,707,197)		(2,707,197)	A
Investment in associates, net	423,740		423,740	
Other real estate, net	876,264		876,264	
Goodwill	393,513		393,513	B
Other intangible assets	76,769		76,769	C
Property and equipment, net	3,716,091		3,716,091	
Other assets	11,663,800		11,663,800	
<b>Total assets</b>	<b>449,340,429</b>		<b>449,340,429</b>	
<b>Liabilities</b>				
Due to Banks and other financial institutions	47,719,572		47,719,572	
Customer deposits	323,282,273		323,282,273	
Debt securities in issue	9,862,828		9,862,828	
Other liabilities	12,930,199		12,930,199	
<b>Subtotal</b>	<b>393,794,872</b>		<b>393,794,872</b>	
Paid up share capital	20,000,000		20,000,000	
Treasury Shares	(190,510)		(190,510)	D
Statutory reserves	19,383,697		19,383,697	
Other reserves	726,547		726,547	
Retained earnings	9,833,777		9,833,777	
Minority Interest	1,383,071		1,383,071	
of which Common share capital issued by subsidiaries and held by third parties (amount allowed in group CET1)	1,235,717		1,235,717	E
Proposed dividends	1,495,975		1,495,975	
Foreign currency translation reserve	(2,787,000)		(2,787,000)	
Tier 1 Sukuk	5,700,000		5,700,000	
<b>Total liabilities and equity</b>	<b>449,340,429</b>		<b>449,340,429</b>	

\*Please refer to pages 7 and 8 for the impact of these adjustments on the capital structure





TABLE 2: CAPITAL STRUCTURE
Common template (transition) - Step 3 (Table 2(d)) i
(From January 2013 to 2018 identical to post 2018) With amount subject to Pre- Basel III Treatment
All figures are in SAR'000

Source based on reference numbers / letters of the balance sheet under the regulatory scope of consolidation from step 2 (see page 6)

	Components of regulatory capital reported by the bank	Amounts subject to Pre - Basel III treatment	
<b>Common Equity Tier 1 capital: Instruments and reserves</b>			
Directly issued qualifying common share capital (and equivalent for non-joint stock companies) plus related stock surplus	20,000,000		
Retained earnings	11,329,752		
Accumulated other comprehensive income (and other reserves)	17,323,244		
Common share capital issued by subsidiaries and held by third parties (amount allowed in group Common Equity Tier 1 - CET1)	1,235,717		E
<b>Common Equity Tier 1 capital before regulatory adjustments</b>	<b>49,888,713</b>		
<b>Common Equity Tier 1 capital: Regulatory adjustments</b>			
Goodwill (net of related tax liability)	393,513		B
Other intangibles other than mortgage-servicing rights (net of related tax liability)	76,769		C
Cash-flow hedge reserve	(173,145)		
Investments in own shares (if not already netted off paid-in capital on reported balance sheet)	190,510		D
<b>Total regulatory adjustments to Common equity Tier 1</b>	<b>487,647</b>		
<b>Common Equity Tier 1 capital (CET1)</b>	<b>49,401,066</b>		
Directly issued qualifying Additional Tier 1 instruments plus related stock surplus	5,700,000		
of which: classified as equity under applicable accounting standards	5,700,000		
<b>Additional Tier 1 capital (AT1)</b>	<b>5,700,000</b>		
<b>Tier 1 capital (T1 = CET1 + Additional Tier 1 Capital AT1)</b>	<b>55,101,066</b>		

**TABLE 2: CAPITAL STRUCTURE**  
 Common template (transition) - Step 3 (Table 2(d)) ii  
 (From January 2013 to 2018 identical to post 2018) With amount subject to Pre- Basel III Treatment  
*All figures are in SAR'000*

	Components of regulatory capital reported by the bank	Amounts subject to Pre - Basel III treatment	Source based on reference numbers / letters of the balance sheet under the regulatory scope of consolidation from step 2(see page 6)
<b>Tier 2 capital: instruments and provisions</b>			
Directly issued qualifying Tier 2 instruments plus related stock surplus	5,000,000		
Provisions	2,707,197		
<b>Tier 2 capital before regulatory adjustments</b>	<b>7,707,197</b>		
<b>Tier 2 capital: regulatory adjustments</b>			
<b>Tier 2 capital (T2)</b>	<b>7,707,197</b>		
<b>Total capital (TC = T1 + T2)</b>	<b>62,808,263</b>		
<b>Total risk weighted assets</b>	<b>365,154,166</b>		
<b>Capital ratios</b>			
Common Equity Tier 1 (as a percentage of risk weighted assets)	13.5%		
Tier 1 (as a percentage of risk weighted assets)	15.1%		
<b>Total capital (as a percentage of risk weighted assets)</b>	<b>17.2%</b>		
Provisions eligible for inclusion in Tier 2 in respect of exposures subject to standardized approach (prior to application of cap)	2,707,197		
Cap on inclusion of provisions in Tier 2 under standardized approach	4,103,522		

A

TABLE 2: CAPITAL STRUCTURE		
Main features template of regulatory capital instruments - (Table 2(e))		
1	Issuer	National Commercial Bank (NCOMBK)
2	Unique identifier (eg CUSPIN, ISIN or Bloomberg identifier for private placement)	ISIN No. SA13HFK0IEJ4
3	Governing law(s) of the instrument	The instrument is governed by the laws of the Kingdom of Saudi Arabia
Regulatory treatment		
4	Transitional Basel III rules	Tier 2
5	Post-transitional Basel III rules	Eligible
6	Eligible at solo/group/group & solo	Group and Solo
7	Instrument type	Subordinated Sukuk
8	Amount recognized in regulatory capital (Currency in mil, as of most recent reporting date)	SAR 5,000mil
9	Par value of instrument	SAR 5,000mil
10	Accounting classification	Liability - amortized cost
11	Original date of issuance	25th February 2014
12	Perpetual or dated	Dated
13	Original maturity date	25th February 2024
14	Issuer call subject to prior supervisory approval	Yes
15	Option call date, contingent call dates and redemption amount	Call option only available after 5 years or for a regulatory or tax event, 25th February 2019 as the date for redemption, NCB shall be entitled to redeem in whole, but not in part, by giving not less than thirty (30) days' nor more than sixty (60) days' notice to the Sukukholders
16	Subsequent call dates if applicable	As above
Coupons / dividends		
17	Fixed or Floating dividend/coupon	Floating
18	Coupon rate and any related index	6 months SIBOR + 110bps
19	Existence of a dividend stopper	No
20	Fully discretionary, partially discretionary or mandatory	Mandatory
21	Existence of step up or other incentive to redeem	No
22	Non-cumulative or cumulative	Non-cumulative
23	Convertible or non-convertible	Non - convertible
24	If convertible, conversion trigger (s)	N/A
25	If convertible, fully or partially	N/A
26	If convertible, conversion rate	N/A
27	If convertible, mandatory or optional conversion	N/A
28	If convertible, specify instrument type convertible into	N/A
29	If convertible, specify issuer of instrument it converts into	N/A
30	Write-down feature	Yes
31	If write-down, write-down trigger (s)	Terms of contract of the instrument provide the legal basis for SAMA to trigger write-down (a contractual approach)
32	If write-down, full or partial	Written down fully or partial
33	If write-down, permanent or temporary	Permanent
34	If temporary write-down, description of the write-up mechanism	N/A
35	Position in subordination hierarchy in liquidation (specify instrument type immediately senior to instrument)	Subordinated. Senior bondholders are immediately senior to this instrument
36	Non-compliant transitioned features	N/A
37	If yes, specify non-compliant features	N/A

TABLE 2: CAPITAL STRUCTURE	
Main features template of regulatory capital instruments - (Table 2(e))	
1 Issuer	National Commercial Bank
2 Unique identifier (eg CUSIP, ISIN or Bloomberg identifier for private placement)	N/A
3 Governing law(s) of the instrument	The instrument is governed by the laws of the Kingdom of Saudi Arabia
Regulatory treatment	
4 Transitional Basel III rules	Additional Tier 1
5 Post-transitional Basel III rules	Eligible
6 Eligible at solo/group/group & solo	Group and Solo
7 Instrument type	Subordinated Sukuk
8 Amount recognized in regulatory capital (Currency in mil, as of most recent reporting date)	SAR 1,000mil
9 Par value of instrument	SAR 1,000mil
10 Accounting classification	Equity
11 Original date of issuance	22nd June 2015
12 Perpetual or dated	Perpetual
13 Original maturity date	N/A
14 Issuer call subject to prior supervisory approval	Yes
15 Option call date, contingent call dates and redemption amount	In compliance with Basel III, call date is equal to or greater than 5 years
16 Subsequent call dates if applicable	Any profit distribution dates after the first call date
Coupons / dividends	
17 Fixed or Floating dividend/coupon	N/A
18 Coupon rate and any related index	N/A
19 Existence of a dividend stopper	Yes
20 Fully discretionary, partially discretionary or mandatory	Fully Discretionary
21 Existence of step up or other incentive to redeem	None
22 Non-cumulative or cumulative	Non-cumulative
23 Convertible or non-convertible	Non - convertible
24 If convertible, conversion trigger (s)	N/A
25 If convertible, fully or partially	N/A
26 If convertible, conversion rate	N/A
27 If convertible, mandatory or optional conversion	N/A
28 If convertible, specify instrument type convertible into	N/A
29 If convertible, specify issuer of instrument it converts into	N/A
30 Write-down feature	Yes
31 If write-down, write-down trigger (s)	Terms of contract of the instrument provide the legal basis for SAMA to trigger write-down (a contractual approach)
32 If write-down, full or partial	Written down fully or partial
33 If write-down, permanent or temporary	Permanent
34 If temporary write-down, description of the write-up mechanism	N/A
35 Position in subordination hierarchy in liquidation (specify instrument type immediately senior to instrument)	Subordinated. Senior and Tier II subordinated sukukholders are senior to this instrument
36 Non-compliant transitioned features	N/A
37 If yes, specify non-compliant features	N/A

TABLE 2: CAPITAL STRUCTURE		
Main features template of regulatory capital instruments - (Table 2(e))		
1	Issuer	National Commercial Bank
2	Unique identifier (eg CUSIP, ISIN or Bloomberg identifier for private placement)	N/A
3	Governing law(s) of the instrument	The instrument is governed by the laws of the Kingdom of Saudi Arabia
Regulatory treatment		
4	Transitional Basel III rules	Additional Tier 1
5	Post-transitional Basel III rules	Eligible
6	Eligible at solo/group/group & solo	Group and Solo
7	Instrument type	Subordinated Sukuk
8	Amount recognized in regulatory capital (Currency in mil, as of most recent reporting date)	SAR 2,000mil
9	Par value of instrument	SAR 2,000mil
10	Accounting classification	Equity
11	Original date of issuance	15th July 2015
12	Perpetual or dated	Perpetual
13	Original maturity date	N/A
14	Issuer call subject to prior supervisory approval	Yes
15	Option call date, contingent call dates and redemption amount	In compliance with Basel III, call date is equal to or greater than 5 years
16	Subsequent call dates if applicable	Any profit distribution dates after the first call date
Coupons / dividends		
17	Fixed or Floating dividend/coupon	N/A
18	Coupon rate and any related index	N/A
19	Existence of a dividend stopper	Yes
20	Fully discretionary, partially discretionary or mandatory	Fully Discretionary
21	Existence of step up or other incentive to redeem	None
22	Non-cumulative or cumulative	Non-cumulative
23	Convertible or non-convertible	Non - convertible
24	If convertible, conversion trigger (s)	N/A
25	If convertible, fully or partially	N/A
26	If convertible, conversion rate	N/A
27	If convertible, mandatory or optional conversion	N/A
28	If convertible, specify instrument type convertible into	N/A
29	If convertible, specify issuer of instrument it converts into	N/A
30	Write-down feature	Yes
31	If write-down, write-down trigger (s)	Terms of contract of the instrument provide the legal basis for SAMA to trigger write-down (a contractual approach)
32	If write-down, full or partial	Written down fully or partial
33	If write-down, permanent or temporary	Permanent
34	If temporary write-down, description of the write-up mechanism	N/A
35	Position in subordination hierarchy in liquidation (specify instrument type immediately senior to instrument)	Subordinated. Senior and Tier II subordinated sukukholders are senior to this instrument
36	Non-compliant transitioned features	N/A
37	If yes, specify non-compliant features	N/A

TABLE 2: CAPITAL STRUCTURE	
Main features template of regulatory capital instruments - (Table 2(e))	
1 Issuer	National Commercial Bank
2 Unique identifier (eg CUSIP, ISIN or Bloomberg identifier for private placement)	N/A
3 Governing law(s) of the instrument	The instrument is governed by the laws of the Kingdom of Saudi Arabia
Regulatory treatment	
4 Transitional Basel III rules	Additional Tier 1
5 Post-transitional Basel III rules	Eligible
6 Eligible at solo/group/group & solo	Group and Solo
7 Instrument type	Subordinated Sukuk
8 Amount recognized in regulatory capital (Currency in mil, as of most recent reporting date)	SAR 2,700mil
9 Par value of instrument	SAR 2,700mil
10 Accounting classification	Equity
11 Original date of issuance	23rd December 2015
12 Perpetual or dated	Perpetual
13 Original maturity date	N/A
14 Issuer call subject to prior supervisory approval	Yes
15 Option call date, contingent call dates and redemption amount	In compliance with Basel III, call date is equal to or greater than 5 years
16 Subsequent call dates if applicable	Any profit distribution dates after the first call date
Coupons / dividends	
17 Fixed or Floating dividend/coupon	N/A
18 Coupon rate and any related index	N/A
19 Existence of a dividend stopper	Yes
20 Fully discretionary, partially discretionary or mandatory	Fully Discretionary
21 Existence of step up or other incentive to redeem	None
22 Non-cumulative or cumulative	Non-cumulative
23 Convertible or non-convertible	Non - convertible
24 If convertible, conversion trigger (s)	N/A
25 If convertible, fully or partially	N/A
26 If convertible, conversion rate	N/A
27 If convertible, mandatory or optional conversion	N/A
28 If convertible, specify instrument type convertible into	N/A
29 If convertible, specify issuer of instrument it converts into	N/A
30 Write-down feature	Yes
31 If write-down, write-down trigger (s)	Terms of contract of the instrument provide the legal basis for SAMA to trigger write-down (a contractual approach)
32 If write-down, full or partial	Written down fully or partial
33 If write-down, permanent or temporary	Permanent
34 If temporary write-down, description of the write-up mechanism	N/A
35 Position in subordination hierarchy in liquidation (specify instrument type immediately senior to instrument)	Subordinated. Senior and Tier II subordinated sukukholders are senior to this instrument
36 Non-compliant transitioned features	N/A
37 If yes, specify non-compliant features	N/A

### 3.0 Capital Adequacy

The bank defines capital as the resources necessary to cover unexpected losses and thus NCB, at all times, maintains a sufficient capital to cover risks inherent in its business operations and to maintain a strong credit rating.

The Bank has an Internal Capital Adequacy Assessment Process (ICAAP) by which it examines its risk profile from both regulatory and economic capital point of view and ensures that the level of capital supply:

- remains sufficient to support the Bank's risk profile;
- exceeds the Bank's formal, minimum regulatory capital requirements by a predefined buffer;
- is capable of withstanding stressed scenarios;
- remains consistent with the Bank's strategic and operational plans.

Within the framework of the ICAAP, an annual Capital Plan is prepared. The Capital Plan is reviewed by the Senior Management and approved by the Board of Directors of the Bank and is submitted to SAMA in accordance with their directives.

Regulatory and economic capital assessments are used for the management of risk and capital within the Bank. The economic capital assessment is the more risk-sensitive measure and it takes into account the correlation between different risks.

The economic capital models employed at the Bank are calibrated to quantify the level of capital that is sufficient to absorb potential losses over a one-year time horizon at a 99.9 percent degree of confidence.

The Bank identifies and manages the risks it faces through defined internal control procedures and stress testing. It assesses and manages the following risks via the capital planning process:

- Credit risk
- Market risk
- Operational risk
- Liquidity risk
- Interest rate risk
- Concentration risk
- Macroeconomic and business cycle risk
- Strategic risk
- Reputation risk
- Settlement and Pre-settlement Risks

Scenario analysis and stress testing

The Bank regularly assesses eligible capital supply against stressed losses under a range of scenarios. Stress scenarios are developed using historical losses, qualitative and quantitative techniques, and are employed to estimate the impact on capital requirements. The Senior Management and the Board are regularly informed of the results of the stress tests to ensure that the Bank has sufficient capital and that any unacceptable risks are mitigated. These scenarios are regularly reviewed and updated to account for the changing market conditions.

The Bank's Capital Plan examines that the Bank's current and projected capital is adequate to bear any stressed losses and to support its current activities and future strategies and operational plans.

Following table gives the Bank's Capital Adequacy Ratios (CAR) as of 31<sup>st</sup> of December 2015.

<b>CAPITAL ADEQUACY – CAR (SAMA reference table 3)</b>		
<b>Capital Adequacy Ratios (TABLE 3, (f))</b>		
<b>Particulars</b>	<b>Total capital ratio</b>	<b>Tier 1 capital ratio</b>
	<b>%</b>	
Top consolidated level	17.2%	15.1%



## 4.0 Credit risk

Credit risk is the risk of financial loss resulting from the failure of a borrower or counterparty to honor its financial or contractual obligations. Credit exposures arise principally in credit-related risk that is embedded in financing and advances and investments. There is also credit risk in foreign exchange and derivative transactions, as well as off-balance sheet financial instruments, such as trade-finance related products derivatives and financing commitments. Among the risks the Bank engages in, credit risk generates the largest regulatory capital requirement.

Following table gives exposures subject to credit risk and related capital charges as of 31<sup>st</sup> of December 2015.

<b>CAPITAL ADEQUACY – Credit Risk (SAMA reference table 3)</b>						
<b>Amount of Exposures Subject To Standardized Approach of Credit Risk and related Capital Requirements (TABLE 3, (b))</b>						
<b>Portfolios</b>	<b>Amount of exposures (On Balance Sheet)</b>	<b>Capital requirements</b>	<b>Amount of exposures (Off Balance Sheet + Derivatives)</b>	<b>Capital requirements</b>	<b>Total Amount of Exposure</b>	<b>Total Capital requirements</b>
	<b>(SAR '000)</b>	<b>(SAR '000)</b>	<b>(SAR '000)</b>	<b>(SAR '000)</b>	<b>(SAR '000)</b>	<b>(SAR '000)</b>
Sovereigns and central banks:	68,973,666	419,942	1,449,081	14,921	70,422,747	434,864
<i>SAMA and Saudi Government</i>	31,161,339	-	-	-	31,161,339	-
<i>Others</i>	37,812,326	419,942	1,449,081	14,921	39,261,407	434,864
Multilateral Development Banks (MDBs)	6,625,370	-	-	-	6,625,370	-
Public Sector Entities (PSEs)	49,395	3,952	7,447	583	56,842	4,534
Banks and securities firms	27,341,932	929,743	11,698,738	458,149	39,040,670	1,387,891
Corporates	199,042,050	12,082,391	40,930,252	2,836,188	239,972,302	14,918,579
Retail non-mortgages	72,962,669	4,350,334	4,207,573	219,143	77,170,243	4,569,477
<i>Small Business Facilities Enterprises(SBFE's)</i>	6,560,350	367,758	2,416,816	138,649	8,977,166	506,407
Mortgages	29,007,885	2,320,631	998,334	79,867	30,006,219	2,400,498
<i>Residential</i>	19,135,484	1,530,839	420,181	33,614	19,555,666	1,564,453
<i>Commercial</i>	9,872,400	789,792	578,153	46,252	10,450,553	836,044
Securitized assets	8,931,170	142,899	-	-	8,931,170	142,899
Equity	1,278,677	111,993	-	-	1,278,677	111,993
Others	29,649,300	1,691,198	1,273	600,606	29,650,572	2,291,804
<b>Total</b>	<b>443,862,114</b>	<b>22,053,082</b>	<b>59,292,699</b>	<b>4,209,456</b>	<b>503,154,813</b>	<b>26,262,538</b>

Following tables give exposures subject to credit risk as of 31<sup>st</sup> of December 2015 and the average exposure during the year then ended.

<b>CREDIT RISK (SAMA reference table 4)</b>		
<b>Credit Risk Exposure (Table 4, (b))</b>		
<b>Portfolios</b>	<b>Total gross credit risk exposure (SAR '000)</b>	<b>Average gross credit risk exposure over the period * (SAR '000)</b>
Sovereigns and central banks:	70,422,747	119,200,724
<i>SAMA and Saudi Government</i>	31,161,339	80,335,195
<i>Others</i>	39,261,407	38,865,529
Multilateral Development Banks (MDBs)	6,625,370	7,853,391
Public Sector Entities (PSEs)	56,842	67,293
Banks and securities firms	39,040,670	30,147,007
Corporates	239,972,302	189,936,251
Retail non-mortgages	77,170,243	68,620,981
<i>Small Business Facilities Enterprises (SBFE's)</i>	8,977,166	7,588,641
Mortgages	30,006,219	23,404,616
<i>Residential</i>	19,555,666	15,209,226
<i>Commercial</i>	10,450,553	8,195,390
Securitized assets	8,931,170	8,241,246
Equity	1,278,677	2,152,467
Others	29,650,573	22,454,808
<b>Total</b>	<b>503,154,813</b>	<b>472,078,785</b>

\* The average is calculated on a quarterly basis

## 4.1 Strategies

The principal objective of credit risk management is to ensure a high quality credit portfolio and the minimization of losses. This objective is accomplished by:

- maintaining a strong culture of responsible lending, supported by a robust risk policy and control framework;
- challenging business originators effectively in defining and implementing risk appetite within individual obligor and industry concentration limits; and
- ensuring independent, expert scrutiny and approval of credit risks and their mitigation.

## 4.2 Organization Structure

### Corporate Group

The Head of Corporate Risk Management (HCRM) within the Credit Risk function supports the Chief Risk Officer (CRO), as head of the Risk function, in overseeing credit risks at the highest level. The Credit Risk function primarily comprises: undertaking independent reviews and approval of larger and higher-risk credit proposals, setting a risk appetite framework and developing and maintaining the Bank's credit policy and credit programs.

The credit risk function includes Senior Credit Officers based regionally and with industry specialization Kingdom-wide. These officers including the HCRM, fulfill an essential role as independent risk control and approving units as distinct from business line management. They objectively scrutinize and approve credit proposals within the limits set by the credit policy of the Bank.

Approval of the Credit and Remedial Management Committee, Executive Committee and/or Board is required to extend facilities to customers above certain risk-based thresholds.

### **Retail Group**

The Head of Retail Risk Management within the Credit Risk function supports the Chief Risk Officer (CRO), and is responsible for consumer credit risk management including setting the risk appetite framework and developing and maintaining the Bank's credit policies. The Consumer Lending business is governed by Consumer Finance Islamic Credit Policy (CFICP) Manual which is approved by the Board of Directors, and defines the policies and procedures for the handling of all activities related to consumer lending.

### **Enterprise Risk Management**

Enterprise Risk Management Department, as part of Risk Group, is responsible for reporting on risk matters to Senior Management, Board and to regulator, providing credit analytics, calculating and reporting the Bank's regulatory and economic capital and performing stress tests. It owns and develops risk models. It prepares quarterly risk reports for the Senior Management and the Risk Committee of the Board.

Enterprise Risk Management includes the Retail Portfolio Management & Risk Analytics which handles all portfolio and risk analytic activities, including application and behavioural scoring models related to the consumer portfolio.

### **4.3 Risk reporting and monitoring – risk rating systems**

The Bank's exposure to credit risk arises from a wide range of asset classes, customers and product types. A breakdown of the Bank's financing and advances to major economic sectors is provided in note 7.5 of the *Audited Financial Statements for the year ended 31 December 2015*.

To measure and manage the risk in these exposures, both to individually assessed customers and to those aggregated into portfolios, the Bank employs risk rating systems and other methodologies (such as analysis of past dues). The main characteristics of the Bank's credit risk rating system are set out in notes 7.4 and 31 of the *Audited Financial Statements for the year ended 31 December 2015*.

Following table gives a geographic breakdown of exposures as of 31<sup>st</sup> of December 2015.

TABLE 4 (STA): CREDIT RISK: GENERAL DISCLOSURES								
Geographic Breakdown (Table 4, (c))								
Portfolios	Geographic Area (SAR '000)							
	Saudi Arabia	Other GCC & Middle East	Europe	North America	South East Asia	Turkey	Other Countries	Total
Sovereigns and central banks:	31,161,340	11,638,920	1,096,608	8,297,278	2,128,125	10,974,670	5,125,806	70,422,747
SAMA and Saudi Government	31,161,340							31,161,340
Others		11,638,920	1,096,608	8,297,278	2,128,125	10,974,670	5,125,806	39,261,407
Multilateral Development Banks (MDBs)	3,373,570		774,000	2,344,301	133,500			6,625,370
Public Sector Entities (PSEs)						56,842		56,842
Banks and securities firms	9,048,771	7,556,617	6,752,308	5,778,346	395,298	1,589,578	7,919,753	39,040,670
Corporate	161,032,816	26,812,773	4,996,949	18,243,655	2,000,081	17,830,890	9,055,138	239,972,302
Retail non-mortgages	65,623,394					11,546,849		77,170,243
Small Business Facilities Enterprises (SBFE's)						8,977,166		8,977,166
Mortgages	17,954,226					12,051,993		30,006,219
Residential	13,809,973					5,745,693		19,555,666
Commercial	4,144,254					6,306,300		10,450,553
Securitized assets				6,936,782			1,994,388	8,931,170
Equity	1,253,071	19,314				6,292		1,278,676
Others	20,298,340	455,363	5,030,243	1,428,750	8,058	2,429,819		29,650,572
<b>Total</b>	<b>309,745,528</b>	<b>46,482,986</b>	<b>18,650,108</b>	<b>43,029,111</b>	<b>4,665,062</b>	<b>56,486,932</b>	<b>24,095,085</b>	<b>503,154,813</b>

Following table gives an industry sector breakdown of exposures as of 31<sup>st</sup> of December 2015.

**TABLE 4 (STA): CREDIT RISK: GENERAL DISCLOSURES**

Industry Sector Breakdown (Table 4, (d))													
Portfolios	Industry sector (SAR '000)												
	Government and quasi government	Banks and other financial institutions	Agriculture and fishing	Manufacturing	Mining and quarrying	Electricity, water, gas and health services	Building and construction	Commerce	Transportation and communication	Services	Consumer loans and credit cards	Others	Total
Sovereigns and central banks:	70,422,747												70,422,747
SAMA and Saudi Government	31,161,339												31,161,339
Others	39,261,407												39,261,407
Multilateral Development Banks (MDBs)		6,625,370											6,625,370
Public Sector Entities (PSEs)					42,296	2,296		108	4,607	7,271		264	56,843
Banks and securities firms		39,027,350										13,320	39,040,670
Corporates	8,001,774	22,291,402	1,364,085	36,100,506	7,367,976	27,145,523	34,442,029	50,105,127	20,870,193	22,577,137		9,706,550	239,972,302
Retail non-mortgages		19,372	140,055	2,447,639	78,186	107,901	1,254,219	3,890,624	324,478	608,570	68,152,676	146,524	77,170,243
Small Business Facilities Enterprises (SBFE's)		18,196	139,919	2,427,670	78,143	107,870	1,252,736	3,883,626	324,362	608,014		136,631	8,977,166
Mortgages		8,388	155,864	2,155,636	65,305	236,077	3,388,165	4,684,111	262,301	1,530,797	16,867,832	651,741	30,006,219
Residential		5,909	39,861	441,937	14,965	54,196	874,240	839,427	121,023	296,276	16,867,832		19,555,666
Commercial		2,479	116,003	1,713,699	50,340	181,882	2,513,925	3,844,685	141,278	1,234,521		651,741	10,450,553
Securitized assets												8,931,170	8,931,170
Equity		884,324		11,050				367,802		9,438		6,063	1,278,678
Others		9,771,783	8,601	97,492	19,411	12,236	123,921	214,630	23,722	26,508		19,352,267	29,650,572
<b>Total</b>	<b>78,424,521</b>	<b>78,627,989</b>	<b>1,668,606</b>	<b>40,812,323</b>	<b>7,573,173</b>	<b>27,504,034</b>	<b>39,208,333</b>	<b>59,262,403</b>	<b>21,485,301</b>	<b>24,759,721</b>	<b>85,020,508</b>	<b>38,807,902</b>	<b>503,154,813</b>

Following table gives a maturity breakdown of exposures as of 31<sup>st</sup> of December 2015.

CREDIT RISK (SAMA reference table 4)									
Residual Contractual Maturity Breakdown (Table 4, (e))									
Portfolios	Maturity breakdown (SAR '000)								
	Less than 8 days	8-30 days	30-90 days	90-180 days	180-360 days	1-3 years	3-5 years	Over 5 years	Total
Sovereigns and central banks:	8,556,472	49,891	702,511	681,354	2,955,446	4,953,886	8,069,688	44,453,498	70,422,747
<i>SAMA and Saudi Government</i>	1,011,233	4,984	16,727	215,682	319,626	222,246	891	29,369,951	31,161,340
<i>Others</i>	7,545,239	44,907	685,785	465,671	2,635,820	4,731,640	8,068,798	15,083,547	39,261,407
Multilateral Development Banks (MDBs)				151,875		1,411,500	3,075,537	1,986,459	6,625,370
Public Sector Entities (PSEs)	2,528		72	11,102	21	38,737	115	4,267	56,842
Banks and securities firms	7,802,346	3,317,633	4,159,533	5,424,129	4,344,988	9,215,835	2,410,968	2,365,238	39,040,670
Corporates	8,216,639	10,844,731	23,519,643	27,627,742	25,453,778	46,982,085	35,243,530	62,084,153	239,972,302
Retail non-mortgages	6,169,900	597,428	3,100,440	8,124,780	10,820,049	25,241,727	20,506,160	2,609,758	77,170,242
<i>Small Business Facilities Enterprises (SBFE's)</i>	381,863	329,849	1,073,595	1,695,170	2,251,672	2,333,794	454,557	456,667	8,977,166
Mortgages	460,207	172,360	574,780	1,100,952	1,611,361	4,795,923	3,491,618	17,799,019	30,006,219
<i>Residential</i>	295,232	53,237	153,627	322,479	692,551	1,826,956	1,436,308	14,775,276	19,555,666
<i>Commercial</i>	164,975	119,122	421,154	778,473	918,810	2,968,966	2,055,310	3,023,743	10,450,554
Securitized assets						241,594	274,937	8,414,639	8,931,170
Equity	6,292							1,272,385	1,278,677
Others	10,104,822	221,422	221,289	1,802,203	1,340,563	388,344	137,767	15,434,163	29,650,572
<b>Total</b>	<b>41,319,206</b>	<b>15,203,465</b>	<b>32,278,270</b>	<b>44,924,137</b>	<b>46,526,205</b>	<b>93,269,629</b>	<b>73,210,321</b>	<b>156,423,580</b>	<b>503,154,813</b>

#### **4.4 Internal methodologies for calculating economic capital requirements**

The Bank's credit risk rating framework incorporates probability of default ('PD') of an obligor and loss severity expressed in terms of exposure-at-default ('EAD') and loss-given-default ('LGD'). These measures are used to calculate expected loss and capital requirements.

For Corporate business, obligor PD is estimated using a 16-grade Customer Risk Rating scale for performing customers. These grades represent varying degrees of strength of financial condition and qualitative factors. The Customer Risk Ratings are mapped to a PD value range.

For retail business, the portfolios are analyzed by pools and models are available to provide PD and LGD estimates based on historical experience.

#### **4.5 Credit risk management policy, past due and impaired, specific and general allowances**

A discussion on the bank's credit risk management policy is included in note 32 of the *Audited Financial Statements for the year ended 31 December 2015*.

The bank considers all the facilities for a counterparty to be defaulted if any one of the facilities of the counterparty is past due more than 90 days.

The approaches followed for specific and general allowances (collective allowances) are explained in note 2.5 of the *Audited Financial Statements for the year ended 31 December 2015*.



Following table gives an industry sector breakdown of impaired and past due loans and related allowances as of 31<sup>st</sup> December 2015.

<b>CREDIT RISK (SAMA reference table 4)</b>										
<b>Impaired Loans, Past Due Loans and Allowances (Table 4, (f))</b>										
Industry sector	Impaired loans (SR '000)	Defaulted (SR '000)	Aging of Past Due Loans (days) (SR '000)				Specific allowances (SR '000)			General allowances (SR '000)
			Less than 90	90-180	180-360	Over 360	Charges during the period	Charge-offs during the period	Balance at the end of the period	
Government and quasi government										
Banks and other financial institutions	199	199	1,068	131	53	15	(2,865)	-	131	
Agriculture and fishing	38,231	38,231	44,897	3,334	13,458	21,438	6,283	(124)	24,005	
Manufacturing	628,839	628,839	493,568	40,559	151,555	436,725	110,104	(5,872)	525,561	
Mining and quarrying	55,830	55,830	34,973	2,728	48,934	4,167	39,992	-	42,731	
Electricity, water, gas and health services	23,554	23,554	57,963	8,820	4,603	10,132	1,958	-	9,833	
Building and construction	613,663	613,663	716,538	77,433	112,162	424,069	179,740	(195,034)	497,118	
Commerce	1,308,843	1,308,843	922,122	156,777	279,598	872,468	289,732	(122,364)	1,103,384	
Transportation and communication	90,151	90,151	119,162	6,528	25,023	58,600	41,585	(41)	79,615	
Services	133,203	133,203	223,022	77,420	24,367	31,416	70,210	(46)	102,932	
Consumer loans and credit cards	715,177	715,177	3,997,190	544,873	124,906	45,398	1,215,838	(1,152,327)	410,495	
Others	74,260	74,260	3,584	3,505	6,880	63,876	3,173	(282)	60,621	
<b>Total</b>	<b>3,681,949</b>	<b>3,681,949</b>	<b>6,614,089</b>	<b>922,107</b>	<b>791,538</b>	<b>1,968,304</b>	<b>1,955,749</b>	<b>(1,476,089)</b>	<b>2,856,426</b>	<b>2,707,197</b>

Following table gives a geographic breakdown of impaired and past due loans and related allowances as of 31<sup>st</sup> December 2015.

CREDIT RISK (SAMA reference table 4)							
Impaired Loans, Past Due Loans And Allowances (Table 4, (g))							
Geographic area (SR '000)	Impaired loans (SR '000)	Aging of Past Due Loans (days) (SR '000)				Specific allowances (SR '000)	General allowances (SR '000)
		Less than 90	90-180	180-360	Over 360		
Saudi Arabia	2,074,866	4,752,660	669,286	279,815	1,125,765	1,790,210	2,454,609
Other GCC & Middle East							
Turkey	1,607,082	1,861,428	252,820	511,723	842,539	1,066,216	252,588
Others Countries							
<b>Total</b>	<b>3,681,949</b>	<b>6,614,089</b>	<b>922,107</b>	<b>791,538</b>	<b>1,968,304</b>	<b>2,856,426</b>	<b>2,707,197</b>

Following table gives the movement in specific and general allowances for the year ended 31<sup>st</sup> December 2015.

<b>CREDIT RISK (SAMA reference table 4)</b>		
<b>Reconciliation Of Changes In The Allowances For Loan Impairment (Table 4, (h))</b>		
<b>Particulars</b>	<b>Specific allowances (SAR '000)</b>	<b>General allowances (SAR '000)</b>
Balance, beginning of the year	2,376,767	2,755,498
Charge-offs taken against the allowances during the period	(1,476,089)	
Amounts set aside (or reversed) during the period	2,096,188	(27,397)
Other adjustments:		
- exchange rate differences	(140,440)	(39,712)
- business combinations		
- acquisitions and disposals of subsidiaries		
- etc.		18,808
Transfers between allowances		
Balance, end of the year	2,856,426	2,707,197

*Charge-offs and recoveries that have been recorded directly to the income statement are SAR 671K and SAR (371,472)K respectively.*

#### **4.6 Application of the standardized approach for credit risk**

The Bank uses the Standardized approach of Basel III to calculate the risk weighted assets and required Regulatory Capital for Pillar -1 (including credit risk, market risk and operational risk). It requires banks to use risk assessments prepared by External Credit Assessment Institutions (ECAI) to determine the risk weightings applied to rated counterparties. For counterparties not rated externally the assigned risk weightings are in accordance with SAMA guidelines.

Following table gives a breakdown by risk weightings (buckets) of the Bank's exposures after the impact of credit risk mitigation (CRM), as of 31<sup>st</sup> December 2015.

CREDIT RISK: DISCLOSURES FOR PORTFOLIOS SUBJECT TO THE STANDARDIZED APPROACH (SAMA reference table 5)										
Allocation Of Exposures To Risk Buckets (Table 5, (b))										
Particulars	Risk buckets (SAR '000)									Deducted (SAR '000)
	0%	20%	35%	50%	75%	100%	150%	Other risk weights	Unrated	
Sovereigns and central banks:	77,147,353	972,800		7,007,646		1,737,413				
<i>SAMA and Saudi Government</i>	43,356,619									
<i>Others</i>	33,790,734	972,800		7,007,646		1,737,413				
Multilateral Development Banks (MDBs)	6,625,370									
Public Sector Entities (PSEs)	131	39				56,674				
Banks and securities firms		7,792,632		29,130,665		1,218,969	3,902			
Corporates	431,791	29,082,743		20,432,449		170,449,835	167			
Retail non-mortgages	333,268	152,437		59,817	75,933,027	108,752				
<i>Small Business Facilities Enterprises (SBFE's)</i>	297,555	126,934		925	8,391,892	10,316				
Mortgages						30,006,219				
<i>Residential</i>						19,555,666				
<i>Commercial</i>						10,450,553				
Securitized assets		8,931,170								
Equity						1,197,855		80,821		
Others	8,426,334	4,785,104		53,487		20,831,407	164,534			

## 4.7 Credit Risk Mitigation

Risk mitigation is an important aspect of the Bank's effective credit risk management and it takes many forms.

The Bank in the ordinary course of lending activities holds collaterals as security to mitigate credit risk in the financing and advances. The collaterals are held mainly against commercial and individual loans and are managed against relevant exposures at their net realizable values. The Bank monitors the market value of collateral obtained periodically and requests additional collateral in accordance with the terms of the underlying agreements.

These collaterals mostly include time and other cash deposits, financial guarantees from other banks, local and international equities, real estate and other fixed assets

The Bank's policy is set out in note 32 of the *Audited Financial Statements for the year ended 31 December 2015*.

In terms of the regulatory guidelines, not all forms of collateral currently used by the Bank are recognized for the purposes of the calculation of the credit risk capital requirement. The bank uses the Basel III 'comprehensive method' for the treatment of financial collaterals which requires a standard supervisory haircut to be applied to the collateral to account for currency and maturity mismatches between the underlying exposure and the collateral applied.

Eligible financial collaterals under the Standardised Approach as per SAMA guidelines is restricted to:

- a. Cash (as well as certificates of deposit or comparable instruments);
- b. Gold; and
- c. Debt Securities

Non-financial collaterals mainly include guarantees.

Following table gives the eligible collateral held by the bank as of 31<sup>st</sup> December 2015.

<b>CREDIT RISK MITIGATION (CRM): DISCLOSURES FOR STANDARDIZED APPROACH (SAMA reference table 7)</b>		
<b>Credit Risk Exposure Covered By CRM (Table 7, (b) and (c))</b>		
<b>Portfolios</b>	<b>Covered by</b>	
	<b>Eligible financial collateral (SAR '000)</b>	<b>Guarantees / credit derivatives (SAR '000)</b>
Sovereigns and central banks:	1,249,544	
<i>SAMA and Saudi Government</i>		
<i>Others</i>	1,249,544	
Multilateral Development Banks (MDBs)		
Public Sector Entities (PSEs)	413	
Banks and securities firms	21,855	978,964
Corporates	5,301,027	15,756,416
Retail non-mortgages	1,036,316	162,512
<i>Small Business Facilities Enterprises (SBFE's)</i>	523,879	162,512
Mortgages		
<i>Residential</i>		
<i>Commercial</i>		
Securitized assets		
Equity		
Others	2,290	
<b>Total</b>	<b>7,611,445</b>	<b>16,897,892</b>

#### **4.8 Use of External Credit Assessment Institutions (ECAIs)**

The Bank uses the following External Credit Assessment Institutions (ECAIs)

- i) Standards and Poor's Rating Group
- ii) Moody's Investor Service
- iii) Fitch Group

External Credit Assessment Institutions risk assessments are used by the Bank as part of the determination of risk weightings for the following classes of exposure:

- Sovereign and Central Banks;
- Banks and Securities Firms; and
- Corporates.

The process used to transfer credit assessment ratings to the banks' counterparties is as follows. A data file containing external ratings is downloaded from a specialist third party supplier (Bloomberg). The rating records from the External Credit Assessment Institutions specified above are then linked with the Bank's counterparty records. As the majority of the bank's corporate borrowers are not rated by external agencies, for regulatory capital calculations under the Basel III 'Standardised Approach' these are treated as 'unrated' exposures. The use of external ratings within the Corporate exposure class mainly relates to its investments in corporate bonds.

The alignment of the alphanumerical scale of agencies used with risk buckets is based on the guidance issued by SAMA.

#### **4.9 Exposure related to counterparty credit risk**

Economic and Regulatory Capital is calculated for counterparty credit exposures on the Bank's derivatives portfolio using the 'Current Exposure Method' within the Basel III Standardised Approach. Limits for corporate and banking counterparty credit exposures including derivatives are approved by the relevant authority. Risk Group of the Bank is responsible for monitoring adherence to these limits on a daily basis.

Following table gives the exposures to counterparty credit risk for derivatives as of 31<sup>st</sup> of December 2015.

<b>GENERAL DISCLOSURES FOR EXPOSURES RELATED TO COUNTERPARTY CREDIT RISK (CCR) (SAMA reference table 8)</b>	
<b>General Disclosures (Table 8, (b) and (d))</b>	
<b>Particulars</b>	<b>Amount (SAR '000)</b>
Gross positive fair value of contracts	2,489,033
Netting Benefits	
Netted Current Credit Exposure*	
Collateral held:	
-Cash	
-Government securities	
-Others	
Exposure amount (under the applicable method)	3,696,655
-Current Exposure Method (CEM)	3,696,655
Notional value of credit derivative hedges	
Current credit exposure (by type of credit exposure):	3,696,655
-Interest rate contracts	620,903
-FX contracts	3,043,729
-Equity contracts	27,912
-Credit derivatives	
-Commodity/other contracts	4,107

\* Currently, netting for credit exposure measurement purposes not permitted in KSA.



Specific wrong-way risk arises, if future exposure to a specific counterparty is expected to be high when the counterparty's probability of default is also high. The Bank's Treasury Products Approval Committee (TPAC) approves all new products. As part of its approval process the TPAC ensures that any new treasury product will not result in specific wrong-way risk.

The Bank usually does not take collateral nor is it required to provide collateral in connection with its over-the-counter derivatives activity. Credit reserves are created in accordance with impairment of financial assets policy stated in note 3.14 of the *Audited Financial Statements for the year ended 31 December 2015*.

#### **4.10 Securitization**

The Bank is not involved in any securitization activities which transfer credit risk away from the Bank to other entities.

## 5.0 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.

For risk capital computations, the Bank separates its exposure to market risk between trading and banking books. Trading book is mainly held by the Treasury division and includes positions arising from market making and proprietary position taking, together with financial assets and liabilities that are managed on a fair value basis.

### 5.1 Strategies

The objective of market risk management is to manage and control market risk exposures within acceptable parameters.

### 5.2 Organization Structure

Overall authority for market risk is vested in the Board of Directors. Risk Group is responsible for the development of detailed risk management policies (subject to review and approval by the Board of Directors) and for the day-to-day review of their implementation.

The Group has an independent market risk management and control function which is responsible for measuring, monitoring and reporting market risk exposures according to defined policies and limits on a regular basis.

### 5.3 Risk reporting and monitoring

The Bank uses tools such as Value-at-Risk (VaR) and other measures to monitor and limit market risk exposures. The scope and nature of risk reporting and measurement systems used are explained in detail in note 33 of the *Audited Financial Statements for the year ended 31 December 2015*.

### Stress testing

As VaR is a measure based on historical volatilities and correlations, which may break down during stressed market conditions, the Bank also performs stress testing to evaluate the potential impact on portfolio values of more extreme, although plausible, events or movements in a set of financial variables. Consideration is given to the actual market risk exposures, along with market events, in determining the stress scenarios.

Stress testing is performed by the Risk Group at a bank wide level, based on historical and stressed scenarios which are regularly reviewed and updated. The stress testing results are regularly reported to the Senior Management and provide them with an assessment of the financial impact such events would have on the capital and profitability of the bank.

### **5.4 Risk Mitigation – Hedging**

The Bank's hedging and risk mitigation strategies primarily comprise the use of traditional market instruments, such as swaps and cash instruments, to address risk factors arising at portfolio level.

### **5.5 Internal methodologies for calculating economic capital requirements**

The main principal tool used by the Bank to calculate Economic Capital requirements for market risk is Value at Risk (VaR). The key assumptions used in the VaR model are explained in note 33.1 of the *Audited Financial Statements for the year ended 31 December 2015*.

### 5.6 Application of the standardized approach for market risk

The Bank uses the Standardized approach of Basel III to calculate the required Regulatory Capital for market risk which covers general market and specific risks. Brief descriptions of the risk items covered by market risk are given below:

- a. Interest rate risk is the impact on Bank’s earnings and equity of changes in interest rates; the risk is two-fold:
  - Specific Risk: risk of loss caused by an adverse price movement of a debt instrument or security due principally to factors related to the issuer.
  - General Market Risk: risk of loss arising from adverse changes in market conditions.
- b. Equity risk is the risk that the Bank’s investments will depreciate due to equity market dynamics.
- c. Foreign exchange risk is the risk arising from a change in exchange-rates on the Bank net asset / liability positions.
- d. Commodity risk refers to the uncertainties of future market values and of the size of the future income, caused by the fluctuation in the prices of commodities.

The primary market risks to which the Bank is exposed are foreign exchange risk and interest rate risk associated with its trading book that is marked-to-market daily (mainly derivatives).

Following table gives the capital requirement for market risk as of 31<sup>st</sup> of December 2015.

<b>CAPITAL ADEQUACY – Market Risk (SAMA reference table 3)</b>					
<b>Capital Requirements For Market Risk (822, Table 3, (d) &amp; Table 10, (b))</b>					
	<b>Interest rate risk (SAR '000)</b>	<b>Equity position risk (SAR '000)</b>	<b>Foreign exchange risk (SAR '000)</b>	<b>Commodity risk (SAR '000)</b>	<b>Total (SAR '000)</b>
Standardized approach	347,150	-	237,528	3,093	587,771

## 6.0 Operational risk

The Bank defines operational risk as the risk of loss resulting from inadequate or failed processes, people, systems or external events. Operational risks are inherent in the Bank's operations and are typical of all banking and financial institutions. Operational risk management is a primary duty of the business units.

The operational risk management function is established as a department of the Risk Group that primarily coordinates the implementation and maintenance of the framework.

The Operational risk strategy for managing the effectiveness of the operational risk framework is as follows:

- Proactive approach through Risk & Control Self-Assessment process.
- Reactive approach through Loss & Events Data Collection, and Analysis.
- Maintaining culture and awareness programs.
- Introducing comprehensive monitoring and reporting tools.
- Developing supportive practices for managing Operational Risk exposures.

### 6.1 Operational Risk Framework

The main elements comprising the operational risk framework are:

- Governance
- Loss data collection
- Risk and control self-assessment
- Key risk indicators
- Stress testing & scenario analysis
- Monitoring and reporting

## 6.2 Operational Risk Assessment

### 6.2.1 Governance

The Board of Directors approves, monitors and reviews the operational risk appetite, framework, policies and practices; ensuring proper development, implementation and maintenance of a framework that is fully integrated into the bank's overall risk management processes.

Business Group Heads are actively involved in evaluating exposure to operational risks associated with their business through the Operational Risk Committee. A network of Divisional Operational Risk Managers (DORMs) within business units assists management with the monitoring and mitigation of operational risks. Material operational risks are addressed to the senior management of the individual business units, escalated to the Operational Risk department and to the ORC when necessary.

### 6.2.2 System and Loss Data Collection

The SAS Operational Risk Monitor is being used for collecting operational risk losses that occur within the bank. The tool is considered to be the industry's prime tool for operational risk losses collection. From this system, NCB is able to record and consider major operational risks/incidents and effectively determine the appropriate measures to mitigate and manage the exposure to these risks. Recorded events are rigorously monitored and analyzed for further escalation. As a result, a comprehensive loss data collection for managing, tracking and reporting risk information is effectively in place.

### 6.2.3 Risk and Control Self-Assessment [RCSA]

A qualitative and quantitative risk assessment is conducted within NCB using an identified universe of operational risks contained in the Risk & Control Self-Assessment Framework (RCSA). The assessment of risks and controls is conducted at the business unit level and is subject to treatment and escalation to Group Heads, which set out the operational risk exposure that NCB is willing to tolerate. In 2015, the Operational Risk department continued conducting the RCSA exercise across NCB covering core and support function divisions in order to ensure active comprehensive operational risk register for NCB is being held.

### 6.2.4 High level of awareness culture across NCB

Operational risk management continues the training programs (Internal & External) and encourages the participation of all staff, mainly those with functions that are assigned with roles and responsibilities that oversee operational risks within their respective areas. Operational Risk Awareness sessions were delivered to officers across the Kingdom.

### 6.2.5 Key Risk Indicator [KRI]

To ensure that NCB is compliant with Basel III requirements, the Operational Risk department uses its risk management and control system to provide a reliable and effective reporting mechanism. Key Risk Indicators (KRIs) are used as a monitoring tool to provide early warnings of operational problems or highlight failures. KRI reports that are generated by businesses are reviewed on a quarterly basis and monitored by the Operational Risk department for effective management.

### 6.3 Application of the standardized approach for Operational Risk

The Bank uses the Standardized Approach\* of Basel III to calculate the required Regulatory Capital as well as Economic Capital for operational risk. This approach requires banks to divide its activities into eight business lines: corporate finance, trading and sales, retail banking, commercial banking, payment and settlement, agency services, asset management, and retail brokerage. A range of beta coefficients (12%-18%) is then applied to the average gross income for the preceding three financial years for each of the eight business lines to calculate the required regulatory capital.

Following table gives the capital requirement for operational risk as of 31<sup>st</sup> of December 2015.

<b>CAPITAL ADEQUACY – Operational Risk (SAMA reference table 3)</b>	
<b>Capital Requirements for Operational Risk (Table 3, (e))</b>	
<b>Particulars</b>	<b>Capital requirement (SAR '000)</b>
Standardized approach	2,362,024
<b>Total</b>	<b>2,362,024</b>

\* Türkiye Finans Katılım Bankası A.Ş.(TFK) uses Basic Indicator Approach for their standalone Prudential. However, this is not impacting the computations at the group level.



## 7.0 Equities in Banking Book

The Bank's equity investments are intended to be held for an unspecified period of time, and may be sold in response to the Bank's needs. Quoted equity investments are valued based on market prices whereas unquoted equity investments are carried at cost. Impairment allowances, if required, are created in accordance with the accounting policies mentioned in note 3.14 of the *Audited Financial Statements for the year ended 31 December 2015*. The Bank does not actively trade these investments.

Following table gives the value of equity investments as of 31<sup>st</sup> of December 2015.

<b>EQUITIES: DISCLOSURES FOR BANKING BOOK POSITIONS (SAMA reference table 13)</b>					
<b>Value Of Investments (Table 13, (b))</b>					
	<b>Un-quoted investments</b>		<b>Quoted investments</b>		
	<b>Value disclosed in Financial Statements (SAR '000)</b>	<b>Fair value (SAR '000)</b>	<b>Value disclosed in Financial Statements (SAR '000)</b>	<b>Fair value (SAR '000)</b>	<b>Publicly quoted share values (if materially different from fair value) (SAR '000)</b>
Investments	471,748	N/A	806,928	806,928	N/A

Following table gives an industry sector breakdown of equity investments as of 31<sup>st</sup> of December 2015.

<b>EQUITIES: DISCLOSURES FOR BANKING BOOK POSITIONS (SAMA reference table 13)</b>		
<b>Types And Nature of Investments (Table 13, (c))</b>		
<b>Investments</b>	<b>Publicly traded (SAR '000)</b>	<b>Privately held (SAR '000)</b>
Government and quasi government		
Banks and other financial institutions	806,928	83,459
Agriculture and fishing		
Manufacturing		11,050
Mining and quarrying		
Electricity, water, gas and health services		
Building and construction		
Commerce		367,802
Transportation and communication		
Services		9,438
Others		
<b>Total</b>	<b>806,928</b>	<b>471,749</b>

Following table gives the realized and unrealized gains on equity investments as of 31<sup>st</sup> of December 2015.

<b>EQUITIES: DISCLOSURES FOR BANKING BOOK POSITIONS (SAMA reference table 13)</b>	
<b>Gains / Losses Etc. (Table 13, (d) and (e))</b>	
<b>Particulars</b>	<b>Amount (SAR '000)</b>
Cumulative realized gains (losses) arising from sales and liquidations in the reporting period	24,612
Total unrealized gains (losses)	656,294
Total latent revaluation gains (losses)	
Unrealized gains (losses) included in Capital	656,294
Latent revaluation gains (losses) included in Capital	

Following table gives an industry sector breakdown of capital requirements on equity investments as of 31<sup>st</sup> of December 2015.

<b>EQUITIES: DISCLOSURES FOR BANKING BOOK POSITIONS (SAMA reference table 13)</b>	
<b>Capital Requirements (Table 13, (f))</b>	
<b>Equity grouping</b>	<b>Capital requirements (SAR '000)</b>
Government and quasi government	
Banks and other financial institutions	79,917
Agriculture and fishing	
Manufacturing	884
Mining and quarrying	
Electricity, water, gas and health services	
Building and construction	
Commerce	29,424
Transportation and communication	
Services	1,768
Others	
<b>Total</b>	<b>111,993</b>

## 8.0 Interest Rate Risk in Banking Book

An explanation of the nature of Interest Rate Risk in the Banking Book, the Bank's processes to monitor and manage this risk and a sensitivity analysis is given in the note 33.2.1 of the *Audited Financial Statements for the year ended 31 December 2015*.

Following table gives the impact of a 200 basis points change in interest rates on the bank's earnings by major currencies based on outstanding position as of 31<sup>st</sup> December 2015.

<b>INTEREST RATE RISK IN THE BANKING BOOK (IRRBB) (SAMA reference table 14)</b>	
<b>200bp Interest Rate Shocks for currencies with more than 5% of Assets or Liabilities (Table 14, (b))</b>	
<b>Rate Shocks</b>	<b>Change in earnings (SAR '000)</b>
<b>Upward rate shocks:</b>	
SAR	1,745,780
USD	320,960
<b>Downward rate shocks:</b>	
SAR	(1,745,780)
USD	(320,960)

**Summary of Pillar 3 Qualitative disclosure requirements.**

Reference	Description	Section	Page
Table 1	Scope of Application	1.0	1
Table 2	Capital Structure	2.0	4
Table 3	Capital Adequacy	3.0	13
Risk Exposure and Assessment	General Qualitative Disclosure Requirements	4.1 – 4.5, 5.1 – 5.5, 6.1 – 6.2, 7.0 & 8.0	17-25 32-34 35-37 39-43
Risk Exposure and Assessment	Credit Risk	4.3, 4.4& 4.6	18, 22, 25
Table 4	Credit Risk: General Disclosures for All Banks	4.5	22
Table 5	Credit Risk: Disclosures for Portfolios Subject to the Standardized Approach and Supervisory Risk Weights in the IRB Approaches	4.8	29
Table 6	Credit Risk: Disclosures for Portfolios Subject to IRB Approaches	Not Applicable	
Table 7	Credit Risk Mitigation : Disclosures for Standardized and IRB Approaches	4.7	27
Table 8	General Disclosure for Exposure Related To Counterparty Credit Risk	4.9	29
Table 9	Securitization : Disclosure For Standardized and IRB Approaches	4.10	31
Table 10	Market Risk : Disclosure For Banks Using the Standardized Approaches	5.6	34
Table 11	Market Risk : Disclosures For Banks Using the Internal Models Approach (IMA) for Trading Portfolios	Not Applicable	
Table 12	Operational Risk	6.1 – 6.3	35-38
Table 13	Equities : Disclosures for Banking Book Positions	7.0	39-42
Table 14	Interest Rate Risk in the Banking Book (IRRBB)	8.0	43

**Summary of Pillar 3 Quantitative disclosure requirements.**

Reference	Description	Section	Page
Table 1, (e)	Capital Deficiencies (for subsidiaries not consolidated)	1.2	1
Table 2, (b)	Capital Structure	2.0	5
Table 2, (c)	Capital Structure	2.0	6
Table 2, (d) i	Capital Structure	2.0	7
Table 2, (d) ii	Capital Structure	2.0	8
Table 2, (e)	Capital Structure	2.0	9-12
Table 3, (b)	Amount of Exposures Subject to Standardized Approach of Credit Risk and related Capital Requirements	4.0	15
Table 3, (d)	Capital Requirements for Market Risk	5.6	34
Table 3, (e)	Capital Requirements for Operational Risk	6.3	38
Table 3, (f)	Capital Adequacy Ratio	3.0	14
Table 4, (b)	Credit Risk Exposures - Standardized Approach (STA)	4.0	16
Table 4, (c)	Geographical Breakdown – STA	4.3	19
Table 4, (d)	Industry Sector Breakdown – STA	4.3	20
Table 4, (e)	Residual Contractual Maturity Breakdown – STA	4.3	21
Table 4, (f)	Impaired Loans, Past Due Loans and Allowances – STA (Industry Sector)	4.5	23
Table 4, (g)	Impaired Loans, Past Due Loans and Allowances – STA (Geographical)	4.5	24
Table 4, (h)	Reconciliation of Changes in the Allowances for Loan Impairment	4.5	25
Table 5, (b)	Allocation of Exposures to Risk Buckets - STA	4.6	26
Table 7, (b) and (c)	Credit Risk Exposures Covered by CRM (Collateral) - STA	4.7	28
Table 8, (b) and (d)	General Disclosures (for exposure related to counterparty credit risk)	4.9	30
Table 10, (b)	Level of Market Risk in Terms of Capital Requirements	5.6	34
Table 13, (b)	Equities : Value of Investments	7.0	39
Table 13, (c)	Equities : Types and Nature of Investments	7.0	40
Table 13, (d) and (e)	Equities : Gains/Losses etc.	7.0	41
Table 13, (f)	Equities : Capital Requirements	7.0	42
Table 14, (b)	200 bps Interest Rate Shocks for currencies with more than 5% of Assets or Liabilities	8.0	43