

NCB Board of Directors' Report for the Year 2012

Economic Environment

The Saudi economy maintained its robust trend during 2012, with real GDP registering 6.8 percent growth – driven by the oil sector, which grew 5.5 percent, and 7.2 percent growth in the non-oil sector. Private sector GDP remained strong, rising by 7.5 percent on the back of broad-based activity in the non-oil industrial, construction, and transportation sectors.

Oil prices ended the year at relatively high levels, although the economic difficulties of the Eurozone, lower growth rates in China, and OPEC's increased production have limited the upside potential. Saudi Arabian light crude averaged \$110 a barrel in 2012, just 2.0 percent more than in 2011. European Union sanctions on Iranian crude exports that began in July enabled Saudi Arabia (as a swing producer) to maintain its daily production at a 30-year high, with output rising by 7.6 percent in 2012 and averaging 9.95 million barrels per day.

The higher crude oil prices and output further boosted the Kingdom's current and fiscal account surpluses, which respectively stood at 24.5 percent and 14.2 percent of GDP. While government expenditure rose by 3.2 percent over 2011 to SR 853 billion, revenues grew by 10.9 percent to SR 1,239.5 billion. Consequently, the Kingdom's 2012 fiscal budget recorded a surplus of SR 386.5 billion.

Despite the surplus, fiscal prudence was evident in the sustained growth in government deposits at the Saudi Arabian Monetary Agency (SAMA), where the Kingdom's holdings of net foreign assets reached SR 2.4 trillion in 2012, a historical record that covers almost 59 months of imports. Meanwhile, government debt fell to SR 98.9 billion (all of it domestic) and, at 3.6 percent of GDP, the lowest in the world.

The Saudi Government is committed to pursuing its expansionary fiscal policy to diversify the economy and ensure sustainable growth. The 2013 budget continues to reflect the focus on long-term sustainable development that requires investment in physical infrastructure, education, healthcare, and social and economic projects. As expected, education and training continue to be central to this policy, receiving 24.9 percent of total allocations, with health accounting for 12.2 percent.

The Kingdom's strong external position, coupled with huge foreign reserves, will continue to underpin capital expenditure. On the execution side, the value of construction contracts awarded through the first three quarters of 2012 maintained 2011's momentum, reaching SR 166 billion compared to the record SR 179 billion awarded during the same period in 2011.

Alternative measures of finance for small and medium-size enterprises continue to gain ground. Kafala is the Government's loan guarantee program that provides direct financial support for SMEs, thereby stimulating job creation. In the first nine months of 2012, the Kafala program provided credit of about SR 1.3 billion to 646 companies, representing 24.5 percent of the total beneficiaries since the program began in 2006.

Business Review

As the Government's economic stimulus program took effect during 2012, triggering a surge in employment, NCB experienced a corresponding rise in new accounts being opened. The Bank was prepared for growth, with a widespread network and diverse channels, so it was able to secure a significant proportion of the new business arising from infrastructure projects and the trickle-down benefits for all market segments.

The value of investing in new branches and ATMs was clearly instrumental in the accompanying boost to NCB's market share. Two new branches increased the total to 290 Kingdom-wide, with 68 of these incorporating sections exclusively for ladies. 169 ATMs were added to the network, bringing the total to 1,960.

NCB's customer base now numbers more than 3.3 million, responsible for around 300 million transactions annually – 86 percent of which are conducted electronically, reflecting the 20 percent growth in online users during the year.

Our 28 *QuickPay* remittance centers served 700,000 customers. This has become another vital NCB channel, providing financial services to a previously under-served segment.

To help ensure that NCB holds true to its core values of giving customers the best possible service at all points of contact, in 2012 the Bank created the new position of Chief Customer Officer, whose mandate is to objectively monitor the experience of all NCB customers, in turn helping to identify priority areas for developing enhancement plans.

AlAhliMobile, the Bank's new smartphone and tablet app, was launched in 2012. Compatible with most Apple, Android, and Blackberry devices, the app allows customers to check their balances and account statements, as well as access to a wide range of services. A unique feature is card-less ATM cash withdrawals, providing emergency support when customers urgently need cash but do not have their ATM or debit card to hand.

NCB's residential finance portfolio rapidly expanded in 2012. But the growth in lending was not confined to home finance – the higher levels of employment led to rapid growth in all types of personal finance.

At the smaller end of the corporate scale, NCB leads the way in SMEs. The Bank has been the largest lender through the Government's Kafala loan guarantee program, providing some 30 percent of the total Kafala funds to more than 4,000 companies.

Many large corporate customers also turned to NCB, whether for major projects, financing imports, working capital for SME operations or, reflecting the employment trend, payroll lending.

NCB led two Shariah-compliant aircraft finance deals and secured mandates for projects such as the Prince Mohammad Bin Abdulaziz Airport in Madinah – at \$1.3 billion, the world's first large project finance transaction to be entirely structured as a Shariah-compliant private-public partnership.

It is also Saudi Arabia's first full airport privatization. As the Islamic structuring bank, NCB led the project finance for senior debt and an equity bridge loan. The new terminal will have annual capacity to handle eight million passengers when operational in 2015 and the operating rights have been awarded to a private consortium for 25 years.

NCB Capital, the group's wealth management business, established global strategic alliances with the Trust Company of the West and Amundi in 2012. These alliances will create one of the largest and most diversified Shariah fund platforms in the world. NCB Capital also became the first Saudi asset manager to launch Shariah-compliant funds on a new UCITS platform, registered in Ireland, a significant innovation that will boost international investor access to the Kingdom.

Türkiye Finans Katılım Bankası, the leading Turkish participation bank that is majority owned by NCB, recorded exceptional results in 2012. Lending grew by 27 percent, deposits by 21 percent, and revenue increased by 38 percent. Asset quality and the ratio of non-performing loans continued to be very positive. With 38 new branches opened during the year, taking the total to 220, Türkiye Finans now employs about 4,000 staff and is well set for further growth.

NCB's overall IT efficiency improved significantly during 2012, with 4,200 new devices installed as part of an upgrading program for the branch communications network. This contributed to a reduction in communication outages in branches and the halving of IT incidents, as well as boosting ATM services availability.

NCB's new partnership with IBM and ITC Infotech in India has created offshore IT capacity, enabling further enhancements to systems and increasing the existing development and testing resource capability. Further investment was also made in information security capability.

NCB continues to gather awards, being named Best Bank in Saudi Arabia in 2012 by *The Banker magazine*, and Best Islamic Bank by *Global Finance*. The Bank also received a number of Islamic mutual fund awards, including Best Islamic Asset Management Company in the Middle East from *Islamic Finance News*, and a broader industry award, Best Wealth Manager from *The Banker Middle East*.

The Bank's Corporate Social Responsibility activities have four distinct pillars: job creation, education, health, and social welfare. Activity continued in all four areas during 2012, particularly the Entrepreneurs Support schemes – the 'NCB Start-Up Award' and 'Financing Small Projects' – which flow naturally from the Bank's commitment to fostering the SME sector.

These efforts were recognized by the 2012 award for 'Best Bank Supporting SMEs in the Arab World', presented at the Mohammed Bin Rashid Awards for Young Business Leaders, held in Dubai in conjunction with the Global Entrepreneurship Summit.

Sustainability is now an integral part of NCB's corporate philosophy, not only applicable to the Bank's own operations but increasingly leading by example. Response to the Bank's pioneering sustainability initiatives is increasing, and will continue to gather momentum as the Bank adopts and implements ambitious new plans.

For example, NCB's 2011-15 Environmental Plan – which cites specific targets for saving electricity, water, and paper – has already improved the energy efficiency of the Bank's operations: emphasizing water conservation, energy and emission reduction, minimizing waste, and adopting sustainable methods and materials in the design of new buildings. Further advances are planned for 2013, when NCB will apply a range of electricity-saving measures across its branch network.

Employees

NCB hired 1,831 new employees in 2012. At the year-end, NCB had 6,619, full-time staff, up from 5,879 in 2011, and it achieved a Saudization rate of 92.1 percent. NCB is a leader in the recruitment and development of Saudis, not only in the banking sector but among all private sector organizations.

The Bank has a number of associate programs to give recent college graduates 4-6 months of intensive training and work experience. More than 75 young Saudis undertook these programs in 2012 and most of them went on to become permanent NCB employees. A new version of the Management Associate Program (MAP) was launched to accelerate the development of staff working within the consumer lending area.

Financial Results

With net income increasing by 7.3 percent to SR 6,453 million, 2012 was the best year in NCB's long history, eclipsing even the Bank's outstanding results in the period before the global economic crisis. The performance and achievements of 2012 reflect the effectiveness of NCB's strategy for optimally deploying its assets and diversifying revenue sources. The strength of the operational base that the Bank has built – and the customer support that has stemmed from this – has never been so evident.

Fee income from banking services increased by a remarkable 21 percent during the year, the result of across-the-board growth in all business segments. Foreign exchange income increased by 15 percent. Despite the prevailing low interest rates, net special commission income grew by 5 percent to SR 8,993 million. Operating costs increased by 11 percent to SR 5,263 million.

Shareholders' equity increased by 11 percent to SR 39 billion, and customer deposits by 14 percent to SR 274 billion. Total assets were up 15 percent to SR 345 billion. This increase was reflected in expanded lending activities, with the loan portfolio growing by 21 percent to SR 164 billion.

NCB continued to effectively manage credit risk, taking provisions in 2012 in accordance with its prudent provisioning methodology. As a result, its coverage ratio increased to 142.5 percent in 2012.

The Bank's return on equity was 17.9 percent in 2012 and its Pillar 1 capital adequacy ratio (Tiers 1 and 2) was 17.5 percent.

NCB also maintained its A+ rating from Standard & Poor's and Fitch Ratings. This is the highest rating given to any bank in Saudi Arabia and reflects NCB's financial strength and high liquidity levels, as well as its leading local and regional position.

Appropriation Of Net Income

The Board of Directors recommends that net income for the year 2012 attributable to equity holders of the Bank company be appropriated as follows:

	<u>SR millions</u>
Net Income for the year attributable to equity holders of the Bank	6,453
Net Income for the year attributable to equity holders of the Bank is appropriated as follows:	
Transfer to Statutory Reserve	1,518
Zakat	479
Interim paid Dividend (SR 0.8 per share)	1,197
Final proposed Dividend (SR 1.0 per share)	1,496
Transfer to Retained Earnings	1,763
Net Income for the year attributable to equity holders of the Bank	6,453

Directors' Remuneration

Annual remuneration of the Board of Directors and its related committees for the year totalled SR 11,840 thousand (2011: SR 8,473 thousand). Attendance fees for the Board and related committees totalled SR 708 thousand (2011: SR 486 thousand). Travel and related expenses were SR 164 thousand (2011: SR 142 thousand).

Auditors

At the annual ordinary general meeting of shareholders held on 31 March, 2012 (corresponding to 8 Jumada AlAwal H), KPMG Al Fozan & Al Sadhan and Ernst & Young were reappointed as joint external auditors to the Bank for the financial year ending December 31, 2012.

Gratitude

The Board of Directors humbly extends sincere appreciation to the Custodian of the Two Holy Mosques, King Abdullah Bin Abdulaziz Al Saud; Prince Salman Bin Abdulaziz Al Saud, Crown Prince, Deputy Premier and Minister of Defense; Prince Muqrin Bin Abdulaziz Al-Saud, Second Deputy Premier, Advisor and Special Envoy of the Custodian of the Two Holy Mosques; and all Government ministers. The Board also expresses its thanks to the Ministry of Finance, the Saudi Arabian Monetary Agency, and the Capital Market Authority for their unfailing support of the Saudi banking sector, a commitment that is clearly evident in the Kingdom's continued economic achievements.

The Board also gratefully acknowledges the role of NCB's shareholders, who consistently endorse the Bank's business strategies. Customer loyalty is one of NCB's strongest assets and a cornerstone of the Bank's continued success, so the Board once again takes great pleasure in declaring its heartfelt appreciation. Likewise, the Bank's employees represent an incomparable asset, and we pay tribute to the energy and enthusiasm that they display so consistently in executing their responsibilities.

May the peace, mercy, and blessings of Allah be upon you.

Board of Directors