



Deloitte & Touche  
Bakr Abulkhair & Co.

**AUDITORS' REPORT**

**TO: THE SHAREHOLDERS OF ARAB NATIONAL BANK  
(SAUDI JOINT STOCK COMPANY)**

We have audited the balance sheet of Arab National Bank (the Bank) as of December 31, 2005 and the related statements of income, changes in shareholders' equity and cash flows for the year then ended, including the related notes. These financial statements are the responsibility of the Bank's management and have been prepared by them in accordance with the provisions of the Regulations for Companies and the Banking Control Law 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 an 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 at December 31, 2005 and the results of its operations and its cash flows for the year then ended in accordance with Accounting Standards for Financial Institutions issued by the Saudi Arabian Monetary Agency and with International Financial Reporting Standards, and
- comply with the requirements of the Regulations for Companies, the Banking Control Law and the Bank's Articles of Association in so far as they affect the preparation and presentation of financial statements.

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Riyadh: Dhul-Hijja 16, 1426H  
(January 16, 2006)

## Arab National Bank – Saudi Joint Stock Company

### BALANCE SHEET

As at December 31, 2005 and 2004

|   | Notes | 2005<br>SAR' 000  | 2004<br>SAR' 000  |
|---|-------|-------------------|-------------------|
| <b>ASSETS</b>                                     |       |                   |                   |
| Cash and balances with SAMA                       | 3     | 2,495,186         | 7,061,456         |
| Due from banks and other financial institutions   | 4     | 3,933,675         | 4,731,873         |
| Investments, net                                  | 5     | 20,422,650        | 21,187,466        |
| Loans and advances, net                           | 6     | 38,778,556        | 28,557,967        |
| Other real estate                                 |       | 158,865           | 191,899           |
| Fixed assets, net                                 | 7     | 418,108           | 382,415           |
| Other assets                                      | 8     | 1,285,039         | 1,211,967         |
| <b>Total assets</b>                               |       | <b>67,492,079</b> | <b>63,325,043</b> |
| <b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>       |       |                   |                   |
| <b>Liabilities</b>                                |       |                   |                   |
| Due to banks and other financial institutions     | 10    | 8,376,934         | 9,820,827         |
| Customer deposits                                 | 11    | 48,832,464        | 46,315,710        |
| Other liabilities                                 | 12    | 2,633,502         | 2,218,886         |
| Term Loan   | 13    | 1,312,500         | -                 |
| <b>Total liabilities</b>                          |       | <b>61,155,400</b> | <b>58,355,423</b> |
| <b>Shareholders' equity</b>                       |       |                   |                   |
| Share capital                                     | 14    | 2,500,000         | 2,000,000         |
| Statutory reserve                                 | 15    | 2,500,000         | 2,000,000         |
| General reserve                                   | 15    | 780,000           | 550,000           |
| Other reserves                                    | 16    | 217,690           | 226,759           |
| Retained earnings                                 |       | 64,242            | 17,659            |
| Proposed dividend                                 | 27    | 274,747           | 175,202           |
| <b>Total shareholders' equity</b>                 |       | <b>6,336,679</b>  | <b>4,969,620</b>  |
| <b>Total liabilities and shareholders' equity</b> |       | <b>67,492,079</b> | <b>63,325,043</b> |

The accompanying notes 1 to 40 form an integral part of these financial statements.

## Arab National Bank – Saudi Joint Stock Company

### STATEMENT OF INCOME

For the years ended December 31, 2005 and 2004

|  | Notes | 2005<br>SAR' 000               | 2004<br>SAR' 000               |
|--|-------|--------------------------------|--------------------------------|
| Special commission income                              | 18    | 3,445,180                      | 2,456,310                      |
| Special commission expense                             | 18    | <u>1,256,051</u>               | <u>570,032</u>                 |
| <b>Net special commission income</b>                   |       | <b>2,189,129</b>               | <b>1,886,278</b>               |
| Fees from banking services, net                        | 19    | 693,915                        | 422,207                        |
| Exchange income  |       | 113,956                        | 93,106                         |
| Income from FVIS financial instruments                 | 20    | 259                            | -                              |
| Trading income, net                                    | 21    | 17,614                         | 9,182                          |
| Dividend income  | 22    | 2,396                          | 1,140                          |
| Gains on non-trading investments, net                  | 23    | 90,670                         | 8,416                          |
| Other operating income                                 | 24    | <u>33,753</u>                  | <u>7,601</u>                   |
| <b>Total operating income</b>                          |       | <b><u>3,141,692</u></b>        | <b><u>2,427,930</u></b>        |
| Salaries and employee related expenses                 |       | 657,689                        | 568,857                        |
| Rent and premises related expenses                     |       | 62,146                         | 56,297                         |
| Depreciation and amortization                          | 7     | 75,544                         | 60,065                         |
| Other general and administrative expenses              |       | 251,339                        | 247,945                        |
| Provision for credit losses                            | 6     | 248,390                        | 321,221                        |
| Impairment of other financial assets                   |       | 18,750                         | 6,545                          |
| Other operating expenses                               | 25    | <u>202</u>                     | <u>199</u>                     |
| <b>Total operating expenses</b>                        |       | <b><u>1,314,060</u></b>        | <b><u>1,261,129</u></b>        |
| <b>Net income</b>                                      |       | <b><u><u>1,827,632</u></u></b> | <b><u><u>1,166,801</u></u></b> |
| <b>Earnings per share (Expressed in SAR per share)</b> | 26    | <b><u><u>36.55</u></u></b>     | <b><u><u>23.34</u></u></b>     |

The accompanying notes 1 to 40 form an integral part of these financial statements.

## Arab National Bank – Saudi Joint Stock Company

### STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY For the years ended December 31, 2005 and 2004

|   | Notes | Share capital<br>SAR' 000 | Statutory<br>reserve<br>SAR' 000 | General<br>reserve<br>SAR' 000 | Other<br>reserves<br>SAR' 000 | Retained<br>earnings<br>SAR' 000 | Proposed<br>dividend<br>SAR' 000 | Total<br>SAR' 000 |
|---|-------|---------------------------|----------------------------------|--------------------------------|-------------------------------|----------------------------------|----------------------------------|-------------------|
| <b>2005</b>   |       |                           |                                  |                                |                               |                                  |                                  |                   |
| Balance at beginning of the year, as adjusted             |       | 2,000,000                 | 2,000,000                        | 550,000                        | 226,759                       | 17,659                           | 175,202                          | 4,969,620         |
| Bonus share issue   | 15    | 500,000                   | -                                | (500,000)                      | -                             | -                                | -                                | -                 |
| Net income  |       | -                         | -                                | -                              | -                             | 1,827,632                        | -                                | 1,827,632         |
| Transfer to statutory reserve                             | 15    | -                         | 500,000                          | -                              | -                             | (500,000)                        | -                                | -                 |
| Transfer to general reserve                               | 15    | -                         | -                                | 730,000                        | -                             | (730,000)                        | -                                | -                 |
| Dividend paid   | 27    | -                         | -                                | -                              | -                             | (272,941)                        | (175,202)                        | (448,143)         |
| Proposed gross final dividend                             | 27    | -                         | -                                | -                              | -                             | (274,747)                        | 274,747                          | -                 |
| Net changes in fair value and cash flow hedges            | 16    | -                         | -                                | -                              | (9,069)                       | (3,361)                          | -                                | (12,430)          |
| <b>Balance at end of the year</b>                         |       | <b>2,500,000</b>          | <b>2,500,000</b>                 | <b>780,000</b>                 | <b>217,690</b>                | <b>64,242</b>                    | <b>274,747</b>                   | <b>6,336,679</b>  |
| <b>2004</b>   |       |                           |                                  |                                |                               |                                  |                                  |                   |
| Balance at beginning of the year, as previously reported  |       | 1,800,000                 | 1,800,000                        | 200,000                        | 170,728                       | 6,613                            | -                                | 3,977,341         |
| Adjustment arising from the application of revised IAS 10 | 2b    | -                         | -                                | -                              | -                             | -                                | 415,651                          | 415,651           |
| Balance at the beginning of the year, as adjusted         |       | 1,800,000                 | 1,800,000                        | 200,000                        | 170,728                       | 6,613                            | 415,651                          | 4,392,992         |
| Bonus share issue   | 15    | 200,000                   | -                                | (200,000)                      | -                             | -                                | -                                | -                 |
| Net income  |       | -                         | -                                | -                              | -                             | 1,166,801                        | -                                | 1,166,801         |
| Transfer to statutory reserve                             | 15    | -                         | 200,000                          | -                              | -                             | (200,000)                        | -                                | -                 |
| Transfer to general reserve                               | 15    | -                         | -                                | 550,000                        | -                             | (550,000)                        | -                                | -                 |
| Dividend paid   | 27    | -                         | -                                | -                              | -                             | (214,830)                        | (415,651)                        | (630,481)         |
| Proposed gross final dividend                             | 27    | -                         | -                                | -                              | -                             | (175,202)                        | 175,202                          | -                 |
| Net changes in fair value and cash flow hedges            | 16    | -                         | -                                | -                              | 56,031                        | (15,723)                         | -                                | 40,308            |
| <b>Balance at end of the year, as adjusted</b>            | 39    | <b>2,000,000</b>          | <b>2,000,000</b>                 | <b>550,000</b>                 | <b>226,759</b>                | <b>17,659</b>                    | <b>175,202</b>                   | <b>4,969,620</b>  |

The accompanying notes 1 to 40 form an integral part of these financial statements.

**Arab National Bank – Saudi Joint Stock Company**  
**STATEMENT OF CASH FLOWS**  
For the years ended December 31, 2005 and 2004

|   | Notes | 2005<br>SAR' 000   | 2004<br>SAR' 000 |
|---|-------|--------------------|------------------|
| <b>OPERATING ACTIVITIES</b>   |       |                    |                  |
| <b>Net income</b>   |       | <b>1,827,632</b>   | 1,166,801        |
| <b>Adjustments to reconcile net income to net cash (used in) from operating activities:</b> |       |                    |                  |
| Accretion of discounts on investments   |       | (15,931)           | (32,094)         |
| Gains on non-trading investments, net   |       | (90,670)           | (8,416)          |
| Depreciation and amortization   |       | 75,544             | 60,065           |
| (Gains) losses on disposal of fixed assets, net   |       | (1,151)            | 35               |
| Provision for credit losses   |       | 248,390            | 321,221          |
| Impairment of other financial assets  |       | 18,750             | 6,545            |
|   |       | <b>2,062,564</b>   | 1,514,157        |
| <b>Net (increase) decrease in operating assets:</b>   |       |                    |                  |
| Statutory deposit with SAMA   | 3     | (185,039)          | (370,172)        |
| Investments held for trading  |       | (14,092)           | (101,107)        |
| Loans and advances  |       | (10,456,303)       | (8,701,423)      |
| Other real estate   |       | 33,034             | 6,630            |
| Other assets  |       | (231,055)          | (257,409)        |
| <b>Net increase (decrease) in operating liabilities:</b>                                    |       |                    |                  |
| Due to banks and other financial institutions   |       | (1,443,893)        | 712,258          |
| Customer deposits   |       | 2,513,257          | 12,592,346       |
| Other liabilities   |       | 564,747            | 463,365          |
| <b>Net cash (used in) from operating activities</b>   |       | <b>(7,156,780)</b> | 5,858,645        |
| <b>INVESTING ACTIVITIES</b>   |       |                    |                  |
| Proceeds from sale of and matured non-trading investments                                   |       | 6,483,432          | 2,128,306        |
| Purchase of non trading investments   |       | (5,607,313)        | (1,695,979)      |
| Purchase of fixed assets  |       | (119,256)          | (138,489)        |
| Proceeds from sale of fixed assets  |       | 9,170              | 15,282           |
| <b>Net cash from investing activities</b>   |       | <b>766,033</b>     | 309,120          |
| <b>FINANCING ACTIVITIES</b>   |       |                    |                  |
| Term loan   | 13    | 1,312,500          | -                |
| Dividends paid  |       | (471,260)          | (617,124)        |
| <b>Net cash from (used in) financing activities</b>   |       | <b>841,240</b>     | (617,124)        |
| <b>(Decrease) increase in cash and cash equivalents</b>                                     |       | <b>(5,549,507)</b> | 5,550,641        |
| <b>Cash and cash equivalents at the beginning of the year</b>                               |       | <b>10,187,697</b>  | 4,637,056        |
| <b>Cash and cash equivalents at the end of the year</b>                                     | 28    | <b>4,638,190</b>   | 10,187,697       |
| <b>Supplemental non-cash information</b>  |       |                    |                  |
| Net changes in fair value and cash flow hedges  |       | (12,430)           | 40,308           |

The accompanying notes 1 to 40 form an integral part of these financial statements.

# Arab National Bank – Saudi Joint Stock Company

## NOTES TO THE FINANCIAL STATEMENTS

For the years ended December 31, 2005 and 2004

(Saudi Riyals in Thousands)

### 1. General

Arab National Bank (a Saudi Joint Stock Company, the Bank) was formed pursuant to Royal Decree No. M/38 dated Rajab 18,1399H (June 13, 1979). The Bank commenced business on February 2, 1980 by taking over the operations of Arab Bank Limited in the Kingdom of Saudi Arabia. The Bank operates under Commercial Registration No. 1010027912 dated Rabi Awal 1,1400H (January 19, 1980) through its 116 branches (2004: 114 branches) in the Kingdom of Saudi Arabia and one branch in the United Kingdom. The address of the Bank's head office is as follows:

Arab National Bank  
P.O. Box 56921  
Riyadh 11564  
Kingdom of Saudi Arabia

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

### 2. Summary of significant accounting policies

The significant accounting policies adopted in the preparation of these financial statements are set out below.

Except for the changes in accounting policies as detailed in note 2 (b) below, the accounting policies are consistent with those used in the previous year.

#### a) Basis of preparation

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

The financial statements are prepared under the historical cost convention as modified for the measurement at fair value of derivatives, available for sale and fair value through income statement (FVIS) financial instruments. The carrying values of recognized assets and liabilities that are hedged through fair value hedges, and otherwise carried at cost, are adjusted to record changes in fair values attributed to risks that are being hedged.

In the ordinary course of business, the Bank makes certain estimates and assumptions that affect the reported amounts of assets and liabilities within the next financial year. Estimates and judgments are continually evaluated and are based on historical experience and other factors, including obtaining professional advice and expectations of future events that are believed to be reasonable under the circumstances.

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

#### b) Change in accounting policies and reporting

The Bank has implemented the revised versions of International Accounting Standard (IAS) 32 Financial Instruments: Disclosure and Presentation and IAS 39 Financial Instruments: Recognition and Measurement and IAS 10 Events after the Balance Sheet Date effective January 1, 2005 with retrospective effect wherever applicable, with respect to the recognition, measurement and disclosure of financial instruments.

The revised IAS 39 has introduced a new classification "Fair Value through Income Statement (FVIS)" under which financial assets and liabilities, except for investments in equity instruments that do not have a quoted market price and whose fair value cannot be reliably measured, can be classified and carried at fair value with the changes in fair values recognized in the statement of income. This new classification includes financial assets and liabilities held for trading and items that are designated as FVIS at the time of initial recognition. Following initial recognition, transfers between the various classifications of financial assets or liabilities are not ordinarily permissible.

Upon the implementation of the revised IAS 32 and 39, the Bank was not required to reclassify any of its assets and liabilities.

In accordance with the revised IAS 10, the Bank has changed its reporting for proposed final dividend. Previously the Bank recognized final dividend proposed by the Bank's Board of Directors as a liability with a corresponding charge to retained earnings. The Bank no longer recognizes a liability for such proposed dividend until approved by the Bank's general assembly. This changes in reporting was applied retroactively to January 1, 2004.

**2. Summary of significant accounting policies (continued)**

**c) Trade date accounting**

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

**d) Derivative financial instruments and hedging**

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

Any changes in the fair value of derivatives that are held for trading purposes are taken directly to income. Derivatives held for trading also include those derivatives, which do not qualify for hedge accounting described below.

For the purpose of hedge accounting, hedges are classified into two categories: (a) fair value hedges which hedge the exposure to changes in the fair value of a recognized asset or liability and (b) cash flow hedges which hedge exposure to variability in cash flows that is either attributable to a particular risk associated with a recognized asset or liability or to a highly probable forecasted transaction that will affect the reported net gain or loss.

In order to qualify for hedge accounting, the hedge should be expected to be highly effective, i.e. the changes in fair value or cash flows of the hedging instrument should effectively offset corresponding changes in the hedged item, and should be reliably measurable. At inception of the hedge, the risk management objective and strategy is documented including the identification of the hedging instrument, the related hedged item, the nature of risk being hedged, and how the Bank will assess the effectiveness of the hedging relationship. Subsequently, the hedge is required to be assessed and determined to be an effective hedge on an ongoing basis.

In relation to fair value hedges which meet the criteria for hedge accounting, any gain or loss from remeasuring the hedging instruments to fair value is recognized immediately in the statement of income. The corresponding change in fair value of the hedged item is adjusted against the carrying amount of the hedged item and is recognized in the statement of income. Where the fair value hedge of a commission bearing financial instrument ceases to meet the criteria for hedge accounting, the adjustment in the carrying value is amortized to the statement of income over the remaining life of the instrument.

In relation to cash flow hedges which meet the criteria for hedge accounting, the portion of the gain or loss on the hedging instrument that is determined to be an effective hedge is recognized initially in other reserves under shareholders' equity and the ineffective portion, if any, is recognized in the statement of income. For cash flow hedges affecting future transactions, the gains or losses recognized in other reserves, are transferred to the statement of income in the same period in which the hedged transaction affects the statement of income. Where the hedged forecasted transaction results in the recognition of an asset or a liability, then at the time the asset or liability is recognized, the associated gains or losses that had previously been recognized in other reserves are included in the initial measurement of the acquisition and related costs of the asset or liability. For all other cash flow hedges, gains or losses recognized initially in other reserves are transferred to the statement of income in the period in which the hedged transaction impacts the statement of income.

Hedge accounting is discontinued when the hedging instrument is expired or sold, terminated or exercised, or no longer qualifies for hedge accounting, or the forecasted transaction is no longer expected to occur or the Bank revokes the designation. At that point of time, any cumulative gain or loss on the cash flow hedging instrument that was recognized in other reserves is retained in shareholders' equity until the forecasted transaction occurs. Where the hedged forecasted transaction is no longer expected to occur, the net cumulative gain or loss recognized in "other reserves" is transferred to the statement of income for the period.

**e) Foreign currencies**

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

Transactions in foreign currencies are translated into Saudi Arabian Riyals at the exchange rates prevailing at transaction dates. Monetary assets and liabilities at year end, denominated in foreign currencies, are translated into Saudi Arabian Riyals at the exchange rates prevailing at the balance sheet date. Foreign exchange gains or losses on translation of monetary assets and liabilities denominated in foreign currencies are recognized in the statement of income, except when deferred in equity as qualifying cash flow hedges and qualifying net investment hedges.

**2. Summary of significant accounting policies (continued)**

**f) Offsetting**

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

**g) Revenue recognition**

Special commission income and expense are recognized in the statement of income on the accrual basis and include premiums amortized and discounts accreted during the year. Fees and exchange income from banking services are recognized when contractually earned. Dividend income is recognized when declared. When the bank enters into a commission rate swap for hedging purpose, special commission income or expense of hedged items is adjusted by the net commission accrued on the swap.

**h) Sale and repurchase agreements**

Assets sold with a simultaneous commitment to repurchase at a specified future date (repos) continue to be recognized in the balance sheet and are measured in accordance with related accounting policies for financial assets held as FVIS, held at amortized cost, available for sale and held to maturity investments. The counter-party liability for amounts received under these agreements is included in “due to banks and other financial institutions” or “customers’ deposits”, as appropriate. The difference between sale and repurchase price is treated as special commission expense and accrued over the life of the repo agreement using the effective yield method. Assets purchased with a corresponding commitment to resell at a specified future date (reverse repo) are not recognized in the balance sheet, as the bank does not obtain control over the assets. Amounts paid under these agreements are included in “Cash and balances with SAMA”, “Due from banks and other financial institutions” or “Loans and advances”, as appropriate. The difference between purchase and resale price is treated as special commission income and accrued over the life of the reverse repo agreement using the effective yield method.

**i) Investments**

All investment securities are initially recognized at cost, being the fair value of the consideration given, including acquisition charges associated with the investment. Premiums are amortized and discounts accreted using the effective yield method and are taken to special commission income.

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

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

Following the initial recognition of the various classes of investment securities, the subsequent period-end reporting values are determined on the basis as set out in the following paragraphs.

**(i) Held at fair value through income statement (FVIS)**

Investments in this category are classified as either investment held for trading or those designated at fair value through income statement at inception. Investments are classified in this category if their fair value can be reliably measured and are acquired principally for the purpose of selling or repurchasing in short term (trading) or if designated as such by the management. After initial recognition, investments are measured at fair value and any change in the fair value is recognized in the statement of income for the period in which it arises. Transaction cost, if any, are not added to the fair value measurement at initial recognition of FVIS investments.

**(ii) Available for sale**

Available for sale investments are those designated as available for sale or are not classified in any of the other three investment categories. Investments, which are classified as “available for sale”, are subsequently measured at fair value. For an available-for-sale investment where the fair value has not been hedged, any gain or loss arising from a change in its fair value is recognized directly in “other reserves” under shareholders’ equity. On derecognition or impairment, the cumulative gain or loss previously reported as “cumulative changes in fair value” within equity, is included in the income statement for the year. Available-for-sale investments whose fair value cannot be reliably measured are carried at amortized cost less impairment.



**2. Summary of significant accounting policies (continued)**

**i) Investments (continued)**

**(iii) Held at amortized cost, other**

Securities with fixed or determinable payments that are not quoted in an active market, and are not held as available for sale are classified as Held at amortized cost, other. Held at amortized cost, other investments whose fair values have not been hedged are stated at amortized cost, less provision for impairment. Amortized cost is calculated by taking into account any discount or premium on acquisition. Any gain or loss is recognized in the statement of income when the investment is derecognized or impaired.

**(iv) Held to maturity**

Investments which have fixed or determinable payments and fixed maturity that the Bank has the positive intention and ability to hold to maturity other than those that meet the definition of held at amortized cost, other are classified as held to maturity. Held to maturity investments are subsequently measured at amortized cost, less provision for impairment in value. Amortized cost is calculated by taking into account any discount or premium on acquisition. Any gain or loss on such investments is recognized in the statement of income when the investment is derecognized or impaired.

Investments classified as held to maturity cannot ordinarily be sold or reclassified and cannot be designated as a hedged item with respect to commission rate or prepayment risk, reflecting the longer-term nature of these investments.

**j) Loans and advances**

All loans and advances are initially measured at cost, being the fair value of the consideration given.

Following the initial recognition of the various classes of loans and advances, the subsequent period-end reporting values are determined on the basis as set out in the following paragraphs

**(i) Held at amortized cost, other and held to maturity**

Loans and advances originated or acquired by the Bank that are not quoted in an active market for which fair value has not been hedged, and those that are to be held to maturity, are stated at cost less any amount written off and provisions for impairment.

**(ii) Available for sale**

Loans and advances classified as available for sale are subsequently measured at fair value. Any changes in fair value, other than those relating to hedged risks, are recognized directly in "other reserves" under shareholders' equity until these are derecognized or impaired, at which time the cumulative gain or loss previously recognized in shareholders' equity is included in the statement of income for the period.

A loan is classified as impaired when, in management's opinion, there has been deterioration in credit quality to the extent that there is no longer reasonable assurance of timely collection of the full amount of principal and special commission.

Provisions for credit losses, including those arising from sovereign risk exposures, are based upon the management's assessment of the adequacy of the provisions on a periodic basis. Such assessment takes into account the composition and volume of the loans and advances, the general economic conditions, and the collectibility of the outstanding loans and advances.

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

**k) Impairment of financial assets**

An assessment is made at each balance sheet date to determine whether there is objective evidence that a financial asset or group of financial assets may be impaired. If such evidence exists, the estimated recoverable amount of that asset is determined and any impairment loss, based on the net present value of future anticipated cash flows, is recognized for changes in its carrying amounts as follows:

- i) For financial assets at amortized cost, the carrying amount of the asset is adjusted either directly or through the use of an allowance account and the amount of the adjustment is included in the statement of income; and

**2. Summary of significant accounting policies (continued)**

**k) Impairment of financial assets (continued)**

- ii) For financial assets at fair value, where a loss has been recognized directly under shareholders' equity as a result of the write-down of the asset to recoverable amount, the cumulative net loss recognized in shareholders' equity is transferred to the statement of income.
- iii) For assets carried at cost, impairment is the difference between carrying amount of the asset and the present value of expected future cash flows discounted at the original rate of return. The carrying amount of the asset is adjusted either directly or through the use of an allowance account and the amount of the adjustment is included in the statement of income.

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

The Bank reviews its problem loans and advances on a quarterly basis to assess whether a provision for impairment should be recorded in the income statement. In particular, considerable judgment by management is required in the estimation of the amount and timing of future cash flows when determining the level of provisions required. Such estimates are necessarily based on assumptions about several factors involving varying degrees of judgment and uncertainty, and actual results may differ resulting in future changes to such provisions.

In addition to specific provisions against individually significant loans and advances (and investment in debt instruments), the Bank also makes a collective impairment provision against loans and advances (and investment in debt instruments) which although not specifically identified as requiring a specific provision have a greater risk of default than when originally granted. This collective provision is based on any deterioration in the internal grade of the loan (or the internal/external grade of the investment) since it was granted (acquired). The amount of the provision is based on the historical loss pattern for loans (and investments) within each grade and is adjusted to reflect current economic changes.

These internal gradings take into consideration factors such as any deterioration in country risk, industry, as well as identified structural weaknesses or deterioration in cash flows.

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

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

**l) Other real estate**

The Bank, in the ordinary course of business, acquires certain real estate against settlement of due loans and advances. Such real estate is stated at the lower of carrying value of due loans and advances and the current fair value of the related properties.

Properties are revalued on a periodic basis and unrealized losses on revaluation and losses or gains on disposal are charged or credited to operating income or expense.

**m) Fixed assets**

Fixed assets are stated at cost and presented net of accumulated depreciation and amortization. Freehold land is not depreciated.

The cost of other fixed assets is depreciated and amortized on the straight-line method over the estimated useful lives of the assets as follows:

|                                   |   |
|-----------------------------------|---|
| Buildings                         | 33 years  |
| Leasehold improvements            | over lease period or 10 years, whichever is shorter |
| Furniture, equipment and vehicles | 2.5 to 5 years                                      |

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

**2. Summary of significant accounting policies (continued)**

**m) Fixed assets (continued)**

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

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

**n) Liabilities**

All money market deposits, placements and customer deposits are initially recognized at cost, being the fair value of the consideration received.

Subsequently all commission-bearing deposits and money market placements, other than those held at FVIS or where fair values have been hedged are measured at amortized cost. Amortized cost is calculated by taking into account any discount or premium on acquisition. Premiums are amortized and discounts accreted on a systematic basis to maturity and taken to special commission expense.

Financial liabilities classified as FVIS, if any, include (i) liabilities held for trading and (ii) liabilities designated as FVIS on initial recognition or on adoption of the revised IAS 39. After initial recognition, these liabilities are measured at fair value and the resulting gain or loss is included in the statement of income.

Deposits and money market placements in a fair value hedge relationship are adjusted for fair value changes to the extent of the risk being hedged. The resultant gain or loss is recognized in the statement of income. For deposits and money market placements carried at amortized cost, any gain or loss is recognized in the statement of income when derecognized or impaired.

**o) Provisions**

Provisions are recognized when the Bank has a present legal or constructive obligation as a result of past events; it is more likely than not that an outflow of resources will be required to settle the obligation; and the amount has been reliably estimated.

**p) Accounting for leases**

**i) Where the Bank is the lessee**

Leases entered into by the Bank are all operating leases. Payments made under operating leases are charged to the statement of income on a straight-line basis over the period of the lease.

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

**ii) Where the Bank is the lessor**

When assets are sold under a finance lease, including assets under Islamic lease the present value of the lease payments is recognized as a receivable and disclosed under "loans and advances". The difference between the gross receivable and the present value of the receivable is recognized as unearned finance income. Lease income is recognized over the term of the lease using the net investment method, which reflects a constant periodic rate of return.

**q) Cash and cash equivalents**

For the purpose of the statement of cash flows, "cash and cash equivalents" are defined as those amounts included in cash, balances with SAMA excluding statutory deposit, and due from banks and other financial institutions maturing within ninety days.

**r) Derecognition of financial instruments**

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

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

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

# Arab National Bank – Saudi Joint Stock Company

## NOTES TO THE FINANCIAL STATEMENTS

For the years ended December 31, 2005 and 2004

(Saudi Riyals in Thousands)

### 2. Summary of significant accounting policies (continued)

#### s) End of service benefits

Indemnities payable to employees of the Bank at the end of their services are provided for as required by the Saudi Arabian Labor Law using actuarial valuation. Provision for indemnities is included in other liabilities

#### t) Prospective changes in accounting policies

Certain new IFRS and amendments and interpretations to existing IFRS, have been published and are mandatory for the Bank's accounting period beginning on or after January 1, 2006 which the Bank has opted not to adopt earlier. These include:

IAS 39 - Fair Value Options (effective from January 1, 2006)

IFRIC IV - Determining whether an arrangement contains a lease (effective from January 1, 2006)

IFRS 7 - Financial Instrument Disclosure (effective from January 1, 2007)

Management anticipates the impact of these standards on its future financial reporting to be minimal.

### 3. Cash and balances with SAMA

|                           | <u>2005</u>             | <u>2004</u>             |
|---------------------------|-------------------------|-------------------------|
| Cash in hand              | 680,372                 | 421,300                 |
| Statutory deposit         | 1,790,671               | 1,605,632               |
| Special deposit with SAMA | -                       | 5,027,371               |
| Other balance             | 24,143                  | 7,153                   |
| <b>Total</b>              | <u><u>2,495,186</u></u> | <u><u>7,061,456</u></u> |

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

### 4. Due from banks and other financial institutions

|                         | <u>2005</u>             | <u>2004</u>             |
|-------------------------|-------------------------|-------------------------|
| Current accounts        | 476,498                 | 369,244                 |
| Money market placements | 3,457,177               | 4,362,629               |
| <b>Total</b>            | <u><u>3,933,675</u></u> | <u><u>4,731,873</u></u> |

### 5. Investments, net

#### a) Investment securities are classified as follows:

|   | Domestic              |                | International           |                  | Total                   |                  |
|---|-----------------------|----------------|-------------------------|------------------|-------------------------|------------------|
|   | <u>2005</u>           | 2004           | <u>2005</u>             | 2004             | <u>2005</u>             | 2004             |
| <b>i) Held as fair value through income statement</b> |                       |                |                         |                  |                         |                  |
| Other   | -                     | -              | 307,159                 | 199,059          | 307,159                 | 199,059          |
| <b>Held as fair value through income statement</b>    | <u>-</u>              | <u>-</u>       | <u>307,159</u>          | <u>199,059</u>   | <u>307,159</u>          | <u>199,059</u>   |
| <b>ii) Available for sale</b>                         |                       |                |                         |                  |                         |                  |
| Fixed rate securities                                 | 317,296               | 389,787        | 3,507,115               | 1,311,285        | 3,824,411               | 1,701,072        |
| Floating rate notes                                   | 59,999                | -              | 147,032                 | 301,414          | 207,031                 | 301,414          |
| Equities  | 4,516                 | 121,281        | -                       | -                | 4,516                   | 121,281          |
| Other   | 169,433               | 91,485         | 940,474                 | 743,981          | 1,109,907               | 835,466          |
| <b>Available for sale, net</b>                        | <u><u>551,244</u></u> | <u>602,553</u> | <u><u>4,594,621</u></u> | <u>2,356,680</u> | <u><u>5,145,865</u></u> | <u>2,959,233</u> |

**Arab National Bank – Saudi Joint Stock Company**

**NOTES TO THE FINANCIAL STATEMENTS**

For the years ended December 31, 2005 and 2004

(Saudi Riyals in Thousands)

**5. Investments, net (continued)**

|   | Domestic          |                   | International    |                  | Total             |                   |
|---|-------------------|-------------------|------------------|------------------|-------------------|-------------------|
|   | 2005              | 2004              | 2005             | 2004             | 2005              | 2004              |
| <b>iii) Held at amortized cost, other</b> |                   |                   |                  |                  |                   |                   |
| Fixed rate securities                     | 8,974,464         | 11,810,513        | 123,464          | 93,750           | 9,097,928         | 11,904,263        |
| Floating rate notes                       | 2,165,000         | 2,165,000         | 2,014,275        | 2,075,555        | 4,179,275         | 4,240,555         |
| Other                                     | -                 | -                 | 712,196          | -                | 712,196           | -                 |
| Held at amortized cost, other, gross      | 11,139,464        | 13,975,513        | 2,849,935        | 2,169,305        | 13,989,399        | 16,144,818        |
| Accumulated provision for impairment      | -                 | -                 | (18,750)         | -                | (18,750)          | -                 |
| <b>Held at amortized cost, other, net</b> | <b>11,139,464</b> | <b>13,975,513</b> | <b>2,831,185</b> | <b>2,169,305</b> | <b>13,970,649</b> | <b>16,144,818</b> |
| <b>iv) Held to maturity</b>               |                   |                   |                  |                  |                   |                   |
| Fixed rate securities                     | 998,977           | 1,884,356         | -                | -                | 998,977           | 1,884,356         |
| <b>Held to maturity, net</b>              | <b>998,977</b>    | <b>1,884,356</b>  | <b>-</b>         | <b>-</b>         | <b>998,977</b>    | <b>1,884,356</b>  |
| <b>Investments, net</b>                   | <b>12,689,685</b> | <b>16,462,422</b> | <b>7,732,965</b> | <b>4,725,044</b> | <b>20,422,650</b> | <b>21,187,466</b> |

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

|                                      | 2005             |                   |                   | 2004             |                   |                   |
|--------------------------------------|------------------|-------------------|-------------------|------------------|-------------------|-------------------|
|                                      | Quoted           | Unquoted          | Total             | Quoted           | Unquoted          | Total             |
| Fixed rate securities                | 1,838,783        | 12,082,533        | 13,921,316        | 1,253,399        | 14,236,292        | 15,489,691        |
| Floating rate notes                  | 83,933           | 5,014,569         | 5,098,502         | 149,086          | 4,392,883         | 4,541,969         |
| Equities                             | -                | 4,516             | 4,516             | 120,281          | 1,000             | 121,281           |
| Other                                | 19,880           | 1,397,186         | 1,417,066         | -                | 1,034,525         | 1,034,525         |
| Accumulated provision for impairment | -                | (18,750)          | (18,750)          | -                | -                 | -                 |
| <b>Investments, net</b>              | <b>1,942,596</b> | <b>18,480,054</b> | <b>20,422,650</b> | <b>1,522,766</b> | <b>19,664,700</b> | <b>21,187,466</b> |

Unquoted fixed and floating rate investments are mainly Saudi Government Development Bonds.

**c) The analysis of unrealized gains and losses and fair values of held at amortized cost, other, net of hedging, and held-to-maturity investments are as follows:**

|   | 2005              |                        |                         |                   | 2004              |                        |                         |                   |
|---|-------------------|------------------------|-------------------------|-------------------|-------------------|------------------------|-------------------------|-------------------|
|   | Carrying value    | Gross unrealized gains | Gross unrealized losses | Fair value        | Carrying value    | Gross unrealized gains | Gross unrealized losses | Fair value        |
| <b>i) Held at amortized cost, other</b> |                   |                        |                         |                   |                   |                        |                         |                   |
| Fixed rate securities                   | 9,068,214         | 117,555                | 69,989                  | 9,115,780         | 11,915,007        | 310,792                | 8,888                   | 12,216,911        |
| Floating rate notes                     | 4,921,185         | 5,747                  | 34,717                  | 4,892,215         | 4,240,555         | 5,160                  | 1,012                   | 4,244,703         |
| Accumulated provision for impairment    | (18,750)          | -                      | -                       | (18,750)          |                   |                        |                         |                   |
| <b>Total</b>                            | <b>13,970,649</b> | <b>123,302</b>         | <b>104,706</b>          | <b>13,989,245</b> | <b>16,155,562</b> | <b>315,952</b>         | <b>9,900</b>            | <b>16,461,614</b> |
| <b>ii) Held to maturity</b>             |                   |                        |                         |                   |                   |                        |                         |                   |
| Fixed rate securities                   | 998,977           | 42,157                 | 28                      | 1,041,106         | 1,884,356         | 99,523                 | -                       | 1,983,879         |
| <b>Total</b>                            | <b>998,977</b>    | <b>42,157</b>          | <b>28</b>               | <b>1,041,106</b>  | <b>1,884,356</b>  | <b>99,523</b>          | <b>-</b>                | <b>1,983,879</b>  |

# Arab National Bank – Saudi Joint Stock Company

## NOTES TO THE FINANCIAL STATEMENTS

For the years ended December 31, 2005 and 2004

(Saudi Riyals in Thousands)

### 5. Investments, net (continued)

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

|  | <u>2005</u>              | <u>2004</u>              |
|--|--------------------------|--------------------------|
| Government and quasi government        | 16,043,916               | 16,919,859               |
| Corporate                              | 222,708                  | 183,456                  |
| Banks and other financial institutions | 3,982,077                | 3,874,776                |
| Other                                  | 173,949                  | 209,375                  |
| <b>Total</b>                           | <b><u>20,422,650</u></b> | <b><u>21,187,466</u></b> |

Investments include SAR 6,140 million (2004: SAR 9,422 million), which have been pledged under repurchase agreements with other banks and customers. The market value of such investment is SAR 6,113 million (2004: SAR 9,629 million).

During 2005, an impairment charge of SAR 18.8 millions was computed on securities classified as "Held at amortized cost, other".

### 6. Loans and advances, net

#### a) Loans and advances are comprised of the following:

|  | <u>2005</u>              | <u>2004</u>              |
|--|--------------------------|--------------------------|
| Performing:                            |                          |                          |
| Overdrafts                             | 4,122,916                | 3,653,489                |
| Credit cards                           | 440,869                  | 156,285                  |
| Commercial loans                       | 19,795,679               | 16,331,057               |
| Consumer loans                         | 15,260,444               | 9,129,828                |
| Other                                  | 10,671                   | 14,843                   |
| Performing loans and advances, gross   | <u>39,630,579</u>        | <u>29,285,502</u>        |
| Non-performing loans and advances, net | 846,626                  | 890,233                  |
| <b>Total</b>                           | <b><u>40,477,205</u></b> | <b><u>30,175,735</u></b> |
| Provision for credit losses            | <u>(1,698,649)</u>       | <u>(1,617,768)</u>       |
| <b>Loans and advances, net</b>         | <b><u>38,778,556</u></b> | <b><u>28,557,967</u></b> |

Non-performing loans and advances are disclosed net of accumulated commission in suspense of SAR 471.9 million (2004: SAR 528.6) million.

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

|                                   | <u>2005</u>             | <u>2004</u>             |
|-----------------------------------|-------------------------|-------------------------|
| Balance at beginning of the year  | 1,617,768               | 1,387,803               |
| Provided during the year          | 248,390                 | 321,221                 |
| Bad debts written off             | (167,509)               | (91,256)                |
| <b>Balance at end of the year</b> | <b><u>1,698,649</u></b> | <b><u>1,617,768</u></b> |

Recoveries of loans and advances previously written off are included in other operating income (note 24).

# Arab National Bank – Saudi Joint Stock Company

## NOTES TO THE FINANCIAL STATEMENTS

For the years ended December 31, 2005 and 2004

(Saudi Riyals in Thousands)

### 6. Loans and advances, net (continued)

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

|  | <u>2005</u>              | <u>Non performing,<br/>net</u> | <u>Credit loss<br/>provision</u> | <u>Loans and<br/>advances, net</u> |
|--|--------------------------|--------------------------------|----------------------------------|------------------------------------|
|  | <u>Performing</u>        |                                |                                  |                                    |
| 1. Government and quasi government             | 69,643                   | -                              | -                                | 69,643                             |
| 2. Banks and other financial institutions      | 2,726,815                | -                              | -                                | 2,726,815                          |
| 3. Agriculture and fishing                     | 425,362                  | 7,371                          | (12,718)                         | 420,015                            |
| 4. Manufacturing                               | 4,910,616                | 227,400                        | (335,482)                        | 4,802,534                          |
| 5. Mining and quarrying                        | 40,140                   | 29                             | (201)                            | 39,968                             |
| 6. Electricity, water, gas and health services | 1,409,553                | -                              | -                                | 1,409,553                          |
| 7. Building and construction                   | 2,387,471                | 298,993                        | (234,547)                        | 2,451,917                          |
| 8. Commerce                                    | 4,541,275                | 172,758                        | (321,811)                        | 4,392,222                          |
| 9. Transportation and communication            | 917,271                  | 7,148                          | (10,724)                         | 913,695                            |
| 10. Services                                   | 639,921                  | 21,990                         | (24,080)                         | 637,831                            |
| 11. Consumer loans and credit cards            | 15,686,689               | 34,460                         | (32,467)                         | 15,688,682                         |
| 12. Other                                      | 5,875,823                | 76,477                         | (80,848)                         | 5,871,452                          |
|  | <u>39,630,579</u>        | <u>846,626</u>                 | <u>(1,052,878)</u>               | <u>39,424,327</u>                  |
| 13. Portfolio provision                        | -                        | -                              | (645,771)                        | (645,771)                          |
| <b>Total</b>                                   | <u><u>39,630,579</u></u> | <u><u>846,626</u></u>          | <u><u>(1,698,649)</u></u>        | <u><u>38,778,556</u></u>           |
|  | <u>2004</u>              |                                |                                  |                                    |
| 1. Government and quasi government             | 37,500                   | -                              | -                                | 37,500                             |
| 2. Banks and other financial institutions      | 3,205,130                | -                              | -                                | 3,205,130                          |
| 3. Agriculture and fishing                     | 319,554                  | 3,352                          | (9,059)                          | 313,847                            |
| 4. Manufacturing                               | 4,650,578                | 164,709                        | (151,797)                        | 4,663,490                          |
| 5. Mining and quarrying                        | 117,859                  | 29                             | (281)                            | 117,607                            |
| 6. Electricity, water, gas and health services | 785,885                  | -                              | -                                | 785,885                            |
| 7. Building and construction                   | 1,822,698                | 293,174                        | (226,691)                        | 1,889,181                          |
| 8. Commerce                                    | 3,329,318                | 190,327                        | (318,388)                        | 3,201,257                          |
| 9. Transportation and communication            | 820,889                  | 8,726                          | (15,541)                         | 814,074                            |
| 10. Services                                   | 510,340                  | 26,143                         | (32,698)                         | 503,785                            |
| 11. Consumer loans and credit cards            | 9,286,113                | 115,836                        | (122,294)                        | 9,279,655                          |
| 12. Other                                      | 4,399,638                | 87,937                         | (95,248)                         | 4,392,327                          |
|  | <u>29,285,502</u>        | <u>890,233</u>                 | <u>(971,997)</u>                 | <u>29,203,738</u>                  |
| 13. Portfolio provision                        | -                        | -                              | (645,771)                        | (645,771)                          |
| <b>Total</b>                                   | <u><u>29,285,502</u></u> | <u><u>890,233</u></u>          | <u><u>(1,617,768)</u></u>        | <u><u>28,557,967</u></u>           |

### 7. Fixed assets, net

|                                  | <u>Land and<br/>Buildings</u> | <u>Leasehold<br/>improve-<br/>ments</u> | <u>Equipment,<br/>furniture and<br/>vehicles</u> | <u>Total<br/>2005</u> | <u>Total<br/>2004</u> |
|----------------------------------|-------------------------------|---|--|-----------------------|-----------------------|
| <b>Cost</b>                      |                               |   |  |                       |                       |
| Balance at beginning of the year | 357,037                       | 178,865                                 | 410,133  | 946,035               | 867,577               |
| Additions                        | 19,027                        | 46,327                                  | 53,902   | 119,256               | 138,489               |
| Disposals                        | (22,701)                      | (275)                                   | (21,796)   | (44,772)              | (60,031)              |
| Balance at end of the year       | <u>353,363</u>                | <u>224,917</u>                          | <u>442,239</u>                                   | <u>1,020,519</u>      | 946,035               |
| <b>Accumulated depreciation</b>  |                               |   |  |                       |                       |
| Balance at beginning of the year | 133,218                       | 118,414                                 | 311,988  | 563,620               | 544,493               |
| Charge for the year              | 4,675                         | 18,680                                  | 52,189   | 75,544                | 60,065                |
| Disposals                        | (14,820)                      | (164)                                   | (21,769)   | (36,753)              | (40,938)              |
| Balance at end of the year       | <u>123,073</u>                | <u>136,930</u>                          | <u>342,408</u>                                   | <u>602,411</u>        | 563,620               |
| <b>Net book value</b>            |                               |   |  |                       |                       |
| <b>As at December 31, 2005</b>   | <u><u>230,290</u></u>         | <u><u>87,987</u></u>                    | <u><u>99,831</u></u>                             | <u><u>418,108</u></u> |                       |
| <b>As at December 31, 2004</b>   | <u><u>223,819</u></u>         | <u><u>60,451</u></u>                    | <u><u>98,145</u></u>                             |                       | 382,415               |

Fixed assets include work in progress as at December 31, 2005 amounting to SAR 87.7 million (2004: SAR 60.2 million). Equipment, furniture and vehicles include information technology related assets.

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### 8. Other assets

|  | <u>2005</u>             | <u>2004</u>             |
|--|-------------------------|-------------------------|
| Accrued special commission receivable - banks and other financial institutions | 1,526                   | 1,819                   |
| - investments  | 315,405                 | 364,310                 |
| - loans and advances   | 175,580                 | 68,155                  |
| - derivatives  | 88,880                  | 47,405                  |
| - other  | 115                     | 471                     |
| Total accrued special commission receivable                                    | <u>581,506</u>          | <u>482,160</u>          |
| Positive fair value of derivatives (note 9)                                    | 183,284                 | 313,951                 |
| Other  | 520,249                 | 415,856                 |
| <b>Total</b>   | <u><b>1,285,039</b></u> | <u><b>1,211,967</b></u> |

### 9. Derivatives

In the ordinary course of business, the Bank utilizes the following derivative financial instruments for both trading and hedging purposes:

#### a) Swaps

Swaps are commitments to exchange one set of cash flows for another. For commission rate swaps, counterparties generally exchange fixed and floating rate commission payments in a single currency without exchanging principal. For currency swaps, fixed commission payments and principal are exchanged in different currencies. For cross-currency commission rate swaps, principal, fixed and floating commission payments are exchanged in different currencies.

#### b) Forwards and futures

Forwards and futures are contractual agreements to either buy or sell a specified currency, commodity or financial instrument at a specified price and date in the future. Forwards are customized contracts transacted in the over-the-counter market. Foreign currency and commission rate futures are transacted in standardized amounts on regulated exchanges and changes in futures contract values are settled daily.

#### c) Forward rate agreements

Forward rate agreements are individually negotiated commission rate futures that call for a cash settlement for the difference between a contracted commission rate and the market rate on a specified future date, on a notional principal for an agreed period of time.

#### d) Options

Options are contractual agreements under which the seller (writer) grants the purchaser (holder) the right, but not the obligation, to either buy or sell at fixed future date or at any time during a specified period, a specified amount of a currency, commodity or financial instrument at a pre-determined price.

#### Held for trading purposes

Most of the Bank's derivative trading activities relate to sales, positioning and arbitrage. Sales activities involve offering products to customers and banks in order, inter alias, to enable them to transfer, modify or reduce current and future risks. Positioning involves managing market risk positions with the expectation of profiting from favorable movements in prices, rates or indices. Arbitrage involves identifying, with the expectation of profiting from price differentials between markets or products.

#### Held for hedging purposes

The Bank has adopted a comprehensive system for the measurement and management of risk. Part of the risk management process involves managing the Bank's exposure to fluctuations in foreign exchange and commission rates to reduce its exposure to currency and commission rate risks to acceptable levels as determined by the Board of Directors within the guidelines issued by SAMA.



# Arab National Bank – Saudi Joint Stock Company

## NOTES TO THE FINANCIAL STATEMENTS

For the years ended December 31, 2005 and 2004

(Saudi Riyals in Thousands)

### 9. Derivatives (continued)

The Board of Directors has established levels of currency risk by setting limits on counterparty and currency position exposures. Positions are monitored on a daily basis and hedging strategies are used to ensure positions are maintained within the established limits. The Board of Directors has established the level of commission rate risk by setting limits on commission rate gaps for stipulated periods. Asset and liability commission rate gaps are reviewed on a periodic basis and hedging strategies are used to reduce commission rate gap within the established limits.

As part of its asset and liability management the Bank uses derivatives for hedging purposes in order to adjust its exposure to currency and commission rate risks. This is generally achieved by hedging specific transactions as well as strategic hedging against overall balance sheet exposures. Strategic hedging, other than portfolio hedges for commission rate risk, do not qualify for special hedge accounting and related derivatives are accounted for as held for trading.

The Bank uses forward foreign exchange contracts and currency swaps to hedge against specifically identified currency risks. In addition, the Bank uses commission rate swaps and commission rate futures to hedge against the commission rate risk arising from specifically identified fixed commission-rate exposures.

The Bank also uses commission rate swaps to hedge against the cash flow risk arising on certain floating rate exposures. In all such cases, the hedging relationship and objective, including details of the hedged items and hedging instrument are formally documented and the transactions are accounted for as fair value or cash flow hedges.

The tables below show the positive and negative fair values of derivative financial instruments, together with the notional amounts, analyzed by the term to maturity and monthly average. The notional amounts, which provide an indication of the volumes of the transactions outstanding at the year-end, do not necessarily reflect the amounts of future cash flows involved. These notional amounts, therefore, are neither indicative of the Bank's exposure to credit risk, which is generally limited to the positive fair value of the derivatives, nor market risk.

#### Notional amounts by term to maturity

| Derivative financial instruments    |                     |                     |                       |                   |                   |                  |                  |                   |
|-------------------------------------|---------------------|---------------------|-----------------------|-------------------|-------------------|------------------|------------------|-------------------|
| <u>2005</u>                         | Positive fair value | Negative fair value | Notional amount total | Within 3 months   | 3-12 months       | 1-5 years        | Over 5 years     | Monthly average   |
| <b>Held for trading:</b>            |                     |                     |                       |                   |                   |                  |                  |                   |
| Commission rate swaps               | 14,091              | 10,707              | 5,176,395             | -                 | 1,050,000         | 3,343,200        | 783,195          | 3,299,734         |
| Commission rate futures and options | -                   | -                   | -                     | -                 | -                 | -                | -                | 67,923            |
| Forward foreign exchange contracts  | 124,933             | 65,865              | 13,944,716            | 8,257,741         | 5,326,795         | 360,180          | -                | 18,402,041        |
| Currency options                    | 25,373              | 24,811              | 997,809               | 594,094           | 403,715           | -                | -                | 2,940,211         |
| Other                               | 1,662               | 1,662               | 100,000               | -                 | -                 | 100,000          | -                | 100,000           |
| <b>Held as fair value hedges:</b>   |                     |                     |                       |                   |                   |                  |                  |                   |
| Commission rate swaps               | 15,544              | 35,540              | 11,367,588            | 4,405,324         | 3,012,028         | 2,044,405        | 1,905,831        | 5,846,189         |
| <b>Held as cash flow hedges:</b>    |                     |                     |                       |                   |                   |                  |                  |                   |
| Commission rate swaps               | 1,681               | 9,571               | 817,500               | -                 | 352,500           | 465,000          | -                | 795,417           |
| <b>Total</b>                        | <b>183,284</b>      | <b>148,156</b>      | <b>32,404,008</b>     | <b>13,257,159</b> | <b>10,145,038</b> | <b>6,312,785</b> | <b>2,689,026</b> | <b>31,451,515</b> |
| <br>                                |                     |                     |                       |                   |                   |                  |                  |                   |
| <u>2004</u>                         |                     |                     |                       |                   |                   |                  |                  |                   |
| <b>Held for trading:</b>            |                     |                     |                       |                   |                   |                  |                  |                   |
| Commission rate swaps               | 8,551               | 8,650               | 825,000               | -                 | 825,000           | -                | -                | 1,265,725         |
| Commission rate futures and options | -                   | -                   | 375,000               | -                 | 375,000           | -                | -                | 224,959           |
| Forward foreign exchange contracts  | 207,798             | 143,492             | 16,960,321            | 7,809,196         | 9,151,125         | -                | -                | 15,854,763        |
| Currency options                    | 42,086              | 38,247              | 5,511,724             | 2,854,422         | 2,657,302         | -                | -                | 7,172,032         |
| Other                               | 1,083               | 1,083               | 100,000               | -                 | -                 | 100,000          | -                | 68,335            |
| <b>Held as fair value hedges:</b>   |                     |                     |                       |                   |                   |                  |                  |                   |
| Commission rate swaps               | 36,669              | 44,971              | 5,369,494             | 350,000           | 1,276,623         | 3,742,871        | -                | 5,416,377         |
| <b>Held as cash flow hedges:</b>    |                     |                     |                       |                   |                   |                  |                  |                   |
| Commission rate swaps               | 17,764              | -                   | 552,500               | -                 | -                 | 552,500          | -                | 797,031           |
| <b>Total</b>                        | <b>313,951</b>      | <b>236,443</b>      | <b>29,694,039</b>     | <b>11,013,618</b> | <b>14,285,050</b> | <b>4,395,371</b> | <b>-</b>         | <b>30,799,222</b> |

# Arab National Bank – Saudi Joint Stock Company

## NOTES TO THE FINANCIAL STATEMENTS

For the years ended December 31, 2005 and 2004

(Saudi Riyals in Thousands)

### 9. Derivatives (continued)

The tables below show a summary of hedged items and portfolios, the nature of the risk being hedged, the hedging instrument and its fair value.

| Description of hedged items       | Fair value | Cost      | Risk       | Hedging instrument   | Positive fair value | Negative fair value |
|-----------------------------------|------------|-----------|------------|----------------------|---------------------|---------------------|
| <b>2005</b>                       |            |           |            |                      |                     |                     |
| Fixed commission rate investments | 1,060,939  | 1,039,218 | Fair value | Commission rate swap | 2,859               | 14,707              |
| Fixed commission rate loans       | 9,241,944  | 9,237,745 | Fair value | Commission rate swap | 12,685              | 16,884              |
| Fixed commission rate deposits    | 1,086,676  | 1,090,625 | Fair value | Commission rate swap | -                   | 3,949               |
| Floating commission rate loans    | 817,462    | 817,500   | Cash flow  | Commission rate swap | 1,681               | 9,571               |
| <b>2004</b>                       |            |           |            |                      |                     |                     |
| Fixed commission rate investments | 3,722,587  | 3,642,138 | Fair value | Commission rate swap | 27,340              | 44,519              |
| Fixed commission rate loans       | 1,537,934  | 1,528,606 | Fair value | Commission rate swap | 9,329               | -                   |
| Fixed commission rate deposits    | 198,298    | 198,750   | Fair value | Commission rate swap | -                   | 452                 |
| Floating commission rate loans    | 554,642    | 552,500   | Cash flow  | Commission rate swap | 17,764              | -                   |

Approximately 35% (2004: 52.4%) of the positive fair value of the Bank's derivatives are entered into with financial institutions and less than 7.2% (2004: 12.6%) of the positive fair value contracts are with any single counter-party at the balance sheet date. Derivative activities are mainly carried out under the Bank's treasury banking segment.

### 10. Due to banks and other financial institutions

|                       | 2005             | 2004             |
|-----------------------|------------------|------------------|
| Current accounts      | 120,573          | 228,130          |
| Money market deposits | 8,256,361        | 9,592,697        |
| <b>Total</b>          | <b>8,376,934</b> | <b>9,820,827</b> |

### 11. Customer deposits

|              | 2005              | 2004              |
|--------------|-------------------|-------------------|
| Demand       | 18,814,567        | 17,983,622        |
| Saving       | 96,120            | 128,111           |
| Time         | 28,322,891        | 26,857,412        |
| Other        | 1,598,886         | 1,346,565         |
| <b>Total</b> | <b>48,832,464</b> | <b>46,315,710</b> |

Time deposits include deposits against sales of securities of SAR 5,265 million (2004: SAR 9,261 million) with agreements to repurchase the same at fixed future dates. Other customer deposits include SAR 972 million (2004: SAR 917 million) of margins held for irrevocable commitments.

The above include foreign currency deposits as follows:

|              | 2005              | 2004              |
|--------------|-------------------|-------------------|
| Demand       | 683,340           | 598,721           |
| Saving       | 4,510             | 5,211             |
| Time         | 14,809,286        | 10,374,623        |
| Other        | 217,470           | 283,032           |
| <b>Total</b> | <b>15,714,606</b> | <b>11,261,587</b> |

# Arab National Bank – Saudi Joint Stock Company

## NOTES TO THE FINANCIAL STATEMENTS

For the years ended December 31, 2005 and 2004

(Saudi Riyals in Thousands)

### 12. Other liabilities

|   | <u>2005</u>      | <u>2004</u>      |
|---|------------------|------------------|
| Accrued special commission payable - banks and other financial institutoins | 32,534           | 31,571           |
| - customer deposits   | 139,575          | 101,402          |
| - derivatives   | 209,473          | 149,328          |
| - term loan   | 14,944           | -                |
| - other   | -                | 357              |
| <b>Total accrued special commission payable</b>                             | <u>396,526</u>   | <u>282,658</u>   |
| Negative fair value of derivatives (note 9)                                 | 148,156          | 236,443          |
| IPO Subscription  | 658,967          | 166,436          |
| Other   | 1,429,853        | 1,533,349        |
| <b>Total</b>  | <u>2,633,502</u> | <u>2,218,886</u> |

### 13. Term loan

On March 22, 2005, the Bank entered into a three year syndicate term loan facility agreement for an amount of USD 350 million for general banking purposes. The facility was drawn down in full on April 4, 2005 and is repayable in 2008. The Bank, however, has an option to effect an early repayment, subject to the terms and conditions of the related syndicate agreement.

### 14. Share capital

The authorized, issued and fully paid share capital of the Bank as at December 31, 2005 consists of 50 million shares of SAR 50 each (2004: 40 million). The ownership of the Bank's share capital is as follows:

|                        | <u>2005</u> | <u>2004</u> |
|------------------------|-------------|-------------|
| Saudi shareholders     | 60%         | 60%         |
| Arab Bank PLC – Jordan | 40%         | 40%         |

During the year ended December 31, 2005, ten million shares of SAR 50 each were issued after approval by the shareholders at their Extraordinary General Assembly meeting held on March 13, 2005 to increase the share capital of the bank from SAR 2,000 million to 2,500 million by transferring SAR 500 million from the general reserve through the issuance of one bonus share for every four shares held. Furthermore, during the year ended December 31, 2004, four million shares of SAR 50 each were issued after approval by the shareholders at their Extraordinary General Assembly meeting held on March 14, 2004 through the issuance of one bonus share for every nine shares held.

### 15. Statutory and general reserves

In accordance with Saudi Arabian Banking Control Law and the Articles of Association of the Bank, a minimum of 25% of the annual net income is required to be transferred to a statutory reserve until this reserve equals the paid up capital of the Bank. Accordingly, SAR 500 million has been transferred from 2005 net income (2004: SAR 200 million). The statutory reserve is not currently available for distribution.

Further to the bonus share issue (see note 14 above), SAR 500 million has been transferred from general reserve to share capital during 2005 (2004: SAR 200 million).

On December 18, 2005, the Board of Directors has approved a proposed transfer to general reserve amounting to SAR 730 million with the intention to increase the Bank's share capital through a three-for-ten bonus share dividend subject to a final approval of the Extraordinary General Assembly meeting.

# Arab National Bank – Saudi Joint Stock Company

## NOTES TO THE FINANCIAL STATEMENTS

For the years ended December 31, 2005 and 2004

(Saudi Riyals in Thousands)

### 16. Other reserves

|                                   | Cash flow<br>hedges | Available for<br>sale<br>investments | Total          |
|-----------------------------------|---------------------|--------------------------------------|----------------|
| <u>2005</u>                       |                     |                                      |                |
| Balance at beginning of the year  | 17,763              | 208,996                              | 226,759        |
| Net change in fair value          | (25,653)            | 103,893                              | 78,240         |
| Transfer to statement of income   | -                   | (87,309)                             | (87,309)       |
| Net movement during the year      | (25,653)            | 16,584                               | (9,069)        |
| <b>Balance at end of the year</b> | <b>(7,890)</b>      | <b>225,580</b>                       | <b>217,690</b> |
| <u>2004</u>                       |                     |                                      |                |
| Balance at beginning of the year  | 38,538              | 132,190                              | 170,728        |
| Net change in fair value          | (20,775)            | 66,322                               | 45,547         |
| Transfer to statement of income   | -                   | 10,484                               | 10,484         |
| Net movement during the year      | (20,775)            | 76,806                               | 56,031         |
| <b>Balance at end of the year</b> | <b>17,763</b>       | <b>208,996</b>                       | <b>226,759</b> |

### 17. Commitments and contingencies

#### a) Legal proceedings

As at December 31, 2005 there were legal proceedings of a routine nature outstanding against the Bank. No material provision has been made as related professional legal advice indicates that it is unlikely that any significant loss will event.

#### b) Credit related commitments and contingencies

The primary purpose of these instruments is to ensure that funds are available to customers as required.

Guarantee and standby letters of credit, which represent irrevocable assurances that the Bank will make payments in the event that a customer cannot meet its obligations to third parties, carry the same credit risk as loans and advances.

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

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

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

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

# Arab National Bank – Saudi Joint Stock Company

## NOTES TO THE FINANCIAL STATEMENTS

For the years ended December 31, 2005 and 2004

(Saudi Riyals in Thousands)

### 17. Commitments and contingencies (continued)

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

|  | <u>2005</u> | <u>Within 3<br/>months</u> | <u>3-12<br/>months</u> | <u>1-5<br/>years</u> | <u>Over 5<br/>years</u> | <u>Total</u>      |
|--|-------------|----------------------------|------------------------|----------------------|-------------------------|-------------------|
| Letters of credit                        |             | 1,416,283                  | 981,923                | 471,270              | -                       | 2,869,476         |
| Letters of guarantee                     |             | 2,285,306                  | 1,822,523              | 1,031,486            | 14,283                  | 5,153,598         |
| Acceptances                              |             | 576,313                    | 476,286                | 22,344               | -                       | 1,074,943         |
| Irrevocable commitments to extend credit |             | 182,616                    | 539,441                | 882,011              | 503,879                 | 2,107,947         |
| Other                                    |             | -                          | -                      | -                    | 439,236                 | 439,236           |
| <b>Total</b>                             |             | <u>4,460,518</u>           | <u>3,820,173</u>       | <u>2,407,111</u>     | <u>957,398</u>          | <u>11,645,200</u> |
|  | <u>2004</u> |                            |                        |                      |                         |                   |
| Letters of credit                        |             | 1,531,591                  | 399,440                | 144,636              | -                       | 2,075,667         |
| Letters of guarantee                     |             | 1,224,128                  | 1,904,650              | 1,008,925            | 7,122                   | 4,144,825         |
| Acceptances                              |             | 625,755                    | 89,584                 | 12,014               | 4,166                   | 731,519           |
| Irrevocable commitments to extend credit |             | -                          | 653,775                | 79,103               | 1,146,511               | 1,879,389         |
| Other                                    |             | -                          | -                      | -                    | 505,626                 | 505,626           |
| <b>Total</b>                             |             | <u>3,381,474</u>           | <u>3,047,449</u>       | <u>1,244,678</u>     | <u>1,663,425</u>        | <u>9,337,026</u>  |

The unutilized portion of non-firm commitments as at December 31, 2005, which can be revoked unilaterally at any time by the Bank, amounts to SAR 8,838 million (2004: SAR 6,722 million).

#### ii) The analysis of commitments and contingencies by counter-party is as follows:

|  | <u>2005</u>       | <u>2004</u>      |
|--|-------------------|------------------|
| Government and quasi government        | 159,008           | 1,498,530        |
| Corporate                              | 8,794,035         | 4,973,967        |
| Banks and other financial institutions | 1,716,957         | 1,105,060        |
| Other                                  | 975,200           | 1,759,469        |
| <b>Total</b>                           | <u>11,645,200</u> | <u>9,337,026</u> |

#### c) Assets pledged

Assets pledged as collateral with other financial institutions for security deposits are as follows:

|  | <u>2005</u>      |                                | <u>2004</u>      |                        |
|--|------------------|--------------------------------|------------------|------------------------|
|  | <u>Assets</u>    | <u>Related<br/>liabilities</u> | Assets           | Related<br>liabilities |
| Available for sale investments (note 5)            | 551,083          | 550,808                        | -                | -                      |
| Held at amortized cost, other investments (note 5) | 6,026,879        | 5,908,280                      | 9,421,581        | 8,866,270              |
| Held to maturity investments (note 5)              | 437,792          | 421,352                        | 441,709          | 488,697                |
| <b>Total</b>                                       | <u>7,015,754</u> | <u>6,880,440</u>               | <u>9,863,290</u> | <u>9,354,967</u>       |

#### d) Operating lease commitments

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

|                  | <u>2005</u>    | <u>2004</u>    |
|------------------|----------------|----------------|
| Less than 1 year | 48,795         | 37,912         |
| 1 to 5 years     | 131,491        | 82,103         |
| Over 5 years     | 89,979         | 46,931         |
| <b>Total</b>     | <u>270,265</u> | <u>166,946</u> |

# Arab National Bank – Saudi Joint Stock Company

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### 18. Net special commission income

#### Special commission income

|   | <u>2005</u>             | <u>2004</u>             |
|---|-------------------------|-------------------------|
| Investments - Available for sale                | 45,900                  | 25,577                  |
| - Held at amortized cost, other                 | 759,116                 | 742,590                 |
| - Held to maturity                              | 100,138                 | 136,426                 |
|   | <u>905,154</u>          | <u>904,593</u>          |
| Due from banks and other financial institutions | 90,120                  | 47,670                  |
| Loans and advances                              | 2,449,460               | 1,503,957               |
| Other   | 446                     | 90                      |
| <b>Total</b>                                    | <u><b>3,445,180</b></u> | <u><b>2,456,310</b></u> |

#### Special commission expense

|   |                         |                       |
|---|-------------------------|-----------------------|
| Due to banks and other financial institutions | 486,271                 | 260,089               |
| Customer deposits                             | 721,027                 | 309,943               |
| Term loan                                     | 48,753                  | -                     |
| <b>Total</b>                                  | <u><b>1,256,051</b></u> | <u><b>570,032</b></u> |

|                                      |                         |                         |
|--------------------------------------|-------------------------|-------------------------|
| <b>Net special commission income</b> | <u><b>2,189,129</b></u> | <u><b>1,886,278</b></u> |
|--------------------------------------|-------------------------|-------------------------|

### 19. Fees from banking services, net

|                       | <u>2005</u>           | <u>2004</u>           |
|-----------------------|-----------------------|-----------------------|
| Fee income            | 998,247               | 616,634               |
| Fee expense           | 304,332               | 194,427               |
| <b>Net fee income</b> | <u><b>693,915</b></u> | <u><b>422,207</b></u> |

### 20. Income from FVIS financial instruments

|  | <u>2005</u>       | <u>2004</u>     |
|--|-------------------|-----------------|
| Fair value change on financial assets and liabilities held as FVIS investments | 259               | -               |
| <b>Total</b>   | <u><b>259</b></u> | <u><b>-</b></u> |

### 21. Trading income, net

|                            | <u>2005</u>          | <u>2004</u>         |
|----------------------------|----------------------|---------------------|
| Derivatives                | 3,646                | 636                 |
| Other                      | 13,968               | 8,546               |
| <b>Trading income, net</b> | <u><b>17,614</b></u> | <u><b>9,182</b></u> |

### 22. Dividend income

|                                | <u>2005</u>         | <u>2004</u>         |
|--------------------------------|---------------------|---------------------|
| Available for sale investments | 2,396               | 1,140               |
| <b>Total</b>                   | <u><b>2,396</b></u> | <u><b>1,140</b></u> |

### 23. Gains on non-trading investments, net

|                               | <u>2005</u>          | <u>2004</u>         |
|-------------------------------|----------------------|---------------------|
| Available for sale            | 90,670               | 5,239               |
| Held at amortized cost, other | -                    | 3,177               |
| <b>Total</b>                  | <u><b>90,670</b></u> | <u><b>8,416</b></u> |

# Arab National Bank – Saudi Joint Stock Company

## NOTES TO THE FINANCIAL STATEMENTS

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### 24. Other operating income

|   | <u>2005</u>          | <u>2004</u>         |
|---|----------------------|---------------------|
| Gains on disposal of fixed assets                       | 1,286                | 137                 |
| Gains on disposal of other real estate                  | 1,569                | -                   |
| Recoveries of loans and advances previously written off | 27,851               | 3,634               |
| Other   | 3,047                | 3,830               |
| <b>Total</b>  | <b><u>33,753</u></b> | <b><u>7,601</u></b> |

### 25. Other operating expenses

|                                       | <u>2005</u>       | <u>2004</u>       |
|---------------------------------------|-------------------|-------------------|
| Loss on disposal of fixed assets      | 135               | 199               |
| Loss on disposal of other real estate | 67                | -                 |
| <b>Total</b>                          | <b><u>202</u></b> | <b><u>199</u></b> |

### 26. Earnings per share

Earnings per share is calculated by dividing the net income attributable to equity holders of the Bank by the weighted average number of ordinary shares in issue during the year.

No figure for diluted earnings per share has been presented as the Bank has not issued any instruments which would have an impact on earnings per share when exercised.

The calculations of earnings per share for 2004 have been adjusted retrospectively to reflect the impact of the bonus shares issued during 2005.

### 27. Gross dividend, Zakat and Income Tax

Gross dividend is comprised of the following :

|                                       | <u>2005</u>           | <u>2004</u>           |
|---------------------------------------|-----------------------|-----------------------|
| Interim dividend paid during the year | 272,941               | 214,830               |
| Proposed final dividend               | 274,747               | 175,202               |
| <b>Total</b>                          | <b><u>547,688</u></b> | <b><u>390,032</u></b> |

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

#### Zakat

Zakat attributable to Saudi Shareholders for the year amounted to approximately SAR 28.6 million (2004: SAR 18 million) which will be deducted from their share of dividend, resulting in a net dividend to Saudi Shareholders of SAR 10 per share (2004: SAR 9 per share).

#### Income Tax

Income tax payable by the non Saudi Shareholder on the current year's share of income is SAR 152.6 million (2004: SAR 142.3 million), which will be deducted from its share of dividend.

### 28. Cash and cash equivalents

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

|   | <u>2005</u>             | <u>2004</u>              |
|---|-------------------------|--------------------------|
| Cash and balances with SAMA excluding statutory deposit (note 3)            | 704,515                 | 5,455,824                |
| Due from banks and other financial institutions maturing within ninety days | 3,933,675               | 4,731,873                |
| <b>Total</b>  | <b><u>4,638,190</u></b> | <b><u>10,187,697</u></b> |

# Arab National Bank – Saudi Joint Stock Company

## NOTES TO THE FINANCIAL STATEMENTS

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### 29. Business segments

For management purpose the Bank is organized into the following major business segments:

#### Retail banking

Deposit, credit and investment product for individuals.

#### Corporate banking

Loans, deposits and other credit products for corporate and institutional customers, small to medium sized businesses and the London Branch.

#### Treasury banking

Manages the Bank's trading and investment portfolios and the Bank's liquidity, currency and commission rate risk.

Transactions between the business segments are reported as recorded in the Bank's transfer pricing system. Segment assets and liabilities comprise operating assets and liabilities, being the majority of the balance.

The Bank's primary business is conducted in the Kingdom of Saudi Arabia with one international branch. However, the total assets, liabilities, commitments and results of operations of this branch are not material to the Bank's overall financial statements.

- a) The Bank's total assets and liabilities as at December 31, 2005 and 2004, its total operating income, expenses and net income for the year then ended, by business segments, are as follows:

|                          | <u>Retail<br/>banking</u> | <u>Corporate<br/>banking</u> | <u>Treasury<br/>banking</u> | <u>Total</u> |
|--------------------------|---------------------------|------------------------------|-----------------------------|--------------|
| <u>2005</u>              |                           |                              |                             |              |
| Total assets             | 20,514,936                | 21,200,820                   | 25,776,323                  | 67,492,079   |
| Total liabilities        | 22,024,343                | 4,169,135                    | 34,961,922                  | 61,155,400   |
| Total operating income   | 2,281,752                 | 494,310                      | 365,630                     | 3,141,692    |
| Total operating expenses | 866,231                   | 372,836                      | 74,993                      | 1,314,060    |
| Net income               | 1,415,521                 | 121,474                      | 290,637                     | 1,827,632    |
| <u>2004</u>              |                           |                              |                             |              |
| Total assets             | 12,382,833                | 18,583,522                   | 32,358,688                  | 63,325,043   |
| Total liabilities        | 20,571,905                | 3,390,670                    | 34,392,848                  | 58,355,423   |
| Total operating income   | 1,718,803                 | 446,841                      | 262,286                     | 2,427,930    |
| Total operating expenses | 862,395                   | 342,365                      | 56,369                      | 1,261,129    |
| Net income               | 856,408                   | 104,476                      | 205,917                     | 1,166,801    |

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

|                              | <u>Retail<br/>banking</u> | <u>Corporate<br/>banking</u> | <u>Treasury<br/>banking</u> | <u>Total</u> |
|------------------------------|---------------------------|------------------------------|-----------------------------|--------------|
| <u>2005</u>                  |                           |                              |                             |              |
| Balance sheet assets         | 19,204,341                | 20,732,423                   | 25,012,932                  | 64,949,696   |
| Commitment and contingencies | 1,171,453                 | 4,327,776                    | -                           | 5,499,229    |
| Derivatives                  | -                         | 35,694                       | 507,633                     | 543,327      |
| <u>2004</u>                  |                           |                              |                             |              |
| Balance sheet assets         | 11,485,348                | 18,146,856                   | 31,485,258                  | 61,117,462   |
| Commitment and contingencies | 456,420                   | 3,955,153                    | -                           | 4,411,573    |
| Derivatives                  | -                         | 19,149                       | 569,353                     | 588,502      |

Credit exposure comprises the carrying value of balance sheet assets, excluding cash and balances with SAMA, fixed assets, other real estate, and other assets. The credit equivalent value of commitments, contingencies and derivatives are included in credit exposure.



### **30. Credit risk**

Credit risk is the risk that one party to a financial instrument will fail to discharge an obligation and will cause the other party to incur a financial loss. The Bank attempts to control credit risk by monitoring credit exposures, limiting transactions with specific counterparties, and continually assessing the creditworthiness of counterparties.

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

Concentrations of credit risk arise when a number of counterparties are engaged in similar business activities, or activities in the same geographic region, or have similar economic features that would cause their ability to meet contractual obligations to be similarly affected by changes in economic, political or other conditions.

Concentrations of credit risk indicate the relative sensitivity of the bank's performance to developments affecting a particular industry or geographical location.

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

The debt securities included in investment portfolio are mainly sovereign risk. Analysis of investments by counterparty is provided in note 5. For details of the composition of the loans and advances refer to note 6. Information on credit risk relating to derivative instruments is provided in note 9, and for commitments and contingencies in note 16.

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

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### 31. Geographical concentration

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

| <u>2005</u>  | Saudi<br>Arabia   | Other<br>GCC &<br>Middle<br>East | Europe           | North<br>America | Latin<br>America | South<br>East<br>Asia | Other<br>Countries | Total             |
|--|-------------------|----------------------------------|------------------|------------------|------------------|-----------------------|--------------------|-------------------|
| <b>Assets</b>  |                   |                                  |                  |                  |                  |                       |                    |                   |
| Cash and balances with SAMA                                  | 2,493,456         | -                                | 1,730            | -                | -                | -                     | -                  | 2,495,186         |
| Due from banks and other financial institutions              | 637,500           | 439,661                          | 2,624,143        | 152,290          | -                | 78,872                | 1,209              | 3,933,675         |
| Investments, net   | 12,629,584        | 351,389                          | 3,753,828        | 3,600,186        | -                | -                     | 87,663             | 20,422,650        |
| Loans and advances, net                                      | 37,508,070        | 1,106,038                        | 117,009          | -                | -                | -                     | 47,439             | 38,778,556        |
| <b>Total</b>   | <u>53,268,610</u> | <u>1,897,088</u>                 | <u>6,496,710</u> | <u>3,752,476</u> | <u>-</u>         | <u>78,872</u>         | <u>136,311</u>     | <u>65,630,067</u> |
| <b>Liabilities</b>   |                   |                                  |                  |                  |                  |                       |                    |                   |
| Due to banks and other financial institutions                | 1,717,000         | 4,293,952                        | 1,283,117        | 1,059,698        | -                | 20,579                | 2,588              | 8,376,934         |
| Customer deposits  | 48,443,376        | 186,120                          | 200,429          | 352              | -                | -                     | 2,187              | 48,832,464        |
| Term loan  | 296,250           | 461,250                          | 543,750          | 11,250           | -                | -                     | -                  | 1,312,500         |
| <b>Total</b>   | <u>50,456,626</u> | <u>4,941,322</u>                 | <u>2,027,296</u> | <u>1,071,300</u> | <u>-</u>         | <u>20,579</u>         | <u>4,775</u>       | <u>58,521,898</u> |
| <b>Commitments and contingencies</b>                         | <u>6,452,123</u>  | <u>862,415</u>                   | <u>2,192,244</u> | <u>514,422</u>   | <u>28,942</u>    | <u>1,502,039</u>      | <u>93,015</u>      | <u>11,645,200</u> |
| <b>Credit exposure (stated at credit equivalent amounts)</b> |                   |                                  |                  |                  |                  |                       |                    |                   |
| Commitments and contingencies                                | 3,163,568         | 434,038                          | 981,239          | 226,206          | 8,315            | 661,320               | 24,543             | 5,499,229         |
| Derivatives  | 393,927           | 5,497                            | 127,577          | 15,948           | -                | 378                   | -                  | 543,327           |
| <b>2004</b>  |                   |                                  |                  |                  |                  |                       |                    |                   |
| <b>Assets</b>  |                   |                                  |                  |                  |                  |                       |                    |                   |
| Cash and balances with SAMA                                  | 7,060,412         | -                                | 1,044            | -                | -                | -                     | -                  | 7,061,456         |
| Due from banks and other financial institutions              | 985,000           | 893,927                          | 2,522,820        | 108,507          | -                | 65,557                | 156,062            | 4,731,873         |
| Investments, net   | 16,462,422        | 430,829                          | 3,005,137        | 1,267,298        | -                | -                     | 21,780             | 21,187,466        |
| Loans and advances, net                                      | 26,319,919        | 1,811,746                        | 300,519          | -                | -                | -                     | 125,783            | 28,557,967        |
| <b>Total</b>   | <u>50,827,753</u> | <u>3,136,502</u>                 | <u>5,829,520</u> | <u>1,375,805</u> | <u>-</u>         | <u>65,557</u>         | <u>303,625</u>     | <u>61,538,762</u> |
| <b>Liabilities</b>   |                   |                                  |                  |                  |                  |                       |                    |                   |
| Due to banks and other financial institutions                | 5,059,056         | 3,388,234                        | 1,200,474        | 46,403           | -                | 12,016                | 114,644            | 9,820,827         |
| Customer deposits  | 45,888,022        | 246,455                          | 177,629          | 1,100            | -                | 717                   | 1,787              | 46,315,710        |
| <b>Total</b>   | <u>50,947,078</u> | <u>3,634,689</u>                 | <u>1,378,103</u> | <u>47,503</u>    | <u>-</u>         | <u>12,733</u>         | <u>116,431</u>     | <u>56,136,537</u> |
| <b>Commitments and contingencies</b>                         | <u>5,704,888</u>  | <u>833,347</u>                   | <u>1,292,629</u> | <u>583,032</u>   | <u>12,721</u>    | <u>811,161</u>        | <u>99,248</u>      | <u>9,337,026</u>  |
| <b>Credit exposure (stated at credit equivalent amounts)</b> |                   |                                  |                  |                  |                  |                       |                    |                   |
| Commitments and contingencies                                | 2,821,046         | 412,950                          | 558,775          | 194,800          | 3,636            | 370,800               | 49,566             | 4,411,573         |
| Derivatives  | 238,165           | 9,436                            | 253,397          | 85,254           | -                | 2,250                 | -                  | 588,502           |

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

|              | Non-performing<br>loans, net |                | Provision for<br>credit losses |                  |
|--------------|------------------------------|----------------|--------------------------------|------------------|
|              | 2005                         | 2004           | 2005                           | 2004             |
| Saudi Arabia | 846,626                      | 890,233        | 1,667,983                      | 1,587,234        |
| Europe       | -                            | -              | 30,666                         | 30,534           |
| <b>Total</b> | <u>846,626</u>               | <u>890,233</u> | <u>1,698,649</u>               | <u>1,617,768</u> |

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### 32. Currency risk

The Bank manages exposure to the effects of fluctuations in prevailing foreign currency exchange rates on its financial position and cash flows. The Board of Directors sets limits on the level of exposure by currency and in total for both overnight and intra-day positions, which are monitored daily. At the end of the year, the Bank had the following significant net exposures denominated in foreign currencies:

|                | Long   |         |
|----------------|--------|---------|
|                | 2005   | 2004    |
| US Dollar      | 96,140 | 692,299 |
| Euro           | 14     | 116     |
| Pound Sterling | 17     | 13,222  |
| Other          | 27,750 | 9,340   |

### 33. Commission rate risk

#### Commission sensitivity of assets, liabilities and off balance sheet items

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

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

| 2005  | Within 3 months    | 3-12 months        | 1-5 years          | Over 5 years       | Non-commission bearing | Total             | Effective commission rate |
|---|--------------------|--------------------|--------------------|--------------------|------------------------|-------------------|---------------------------|
| <b>Assets</b>                                     |                    |                    |                    |                    |                        |                   |                           |
| Cash and balances with SAMA                       | -                  | -                  | -                  | -                  | 2,495,186              | 2,495,186         | -                         |
| Due from banks and other financial institutions   | 3,457,177          | -                  | -                  | -                  | 476,498                | 3,933,675         | 3.79%                     |
| Investments, net                                  | 4,868,402          | 1,958,114          | 10,131,824         | 2,120,625          | 1,343,685              | 20,422,650        | 4.81%                     |
| Loans and advances, net                           | 16,157,432         | 8,790,459          | 8,537,489          | 5,293,176          | -                      | 38,778,556        | 8.05%                     |
| Other real estate                                 | -                  | -                  | -                  | -                  | 158,865                | 158,865           | -                         |
| Fixed assets, net                                 | -                  | -                  | -                  | -                  | 418,108                | 418,108           | -                         |
| Other assets                                      | -                  | -                  | -                  | -                  | 1,285,039              | 1,285,039         | -                         |
| <b>Total assets</b>                               | <u>24,483,011</u>  | <u>10,748,573</u>  | <u>18,669,313</u>  | <u>7,413,801</u>   | <u>6,177,381</u>       | <u>67,492,079</u> |                           |
| <b>Liabilities and shareholders' equity</b>       |                    |                    |                    |                    |                        |                   |                           |
| Due to banks and other financial institutions     | 7,067,612          | 1,188,750          | -                  | -                  | 120,572                | 8,376,934         | 4.40%                     |
| Customer deposits                                 | 23,451,548         | 5,287,484          | 583,183            | -                  | 19,510,249             | 48,832,464        | 3.13%                     |
| Other liabilities                                 | -                  | -                  | -                  | -                  | 2,633,502              | 2,633,502         | -                         |
| Term Loan   | -                  | 1,312,500          | -                  | -                  | -                      | 1,312,500         | 4.23%                     |
| Shareholders' equity                              | -                  | -                  | -                  | -                  | 6,336,679              | 6,336,679         | -                         |
| <b>Total Liabilities and shareholders' equity</b> | <u>30,519,160</u>  | <u>7,788,734</u>   | <u>583,183</u>     | <u>-</u>           | <u>28,601,002</u>      | <u>67,492,079</u> | <u>-</u>                  |
| <b>On balance sheet gap</b>                       | <u>(6,036,149)</u> | <u>2,959,839</u>   | <u>18,086,130</u>  | <u>7,413,801</u>   | <u>(22,423,621)</u>    |                   |                           |
| <b>Off balance sheet gap</b>                      | <u>4,581,475</u>   | <u>(1,230,755)</u> | <u>(1,444,889)</u> | <u>(1,905,831)</u> | <u>-</u>               |                   |                           |
| <b>Total commission rate sensitivity gap</b>      | <u>(1,454,674)</u> | <u>1,729,084</u>   | <u>16,641,241</u>  | <u>5,507,970</u>   | <u>(22,423,621)</u>    |                   |                           |
| <b>Cumulative commission rate sensitivity gap</b> | <u>(1,454,674)</u> | <u>274,410</u>     | <u>16,915,651</u>  | <u>22,423,621</u>  | <u>-</u>               |                   |                           |

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### 33. Commission rate risk (continued)

| <u>2004</u>                                       | <u>Within 3 months</u> | <u>3-12 months</u> | <u>1-5 years</u>  | <u>Over 5 years</u> | <u>Non commission bearing</u> | <u>Total</u>      | <u>Effective commission rate</u> |
|---|------------------------|--------------------|-------------------|---------------------|-------------------------------|-------------------|----------------------------------|
| <b>Assets</b>                                     |                        |                    |                   |                     |                               |                   |                                  |
| Cash and balances with SAMA                       | 5,027,371              | -                  | -                 | -                   | 2,034,085                     | 7,061,456         |                                  |
| Due from banks and other financial institutions   | 4,362,629              | -                  | -                 | -                   | 369,244                       | 4,731,873         | 2,18%                            |
| Investments, net                                  | 5,093,171              | 3,595,992          | 7,114,439         | 4,181,680           | 1,202,184                     | 21,187,466        | 4,55%                            |
| Loans and advances, net                           | 14,437,680             | 6,343,068          | 5,988,503         | 1,788,716           | -                             | 28,557,967        | 6.68%                            |
| Other real estate                                 | -                      | -                  | -                 | -                   | 191,899                       | 191,899           | -                                |
| Fixed assets, net                                 | -                      | -                  | -                 | -                   | 382,415                       | 382,415           | -                                |
| Other assets                                      | -                      | -                  | -                 | -                   | 1,211,967                     | 1,211,967         | -                                |
| <b>Total assets</b>                               | <u>28,920,851</u>      | <u>9,939,060</u>   | <u>13,102,942</u> | <u>5,970,396</u>    | <u>5,391,794</u>              | <u>63,325,043</u> | -                                |
| <b>Liabilities and shareholders' equity</b>       |                        |                    |                   |                     |                               |                   |                                  |
| Due to banks and other financial institutions     | 8,082,285              | 1,510,412          | -                 | -                   | 228,130                       | 9,820,827         | 2,41%                            |
| Customer deposits                                 | 19,554,817             | 7,195,868          | 971,397           | -                   | 18,593,628                    | 46,315,710        | 1,72%                            |
| Other liabilities                                 | -                      | -                  | -                 | -                   | 2,218,886                     | 2,218,886         | -                                |
| Shareholders' equity                              | -                      | -                  | -                 | -                   | 4,969,620                     | 4,969,620         | -                                |
| <b>Total Liabilities and shareholders' equity</b> | <u>27,637,102</u>      | <u>8,706,280</u>   | <u>971,397</u>    | <u>-</u>            | <u>26,010,264</u>             | <u>63,325,043</u> | -                                |
| On balance sheet gap                              | 1,283,749              | 1,232,780          | 12,131,545        | 5,970,396           | (20,618,470)                  |                   |                                  |
| Off balance sheet gap                             | 4,421,993              | (1,231,622)        | (2,430,085)       | (760,286)           | -                             |                   |                                  |
| <b>Total commission rate sensitivity gap</b>      | <u>5,705,742</u>       | <u>1,158</u>       | <u>9,701,460</u>  | <u>5,210,110</u>    | <u>(20,618,470)</u>           |                   |                                  |
| <b>Cumulative commission rate sensitivity gap</b> | <u>5,705,742</u>       | <u>5,706,900</u>   | <u>15,408,360</u> | <u>20,618,470</u>   | <u>-</u>                      |                   |                                  |

The off-balance sheet gap represents the net notional amounts of derivative financial instruments, which are used to manage the commission rate risk.

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

### 34. Liquidity risk

Liquidity risk is the risk that the Bank will be unable to meet its net funding requirements. Liquidity risk can be caused by market disruptions or credit downgrades, which may cause certain sources of funding to dry up immediately. To mitigate this risk, management has diversified funding sources and assets are managed with liquidity in mind, maintaining a healthy balance of cash, cash equivalents, and readily marketable securities.

The table below summarizes the maturity profile of the Bank's assets and liabilities. The contractual maturities of assets and liabilities have been determined on the basis of the remaining period at the balance sheet date to the contractual maturity date and do not take account of the effective maturities as indicated by the Bank's deposit retention history and the availability of liquid funds. Management monitors the maturity profile to ensure that adequate liquidity is maintained.

In accordance with Banking Control Law and the regulations issued by SAMA, the Bank maintains a statutory deposit with SAMA equal to 7% of total demand deposits and 2% of saving and time deposits. In addition to the statutory deposit, the Bank also maintains liquid reserves of no less than 20% of its deposit liabilities, in the form of cash, gold, Saudi Government Development Bonds or assets, which can be converted into cash within a period not exceeding 30 days.

The Bank has the ability to raise additional funds through repo facilities with SAMA against Saudi Government Development Bonds up to 75% of the nominal value of bonds held.

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### 34. Liquidity risk (continued)

The maturity profile of the assets and liabilities is as follows:

| <u>2005</u>                                       | Within 3<br>months | 3-12<br>months    | 1-5<br>years      | Over 5<br>years  | No fixed<br>maturity | Total             |
|---|--------------------|-------------------|-------------------|------------------|----------------------|-------------------|
| <b>Assets</b>                                     |                    |                   |                   |                  |                      |                   |
| Cash and balances with SAMA                       | -                  | -                 | -                 | -                | 2,495,186            | 2,495,186         |
| Due from banks and other financial institutions   | 3,457,177          | -                 | -                 | -                | 476,498              | 3,933,675         |
| Investments, net                                  | 312,406            | 3,697,489         | 12,182,414        | 2,886,656        | 1,343,685            | 20,422,650        |
| Loans and advances, net                           | 8,462,061          | 7,021,559         | 11,808,090        | 6,857,384        | 4,629,462            | 38,778,556        |
| Other real estate                                 | -                  | -                 | -                 | -                | 158,865              | 158,865           |
| Fixed assets, net                                 | -                  | -                 | -                 | -                | 418,108              | 418,108           |
| Other assets                                      | -                  | -                 | -                 | -                | 1,285,039            | 1,285,039         |
| <b>Total assets</b>                               | <u>12,231,644</u>  | <u>10,719,048</u> | <u>23,990,504</u> | <u>9,744,040</u> | <u>10,806,843</u>    | <u>67,492,079</u> |
| <b>Liabilities and shareholders' equity</b>       |                    |                   |                   |                  |                      |                   |
| Due to banks and other financial institutions     | 7,067,611          | 1,188,750         | -                 | -                | 120,573              | 8,376,934         |
| Customer deposits                                 | 22,986,493         | 5,286,513         | 583,183           | -                | 19,976,275           | 48,832,464        |
| Other liabilities                                 | -                  | -                 | -                 | -                | 2,633,502            | 2,633,502         |
| Term Loan   | -                  | -                 | 1,312,500         | -                | -                    | 1,312,500         |
| Shareholders' equity                              | -                  | -                 | -                 | -                | 6,336,679            | 6,336,679         |
| <b>Total liabilities and shareholders' equity</b> | <u>30,054,104</u>  | <u>6,475,263</u>  | <u>1,895,683</u>  | <u>-</u>         | <u>29,067,029</u>    | <u>67,492,079</u> |
| <br>  |                    |                   |                   |                  |                      |                   |
| <u>2004</u>                                       |                    |                   |                   |                  |                      |                   |
| <b>Assets</b>                                     |                    |                   |                   |                  |                      |                   |
| Cash and balances with SAMA                       | 5,027,371          | -                 | -                 | -                | 2,034,085            | 7,061,456         |
| Due from banks and other financial institutions   | 4,362,629          | -                 | -                 | -                | 369,244              | 4,731,873         |
| Investments, net                                  | 1,136,999          | 3,098,433         | 10,186,158        | 5,563,292        | 1,202,584            | 21,187,466        |
| Loans and advances, net                           | 7,331,794          | 5,458,466         | 8,859,253         | 3,066,257        | 3,842,197            | 28,557,967        |
| Other real estate                                 | -                  | -                 | -                 | -                | 191,899              | 191,899           |
| Fixed assets, net                                 | -                  | -                 | -                 | -                | 382,415              | 382,415           |
| Other assets                                      | -                  | -                 | -                 | -                | 1,211,967            | 1,211,967         |
| <b>Total assets</b>                               | <u>17,858,793</u>  | <u>8,556,899</u>  | <u>19,045,411</u> | <u>8,629,549</u> | <u>9,234,391</u>     | <u>63,325,043</u> |
| <b>Liabilities and shareholders' equity</b>       |                    |                   |                   |                  |                      |                   |
| Due to banks and other financial institutions     | 8,082,285          | 1,510,412         | -                 | -                | 228,130              | 9,820,827         |
| Customer deposits                                 | 19,148,755         | 7,195,810         | 971,397           | -                | 18,999,748           | 46,315,710        |
| Other liabilities                                 | -                  | -                 | -                 | -                | 2,218,886            | 2,218,886         |
| Shareholders' equity                              | -                  | -                 | -                 | -                | 4,969,620            | 4,969,620         |
| <b>Total liabilities and shareholders' equity</b> | <u>27,231,040</u>  | <u>8,706,222</u>  | <u>971,397</u>    | <u>-</u>         | <u>26,416,384</u>    | <u>63,325,043</u> |

# Arab National Bank – Saudi Joint Stock Company

## NOTES TO THE FINANCIAL STATEMENTS

For the years ended December 31, 2005 and 2004

(Saudi Riyals in Thousands)

### 35. Fair values of financial assets and liabilities

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

The fair values of on-balance sheet financial instruments, except for those held at amortized cost, other securities, held-to-maturity investments, loans and advances and customer deposits which are carried at amortized cost, are not significantly different from the carrying values included in the financial statements. The estimated fair values of held at amortized cost, other and held-to-maturity investments are based on quoted market prices when available or pricing models in the case of certain fixed rate bonds. The fair values of these investments are disclosed in note 5. It is not practical to determine the fair value of customer deposits except for those disclosed as under FVIS category with sufficient reliability. Loans and advances are stated at cost, adjusted for effective hedge, and stated net of interest suspended, provision for impairment and any amounts written off.

The fair values of derivatives and other off-balance sheet financial instruments are based on the quoted market prices when available or by using the appropriate valuation models. The total amount of the changes in fair value recognized in the statement of income, which was estimated using valuation models, is SAR 35.1 millions (2004: SAR 77.5 millions).

### 36. Related party transactions

In the ordinary course of its activities, the Bank transacts business with related parties. In the opinion of the management and the board, the related party transactions are performed on an arm's length basis. The related party transactions are governed by limits set by the Banking Control Law and regulations issued by SAMA. The balances as at December 31 resulting from such transactions included in the financial statements are as follows:

|  | 2005      | 2004      |
|--|-----------|-----------|
| <b>Arab Bank PLC</b>   |           |           |
| Due from banks and other financial institutions  | 376,335   | 696,270   |
| Due to banks and other financial institutions  | 896,813   | 1,485,967 |
| Derivatives (at fair value)  | -         | 16        |
| Commitments and contingencies  | 1,259,605 | 914,763   |
| <b>Directors, key management personnel, other major shareholders and their affiliates:</b> |           |           |
| Loans and advances   | 987,976   | 1,210,406 |
| Customer deposits  | 3,613,009 | 3,806,375 |
| Derivatives (at fair value)  | 8,079     | 10,476    |
| Commitments and contingencies  | 377,891   | 371,247   |
| <b>Bank's mutual funds</b>   |           |           |
| Investments  | 98,776    | 91,485    |
| Loans and advances   | 106,840   | 16,124    |
| Customer deposits  | 1,366,443 | 1,962,919 |

Other major shareholders represent shareholdings (excluding the non-Saudi shareholder) of more than 5% of the Bank's issued share capital

Income and expenses pertaining to transactions with related parties included in the financial statements are as follows:

|                            | 2005    | 2004    |
|----------------------------|---------|---------|
| Special commission income  | 37,757  | 41,074  |
| Special commission expense | 149,777 | 106,242 |
| Fees from banking services | 31,848  | 23,232  |
| Directors' remuneration    | 1,940   | 2,024   |

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

|   | 2005   | 2004   |
|---|--------|--------|
| Short-term employee benefits (Salaries and allowances)                  | 23,558 | 20,299 |
| Post-employment benefits (End of service indemnity and social security) | 1,633  | 1,387  |

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

# Arab National Bank – Saudi Joint Stock Company

## NOTES TO THE FINANCIAL STATEMENTS

For the years ended December 31, 2005 and 2004

(Saudi Riyals in Thousands)

### 37. Capital Adequacy

The Bank monitors the adequacy of its capital using ratios established by SAMA. These ratios measure capital adequacy by comparing the Bank's eligible capital with its balance sheet assets, commitments and notional amount of derivatives at a weighted amount to reflect their relative risk.

|                 | 2005      |         | 2004      |         |
|-----------------|-----------|---------|-----------|---------|
|                 | Capital   | Ratio % | Capital   | Ratio % |
| Tier 1          | 6,336,679 | 14.0    | 4,969,620 | 14.7    |
| Tier 1 + Tier 2 | 6,902,147 | 15.3    | 5,393,044 | 15.9    |

  

| <u>Risk weighted assets</u>          | 2005                      |                   |                      | 2004                      |                   |                      |
|--------------------------------------|---------------------------|-------------------|----------------------|---------------------------|-------------------|----------------------|
|                                      | Carrying value / notional | Credit equivalent | Risk weighted assets | Carrying value / notional | Credit equivalent | Risk weighted assets |
| <b>Balance sheets assets</b>         |                           |                   |                      |                           |                   |                      |
| 0 %                                  | 20,077,637                | -                 | -                    | 24,794,669                | -                 | -                    |
| 20 %                                 | 7,888,915                 | -                 | 1,577,783            | 9,881,010                 | -                 | 1,976,202            |
| 100 %                                | 39,525,527                | -                 | 39,525,527           | 28,649,364                | -                 | 28,649,364           |
| <b>Total</b>                         | <b>67,492,079</b>         | <b>-</b>          | <b>41,103,310</b>    | <b>63,325,043</b>         | <b>-</b>          | <b>30,625,566</b>    |
| <b>Commitments and contingencies</b> |                           |                   |                      |                           |                   |                      |
| 0 %                                  | 328,169                   | 147,112           | -                    | 414,624                   | 193,702           | -                    |
| 20 %                                 | 3,732,789                 | 1,770,987         | 354,197              | 2,980,475                 | 1,405,582         | 281,116              |
| 100 %                                | 7,584,242                 | 3,581,130         | 3,581,130            | 5,941,927                 | 2,812,289         | 2,812,289            |
| <b>Total</b>                         | <b>11,645,200</b>         | <b>5,499,229</b>  | <b>3,935,327</b>     | <b>9,337,026</b>          | <b>4,411,573</b>  | <b>3,093,405</b>     |
| <b>Derivatives</b>                   |                           |                   |                      |                           |                   |                      |
| 20 %                                 | 29,118,779                | 242,839           | 48,568               | 24,182,315                | 464,397           | 92,879               |
| 50 %                                 | 3,285,229                 | 300,488           | 150,245              | 5,511,724                 | 124,105           | 62,053               |
| <b>Total</b>                         | <b>32,404,008</b>         | <b>543,327</b>    | <b>198,813</b>       | <b>29,694,039</b>         | <b>588,502</b>    | <b>154,932</b>       |
| <b>Grand total</b>                   |                           |                   | <b>45,237,450</b>    |                           |                   | <b>33,873,903</b>    |

### 38. Investment management services

The Bank offers investment services to its customers, which include management of investment funds with assets totaling of SAR 4,086 million (2004: SAR 3,341 million).

The financial statements of these funds are not consolidated with these financial statements. However, the Bank's share of these funds is included in available-for-sale investments and fees earned are disclosed under related party transactions.

Assets held in trust or in a fiduciary capacity are not treated as assets of the Bank and accordingly are not included in the financial statements.

### 39. Comparative figures

Other than reclassifications required by adoption of the revised IAS 39 and IAS 32, certain prior year figures have been reclassified to conform with current year presentation.

### 40. Board of directors' approval

The financial statements were approved by the Board of Directors on January 16, 2006.