Arab National Bank

(A Saudi Joint Stock Company)

Interim Condensed Consolidated Financial Statements
For the period ended 30 September 2018

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Certified Public Accountants

Independent Auditors' Review Report on Interim Condensed Consolidated Financial Statements

To: The Shareholders of Arab National Bank
(A Saudi Joint Stock Company)

Introduction

We have reviewed the accompanying interim consolidated statement of financial position of Arab National Bank ("the Bank") and its subsidiaries (collectively referred to as "the Group") as at 30 September 2018, and the related interim consolidated statements of income and comprehensive income for the three and nine month periods then ended and the related interim consolidated statements of changes in equity and cash flows for the nine month period then ended and other explanatory notes (the "interim condensed consolidated financial statements"). Management is responsible for the preparation and presentation of these interim condensed consolidated financial statements in accordance with International Accounting Standard No. 34 "Interim Financial Reporting" ("IAS 34") as modified by the Saudi Arabian Monetary Authority ("SAMA") for the accounting of zakat and income tax. Our responsibility is to express a conclusion on these interim condensed consolidated financial statements based on our review.

Scope of Review

We conducted our review in accordance with the International Standard on Review Engagements 2410, "Review of Interim Financial Information Performed by the Independent Auditor of the Entity", as endorsed in the Kingdom of Saudi Arabia. A review of interim financial information consists of making inquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with International Standards on Auditing that are endorsed in the Kingdom of Saudi Arabia and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

Conclusion

Based on our review, nothing has come to our attention that causes us to believe that the accompanying interim condensed consolidated financial statements are not prepared, in all material respects, in accordance with IAS 34 as modified by SAMA for the accounting of zakat and income tax.

Other Regulatory Matters

As required by SAMA, certain capital adequacy information has been disclosed in note (17) to the accompanying interim condensed consolidated financial statements. As part of our review, we compared the information in note (17) to the relevant analysis prepared by the Bank for submission to SAMA and found no material inconsistencies.

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(28 October 2018)

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ARAB NATIONAL BANK – Saudi Joint Stock Company
INTERIM CONSOLIDATED STATEMENT OF FINANCIAL POSITION
(SAR'000)

As at	**Notes**	**September 30, 2018 (Unaudited)**	December 31, 2017 (Audited)	September 30, 2017 (Unaudited)
ASSETS				
Cash and balances with SAMA		**14,132,693**	17,251,379	12,612,587
Due from banks and other financial institutions		**809,744**	1,710,123	3,249,371
Positive fair value of derivatives	9	**2,145,757**	943,760	735,798
Investments, net	6	**27,486,440**	32,320,816	25,759,420
Loans and advances, net	7	**120,489,435**	114,542,929	115,931,970
Investments in associates		**623,418**	637,222	631,527
Other real estate		**220,697**	220,697	220,697
Investment property, net		**1,607,963**	1,626,563	1,632,862
Property and equipment, net		**1,592,787**	1,694,591	1,716,110
Other assets		**856,023**	753,619	1,152,836
Total assets		**169,964,957**	171,701,699	163,643,178
LIABILITIES AND EQUITY				
Liabilities				
Due to banks and other financial institutions		**3,810,078**	2,691,549	2,966,452
Negative fair value of derivatives	9	**1,513,531**	855,902	696,138
Customers' deposits	8	**130,830,470**	136,048,089	128,546,906
Other liabilities		**6,373,915**	5,023,920	4,663,617
Sukuk		**2,037,706**	2,016,274	2,033,104
Total liabilities		**144,565,700**	146,635,734	138,906,217
Equity				
Equity attributable to equity holders of the Bank				
Share capital	13	**10,000,000**	10,000,000	10,000,000
Statutory reserve		**10,000,000**	10,000,000	9,446,000
Other reserves		**88,552**	(75,807)	46,198
Retained earnings		**4,636,896**	3,795,494	4,550,683
Proposed dividends		**-**	650,000	-
Total equity attributable to equity holders of the Bank		**24,725,448**	24,369,687	24,042,881
Non-controlling interests		**673,809**	696,278	694,080
Total equity		**25,399,257**	25,065,965	24,736,961
Total liabilities and equity		**169,964,957**	171,701,699	163,643,178

The accompanying notes 1 to 19 form an integral part of these interim condensed consolidated financial statements.

ARAB NATIONAL BANK – Saudi Joint Stock Company
INTERIM CONSOLIDATED STATEMENT OF INCOME
(Unaudited)
(SAR'000)

		For the three month period ended		For the nine month period ended	
	Notes	**September 30, 2018**	September 30, 2017	**September 30, 2018**	September 30, 2017
Special commission income		**1,779,138**	1,489,116	**4,952,098**	4,524,821
Special commission expense		**456,571**	305,178	**1,163,740**	1,056,594
Net special commission income		**1,322,567**	1,183,938	**3,788,358**	3,468,227
Fees and commission income, net		**180,330**	180,489	**524,642**	655,250
Exchange income, net		**107,976**	100,455	**304,679**	308,835
Unrealized (loss)/gain on FVTPL financial instruments, net		**(1,261)**	-	**15,445**	31
Trading income, net		**2,433**	2,560	**19,762**	18,827
Dividend income		**25,869**	22,535	**51,441**	51,604
Loss on sale of FVOCI debt financial assets, net		**-**	-	**(208)**	-
Gains on available for sale investments, net		**-**	127,840	**-**	136,322
Other operating income, net		**46,011**	58,932	**159,214**	154,196
Total operating income		**1,683,925**	1,676,749	**4,863,333**	4,793,292
Salaries and employee related expenses		**316,423**	323,338	**937,377**	931,238
Rent and premises related expenses		**39,929**	39,903	**117,842**	132,098
Depreciation and amortization		**51,050**	55,154	**154,224**	167,605
Other general and administrative expenses		**148,752**	156,215	**442,638**	412,707
Impairment charges for credit losses and other provisions, net	7	**241,816**	327,629	**591,041**	771,206
(Reversal of impairment charges) impairment charges for other financial assets, net		**(1,977)**	5,970	**(7,610)**	5,970
Total operating expenses		**795,993**	908,209	**2,235,512**	2,420,824
Net operating income		**887,932**	768,540	**2,627,821**	2,372,468
Share in earnings of associates, net		**1,113**	8,445	**196**	24,963
Net income for the period		**889,045**	776,985	**2,628,017**	2,397,431
Attributable to:					
Equity holders of the Bank		**890,107**	775,459	**2,625,706**	2,392,543
Non-controlling interests		**(1,062)**	1,526	**2,311**	4,888
Net income for the period		**889,045**	776,985	**2,628,017**	2,397,431
Basic and diluted earnings (in SAR per share)	13	**0.89**	0.78	**2.63**	2.39

The accompanying notes 1 to 19 form an integral part of these interim condensed consolidated financial statements.

ARAB NATIONAL BANK – Saudi Joint Stock Company
INTERIM CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME
(Unaudited)
(SAR'000)

	For the three month period ended		For the nine month period ended	
	September 30, 2018	September 30, 2017	**September 30, 2018**	September 30, 2017
Net income for the period	**889,045**	776,985	**2,628,017**	2,397,431
Other comprehensive income:				
Items that cannot be reclassified to interim consolidated statement of income in subsequent periods				
Equity instruments at fair value through other comprehensive income:				
- Net changes in fair value	**(37,833)**	-	**117,123**	-
Items that can be reclassified to interim consolidated statement of income in subsequent periods				
Debt instruments at fair value through other comprehensive income:				
- Net changes in fair value	**29,391**	-	**27,919**	-
- Net amounts transferred to interim consolidated statement of income	**(180)**	-	**(2,453)**	-
Available for sale financial assets:				
- Net changes in fair value	**-**	(39,336)	**-**	9,840
- Net amounts transferred to interim consolidated statement of income	**-**	(121,870)	**-**	(130,156)
Total other comprehensive (loss) income for the period	**(8,622)**	(161,206)	**142,589**	(120,316)
Total comprehensive income for the period	**880,423**	615,779	**2,770,606**	2,277,115
Attributable to:				
Equity holders of the Bank	**881,485**	614,253	**2,768,295**	2,272,227
Non-controlling interest	**(1,062)**	1,526	**2,311**	4,888
Total comprehensive income for the period	**880,423**	615,779	**2,770,606**	2,277,115

The accompanying notes 1 to 19 form an integral part of these interim condensed consolidated financial statements.

ARAB NATIONAL BANK – Saudi Joint Stock Company
INTERIM CONSOLIDATED STATEMENT OF CHANGES IN EQUITY
For the nine months period ended September 30, 2018 and 2017
(Unaudited)
(SAR'000)

2018	**Notes**	**Share capital**	**Statutory reserve**	**FVOCI/ AFS**	**Acturial losses on defined benefit plan**	**Retained earnings**	**Proposed dividends**	**Total**	**Non-controlling interests**	**Total equity**
		Attributable to equity holders of the Bank								
				Other Reserves						
Balance at the beginning of the period (as previously reported)		**10,000,000**	**10,000,000**	**(15,990)**	**(59,817)**	**3,795,494**	**650,000**	**24,369,687**	**696,278**	**25,065,965**
Impact of adopting of new standards at January 1, 2018	4	**-**	**-**	**4,793**	**-**	**(634,327)**	**-**	**(629,534)**	**-**	**(629,534)**
Restated balance at January 1, 2018		**10,000,000**	**10,000,000**	**(11,197)**	**(59,817)**	**3,161,167**	**650,000**	**23,740,153**	**696,278**	**24,436,431**
Changes in equity for the period:										
Net changes in fair values of FVOCI equity investments				**117,123**	**-**	**-**	**-**	**117,123**	**-**	**117,123**
Net changes in fair values of FVOCI debt instruments				**27,919**	**-**	**-**	**-**	**27,919**	**-**	**27,919**
Net transfers to interim consolidated statement of income				**(2,453)**	**-**	**-**	**-**	**(2,453)**	**-**	**(2,453)**
Net income for the period				**-**	**-**	**2,625,706**	**-**	**2,625,706**	**2,311**	**2,628,017**
Total comprehensive income for the period				**142,589**	**-**	**2,625,706**	**-**	**2,768,295**	**2,311**	**2,770,606**
Net loss on derecognition of FVOCI equity				**16,977**	**-**	**(16,977)**	**-**	**-**	**-**	**-**
Distribution from a subsidiary				**-**	**-**	**-**	**-**	**-**	**(24,780)**	**(24,780)**
2017 final dividends				**-**	**-**	**-**	**(650,000)**	**(650,000)**	**-**	**(650,000)**
2018 interim dividends	14			**-**	**-**	**(650,000)**	**-**	**(650,000)**	**-**	**(650,000)**
Zakat for the current period				**-**	**-**	**(289,800)**	**-**	**(289,800)**	**-**	**(289,800)**
Income tax for the current period				**-**	**-**	**(193,200)**	**-**	**(193,200)**	**-**	**(193,200)**
Balance at the end of the period		**10,000,000**	**10,000,000**	**148,369**	**(59,817)**	**4,636,896**	**-**	**24,725,448**	**673,809**	**25,399,257**

2017	Note	Share capital	Statutory reserve	Available for sale fianancial assets	Acturial gains/ (losses) on defined benefit plan	Retained earnings	Proposed dividends	Total	Non-controlling interests	Total equity
		Attributable to equity holders of the Bank								
				Other Reserves						
Balance at the beginning of the period		10,000,000	9,446,000	166,514	-	3,172,847	450,000	23,235,361	689,192	23,924,553
Changes in equity for the period:										
Net changes in fair values of available for sale investments				9,840	-	-	-	9,840	-	9,840
Net transfers to interim consolidated statement of income				(130,156)	-	-	-	(130,156)	-	(130,156)
Net income for the period				-	-	2,392,543	-	2,392,543	4,888	2,397,431
Total comprehensive income for the period				(120,316)	-	2,392,543	-	2,272,227	4,888	2,277,115
2016 final dividends		-	-	-	-	-	(450,000)	(450,000)	-	(450,000)
2017 interim divendends	14	-	-	-	-	(550,000)	-	(550,000)	-	(550,000)
Zakat for the current period		-	-	-	-	(279,074)	-	(279,074)	-	(279,074)
Income tax for the current period		-	-	-	-	(185,633)	-	(185,633)	-	(185,633)
Balance at the end of the period		10,000,000	9,446,000	46,198	-	4,550,683	-	24,042,881	694,080	24,736,961

The accompanying notes 1 to 19 form an integral part of these interim condensed consolidated financial statements.

ARAB NATIONAL BANK – Saudi Joint Stock Company
INTERIM CONSOLIDATED STATEMENT OF CASH FLOWS
For the nine months ended
(Unaudited)
(SAR'000)

OPERATING ACTIVITIES	**Note**	**September 30, 2018**	September 30, 2017
Net income for the period		**2,628,017**	2,397,431
Adjustments to reconcile net income to net cash used in operating activities for the period:			
Amortization of premium on non-trading investments, net		**813**	3,247
Special commission expense on sukuk		**56,278**	53,862
Losses/(gains) on investments not held as FVTPL, net		**208**	(136,322)
Unrealized gains on FVTPL financial instruments, net		**(15,445)**	(31)
Dividend income		**(51,441)**	(51,604)
Depreciation of investment property		**18,600**	18,501
Depreciation and amortization of property and equipment		**154,224**	167,605
Losses on disposal of property and equipment, net		**1,304**	4,839
Impairment charges for credit losses and other provisions, net		**591,041**	771,206
(Reversal of impairment charges) impairment charges for other financial assets, net		**(7,610)**	5,970
Share in earnings of associates, net		**(196)**	(24,963)
		3,375,793	3,209,741
Net (increase)/decrease in operating assets:			
Statutory deposit with SAMA		**83,859**	(182,303)
Investments held at FVTPL (including trading investments)		**(447,621)**	757
Positive fair value of derivatives		**(1,201,997)**	(276,028)
Loans and advances		**(7,129,909)**	(1,256,151)
Other assets		**(102,122)**	(442,241)
Net increase/(decrease) in operating liabilities:			
Due to banks and other financial institutions		**1,118,529**	(892,419)
Negative fair value of derivatives		**657,629**	256,349
Customers' deposits		**(5,217,619)**	(7,360,551)
Other liabilities		**1,556,528**	637,602
Net cash used in operating activities		**(7,306,930)**	(6,305,244)
INVESTING ACTIVITIES			
Proceeds from sale and maturities of investments not held as FVTPL		**7,252,843**	3,663,620
Purchase of investments not held as FVTPL		**(2,214,709)**	(3,902,677)
Purchase of property and equipment		**(55,500)**	(51,500)
Proceeds from sale of property and equipment		**1,776**	2,168
Dividends received		**51,441**	51,604
Net cash from (used in) investing activities		**5,035,851**	(236,785)
FINANCING ACTIVITIES			
Dividends paid		**(1,295,465)**	(993,686)
Zakat and tax paid		**(308,613)**	(280,504)
Special commission paid on sukuk		**(34,846)**	(38,948)
Non-controlling interest from distributions from a subsidiary		**(24,780)**	-
Net cash used in financing activities		**(1,663,704)**	(1,313,138)
Net decrease in cash and cash equivalents		**(3,934,783)**	(7,855,167)
Cash and cash equivalents at the beginning of the period		**11,772,360**	16,347,323
Cash and cash equivalents at the end of the period	11	**7,837,577**	8,492,156
Special commission received during the period		**4,905,944**	4,264,184
Special commission paid during the period		**(1,031,737)**	(985,185)
Supplemental non-cash information			
Net changes in fair value of investments held at fair value through other comprehensive income		**145,042**	-
Net changes in fair value of available for sale investments (2017)		**-**	9,840

The accompanying notes 1 to 19 form an integral part of these interim condensed consolidated financial statements.

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 (corresponding to 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 (corresponding to January 19, 1980) through its 140 branches (2017: 144 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. The Bank also provides its customers non-commission based banking products which are approved and supervised by an independent Shariah Board established by the Bank.

The interim condensed consolidated financial statements comprise the interim condensed financial statements of the Bank and the following subsidiaries:

Arab National Investment Company (ANB Invest)

In accordance with the Capital Market Authority (CMA) directives, the Bank has established ANB Invest, a wholly owned subsidiary (directly and indirectly), a Saudi closed joint stock company, registered in the Kingdom under Commercial Registration No. 1010239908 issued on Shawwal 26, 1428H (corresponding to November 7, 2007), to takeover and manage the Bank's investment services and asset management activities related to dealing, managing, arranging, advising and custody of securities regulated by the CMA. The subsidiary commenced its operations effective Muharram 3, 1429H (corresponding to January 12, 2008). Accordingly, the Bank started consolidating the financial statements of the above mentioned subsidiary effective January 12, 2008. On Muharram 19, 1436H (corresponding to November 12, 2014), the subsidiary changed its legal structure from a limited liability company to a closed joint stock company. The objective of the subsidiary was amended and approved by CMA Board of Commissioners on Muharram 28, 1437 H (corresponding to November 10, 2015) through a resolution number S/1/6/14832/15 to include dealing as a principal activity. The objective of the subsidiary was further amended on Sha'ban 26, 1437H (corresponding to June 2, 2016) to provide loans to the subsidiary's customers to trade in financial papers as per the Saudi Arabian Monetary Authority's circular No. 371000014867 dated 5/2/1437H, and the CMA's circular No. S/6/16287/15 dated 10/3/1437H.

Arabian Heavy Equipment Leasing Company (AHEL)

An 87.5% owned subsidiary incorporated in the Kingdom, as a Saudi closed joint stock company, under Commercial Registration no 1010267489 issued in Riyadh dated Jumada I 15, 1430H (corresponding to May 10, 2009). The company is engaged in the leasing of heavy equipment and operates in compliance with Shari'ah principles. The Bank started consolidating the subsidiary's financial statements effective May 10, 2009, the date the subsidiary started its operations. On May 6, 2014 the Bank increased its ownership percentage in this subsidiary from 62.5% to reach 87.5%.

ANB Insurance Agency

A Saudi limited liability company established during 2013 as a wholly owned subsidiary, registered in the Kingdom under Commercial Registration no. 1010396423 issued in Riyadh dated Muharram 28, 1435H (corresponding to December 1, 2013). The subsidiary obtained its license from the Saudi Arabian Monetary Authority (SAMA) to start its activities in insurance agency and related business on Jumada I 5, 1435H (corresponding to March 6, 2014).

Al-Manzil Al-Mubarak Real Estate Financing Ltd.

A wholly owned Saudi limited liability company, registered in the Kingdom under the commercial registration no. 1010199647 issued in Riyadh dated Jumada I 18, 1425H (corresponding to July 6, 2004). The subsidiary is engaged in the purchase of lands and real estates and invest them through sale or rent in favor of the company, maintenance and management of owners and others' assets as guarantee, sale and purchase of real estates for financing purposes as per SAMA approval No. 361000109161 dated 10/8/1436H.

1. General (continued)

ANBI Business Gate Fund (the Fund)

The Bank owns indirectly 25.47% of the Fund, which is a closed-ended private placement real estate investment fund launched on August 25, 2014 for a period of 5 years starting from date of closure of first offering on January 11, 2015. CMA has been informed of the offering of the Fund through letter number 8/14//411 dated Shawwal 9, 1435H (corresponding to August 5, 2014). The Fund's purpose is to acquire real estate assets, an income generating real estate property located in the city of Riyadh, out of which the Fund will receive rental and hotel operating income over the Fund term. The Group has significant aggregate economic interest in the Fund and manages the Fund through an agreement between Arab National Investment Company (the "Fund Manager") and the Fund Investors (the "Unitholders"). As a result, management has concluded that the Group has effective control of the Fund and started consolidating the Fund's financial statements effective December 31, 2015, the date of effective control.

ANB Global Markets Limited

The Bank established on January 31, 2017 ANB Global Markets Limited, as a limited liability company registered in the Cayman Islands. The Bank has 100% ownership. The objective of ANB Global Markets Limited is trading in derivatives and Repo activities on behalf of the Bank.

2. Basis of preparation

The interim condensed consolidated financial statements for the nine months ended September 30, 2018 have been prepared in accordance with IAS 34 "Interim Financial Reporting" as modified by SAMA for the accounting of zakat and income tax. The interim condensed consolidated financial statements do not include all the information and disclosures required in the annual consolidated financial statements, and should be read in conjunction with the Group's annual consolidated financial statements as at December 31, 2017. The Bank has adopted IFRS 9 "Financial Instruments" and IFRS 15 "Revenue from Contracts with Customers" from January 1, 2018 and accounting policies for these new standards are disclosed in the Note 5. Significant judgments and estimates relating to impairment are disclosed in the financial risk management note considering IFRS 9 first time adoption.

As permissible in the transitional provisions of these standards, the Bank has opted for modified retrospective application of these standards. Accordingly, the comparative period continues to apply the previously applicable accounting policies and the comparatives have not been restated. The transitional provisions have been discussed in Note 4.

These interim condensed consolidated financial statements are expressed in Saudi Arabian Riyals (SAR) and are rounded off to the nearest thousand, except where indicated otherwise.

3. Basis of consolidation

The interim condensed consolidated financial statements comprise the interim condensed financial statements of the Bank and its subsidiaries (collectively referred to as the Group). The financial statements of the subsidiaries are prepared for the same reporting period as that of the Bank, using consistent accounting policies. Adjustments have been made to the financial statements of the subsidiaries where necessary to align them with the Bank's interim condensed consolidated financial statements.

Subsidiaries are investees controlled by the Group. The Group controls an investee when it is exposed to, or has rights to, variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee. The financial statements of subsidiaries are included in the interim condensed consolidated financial statements from the date that control commences until the date that control ceases.

Specifically, the Group controls an investee if and only if the Group has:

Power over the investee (i.e. existing rights that give it the current ability to direct the relevant activities of the investee);

- Exposure, or rights, to variable returns from its involvement with the investee; and
- The ability to use its power over the investee to affect its returns.

When the Group has less than a majority of the voting or similar rights of an investee, the Group considers all relevant facts and circumstances in assessing whether it has power over an investee, including:

- The contractual arrangements with the other vote holders of the investee;
- Rights arising from other contractual arrangements; and
- The Group's voting rights and potential voting rights granted by equity instruments such as shares.

3. Basis of consolidation (continued)

The Group re-assesses whether or not it controls an investee if facts and circumstances indicate that there are changes to one or more of the three elements of control. Consolidation of a subsidiary begins when the Group obtains control over the subsidiary and ceases when the Group loses control of the subsidiary. Assets, liabilities, income and expenses of a subsidiary acquired or disposed of during the period are included in the interim consolidated statement of comprehensive income from the date the Group gains control until the date the Group ceases to control the subsidiary.

If the Group loses control over a subsidiary, it:

- Derecognises the assets (including goodwill) and liabilities of the subsidiary;
- Derecognises the carrying amount of any non-controlling interests;
- Derecognises the cumulative translation differences recorded in equity;
- Recognises the fair value of the consideration received;
- Recognises the fair value of any investment retained;
- Recognises any surplus or deficit in profit or loss; and
- Reclassifies the parent's share of components previously recognised in Other Comprehensive Income to profit or loss or retained earnings, as appropriate, as would be required if the Group had directly disposed of the related assets or liabilities.

Non-controlling interests represent the portion of net income or loss and net assets not owned, directly or indirectly, by the Bank and are presented separately in the interim consolidated statement of income and within equity in the interim consolidated statement of financial position, separately from equity attributable to the equity holders of the Bank. Any losses applicable to the non-controlling interests in a subsidiary are allocated to the non-controlling interests even if doing so causes the non-controlling interests to have a deficit balance. Acquisitions of non-controlling interests are accounted for using the purchase method of accounting, whereby, the difference between the cost of acquisition and the fair value of the share of the net assets acquired is recognized as goodwill.

Transactions with non-controlling interests that do not result in loss of control are accounted for as equity transactions – that is, as transactions with the owners in their capacity as owners. The difference between fair value of any consideration paid and the relevant share acquired of the carrying value of net assets of the subsidiary is recorded in equity. Gains or losses on disposals to non-controlling interests are also recorded in equity.

Non-controlling interests are subsequently adjusted for their share of changes in equity of the consolidated subsidiary after the date of acquisition.

All intra-group assets and liabilities, equity, income and expenses relating to transactions between members of the Group are eliminated in full on consolidation.

4. Impact of changes in accounting policies due to adoption of new standards

IFRS 15 – Revenue from Contracts with Customers

The Bank adopted IFRS 15 'Revenue from Contracts with Customers' resulting in a change in the revenue recognition policy of the bank in relation to its contracts with customers.

IFRS 15 was issued in May 2014 and is effective for annual periods commencing on or after January 1, 2018. IFRS 15 outlines a single comprehensive model of accounting for revenue arising from contracts with customers and supersedes current revenue guidance, which is found currently across several Standards and Interpretations within IFRS. It established a new five-step model that will apply to revenue arising from contracts with customers. Under IFRS 15, revenue is recognised at an amount that reflects the consideration to which an entity expects to be entitled in exchange for transferring goods or services to a customer.

The Bank has opted for the modified retrospective application permitted by IFRS 15 upon adoption of the new standard. Modified retrospective application also requires the recognition of the cumulative impact of adoption of IFRS 15 on all contracts as at January 1, 2018 in equity.

4. Impact of changes in accounting policies due to adoption of new standards (continued)

IFRS 9 – Financial Instruments

The Bank has adopted IFRS 9 - Financial Instruments issued in July 2014 with a date of initial application of January 1, 2018. The requirements of IFRS 9 represent a significant change from IAS 39 Financial Instruments: Recognition and Measurement. The new standard brings fundamental changes to the accounting for financial assets and to certain aspects of the accounting for financial liabilities.

As permitted by IFRS 9, the Bank has elected to continue to apply the hedge accounting requirements of IAS 39.

The key changes to the Bank's accounting policies resulting from its adoption of IFRS 9 are summarized below.

Classification of financial assets and financial liabilities

IFRS 9 contains three principal classification categories for financial assets: measured at amortized cost ("AC"), fair value through other comprehensive income ("FVOCI") and fair value through profit or loss ("FVTPL"). This classification is generally based, except equity instruments and derivatives, on the business model in which a financial asset is managed and its contractual cash flows. The standard eliminates the existing IAS 39 categories of held-to-maturity, loans and receivables and available-for-sale. Under IFRS 9, derivatives embedded in contracts where the host is a financial asset in the scope of the standard are never bifurcated. Instead, the whole hybrid instrument is assessed for classification. For an explanation of how the Bank classifies financial assets under IFRS 9, see respective section of significant accounting policies.

IFRS 9 largely retains the existing requirements in IAS 39 for the classification of financial liabilities. However, although under IAS 39 all fair value changes of liabilities designated under the fair value option were recognized in profit or loss, under IFRS 9 fair value changes are presented as follows:

- The amount of change in the fair value that is attributable to changes in the credit risk of the liability is presented in OCI; and
- The remaining amount of change in the fair value is presented in profit or loss.

For an explanation of how the Bank classifies financial liabilities under IFRS 9, see respective section of significant accounting policies.

Impairment of financial assets

IFRS 9 replaces the 'incurred loss' model in IAS 39 with an 'expected credit loss' model ("ECL"). IFRS 9 requires the Bank to record an allowance for ECLs for all loans and other debt financial assets not held at FVPL, together with loan commitments and financial guarantee contracts. The allowance is based on the ECLs associated with the probability of default in the next twelve months unless there has been a significant increase in credit risk since origination. If the financial asset meets the definition of purchased or originated credit impaired (POCI), the allowance is based on the change in the ECLs over the life of the asset.

Under IFRS 9, credit losses are recognized earlier than under IAS 39. For an explanation of how the Bank applies the impairment requirements of IFRS 9, see respective section of significant accounting policies.

(SAR'000)

4. Impact of changes in accounting policies due to adoption of new standards (continued)

Transition

Changes in accounting policies resulting from the adoption of IFRS 9 have been applied retrospectively, except as described below.

- Comparative periods have not been restated. A difference in the carrying amounts of financial assets and financial liabilities resulting from the adoption of IFRS 9 are recognized in retained earnings and other reserves as at January 1, 2018. Accordingly, the information presented for 2017 does not reflect the requirements of IFRS 9 and therefore is not comparable to the information presented for 2018 under IFRS 9.
- The following assessments have been made on the basis of the facts and circumstances that existed at the date of initial application.

  i. The determination of the business model within which a financial asset is held.
  ii. The designation and revocation of previous designated financial assets and financial liabilities as measured at FVTPL.
  iii. The designation of certain investments in equity instruments not held for trading as FVOCI. For financial liabilities designated as at FVTPL, the determination of whether presenting the effects of changes in the financial liability's credit risk in OCI would create or enlarge an accounting mismatch in profit or loss.

It is assumed that the credit risk has not increased significantly for those debt securities which carry low credit risk at the date of initial application of IFRS 9.

a) Financial assets and financial liabilities

i) Classification of financial assets and financial liabilities on the date of initial application of IFRS 9

The following table shows the original measurement categories in accordance with IAS 39 and the new measurement categories under IFRS 9 for the Bank's financial assets and financial liabilities as at January 1, 2018.

	Notes	Measurement basis under IAS 39	Measurement basis under IFRS 9	Original carrying value under IAS 39	New carrying value under IFRS 9
Financial assets					
Cash and balances with SAMA		Amortised cost	Amortised cost	17,251,379	17,251,379
Due from banks and other financial institutions		Amortised cost	Amortised cost	1,710,123	1,709,700
Investments, net	6	AFS	FVOCI	10,454,174	10,404,322
		Amortised cost	Amortised cost	21,866,642	21,851,371
		Held for trading/FVTPL	FVTPL	-	49,852
Positive fair value of derivatives	9	FVTPL	FVTPL	943,760	943,760
Loans and advances, net	7	Amortised cost	Amortised cost	114,542,929	114,156,749
Other assets - accounts receivable		Amortised cost	Amortised cost	550,953	550,953
				167,319,960	166,918,086
Financial liabilities					
Due to banks and other financial institutions		Amortised cost	Amortised cost	2,691,549	2,691,549
Customers' deposits	8	Amortised cost	Amortised cost	136,048,089	136,048,089
Negative fair value of derivatives	9	FVTPL	FVTPL	855,902	855,902
Sukuk		Amortised cost	Amortised cost	2,016,274	2,016,274
Other liabilities - accounts payable		Amortised cost	Amortised cost	3,946,285	4,075,401
				145,558,099	145,687,215

(SAR'000)

4. Impact of changes in accounting policies due to adoption of new standards (continued)

a) Financial assets and financial liabilities (continued)

ii) Reconciliation of carrying amounts under IAS 39 to carrying amounts under IFRS 9 at the adoption of IFRS 9

The following table reconciles the carrying amounts under IAS 39 to the carrying amounts under IFRS 9 on transition to IFRS 9 on January 1, 2018.

	IAS 39 carrying amount as at December 31, 2017	Re-classification	Re-measurement	IFRS 9 carrying amount as at January 1, 2018
Financial assets				
Amortized cost				
Cash and balances with SAMA	17,251,379	-	-	17,251,379
Due from banks and other financial institutions	1,710,123	-	(423)	1,709,700
Loans and advances, net	114,542,929	-	(386,180)	114,156,749
Investments, net	21,866,642	-	(15,271)	21,851,371
Other assets	550,953	-	-	550,953
Total amortized cost	155,922,026	-	(401,874)	155,520,152
Available for sale				
Investments:				
Opening balance	10,454,174	-	-	10,454,174
Transferred to:				
FVOCI – equity	-	(766,287)	-	(766,287)
FVOCI – debt	-	(9,638,035)	-	(9,638,035)
FVTPL	-	(49,852)	-	(49,852)
Total available for sale	10,454,174	(10,454,174)	-	-
FVOCI				
Investments:				
Opening balance	-	-	-	-
From available for sale	-	10,404,322	-	10,404,322
Closing balance	-	10,404,322	-	10,404,322
Total FVOCI	10,454,174	(49,852)	-	10,404,322
FVTPL				
- Investments:				
Opening balance	-	-	-	-
From available for sale	-	49,852	-	49,852
Closing balance	-	49,852	-	49,852
- Positive fair value of derivatives	943,760	-	-	943,760
Total FVTPL	943,760	49,852	-	993,612

(SAR'000)

4. Impact of changes in accounting policies due to adoption of new standards (continued)

a. Financial assets and financial liabilities (continued)

ii) Reconciliation of carrying amounts under IAS 39 to carrying amounts under IFRS 9 at the adoption of IFRS 9 (continued)

	IAS 39 carrying amount as at December 31, 2017	Re-classification	Re-measurement	IFRS 9 carrying amount as at January 1, 2018
Financial liabilities				
At amortized cost				
Due to banks and other financial institutions	2,691,549	-	-	2,691,549
Customers' deposits	136,048,089	-	-	136,048,089
Other liabilities	3,946,285	-	129,116	4,075,401
Sukuk	2,016,274	-	-	2,016,274
Total amortized cost	144,702,197	-	129,116	144,831,313
At FVTPL				
Negative fair value of derivatives	855,902	-	-	855,902
Total FVTPL	855,902	-	-	855,902

b. Non financial assets

i) Classification of non-financial assets on the date of initial application of IFRS 9

The following table shows the original measurement categories in accordance with IAS 39 and the new measurement categories under IFRS 9 for the Bank's non-financial assets as at January 1, 2018.

	Original carrying value under IAS 39	New carrying value under IFRS 9
Non-financial assets		
Investments in associates	637,222	623,222

ii) Reconciliation of carrying amounts under IAS 39 to carrying amounts under IFRS 9 at the adoption of IFRS 9

The following table reconciles the carrying amounts under IAS 39 to the carrying amounts under IFRS 9 on transition to IFRS 9 on January 1, 2018.

	IAS 39 carrying amount as at December 31, 2017	Re-classification	Re-measurement	IFRS 9 carrying amount as at January 1, 2018
Non-financial assets				
Investments in associates	637,222	-	(14,000)	623,222

(SAR'000)

4. Impact of changes in accounting policies due to adoption of new standards (Continued)

c. Impact on retained earnings and other reserves

Impact of changes to retained earnings and other reserves is summarised as below:

	Retained earnings	Other reserves
Balance as reported (31 December 2017)	3,795,494	(75,807)
Revenue recognition adjustments	(84,544)	-
Reclassifications under IFRS 9	(4,793)	4,793
Recognition of expected credit losses under IFRS 9 (including lease receivables, loan commitments and financial guarantee contracts. including those measured at FVOCI)	(530,990)	-
Recognition of expected credit losses under IFRS 9 resulting from equity-accounting of an associate	(14,000)	-
Balance as adjusted (1 January 2018)	**3,161,167**	**(71,014)**

The following table reconciles the provision recorded as per the requirements of IAS 39 to that of IFRS 9:

- The closing impairment allowance for financial assets in accordance with IAS 39 and provisions for loan commitments and financial guarantee contracts in accordance with IAS 37 Provisions, Contingent Liabilities and Contingent Assets as at December 31, 2017; to
- The opening ECL allowance determined in accordance with IFRS 9 as at January 1, 2018.

	December 31, 2017 (IAS 39/IAS 37)	Re-classification	Re-measurement	January 1, 2018 (IFRS 9)
Loans and receivables (IAS 39)/ Financial assets at amortised cost (IFRS-9)				
Cash and balances with SAMA	-	-	-	-
Due from banks and other financial institutions	-	-	423	423
Investments, net	-	-	15,271	15,271
Loans and advances, net	2,253,542	-	386,180	2,639,722
	2,253,542	-	401,874	2,655,416
Loan commitments and financial guarantee contracts	586,285	-	129,116	715,401
Total	2,839,827	-	530,990	3,370,817

5. Significant Accounting policies

The accounting policies, estimates and assumptions used in the preparation of these interim condensed consolidated financial statements are consistent with those used in the preparation of the annual consolidated financial statements for the year ended December 31, 2017 except for the policies explained below. Based on the adoption of new standards explained in note 4, the following accounting policies are applicable effective January 1, 2018 replacing / amending or adding to the corresponding accounting policies set out in 2017 consolidated financial statements.

5. Significant Accounting policies (continued)

a. Classification of financial assets

On initial recognition, a financial asset is classified as measured at: amortized cost, FVOCI or FVTPL.

Financial Asset at amortised cost

A financial asset is measured at amortized cost if it meets both of the following conditions and is not designated as at FVTPL:

- the asset is held within a business model whose objective is to hold assets to collect contractual cash flows; and
- the contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

Financial Asset at FVOCI

A debt instrument is measured at FVOCI only if it meets both of the following conditions and is not designated as at FVTPL:

- the asset is held within a business model whose objective is achieved by both collecting contractual cash flows and selling financial assets; and
- the contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

FVOCI debt instruments are subsequently measured at fair value with gains and losses arising due to changes in fair value recognised in Other Comprehensive Income (OCI). Interest income and foreign exchange gains and losses are recognised in profit or loss.

Equity Instruments

On initial recognition, for an equity investment that is not held for trading, the Bank may irrecoverably elect to present subsequent changes in fair value in OCI. This election is made on an investment-by-investment basis.

Financial Asset at FVTPL

All other financial assets are classified measured at FVTPL.

In addition, on initial recognition, the Bank may irrevocably designate a financial asset that otherwise meets the requirements to be measured at amortized cost or at FVOCI or at FVTPL if doing so eliminates or significantly reduces an accounting mismatch that would otherwise arise.

Financial assets are not reclassified subsequent to their initial recognition, except in the period after the Bank changes its business model for managing financial assets.

Business model assessment

The Bank assesses the objective of a business model in which an asset is held at a portfolio level because this best reflects the way the business is managed and information is provided to management. The information considered includes:

- the stated policies and objectives for the portfolio and the operation of those policies in practice. In particular, whether management's strategy focuses on earning contractual interest revenue, maintaining a particular interest rate profile, matching the duration of the financial assets to the duration of the liabilities that are funding those assets or realizing cash flows through the sale of the assets;
- how the performance of the portfolio is evaluated and reported to the Bank's management;
- the risks that affect the performance of the business model (and the financial assets held within that business model) and how those risks are managed;
- how managers of the business are compensated- e.g. whether compensation is based on the fair value of the assets managed or the contractual cash flows collected; and
- the frequency, volume and timing of sales in prior periods, the reasons for such sales and its expectations about future sales activity. However, information about sales activity is not considered in isolation, but as part of an overall assessment of how the Bank's stated objective for managing the financial assets is achieved and how cash flows are realized.

5. Significant Accounting policies (continued)

a. Classification of financial assets (continued)

The business model assessment is based on reasonably expected scenarios without taking 'worst case' or 'stress case’ scenarios into account. If cash flows after initial recognition are realised in a way that is different from the Bank's original expectations, the Bank does not change the classification of the remaining financial assets held in that business model, but incorporates such information when assessing newly originated or newly purchased financial assets going forward.

Financial assets that are held for trading and whose performance is evaluated on a fair value basis are measured at FVTPL because they are neither held to collect contractual cash flows nor held both to collect contractual cash flows and to sell financial assets.

Assessments whether contractual cash flows are solely payments of principal and interest

For the purposes of this assessment, 'principal' is the fair value of the financial asset on initial recognition. 'Interest' is the consideration for the time value of money, the credit and other basic lending risks associated with the principal amount outstanding during a particular period and other basic lending costs (e.g. liquidity risk and administrative costs), along with profit margin.

In assessing whether the contractual cash flows are solely payments of principal and interest, the Bank considers the contractual terms of the instrument. This includes assessing whether the financial asset contains a contractual term that could change the timing or amount of contractual cash flows such that it would not meet this condition. In making the assessment, the Bank considers:

- contingent events that would change the amount and timing of cash flows;
- leverage features;
- prepayment and extension terms;
- terms that limit the Bank's claim to cash flows from specified assets (e.g. non-recourse asset arrangements); and
- features that modify consideration of the time value of money- e.g. periodical reset of interest rates.

Designation at fair value through profit or loss

At initial recognition, the Bank may designate certain financial assets at FVTPL. The designated financial assets (if any) are required to be managed, evaluated and reported internally on a fair value basis.

b. Classification of financial liabilities

(Policy applicable before January 1, 2018)

Derivatives embedded in other financial instruments are treated as separate derivatives and recorded at fair value if their economic characteristics and risks are not closely related to those of the host contract, and the host contract is not itself held for trading or designated at fair value through profit or loss. The embedded derivatives separated from the host are carried at fair value in the trading portfolio with changes in fair value recognised in the interim consolidated statement of income.

All money market deposits, customer deposits, term loans, subordinated debts and other debt securities in issue are initially recognized at fair value less transaction costs.

Subsequently, financial liabilities are measured at amortized cost, unless they are required to be measured at fair value through profit or loss or an entity has opted to measure a liability at fair value through profit or loss as per the requirements of IFRS 9.

Financial liabilities classified as FVTPL using fair value option, if any, after initial recognition, for such liabilities, changes in fair value related to changes in own credit risk are presented separately in OCI and all other fair value changes are presented in the income statement.

Amounts in OCI relating to own credit are not recycled to the income statement even when the liability is derecognized and the amounts are realized.

Financial guarantees and loan commitments that entities choose to measure at fair value through profit or loss will have all fair value movements recognized in profit or loss.

5. Significant Accounting policies (continued)

b. Classification of financial liabilities (continued)

(Policy applicable after January 1, 2018)

The Bank classifies its financial liabilities, other than financial guarantees and loan commitments, as measured at amortized cost. Amortized cost is calculated by taking into account any discount or premium on issue funds, and costs that are an integral part of the EIR.

Embedded derivatives

Derivatives may be embedded in another contractual arrangement (a host contract). The Bank accounts for an embedded derivative separately from the host contract when:

Separated embedded derivatives are measured at fair value, with all changes in fair value recognized in profit or loss unless they form part of a qualifying cash flow or net investment hedging relationship. Separated embedded derivatives are presented in the statement of financial position together with the host contract.

c. Derecognition

i) Financial assets

The Bank derecognizes a financial asset when the contractual rights to the cash flows from the financial asset expire, or it transfers the rights to receive the contractual cash flows in a transaction in which substantially all of the risks and rewards of ownership of the financial asset are transferred or in which the Bank neither transfers nor retains substantially all of the risks and rewards of ownership and it does not retain control of the financial asset.

On derecognition of a financial asset, the difference between the carrying amount of the asset (or the carrying amount allocated to the portion of the asset derecognized) and the sum of (i) the consideration received (including any new asset obtained less any new liability assumed) and (ii) any cumulative gain or loss that had been recognized in OCI is recognized in profit or loss.

From January 1, 2018, any cumulative gain/loss recognized in OCI in respect of equity investment securities designated as at FVOCI is not recognized in profit or loss on derecognition of such securities. Any interest in transferred financial assets that qualify for derecognition that is created or retained by the Bank is recognized as a separate asset or liability.

When assets are sold to a third party with a concurrent total rate of return swap on the transferred assets, the transaction is accounted for as a secured financing transaction similar to sale-and- repurchase transactions, as the Bank retains all or substantially all of the risks and rewards of ownership of such assets.

In transactions in which the Bank neither retains nor transfers substantially all of the risks and rewards of ownership of a financial asset and it retains control over the asset, the Bank continues to recognize the asset to the extent of its continuing involvement, determined by the extent to which it is exposed to changes in the value of the transferred asset.

In certain transactions, the Bank retains the obligation to service the transferred financial asset for a fee. The transferred asset is derecognized if it meets the derecognition criteria. An asset or liability is recognized for the servicing contract if the servicing fee is more than adequate (asset) or is less than adequate (liability) for performing the servicing.

Before January 1, 2018, retained interests were primarily classified as available-for-sale investment securities and measured at fair value.

5. Significant Accounting policies (continued)

d. Modifications of financial assets and financial liabilities

i) Financial assets

If the terms of a financial asset are modified, the Bank evaluates whether the cash flows of the modified asset are substantially different. If the cash flows are substantially different, then the contractual rights to cash flows from the original financial asset are deemed to have expired. In this case, the original financial asset is derecognized with the difference recognized as a de-recognition gain or loss and a new financial asset is recognized at fair value.

If the cash flows of the modified asset carried at amortized cost are not substantially different, then the modification does not result in derecognition of the financial asset. In this case, the Bank recalculates the gross carrying amount of the financial asset and recognizes the amount arising from adjusting the gross carrying amount as a modification gain or loss in profit or loss. If such a modification is carried out because of financial difficulties of the borrower, then the gain or loss is presented together with impairment losses. In other cases, it is presented as interest income.

ii) Financial liabilities

The Bank derecognizes a financial liability when its terms are modified and the cash flows of the modified liability are substantially different. In this case, a new financial liability based on the modified terms is recognized at fair value. The difference between the carrying amount of the financial liability extinguished and the new financial liability with modified terms is recognized in profit or loss.

e. Impairment

The Bank recognizes loss allowances for ECL on the following financial instruments that are not measured at FVTPL:

- Due from banks and other financial institutions;
- Financial assets that are debt instruments;
- Lease receivables;
- Loans and advances;
- Financial guarantee contracts issued; and
- Loan commitments issued.

No impairment loss is recognized on equity investments.

The Bank measures loss allowances at an amount equal to lifetime ECL, except for the following, for which they are measured as 12-month ECL:

- debt investment securities that are determined to have low credit risk at the reporting date; and
- other financial instruments on which credit risk has not increased significantly since their initial recognition.

Loss allowances for lease receivables are always measured at an amount equal to lifetime ECL.

The Bank considers a debt security to have low credit risk when their credit risk rating is equivalent to the globally understood definition of 'investment grade'.

12-month ECL are the portion of ECL that result from default events on a financial instrument that are possible within the 12 months after the reporting date.

5. Significant Accounting policies (continued)

e. Impairment (continued)

Measurement of ECL

ECL are a probability-weighted estimate of credit losses. They are measured as follows:

- financial assets that are not credit-impaired at the reporting date: as the present value of all cash shortfalls (i.e. the difference between the cash flows due to the entity in accordance with the contract and the cash flows that the Bank expects to receive);
- financial assets that are credit-impaired at the reporting date: as the difference between the gross carrying amount and the present value of estimated future cash flows;
- undrawn loan commitments: as the present value of the difference between the contractual cash flows that are due to the Bank if the commitment is drawn down and the cash flows that the Bank expects to receive; and
- financial guarantee contracts: the expected payments to reimburse the holder less any amounts that the Bank expects to recover.

Restructured financial assets

If the terms of a financial asset are renegotiated or modified or an existing financial asset is replaced with a new one due to financial difficulties of the borrower, then an assessment is made of whether the financial asset should be derecognized and ECL are measured as follows:

If the expected restructuring will not result in derecognition of the existing asset, and then the expected cash flows arising from the modified financial asset are included in calculating the cash shortfalls from the existing asset.

If the expected restructuring will result in derecognition of the existing asset, then the expected fair value of the new asset is treated as the final cash flow from the existing financial asset at the time of its derecognition. This amount is included in calculating the cash shortfalls from the existing financial asset that are discounted from the expected date of derecognition to the reporting date using the original effective interest rate of the existing financial asset.

Credit-impaired financial assets

At each reporting date, the Bank assesses whether financial assets carried at amortized cost are credit-impaired. A financial asset is 'credit-impaired' when one or more events that have detrimental impact on the estimated future cash flows of the financial asset have occurred.

Evidence that a financial asset is credit-impaired includes the following observable data:

- significant financial difficulty of the borrower or issuer;
- a breach of contract such as a default or past due event;
- the restructuring of a loan or advance by the Bank on terms that the Bank would not consider otherwise;
- it is becoming probable that the borrower will enter bankruptcy or other financial reorganization; or
- the disappearance of an active market for a security because of financial difficulties.

A loan that has been renegotiated due to deterioration in the borrower's condition is usually considered to be credit-impaired unless there is evidence that the risk of not receiving contractual cash flows has reduced significantly and there are no other indicators of impairment. In addition, a retail loan that is overdue for 90 days or more is considered impaired.

5. Significant Accounting policies (continued)

e. Impairment (continued)

Credit-impaired financial assets (continued)

In making an assessment of whether an investment in sovereign debt is credit-impaired, the Bank considers the following factors.

- The market's assessment of creditworthiness as reflected in the bond yields.
- The rating agencies' assessments of creditworthiness.
- The country's ability to access the capital markets for new debt issuance.
- The probability of debt being restructured, resulting in holders suffering losses through voluntary or mandatory debt forgiveness.
- The international support mechanisms in place to provide the necessary support as 'lender of last resort' to that country, as well as the intention, reflected in public statements, of governments and agencies to use those mechanisms. This includes an assessment of the depth of those mechanisms and, irrespective of the political intent, whether there is the capacity to fulfil the required criteria.

Presentation of allowance for ECL in the statement of financial position

Loss allowances for ECL are presented in the statement of financial position as follows:

- financial assets measured at amortized cost: as a deduction from the gross carrying amount of the assets;
- loan commitments and financial guarantee contracts: generally, as a provision;
- where a financial instrument includes both a drawn and an undrawn component, and the Bank cannot identify the ECL on the loan commitment component separately from those on the drawn component: the Bank presents a combined loss allowance for both components. The combined amount is presented as a deduction from the gross carrying amount of the drawn component. Any excess of the loss allowance over the gross amount of the drawn component is presented as a provision; and
- debt instruments measured at FVOCI: no loss allowance is recognized in the statement of financial position because the carrying amount of these assets is their fair value. However, the loss allowance is disclosed and is recognized in the fair value reserve. Impairment losses are recognized in profit and loss and changes between the amortised cost of the assets and their fair value are recognized in OCI.

Write-off

Loans and debt securities are written off (either partially or in full) when there is no realistic prospect of recovery. However, financial assets that are written off could still be subject to enforcement activities in order to comply with the Bank's procedures for recovery of amounts due. If the amount to be written off is greater than the accumulated loss allowance, the difference is first treated as an addition to the allowance that is then applied against the gross carrying amount. Any subsequent recoveries are credited to credit loss expense.

Collateral valuation

To mitigate its credit risks on financial assets, the Bank seeks to use collateral, where possible. The collateral comes in various forms, such as cash, securities, letters of credit/guarantees, real estate, receivables, inventories, other non-financial assets and credit enhancements such as netting agreements. The Bank's accounting policy for collateral assigned to it through its lending arrangements under IFRS 9 is the same is it was under IAS 39. Collateral, unless repossessed, is not recorded on the Bank's statement of financial position. However, the fair value of collateral affects the calculation of ECLs. It is generally assessed, at a minimum, at inception and re-assessed on a periodic basis. However, some collateral, for example, cash or securities relating to margining requirements, is valued daily.

To the extent possible, the Bank uses active market data for valuing financial assets held as collateral. Other financial assets which do not have readily determinable market values are valued using models. Non-financial collateral, such as real estate, is valued based on data provided by third parties such as mortgage brokers, or based on housing price indices.

5. Significant Accounting policies (continued)

e. Impairment (continued)

Collateral repossessed

The Bank's accounting policy under IFRS 9 remains the same as it was under IAS 39. The Bank's policy is to determine whether a repossessed asset can be best used for its internal operations or should be sold. Assets determined to be useful for the internal operations are transferred to their relevant asset category at the lower of their repossessed value or the carrying value of the original secured asset. Assets for which selling is determined to be a better option are transferred to assets held for sale at their fair value (if financial assets) and fair value less cost to sell for non-financial assets at the repossession date in, line with the Bank's policy.

In its normal course of business, the Bank does not physically repossess properties or other assets in its retail portfolio, but engages external agents to recover funds, generally at auction, to settle outstanding debt. Any surplus funds are returned to the customers/obligors. As a result of this practice, the residential properties under legal repossession processes are not recorded on the balance sheet.

f. Financial guarantees and loan commitments

'Financial guarantees' are contracts that require the Bank to make specified payments to reimburse the holder for a loss that it incurs because a specified debtor fails to make payment when it is due in accordance with the terms of a debt instrument. 'Loan commitments' are firm commitments to provide credit under pre-specified terms and conditions.

Financial guarantees issued or commitments to provide a loan at a below-market interest rate are initially measured at fair value and the initial fair value is amortized over the life of the guarantee or the commitment. Subsequently, they are measured as follows:

- from January 1, 2018: at the higher of this amortized amount and the amount of loss allowance; and
- Before January 1, 2018: at the higher of this amortized amount and the present value of any expected payment to settle the liability when a payment under the contract has become probable.

The Bank has issued no loan commitments that are measured at FVTPL. For other loan commitments:

- from January 1, 2018: the Bank recognizes loss allowance;
- Before January 1, 2018: the Bank recognizes a provision in accordance with IAS 37 if the contract was considered to be onerous.

g. Foreign currencies

The consolidated financial statements are presented in Saudi Arabian Riyals ("SAR"), which is also the Bank's functional currency. Each entity determines its own functional currency and items included in the interim consolidated financial statements of each entity are measured using that functional currency.

Transactions in foreign currencies are translated into SAR at exchange rates prevailing on the dates of the transactions. Monetary assets and liabilities at the year-end (other than monetary items that form part of the net investment in a foreign operation), denominated in foreign currencies, are translated into SAR at exchange rates prevailing at the date of the interim consolidated statement of financial position.

The foreign currency gain or loss on monetary items is the difference between amortised cost in the functional currency at the beginning of the year adjusted for the effective profits rate and payments during the year and the amortized cost in foreign currency translated at exchange rate at the end of the year.

Realized and unrealized gains or losses on exchange are credited or charged to the interim consolidated statement of comprehensive income.

Foreign currency differences arising from the translation of the following items are recognized in OCI:

Available-for-sale equity instruments (before January 1, 2018) or equity investments in respect of which an election has been made to present subsequent changes in fair value in OCI (from January 1, 2018);

Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rates as at the dates of the initial transactions. Non-monetary items measured at fair value in a foreign currency are translated using the exchange rates at the date when the fair value is determined.

5. Significant Accounting policies (continued)

g. Foreign currencies (continued)

As at the reporting date, the assets and liabilities of foreign operations are translated into SAR at the rate of exchange as at the statement of financial position date, and their statement of incomes are translated at the weighted average exchange rates for the year. Exchange differences arising on translation are recognized in the statements of other comprehensive income.

When a foreign operation is disposed of such that control, significant influence or joint control is lost, the cumulative amount in the translation reserve related to that foreign operation is reclassified to the statement of income as part of the gain or loss on disposal. When the Group disposes of only part of its interest in a subsidiary that includes a foreign operation while retaining control, the relevant proportion of the cumulative amount is reattributed to non-controlling interests.

h. Revenue/expenses recognition

Special commission income and expenses

Special commission income and expense are recognized in profit or loss using the effective interest method. The 'effective interest rate' is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument to or the amortized cost of the financial instrument.

When calculating the effective interest rate for financial instruments other than credit-impaired assets, the Bank estimates future cash flows considering all contractual terms of the financial instrument, but not expected credit losses. For credit-impaired financial assets, a credit-adjusted effective interest rate is calculated using estimated future cash flows including expected credit losses.

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

Measurement of amortized cost and special commission income

The 'amortized cost' of a financial asset or financial liability is the amount at which the financial asset or financial liability is measured on initial recognition minus the principal repayments, plus or minus the cumulative amortization using the effective interest method of any difference between that initial amount and the maturity amount and, for financial assets, adjusted for any expected credit loss allowance.

The 'gross carrying amount of a financial asset' is the amortized cost of a financial asset before adjusting for any expected credit loss allowance.

In calculating interest income and expense, the effective interest rate is applied to the gross carrying amount of the asset (when the asset is not credit-impaired) or to the amortized cost of the liability.

However, for financial assets that have become credit-impaired subsequent to initial recognition, interest income is calculated by applying the effective interest rate to the amortized cost of the financial asset. If the asset is no longer credit-impaired, then the calculation of interest income reverts to the gross basis.

For financial assets that were credit-impaired on initial recognition, interest income is calculated by applying the credit-adjusted effective interest rate to the amortized cost of the asset. The calculation of interest income does not revert to a gross basis, even if the credit risk of the asset improves.

(SAR'000)

5. Significant Accounting policies (continued)

i. Critical accounting judgements, estimates and assumptions

The preparation of the interim condensed consolidated financial statements in conformity with IFRS requires the use of certain critical accounting judgements, estimates and assumptions that affect the reported amounts of assets and liabilities. It also requires management to exercise its judgement in the process of applying the Bank's accounting policies. Such judgements, estimates, and assumptions are continually evaluated and are based on historical experience and other factors, including obtaining professional advices and expectations of future events that are believed to be reasonable under the circumstances. Revisions to accounting estimates are recognised in the period in which the estimate is revised, if the revision affects only that period, or in the period of revision and in future periods if the revision affects both current and future periods. Significant areas where management has used estimates, assumptions or exercised judgements are as follows:

- Impairment for credit losses on loans & advances (Note 7)
- Fair value Measurement (Note 9)
- Impairment of available for-sale equity and debt investments (Note 6)
- Determination of control over investees
- Provisions for liabilities and charges
- Defined benefit plans
- Going concern

6. Investments, net

Investment securities are classified as follows:

	September 30, 2018 (Unaudited)	December 31, 2017 (Audited)	September 30, 2017 (Unaudited)
Investments:			
Investments at amortized cost	**22,863,345**	21,866,642	17,403,266
Investments at FVOCI - equity	**1,007,840**	-	-
Investments at FVOCI - debt	**3,102,337**	-	-
Available for sale investments (2017)	**-**	10,454,174	8,356,154
Investments at FVTPL (including trading investments)	**512,918**	-	-
Total	**27,486,440**	32,320,816	25,759,420

Equity investment securities designated as at FVOCI

At January 1, 2018, the Bank designated certain investments as equity securities as at FVOCI. In 2017, these investments were classified as available-for-sale and measured at fair value. The FVOCI designation was made because the investments are expected to be held for the long-term for strategic purposes. The fair value of these equity investment securities designated as at FVOCI amounted to SAR 1,007,840 thousands as of September 30, 2018. Dividend income recognized in the interim consolidated statement of income amounted to SAR 41,948 thousands for the period ended September 30, 2018.

(SAR'000)

7. Loans and advances, net

Loans and advances (all held at amortized cost) comprise the following:

September 30, 2018 (Unaudited)	**Overdrafts**	**Credit cards**	**Consumer loans**	**Commercial loans and others**	**Total**
Performing loans and advances-gross	**3,996,026**	**520,293**	**24,204,682**	**92,688,742**	**121,409,743**
Non-performing loans and advances, net	**17,519**	**12,711**	**116,493**	**1,758,377**	**1,905,100**
Total loans and advances	**4,013,545**	**533,004**	**24,321,175**	**94,447,119**	**123,314,843**
Allowance for impairment	**(56,991)**	**(47,402)**	**(439,861)**	**(2,281,154)**	**(2,825,408)**
Loans and advances, net	**3,956,554**	**485,602**	**23,881,314**	**92,165,965**	**120,489,435**

December 31, 2017 (Audited)	Overdrafts	Credit cards	Consumer loans	Commercial loans and others	Total
Performing loans and advances-gross	3,734,884	500,540	24,469,442	86,691,122	115,395,988
Non-performing loans and advances, net	7,487	14,482	103,286	1,275,228	1,400,483
Total loans and advances	3,742,371	515,022	24,572,728	87,966,350	116,796,471
Allowance for impairment	(6,839)	(9,350)	(64,921)	(2,172,432)	(2,253,542)
Loans and advances, net	3,735,532	505,672	24,507,807	85,793,918	114,542,929

September 30, 2017 (Unaudited)	Overdrafts	Credit cards	Consumer loans	Commercial loans and others	Total
Performing loans and advances-gross	3,963,548	535,801	24,313,934	88,802,621	117,615,904
Non-performing loans and advances, net	42,910	14,539	132,670	1,059,646	1,249,765
Total loans and advances	4,006,458	550,340	24,446,604	89,862,267	118,865,669
Allowance for impairment	(38,793)	(8,145)	(140,399)	(2,746,362)	(2,933,699)
Loans and advances, net	3,967,665	542,195	24,306,205	87,115,905	115,931,970

The movement in the allowance for impairment of loans and advances to customers for the period ended September 30, 2018 is as follows:

2018	**Total**
Loss allowance balance as reported at December 31, 2017 (calculated under IAS 39)	**2,253,542**
Amounts restated through opening retained earnings	**386,180**
Adjusted loss allowance balance at January 1, 2018 (calculated under IFRS 9)	**2,639,722**
Charge for the period, net	**722,053**
Bad debts written off against provision	**(536,367)**
Balance at the end of the period	**2,825,408**

Impairment charge for credit losses, net for the period ended September 30, 2018 amounted to SAR 684,299 thousand (September 30, 2017: SAR 473,022 thousand), including bad debts directly written-off to interim consolidated income statement amounting to SAR 68,089 thousand (September 30, 2017: SAR 44,147 thousand) and net of recoveries amounting to SAR 105,843 thousand (September 30, 2017: SAR 103,567 thousand)

Impairment charges for credit losses and other provisions, net as reflected in the interim consolidated statement of income are detailed as follows:

	For the nine month period ended	
	September 30, 2018 (Unaudited)	September 30, 2017 (Unaudited)
Impairment charges for credit losses, net	**684,299**	473,022
(Reversal) provisions for credit-related commitments and contingencies	**(93,258)**	298,184
	591,041	771,206

(SAR'000)

8. Customers' deposits

	September 30, 2018 (Unaudited)	December 31, 2017 (Audited)	September 30, 2017 (Unaudited)
Demand	**64,892,689**	71,003,290	65,456,764
Time	**62,071,746**	58,204,406	59,568,064
Saving	**114,339**	93,944	89,338
Others	**3,751,696**	6,746,449	3,432,740
Total	**130,830,470**	136,048,089	128,546,906

9. Derivatives

The table below sets out the positive and negative fair values of derivative financial instruments, together with their notional amounts, analysed by the term to maturity. The notional amounts, which provide an indication of the volumes of the transactions outstanding at the end of the period, do not necessarily reflect the amounts of future cash flows involved. These notional amounts, therefore, are neither indicative of the Group's exposure to credit risk, which is generally limited to the positive fair value of the derivatives, nor to market risk.

	September 30, 2018 (Unaudited)			December 31, 2017 (Audited)			September 30, 2017 (Unaudited)		
	Positive fair value	**Negative fair value**	**Notional amount**	Positive fair value	Negative fair value	Notional amount	Positive fair value	Negative fair value	Notional amount
Held for trading:									
Commission rate and cross currency swaps	**744,465**	**707,084**	**19,063,898**	443,057	417,595	16,869,829	341,169	316,604	19,684,561
Commission rate futures and options	**787,560**	**785,064**	**14,608,356**	367,552	364,373	11,951,618	292,074	288,703	10,395,596
Forward foreign exchange and commodity contracts	**38,205**	**12,139**	**5,315,522**	50,545	18,959	3,330,684	62,334	27,389	5,117,287
Currency and commodity options	**2,570**	**1,947**	**218,287**	8,869	9,043	1,502,128	12,350	12,204	2,919,851
Held as fair value hedges:									
Commission rate swaps	**572,957**	**7,297**	**17,092,531**	73,737	45,932	16,081,637	27,871	51,238	11,124,727
Total	**2,145,757**	**1,513,531**	**56,298,594**	943,760	855,902	49,735,896	735,798	696,138	49,242,022

Derivatives have been disclosed at gross amounts as at the date of the interim consolidated statement of financial position, and have not been netted off by cash margins placed and received against derivatives, amounting to SAR 469,103 thousands received (December 31, 2017: SAR 41,472 thousands placed, and September 30, 2017: SAR 105,491 thousands placed).

10. Credit related commitments and contingencies

a) The Group is subject to legal proceedings in the ordinary course of business. There was no change in the status of legal proceedings as disclosed at December 31, 2017.

b) The Group's consolidated credit related commitments and contingencies are as follows:

	September 30, 2018 (Unaudited)	December 31, 2017 (Audited)	September 30, 2017 (Unaudited)
Letters of credit	**5,376,892**	4,502,451	4,240,590
Letters of guarantee	**23,651,700**	22,915,086	22,732,279
Acceptances	**1,491,717**	1,305,345	1,567,585
Irrevocable commitments to extend credit	**2,799,886**	3,059,532	2,217,653
Other	**86,800**	94,965	96,482
Total	**33,406,995**	31,877,379	30,854,589

The unutilized portion of non-firm commitments as at September 30, 2018 which can be revoked unilaterally at any time by the Bank, amounts SAR 12,546 million (December 31, 2017: SAR 14,889 million and September 30, 2017: SAR 14,255 million).

(SAR'000)

11. Cash and cash equivalents

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

	September 30, 2018 (Unaudited)	December 31, 2017 (Audited) (Restated)	September 30, 2017 (Unaudited)
Cash and balances with SAMA excluding statutory deposit	**7,027,833**	10,062,660	5,242,785
Due from banks and other financial institutions maturing within 90 days from the acquisition date	**809,744**	1,709,700	3,249,371
Total	**7,837,577**	11,772,360	8,492,156

12. Operating segments

IFRS 8 requires operating segments to be identified on the basis of internal reports about components of the Group that are regularly reviewed by the chief executive officer in order to allocate resources to segments and to assess its performance.

For management purposes, the Group is organized into the following major operating segments:

Retail banking

Deposit, credit and investment products for individuals.

Corporate banking

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

Treasury

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

Investment and brokerage services

Investment management services and asset management activities related to dealing, managing, arranging and advising, and custody of securities.

Other

Includes income on capital and unallocated costs, assets and liabilities pertaining to the Head Office and other supporting departments.

Transactions between the operating segments are reported as recorded in the Group's transfer pricing system. The basis for determining intersegment operating income/(expense) for the current period are consistent with the basis used for September 30, 2017. Segment assets and liabilities comprise mainly operating assets and liabilities.

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

(SAR'000)

12. Operating segments (continued)

The Group's total interim consolidated assets and liabilities as at September 30, 2018 and 2017, its total operating income, expenses and net income for the nine months then ended, by operating segments, are as follows:

September 30, 2018 (Unaudited)	**Retail banking**	**Corporate banking**	**Treasury**	**Investment and brokerage services**	**Other**	**Total**
Total assets	**38,931,415**	**84,856,179**	**42,347,767**	**1,702,324**	**2,127,272**	**169,964,957**
Investments in associates	**-**	**-**	**-**	**-**	**623,418**	**623,418**
Total liabilities	**66,792,909**	**67,282,329**	**7,682,647**	**94,364**	**2,713,451**	**144,565,700**
Operating income from external customers	**1,528,558**	**3,037,275**	**48,715**	**149,021**	**99,764**	**4,863,333**
Intersegment operating income/(expense)	**235,865**	**(1,234,135)**	**815,048**	**-**	**183,222**	**-**
Total operating income	**1,764,423**	**1,803,140**	**863,763**	**149,021**	**282,986**	**4,863,333**
Of which:						
Net special commission income	**1,591,187**	**1,485,199**	**491,728**	**27,467**	**192,777**	**3,788,358**
Fees and commission income, net	**110,489**	**351,525**	**6,856**	**43,944**	**11,828**	**524,642**
Impairment charges for credit losses and other provisions, net	**148,552**	**442,489**	**-**	**-**	**-**	**591,041**
Reversal of impairment charges for other financial assets, net	**-**	**-**	**(7,610)**	**-**	**-**	**(7,610)**
Depreciation and amortization	**77,326**	**6,089**	**1,193**	**1,588**	**68,028**	**154,224**
Total operating expenses	**1,300,720**	**762,678**	**62,865**	**70,571**	**38,678**	**2,235,512**
Share in earnings of associates, net	**-**	**-**	**-**	**-**	**196**	**196**
Net income attributed to equity holders of the Bank	**463,703**	**1,040,462**	**800,898**	**78,450**	**242,193**	**2,625,706**
Net income attributed to non-controlling interest	**-**	**-**	**-**	**-**	**2,311**	**2,311**

September 30, 2017 (Unaudited)	Retail banking	Corporate banking	Treasury	Investment and brokerage services	Other	Total
Total assets	36,551,018	84,377,317	38,804,571	1,718,639	2,191,633	163,643,178
Investments in associates	-	-	-	-	631,527	631,527
Total liabilities	66,341,458	65,465,521	4,742,859	129,455	2,226,924	138,906,217
Operating income from external customers	1,531,930	2,957,485	87,477	123,766	92,634	4,793,292
Intersegment operating income/(expense)	246,007	(1,128,919)	805,156	-	77,756	-
Total operating income	1,777,937	1,828,566	892,633	123,766	170,390	4,793,292
Of which:						
Net special commission income	1,508,204	1,475,671	380,086	14,261	90,005	3,468,227
Fees and commission income, net	226,168	379,558	9,882	47,262	(7,620)	655,250
Impairment charges for credit losses and other provisions, net	244,426	526,780	-	-	-	771,206
Impairment charges for other financial assets, net	-	-	5,970	-	-	5,970
Depreciation and amortization	88,013	4,029	2,871	1,716	70,976	167,605
Total operating expenses	1,299,905	904,110	74,072	71,768	70,969	2,420,824
Share in earnings of associates, net	-	-	-	-	24,963	24,963
Net income attributed to equity holders of the Bank	478,032	924,456	818,561	51,998	119,496	2,392,543
Net income attributed to non-controlling interest	-	-	-	-	4,888	4,888

13. Share capital and earnings per share

As at September 30, 2018, the authorized, issued and fully paid share capital of the Bank consists of 1,000 million shares of SAR 10 each (December 31, 2017 and September 30, 2017: 1,000 million shares of SAR 10 each).

Basic and diluted earnings per share for the periods ended September 30, 2018 and 2017 are calculated by dividing the net income for the period attributable to equity holders of the Bank by 1,000 million shares. The diluted earnings per share is the same as the basic earnings per share.

14. Interim Dividends

The Board of Directors has approved an interim dividend of SAR 650 million (September 30, 2017: SAR 550 million) for distribution to the shareholders from the net income for the period ended September 30, 2018. This interim dividend resulted in a payment to the shareholders of SAR 0.65 per share, net (September 30, 2017: SAR 0.55 per share, net).

15. Financial Risk Management

i) Credit Risk

Credit risk is the risk that a customer or counter-party may not settle an obligation for full value, either when due or at any time thereafter. This risk arises from the potential that a customer or counter-party is either unwilling to perform an obligation or its ability to perform such an obligation is impaired, resulting in an economic loss to the Bank. The Bank is exposed to credit risk when its business units extend credit to counterparties. The Bank's Executive Committee (ExCom)/Board provides oversight of Credit Risk through Credit Policy document.

The enterprise-wide requirements for identification, assessment, monitoring and reporting of credit risk is set by the Risk Management Group, while business/support units are accountable for the credit risks within their respective areas, aligning business strategies with Bank's risk appetite.

Credit Risk policies and procedures are established to provide control on credit portfolios through periodic assessment of the credit standing of borrowers and quantifying maximum permissible exposure to specific borrower. Such individual and/or group exposures are monitored periodically on a portfolio basis . The Bank's Credit Policy provides detailed guidelines to manage credit risk effectively; it is reviewed and updated from time to time based on experience, emerging issues, best market practices and directives from regulatory authorities. The Credit Policy is designed to ensure clear recognition of credit risk management strategies and objectives, which, inter-alia, include:

- Strengthening and enhancing Bank's ability to measure and mitigate credit risks on pre-emptive basis to minimize credit losses.
- Strengthening and enhancing credit portfolio management process.
- Strengthening and enhancing Bank's systems and procedures for early problem recognition.
- Compliance with local regulatory requirement and industry's best practices for credit risk management.

The Policy addresses all functions and activities related to the credit process including the underwriting criteria. It stipulates Bank's appetite for risk, which, inter-alia, provides guidance on the target markets (Corporate, Commercial/Small and Medium Enterprises (SMEs), Consumer and High Net-Worth Individuals) and desirable type of borrowers/industries. Some criteria are product-specific and are governed by individual credit product policies while others generally include credit quality standards, purpose and terms of facilities, undesirable loans, credit analysis, concentrations of credit, repayment ability, compliance with laws & regulations, expected losses and documentation.

Portfolio Monitoring

Portfolio management is ensured through diversification of the credit portfolio on the basis of tenor, industries/business segments, risk grades and geographical areas to avoid the risk of over-exposure to certain economic sectors/credit products, which might be impacted by unfavorable developments in the economy. The Bank broadly uses borrower and sector criteria for mitigating concentration risk. The Bank's business is predominantly concentrated in Saudi Arabia, minimizing cross-currency risk although geographical concentration remains but this is considered acceptable and within Bank's risk appetite.

Consumer Banking portfolio is a diversified one since relatively small exposures are approved to a large number of individuals, based mainly on assignment of salary or security with exposure caps on products/employers, etc.

15. Financial Risk Management (continued)

i) Credit Risk (continued)

Risk Measurement and Reporting System

Credit Risk tracks trends and identifies weaknesses in the quality of corporate, commercial, retail and private banking loans portfolio by employing:

- Obligor and Facility risk rating system to assess the quality of obligor and riskiness of facilities; and
- Periodic reviews and reporting of aggregate statistics on asset diversification and credit quality for key segments of the portfolio.

Rating system is established with the objective to:

- place the responsibility on business units to regularly evaluate credit risk on exposures and identify problems within their portfolios;
- establish early warning signals for detecting deterioration in credit quality;
- set standards for business units to submit their inputs on problematic exposures;
- provide guidelines to respond and take remedial actions as soon as deterioration in credit quality is detected.

The Bank classifies its exposures into 13 risk categories, of which 10 are for performing obligors and 3 are for non-performing obligors. Rating is assigned to a borrower through a system-based methodology, which takes into account financial and non-financial information, translating into a grade and Probability of Default (PD) for the relationship.

Facility Risk Rating (FRR), which assesses the riskiness of facilities, is used for deriving the Loss Given Default (LGD) for a relationship, thus assigning separate rating for obligor and facility characteristics.

Management reports are generated for monitoring and control purposes on periodical basis - monthly, quarterly, semi-annually and annually. These reports are comprehensive, have wide scope and address several issues including:

- Portfolio quality, industry concentration and large exposures;
- Product concentration, credit monitoring and concentration of shares held by the Bank as collateral;
- Past due follow-up, customer-provisioning details and provision movement.

Retail portfolio comprises of personal loans, credit cards, housing loans and auto leasing.

Individual customers are assessed on the basis of standardized pre-set criteria for specific schemes to assess eligibility for each of the above products. Delinquent customers, based on days past due (bucket-wise), are classified as non-performing.

Major portion of retail portfolio is personal loans, which are granted against salary assignments to borrowers who are employees of approved list of acceptable employers, mainly government departments. The main criteria for lending to this portfolio include approved employer, minimum salary requirements, length of service and pre-specified Debt Service Ratio (DSR). Housing loan and auto leasing products are considered generally secured since the underlying assets are owned by the Bank and leased to customers, thus mitigating risk to a large extent.

The Bank has developed application score-cards and behavior score-cards, using internal and external data, to evaluate, monitor and control consumer credits as this is expected to go a long way in making consumer credit risk management more effective and efficient.

a. Amounts arising from ECL – Significant increase in credit risk

When determining whether the risk of default on a financial instrument has increased significantly since initial recognition, the Bank considers reasonable and supportable information that is relevant and available without undue cost or effort. This includes both quantitative and qualitative information and analysis, based on the Bank's historical experience and expert credit assessment and including forward-looking information.

15. Financial Risk Management (continued)

i) Credit Risk (continued)

a. Amounts arising from ECL – Significant increase in credit risk (continued)

Credit risk grades

The Bank allocates credit risk grades to each exposure based on a variety of variables that is determined to be predictive of the risk of default and applying experienced credit judgment. Credit risk grades are defined using qualitative and quantitative factors that are indicative of risk of default. These factors vary depending on the nature of the exposure and the type of borrower.

Credit risk grades are defined and calibrated such that the risk of default occurring increases significantly as the credit risk deteriorates so, for example, the difference in risk of default between credit risk grades 1 and 2 is smaller than the difference between credit risk grades 8 and 9.

Credit risk grade or score is allocated to corporate exposures at initial recognition based on available information about the borrower. Exposures are subject to ongoing monitoring, which may result in an exposure being moved to a different credit risk grade or score. The monitoring of exposures involve use of the following data:

Corporate exposures	Retail exposures
• Information obtained during periodic review of customer files – e.g. audited financial statements, management accounts, budgets and projections. Examples of areas of particular focus are: gross profit margins, financial leverage ratios, debt service coverage, compliance with covenants, quality of management, etc. and senior management changes. • Data from credit reference agencies, press articles, changes in external credit ratings. • Quoted bond and credit default swap (CDS) prices for the borrower where available. • Actual and expected significant changes in the political, regulatory and technological environment of the borrower or in its business activities.	• Internally collected data and customer behavior data – e.g. utilization of credit card facilities • Affordability metrics • External data from credit reference agencies including default information.

i) Generating the term structure of PD

Credit risk grades are a primary input in the determination of the term structure of PD for exposures. The Bank collects performance and default information about its credit risk exposures analyzed by type of product and borrower as well as by credit risk grading. For retail portfolios, SIMAH information is also used.

The Bank employs statistical models to analyze the data collected and generate estimates of the remaining lifetime PD of exposures and how these are expected to change over a period of time.

This analysis includes the identification and calibration of relationships between changes in default rates and macro-economic factors. For most exposures, key macro-economic indicators include Oil Price, GDP growth, Government Expenditures, Share Price Index and Employment.

Based on the available economic data and consideration of a variety of external actual and forecast information, the Bank formulates a 'base case' view of the future direction of relevant economic variables as well as a representative range of other possible forecast scenarios.. The Bank then uses these forecasts to adjust its estimates of PDs.

15. Financial Risk Management (continued)

i) Credit Risk (continued)

a. Amounts arising from ECL – Significant increase in credit risk (continued)

ii) Determining whether credit risk has increased significantly

The criteria for determining whether credit risk has increased significantly vary by portfolio and include quantitative changes in PDs and a backstop based on delinquency.

Using its expert credit judgment and, where possible, relevant historical experience, the Bank may determine that an exposure has undergone a significant increase in credit risk based on particular qualitative indicators that it considers are indicative of such and whose effect may not otherwise be fully reflected in its quantitative analysis on a timely basis.

As a backstop, the Bank considers that a significant increase in credit risk occurs no later than when an asset is more than 30 days past due. Days past due are determined by counting the number of days since the earliest elapsed due date when full payment became due.

The Bank monitors the effectiveness of the criteria used to identify significant increases in credit risk by regular reviews to confirm that:

- the criteria are capable of identifying significant increases in credit risk before an exposure is in default;
- the criteria do not align with the point in time when an asset becomes 30 days past due; and
- there is no unwarranted volatility in loss allowance from transfers between 12-month PD (stage 1) and lifetime PD (stage 2).

iii) Modified financial assets

The contractual terms of a loan may be modified for a number of reasons, including changing market conditions, customer retention and other factors not related to a current or potential credit deterioration of the customer. An existing loan whose terms have been modified may be derecognized and the renegotiated loan recognized as a new loan at fair value in accordance with the accounting policy.

When the terms of a financial asset are modified and the modification does not result in de-recognition, the determination of whether the asset's credit risk has increased significantly reflects comparison of:

- its remaining Net Present Value (NPV) of the cash-flows at the reporting date based on the modified terms; with
- the remaining NPV of the cash-flows calculated based on data at initial recognition and the original contractual terms.

The Bank renegotiates loans to customers in financial difficulties to maximize collection opportunities and minimize the risk of default. As per Bank's policy, loan restructuring is granted on a selective basis if the debtor is currently in default on its debt or if there is a high risk of default, there is evidence that the debtor made all reasonable efforts to pay under the original contractual terms and the debtor is expected to be able to meet the revised terms.

The revised terms usually include extending the maturity, changing the timing of interest payments and amending the terms of loan covenants. Both retail and corporate loans are subject to the restructuring policy.

For financial assets modified as part of the Bank's policy, the estimate of PD reflects whether the modification has improved or restored the Bank's ability to collect interest and principal and the Bank's previous experience of similar restructuring action. As part of this process, the Bank evaluates the borrower's payment performance against the modified contractual terms and considers various behavioral indicators.

15. Financial Risk Management (continued)

i) Credit Risk (continued)

a. Amounts arising from ECL – Significant increase in credit risk (continued)

iii) Modified financial assets (continued)

Generally, restructuring is a qualitative indicator of a significant increase in credit risk and an expectation of restructuring may constitute evidence that an exposure is credit-impaired /in default. A customer needs to demonstrate consistently good payment behavior over a period of time before the exposure is no longer considered to be credit-impaired/ in default or the PD is considered to have decreased such that the loss allowance reverts to being measured at an amount equal to 12-month ECL.

iv) Definition of 'Default'

The following criteria are used to determine obligor default. The obligor:

- Has an obligation which is 90 (or more) days past due.
- Has an obligation for which the Bank has stopped accruing interest.
- Has obligation(s) that has/have been restructured with loss to the Bank.
- Has an obligation that is classified as non-performing by the Bank.
- Has an obligation that the Bank has charged off in part or in full.

In assessing whether a borrower is in default, the Bank considers indicators that are:

- qualitative- e.g. breaches of covenant;
- quantitative- e.g. overdue status and non-payment on another obligation of the same issuer to the Bank; and
- based on data developed internally and obtained from external sources.

Inputs to the assessment of whether a financial instrument is in default and their significance may vary over time to reflect changes in circumstances.

The definition of default largely aligns with that applied by the Bank for regulatory capital purposes.

v) Incorporation of forward looking information

The Bank incorporates forward-looking information into both its assessment of whether the credit risk of an instrument has increased significantly since its initial recognition and its measurement of ECL. Based on consideration of a variety of actual and forecast information, the Bank formulates a 'base case' view of the future direction of relevant economic variables as well as a representative range of other possible forecast scenarios. This process involves developing two or more additional economic scenarios and considering the relative probabilities of each outcome. External information includes economic data and forecasts published by agencies, such as Moody's Economic Data services.

The base case represents a most-likely outcome and is aligned with information used by the Bank for other purposes such as strategic planning and budgeting. The other scenarios represent more optimistic and pessimistic outcomes. Periodically, the Bank carries out stress testing of more extreme shocks to calibrate its determination of these other representative scenarios.

The Bank has identified and documented key drivers of credit risk and credit losses for each portfolio using an analysis of historical data and estimated relationships between macro-economic variables and credit risk and credit losses. The economic scenarios used as at September 30, 2018 included the following ranges of key indicators.

Oil Price
GDP growth
Employment rates
Government Expenditures
Share Price Index

Predicted relationships between the key indicators and default and loss rates on various portfolios of financial assets have been developed based on analyzing historical data over the past 10 to 15 years.

15. Financial Risk Management (continued)

i) Credit Risk (continued)

a. Amounts arising from ECL – Significant increase in credit risk (continued)

vi) Measurement of ECL

The key inputs into the measurement of ECL are the term structure of the following variables:

i. Probability of default (PD);
ii. Loss given default (LGD);
iii. Exposure at default (EAD).

These parameters are generally derived from internally developed statistical models and other historical data. They are adjusted to reflect forward-looking information as described above.

PD estimates are estimates at a certain date, which are calculated, based on statistical rating models, and assessed using rating tools tailored to the various categories of counterparties and exposures. These statistical models are based on internally and externally compiled data comprising both quantitative and qualitative factors. Where it is available, market data may also be used to derive the PD for large corporate counterparties. If a counterparty or exposure migrates between rating classes, then this will lead to a change in the estimate of the associated PD.

LGD is the magnitude of the likely loss if there is a default. The Bank estimates LGD parameters based on the history of recovery rates of claims against defaulted counterparties. The LGD models consider the structure, collateral and recovery costs of any collateral that is integral to the financial asset. For secured retail loans, asset value / type are a key parameter in determining LGD. LGD estimates are recalibrated for different economic scenarios. They are calculated on a discounted cash flow basis using the effective interest rate as the discounting factor.

EAD represents the expected exposure in the event of a default. The Bank derives the EAD from the current exposure to the counterparty and potential changes to the current amount allowed under the contract including amortization. The EAD of a financial asset is its gross carrying amount. For lending commitments and financial guarantees, the EAD includes the amount drawn, as well as potential future amounts that may be drawn under the contract, which are estimated based on historical observations and forward-looking forecasts. For some financial assets, EAD is determined by modeling the range of possible exposure outcomes at various points in time using scenario and statistical techniques.

As described above and subject to using a maximum of a 12-month PD for financial assets for which credit risk has not significantly increased, the Bank measures ECL considering the risk of default over the maximum contractual period (including any borrower's extension options) over which it is exposed to credit risk, even if, for risk management purposes, the Bank considers a longer period. The maximum contractual period extends to the date at which the Bank has the right to require repayment of an advance or terminate a loan commitment or guarantee.

However, for overdrafts and credit card facilities that include both a loan and an undrawn commitment component, the Bank measures ECL over a period longer than the maximum contractual period if the Bank's contractual ability to demand repayment and cancel the undrawn commitment does not limit the Bank's exposure to credit losses to the contractual notice period. These facilities do not have a fixed term or repayment structure and are managed on a collective basis. The Bank can cancel them with immediate effect, however this contractual right is not enforced in the normal day-to-day management but only when the Bank becomes aware of significant increase in credit risk at the facility level, prompting such action. This longer period is estimated taking into account the credit risk management actions that the Bank expects to take and that serve to mitigate ECL. These include a reduction in limits cancellation of the facility and/or turning the outstanding balance into a loan with fixed repayment terms.

(SAR'000)

15. Financial Risk Management (continued)

i) Credit Risk (continued)

b. Loss allowance

The following table shows reconciliations from the opening to the closing balance of the loss allowance by class of financial instruments.

September 30, 2018 (Unaudited)	**12 month ECL**	**Life time ECL not credit impaired**	**Lifetime ECL credit impaired**	**Total**
Loans and advances to customers at amortized cost				
Balance at January 1, 2018	**390,196**	**1,174,118**	**1,075,408**	**2,639,722**
Transfer to 12-month ECL	**34,998**	**(25,368)**	**(9,630)**	**-**
Transfer to lifetime ECL not credit - impaired	**(35,015)**	**61,848**	**(26,833)**	**-**
Transfer to lifetime ECL credit impaired	**(2,327)**	**(71,946)**	**74,273**	**-**
Net charge for the period	**1,920**	**(193,036)**	**913,169**	**722,053**
Write-offs	**-**	**-**	**(536,367)**	**(536,367)**
Balance at September 30, 2018	**389,772**	**945,616**	**1,490,020**	**2,825,408**

For "Lifetime ECL credit impaired (Stage 3)", it includes loss allowance for NPL portfolio along with the impact of other factors related to IFRS 9.

c. Collateral

In the ordinary course of lending activities, the Bank hold collaterals as security to mitigate credit risk. These collaterals mostly include time, demand, and other cash deposits, financial guarantees, local and international equities, real estate and other fixed assets. The collaterals are held mainly against commercial loans and are managed against relevant exposures at their net realizable values. For financial assets that are credit impaired at the reporting period, quantitative information about the collateral held as security is needed to the extent that such collateral mitigates credit risk.

16. Fair values of financial assets and liabilities

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The fair value measurement is based on the presumption that the transaction to sell the asset or transfer the liability takes place either:

i) In the accessible principal market for the asset or liability; or
ii) In the absence of a principal market, in the most advantageous accessible market for the asset or liability.

The fair values of on-balance sheet financial instruments are not significantly different from their carrying amounts included in the interim condensed consolidated financial statements.

Determination of fair value and fair value hierarchy

The Bank uses the following hierarchy for determining and disclosing the fair value of financial instruments:

Level 1: quoted prices in active markets for the same instrument (i.e., without modification or repacking);

Level 2: quoted prices in active markets for similar assets and liabilities or other valuation techniques for which all significant inputs are based on observable market data; and

Level 3: valuation techniques for which any significant input is not based on observable market data.

a. Carrying amounts and fair value

The following table shows the carrying amount and fair values of financial assets and financial liabilities, including their levels in the fair value hierarchy for financial instruments. It does not include fair value hierarchy information for financial assets and financial liabilities not measured at fair value if the carrying amount is a reasonable approximation of fair value.

(SAR'000)

16. Fair values of financial assets and liabilities (continued)

a. Carrying amounts and fair value (continued)

Financial assets

September 30, 2018 (Unaudited)	**Carrying value**	**Fair value**			
		Level 1	**Level 2**	**Level 3**	**Total**
Financial assets measured at fair value					
Investments at FVTPL (including trading investments)	**512,918**	**-**	**40,339**	**472,579**	**512,918**
Investments at FVOCI	**4,110,177**	**3,031,556**	**1,076,728**	**1,893**	**4,110,177**
Positive fair value of derivatives	**2,145,757**	**-**	**2,145,757**	**-**	**2,145,757**
Financial assets not measured at fair value					
Due from banks and other financial institutions	**809,744**	**-**	**-**	**-**	**809,744**
Investments at amortised cost	**22,863,345**	**405,730**	**22,320,645**	**-**	**22,726,375**
Loans and advances	**120,489,435**	**-**	**-**	**122,269,357**	**122,269,357**

December 31, 2017 (Audited)	Carrying value	Fair value			
		Level 1	Level 2	Level 3	Total
Financial assets measured at fair value					
Available for sale investments	10,454,174	9,536,248	907,210	10,716	10,454,174
Positive fair value of derivatives	943,760	-	943,760	-	943,760
Financial assets not measured at fair value					
Due from banks and other financial institutions	1,710,123	-	-	-	1,710,123
Investments at amortised cost	21,866,642	465,373	21,293,723	-	21,759,096
Loans and advances	114,542,929	-	-	116,229,580	116,229,580

Financial Liabilities

September 30, 2018 (Unaudited)	**Carrying value**	**Fair value**			
		Level 1	**Level 2**	**Level 3**	**Total**
Financial liabilities measured at fair value					
Negative fair value of derivatives	**1,513,531**	**-**	**1,513,531**	**-**	**1,513,531**
Financial liabilities not measured at fair value					
Due to banks and other financial institutions	**3,810,078**	**-**	**-**	**-**	**3,810,078**
Customer deposits	**130,830,470**	**-**	**-**	**-**	**130,830,470**
Sukuk	**2,037,706**	**-**	**-**	**2,031,960**	**2,031,960**

(SAR'000)

16. Fair values of financial assets and liabilities (continued)

a. Carrying amounts and fair value (continued)

Financial Liabilities (continued)

December 31, 2017 (Audited)	Carrying value	Fair value			
		Level 1	Level 2	Level 3	Total
Financial liabilities measured at fair value					
Negative fair value of derivatives	855,902	-	855,902	-	855,902
Financial liabilities not measured at fair value					
Due to banks and other financial institutions	2,691,549	-	-	-	2,691,549
Customer deposits	136,048,089	-	-	-	136,048,089
Sukuk	2,016,274	-	-	1,985,606	1,985,606

b. Measurement of fair values

i. Transfer between levels of the fair value hierarchy

There have been no transfers within levels of the fair value hierarchy during the nine months period ended September 30, 2018 and 2017.

ii. Level 3 fair values

Reconciliation of Level 3 fair values

The following table shows a reconciliation from the opening balances for Level 3 fair values.

	September 30, 2018 (Unaudited)	
	Investments at FVTPL	**Investments at FVOCI**
Balance at the beginning of the period	**-**	**-**
Transferred from available for sale financial assets at initial application of IFRS 9	**8,823**	**1,893**
Total unrealized gain in interim consolidated statement of income	**16,122**	**-**
Settlements	**(2,366)**	**-**
Purchases	**450,000**	**-**
Balance at the end of the period	**472,579**	**1,893**

Financial investments held as available for sale (2017):

The following table shows a reconciliation from the opening balances to the closing balances for Level 3 fair values.

	September 30, 2018 (Unaudited)	September 30, 2017 (Unaudited)
Balance at the beginning of the period	**10,716**	24,215
Transferred to FVTPL at initial application of IFRS 9	**(8,823)**	-
Transferred to FVOCI at initial application of IFRS 9	**(1,893)**	-
Total unrealized losses in other comprehensive income	**-**	(39)
Settlements	**-**	(14,659)
Balance at the end of the period	**-**	9,517

16. Fair values of financial assets and liabilities (continued)

b. Measurement of fair values (continued)

iii. Valuation technique and significant unobservable inputs

The following table shows the valuation techniques used in measuring level 2 and Level 3 fair values at September 30, 2018 and December 31, 2017 as well as the significant unobservable inputs used.

Type	**Valuation technique**	**Significant unobservable inputs**	**Inter-relationship between significant unobservable inputs and fair value measurement**
FVTPL investments	Fair value is determined based on the investee fund's most recent reported net assets value of the funds.	None	Not applicable
FVOCI / Available for sale (2017) investments classified as Level 2 include plain vanilla bonds for which market quotes are not available.	Fair valued using simple discounted cash flow techniques that use observable market data inputs for yield curves and credit spreads.	None	Not applicable
FVOCI / Available for sale (2017) investments classified as Level 3 include Private Equity Funds	Fair value is determined based on the fund's most recent reported net assets value of the funds.	None	Not applicable
Derivatives classified as Level 2 are comprised of over the counter special commission rate swaps, cross currency swaps, special commission rate futures and options, forward foreign exchange contracts, currency and commodity options and other derivative financial instruments	These instruments are fair valued using the Bank's proprietary valuation models that are based on discounted cash flow techniques. The data inputs on these models are based on observable market parameters relevant to the markets in which they are traded and are sourced from widely used market data service providers.	None	Not applicable
Financial assets and liabilities that are disclosed at fair value and classified as Level 2 include investments held at amortized cost.	These instruments are fair valued using simple discounted cash flow techniques that use observable market data inputs for yield curves and credit spreads.	Additional buffer is added to account for any potential model discrepancy or any stressed market conditions.	Not applicable
Financial assets and liabilities that are disclosed at fair value and classified as Level 3 include loans and advances and debt issuances.	These instruments are fair valued using simple discounted cash flow techniques that use observable market data inputs for yield curves and credit spreads.	Additional buffer is added to the credit spreads to account for any potential model discrepancy or any stressed market conditions.	The higher the credit spread, the lower is the valuation; vice versa.

(SAR'000)

17. Capital Adequacy

The Group's objectives when managing capital are, to comply with the capital requirements set by SAMA; to safeguard the Group's ability to continue as a going concern; and to maintain a strong capital base. During the period, the Group has fully complied with regular capital requirements.

The Group monitors the adequacy of its capital using ratios established by SAMA. These ratios measure capital adequacy by comparing the Group's eligible capital with its interim consolidated statement of financial position assets, commitments and notional amount of derivatives at a weighted amount to reflect their relative risk.

SAMA has issued the framework and guidance regarding implementation of the capital reforms under Basel III – which are effective starting January 1, 2013. Accordingly, the Group's pillar I consolidated Risk Weighted Assets (RWA), total capital and related ratios are as follows:

	September 30, 2018 (Unaudited)	December 31, 2017 (Audited)	September 30, 2017 (Unaudited)
Credit Risk RWA	**149,342,121**	138,475,268	143,487,130
Operational Risk RWA	**13,536,670**	13,253,250	13,269,300
Market Risk RWA	**1,843,793**	608,966	1,703,666
Total Pillar-I RWA	**164,722,584**	152,337,484	158,460,096
Tier I Capital	**25,166,479**	23,719,687	24,042,881
Tier II Capital	**2,479,389**	3,026,724	3,066,451
Total Tier I & II Capital	**27,645,868**	26,746,411	27,109,332
Capital Adequacy Ratio %			
Tier I ratio	**15.28%**	15.57%	15.17%
Tier I + Tier II ratio	**16.78%**	17.56%	17.11%

The Group maintains an actively managed capital base to cover risks inherent in the business. The adequacy of the Group's capital is monitored using, among other measures, the rules and ratios established by the Basel Committee on Banking Supervision as adopted by the SAMA in supervising the Bank.

18. Comparative figures

During the current period, rental income from a subsidiary relating to prior period have been reclassified from "Fee and commission income, net" to "Other operating income, net" in the interim consolidated income statement to conform to the current period's presentation.

The impact of this reclassification on the interim consolidated statement of income is disclosed below:

September 30, 2017 (unaudited)

For the three months period ended	As originally reported	Reclassification	Amounts reported after reclassification
Fees and commission income, net	206,613	(26,124)	180,489
Other operating income, net	32,808	26,124	58,932
	239,421	-	239,421

For the nine months period ended	As originally reported	Reclassification	Amounts reported after reclassification
Fees and commission income, net	732,231	(76,981)	655,250
Other operating income, net	77,215	76,981	154,196
	809,446	-	809,446

19. Board of Directors' approval

The interim condensed consolidated financial statements were approved by the Board on Safar 14, 1440 (corresponding to October 23, 2018).