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# **BANK ALJAZIRA**

**(A Saudi Joint Stock Company)**

**UNAUDITED INTERIM CONDENSED  
CONSOLIDATED FINANCIAL STATEMENTS  
FOR THE THREE MONTH AND NINE MONTH  
PERIODS ENDED 30 SEPTEMBER 2018**

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Ernst & Young & Co. (Public Accountants)  
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King Abdulaziz Road  
P. O. Box 1994  
Jeddah 21441  
Kingdom of Saudi Arabia  
Registration Number: 45



Al Fozan & Partners  
Certified Public Accountants  
9th Floor, Zahran Business Centre  
Prince Sultan Street  
P. O. Box 55078  
Jeddah 21534  
Kingdom of Saudi Arabia  
License No. 46/11/323 issued 11/3/1992

## **Independent Auditors' Report on Review of Interim Condensed Consolidated Financial Statements**

To the Shareholders of Bank AlJazira  
(A Saudi Arabian Joint Stock Company)

### ***Introduction***

We have reviewed the accompanying interim condensed consolidated statement of financial position of Bank AlJazira (the "Bank") and its subsidiaries (collectively referred to as the "Group") as at 30 September 2018 and the related interim condensed consolidated statements of income and comprehensive income for the three month and nine month periods then ended and the interim condensed consolidated statements of changes in equity and cash flows for the nine month period then ended and the notes which form an integral part of these 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 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 condensed consolidated financial statements 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 ('ISAs'), as 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 matter***

As required by SAMA, certain capital adequacy information has been disclosed in note 19 of the accompanying interim condensed consolidated financial statements. As part of our review, we compared the information in note 19 to the relevant analysis prepared by the Bank for submission to SAMA and found no material inconsistencies.

for Ernst & Young  
(Public Accountants)

Ahmed I. Reda  
Certified Public Accountant  
License Number 356



for KPMG Al Fozan & Partners  
Certified Public Accountants

Khalil Ibrahim Al Sedais  
Certified Public Accountant  
License Number 371



23 Safar 1440H  
Corresponding to 1 November 2018

# Bank AlJazira

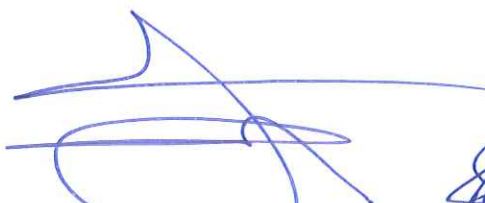
(A Saudi Joint Stock Company)

## INTERIM CONDENSED CONSOLIDATED STATEMENT OF FINANCIAL POSITION

	Notes	30 September 2018 (Unaudited) SR'000	31 December 2017 (Audited) SR'000	30 September 2017 (Unaudited) SR'000
<b>ASSETS</b>				
Cash and balances with SAMA	15	4,560,067	5,975,067	3,841,706
Due from banks and other financial institutions		464,384	369,249	474,093
Investments	6	24,645,392	20,360,547	20,401,371
Positive fair value of derivatives	10	92,637	104,021	113,964
Loans and advances	7	40,255,184	39,789,846	40,926,323
Investment in an associate	8	133,163	134,071	131,789
Other real estate		451,748	445,046	445,046
Property and equipment		768,061	784,526	775,282
Other assets		360,387	325,082	418,758
<b>Total assets</b>		<b>71,731,023</b>	<b>68,287,455</b>	<b>67,528,332</b>
<b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>				
<b>LIABILITIES</b>				
Due to banks and other financial institutions		6,798,339	6,172,545	6,216,824
Customers' deposits	9	50,210,745	50,278,366	49,676,106
Negative fair value of derivatives	10	137,409	220,987	267,541
Subordinated Sukuk	11	2,030,175	2,006,382	2,025,792
Other liabilities		908,558	780,336	734,765
<b>Total liabilities</b>		<b>60,085,226</b>	<b>59,458,616</b>	<b>58,921,028</b>
<b>SHAREHOLDERS' EQUITY</b>				
Share capital	12	8,200,000	5,200,000	5,200,000
Statutory reserve		2,159,483	2,159,483	1,945,105
General reserve		68,000	68,000	68,000
Other reserves	13	(44,797)	(125,185)	(154,339)
Retained earnings		1,263,111	1,526,541	1,548,538
<b>Total shareholders' equity</b>		<b>11,645,797</b>	<b>8,828,839</b>	<b>8,607,304</b>
<b>Total liabilities and shareholders' equity</b>		<b>71,731,023</b>	<b>68,287,455</b>	<b>67,528,332</b>



Tarek Al-Kasabi  
Chairman



Nabil Al-Hoshan  
CEO and Managing Director



Shahid Amin  
Chief Financial Officer



The accompanying notes 1 to 22 form an integral part of these interim condensed consolidated financial statements.

# Bank AlJazira

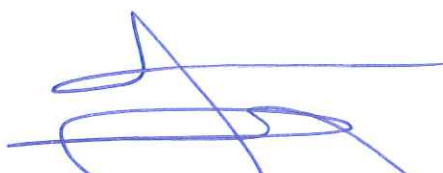
(A Saudi Joint Stock Company)

## INTERIM CONDENSED CONSOLIDATED STATEMENT OF INCOME (UNAUDITED) FOR THE THREE MONTH AND NINE MONTH PERIODS ENDED 30 SEPTEMBER 2018

	For the three month period ended		For the nine month period ended	
	30 September 2018	30 September 2017	30 September 2018	30 September 2017
Notes	SR'000	SR'000	SR'000	SR'000
Special commission income	702,799	632,946	1,998,319	1,857,649
Special commission expense	(215,602)	(162,863)	(556,778)	(500,143)
<b>Net special commission income</b>	<b>487,197</b>	<b>470,083</b>	<b>1,441,541</b>	<b>1,357,506</b>
Fees and commission income, net	140,859	146,823	437,359	455,159
Exchange income, net	53,656	44,870	141,365	107,063
Trading (loss) / income, net	(4,439)	6,052	(1,815)	9,190
Other operating income	1,933	1,417	5,082	2,738
<b>Total operating income</b>	<b>679,206</b>	<b>669,245</b>	<b>2,023,532</b>	<b>1,931,656</b>
Salaries and employee-related expenses	231,213	208,704	682,756	644,188
Rent and premises-related expenses	34,526	33,217	103,625	103,154
Depreciation and amortisation	23,120	22,055	67,749	64,192
Other general and administrative expenses	110,891	94,531	333,072	269,251
Impairment charge for credit losses, net	21,448	85,429	75,467	194,175
Other operating expenses	5,200	782	14,768	1,224
<b>Total operating expenses</b>	<b>426,398</b>	<b>444,718</b>	<b>1,277,437</b>	<b>1,276,184</b>
<b>Operating income</b>	<b>252,808</b>	<b>224,527</b>	<b>746,095</b>	<b>655,472</b>
Share in net income of an associate	2,278	3,105	7,678	8,290
<b>Net income for the period</b>	<b>255,086</b>	<b>227,632</b>	<b>753,773</b>	<b>663,762</b>
<b>Basic earnings per share for the period – restated (expressed in SR per share)</b>	<b>0.31</b>	<b>0.40</b>	<b>1.03</b>	<b>1.17</b>



Tarek Al-Kasabi  
Chairman



Nabil Al-Hoshan  
CEO and Managing Director



Shahid Amin  
Chief Financial Officer

The accompanying notes 1 to 22 form an integral part of these interim condensed consolidated financial statements.

*Yasmin Al-Mutairi*




# Bank AlJazira


(A Saudi Joint Stock Company)

## INTERIM CONDENSED CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME (UNAUDITED) FOR THE THREE MONTH AND NINE MONTH PERIODS ENDED 30 SEPTEMBER 2018

		For the three month period ended		For the nine month period ended	
		30 September 2018	30 September 2017	30 September 2018	30 September 2017
	Notes	SR'000	SR'000	SR'000	SR'000
Net income for the period		255,086	227,632	753,773	663,762
<b>Other comprehensive income:</b>					
<i>Items that can be reclassified to consolidated statement of income in subsequent periods:</i>					
Cash flow hedges:					
- Effective portion of change in the fair value	13	3,935	56,549	69,962	55,107
- Net amount transferred to consolidated statement of income	13	124	50	206	193
<i>Items that cannot be reclassified to consolidated statement of income in subsequent periods:</i>					
- Net changes in fair value of investments classified as at Fair Value Through Other Comprehensive Income (FVOCI) – equity	13	-	1,182	23	2,876
<b>Other comprehensive income for the period</b>		<b>4,059</b>	<b>57,781</b>	<b>70,191</b>	<b>58,176</b>
<b>Total comprehensive income for the period</b>		<b>259,145</b>	<b>285,413</b>	<b>823,964</b>	<b>721,938</b>

  
Tarek Al-Kasabi  
Chairman

  
Nabil Al-Hoshan  
CEO and Managing Director

  
Shahid Amin  
Chief Financial Officer

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*Handwritten signature and stamp:*  
Yasir  
\*Allah

# Bank AlJazira

(A Saudi Joint Stock Company)

## INTERIM CONDENSED CONSOLIDATED STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY (UNAUDITED) FOR THE NINE MONTH PERIOD ENDED 30 SEPTEMBER 2018

	Notes	Share capital SR'000	Statutory reserve SR'000	General reserve SR'000	Other reserves SR'000	Retained earnings SR'000	Proposed dividend SR'000	Total shareholders' equity SR'000
Balance at 1 January 2018 (audited)		5,200,000	2,159,483	68,000	(125,185)	1,526,541	-	8,828,839
Impact of adoption of IFRS 9 at 1 January 2018	4(II)	-	-	-	-	(636,157)	-	(636,157)
Balance at 1 January 2018 - restated		5,200,000	2,159,483	68,000	(125,185)	890,384	-	8,192,682
Net income for the period		-	-	-	-	753,773	-	753,773
Other comprehensive income		-	-	-	70,191	-	-	70,191
Gain on sale of investment classified as at FVOCI	6(a)	-	-	-	(10,951)	10,951	-	-
Total comprehensive income for the period		-	-	-	59,240	764,724	-	823,964
Zakat and income tax		-	-	-	-	(25,648)	-	(25,648)
Share in Zakat of an associate		-	-	-	-	(11)	-	(11)
Issue of right shares	12	3,000,000	-	-	-	-	-	3,000,000
Proposed dividend	20	-	-	-	-	(262,400)	262,400	-
Dividend paid		-	-	-	-	-	(252,802)	(252,802)
Adjustments in proposed dividend		-	-	-	-	9,598	(9,598)	-
Transfer of gain on investment at FVOCI to other liabilities		-	-	-	-	(1,540)	-	(1,540)
Others	13	-	-	-	(90,848)	-	-	(90,848)
Transfer of right issue cost to retained earnings	13	-	-	-	111,996	(111,996)	-	-
Balance at 30 September 2018 (unaudited)		8,200,000	2,159,483	68,000	(44,797)	1,263,111	-	11,645,797
Balance at 1 January 2017 (audited)		4,000,000	1,945,105	68,000	(211,790)	2,302,211	-	8,103,526
Net income for the period		-	-	-	-	663,762	-	663,762
Other comprehensive income		-	-	-	58,176	-	-	58,176
Total comprehensive income for the period		-	-	-	58,176	663,762	-	721,938
Zakat and income tax		-	-	-	-	(25,854)	-	(25,854)
Share in zakat of an associate		-	-	-	-	(354)	-	(354)
Issue of bonus shares		1,200,000	-	-	-	(1,200,000)	-	-
Proposed dividend	20	-	-	-	-	(200,000)	200,000	-
Dividend paid		-	-	-	-	-	(191,227)	(191,227)
Adjustments in proposed dividend		-	-	-	-	8,773	(8,773)	-
Other	13	-	-	-	(725)	-	-	(725)
Balance at 30 September 2017 (unaudited)		5,200,000	1,945,105	68,000	(154,339)	1,548,538	-	8,607,304

Tarek Al-Kasabi  
Chairman

Nabil Al-Hoshan  
CEO and Managing Director

Shahid Amin  
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# Bank AlJazira

(A Saudi Joint Stock Company)

## INTERIM CONDENSED CONSOLIDATED STATEMENT OF CASH FLOWS (UNAUDITED) FOR THE NINE MONTH PERIOD ENDE 30 SEPTEMBER 2018

		For the nine month period ended	
		30 September 2018 SR'000	30 September 2017 SR'000
	Notes		
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>			
Net income for the period		753,773	663,762
Adjustments to reconcile net income to net cash from operating activities:			
Trading loss / (income), net		6,153	(9,190)
Impairment charge for credit losses, net		75,467	194,175
Share in net income of an associate		(7,678)	(8,290)
Depreciation and amortization		67,749	64,192
Dividend income		(108)	(49)
(Gain) / loss on disposal of property and equipment		(132)	81
		<u>895,224</u>	<u>904,681</u>
<b>Net changes in operating assets:</b>			
Statutory deposit with SAMA		(41,548)	(78,425)
Due from banks and other financial institutions maturing after ninety days from the date of acquisition		167,049	(166,132)
Investments held at FVTPL		20,536	1,746
Positive fair value of derivatives		11,384	14,754
Loans and advances		(1,063,071)	978,197
Other real estate, net		(6,702)	(383,034)
Other assets		(35,305)	(47,788)
<b>Net changes in operating liabilities:</b>			
Due to banks and other financial institutions		625,794	2,671,712
Customers' deposits		(67,621)	(1,926,248)
Negative fair value of derivatives		(83,578)	(66,177)
Other liabilities		82,653	62,206
<b>Net cash from operating activities</b>		<u>504,815</u>	<u>1,965,492</u>
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>			
Proceeds from maturity and sale of non-trading investments		214,627	524,683
Acquisition of non-trading investments		(4,526,161)	(4,625,866)
Investment in an associate		8,575	6,125
Acquisition of property and equipment		(51,304)	(138,096)
Proceeds from sale of property and equipment		152	200
Dividends received		108	49
<b>Net cash used in investing activities</b>		<u>(4,354,003)</u>	<u>(4,232,905)</u>
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>			
Proceeds from issue of right shares	12	3,000,000	-
Payment of right issue cost	13	(90,848)	-
Special commission on Subordinated Sukuk		23,793	19,321
Zakat and income tax paid		(28,372)	(25,246)
Dividends paid		(249,438)	(190,013)
<b>Net cash from / (used in) financing activities</b>		<u>2,655,135</u>	<u>(195,938)</u>
Net decrease in cash and cash equivalents held		(1,194,053)	(2,463,351)
Cash and cash equivalents at the beginning of the period		3,478,824	3,796,821
<b>Cash and cash equivalents at the end of the period</b>	15	<u>2,284,771</u>	<u>1,333,470</u>
Special commission income received during the period		1,893,496	1,798,296
Special commission expense paid during the period		507,774	493,031

### Supplemental non-cash information

Net changes in fair value and transfers of cash flow hedge derivatives to the interim condensed consolidated statement of income	13	70,168	55,300
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Tarek Al-Kasabi  
Chairman

Nabil Al-Hoshan  
CEO and Managing Director

Shahid Amin  
Chief Financial Officer

The accompanying notes 1 to 22 form an integral part of these interim condensed consolidated financial statements.

*Handwritten signature:* Tarek Al-Kasabi

# Bank AlJazira

(A Saudi Joint Stock Company)

## NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) FOR THE NINE MONTH PERIOD ENDED 30 SEPTEMBER 2018

### 1. GENERAL

These interim condensed consolidated financial statements comprise the financial statements of Bank AlJazira (the “Bank”) and its subsidiaries (collectively referred to as the “Group”). Bank AlJazira is a Saudi Joint Stock Company incorporated in the Kingdom of Saudi Arabia and formed pursuant to Royal Decree number 46/M dated 12 Jumad Al-Thani 1395H (21 June 1975). The Bank commenced its business on 16 Shawwal 1396H (9 October 1976) with the takeover of The National Bank of Pakistan’s branches in the Kingdom of Saudi Arabia that was registered under commercial registration number 4030010523 dated 29 Rajab 1396H (27 July 1976) issued in Jeddah. The Bank operates through its 80 branches (31 December 2017: 79 branches, 30 September 2017: 79 branches) and 53 Fawri Remittance Centers (31 December 2017: 50 Fawri Remittance Centers, 30 September 2017: 48 Fawri Remittance Centers) in the Kingdom of Saudi Arabia. The Bank’s Head Office is located at the following address:

Bank AlJazira  
Nahda District, King Abdulaziz Road,  
P.O. Box 6277  
Jeddah 21442, Kingdom of Saudi Arabia

The objective of the Bank is to provide a full range of Shari’ah compliant (non-interest based) banking products and services comprising of Murabaha, Istisna’a, Ijarah, Tawaraq, Musharaka, Wa’ad Fx and Sukuk which are approved and supervised by an independent Shari’ah Board established by the Bank. The Bank’s shares are listed on Tadawul in the Kingdom of Saudi Arabia.

The Bank’s subsidiaries and its associate are as follows:

			<b>Ownership (direct and indirect) 30 September 2018</b>	<b>Ownership (direct and indirect) 31 December 2017</b>	<b>Ownership (direct and indirect) 30 September 2017</b>
<b>Subsidiaries</b>	<b>Country of incorporation</b>	<b>Nature of business</b>			
AlJazira Capital Company	Kingdom of Saudi Arabia	Brokerage, margin financing and asset management	<b>100%</b>	100%	100%
Aman Development and Real Estate Investment Company	Kingdom of Saudi Arabia	Holding and managing real estate collaterals on behalf of the Bank	<b>100%</b>	100%	100%
Aman Insurance Agency Company	Kingdom of Saudi Arabia	Acting as an agent for bancassurance activities on behalf of the Bank	<b>100%</b>	100%	-
AlJazira Securities Limited	Cayman Islands	Carryout Shari’ah compliant derivative and capital market transactions	<b>100%</b>	100%	-
<b>Associate</b>					
AlJazira Takaful Ta’awuni Company	Kingdom of Saudi Arabia	Fully Shari’ah compliant protection and saving products	<b>35%</b>	35%	35%



# Bank AlJazira

(A Saudi Joint Stock Company)

## NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) FOR THE NINE MONTH PERIOD ENDED 30 SEPTEMBER 2018 (CONTINUED)

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### 2. BASIS OF PREPARATION

These interim condensed consolidated financial statements are prepared in accordance with IAS 34-Interim Financial Reporting as modified by the Saudi Arabian Monetary Authority (“SAMA”) for the accounting of Zakat and income tax. The Bank prepares its interim condensed consolidated financial statements to comply with the Banking Control Law and the Regulation for Companies in the Kingdom of Saudi Arabia and the Bank’s By-laws. These interim condensed consolidated financial statements do not include all of the information required for full annual financial statements, and should be read in conjunction with the Group’s annual financial statements for the year ended 31 December 2017.

The accounting policies applied by the Group in the preparation of the interim condensed consolidated financial statements are consistent with those applied by the Group in the annual consolidated financial statements for the year ended 31 December 2017, except for changes in accounting policies explained in Notes 4 and 5.

In preparing these interim condensed consolidated financial statements, significant judgments made by the management in applying the Group’s accounting policies and the key sources of estimation were the same as those that were applied to the consolidated financial statements as at and for the year ended 31 December 2017 except for the new judgments and estimates explained in Note 5.

The Group has applied accounting policies retrospectively except as disclosed under Transition note under Note 4.

These interim condensed consolidated financial statements are expressed in Saudi Arabian Riyals (SR) and are rounded off to the nearest thousands except where otherwise stated.

### 3. BASIS OF CONSOLIDATION

These interim condensed consolidated financial statements comprise the financial statements of Bank AlJazira and its subsidiaries as set out in Note 1. The financial statements of the subsidiaries are prepared for the same reporting period as that of the Bank.

The interim condensed consolidated financial statements have been prepared using uniform accounting policies and valuation methods for like transactions and other events in similar circumstances. The accounting policies of subsidiaries have been changed when necessary to align them with the policies adopted by the Group.

#### a) Subsidiaries

Subsidiaries are entities which are controlled by the Bank. The Bank controls an entity when it is exposed to, or has rights to, variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity. To meet the definition of control, all of the following three criteria must be met:

- i. the Group has power over an entity;
- ii. the Group has exposure, or rights, to variable returns from its involvement with the entity; and
- iii. the Group has the ability to use its power over the entity to affect the amount of the entity’s returns.

# Bank AlJazira

(A Saudi Joint Stock Company)

## NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) FOR THE NINE MONTH PERIOD ENDED 30 SEPTEMBER 2018 (CONTINUED)

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### 3. BASIS OF CONSOLIDATION (continued)

#### a) Subsidiaries (continued)

The Group re-assesses whether or not it controls an investee in case facts and circumstances indicate that there are changes to one or more of the criteria of control. Subsidiaries are consolidated from the date on which control is transferred to the Bank and cease to be consolidated from the date on which the control is transferred from the Group. The results of subsidiaries acquired or disposed of during the period, if any, are included in the interim condensed consolidated statement of income from the date of the acquisition or up to the date of disposal, as appropriate.

#### b) Non-controlling interests

Non-controlling interests represent the portion of net income and net assets of subsidiaries not owned, directly or indirectly, by the Group in its subsidiaries and are presented separately in the interim condensed consolidated statement of income and within equity in the interim condensed consolidated statement of financial position, separately from the Bank's equity. 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. Changes in the Group's interest in a subsidiary that do not result in a loss of control are accounted for as equity transactions.

#### c) Transactions eliminated on consolidation

Balances between the Group entities, and any unrealized income and expenses arising from intra-group transactions, are eliminated in preparing the interim condensed consolidated financial statements. Unrealized losses are eliminated in the same way as unrealized gains, but only to the extent that there is no evidence of impairment.

#### d) Investment in an associate

Associates are entities over which the Group exercises significant influence. Investments in associates are initially recognized at cost and subsequently accounted for under the equity method of accounting and are carried in the interim condensed consolidated statement of financial position at the lower of the equity-accounted value or the recoverable amount.

Equity-accounted value represents the cost plus post-acquisition changes in the Group's share of net assets of the associate (share of the results, reserves and accumulated gains/ (losses) based on the latest available financial information) less impairment, if any.

After application of the equity method, the Group determines whether it is necessary to recognise an additional impairment loss on its investment in its associates. The Group determines at each reporting date whether there is any objective evidence that the investment in the associate is impaired. If this is the case, the Group calculates the amount of impairment as the difference between the recoverable amount of the associate and its carrying value and recognises the amount in 'share in net income / (loss) of an associate' in the interim condensed consolidated statement of income.

# Bank AlJazira

(A Saudi Joint Stock Company)

## NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) FOR THE NINE MONTH PERIOD ENDED 30 SEPTEMBER 2018 (CONTINUED)

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### 3. BASIS OF CONSOLIDATION (continued)

#### d) Investment in an associate (continued)

The previously recognized impairment loss in respect of investment in associate can be reversed through the interim condensed consolidated statement of income, such that the carrying amount of the investment in the interim condensed consolidated statement of financial position remains at the lower of the equity-accounted (before allowance for impairment) or the recoverable amount.

Unrealized gains and losses on transactions between the Group and its associates are eliminated to the extent of the Group's interest in the associates.

### 4. IMPACT OF CHANGES IN ACCOUNTING POLICIES DUE TO ADOPTION OF NEW STANDARDS

Effective 1 January 2018 the Group has adopted following IFRSs. The impact of the adoption of these standards is explained below:

#### I. IFRS 15 Revenue from Contracts with Customers

The Group adopted IFRS 15 'Revenue from Contracts with Customers' during the period ended 31 March 2018. IFRS 15 was issued in May 2014 and is effective for annual periods commencing on or after 1 January 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 Group has completed its assessment of the impact of adoption of IFRS 15 and concluded that the new standard did not have any significant impact on the current revenue recognition practices. The financial impact of adoption of IFRS 15 is not material therefore prior period amounts have not been restated.

# Bank AlJazira

(A Saudi Joint Stock Company)

## NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) FOR THE NINE MONTH PERIOD ENDED 30 SEPTEMBER 2018 (CONTINUED)

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### 4. IMPACT OF CHANGES IN ACCOUNTING POLICIES DUE TO ADOPTION OF NEW STANDARDS (continued)

#### II. IFRS 9 – Financial Instruments

As allowed, the Group in 2011 adopted earlier version of IFRS 9 issued in November 2009 and subsequently revised in October 2010 (the early adopted IFRS 9), which mainly included classification and measurement of financial instruments. Effective from 1 January 2018, the Group adopted IFRS 9 issued in July 2014 (the complete IFRS 9), which supersedes all earlier versions and included classification and measurement, impairment and hedge accounting.

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

The key changes to the Group's accounting policies resulting from its adoption of the complete IFRS 9 are summarized below:

#### *Classification and measurement of financial instruments*

As a result of the adoption of the complete IFRS 9, there are no significant changes with respect to classification and measurement of financial assets other than:

- Contractual cash flow characteristics assessment;
- Introduction of a FVOCI measurement category for debt instruments; and
- Accounting for the reclassification of financial assets between measurement categories.

#### *Impairment of financial assets*

The complete IFRS 9 replaces the 'incurred loss' model in IAS 39 with an 'expected credit loss' model ("ECL"). The complete IFRS 9 requires the Group to record an allowance for ECLs for all loans and other debt financial assets not held at FVTPL, 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 the complete IFRS 9, credit losses are recognized earlier than under IAS 39. For an explanation of how the Group applies the impairment requirements of IFRS 9, see respective section of significant accounting policies.

#### *Transition*

Changes in accounting policies resulting from the adoption of the complete 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 the complete IFRS 9 are recognized in retained earnings as at 1 January 2018. Accordingly, the impairment allowance presented for 2017 does not reflect the requirements of the complete IFRS 9 and therefore impairment allowance is not comparable to the information presented for 2018 under the complete IFRS 9.



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## NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) FOR THE NINE MONTH PERIOD ENDED 30 SEPTEMBER 2018 (CONTINUED)

### 4. IMPACT OF CHANGES IN ACCOUNTING POLICIES DUE TO ADOPTION OF NEW STANDARDS (continued)

#### II. IFRS 9 – Financial Instruments (continued)

##### *Transition (continued)*

- The assessment for the determination of the business model within which a financial asset is held considering the facts and circumstances that existed at the date of initial application.

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 the complete IFRS 9.

##### *Reconciliation of carrying amounts under IAS 39/ the early adopted IFRS 9 to carrying amounts under complete IFRS 9 at 1 January 2018*

- a) The following table reconciles the carrying amounts under IAS 39 / the early adopted IFRS 9 to the carrying amounts under the complete IFRS 9 on transition date of 1 January 2018.

	SR '000		
	31 December 2017 (IAS 39 / early adopted IFRS 9 / IAS 37)	Re-measurement	1 January 2018 (the complete IFRS 9)
<b>Financial assets</b>			
Due from banks and other financial institutions	369,249	(306)	368,943
Loans and advances, net	39,789,846	(472,284)	39,317,562
	<b>40,159,095</b>	<b>(472,590)</b>	<b>39,686,505</b>
<b>Financial liabilities</b>			
Other liabilities	780,336	163,567	943,903

- b) The following table reconciles the impairment allowance recorded as per the requirements of IAS 39 to that of the complete IFRS 9, considering the following:

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

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## NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) FOR THE NINE MONTH PERIOD ENDED 30 SEPTEMBER 2018 (CONTINUED)

### 4. IMPACT OF CHANGES IN ACCOUNTING POLICIES DUE TO ADOPTION OF NEW STANDARDS (continued)

#### II. IFRS 9 – Financial Instruments (continued)

*Reconciliation of carrying amounts under IAS 39/ the early adopted IFRS 9 to carrying amounts under the complete IFRS 9 at 1 January 2018 (continued)*

	SR '000		
	31 December 2017 (IAS 39/ /early adopted IFRS 9/ IAS 37)	Re-measurement	1 January 2018 (the complete IFRS 9)
<b>Financial assets</b>			
Due from banks and other financial institutions	-	306	306
Loans and advances, net	704,729	472,284	1,177,013
	<u>704,729</u>	<u>472,590</u>	<u>1,177,319</u>
<b>Other liabilities</b>	-	163,567	163,567
	<u>-</u>	<u>163,567</u>	<u>163,567</u>

c) The following table summarise the effect on retained earnings of the Group as a result of adoption of the complete IFRS 9:

	SR'000
<b>Retained earnings as at 31 December 2017</b>	<b>1,526,541</b>
Recognition of expected credit losses under IFRS 9 (including credit loss provision against loan commitments and financial guarantee contracts)	(636,157)
<b>Retained earnings under complete IFRS 9 (1 January 2018)</b>	<b><u>890,384</u></b>

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## NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) FOR THE NINE MONTH PERIOD ENDED 30 SEPTEMBER 2018 (CONTINUED)

### 4. IMPACT OF CHANGES IN ACCOUNTING POLICIES DUE TO ADOPTION OF NEW STANDARDS (continued)

#### II. IFRS 9 – Financial Instruments (continued)

##### *Classification of financial assets and financial liabilities*

The following table provides summary of financial instruments of the Group by class of those instruments and their carrying amounts as at 30 September 2018:

30 September 2018					
Notes	Mandatorily at FVTPL	Designated as at FVTPL	FVOCI – equity investments	Amortized cost	Total carrying amount
<u>SR'000</u>					
<b>Financial assets</b>					
Cash and balances with SAMA	15	-	-	-	4,560,067
Due from banks and other financial institutions		-	-	-	464,384
Investments	6	-	34,726	4,899	24,605,767
Positive fair value of derivatives	10	92,637	-	-	-
Loans and advances	7	-	-	-	40,255,184
Other assets		-	-	-	263,981
<b>Total financial assets</b>		<u>92,637</u>	<u>34,726</u>	<u>4,899</u>	<u>70,149,383</u>
<b>Financial liabilities</b>					
Due to banks and other financial institutions		-	-	-	6,798,339
Customers' deposits	9	-	-	-	50,210,745
Negative fair value of derivatives	10	137,409	-	-	-
Subordinated Sukuk	11	-	-	-	2,030,175
Other liabilities		-	-	-	861,683
<b>Total financial liabilities</b>		<u>137,409</u>	<u>-</u>	<u>-</u>	<u>59,900,942</u>

#### III. IFRS 7 (revised) financial instruments: disclosures

IFRS 7 was updated to reflect the differences between IFRS 9 and IAS 39 and the Group has adopted it, together with IFRS 9, for the year beginning 1 January 2018. Changes include transition disclosures as shown in note 4, detailed qualitative and quantitative information about the ECL calculations such as the assumptions, inputs used, reconciliations etc are also disclosed in the other respective notes.

IFRS 7 also requires additional and more detailed disclosures for hedge accounting which will be disclosed in the annual consolidated financial statements for 2018, since the adoption of IFRS 9 for hedge accounting did not have a material impact on the hedging activities/accounting of the Group.

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## NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) FOR THE NINE MONTH PERIOD ENDED 30 SEPTEMBER 2018 (CONTINUED)

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### 5. SIGNIFICANT ACCOUNTING POLICIES

As explained in note 4, as a result of adoption of IFRS 15 and the complete IFRS 9, certain accounting policies are enhanced/modified effective 1 January 2018. The enhanced/modified accounting policies as well as corresponding accounting policies adopted and disclosed in the annual financial statements for the year ended 31 December 2017, are summarized below:

#### **Financial assets and financial liabilities**

##### **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 special commission on the principal amount outstanding.

If a financial asset does not meet both of these conditions, then it is measured at fair value.

Income is recognised on an effective yield basis for debt instruments measured subsequently at amortised cost. Commission income is recognised in the interim condensed consolidated statement of income.

Debt instruments that are measured at amortised cost are subject to impairment.

##### ***Financial assets 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 special commission on the principal amount outstanding.

***Equity instruments:*** On initial recognition, for an equity investment that is not held for trading, the Group may irrevocably elect to present subsequent changes in fair value in Other Comprehensive Income (OCI). This election is made on an investment-by-investment basis.



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## NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) FOR THE NINE MONTH PERIOD ENDED 30 SEPTEMBER 2018 (CONTINUED)

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### 5. SIGNIFICANT ACCOUNTING POLICIES (continued)

#### *Financial asset at FVOCI (continued)*

Investments in debt instruments as FVOCI are initially measured at fair value plus transaction costs. These are subsequently measured at fair value with gains and losses arising due to changes in fair value recognised in OCI. Special commission income and foreign exchange gains and losses are recognised in interim condensed consolidated statement of income.

Investments in equity instruments at FVOCI are initially measured at fair value plus transaction costs. Subsequently, these are measured at fair value with gains and losses arising from changes in fair value recognised in other comprehensive income and accumulated in other reserves. Gains and losses on such equity instruments are never reclassified to the interim condensed consolidated statement of income and no impairment is recognised in the interim condensed consolidated statement of income. Investments in unquoted equity instruments are measured at fair value. The cumulative gains or losses will not be reclassified to the interim condensed consolidated statement of income on disposal of the investments.

On initial recognition the Group designates all investments in equity instruments that are not FVTPL as FVOCI.

Dividends on these investments in equity instruments are recognised in the interim condensed consolidated statement of income when the Group's right to receive the dividend is established, unless the dividend clearly represent a recovery of part of the cost of the investment.

#### *(Policy applicable before 1 January 2018)*

#### *Investment in equity instruments designated as Fair Value Through Other Comprehensive Income (FVTOCI)*

*On initial recognition, the Group can make an irrevocable election (on an instrument-by-instrument basis) to designate investments in equity instruments as FVTOCI. Designation as FVTOCI is not permitted if the equity investment is held for trading.*

*Investments in equity instruments as FVTOCI are initially measured at fair value plus transaction costs.*

*Subsequently, they are measured at fair value with gains and losses arising from changes in fair value recognised in other comprehensive income and accumulated in other reserves. Gains and losses on such equity instruments are never reclassified to the consolidated statement of income and no impairment is recognised in the consolidated statement of income. Investments in unquoted equity instruments are measured at fair value. The cumulative gains or losses will not be reclassified to the consolidated statement of income on disposal of the investments.*

*On initial recognition the Group designates all investments in equity instruments that are not FVTIS as FVTOCI.*

*Dividends on these investments in equity instruments are recognised in the consolidated statement of income when the Group's right to receive the dividend is established, unless the dividend clearly represent a recovery of part of the cost of the investment.*

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## NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) FOR THE NINE MONTH PERIOD ENDED 30 SEPTEMBER 2018 (CONTINUED)

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### 5. SIGNIFICANT ACCOUNTING POLICIES (continued)

#### *Financial asset at FVOCI (continued)*

##### *(Policy applicable before 1 January 2018)*

*Fair value reserve includes the cumulative net change in fair value of equity investment measured at FVOCI. When such equity instruments are derecognised, the related cumulative amount in the fair value reserve is transferred to retained earnings.*

#### *Financial asset at FVTPL*

All other financial assets are classified as measured at FVTPL (for example: equity held for trading and debt securities classified neither as amortised cost nor FVOCI).

In addition, on initial recognition, the Group may irrevocably designate a financial asset that otherwise meets the requirements to be measured at amortized cost or at FVOCI as 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 Group changes its business model for managing financial assets.

Financial assets at FVTPL are measured at fair value at the end of each reporting period, with any gains or losses arising on measurement recognised in the interim condensed consolidated statement of income.

Commission income on debt instruments as FVTPL is included in the interim condensed consolidated statement of income.

Dividend income on investments in equity instruments as FVTPL is recognised in the interim condensed consolidated statement of income when the Group's right to receive the dividend is established and is included in the interim condensed consolidated statement of income.

#### *Business model assessment*

The Group makes an assessment of 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 special commission revenue, maintaining a particular special commission 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 Group'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 Group's stated objective for managing the financial assets is achieved and how cash flows are realized.

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## NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) FOR THE NINE MONTH PERIOD ENDED 30 SEPTEMBER 2018 (CONTINUED)

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### 5. SIGNIFICANT ACCOUNTING POLICIES (continued)

#### *Business model assessment (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 Group's original expectations, the Group 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 special commission (SPPI)*

For the purposes of this assessment, 'principal' is the fair value of the financial asset on initial recognition. 'Special Commission' 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 special commission, the Group 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 Group considers:

- contingent events that would change the amount and timing of cash flows;
- leverage features;
- prepayment and extension terms;
- terms that limit the Group'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 special commission rates.

#### *Designation at fair value through profit or loss*

At initial recognition, the Group may designate certain financial assets at FVTPL if this designation eliminates or significantly reduces an accounting mismatch, which would otherwise arise.

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## NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) FOR THE NINE MONTH PERIOD ENDED 30 SEPTEMBER 2018 (CONTINUED)

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### 5. SIGNIFICANT ACCOUNTING POLICIES (continued)

#### **Classification of financial liabilities**

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

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 the Group 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 interim condensed consolidated statement of income.

Amounts in OCI relating to own credit are not recycled to the interim condensed consolidated statement of income 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.

#### **Designation at fair value through profit or loss**

The Group may designate certain financial liabilities as at FVTPL in either of the following circumstances:

- the liabilities are managed, evaluated and reported internally on a fair value basis; or
- the designation eliminates or significantly reduces an accounting mismatch that would otherwise arise.

At 30 September 2018, there were no financial liabilities designated by the Group as at FVTPL.

#### **Derecognition**

##### ***Financial assets***

The Group 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 Group neither transfers nor retains substantially all of the risks and rewards of ownership and it does not retain control of the financial asset.



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## NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) FOR THE NINE MONTH PERIOD ENDED 30 SEPTEMBER 2018 (CONTINUED)

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### 5. SIGNIFICANT ACCOUNTING POLICIES (continued)

#### Derecognition (continued)

##### *Financial assets (continued)*

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. 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 Group 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 Group retains all or substantially all of the risks and rewards of ownership of such assets.

In transactions in which the Group 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 Group 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 Group 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.

##### *(Policy applicable before 1 January 2018)*

*On derecognition of a financial asset that is classified as FVOCI, the cumulative gain or loss previously accumulated in other comprehensive income is not reclassified to consolidated statement of income, but is transferred to retained earnings.*

##### *Financial liabilities*

The Group derecognizes a financial liability when its contractual obligations are discharged or cancelled, or expire.

#### Modifications of financial assets and financial liabilities

##### *Financial assets*

If the terms of a financial asset are modified, the Group 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.

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## NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) FOR THE NINE MONTH PERIOD ENDED 30 SEPTEMBER 2018 (CONTINUED)

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### 5. SIGNIFICANT ACCOUNTING POLICIES (continued)

#### Modifications of financial assets and financial liabilities (continued)

##### *Financial assets (continued)*

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 Group 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 special commission income.

##### *Financial liabilities*

The Group 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.

#### Impairment

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

- financial assets that are debt instruments;
- lease / Ijarah receivables;
- financial guarantee contracts issued; and
- loan commitments issued.

No impairment loss is recognized on equity investments.

The Group 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 (other than lease receivables) 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 Group 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.

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## NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) FOR THE NINE MONTH PERIOD ENDED 30 SEPTEMBER 2018 (CONTINUED)

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### 5. SIGNIFICANT ACCOUNTING POLICIES (continued)

#### **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 Group 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 Group if the commitment is drawn down and the cash flows that the Group expects to receive; and
- financial guarantee contracts: the expected payments to reimburse the holder less any amounts that the Group 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, 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 yield rate of the existing financial asset.

##### *Credit-impaired financial assets*

At each reporting date, the Group 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 Group on terms that the Group 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.

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## NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) FOR THE NINE MONTH PERIOD ENDED 30 SEPTEMBER 2018 (CONTINUED)

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### 5. SIGNIFICANT ACCOUNTING POLICIES (continued)

#### Impairment (continued)

##### *Credit-impaired financial assets (continued)*

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.

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

- the market's assessment of creditworthiness as reflected in the sukuk 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 interim condensed consolidated 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 Group cannot identify the ECL on the loan commitment component separately from those on the drawn component: the Group 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 under "Other Liabilities"; 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 recognised in interim condensed consolidated statement of income and changes between the amortised cost of the assets and their fair value are recognised 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.

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### 5. SIGNIFICANT ACCOUNTING POLICIES (continued)

#### Impairment (continued)

##### *Write-off (continued)*

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 Group 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 Group's accounting policy for collateral assigned to it through its lending arrangements under IFRS 9 is the same as it was under IAS 39. Collateral, unless repossessed, is not recorded on the interim condensed consolidated 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 Group 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 professional evaluators, or based on housing price indices.

##### *(Policy applicable before 1 January 2018)*

*At each reporting date the Group assesses whether there is objective evidence that financial assets carried at amortised cost are impaired. A financial asset or a group of financial assets is impaired when objective evidence demonstrates that a loss event has occurred after the initial recognition of the asset(s), and that the loss event has an impact on the future cash flows of the asset(s) that can be estimated reliably.*

*Objective evidence that financial assets are impaired can include significant financial difficulty of the borrower or issuer, default or delinquency by a borrower, restructuring of a loan or advance by the Group on terms that the Group would not otherwise consider, indications that a borrower or issuer will enter bankruptcy, the disappearance of an active market for a security, or other observable data relating to a group of assets such as adverse changes in the payment status of borrowers or issuers in the group, or economic conditions that correlate with defaults in the group.*

*The Group considers evidence of impairment for loans and advances and investment securities measured at amortised cost at both a specific asset and collective level. All individually significant loans and advances and investment securities measured at amortised cost are assessed for specific impairment. All individually significant loans and advances and investment securities measured at amortised cost found not to be specifically impaired are then collectively assessed for any impairment that has been incurred but not yet identified. Loans and advances and investment securities measured at amortised cost that are not individually significant are collectively assessed for impairment by grouping together loans and advances and investment securities measured at amortised cost with similar risk characteristics.*

# Bank AlJazira

(A Saudi Joint Stock Company)

## NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) FOR THE NINE MONTH PERIOD ENDED 30 SEPTEMBER 2018 (CONTINUED)

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### 5. SIGNIFICANT ACCOUNTING POLICIES (continued)

#### Impairment (continued)

##### *(Policy applicable before 1 January 2018) (continued)*

*Impairment losses on assets carried at amortised cost are measured as the difference between the carrying amount of the financial asset and the present value of estimated future cash flows discounted at the asset's original effective yield rate. Impairment losses are recognised in the consolidated statement of income and reflected in impairment for credit losses. Commission on impaired assets continues to be recognised until its maturity for all consumer loans.*

*Management uses estimates based on historical loss experience for assets with credit risk characteristics and objective evidence of impairment similar to those in the portfolio when estimating its cashflows. The methodology and assumptions used for estimating both the amount and timing of future cashflows are reviewed regularly to reduce any difference between loss estimates and actual loss experience.*

*When a subsequent event causes the amount of impairment loss to decrease, the decrease in impairment loss is reversed through consolidated statement of income.*

*Loans and advances are written off when they are determined to be uncollectible. This determination is reached after considering information such as the number of days for which the financing has been past due, significant changes in the borrower financial position such that the borrower can no longer settle its obligations, or to the extent that proceeds from collateral held are insufficient to cover the obligations.*

*The carrying amount of the asset is adjusted through the use of an allowance for impairment account and the amount of the adjustment is included in the consolidated statement of income.*

*Loans and advances are generally renegotiated either as part of an ongoing customer relationship or in response to an adverse change in the circumstances of the borrower. In the latter case, renegotiation can result in an extension of the due date of payment or repayment plans under which the Bank offers a revised rate of commission to genuinely distressed borrowers. This results in the asset continuing to be overdue and individually impaired as the renegotiated payments of commission and principal do not recover the original carrying amount of the loan. In other cases, renegotiation leads to a new agreement, this is treated as a new loan. Restructuring policies and practices are based on indicators or criteria which, indicate that payment will most likely continue. The loans continue to be subject to an individual or collective impairment assessment, calculated using the loan's original effective yield rate.*

*The Group also considers evidence of impairment at a collective assets level. The collective allowance for impairment could be based on certain criteria i.e. deterioration in internal grading or external credit ratings allocated to the borrower or group of borrowers, the current economic climate in which the borrowers operate and the experience and historical default patterns that are embedded in the components of the credit portfolio.*

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## NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) FOR THE NINE MONTH PERIOD ENDED 30 SEPTEMBER 2018 (CONTINUED)

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### 5. SIGNIFICANT ACCOUNTING POLICIES (continued)

#### Financial guarantees and loan commitments

'Financial guarantees' are contracts that require the Group 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 special commission 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 1 January 2018: at the higher of this amortized amount and the amount of loss allowance; and
- Before 1 January 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 Group has issued no loan commitments that are measured at FVTPL. For other loan commitments:

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

#### Revenue /expense recognition

##### *Special commission income and expenses*

Special commission income and expense are recognized in interim condensed consolidated statement of income using the effective yield method. The 'effective yield rate' is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument to the gross carrying amount of the financial asset or the amortized cost of the financial liability.

When calculating the effective yield rate for financial instruments other than credit-impaired assets, the Group 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 yield rate is calculated using estimated future cash flows including expected credit losses.

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



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## NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) FOR THE NINE MONTH PERIOD ENDED 30 SEPTEMBER 2018 (CONTINUED)

### 5. SIGNIFICANT ACCOUNTING POLICIES (continued)

#### Revenue /expense recognition (continued)

##### *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 yield method of any difference between that initial amount and the maturity amount and, for financial assets, adjusted for any expected credit loss allowance (or impairment allowance before 1 January 2018).

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 special commission income and expense, the effective yield 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, special commission income is calculated by applying the effective yield rate to the amortized cost of the financial asset. If the asset is no longer credit-impaired, then the calculation of special commission income reverts to the gross basis.

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

When the Group enters into a special commission rate swap to change special commission from fixed to floating (or vice versa), the amount of special commission income or expense is adjusted by the net special commission on the swap to the extent the hedge is considered to be effective.

### 6. INVESTMENTS

	<b>30 September 2018 (Unaudited) SR'000</b>	<b>31 December 2017 (Audited) SR'000</b>	<b>30 September 2017 (Unaudited) SR'000</b>
Fair Value Through Profit and Loss (FVTPL) - designated as at FVTPL	<b>34,726</b>	61,415	100,000
Fair Value Through Other Comprehensive Income (FVOCI) (Refer note (a) below)	<b>4,899</b>	16,388	14,600
Held at amortised cost	<b>24,605,767</b>	20,282,744	20,286,771
<b>Total</b>	<b>24,645,392</b>	20,360,547	20,401,371

- a) During January 2018, the Bank has disposed-off one of its FVOCI investment. The fair value of the investment at the date of disposal was SR 12.08 million. As a result of disposal, a cumulative gain of SR 10.95 million which previously was booked in other comprehensive income, was transferred to retained earnings.

# Bank AlJazira

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## NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) FOR THE NINE MONTH PERIOD ENDED 30 SEPTEMBER 2018 (CONTINUED)

### 7. LOANS AND ADVANCES, NET

The loans and advances are classified as at amortized cost.

	<b>30 September 2018 (Unaudited) SR'000</b>	<b>31 December 2017 (Audited) SR'000</b>	<b>30 September 2017 (Unaudited) SR'000</b>
Credit cards	<b>627,014</b>	463,377	480,348
Consumer loans	<b>18,583,805</b>	17,553,202	17,411,052
Commercial loans and overdrafts	<b>20,861,851</b>	21,550,527	22,851,160
Others	<b>430,052</b>	423,106	416,361
Performing loans and advances	<b>40,502,722</b>	39,990,212	41,158,921
Non - performing loans and advances	<b>802,812</b>	504,363	508,661
Total loans and advances	<b>41,305,534</b>	40,494,575	41,667,582
Allowance for impairment	<b>(1,050,350)</b>	(704,729)	(741,259)
Loans and advances, net	<b>40,255,184</b>	39,789,846	40,926,323

a) Movement in impairment allowance for credit losses is as follows:

	<b>30 September 2018 (Unaudited) SR'000</b>	<b>31 December 2017 (Audited) SR'000</b>	<b>30 September 2017 (Unaudited) SR'000</b>
Balance at the beginning of the period (calculated under IAS 39)	<b>704,729</b>	756,568	756,568
Impact of re-measurement due to adoption of IFRS 9 (note 4 II (a))	<b>472,284</b>	-	-
Balance at the beginning of the period - restated	<b>1,177,013</b>	756,568	756,568
Impairment charge for credit losses	<b>308,573</b>	331,839	240,911
Bad debts written off	<b>(316,626)</b>	(368,415)	(242,423)
Reversal / recoveries of amounts previously impaired	<b>(121,727)</b>	(15,263)	(13,797)
Allowance written back upon restructuring of loan	<b>3,117</b>	-	-
<b>Balance at the end of the period</b>	<b>1,050,350</b>	704,729	741,259

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## NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) FOR THE NINE MONTH PERIOD ENDED 30 SEPTEMBER 2018 (CONTINUED)

### 7. LOANS AND ADVANCES, NET (continued)

- b) Impairment charge for credit losses, net in the interim condensed consolidated statement of income comprised:

	<b>30 September 2018 (Unaudited) <u>SR'000</u></b>	30 September 2017 (Unaudited) <u>SR'000</u>
Impairment charge for credit losses in respect of loans and advances	<b>308,573</b>	240,911
Recoveries / reversal of amounts previously impaired	<b>(121,727)</b>	(13,797)
Recoveries from debts previously written off	<b>(61,397)</b>	(32,939)
Net impairment charge for credit losses in respect of due from banks and other financial institutions	<b>6</b>	-
Reversal of amounts previously provided in respect of credit related contingent liabilities	<b>(49,988)</b>	-
Impairment charge for credit losses, net	<b><u>75,467</u></b>	<u>194,175</u>

### 8. INVESTMENT IN AN ASSOCIATE

Investment in an associate represents the investment made by the Group in AlJazira Takaful Ta'awuni Company (ATT). The Group effectively holds 35% shareholding in ATT.

The share of total comprehensive income in an associate represents the Group's share in the total comprehensive income of ATT and was based on the latest available financial information of ATT. ATT is listed with Saudi Stock Exchange (Tadawul) and the market value of the investment in ATT as of 30 September 2018 was SR 229.56 million (31 December 2017: SR 335.65 million; 30 September 2017: SR 377.9 million) based on Tadawul market price.

### 9. CUSTOMERS' DEPOSITS

	<b>30 September 2018 (Unaudited) <u>SR'000</u></b>	31 December 2017 (Audited) <u>SR'000</u>	30 September 2017 (Unaudited) <u>SR'000</u>
Demand	<b>25,694,853</b>	24,990,180	26,070,153
Time	<b>23,512,833</b>	24,172,493	22,489,693
Other	<b><u>1,003,059</u></b>	<u>1,115,693</u>	<u>1,116,260</u>
Total	<b><u>50,210,745</u></b>	<u>50,278,366</u>	<u>49,676,106</u>

Time deposits comprise deposits received on Shari'ah Compliant (non-commission based) Murabaha products.

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## NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) FOR THE NINE MONTH PERIOD ENDED 30 SEPTEMBER 2018 (CONTINUED)

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### 10. DERIVATIVES

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

#### a) Swaps

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

#### b) Options (Wa'ad Fx)

Foreign exchange options are transactions, whereby a client, in consideration for the payment of a fee agrees to enter into one or a series of trades in which one party (promisor) gives a commitment as a unilateral undertaking, to a second party (promisee).

An option can be a unilateral promise or combination of promises. The Group enters into the option depending on the client's risk profile, whereby the client may promise to buy, sell or buy and sell a currency with or without conditions for hedging its exposure.

#### 10.1 Held for trading purposes

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

#### 10.2 Held for hedging purposes

The Group uses Shari'ah compliant derivatives for hedging purposes in order to reduce its exposure to commission rate risk and foreign exchange risk.

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

As part of its financial asset and liability management, the Group uses derivatives for hedging purposes in order to adjust its own exposure to currency and commission rate risk. This is generally achieved by hedging specific transactions.

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## NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) FOR THE NINE MONTH PERIOD ENDED 30 SEPTEMBER 2018 (CONTINUED)

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### 10. DERIVATIVES (continued)

#### 10.2 Held for hedging purposes (continued)

##### Cash flow hedges

The Group is exposed to variability in future commission cash flows on non-trading assets and liabilities which bear commission at a variable rate. The Group uses commission rate swaps as cash flow hedges of these commission rate risks.

The losses on cash flow hedges reclassified to the interim condensed consolidated statement of income during the period are as follows:

	30 September 2018 <u>SR'000</u>	30 September 2017 <u>SR'000</u>
Special commission income	1,650	1,355
Special commission expense	<u>(1,856)</u>	<u>(1,548)</u>
Net losses on cash flow hedges reclassified to the interim condensed consolidated statement of income	<u>(206)</u>	<u>(193)</u>

The cash flow hedges of special commission rate swap were highly effective in offsetting the variability of special commission expenses. Fair value gain on cash flow hedges amounting to SR 69.96 million (30 September 2017: SR 55.1 million) included in the Interim Condensed Consolidated Statement of Comprehensive Income comprised of net unrealized gain of SR 69.96 million (30 September 2017: SR 49.1 million) and realized gain of SR Nil (30 September 2017: SR 6 million).

During the prior periods, the Bank sold certain of its special commission rate swaps used for cash flows hedges. However, the gain / (loss) would continue to be classified in Interim Condensed Consolidated Statement of Comprehensive Income as the related hedge items are still outstanding. In accordance with the IFRS requirements, the gain / (loss) will be reclassified to Interim Condensed Consolidated Statement of Income in the period when the cash flows pertaining to hedged items will affect the Interim Condensed Consolidated Statement of Income.

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## NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) FOR THE NINE MONTH PERIOD ENDED 30 SEPTEMBER 2018 (CONTINUED)

### 10. DERIVATIVES (continued)

#### 10.2 Held for hedging purposes (continued)

The table below summarize the positive and negative fair values of the Group's derivative financial instruments, together with their notional amounts. The notional amounts, which provide an indication of the volume of 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 market risk.

	30 September 2018 (Unaudited) SR'000			31 December 2017 (Audited) SR'000			30 September 2017 (Unaudited) SR'000		
	Positive fair value	Negative fair value	Notional amount	Positive fair value	Negative fair value	Notional amount	Positive fair value	Negative fair value	Notional amount
<b>Held for trading:</b>									
Options	-	-	-	1,794	1,794	459,895	2,424	2,424	747,531
Special commission rate swaps	34,449	34,449	3,167,536	69,140	69,140	5,652,788	89,551	89,551	6,025,913
Structured deposits	2,000	2,000	800,000	20,558	20,558	2,450,000	7,080	7,080	2,450,000
Currency swaps	99	-	112,500	1,242	-	188,750	1,067	-	191,768
Currency forwards	3	71	203,879	1	-	224	-	-	-
<b>Total</b>	<b>36,551</b>	<b>36,520</b>	<b>4,283,915</b>	<b>92,735</b>	<b>91,492</b>	<b>8,751,657</b>	<b>100,122</b>	<b>99,055</b>	<b>9,415,212</b>
<b>Held as cash flow hedge:</b>									
Special commission rate swaps	56,086	100,889	3,550,625	11,286	129,495	3,250,625	13,842	168,486	3,250,625
<b>Total</b>	<b>92,637</b>	<b>137,409</b>	<b>7,834,540</b>	<b>104,021</b>	<b>220,987</b>	<b>12,002,282</b>	<b>113,964</b>	<b>267,541</b>	<b>12,665,837</b>

The negative fair values of special commission rate swaps are mainly due to a downward shift in the yield curve. The fair values of these swaps are expected to be settled on or before April 2044 (31 December 2017: April 2044 and 30 September 2017: April 2044).

Held for trading special commission rate swaps include special commission income receivable and payable amounting to SR 13.86 million (31 December 2017: SR 15.1 million and 30 September 2017: SR 16.18 million). Held as cash flow hedge special commission rate swaps include special commission income receivable amounting to SR 22.40 million (31 December 2017: SR 11.29 million and 30 September 2017: SR 13.84 million) and special commission payable amounting to SR 24.51 million (31 December 2017: SR 16.85 million and 30 September 2017: SR 23.34 million).

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## NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) FOR THE NINE MONTH PERIOD ENDED 30 SEPTEMBER 2018 (CONTINUED)

### 10. DERIVATIVES (continued)

Pursuant to changes in certain international laws, the Bank has established a Special Purpose Vehicle (SPV) namely Al Jazira Securities Limited and intends to transfer all of its Profit rate swaps ("PRS") derivatives, hedged or traded, to this SPV. In this connection, initially, a novation agreement has been signed among the Bank, the SPV and one of the counter party. Going forward, the SPV will execute all the derivatives with counterparties with a back to back transaction with the Bank. As the change was necessitated by laws, management believe that existing hedging relationships continue to be effective.

### 11. SUBORDINATED SUKUK

On 2 June 2016, the Bank issued 2,000 Subordinated Sukuk Certificates (Sukuk) of SR 1 million each, with a profit distribution rate based on 6 month Saudi Inter-Bank Offered Rate (SIBOR), reset semi-annually in advance, plus a margin of 190 basis point per annum and payable semi-annually in arrears on 2 June and 2 December each year until 2 June 2026, on which date the Sukuk will expire. The Bank has a call option which can be exercised on or after 2 June 2021 on meeting certain conditions and as per the terms mentioned in the related offering circular. The Sukuk may also be called upon occurrence of certain other conditions as per the terms specified in the offering circular. These Sukuk are registered with Saudi Stock Exchange (Tadawul).

### 12. SHARE CAPITAL AND EARNINGS PER SHARE

The authorized, issued and fully paid share capital of the Bank consists of 820 million shares of SR 10 each (31 December 2017: 520 million shares of SR 10 each and 30 September 2017: 520 million shares of SR 10 each).

The shareholders of the Bank in their Extra Ordinary General Assembly meeting held on 19 March 2018 (corresponding to 2 Rajab 1439H), approved the increase in number of shares of the Bank from 520 million shares to 820 million shares through a rights issue of 300 million shares at an exercise price of SR 10 per share amounting to SR 3,000 million. During the period ended 30 June 2018, the Bank, after completing all legal formalities issued the rights shares.

The calculation of basic earnings per share is based on profit attributable to ordinary shareholders and weighted-average number of ordinary shares outstanding, as follows:

	For the three month period ended		For the nine month period ended	
	30 September 2018 <u>SR'000</u>	30 September 2017 <u>SR'000</u> (Restated)	30 September 2018 <u>SR'000</u>	30 September 2017 <u>SR'000</u> (Restated)
<b>Profit attributable to ordinary share holders</b>				
For basic earnings per share	<u>255,086</u>	<u>227,632</u>	<u>753,773</u>	<u>663,762</u>



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## NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) FOR THE NINE MONTH PERIOD ENDED 30 SEPTEMBER 2018 (CONTINUED)

### 12. SHARE CAPITAL AND EARNINGS PER SHARE (continued)

	For the three month period ended		For the nine month period ended	
	30 September 2018 <u>Shares</u>	30 September 2017 <u>Shares</u> (Restated)	30 September 2018 <u>Shares</u>	30 September 2017 <u>Shares</u> (Restated)
<b>Weighted-average number of ordinary shares</b>				
For basic earnings per share	<u>820,000,000</u>	<u>567,547,309</u>	<u>732,420,228</u>	<u>567,547,309</u>
Basic earnings per share (in SR)	<u>0.31</u>	<u>0.40</u>	<u>1.03</u>	<u>1.17</u>

Diluted earnings per share is not applicable to the Bank.

### 13. OTHER RESERVES

<u>30 September 2018</u>	Cash flow hedges <u>SR' 000</u>	Fair value reserve <u>SR' 000</u>	Actuarial losses <u>SR' 000</u>	Right issue costs (note below) <u>SR' 000</u>	Total <u>SR' 000</u>
Balance at beginning of the period	<u>(113,034)</u>	<u>10,928</u>	<u>(1,931)</u>	<u>(21,148)</u>	<u>(125,185)</u>
Net change in fair value	<u>69,962</u>	<u>23</u>	<u>-</u>	<u>-</u>	<u>69,985</u>
Transfer to interim condensed consolidated statement of income	<u>206</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>206</u>
Gain on sale of FVOCI investments transferred to retained earnings	<u>-</u>	<u>(10,951)</u>	<u>-</u>	<u>-</u>	<u>(10,951)</u>
Others	<u>-</u>	<u>-</u>	<u>-</u>	<u>(90,848)</u>	<u>(90,848)</u>
Transfer of right issue cost to retained earnings	<u>-</u>	<u>-</u>	<u>-</u>	<u>111,996</u>	<u>111,996</u>
Net movement during the period	<u>70,168</u>	<u>(10,928)</u>	<u>-</u>	<u>21,148</u>	<u>80,388</u>
Balance at end of the period	<u>(42,866)</u>	<u>-</u>	<u>(1,931)</u>	<u>-</u>	<u>(44,797)</u>

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## NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) FOR THE NINE MONTH PERIOD ENDED 30 SEPTEMBER 2018 (CONTINUED)

### 13. OTHER RESERVES (continued)

<u>30 September 2017</u>	Cash flow hedges <u>SR' 000</u>	Fair value reserve <u>SR' 000</u>	Actuarial losses <u>SR' 000</u>	Right issue costs (note below) <u>SR' 000</u>	Total <u>SR' 000</u>
Balance at beginning of the period	(200,828)	7,157	-	(18,119)	(211,790)
Net change in fair value	55,107	2,876	-	-	57,983
Transfer to interim condensed consolidated statement of income	193	-	-	-	193
Others	-	-	-	(725)	(725)
Net movement during the period	55,300	2,876	-	(725)	57,451
Balance at end of the period	(145,528)	10,033	-	(18,844)	(154,339)

The rights issue cost represents expenses incurred in respect of the legal and professional services for the right issue. During the period ended 30 June 2018, the cumulative right issue costs incurred in prior and current periods are charged directly in retained earnings on completion of right issue (refer note 12).

### 14. COMMITMENTS AND CONTINGENCIES

- 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 31 December 2017.
- The Bank's credit related commitments and contingencies are as follows:

	<b>30 September 2018 (Unaudited) <u>SR'000</u></b>	31 December 2017 (Audited) <u>SR'000</u>	30 September 2017 (Unaudited) <u>SR'000</u>
Letters of credit	<b>780,493</b>	1,015,319	819,834
Letters of guarantee	<b>3,876,043</b>	4,170,845	4,214,905
Acceptances	<b>338,926</b>	405,001	539,920
Irrevocable commitments to extend credit	<b>150,000</b>	150,000	150,000
<b>Total</b>	<b><u>5,145,462</u></b>	<u>5,741,165</u>	<u>5,724,659</u>

# Bank AlJazira

(A Saudi Joint Stock Company)

## NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) FOR THE NINE MONTH PERIOD ENDED 30 SEPTEMBER 2018 (CONTINUED)

### 14. COMMITMENTS AND CONTINGENCIES (continued)

- c) The Group has filed its Zakat and Income Tax returns with the General Authority for Zakat and Tax (GAZT) and paid Zakat and Income Tax for financial years up to and including the year 2017 and has received the assessments for the years up to and including 2011 in which GAZT raised additional demands aggregating to SR 446.9 million for the years 2006 to 2011. These additional demands include SR 392.9 million on account of disallowance of long-term investments and the addition of long term financing to the Zakat base by GAZT. The basis for the additional Zakat demand is being contested by the Bank before the Higher Appeal Committee. Management is confident of a favourable outcome on the aforementioned appeals and has therefore not made any provisions in respect of the above.

The assessments for the years 2012 to 2017 are yet to be raised by the GAZT. However, if long-term investments are disallowed and long-term financing is added to the Zakat base, in line with the assessments finalized by GAZT for the years referred above, it would result in a significant additional Zakat exposure to the Bank which remains an industry wide issue and disclosure of the amount might affect the Bank's position in this matter.

### 15. CASH AND CASH EQUIVALENTS

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

	<b>30 September 2018 (Unaudited) SR'000</b>	<b>31 December 2017 (Audited) SR'000</b>	<b>30 September 2017 (Unaudited) SR'000</b>
Cash and balances with SAMA, excluding statutory deposit	<b>1,820,076</b>	3,276,624	1,025,509
Due from banks and other financial institutions with an original maturity of 90 days or less from the date of acquisition	<b>464,695</b>	202,200	307,961
<b>Total</b>	<b>2,284,771</b>	<b>3,478,824</b>	<b>1,333,470</b>

The reconciliation of cash and cash equivalents to cash and balances with SAMA is as follows:

	<b>30 September 2018 (Unaudited) SR'000</b>	<b>31 December 2017 (Audited) SR'000</b>	<b>30 September 2017 (Unaudited) SR'000</b>
Cash and cash equivalents as per statement of cash flows	<b>2,284,771</b>	3,478,824	1,333,470
Statutory deposit	<b>2,739,991</b>	2,698,443	2,816,197
Due from banks and other financial institutions with original maturity of 90 days or less from the date of acquisition	<b>(464,695)</b>	(202,200)	(307,961)
Cash and balances with SAMA at end of the period	<b>4,560,067</b>	<b>5,975,067</b>	<b>3,841,706</b>

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## NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) FOR THE NINE MONTH PERIOD ENDED 30 SEPTEMBER 2018 (CONTINUED)

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### 16. OPERATING SEGMENTS

The operating segments have been identified on the basis of internal reports about components of the Group that are regularly reviewed by the chief operating decision maker (Chief Executive Officer) in order to allocate resources to the segments and to assess their performance.

All of the Group's operations are based in the Kingdom of Saudi Arabia, except AlJazira Securities Limited (SPV).

Transactions between the operating segments are on normal commercial terms and conditions. The revenue from external parties reported to the chief operating decision maker is measured in a manner consistent with that in the interim condensed consolidated statement of income. Segment assets and liabilities comprise operating assets and liabilities.

There have been no changes to the basis of segmentation or the measurement basis for the segment profit or loss since 31 December 2017.

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

#### **Personal banking**

Deposit, credit and investment products for individuals.

#### **Corporate banking**

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

#### **Treasury**

Treasury includes money market, foreign exchange, trading and treasury services.

#### **Brokerage and asset management**

Provides shares brokerage services to customers (this segment includes the activities of the Bank's subsidiary AlJazira Capital Company).

#### **Takaful Ta'awuni**

Provides protection and saving products services. As required by the Insurance Law of Saudi Arabia, the Group has spun off its insurance business in a separate entity named AlJazira Takaful Ta'awuni Company (ATT) formed under the new Insurance Law of Saudi Arabia. The current division represents the insurance portfolio which will be transferred to ATT at an agreed value and date duly approved by SAMA.

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

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## NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) FOR THE NINE MONTH PERIOD ENDED 30 SEPTEMBER 2018 (CONTINUED)

### 16. OPERATING SEGMENTS (continued)

#### 30 September 2018 (SR'000)

	<u>Personal banking</u>	<u>Corporate banking</u>	<u>Treasury</u>	<u>Brokerage and asset management</u>	<u>Takaful Ta'awuni</u>	<u>Others</u>	<u>Total</u>
Total assets	<u>21,634,101</u>	<u>18,695,594</u>	<u>29,835,097</u>	<u>1,357,871</u>	<u>75,197</u>	<u>133,163</u>	<u>71,731,023</u>
Total liabilities	<u>34,149,083</u>	<u>16,358,968</u>	<u>8,979,908</u>	<u>522,070</u>	<u>75,197</u>	<u>-</u>	<u>60,085,226</u>
Inter - segment operating (loss) / income	<u>(40,902)</u>	<u>(66,925)</u>	<u>118,133</u>	<u>(10,306)</u>	<u>-</u>	<u>-</u>	<u>-</u>
Total operating income	<u>912,152</u>	<u>332,569</u>	<u>812,896</u>	<u>127,785</u>	<u>14,535</u>	<u>(176,405)</u>	<u>2,023,532</u>
Net special commission income	<u>508,854</u>	<u>228,271</u>	<u>663,276</u>	<u>41,989</u>	<u>831</u>	<u>(1,680)</u>	<u>1,441,541</u>
Fee and commission income, net	<u>262,484</u>	<u>93,235</u>	<u>2,800</u>	<u>87,178</u>	<u>13,704</u>	<u>(22,042)</u>	<u>437,359</u>
Trading (loss) / income, net	<u>(1,238)</u>	<u>(1,358)</u>	<u>3,733</u>	<u>(2,952)</u>	<u>-</u>	<u>-</u>	<u>(1,815)</u>
Share in net income of an associate	<u>-</u>	<u>-</u>	<u>-</u>	<u>1,097</u>	<u>-</u>	<u>6,581</u>	<u>7,678</u>
Impairment reversal/(charge) for credit losses, net	<u>25,838</u>	<u>(101,299)</u>	<u>(6)</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>(75,467)</u>
Depreciation and amortisation	<u>(37,480)</u>	<u>(8,279)</u>	<u>(14,141)</u>	<u>(7,314)</u>	<u>(535)</u>	<u>-</u>	<u>(67,749)</u>
Total operating expenses	<u>(649,241)</u>	<u>(283,955)</u>	<u>(217,784)</u>	<u>(107,274)</u>	<u>(21,728)</u>	<u>2,545</u>	<u>(1,277,437)</u>
Net income / (loss)	<u>262,911</u>	<u>48,614</u>	<u>595,112</u>	<u>21,608</u>	<u>(7,193)</u>	<u>(167,279)</u>	<u>753,773</u>

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## NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) FOR THE NINE MONTH PERIOD ENDED 30 SEPTEMBER 2018 (CONTINUED)

### 16. OPERATING SEGMENTS (continued)

	Personal Banking	Corporate banking	Treasury	Brokerage and asset management	Takaful Ta'awuni	Others	Total
<u>31 December 2017 (SR'000)</u>							
Total assets	19,810,852	19,820,983	26,938,427	1,510,873	72,249	134,071	68,287,455
Total liabilities	35,539,607	14,563,514	8,532,527	750,719	72,249	-	59,458,616
<u>30 September 2017 (SR'000)</u>							
Total assets	20,037,659	20,884,918	24,931,406	1,487,309	55,251	131,789	67,528,332
Total liabilities	36,467,181	13,244,779	8,400,526	753,291	55,251	-	58,921,028
Inter - segment operating (loss) / income	(3,525)	(75,077)	86,471	(7,869)	-	-	-
Total operating income	805,686	423,007	691,847	131,522	14,543	(134,949)	1,931,656
Net special commission income	472,333	279,109	574,697	32,854	450	(1,937)	1,357,506
Fee and commission income, net	232,344	130,818	8,145	88,760	14,091	(18,999)	455,159
Trading income, net	-	-	-	9,190	-	-	9,190
Share in net income of an associate	-	-	-	1,184	-	7,106	8,290
Impairment charge for credit losses, net	(18,924)	(175,251)	-	-	-	-	(194,175)
Depreciation and amortisation	(35,669)	(8,043)	(14,143)	(5,734)	(603)	-	(64,192)
Total operating expenses	(613,596)	(339,274)	(205,752)	(104,478)	(16,075)	2,991	(1,276,184)
Net income / (loss)	192,090	83,733	486,095	28,228	(1,532)	(124,852)	663,762

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## NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) FOR THE NINE MONTH PERIOD ENDED 30 SEPTEMBER 2018 (CONTINUED)

### 17. FAIR VALUES OF FINANCIAL INSTRUMENTS

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 in the principal or, in its absence, the most advantageous market to which the Group has access at that date. The fair value of a liability reflects its non-performance risk.

#### Determination of fair value and fair value hierarchy

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

- Level 1: quoted prices in active markets for the same or identical instrument that an entity can access at the measurement date,
- 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) The following table presents the Group's financial assets and liabilities that are measured at fair values:

<b>30 September 2018 (SR'000)</b>				
		<b><u>Fair Value</u></b>		
	<b><u>Carrying Value</u></b>	<b><u>Level 1</u></b>	<b><u>Level 2</u></b>	<b><u>Total</u></b>
<b><u>Financial assets measured at fair value:</u></b>				
FVTPL - Mutual funds	25,464	25,464	-	25,464
FVTPL - Equities	9,262	9,262	-	9,262
Derivatives	92,637	-	92,637	92,637
<b>Total</b>	<b>127,363</b>	<b>34,726</b>	<b>92,637</b>	<b>127,363</b>
<b><u>Financial liabilities measured at fair value:</u></b>				
Derivatives	137,409	-	137,409	137,409
<b>31 December 2017 (SR'000)</b>				
		<b><u>Fair Value</u></b>		
	<b><u>Carrying Value</u></b>	<b><u>Level 1</u></b>	<b><u>Level 2</u></b>	<b><u>Total</u></b>
<b><u>Financial assets measured at fair value:</u></b>				
FVTPL - Mutual funds	60,870	60,870	-	60,870
FVTPL - Equities	545	545	-	545
FVOCI - Equities	12,057	12,057	-	12,057
Derivatives	104,021	-	104,021	104,021
<b>Total</b>	<b>177,493</b>	<b>73,472</b>	<b>104,021</b>	<b>177,493</b>
<b><u>Financial liabilities measured at fair value:</u></b>				
Derivatives	220,987	-	220,987	220,987



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## NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) FOR THE NINE MONTH PERIOD ENDED 30 SEPTEMBER 2018 (CONTINUED)

### 17. FAIR VALUES OF FINANCIAL INSTRUMENTS (continued)

- a) The following table presents the Group's financial assets and liabilities that are measured at fair values: (continued)

		<u>30 September 2017 (SR'000)</u>		
	Carrying	<u>Fair Value</u>		
	<u>Value</u>	<u>Level 1</u>	<u>Level 2</u>	<u>Total</u>
<u>Financial assets measured at fair value:</u>				
FVTPL - Mutual Funds	99,469	99,469	-	99,469
FVTPL – Equities	531	531	-	531
FVOCI - Equities	11,163	11,163	-	11,163
Derivatives	113,964	-	113,964	113,964
	<hr/>	<hr/>	<hr/>	<hr/>
Total	225,127	111,163	113,964	225,127
	<hr/> <hr/>	<hr/> <hr/>	<hr/> <hr/>	<hr/> <hr/>
<u>Financial liabilities measured at fair value:</u>				
Derivatives	267,541	-	267,541	267,541
	<hr/>	<hr/>	<hr/>	<hr/>

Fair value of quoted investments is based on price quoted on the reporting date. Level 2 trading and hedging derivatives comprise foreign exchange, options, profit rate swaps and structured deposits. These foreign exchange contracts have been fair valued using forward exchange rates that are quoted in an active market. Profit rate swaps, options and structured deposits are fair valued using forward profit rates extracted from observable yield curves. The effects of discounting are generally insignificant for Level 2 derivatives.

There were no transfers between Levels 1 and 2 during the year. New investments acquired during the year are classified under the relevant levels. There were no financial assets or financial liabilities classified under level 3.

There were no changes in valuation techniques during the period.

Investments amounting to SR 4.90 million (31 December 2017: SR 4.33 million and 30 September 2017: SR 3.44 million) are carried at cost and, accordingly, are not fair valued.

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## NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) FOR THE NINE MONTH PERIOD ENDED 30 SEPTEMBER 2018 (CONTINUED)

### 17. FAIR VALUES OF FINANCIAL INSTRUMENTS (continued)

- b) Following table represent fair values of financial assets and liabilities measured at amortised cost. There are no financial assets and liabilities that are measured as level 1 fair value.

	30 September 2018 (SR'000)		
	Amortised cost	Level 2	Level 3
<b><u>Financial assets:</u></b>			
Due from banks and other financial institutions	464,384	-	464,141
Investment held at amortised cost	24,605,767	24,615,975	-
Loans and advances, net	40,255,184	-	41,547,279
<b>Total</b>	<b>65,325,335</b>	<b>24,615,975</b>	<b>42,011,420</b>
<b><u>Financial liabilities:</u></b>			
Due to banks and other financial institutions	6,798,339	-	6,779,432
Customers' deposits	50,210,745	-	50,201,860
<b>Total</b>	<b>57,009,084</b>	<b>-</b>	<b>56,981,292</b>
	31 December 2017 (SR'000)		
	Amortised cost	Level 2	Level 3
<b><u>Financial assets:</u></b>			
Due from banks and other financial institutions	369,249	-	369,196
Investment held at amortised cost	20,282,744	20,296,827	-
Loans and advances, net	39,789,846	-	41,260,628
<b>Total</b>	<b>60,441,839</b>	<b>20,296,827</b>	<b>41,629,824</b>
<b><u>Financial liabilities:</u></b>			
Due to banks and other financial institutions	6,172,545	-	6,174,470
Customers' deposits	50,278,366	-	50,288,545
<b>Total</b>	<b>56,450,911</b>	<b>-</b>	<b>56,463,015</b>

The fair value of the cash and balances with SAMA, other assets and other liabilities and subordinated Sukuks approximate to their carrying amount.

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## NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) FOR THE NINE MONTH PERIOD ENDED 30 SEPTEMBER 2018 (CONTINUED)

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### 18. FINANCIAL RISK MANAGEMENT

#### 18.1 Credit Risk

The Board of Directors is responsible for the overall risk management approach and for approving the risk management strategies and principles. The Board has set up Board Risk Committee (BRC) which has the responsibility to monitor the overall risk process within the Bank.

The BRC has the overall responsibility for the development of the risk strategy and implementing principles, frameworks, policies and limits.

The Risk Committee is responsible for supervising risk management decisions and monitoring risk levels and reviewing Risk Management reports / Dashboards on a regular basis. BRC is mandated to escalate to the Board any risk management issue which warrants attention of the Board of Directors of the Bank.

The Group manages exposure to credit risk, which is the risk that one party to a financial instrument will fail to discharge an obligation and cause the other party to incur a financial loss. Credit exposures arise principally in lending activities that lead to loans and advances, and investment activities. There is also credit risk in off-balance sheet financial instruments, such as loan commitments.

The Group assesses the probability of default of counterparties using internal rating tools. Also the Group uses the external ratings, of the major rating agency, where available.

The Group attempts to control credit risk by monitoring credit exposures, limiting transactions with specific counterparties, and continually assessing the creditworthiness of counterparties. The Group's risk management policies are designed to identify and to set appropriate risk limits and to monitor the risks and adherence to limits. Actual exposures against limits are monitored daily. In addition to monitoring credit limits, the Group manages the credit exposure relating to its trading activities by entering into master netting agreements and collateral arrangements with counterparties in appropriate circumstances, and limiting the duration of exposure. In certain cases the Group may also close out transactions or assign them to other counterparties to mitigate credit risk. The Group's credit risk for derivatives represents the potential cost to replace the derivative contracts if counterparties fail to fulfill their obligation, and to control the level of credit risk taken, the Group assesses counterparties using the same techniques as for its lending activities.

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

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

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

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## NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) FOR THE NINE MONTH PERIOD ENDED 30 SEPTEMBER 2018 (CONTINUED)

### 18. FINANCIAL RISK MANAGEMENT (continued)

#### 18.1 Credit Risk (continued)

The Group also seeks additional collateral from the counterparty as soon as impairment indicators are noticed for the relevant individual loans and advances. Management monitors the market value of collateral, requests additional collateral in accordance with the underlying agreement and monitors the market value of collateral obtained during its review of the adequacy of the allowance for impairment losses.

The Group regularly reviews its risk management policies and systems to reflect changes in markets products and emerging best practice.

These interim condensed consolidated financial statements do not include all financial risk management information and disclosures required in the annual financial statements. There have been material changes in the risk management policies and procedures as a result of adoption of IFRS 9 effective from 1 January 2018. The details of all the new/ revised policies and practices adopted, methodology of IFRS 9 implementation and related qualitative disclosures as a result of implementation of IFRS 9 have already been disclosed in interim condensed consolidated financial statements for the period ended 31 March 2018. There have been no material changes to these policies and practices in the current quarter.

#### 18.2 Loss allowance

The following table shows reconciliations from the opening to the closing balance of the loss allowance for loans and advances.

	30 September 2018			
	12 month ECL	Life time ECL not credit impaired	Lifetime ECL credit impaired	Total
	(SR'000)			
<b>Loans and advances to customers at amortized cost</b>				
Balance at 1 January	410,386	-	294,343	704,729
Impact of re-measurement due to adoption of IFRS 9	(268,094)	167,506	572,872	472,284
Balance at 1 January - restated	142,292	167,506	867,215	1,177,013
Transfer to 12-month ECL	94,346	(57,079)	(37,267)	-
Transfer to lifetime ECL not credit – impaired	(7,896)	14,373	(6,477)	-
Transfer to lifetime ECL credit impaired	(857)	(7,021)	7,878	-
Net charge for the period	(96,787)	38,826	244,807	186,846
Write-offs	-	-	(316,626)	(316,626)
Allowance written back upon restructuring of loan	-	-	3,117	3,117
<b>Balance as at 30 September</b>	<b>131,098</b>	<b>156,605</b>	<b>762,647</b>	<b>1,050,350</b>

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## NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) FOR THE NINE MONTH PERIOD ENDED 30 SEPTEMBER 2018 (CONTINUED)

### 19. 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.

Capital adequacy and the use of regulatory capital are monitored on a periodic basis by the Bank's management. SAMA requires holding the minimum level of the regulatory capital and maintaining a ratio of total eligible capital to the risk-weighted assets at or above the agreed minimum of 8%.

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 consolidated statement of financial position assets, commitments and notional amount of derivatives at a weighted amount to reflect their relative risk.

SAMA through its circular number 391000029731 dated 15/03/1439AH, which relates to the interim approach and transitional arrangements for the accounting allocations under IFRS 9, has directed banks that the initial impact on the capital adequacy ratio as a result of applying IFRS 9 shall be transitioned over five years.

The following table summarizes the Group's Pillar-I Risk Weighted Assets ("RWA"), Tier I and Tier II Capital and Capital Adequacy Ratios:

	<b>30 September 2018 (Unaudited) SR'000</b>	<b>31 December 2017 (Audited) SR'000</b>	<b>30 September 2017 (Unaudited) SR'000</b>
Credit Risk RWA	<b>45,726,325</b>	48,032,983	49,054,396
Operational Risk RWA	<b>4,778,292</b>	4,975,084	4,943,887
Market Risk RWA	<b>1,208,754</b>	1,127,857	873,253
<b>Total Pillar-I RWA</b>	<b>51,713,371</b>	<b>54,135,924</b>	<b>54,871,536</b>
Tier I Capital	<b>12,197,589</b>	8,941,872	8,752,830
Tier II Capital	<b>2,305,269</b>	2,396,689	2,407,888
<b>Total Tier I and II Capital</b>	<b>14,502,858</b>	<b>11,338,561</b>	<b>11,160,718</b>
Capital Adequacy Ratio (%)			
Tier I ratio	<b>23.59%</b>	16.52%	15.95%
Total Tier I and II Capital	<b>28.04%</b>	20.94%	20.34%

### 20. PROPOSED DIVIDEND

During the period ended 30 June 2018, the Bank paid final cash dividend of SR 262.4 million equal to SR 0.32 per share (September 2017: SR 200 million equal to SR 0.5 per share), net of zakat after approval of the shareholders' in their Extra Ordinary General Assembly meeting held on 9 May 2018. This dividend was calculated based on increased paid up capital of the Bank after the right issue i.e. 820 million shares.

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## NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED) FOR THE NINE MONTH PERIOD ENDED 30 SEPTEMBER 2018 (CONTINUED)

### 21. COMPARATIVE FIGURES

The following amounts have been reclassified from other general and administrative expenses to Fee and commission income, in line with presentation for the current period and consistent with presentation in the annual consolidated financial statements for year ended 31 December 2017.

For the nine month period ended 30 September 2017	As originally reported	Reclassification SR'000	Amounts reported after reclassification
Fee and commission income, net	496,748	(41,589)	455,159
Other general and administrative expenses	310,840	(41,589)	269,251
<b>For the three month period ended 30 September 2017</b>			
Fee and commission income, net	162,646	(15,823)	146,823
Other general and administrative expenses	110,354	(15,823)	94,531

During the current period, credit cards balances included in the consumer loans have been shown separately for better presentation and enhanced disclosures.

The impact of this reclassification on the amount reported in note 7 as of 31 December 2017 and 30 September 2017 is disclosed below. There was no impact on Interim Condensed Consolidated Statement of Financial Position.

	As originally reported	Reclassification SR'000	Amounts reported after reclassification
<b>As at 31 December 2017</b>			
Credit cards	-	463,377	463,377
Consumer loans	18,016,579	(463,377)	17,553,202
<b>As at 30 September 2017</b>			
Credit cards	-	480,348	480,348
Consumer loans	17,891,400	(480,348)	17,411,052

In addition, certain prior period amounts have been reclassified so as to align with the current period presentation.

### 22. APPROVAL OF INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

The interim condensed consolidated financial statements were authorized for issue by the Board of Directors on 23 Safar 1440H, corresponding to 1 November 2018.