Capital Adequacy and Risk Management Report

(Basel II Pillar 3)

as at 30th June 2008

September 2008

TABLE OF CONTENTS

1. Executive Summary

The following Capital Adequacy and Risk Management report is prepared in accordance with the public disclosure requirements and guidelines in respect of Pillar 3 of the Basel II Accord, as published by the Saudi Arabian Monetary Agency (SAMA) in March 2007. The intent is to encourage market discipline by allowing market participants to assess key pieces of information about the scope and effectiveness of application of an institution's risk measurement processes, risk management systems, and capital adequacy. This will be accomplished by further informing the market about a bank's risk exposure and by providing consistent and understandable disclosure that enhances comparability among institutions.

Samba Financial Group (Samba) has complied with the aforementioned requirements with effect from 1 January 2008, and this is the first report prepared by Samba under these guidelines.

Samba has adopted the Standardized Approach for credit risk, the Standardized Approach for market risk and the Standardized Approach for determining the capital requirements for operational risk.

The Capital Adequacy and Risk Management report provides details on the Group's risk profile, e.g. business volumes by customer categories and risk classes, which form the basis for the calculation of the capital requirement.

The Tier 1 Capital and Total Capital adequacy ratio's of Samba as at 30th June 2008, are 12.46% and 10.02% respectively, and are in accordance with the minimum capital requirements as prescribed under Pillar 1. Total Risk Weighted Assets amounted to SAR 158,451,364,000 comprised of 87.29% credit risk, 5.29% market risk and 7.42% operational risk.

2. Background

Samba Financial Group was incorporated pursuant to the Royal Decree number M/3 dated 26/3/1400H (February 12, 1980) to take over the two branches of Citibank N.A. in Jeddah and Riyadh, which had been opened in 1955 and 1966 respectively.

Samba is a Saudi Joint Stock company and operates under Commercial Registration Number: 1010035319 and is listed on the Saudi Stock Exchange (Tadawul) under symbol 1090.

Samba provides a full range of commercial banking services through its branches and subsidiaries. In compliance with the regulatory mandate of the Capital Market Authority (CMA) that requires all Saudi banks to separate their banking and commercial services from securities related business operations, Samba Capital and Investment Management Company (Samba Capital) was incorporated and licensed by the CMA. Samba Capital commenced its operations on 19 January 2008.

Samba provides commercial banking services such as loans, trade finance, asset management, consumer financing, credit cards, and treasury products to all customer segments including retail and corporate customers and Government institutions. Samba also provides a broad range of Shariah compliant banking products approved by Samba's Shariah Board an independent body of Shariah Scholars.

Samba operates through branches in London and Dubai, and was recently granted a licence by the Qatar Financial Centre to commence operations in Qatar. On March 30th, 2007 Samba also acquired a 68.4% share in Crescent Commercial Bank Limited (CCBL), Pakistan. CCBL is a banking company engaged in commercial banking and related services and is listed on all the stock exchanges in Pakistan.

The Pillar 3 information disclosed in this report is at the highest consolidated level i.e. Samba Financial Group including all branches and subsidiaries, as at 30th June 2008.

The information provided in this document has not been subject to an external audit.

A comparison with the previous year will be incorporated in subsequent Pillar 3 reports.

3. Introduction

In March 2008, SAMA issued a circular[1] allowing banks in the Kingdom to report their capital requirements according to the new Basel II guidelines. Basel II is an international initiative with the purpose to implement a more risk-sensitive framework for the assessment of risk and the calculation of regulatory capital i.e. the minimum capital that the institution must hold. The Basel II framework is intended to strengthen risk management practices and processes within financial institutions.

SAMA's Basel II framework[2] describes the following three pillars which are designed to be mutually re-enforcing and are meant to ensure a capital base which corresponds to the overall risk profile of the bank:

- Pillar 1: calculation of the capital adequacy ratio based on the charge for credit, market and operational risk stemming from its operations
- Pillar 2: The supervisory review process which includes:
    - o the Internal Capital Adequacy Assessment Process (ICAAP) to assess risks not covered under Pillar 1
    - o the quantification of capital required for these risks
    - o the assurance that the bank has sufficient capital (generated from internal/external sources) to cover these risks
- Pillar 3: Market discipline through public disclosures that are designed to provide transparent information on capital structures, risk exposures, risk mitigation and the risk assessment process.

[1] Circular 10243/ B.C.S. 124 dated 5 March 2008, titled 'Transition from Basel I to Basel II'
[2] SAMA Guidance Document issued on 31st May 2005, entitled 'New Basel II Framework Initial Implementation Document for Banks Operating in Saudi Arabia' and related guidelines issued during the course of implementation.

Pillar 1 – Minimum Capital Requirements:

Pillar 1 of the Basel II Accord, as adopted and implemented by SAMA, covers the minimum regulatory capital requirement that a bank is expected to maintain to cover credit, market and operational risk stemming from its operations. It also sets out the basis for the consolidation of entities for capital adequacy reporting requirements, the definition and calculations of Risk Weighted Assets (RWA) and the various options given to banks to calculate these Risk Weighted Assets.

The regulatory capital requirements are calculated according to the following formula (expressed as a percentage):

$$\text{Minimum Capital Requirements} = \frac{\text{Capital Base}}{\text{RWA}}$$

where the Minimum Capital Requirements are to be ≥ 8%

The RWA's are calculated using more sophisticated and risk sensitive methods than previously used under Basel I. In addition, operational risk is now included as a risk under the new Accord, supplementing the credit and market risk components previously used. The table below describes the approaches available for calculating the RWA's for each of the aforementioned risk types:

Credit Risk	**Market Risk**	**Operational Risk**
Standardized Approach	Standardized Approach	Basic Indicator Approach
Foundation Internal Ratings Based Approach	Internal Models Approach	Standardized Approach
Advanced Internal Ratings Based Approach		Advanced Measurement Approach

Samba has elected the following approach for each risk type:

a) Credit Risk

The Standardized Approach is currently being used by Samba for regulatory reporting purposes. This approach differs from the Basel I regulations in that it allows the use of external ratings from accredited ratings agencies for the determination of appropriate risk weights, and also includes a wider range of eligible financial collaterals.

The RWA's are then calculated according to the following formula:

RWA = Credit Equivalent Amount[3] x Regulatory Defined Risk Weight[4]

[3] Credit equivalent amount is determined as gross exposure less specific provisions less eligible credit mitigants. A credit conversion factor (CCF) or add-on percentage is then applied to off-balance sheet and derivative exposures respectively.

b) Market Risk

The capital requirement is based on Risk Weighted Assets as determined under the Standardized Approach for Market Risk as per the respective SAMA guidelines[5].

c) Operational Risk

Samba is currently adopting the Standardized Approach for the measurement of the capital required to cover operational risk. This approach applies a range of beta coefficients (12%-18%) to the average gross income for the preceding three financial years for each of eight predetermined business lines.

[4] The regulatory defined risk weight is determined by the counterparty asset class and the external rating of the counterparty, where applicable.
[5] As defined in SAMA's circular No. BCS 355 of Dec. 29,2004

Pillar 2 – Supervisory Review Process:

The Supervisory Review Process (SRP) requires banks to have an Internal Capital Adequacy Assessment Process (ICAAP) that is aimed at capturing a charge for risks not covered under Pillar 1 (e.g. interest rate risk in the banking book, strategic risk and legal risk). This is designed in order to ensure that banks in the Kingdom have sufficient capital to meet regulatory and internal capital requirements during periods of systemic/cyclical economic downturns or tranches of financial distress.

Samba had submitted its initial ICAAP on the 30th April 2008 and will entrench the process into the upcoming budget cycle.

Pillar 3 – Market Discipline:

Under this pillar the Accord prescribes the qualitative and quantitative disclosures which are required to be made to external stakeholders of the bank[6]. The disclosures are designed to enable stakeholders and market participants to assess an institution's risk appetite and risk exposures and to encourage all banks, to move toward more advanced forms of risk management.

A reporting calendar has also been provided to indicate which disclosures are required at the defined intervals. Quarterly requirements are disclosed in the quarterly financial statements, semi-annual disclosures are contained in this report, and annual disclosures will be done in the annual financial statements of the bank.

[6] SAMA circular 19402/B.C.S 378 dated 24 May 2007, entitled ' Basel II-Consultative Draft : Pillar 3 Disclosure Requirements and Guidance Notes'

4. Risk and Capital Management in Samba Financial Group

In this chapter, the consolidation principles for the capital base within Samba are described, as well as the principles for the management and control of risk and capital.

4.1. Group structure

The Bank follows the Accounting Standards for Financial Institutions promulgated by the Saudi Arabian Monetary Agency (SAMA) and International Financial Reporting Standards (IFRS). The Bank also prepares its consolidated financial statements to comply with the Banking Control Law and the Regulations for Companies in the Kingdom of Saudi Arabia.

The consolidated financial statements as at June 30, 2008 include financial statements of the Bank and its following subsidiaries:

Samba Fund Management (Guernsey) Limited: A wholly owned subsidiary incorporated in Guernsey and specializing in the management of mutual funds.

Crescent Commercial Bank Limited (CCBL): A 68.4% owned subsidiary incorporated as a banking company in Pakistan and engaged in commercial banking and related services. CCBL is listed on all stock exchanges in Pakistan.

Samba Real Estate Company: A wholly owned subsidiary incorporated in Saudi Arabia under commercial registration no. 1010234757 issued in Riyadh dated 9 Jumada II, 1428H (June 24, 2007). The company has been formed as limited liability company with the approval of SAMA and is engaged in managing real estate projects on behalf of Samba Real Estate Fund.

Samba Capital and Investment Management Company: A wholly owned subsidiary incorporated in Saudi Arabia under commercial registration number 1010237159. It was formed in accordance with the Securities Business regulations issued by the Capital Market Authority (CMA), requiring banks in Saudi Arabia to transfer their dealing, arranging, managing, advising and custody businesses into a separate legal entity licensed with CMA.

Co-Invest Offshore Capital Limited (COCL): A wholly owned company incorporated under the laws of Cayman Island for the purpose of managing certain overseas investments.

The aggregation consolidation method is applied to subsidiaries reporting in other regulatory jurisdictions. To this end CCBL calculates it's Risk Weighted Assets according to the regulations defined by the State Bank of Pakistan

4.2. Risk and Capital Management

Samba activities involve the analysis, evaluation, approval and management of risks. Our policies are designed to identify and quantify these risks, set appropriate limits and controls and monitor adherence to the limits. The most important risks assumed by Samba are credit risk, including cross-border risk, market risk, liquidity risk, operational risk and reputation/ franchise risk.

The Executive Committee of the Samba Board formulates high level strategies and policies, determines institutional risk appetite and approves specific transactions or programs that may pose material risks to the institution. This Committee, which has been appointed by the Samba Board of Directors, comprises three Board Members in addition to the Managing Director and Chief Executive Officer

The process of risk management is supported by a set of independent control functions reporting to the Chief Risk Officer. Individual credit transactions are approved jointly by selected Credit Officers including both Business and Independent Risk Management representatives. The Credit Risk Control department reviews approval levels and documentation prior to allowing the availment of facilities. Market Risk reviews limits and provide independent reports about the bank's market risk exposures and liquidity position including stress tests. Risk and Portfolio Department manages the process of risk appetite definition, portfolio targets and overall limit settings.

The risk governance structure includes the following committees:

- Asset Liabilities Committee (ALCO), chaired by the Managing Director is responsible for monitoring and managing of the capital, liquidity, balance sheet and the market risk resulting from the accrual portfolio.
- Market Risk Policy Committee is the highest-level management body within Samba for market and liquidity risk issues, including establishing and updating corporate policies and guidelines, reviewing and approving market risk limits and exceptions thereto.
- The Credit Risk Policy Committee (CRPC) has Samba-wide responsibility for maintaining a sound, effective credit risk management architecture.
- The Capital Management Committee proposes the internal capital adequacy plan for approval by the Executive Committee, allocation of capital across units, setting risk adjusted return targets and monitoring compliance with the approved capital plan.

Samba Audit Risk Review reports functionally to the Audit Committee of the Samba Board and has responsibility for:

- Providing independent evaluations of the Bank's credit portfolio and processes.
- Assessing the adequacy of the Bank's policies, practices, and procedures for credit management.
- Documenting its findings in action-oriented reports to the relevant Board / Management Committees and Senior Management.

5. Regulatory Capital Requirements

This chapter describes the regulatory capital requirements in Samba. The risk types are based on Pillar 1 in the Basel II guidelines issued by SAMA[7] and contain credit, market and operational risk.

Samba's overall capital requirement can be broken down as follows:

Risk type	Capital Requirement (SAR 000's)	% of Total Requirement
Credit Risk	11,064,648	87.29 %
Market Risk	670,321	5.29 %
Operational Risk	941,140	7.42 %
Total	**12,676,109**	**100.00%**

5.1. Capital requirements for credit risk

Samba calculates the capital requirements for credit risk according to the Standardized Approach. Under this approach, exposures are assigned to portfolio segments based on the type of counterparty and/or the nature of the underlying exposure. The major portfolios defined are sovereigns, banks, corporates, retail, securitized assets and VIP/HNI (high net worth individuals). Each segment has a defined risk weight ranging from 0% to 150%, depending on whether the counterparty has an external rating or not.

The following table describes the amount of exposures subject to credit risk and the related capital requirements, by portfolio:

SAR 000's

Portfolio	Amount of exposures	RWA	Capital requirements
Sovereigns and central banks	54,244,167	838,929	67,114
Public sector entities	54,945	10,990	879
Banks and securities firms	16,760,684	5,637,884	451,030
Corporates	89,644,757	88,655,203	7,092,416
Retail non-mortgages	17,609,967	13,203,851	1,056,308
Mortgages – residential & commercial	13,402	4,691	375
Equities	16,282	16,557	1,325
Securitized & other assets	9,178,894	9,178,894	734,312
VIP/HNI	16,705,683	16,705,683	1,336,455
Others	8,573,806	4,055,744	324,434
Total	**212,802,587**	**138,308,422**	**11,064,648**

[7] Refer footnote on page 5

Note that the exposures are on OSUC basis (i.e. Outstandings, Un-used commitments and pre-settlements – which will be not comparable with the financial numbers). Exposures here are stated after taking into account the effects of aggregate credit risk mitigant amounting to SR 6,236,923,000 where applicable. Credit risk mitigation is described in detail in chapter 6.3 of this report.

A definition of each portfolio is described in detail in chapter 6 of the report.

5.2. Capital requirements for market risk

Samba uses the Standardized Approach to calculate the regulatory capital requirements relating to general market and specific market risk. The resultant measure of market risk is multiplied by 12.5, the reciprocal of the theoretical 8% minimum capital ratio, to give market risk-weighted exposure on a basis consistent with credit risk-weighted exposure. The primary market risks to which the bank is exposed are foreign exchange risk, interest rate risk, equity price risk and commodity price risk associated with its trading, investment and asset and liability management activities.

Brief descriptions of the risk items covered by market risk are described below:

a. Interest rate risk is the impact on banks earnings and market value of equity of changes in interest rates; the risk is two-fold:

- Specific Risk: risk of loss caused by an adverse price movement of a debt instrument or security due principally to factors related to the issuer.

- General Market Risk: risk of loss arising from adverse changes in market conditions.

b. Equity risk is the risk that the bank's investments will depreciate due to equity market dynamics.

c. Foreign exchange risk is the risk arising from a change in exchange-rates on bank's net asset / liability positions.

d. Commodity risk refers to the uncertainties of future market values and of the size of the future income, caused by the fluctuation in the prices of commodities.

The calculated capital requirements are presented in the table below:

SAR 000's

Market Risk Type	RWA	Total Capital Requirement
Interest rate - general risk	2,701,750	216,092
Interest rate – specific risk	273,037	21,843
Equity position risk	3,364,988	269,199
Foreign exchange risk	2,003,010	160,241
Commodity risk	36,825	2,946
Total		**670,321**

5.3. Capital requirements for operational risk

Samba uses the Standardized Approach for the calculation of the regulatory capital requirements in terms of operational risk. This approach applies a range of beta coefficients (12%-18%) to the average gross income for the preceding three financial years for each of eight predetermined business lines. The capital requirements are detailed in the table below:

SAR 000's

Business line	Beta Coefficient	Total Capital requirement
Corporate Finance	18%	
Trading and Sales	18%	
Retail Brokerage	12%	
Commercial Banking	15%	941,140
Retail Banking	12%	
Payment and Settlement	18%	
Agency Services	15%	
Asset Management	12%	

5.4. Capital structure

Samba maintains an actively managed capital base to cover risks inherent in the business. The adequacy of the banks capital is monitored using, among other measures, the rules and ratios established under the Basel Accord, as adopted by SAMA[8].

The primary objectives of Samba's capital management are to ensure that it complies with the capital requirements of SAMA and is able to maintain strong credit ratings and healthy capital ratios in order to support its business and to maximize the shareholder's value. In order to maintain or adjust the capital structure, Samba may adjust the amount of dividend payment to shareholders, or issue capital securities.

The total eligible capital (tier 1 and 2) calculated in accordance with SAMA guidelines is a follows:

SAR 000's

Components of capital	Amount
Eligible paid-up share capital	9,000,000
Eligible reserves & Retained earnings	6,518,602
Minority interests in the equity of subsidiaries	385,440
Deductions from Tier I:	
Intangible assets (including goodwill)	(34,690)
Total Tier I	**15,869,352**
Qualifying general provisions & current period profits	3,869,882
Total Tier II	**3,869,882**
Total eligible capital	**19,739,234**

[8] Refer footnote 2 page 5.

5.5. Capital Adequacy Ratio's (Pillar 1)

Entity	Total capital ratio %	Tier 1 capital ratio
Samba Financial Group - consolidated	12.46%	10.02%
Crescent Commercial Bank Ltd.	62.15%	60.85%

Samba has consistently maintained its capital adequacy ratio above the regulatory minimum of 8%. As at the end of December 2007, the capital ratio under Basel I regulations was 15.2%. The decrease in the ratio following the implementation of Basel II is primarily due to:

a. the inclusion of Operational Risk as an additional capital requirement according to the new regulations
b. the inclusion of Market Risk.
c. the growth in the RWA of Samba financial group due to a growth in the underlying credit risk assets.

6. Credit risk

In this chapter, the credit risk and its components are described with respect to:

a. The exposure classes used in the calculations of RWA and capital requirement are defined and explained.
b. The information about exposures is disclosed and presented from several aspects, split by exposure classes, geography and industry.
c. The approaches and methods used in the RWA calculations are presented including information about credit risk mitigation.
d. The information about impaired loans and loan losses is disclosed.

6.1. Exposure classes

Samba has a diversified credit portfolio, which can be divided into the following exposure classes as defined by SAMA[9]:

Sovereigns and central banks
Exposures to sovereigns and central banks carry a risk weight ranging between zero and 100 percent, depending on the external rating provided by the relevant ECAI's. Samba's average risk weight for this portfolio is 1.55%.

Banks and securities firms
SAMA has prescribed that exposures falling into this portfolio are to be treated according to Option 2 of the Basel Accord i.e. the risk weight is determined on the external rating of the bank by a recognized ECAI. A preferential risk weight is assigned to short term exposures, defined as those exposures with a tenor of less than three months. Samba's average risk weight for this portfolio is 33.6%.

Corporates
This portfolio is also assigned a risk weight based on the external rating wherever available of the counterparty with whom the exposure is held. Due to the fact that the majority of the corporates in Saudi Arabia are unrated, a regulatory risk weight of 100% is applied to a large portion of this portfolio. Samba's average risk weight for this portfolio is 98.8 %.

Retail non-mortgages
This portfolio consists of loans to individuals, leases, small business facilities, or car loans and other consumer loans. SAMA excludes certain exposures from this portfolio, based on granularity criteria applied to the individual and relative size of the exposure within the portfolio. The balance of the exposure is assigned a flat 75% risk weight.

Securitized & other assets
Samba's exposures which fall into this category primarily include Auto Installment Sales Receivables, Sukuks as well as CDO's and CLO's. In accordance with SAMA's

[9] Per paragraph 4.1 of "Basel II- SAMA's Detailed Guidance Document Consultative Draft no 2.", issued 6 June 2006

guidelines issued in this regard, this portfolio is assigned a 100% risk weight. In this context, Samba acts only as an investor in these exposures, not an originator.

VIP/HNI

This portfolio has been defined to include exposures to VIP accounts and high net worth individuals that do not meet the criteria for Retail exposures. These would therefore include exposures to individuals in excess of SAR 5million and they are not managed on a pool basis. For regulatory purposes these exposures are assigned a 100% risk weight.

Others

The standard risk weight for all other assets is prescribed at 100%. These typically include fixed assets, prepayments and sundry debtors. Cash and cash equivalents are assigned a risk weight of 0%. Samba's average risk weight for this portfolio is 47.3%.

6.2. Credit Exposure

6.2.1 Gross Credit Exposure

The gross credit exposure as presented in the table below is reflected before applying any credit risk mitigation, such as financial collateral and guarantees.

SAR 000's

Portfolio	Gross credit risk exposure
Sovereigns and central banks	54,244,136
Public sector entities	54,945
Banks and securities firms	10,874,079
Corporates	69,927,978
Retail non-mortgages	17,598,389
Mortgages – residential & commercial	13,433
Securitized assets	9,178,894
Equities	16,282
VIP/HNI	21,322,989
Others	5,736,505
On-balance sheet	**188,967,630**
Off-balance sheet	**23,574,495**
Derivatives*	**6,497,406**
Total Gross Credit Exposure	**219,039,531**

The average gross credit risk exposure has not been disclosed as it does not differ materially from the figures presented above.

* The gross credit exposure for derivative and foreign exchange instruments is the replacement cost (current exposure) representing the cost of replacing the contracts at current market rates should the counterparty default prior to settlement date. It does not include the add-on for potential future exposure which is used to determine the RWA amount for these exposures.

6.2.2 Geographic breakdown of on-balance sheet credit risk exposures

SAR 000's

Portfolio	Geographic area						
	Saudi Arabia	Other GCC & Middle East	Europe	North America	South East Asia	Other	Total
Sovereigns and central banks	43,322,740	64,286	3,633,129	6,964,240	259,741	-	54,244,136
Public sector entities	-	-	-	-	54,945	-	54,945
Banks and securities firms	911,233	588,693	3,922,681	4,531,527	737,430	182,515	10,874,079
Corporates	64,626,124	1,172,366	3,529,360	194,314	118,819	286,995	69,927,978
Retail non-mortgages	17,457,813	-	-	-	140,576	-	17,598,389
Mortgages – retail and commercial	-	-	-	-	13,433	-	13,433
Securitized assets	1,971278	1,087,795	3,583,460	1,458,262	608,069	470,030	9,178,894
Equities	-	-	-	-	16,282	-	16,282
VIP/HNI	20,935,916	63	79,408	306,186	1,416	-	21,322,989
Others	5,585,870	-	-	-	150,635	-	5,736,505
Total	**154,810,974**	**2,913,203**	**14,748,038**	**13,454,529**	**2,101,346**	**939,540**	**188,967,630**

From the table above it can be seen that more than 80% of Samba's portfolio is concentrated in Saudi Arabia, thereby shielding it largely from the global financial markets. Through its recent expansion via acquisitions in Pakistan, coupled with the opening of branches in Dubai and Qatar, Samba is seeking to geographically diversify its exposure.

6.2.3 Industry sector breakdown of on-balance sheet credit risk exposures

SAR 000's

Portfolio	Industry sector											
	Govern-ment and quasi govern-ment	Finance	Agricul-ture and fishing	Manufac-turing	Mining and quarry-ing	Electricity, water, gas and health services	Building and construc-tion	Commerce	Transpor-tation and communi-cation	Services	Consumer loans and credit cards	Others
Sovereigns and central banks	54,244,136	-	-	-	-	-	-	-	-	-	-	-
Public sector entities	54,945	-	-	-	-	-	-	-	-	-	-	-
Banks and securities firms	-	10,874,079	-	-	-	-	-	-	-	-	-	-
Corporates		615,618	1,994,138	11,401,216	765,555	1,474,495	6,988,387	16,520,111	8,627,295	2,995,661		18,545,502
Retail non-mortgages											17,598,389	
Mortgages-retail and commercial											13,433	
Securitized assets	260,693	5,823,336				504,042						2,590,823
Equities								16,282				
VIP/HNI		428,389		7,308			209,505	258,276		755,146		19,664,365
Others												5,736,505
Total	**54,559,774**	**17,741,422**	**1,994,138**	**11,408,524**	**765,555**	**1,978,537**	**7,197,892**	**16,794,669**	**8,627,295**	**3,750,807**	**17,611,822**	**46,537,195**

6.2.4 Maturity breakdown of on-balance sheet credit risk exposures

The maturity profile of the credit exposures based on contractual maturity dates was as follows:

SAR 000's

Portfolio	Maturity breakdown								
	Less than 8 days	8-30 days	30-90 days	90-180 days	180-360 days	1-3 years	3-5 years	Over 5 years	Total
Sovereigns and central banks	736,400	2,758,026	10,787,420	3,245,291	13,557,246	7,625,479	5,172,765	10,361,509	54,244,136
Public sector entities								54,945	54,945
Banks and securities firms	1,205,813	1,785,983	209,621	225,820	667,740	1,132,599	293,438	5,353,065	10,874,079
Corporates	1,933,764	6,857,788	11,580,132	12,248,757	18,075,357	5,055,715	5,919,666	8,256,799	69,927,978
Retail non-mortgages			11,466	49,816	1,671,095	2,669,150	7,383,151	5,813,711	17,598,389
Mortgages – retail and commercial								13,433	13,433
Securitized assets		38,439		87,552	115,951	548,208	3,538,873	4,849,871	9,178,894
Equities								16,282	16,282
VIP/HNI	709,466	2,274,874	1,196,618	1,612,415	14,977,872	323,648	128,096	100,000	21,322,989
Others								5,736,505	5,736,505
Total	**4,585,443**	**13,715,110**	**23,785,257**	**17,469,651**	**49,065,261**	**17,354,799**	**22,435,989**	**40,556,120**	**188,967,630**

6.2.5. Allocation of on-balance sheet exposures to risk weight buckets

An analysis of the portfolio by the regulatory risk weight buckets is presented in the table below:

SAR 000s

Portfolio	Risk buckets					
	0%	20%	50%	75%	100%	150%
Sovereigns and central banks	53,405,207				838,929	
Public sector entities		54,945				
Banks and securities firms		6,705,420	4,030,656		138,001	
Corporates		136,639	1,356,624		68,428,160	8,146
Retail non-mortgages				17,596,799		
Mortgages – retail and commercial			13,433			
Securitized assets					9,178,894	
Equities					15,733	550
VIP/HNI					21,322,989	
Others					5,736,505	
Total	**53,405,207**	**6,897,004**	**5,400,713**	**17,596,799**	**105,659,211**	**8,696**

Exposures attracting a 0% risk weight are primarily to sovereigns and central banks which are historically extremely low risk. The 20% risk weight is applied to highly rated banks and corporates, whereas 50% is applied to lesser rated entities in the aforementioned asset classes. Retail exposures attract a 75% risk weight, while the balance of the asset classes attracts a100% risk weight. Past due exposures whose level of provisioning is up to 20% of the outstanding exposure are assigned a 150% risk weight.

6.3. Credit risk mitigation

The gross credit exposures disclosed in the prior sections have been stated prior to taking credit mitigation effects into account. In terms of the regulatory guidelines, not all forms of collateral currently used by Samba are recognized for the purposes of the calculation of the credit risk capital requirement. These include, inter alia, corporate and personal guarantees, shares and covenants. The bank uses the comprehensive method for the treatment of financial collaterals which requires a standard supervisory haircut to be applied to the collateral to account for currency and maturity mismatches between the underlying exposure and the collateral applied. The exposures with their corresponding credit risk mitigants are disclosed by portfolio in the table below:

SAR 000's

Portfolio	Gross Exposure	Covered by eligible financial collateral
Corporates	69,927,978	1,100,627
Retail non-mortgages	17,598,389	2,599
VIP/HNI	21,322,989	5,133,697
Total		6,236,923

Eligible financial collaterals under the Standardized Approach include[10]:

a. Cash (as well as certificates of deposit or comparable instruments issued by the lending bank);
b. Gold; and
c. Debt securities

[10] Per paragraph 15.4 of Additional Guidance Notes GN-2 contained in the "Basel II Package of Bank Returns and guidance Notes Regarding the Standardized Approach", issued on 29 March 2007 by SAMA.

6.4. Impaired credit facilities and provisions for impairment

A specific provision (for accounting treatment of impairment in assets) is made for past due facilities in respect of individually assessed loans or claims. Samba calculates the specific provision according to the guidelines contained in IAS 39[11]. These are calculated at counterparty level and the bank considers all the facilities for a counterparty to be defaulted if any one of the facilities of the counterparty is past due. The specific provisions are based on an assessment of the impairment in realizable value of the asset first at the facility level and then aggregated at the counterparty level.

6.4.1 Impaired Loans, past due loans and Allowances (by industry sector)

SAR 000's

Industry sector	Impaired loans	Defaulted	Specific allowances	Portfolio Allowances[12]
Finance	1,102		1,102	
Agriculture and fishing	79,124		79,124	
Manufacturing	57,199		52,462	
Mining and quarrying	46,572		47,483	
Electricity, water, gas and health services	35,615		35,628	
Building and construction	351,821		182,417	
Commerce	266,922		232,301	
Transportation and communication	88,131		81,843	
Services	113,126		98,742	
Others	794,436		732,823	
Total	1,834,048		1,543,925	1,449,594

[11] "IAS 39: Financial Instruments: Recognition and Measurement" as issued by the International Accounting Standards Board
[12] Portfolio allowances, by their underlying nature, are not allocated to individual exposures and therefore cannot be distributed across industries

6.4.2 Impaired Loans, past due loans and Allowances (by geographic area):

SAR 000's

Geographic area	Impaired loans	Specific allowances	Portfolio allowances
Saudi Arabia	1,701,905	1,420,435	
Other GCC & Middle East	1,143	1,102	
South East Asia	131,000	122,388	
Total	1,834,048	1,543,925	1,449,594

6.4.3 Reconciliation of changes in the allowances for Loan Impairment

SAR 000's

Particulars	Specific allowances	Portfolio allowances
Balance, beginning of the year	1,545,689	1,453,736
Charge-offs taken against the allowances during the period	(829)	-
Amounts set aside (or reversed) during the period	(8,467)	16,850
FX Translation difference (overseas Subsidiary)	(13,460)	-
Transfers between allowances	20,992	(20,992)
Balance, end of the period	1,543,925	1,449,594

7. Operational Risk

In this chapter, the management of operational risk is described. Operational risk is defined as the risk of loss resulting from inadequate or failed internal processes, people, systems and /or external events. It is evident that Operational risk is inherent in all activities within the organisation, in outsourced activities and in all interactions with external parties. Management of Operational Risk requires robust internal controls coupled with quality supervision and management. The key to successful Operational Risk Management is an integrated risk management framework aligned with leadership and a Risk-enabled culture.

In Samba, Operational Risk Management is an integrated umbrella with all the underlying Operational Risk elements like Anti-Fraud, Quality Assurance, Business Continuity, and Policy & Procedure forming a part of the risk management chain. Operational Risk is embedded into each Business area and the Risk Mitigation technique applied to each activity. All Products / Services are covered in the Self-Assessment Grids which are independently tested periodically and monitored on a global basis. The exceptions and quality deficiencies are documented and monitored for its resolution on a Samba-wide basis. These are complemented by comprehensive reviews by Internal Audit / Quality Assurance unit. The analysis of operational risk-related events, potential risk indicators and other early-warning signals are in focus when developing the processes. The exceptions / issues are highlighted and resolved at the senior levels in Country Business Risk & Compliance Committee (CBRCC). The global KRIs for the Top Ten Operational Risk for the Bank as a whole are monitored and the exceptions along with the heat map is escalated to the Senior Management for its resolution.

The mitigating techniques include robust Information Security framework, strong Anti-Fraud / Compliance regime, comprehensive Physical / Access security and Certified Business Continuity plans together with crisis management preparedness and a broad insurance coverage for handling major incidents.

Each business area in Samba is primarily responsible for managing its own operational risk. Operational Risk Division develops and maintains a framework for identifying, assessing, monitoring and controlling operational risk and supports the line organisation in implementing the framework. Automation of Operational Risk constituents like Loss Data Base, Risk & Control Self-Assessment process, KRIs and the corrective Action tracking have added fillip to the Risk Management efforts.

The techniques and processes for managing operational risk are structured around the risk sources as described in the definition of operational risk. This approach improves the comparability of risk profiles throughout the organisation including Samba's branches and subsidiaries. It also supports the concentration on limiting and mitigating measures in relation to the sources, rather than the symptoms.

As described in chapter 5.3 the capital requirement for operational risk is calculated according to the standardised approach, in which all of the institution's activities are divided into eight standardised business lines and the total capital requirement for operational risk is calculated as the sum of the capital requirements for each of the business lines for each entity. The risk for each business line is the beta coefficient multiplied by the average of the gross income from the preceding three financial years, where the beta coefficients differ between business lines and are in the range of 12% to 18%. Consequently, the operational risk is updated on an annual basis.

8. Other Risks (Pillar 2)

In line with best practices in the banking industry and SAMA's directives[13], Samba is integrating capital planning and risk appetite definitions into its regular budgeting and planning process.
The current ICAAP process results in the calculation of the expected risk impact resulting from our strategies for the ensuing three year period and helps to evaluate whether the banks' capital funds are sufficient to support this level of risk. It also considers the impact on capital as a result of stress conditions and addresses means to raise capital should it fall below the stipulated levels.

For this purpose, two levels of risk have been used as per regulatory guidelines:

- So called "Pillar 1" risks, which include Credit Risk, Market Risk and Operational Risk. For such risks the minimum regulatory ratio is 8%.

- So called "Pillar 2" risks which follow a wider definition and include additional risks such as Interest Rate Risk in the Banking Book, Strategic Risks, and Legal Risk etc... There is no minimum regulatory ratio for these risks, but banks are expected to maintain at all times sufficient capital to cover these risks.

Management is recommending that to cover both risks, minimum target levels of capital be set and monitored.

The three year plans / strategy have been tested against these targets and it can be confirmed that Samba should remain within the set targets, barring any large inorganic growth or deterioration in the economic environment which will be addressed at appropriate times. The projections have also been stress-tested to two recession scenarios. While Samba would remain at all times within the regulatory minimum, a severe recession or a prolonged mild recession scenario could put the bank in temporary breach of the Pillar 2 target that could be corrected within a few months by, for example, slowing down risk-taking.

As part of the process a Capital Management Committee has been instituted comprising of senior executive management who will review actual quarterly capital ratios against the above targets and initiate corrective actions if certain trigger levels are met. The committee will also meet to evaluate capital impact of major strategic decisions including acquisitions etc

The Integrated Capital Plan shows that Samba's current and foreseen capital endowment is suitable to support its business strategy in the future. A set of adequate tools is in place to monitor this process going forward and the exercise has strengthened the awareness of risk appetite and capital needs within Samba.

[13] Per "SAMA's Draft Guidelines on the Internal Capital Assessment Plan (ICAAP)" issued by SAMA in December 2007.

Sensitivity Analysis of Interest Rate Risk in the Banking Book

The sensitivity analysis of the interest rate risk in the banking book is presented in the table below:

SAR 000's

200bp Interest Rate Shocks for currencies with more than 5% of Assets or Liabilities	
Rate Shocks	**Change in earnings**
Upward rate shocks:	
SAR	1,064,303
USD	(1,198,196)
EUR	(468,476)
Downward rate shocks:	
SAR	(1,082,319)
USD	1,221,606
EUR	477,166

9. Glossary

Add-On

Basel-II-defined factor to reflect the potential future increase in exposure stemming from derivatives transactions.

ALCO (Asset and Liability Management Committee)

Committee in the governance process responsible for the development (and follow-up of implementation) of the ALM framework. The activities of the ALCO entail asset allocation, setting internal limits, decision-taking on investments for the ALM positions, the use of ALM opportunities to stimulate specific commercial initiatives, the monitoring of the impact on and of the policies of the business units, and reporting on the ALM profile.

ALM (Asset and Liability Management)

The ongoing process of formulating, implementing, monitoring and revising strategies for on-balance-sheet as well as on off-balance-sheet items, in order to achieve an organisation's financial objectives, given the organisation's risk tolerance and other constraints.

Asset class

A classification of credit exposures according to the SAMA Basel II regulatory guidelines. The main classes are Sovereigns, Bank and Financial Institutions, Corporates, Retail and VIP/HNI. Classification depends on the type of obligor, the total annual sales of the obligor, the type of product and the exposure value.

Banking book

Samba’s banking book is defined as all positions in the group that are not in the trading book. A trading book consists of positions in financial instruments and commodities held either with trading intent or in order to hedge other elements of the trading book. To be eligible for trading book capital treatment, financial instruments must either be free of any covenants restricting their tradability or be able to be hedged completely. In addition, positions should be frequently and accurately valued, and the portfolio actively managed.

Beta factor

The capital charge for a business line in the context of operational risk is approximated by multiplying the gross income of that business line with the beta (ß) factor. Thus the ß factor serves as a proxy for the industry-wide relationship between the operational risk loss experience for a given business line and the aggregate level of gross income of that business line.

Business risk

The potential negative deviation from the expected economic value of the organisation due to changes in the volumes and operational margins resulting from changes in the environment of the organisation and inappropriate or inadequately implemented strategies

CAR (Capital Adequacy Ratio)

Total eligible capital / Risk-weighted assets (the result must be at least 8% according to the Basel regulations)

CDO (Collateralised Debt Obligation)

A type of asset-backed security and structured credit product. CDOs are constructed from a portfolio of fixed-income assets.

CDS (Credit Default Swap)

A privately negotiated bilateral agreement where one party (the protection-buyer or risk-shedder) pays a premium to another party (the protection-seller or risk-taker) in order to secure protection against any losses that may be incurred through exposure to a reference entity or investment as a result of an unforeseen development (or 'credit event').

CLO (Collateralised Loan Obligation)

CDO holding only loans as underlying assets.

Credit risk

Credit risk is the potential shortfall relative to the value expected consequent on non-payment or non-performance by an obligor (a borrower, guarantor, counterparty to an inter-professional transaction or issuer of a debt instrument), due to that party's insolvency or lack of willingness to pay, or to events or measures taken by the political or monetary authorities of a particular country. The latter risk is also referred to as 'country risk'.

EAD (Exposure At Default)

The amount expected to be outstanding if and when an obligor defaults. At the time of default, it is equal to the actual amount outstanding, and therefore is no longer an expectation.

Haircuts

The difference between the market value of a security and its collateral value. Haircuts are taken in order to account for a possible decline in the market value of a collateralising security upon liquidation.

ICAAP (Internal Capital Adequacy Assessment Process)

The internal process a bank should have in place for assessing its overall capital adequacy in relation to its risk profile, as well as its strategy for maintaining adequate capital levels in the future.

Interest rate risk

The potential negative deviation from the expected net asset value of the trading book or the financial investment book due to changes in the level or in the volatility of interest rates.

IRB (Internal Ratings-Based)

An approach defined in the Basel regulations to calculate the credit-risk-related capital requirements, where a financial institution uses its own models to perform the calculation. There are two possibilities: the IRB Foundation or the IRB Advanced approach. When applying the IRB Foundation approach, internal estimates of the Probability of Default are used to calculate minimum requirements, while the IRB Advanced methodology also takes into account the internal estimates of Exposure At Default and Loss Given Default.

Liquidity risk

The potential that an organisation will be unable to meet its obligations as they fall due because of the inability to liquidate assets or obtain adequate funding (liability liquidity risk) or the risk that it cannot easily unwind or offset specific exposures without significantly lowering market prices because of inadequate market depth or market disruptions (asset liquidity risk).

Market risk

Market risk is the potential negative deviation from the expected economic value of a financial instrument caused by fluctuations in market prices, i.e. interest rates, exchange rates and equity or commodity prices.

Market value

The cost that would be incurred or the gain that would be realised if an outstanding contract was replaced at current market prices (also called replacement value).

Mark-to-Market

The act of assigning a market value to an asset

Operational Risk

The potential negative deviation from the expected economic value of the organisation resulting from inadequate or failed internal processes, people and systems or from external events. This definition includes legal, IT and tax risk.

OTC (Over The Counter)

An over-the-counter contract is a bilateral contract where two parties agree on how a particular trade or agreement is to be settled in the future. It is usually a direct contract between a (an investment) bank and its clients. It contrasts with exchange trading, which occurs via corporate-owned facilities constructed for the purpose of trading (i.e. exchanges).

RBA (Ratings-Based Approach)

Basel II approach for calculating the risk-weighted assets applied to securitisation exposures that are externally rated, or where a rating can be inferred.

RWA (Risk-Weighted Asset)

An exposure weighted according to the 'riskiness' of the asset concerned. 'Riskiness' depends on factors such as the probability of default by the obligor, the amount of collateral or guarantees and the maturity of the exposure.

SAMA (Saudi Arabian Monetary Agency)

The regulatory entity responsible for the supervisory review of banks within the Kingdom of Saudi Arabia

Trading book

The trading book consists of positions in financial instruments and commodities held either with trading intent or in order to hedge other elements of the trading book. Positions held for trading intent are those held intentionally for resale in the short term and/or with the intent of benefiting from actual or expected price movements in the short term or to lock in arbitrage profits.