

**Independent Auditors' Report on the Audit of the Consolidated Financial Statements
to the Shareholders of The Saudi British Bank (a Saudi Joint Stock Company)**

Report on the Audit of the Consolidated Financial Statements

Opinion

We have audited the consolidated financial statements of The Saudi British Bank (“SABB” or “the Bank”) and its subsidiaries (collectively referred to as “the Group”), which comprise the consolidated statement of financial position as at 31 December 2018, and the consolidated statement of income, consolidated statement of comprehensive income, consolidated statement of changes in equity and consolidated statement of cash flows for the year then ended, and notes to the consolidated financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the consolidated financial position of the Group as at 31 December 2018, and its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with International Financial Reporting Standards (“IFRS”) as modified by the Saudi Arabian Monetary Authority (“SAMA”) for the accounting of zakat and income tax.

Basis for Opinion

We conducted our audit in accordance with International Standards on Auditing that are endorsed in the Kingdom of Saudi Arabia. Our responsibilities under those standards are further described in the *Auditors' Responsibilities for the Audit of the Consolidated Financial Statements* section of our report. We are independent of the Group in accordance with the professional code of conduct and ethics as endorsed in the Kingdom of Saudi Arabia that are relevant to our audit of the consolidated financial statements, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Key Audit Matters

Key audit matters are those matters that, in our professional judgement, were of most significance in our audit of the consolidated financial statements for the year ended 31 December 2018. These matters were addressed in the context of our audit of the consolidated financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters. For each matter below, a description of how our audit addressed the matter is provided in that context.

**Independent Auditors' Report on the Audit of the Consolidated Financial Statements
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Report on the Audit of the Consolidated Financial Statements (Continued)

Key Audit Matters (continued)

Key audit matter	How our audit addressed the key audit matter
<p>Impairment of loans and advances</p> <p>As at 31 December 2018, the gross loans and advances of the Group were SAR 115.08 billion against which an impairment allowance of SAR 4.75 billion was maintained.</p> <p>During the year the Group has adopted IFRS 9, which introduced a forward-looking, expected credit loss (“ECL”) impairment model. On adoption, the Group has applied the requirements of IFRS 9 retrospectively without restating the comparatives. The adoption of IFRS 9 resulted in a transition adjustment to the Group’s equity as at 1 January 2018 of SAR 1.63 billion. The impact of transition is explained in note 2(B)(iv) to the consolidated financial statements.</p> <p>We considered this as a key audit matter, as the determination of ECL involves significant management judgement, and this has a material impact on the consolidated financial statements of the Group. The key areas of judgement include:</p> <ol style="list-style-type: none"> 1. Categorisation of loans into Stages 1, 2 and 3 based on the identification of: <ol style="list-style-type: none"> (a) exposures with significant deterioration in credit quality since their origination; and (b) individually impaired / defaulted exposures. 2. Assumptions used in the ECL model such as financial condition of counterparty, expected future cash flows, forward looking macroeconomic factors, etc. 3. The need to apply additional overlays to reflect current or future external factors that might not be captured by the ECL model. <p><i>Refer to the summary of significant accounting policies notes 2(A) and 2(B) to the consolidated financial statements for the impact of adoption of IFRS 9 – Financial Instruments and impairment of financial assets; note 1.1(f)(i) which contains the disclosure of critical accounting judgements, estimates and assumptions relating to impairment losses on financial assets and the impairment assessment methodology used by the Group; note 6(b) which contains the disclosure of impairment against loans and advances; and note 31(ii) for details of credit quality analysis and key assumptions and factors considered in determination of ECL.</i></p>	<ul style="list-style-type: none"> ▪ We have obtained an understanding of management’s assessment of impairment of loans and advances including the IFRS 9 implementation process, the Group’s internal rating model, impairment allowance policy and ECL modelling methodology. ▪ We compared the Group’s impairment allowance policy and ECL methodology with the requirements of IFRS 9, and assessed the underlying assumptions and the data inputs used. ▪ We assessed the design and implementation, and tested the operating effectiveness of the key controls over: <ul style="list-style-type: none"> • the modelling process, including governance over the monitoring of the model and approval of key assumptions; • the classification of borrowers into various stages and timely identification of significant increase in credit risk (“SICR”); and • the integrity of data inputs into the ECL model. ▪ For a sample of customers, we assessed: <ul style="list-style-type: none"> • the internal ratings determined by management based on the Group’s internal rating model; • the staging as identified by management; and • management’s computations for ECL. ▪ We checked the Group’s criteria for the determination of SICR and identification of “default” or “individually impaired” exposures; and their classification into stages. Furthermore, for a sample of exposures, we assessed the Group’s staging categorisation. ▪ We assessed the forward looking assumptions used by the Group in the ECL calculations. ▪ Where management overlays were used, we assessed those overlays and the governance process around such overlays. ▪ We checked the completeness and accuracy of data underpinning the ECL calculations as at 31 December 2018. ▪ Where relevant, we involved specialists to assist us in reviewing model calculations and data integrity. ▪ As the Group has used the modified retrospective approach for adoption of IFRS 9, we performed all the above mentioned tasks to evaluate management’s computation of adjustments to the Group’s equity as at 1 January 2018 (as a result of adoption of IFRS 9). ▪ We assessed the disclosures in the consolidated financial statements.

**Independent Auditors' Report on the Audit of the Consolidated Financial Statements
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Report on the Audit of the Consolidated Financial Statements (Continued)

Key Audit Matters (continued)

Key audit matter	How our audit addressed the key audit matter
<p><i>Valuation of derivative financial instruments</i></p> <p>The Group has entered into various derivative transactions, including special commission rate and currency swaps (“swaps”); forward foreign exchange contracts (“forwards”); currency, special commission rate and equity options (“options”); and other derivative contracts. Swaps, forwards, options and other derivative contracts include over-the-counter (“OTC”) derivatives, and the valuation of these contracts is subjective as it takes into account a number of assumptions and model calibrations.</p> <p>The majority of these derivatives are held for trading. However, the Group utilises certain derivatives for hedge accounting purposes in the consolidated financial statements for hedging cash flow or fair value risks. An inappropriate valuation of derivatives could have a material impact on the consolidated financial statements and, in case of hedge ineffectiveness, impact the hedge accounting as well.</p> <p>We considered this as a key audit matter, as there is complexity and subjectivity involved in determining the valuation in general and, in certain cases, due to the use of complex modelling techniques and valuation inputs that are not market observable.</p> <p><i>Refer to the basis of preparation note 1.1(f)(ii) to the consolidated financial statements which sets out the critical accounting judgements, estimates and assumptions regarding fair value measurement; the summary of significant accounting policies note 2(G) for the accounting policy relating to derivative financial instruments and hedge accounting; and note 10 which discloses the derivative positions as at the reporting date.</i></p>	<ul style="list-style-type: none"> ▪ We assessed the design and implementation, and tested the operating effectiveness, of the key controls over management’s processes for valuation of derivatives and hedge accounting, including the testing of relevant automated controls covering the fair valuation process for derivatives. ▪ We selected a sample of derivatives and: <ul style="list-style-type: none"> • Tested the accuracy of the particulars of derivatives by comparing the terms and conditions with relevant agreements and deal confirmations; • Assessed the key inputs to the valuation models; • Performed independent valuations of the derivatives and compared the result with management’s valuation; • Checked the hedge effectiveness performed by the Group and the related hedge accounting; and • Assessed disclosures about the valuation basis and inputs used in the fair value measurement as detailed in the consolidated financial statements.

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Report on the Audit of the Consolidated Financial Statements (Continued)

Key Audit Matters (continued)

Key audit matter	How our audit addressed the key audit matter
<p><i>Fees from banking services</i></p> <p>The Group charges administrative fees up-front to borrowers in respect of certain loan financing transactions.</p> <p>All such fees are an integral part of generating an involvement with the resulting financial instrument, and therefore these fees should be considered as part of the effective yield on loans and advances and recognised within Special Commission Income.</p> <p>However, due to the large volume of transactions with mostly individually insignificant fee amounts, management uses certain assumptions and judgements in relation to the recognition of such fees which are recorded within "Fee and Commission Income, net".</p> <p>We considered this as a key audit matter since the use of management assumptions and judgements could result in material misstatement to the consolidated financial statements, as they affect the timing and recognition of fees.</p> <p><i>Refer to the summary of significant accounting policies note 2(J) to the consolidated financial statements.</i></p>	<ul style="list-style-type: none"> ▪ We performed the following audit procedures: <ul style="list-style-type: none"> • We assessed the design and implementation, and tested the operating effectiveness, of the controls over the consistent application of management's assumptions and judgements for recognition of fee income; and • We assessed the assumptions and judgements used by management for making adjustments to the effective yield of loans and advances and amortizing fee income accordingly. ▪ We obtained management's assessment of the impact of the use of assumptions and judgements and: <ul style="list-style-type: none"> • on a sample basis, traced the historical and current year data used by management to the underlying accounting records; • on a sample basis, checked the accuracy of the management's assessment, including calculations and related assumptions; and • assessed management's estimation of the impact on the recognition of fee and commission income and special commission income.

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Report on the Audit of the Consolidated Financial Statements (Continued)

Key Audit Matters (continued)

Key audit matter	How our audit addressed the key audit matter
<p>Valuation of investments at fair value through other comprehensive income ("FVOCI") and fair value through profit or loss ("FVTPL")</p> <p>Investments classified as FVOCI and FVTPL comprise both debt and equity instruments. These instruments are measured at fair value, with the corresponding unrealised fair value changes recognised in other comprehensive income or in the profit or loss. The fair value of these financial instruments is determined through the application of valuation techniques which often involve the exercise of judgement by management and the use of assumptions and estimates.</p> <p>Estimation uncertainty exists for those instruments not traded in an active market and where the internal modelling techniques use:</p> <ul style="list-style-type: none"> ○ significant observable valuation inputs (i.e. level 2 investments); and ○ significant unobservable valuation inputs (i.e. level 3 investments). <p>Estimation uncertainty is particularly high for level 2 and level 3 investments. The valuation of the Group's investments in the level 2 and level 3 categories was therefore considered a key audit matter, given the degree of complexity involved in valuing these investments and the significance of the judgements and estimates made by the management.</p> <p><i>Refer to the summary of significant accounting policies note 2(C)(i) to the consolidated financial statements; and notes 35 and 1.1(f)(ii) which explain the investment valuation methodology used by the Group and the related critical judgements and estimates.</i></p>	<ul style="list-style-type: none"> ▪ We assessed the design and implementation, and tested the operating effectiveness, of key controls over: <ul style="list-style-type: none"> • managements' processes for performing valuations of investments classified as FVOCI and FVTPL which are not traded in an active market; and • the integrity of data inputs used in the investment portfolio valuation process. ▪ We assessed the valuation techniques and inputs used by management to value the FVOCI and FVTPL investments. As part of these audit procedures, we considered the key inputs and assumptions used in the valuations, such as comparable entity data and liquidity discounts, by benchmarking them with external data. ▪ We re-performed the valuation of a sample of FVOCI and FVTPL investments not traded in an active market and compared the results with management's valuation. ▪ We assessed the disclosures in the consolidated financial statements.

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Other Information included in the Group's 2018 Annual Report

The Board of Directors ("the Directors") is responsible for the other information. Other information consists of the information included in the Group's 2018 annual report, other than the consolidated financial statements and our auditors' report thereon. The annual report is expected to be made available to us after the date of this auditors' report.

Our opinion on the consolidated financial statements does not cover the other information, and we do not and will not express any form of assurance conclusion thereon.

In connection with our audit of the consolidated financial statements, our responsibility is to read the other information identified above when it becomes available and, in doing so, consider whether the other information is materially inconsistent with the consolidated financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated.

When we read the other information, if we conclude that there is a material misstatement therein, we are required to communicate the matter to those charged with governance.

Responsibilities of the Directors and Those Charged with Governance for the Consolidated Financial Statements

The Directors are responsible for the preparation and fair presentation of the consolidated financial statements in accordance with IFRS as modified by SAMA for the accounting of zakat and income tax, applicable provisions of Companies' Law, the Banking Control Law in the Kingdom of Saudi Arabia and the Bank's By-Laws, and for such internal control as the Directors determine is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the consolidated financial statements, the Directors are responsible for assessing the Group's ability to continue as a going concern, disclosing, as applicable, matters related to going concern, and using the going concern basis of accounting unless the Directors either intend to liquidate the Group or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Group's financial reporting process.

Auditors' Responsibilities for the Audit of the Consolidated Financial Statements

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditors' report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with International Standards on Auditing that are endorsed in the Kingdom of Saudi Arabia will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these consolidated financial statements.

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Report on the Audit of the Consolidated Financial Statements (Continued)

Auditors' Responsibilities for the Audit of the Consolidated Financial Statements (continued)

As part of an audit in accordance with International Standards on Auditing that are endorsed in the Kingdom of Saudi Arabia, we exercise professional judgement and maintain professional skepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Group's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the Directors.
- Conclude on the appropriateness of the Directors' use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditors' report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditors' report. However, future events or conditions may cause the Group to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the Group audit. We remain solely responsible for our audit opinion.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide those charged with governance with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence and, where applicable, related safeguards.

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Report on the Audit of the Consolidated Financial Statements (Continued)

Auditors' Responsibilities for the Audit of the Consolidated Financial Statements (continued)

From the matters communicated with those charged with governance, we determine those matters that were of most significance in the audit of the consolidated financial statements for the year ended 31 December 2018 and are therefore the key audit matters. We describe these matters in our auditors' report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

Report on Other Legal and Regulatory Requirements

Based on the information that has been made available to us while performing our audit procedures, nothing has come to our attention that causes us to believe that the Bank is not in compliance with the requirements of Regulation for Companies, the Banking Control Law in the Kingdom of Saudi Arabia and the Bank's By-Laws in so far as they affect the preparation and presentation of the consolidated financial statements.

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