

Economic Developments

Second Quarter of 2006

First: Monetary Developments:

Broad money supply (M3) rose by 2.3 percent (Rls 13.2 billion) to Rls 599.1 billion during the second quarter of 2006, compared to an increase of 5.8 percent (Rls 32.2 billion) during the preceding quarter. It registered an annual growth rate of 12.8 percent (Rls 68.1 billion). An analysis of the components of money supply (M3) indicates that (M1) went up by 3.6 percent (Rls 10.5 billion) to Rls 300.8 billion, or 50.2 percent of total money supply (M3) during the second quarter of 2006 compared to an increase of 2.4 percent (Rls 6.8 billion) in the preceding quarter. Money supply (M1) registered an annual rise of 9.0 percent (Rls 24.7 billion) at the end of the second quarter of 2006. Money supply (M2) also went up by 2.3 percent (Rls 11.0 billion) to Rls 491.4 billion, or 82.0 percent of total money supply (M3) during the second quarter of 2006 compared to a rise of 7.1 percent (Rls 31.7 billion) in the preceding quarter. Money supply (M2) recorded an annual increase of 13.5 percent (Rls 58.4 billion) at the end of the second quarter of 2006.

Second: Monetary Policy

During the second quarter of 2006, SAMA continued to pursue an appropriate monetary policy to support domestic economic activity and cope with international economic developments aiming at maintaining price stability and making available adequate liquidity for the banking sector.

During the quarter, SAMA raised the official repurchase agreements (Repo) rate one time by 20 basis points, from 5.00 percent to 5.20 percent. SAMA also raised reverse repurchase agreements (Reverse Repo) rate one time by 20 basis points from 4.50 percent to 4.70 percent during the second quarter of 2006. The average value of Repo transactions per day stood at Rls 819 million during the second quarter while that of Reverse Repo was Rls 16,917 million.

Inter-bank interest rates recorded a slight decline during the second quarter of 2006, due to available sufficient liquidity. The three-month inter-bank interest rate (SIBOR) went down from 5.10 percent at the end of the first quarter of 2006 to 5.08 percent at the end of the second quarter. The differential between the Riyal and the Dollar interest rates for a three-month period increased to 43 basis points for the Dollar at the end of the second quarter of 2006 against 12 basis points for the Riyal at the end of the first quarter of 2006. Saudi Riyal maintained stability of its exchange rate in the spot market around the official parity rate of 3.75 Riyals per dollar.

Third: Banking Developments:

3-1 Bank Deposits

Total bank deposits registered an increase of 2.0 percent (Rls 10.8 billion) to Rls 535.6 billion during the second quarter of 2006, compared to a rise of 7.2 percent (Rls 35.5 billion) during the preceding quarter. At the end of the second quarter of 2006, it recorded an annual rise of 13.8 percent (Rls 64.8 billion). The ratio of total bank deposits to total broad money supply (M3) stood at 89.4 percent at the end of the second quarter of 2006,

compared with 88.7 percent at the end of the same period of the previous year.

A review of the developments of deposit components by type during the second quarter of 2006 indicates that demand deposits rose by 3.5 percent (Rls 8.0 billion) to Rls 237.3 billion, compared to an increase of 4.6 percent (Rls 10.0 billion) during the preceding quarter. Other quasi-monetary deposits rose by 2.1 percent (Rls 2.3 billion) to Rls 107.7 billion, compared to an increase of 0.5 percent (Rls 0.5 billion) during the preceding quarter. Time and savings deposits went up by 0.2 percent (Rls 0.5 billion) to Rls 190.6 billion, compared to an increase of 15.1 percent (Rls 24.9 billion) during the preceding quarter. Time and savings deposits, other quasi-monetary deposits, and demand deposits recorded annual rises of 21.5 percent (Rls 33.7 billion), 9.9 percent (Rls 9.7 billion), and 9.9 percent (Rls 21.4 billion) respectively.

3-2 Banks' Credit and Investment Activity

Total claims of commercial banks on the private and government sectors (bank credit and investments) decreased by 0.1 percent (Rls 0.5 billion) to Rls 609.5 billion during the second quarter of 2006, compared with a rise of 2.4 percent (Rls 14.0 billion) in the preceding quarter. At the end of the second quarter, it recorded an annual rise of 10.3 percent (Rls 57.1 billion) to constitute 113.8 percent of total bank deposits compared with 117.3 percent at the end of the same quarter of the preceding year.

Total claims of commercial banks on the government and quasi-government sector went down by 4.5 percent (Rls 7.3 billion) to Rls 154.6 billion during the second quarter of 2006 compared with a rise of 1.5 percent (Rls 2.4 billion) in the previous quarter. At the end of the second quarter of 2006, they registered an annual decline of 13.0 percent (Rls 23.1 billion). Their ratio to total bank deposits stood at 28.9 percent at the end of the second quarter of 2006, compared with 37.7 percent at the end of the same period of the preceding year.

Total claims of commercial banks on the private sector rose during the second quarter of 2006 by 1.5 percent (Rls 6.5 billion) to Rls 454.0 billion compared to a rise of 2.6 percent (Rls 11.5 billion) during the previous quarter. At the end of the second quarter of 2006, they registered an annual increase of 21.4 percent (Rls 80.0 billion). The ratio of commercial banks' claims on the private sector to total bank deposits was 84.8 percent at the end of the second quarter of 2006 compared to 79.4 percent at the end of the same period of the previous year.

An analysis of bank credit by maturity (private and public sectors) shows that medium-term bank credit rose by 6.1 percent (Rls 3.5 billion) to Rls 61.1 billion during the second quarter of 2006, compared to an increase of 7.6 percent (Rls 4.1 billion) in the preceding quarter. Long-term credit also went up by 3.5 percent (Rls 5.2 billion) to Rls 156.3 billion compared to a rise of 2.0 percent (Rls 2.9 billion) during the previous quarter. In addition, short-term bank credit increased by 0.2 percent (Rls 0.5 billion) to Rls 259.0

billion compared to an increase of 3.1 percent (Rls 7.7 billion) during the previous quarter.

Total bank credit by economic activity rose by 2.0 percent (Rls 9.2 billion) to Rls 476.4 billion during the second quarter of 2006 compared to an increase of 3.2 percent (Rls 14.6 billion) during the previous quarter, recording an annual rise of 21.1 percent (Rls 82.9 billion) at the end of the second quarter of 2006, compared to the end of the same period of the preceding year. A breakdown of bank credit by different economic activities during the second quarter of 2006 indicates that bank credit extended to the building and construction sector went up by 8.7 percent (Rls 3.0 billion), to “commerce” by 7.8 percent (Rls 6.9 billion), to “water, electricity and other services” by 6.5 percent (Rls 0.2 billion), to “finance” by 6.0 percent (Rls 3.6 billion), to “manufacturing and processing” by 2.2 percent (Rls 0.7 billion), to “government and quasi-government” by 2.2 percent (Rls 0.7 billion), and to “miscellaneous services” by 1.8 percent (Rls 3.0 billion). In contrast, bank credit extended to the transport and communications sector went down by 50.8 percent (Rls 7.3 billion), to “mining and quarrying” by 13.2 percent (Rls 0.3 billion), to “services” by 6.9 percent (Rls 1.3 billion), and to “agriculture and fishing” by 0.9 percent (Rls 0.07 billion).

3.3 Commercial Banks' Foreign Assets and Liabilities

Total foreign assets of commercial banks increased during the second quarter of 2006 by 26.1 percent (Rls 25.1 billion) to Rls 121.2 billion compared to an increase of 5.1 percent (Rls 4.7 billion) in the previous quarter. They recorded an annual growth rate of 46.2 percent (Rls 38.3 billion), constituting 14.9 percent of total commercial banks' assets

compared with a rise of 11.7 percent at the end of the same period of the preceding year.

Commercial banks' total foreign liabilities declined by 6.1 percent (Rls 3.8 billion) to Rls 58.3 billion during the second quarter of 2006 compared to a decrease of 4.6 percent (Rls 3.0 billion) in the preceding quarter. They recorded an annual growth rate of 24.3 percent (Rls 11.4 billion), constituting 7.2 percent of total liabilities compared to an increase of 6.6 percent at the end of the same period of the preceding year. Net foreign assets amounted to Rls 62.9 billion, rising by 84.7 percent (Rls 28.9 billion) at the end of the second quarter of 2006 compared with an increase of 29.1 percent (Rls 7.7 billion) during the previous quarter. Net foreign asset's annual growth rate registered a rise of 74.8 percent (Rls 26.9 billion).

3.4 Commercial Banks' Capital, Reserves, Profits and Branches

The capital and reserves of commercial banks went down by 1.5 percent (Rls 1.2 billion) during the second quarter of 2006. The ratio of commercial banks' capital and reserves to total bank deposits at the end of the second quarter of 2006 stood at 15.3 percent compared to 13.8 percent in the preceding year. Their annual growth rate rose by 25.3 percent (Rls 16.5 billion).

Commercial banks' profits decreased to Rls 9.3 billion during the second quarter of 2006 compared to Rls 9.9 billion in the preceding quarter, recording a decline of 6.2 percent (Rls 0.6 billion) and an annual growth rate of 57.8 percent (Rls 11.9 billion). The number of branches of commercial

banks operating in the Kingdom went up to 1,282 at the end of second quarter of 2006, increasing by 2.5 percent over the previous quarter.

Fourth: Banking Technology:

Saudi Arabian Riyal Interbank Express (SARIE) has made a revolution in the field of electronic banking business and commercial operations in the Kingdom, as it constitutes the infrastructure of a number of sophisticated financial payments and settlement systems. Since its launch on 18/1/1418 H (14/5/1997 G), SARIE has witnessed continued development both in fields of technical technology of the system and banking business.

Technically, the first stage of the development project of SARIE systems was completed as they were developed and upgraded in all banks' sites. Work is in progress on the execution of the second stage of the project, including developing and upgrading SARIE systems in SAMA's sites (Central System). It is expected to be completed in the middle of August 2006 G.

As for the accession of new banks to SARIE, a well-designed plan was completed successfully on 13 May 2006 for linking of Deutsche Bank to SARIE's Live System. Work is still in progress on holding special meetings and explaining requirements and initial work plans as a preliminary step for linking Muscat Bank to SARIE.

As for development of SARIE's security system, required adjustments have completely been defined and development process has already started. This plan is expected to be completed at the end of 2006. As for SARIE's statistics for the second quarter of 2006, the value of transactions carried out

through SARIE totaled Rls 4,245 billion through 493,526 transactions. The value of single payments transactions totaled Rls 4,120 billion, whereas the value of gross payments stood at Rls 125 billion. Customers' payments amounted to Rls 397 billion. Inter-bank total value of payments totaled Rls 3,848 billion. It is expected that transactions via SARIE will continue to increase in upcoming years, especially in commercial transactions and those carried out by individuals, due to increased payment of salaries of employees in the government and private sectors via SARIE.

As for Saudi Payments Network (SPAN) achievements, it is still recording good growth in terms of transactions made through it. Total operations executed in the second quarter of 2006 amounted to 149 million, including banks and SPAN's operations with a value totaling Rls 68 billion. Total transactions of POS terminals executed through SPAN stood at about 20.5 million with a total value of Rls 8 billion. The number of ATMs amounted to 5,377, and the number of cards issued by domestic banks exceeded 9 million at the end of the second quarter of 2006. POS terminals continued their growth, increasing to a total of 49 thousand at the end of the same quarter.

The number of clearing houses in the Kingdom amounted to 10 in all branches of SAMA, 3 of which are automated clearing houses in Riyadh, Jeddah and Dammam. In 2001, they were provided with state-of-the-art machines that archive checks copies using scanning technique in lieu of previously used microfilm.

The number of bank checks (outgoing and incoming) cleared at clearing houses during the quarter totaled 1,932,536 million with a total value of Rls 135.2 billion . The number of household and business checks totaled 1,653,939 million and their total value amounted to Rls 97.8 billion during the period. The number of banks' checks (certified) totaled 278,597 thousand with a total value of Rls 37.3 billion.

Fifth: Domestic Share Market Developments:

The general share price index declined during the second quarter of 2006 by 22.9 percent to 13,145.26 compared to an increase of 2.1 percent in the preceding quarter, recording an annual decrease of 2.3 percent. Due to splitting a share to five, the number of shares traded in the second quarter of 2006 rose by 480.5 percent to 18.8 billion compared to a decrease of 11.6 percent in the preceding quarter. Its annual growth rate increased by 189.9 percent. Total value of shares traded went down by 26.2 percent to Rls 1,332.8 billion compared to a rise of 21.7 percent in the preceding quarter, with its annual growth rate rising by 118.9 percent.

At the end of the second quarter of 2006, the market capitalization of issued shares went down by 22.3 percent to around Rls 1,969 billion compared to a rise of 4 percent at the end of the preceding quarter. The total number of executed transactions during the quarter registered a rise of 37.8 percent to 28,356.3 thousand compared to a rise of 19.9 percent during the preceding quarter, with its annual growth rate increasing by 233.7 percent.

Sixth: Investment Funds:

Total assets of investment funds managed by commercial banks recorded a decline of 20.9 percent (Rls 28.8 billion) to Rls 109.2 billion in the second quarter of 2006 compared to a rise of 0.7 percent (Rls 1.0 billion) in the preceding quarter, registering an annual growth rate of 11.5 percent (Rls 11.3 billion).

A breakdown of the funds' total assets indicates a decline in domestic assets by 23.5 percent (Rls 27.5 billion) to Rls 89.4 billion in the second quarter of 2006 compared to an increase of 1.0 percent (Rls 1.2 billion) in the preceding quarter. Domestic assets recorded an annual growth rate of 9.4 percent (Rls 7.7 billion). Foreign assets registered a decline of 6.2 percent (Rls 1.3 billion) to Rls 19.8 billion during the second quarter of 2006 against a drop of 1.0 percent (Rls 0.2 billion) in the preceding quarter. They recorded an annual growth rate of 22.2 percent (Rls 3.6 billion).

The number of subscribers to investment funds dropped by 15.1 percent (80,662) to 582,578 in the second quarter of 2006 compared to a rise of 16.7 percent (94,956) in the preceding quarter, recording an annual growth rate of 43.3 percent (176,338).

The number of operating funds rose from 204 in the first quarter of 2006 to 209 in the second quarter of 2006, increasing by 2.5 percent, i.e the

same growth rate as in the preceding quarter. The number of operating funds registered an annual growth rate of 6.6 percent.

Seventh: Cost of Living:

During the first quarter of 2006, the average cost of living index went up by 0.6 percent. It registered an annual rise of 0.9 percent compared to the end of the same quarter of the previous year. The cost of living index for "goods and other services" rose by 1.5 percent, "foods and beverages" by 1.3 percent, "fabrics, apparel and shoes" by 0.4 percent, "renovation, rent, fuel and water" by 0.3 percent and "medical care" by 0.2 percent. In contrast, it declined by 0.7 percent for "transport and telecommunications" and by 0.1 percent for "entertainment and education". The index for "house furnishing" remained unchanged.

Eighth: Supervisory and Legislative Developments during the second Quarter of 2006:

- Circular No.13227/B.C.S.197 dated 9/4/1427H (7/5/2006G) was issued to banks concerning Basel Committee's Core Principles for Effective Banking Supervision and the Methodology of the Core Principles for Enhancing Banking Supervision.
- Circular No.18498 B.C.S 290 dated 16/5/1427H (12/6/2006G) on the second guiding draft of instructions on Basel II Capital Adequacy Standard was issued to banks to obtain their comments about it.
- Legal and administrative arrangements for Inma' Bank have recently been initiated. Its Memorandum of Association was documented as a prelude to be floated for public subscription during the last quarter of the current year as expected. The founders (the Public Investment

- Fund and the Pension Organization and General Organization for Social Insurance) have participated in the bank's capital with their full share, which represents 30% of the paid-up capital, while the remaining 70% will be floated for public subscription. Managing director of the bank has been appointed.
- Deutsch Bank has started its activity in Riyadh, and it was inaugurated on 30/4/2006G.
 - National Bank of Kuwait has started its activity in Jeddah city, and it was inaugurated on 5/6 /2006G.

Ninth: Salient Regulatory Developments in the Saudi Economy during the Second Quarter of 2006:

- A Royal Directive was issued on 26/3/1427H (24/4/2006G) to the concerned authorities to take all necessary steps and actions for maintaining discipline and good performance of the share market and dealing with all factors affecting it.
- A Royal Order was issued on 2/4/1427H (30/4/2006 G) on reducing the prices of gasoline and diesel.
- The Council of Ministers' Resolution was issued on 3/4/1427H (1/5/2006 G) approving amending the Charter of Saudi Arabian Mining Company (Ma'aden), increasing its capital, and privatizing it by the end of 2006 through offering 50 percent of its shares for public subscription.
- The Council of Ministers' Resolution was issued on 3/4/1427H (1/5/2006 G) approving the GCC Unified Industrial Regulatory Law.

- A Royal Directive was issued on 11/4/1427H (9/5/2006G) approving the establishment of an advanced financial center in Riyadh that incorporates all financial institutions working in the financial sector.
- The Council of Ministers' Resolution was issued on 24/4/1427H (22/5/2006G) approving the establishment of a Saudi joint-stock company under the name "Saudi Arabian Railways Co." with a capital of one billion Riyals, divided into 100 million shares with a nominal value of Rls 10 each, in addition to approving the establishment of "Saudi Arabian Railways Co." (SAR).
- Establishment of Prince Abdulaziz bin Musa'd bin Jilowy's Economic City in Ha'il region on 17/5/1427 H (13/6/2006G).
- The Council of Ministers' Resolution was issued on 30/5/1427H (26/6/2006G) approving the Charter of the Saudi Bank for Lending and Saving.