

Directors' Report

For the Year Ended 31 December 2020

The Board of Directors of YANAL Finance Company (“the Company” or “YANAL”) is pleased to present its nineteenth annual report with audited financial statements of the Company for the year ended December 31, 2020.

Introduction

The name of the Company was changed from Saudi ORIX Leasing Company to YANAL Finance Company, effective January 1, 2021. YANAL is a closed joint stock company established under the regulations for companies in the Kingdom of Saudi Arabia. The Company operates under commercial registration number 1010163957, issued in Riyadh on 21 Shawal 1421H (corresponding to 16 January 2001), non-industrial license number 99 dated 27 Safar 1421H (corresponding to 31 May 2000), issued by the Ministry of Commerce and Industry, and Finance company license number 7/A Sh/201403 dated 27 /04/ 1435H (corresponding to 27 February 2014), issued by Saudi Central Bank. The Company operates through its head office and five branches (2019: five branches) across the Kingdom.

The objective of the Company is to provide medium term financing to all productive sectors of the economy with particular emphasis on small and medium size enterprises thereby assisting in providing, extending and expanding the credit delivery mechanism in the Kingdom.

1. Business Segments

YANAL offers Finance lease and Commodity Murabaha Financing facilities to its customers, operating in construction & contracting, manufacturing, trading, food and allied industries, health care, education and transportation sectors. Assets leased by the Company mainly include vehicles, plant and machinery, equipment and commercial real estate.

2. Strategy

For the year 2020, and given the economic and business conditions, YANAL business strategy remained to focus on recoveries and execute business with low to moderate risk with an effort to maintain book size. Further, the strategy focused on diversification towards sectors targeted by National Transformation Plan (NTP) 2020 such as Healthcare, Educational and transportation service, Energy and Tourism.

As for 2021, the business strategy will focus the measures and efforts to increase the volume of small ticket transactions that will help to enhance the customer base and overall financing rate, hence the profitability. The Company is looking to continue utilizing the security benefit of Kafalah program as well as the flexibility offered by Murabaha financing to expand the customer base. Further, sector diversification will remain in focus with target on Healthcare, Educational and Transportation service, Energy, tourism.

3. Risk Management

Risk management is a vital part of YANAL's activities. The Company manages a process of ongoing risk identification and measurement using risk limits and other controls and a number of committees and departments are established to coordinate day-to-day risk management. Following is the summary of main risks:

Credit Risk:

Credit risk is the risk that the counter party to a financial transaction will fail to discharge its obligation, resulting in financial loss of the principal amount as well as interest income. Since financing is the main line of business of the Company, credit risk can be considered as the biggest contributor to overall risk profile. In order to minimize credit risk, YANAL follows standard forms and checklists to obtain operational and financial information about the customer and follows cascaded structure for credit review and approval. Moreover, YANAL diversifies its risk and has set prudent exposure limits for individual clients, groups and asset classes.

Impact of COVID-19

During March 2020, the World Health Organisation (“WHO”) declared the Coronavirus (“COVID-19”) outbreak as a pandemic in recognition of its rapid spread across the globe. This outbreak has also affected the GCC region including the Kingdom of Saudi Arabia. Governments all over the world took steps to contain the spread of the virus. Saudi Arabia has managed to control the outbreak by closure of borders, enforced countrywide lockdowns and curfews, released social distancing guidelines, and has taken phased measures towards normalization. However, The COVID-19 pandemic continues to disrupt global markets as many geographies are experiencing a “second wave” of infections.

The Company has evaluated the current situation through conducting stress testing scenarios on expected movements of oil prices and its impact on key credit, liquidity, operational, solvency and performance indicators in addition to other risk management practices to manage the potential business disruption due to COVID-19 outbreak that may have on its operations and financial performance. The steps taken by management also include review of credit exposure concentrations at a more granular level such as the economic sectors, regions, counterparty etc., collateral protection, timely review and customer credit rating actions. Management has appropriately restructured (deferment of rental dues) its portfolio where required and in consideration of government and SAMA support relief programs.

The Company received three tranches of interest free deposits from SAMA in order to compensate the related cost for the deferment, which are repayable by October 2023. Further, rentals of SME portfolio financed under Monsha’at program were deferred from March 2020 to 2021, against moratorium of loan repayment by Social Development Bank for the same period.

Liquidity Risk:

Liquidity risk is the risk that YANAL will be unable to meet its payment obligations when they fall due under normal and stress circumstances. To address its liquidity risk, YANAL uses contractual maturity analysis and cash flow forecasts and aims to create a diversified investment portfolio with manageable correlation risk between its assets and liabilities, with an average financing terms of around three years and a half.

Market Risk:

Market risk refers to the risk resulting from changes in commission rates and foreign exchange rates. YANAL’s exposure to the risk of changes in interest rates is primarily against its financing obligations with floating rate, which is mitigated through interest rate swaps i.e. hedging. With respect to exchange risk, YANAL does not hold any investment in foreign currency and on the other hand, all the foreign currency borrowings are in US Dollars and due to official pegging of Saudi Riyal with US Dollar, YANAL is not exposed to foreign exchange risk, unless Saudi Riyal depreciates against US Dollar.

Operational Risk:

Operational risk is the risk of losses arising from inadequate internal operating procedures, including failures, defects or errors of information, resulting from either human error or technological failings. YANAL manages the operational risk through a control framework and by monitoring and responding to potential risks. Other measures to mitigate operational risk include segregation of duties, access authorization and reconciliation procedures, process automation, staff training and education and assessment procedures.

4. Geographical Concentration

The Company only operates in the Kingdom of Saudi Arabia with its head office in Riyadh and other marketing offices in Dammam, Jubail, Jeddah, Makkah and Khamis Mushait.

5. Financial Highlights

The Company's total revenues for the year ended December 31, 2020 were SR 110.6 million as compared to SR 108.2 million in 2019. Operating expenses increased significantly to SR 97.6 million as against SR 54.6 million in 2019 mainly due to increase in provision for impairment on financial assets and recognition of modification loss arising on deferment of lease rentals in line with SAMA Deferral Program. Net investment in finance leases/Murabaha [before provision] was SR 1,242.82 million as compared to SR 1,239.41 million in the previous year. The Company wrote off doubtful receivables amounting to SR 85.9 million (2019: SR 27.7 million) during the year.

SR' millions	2020	2019	2018	2017	2016
Net investment in finance leases/Murabaha	1,116	1,043	1,051	1,220	1,497
Total assets	1,411	1,141	1,210	1,328	1,593
Total debt and SAMA profit free deposit	463	115	264	392	672
Shareholders' Equity	852	875	855	856	838
Total revenues	110.6	108.2	111.3	131.2	162.4
Special commission expense	13.4	4.6	9.3	14.6	26.1
Other operating expenses	84.1	50.1	44.6	66.5	83.0
Net income before Zakat & Tax	13.1	53.5	57.4	50.1	53.3
Zakat & Tax (refund) / expenses	(1.0)	46.1	-	-	-
Net income after Zakat & Tax	14.1	7.4	57.4	50.1	53.3

6. Key Income Statement Items as a Percentage of Total Income

The table below shows the variation in the key income statement lines for the year 2020 and 2019:

SR millions	2020	2019	% Change
Total income	110.6	108.2	2.22%
Special commission	13.4	4.6	191.30%
Other Operating expenses ¹	84.1	50.1	67.86%
Net Income before Zakat & Tax	13.1	53.5	-75.51%

¹ Other operating expenses include provisions for lease losses amounting to SR 17.2 million (2019: SR 2.5 million) and modification loss (net of Grant) on rentals deferred amounting to SR 15.8 million (2019: Nil).

7. Financial Reporting Standards & Audit

YANAL maintains proper books of accounts and, in compliance with the Implementing Regulations of the Law on Supervision of Finance Companies, the annual audited financial statements for the year ended 31 December 2020 of YANAL have been prepared in accordance with International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board (IASB).

The Company has an Internal Audit department that performs audits as per approved annual plan and reports to Audit committee, established by the Board of Directors. The Audit Committee is entrusted with the responsibilities of assisting the Board of Directors in fulfilling its responsibilities for developing and maintaining system of internal control, and the company's process for monitoring compliance with laws and regulations and the code of conduct. The Committee is also responsible for recommendation of external auditors and rotation thereof, review of financial statements prior to their approval by the Board of Directors, and discussion with external auditors over audited financial statements, management letter and conduct of audit.

8. Compliance, Anti-Money Laundering & Counter Terrorism Financing

The Board and Management believe that the existence of Compliance and Anti-Money Laundering & Counter Terrorism Financing functions are an integral part of sound management framework, therefore, has established a separate department that identifies and assesses the compliance risk, monitors and reports non-compliance issues. It mainly focuses on prevention of risks, consolidating relations with regulatory entities, establishing mechanisms and frameworks to ensure prevention of crimes and safeguard professional values and practices.

9. Effectiveness of Internal Control System

Management is responsible for the appropriate design and implementation of the system, and the Risk Management, Internal Audit and Compliance Departments for the continuous monitoring and evaluation of the system. All employees are ultimately responsible for operating and maintaining an efficient internal control system at their respective levels. The external auditors are responsible to assess the adequacy of the system of internal controls to decide the level of reliance they can place on the Company's internal controls, to design their audit procedures accordingly.

The Company's Internal Control System is subject to ongoing evaluations and improvement to allow for the identification of any gaps and meet the desired level of effectiveness, key controls include:

- Existence of a series of policies and procedures, which are subject to regular updates and reviews to verify their sufficiency and adequacy.
- Most of the Company's operations are automated using sophisticated systems, which minimizes errors and fraud opportunities.
- All work related and major important decisions are supervised through committees created for this purpose and to safeguard the Company's assets.
- Existence of departments specialized in fields of audit, compliance control and risk management.

The Board is of the opinion that the functioning of the internal control system is appropriate and nothing has been reported by Audit Committee, causing it to believe that the system of internal control is not designed properly or implemented effectively.

10. Ethical Standards and Code of Conduct

YANAL is committed to instill and maintain a culture of professionalism through its Code of Conduct which is based on fundamental principles of integrity, confidentiality and professionalism. It applies to the management, employees and any other person that may represent the Company. YANAL operates under the governing authority of its Board of Directors, who respectively, oversees the implementation and effectiveness of its ethical standards and Code of Conduct.

11. Loans

Borrowing details are provided in the Note 11 to the audited Financial Statements. The following is the summary of borrowing activities:

SR millions	Dec 31, 2020	Dec 31, 2019
Opening balance of loans	114.2	263.8
Proceeds from loans	365.6	205.0
Repayments of loans	(18.2)	(354.6)
Closing balance of loans	461.6	114.2

12. Dividend Policy

A. Objective:

The main objective of the dividend policy is to provide a return to shareholders to meet their investment expectations with due consideration to capital management and growth requirements of the Company. The dividend may be paid in cash to shareholders or distributed via issuance of bonus shares or a combination of cash and bonus shares.

B. Guiding Principles:

Following are the guiding principles for reviewing and setting the annual dividend policy by the Board and senior management:

I. Dividend sustainability

To build long term shareholder value and market confidence in the Company's future, the amount and frequency of dividends to be paid, should be evaluated based on the Company's ability to continue paying at an equal or increased level in the foreseeable future.

II. Growth of the Company:

The amount, frequency and type of dividends paid should not impede the ability of the Company to meet its strategic growth plans.

13. Significant Shareholding

Below is shareholding pattern as at December 31, 2020 and there has been no change during the year

Shareholders	Number of Shares	%
The Saudi Investment Bank	20,900,000	38.00
Trade Development & Investment Group Limited	17,600,000	32.00
ORIX Corporation – Japan	15,125,000	27.50
ORIX Leasing Pakistan Limited – Pakistan	1,375,000	2.50
	55,000,000	100

14. Related Party Transactions

In the ordinary course of its activities, the Company transacts business with related parties which are summarized in Note 26 of the audited Financial Statements for the year ended 2020.

15. Board of Directors

All members of Board are non-executive director, except the Managing Director (MD)

Name	Feb 2020	April 2020	July 2020	Oct 2020	Dec 2020
Mohammed Omran Al Omran	Proxy	Proxy	√	√	√
Salman Bader Al Fughom	√	√	√	√	√
Shaheen Amin (MD)	√	√	√	√	√
Sahil Al Omair	√	√	√	√	√
Khalid Abalkhail	√	√	√	√	√
Bader AlSalloom ¹		√	√	√	√
Alaa Rasheed Abukhadra	√	√	√	√	√
Yoshiaki Matsuoka				√	√
Yohie Honda				√	√
Harukazu Yamaguchi ²	Proxy	Proxy			
Kiyokazu Ishinabe ²	Proxy	Proxy			

¹ The Board confirmed SAIB's request to replace Mr. Abdulelah AlAhmed with Mr. Bader AlSalloom through resolution of the Board of Directors passed by Circulation on March 12, 2020 subject to SAMA's approval, which was obtained on April 2, 2020.

² The Board confirmed ORIX Corporation's request to replace Mr. Harukazu Yamaguchi and Mr. Kiyokazu Ishinabe with Mr. Yoshiaki Matsuoka and Mr. Yohie Honda through resolution of the Board of Directors passed by Circulation on June 22, 2020 subject to SAMA's approval, which was obtained on August 30, 2020.

Board Committees

The Board of Directors has established Credit and Risk Management Committee (CRM), Audit Committee (AC) and Nomination and Remuneration Committee (NRM) as follows:

Committee Chairman/ Members	CRM Committee	Audit Committee	NRM Committee
Mr. Mohammed Omran Al Omran	Chairman		Chairman
Mr. Salman Alfughom	Member		member
Mr. Alaa Abukhadra	Member		
Mr. Khalid Mohammad Abalkhail	Member		
Mr. Bader Salloom	Member		
Mr. Yohei Honda			Member
Ms. Khlood Aldukhail		Chairperson	
Mr. Salman Ahmed		Member	
Mr. Mohammed Alsuhaime*		Member	
Mr. Abdulrahman Alzuwaidi*		Member	

* The Board accepted the resignation of Mr. Abdulrahman Alzuwaidi and confirmed SAIB's nomination for audit committee membership through a resolution passed by Circulation on June 22, 2020 subject to SAMA's approval, which was obtained on July 16, 2020.

- A. Credit and Risk Management Committee (“CRM Committee”): The Committee carries out following responsibilities by evaluating the reports or credit proposals submitted to the Committee electronically;
- To assist the Board in reviewing overall risks which the Company might face and to decide on mitigating factors related therewith.
 - To evaluate and review operational and non-operational risks and related mitigating factors.
 - To review and approve credit exposures for lessees.
- B. Audit Committee: The Committee is established with majority of participants being independent (including the Chairperson), to institutionalize and improve the audit process and control environment. The Committee had conducted 6 meetings during the year 2020 all of which were attended by Ms. Khlood and Mr. Salman, while Mr. Abdulrahman attended only one meeting and newly appointed member, Mr. Mohammed Alsuhaimee attended 4 meetings. The Committee assists the Board to ensure integrity of periodic financial statements and effectiveness of:
- external audit, with respect to the appointment, rotation, qualifications and independence and the conduct of audit,
 - the system of internal controls,
 - Internal Audit function and Compliance function.
- C. Nomination and Remuneration Committee: The Board has established Nomination and Remuneration Committee (“NRM Committee”) to set policies and standards for the remunerations of Board members and Company’s senior executives. The Committee meetings are held as and when required to fulfil the stipulated responsibilities.

16. Directors and Senior Executive Interest *(including their spouse and minor children)*

Board Members:

All Board members of the Company are directors nominated by shareholders. Neither any of directors, including any person related to them, hold any share nor have any other interest in the Company.

Senior Management:

None of senior management holds any share in the Company. Further, the CEO and the CFO, including any person related to them, apart from the remuneration, do not have any other interest in the Company.

Compensation

Board and other Key management personnel’s total compensation for the year 2020 was as follows:

Salaries & Other benefits	8,876,852
End of Service Benefits	620,284
Directors’ meeting fee	900,000
Total (SR)	10,397,136

17. External Auditors

Messrs. PricewaterhouseCoopers were reappointed as external auditors for the year ended 31 December 2020 by shareholders in AGM held on April 28, 2020, upon recommendation of Audit Committee and Board of Directors.

18. Payment of Zakat and Income Tax

a) Saudi Shareholders

Zakat payable on the current year's share of income of Saudi Shareholders is estimated at SR 1.89 million.

Zakat liability for prior years have been agreed with General Authority of Zakat & Tax at SR 36.82 million, which have been charged to Profit & Loss account for the year as per guidelines issued by SAMA. Prior years' zakat liability has been partially recovered from shareholders while remaining amount, booked as receivable from shareholders, will be recovered from future dividends.

b) Non-Saudi Shareholders

A refund of SR 3.11 million is expected for Income tax on current year's share of income of foreign shareholders. Refund is primarily due to the impact of write-off of lease receivables.

19. Social Responsibility

The company derives its activities related to its social responsibility from its commitment to contributing towards a better future by caring for the local communities.

20. Applicable Laws and Regulations

YANAL adheres to the provisions of the Saudi Companies' Law, Finance Lease Laws, Finance Companies Control Laws and Implementing Regulations, SAMA guidelines, and other applicable laws, rules and regulations. However during 2020 regulatory fines were imposed as follows:

Type of violation	Number of instances		Amount of Fines (SR)	
	2020	2019	2020	2019
SAMA supervisory and control instructions	1	-	150,000	-
SAMA Customer Protection Instructions	-	-	-	-
Violating SAMA instructions AML and CTF	-	-	-	-

21. Declaration

The Board of Directors hereby confirms that;

- Proper books of accounts have been maintained;
- The Company prepares its financial statements in accordance with International Financial Reporting Standard ["IFRS"] as required by the finance lease laws and regulations;
- The Company has no existing contracts in which a Director, CEO, CFO or any of their associate has a material interest; and
- There is no doubt over the Company's ability to continue as a going concern.

22. Future Prospects

The Company has achieved a strong position in the market in the last nineteen years, and is keen on continuing its successful journey and gradually increase its profitability in line with the expected improvement in the economy of Saudi Arabia over the coming years.

The Board takes this opportunity to express gratitude to the government of the Kingdom of Saudi Arabia, and in particular the Saudi Central Bank, Ministry of Investment and the Ministry of Commerce for their continuing proactive support. The Board also places on record appreciation for Saudi and international shareholders for their confidence and support and to the YANAL team for their tireless effort and professionalism.

May Allah lead us to success

For and on behalf of the Board of Directors

Chairman