# ALISTITHMAR FOR FINANCIAL SECURITIES AND BROKERAGE BUSINESS

# (ALISTITHMAR CAPITAL)

# PILLAR III – DISCLOSURE REPORT

# FOR THE YEAR ENDED 31 DECEMBER 2014

FEBRUARY 2015

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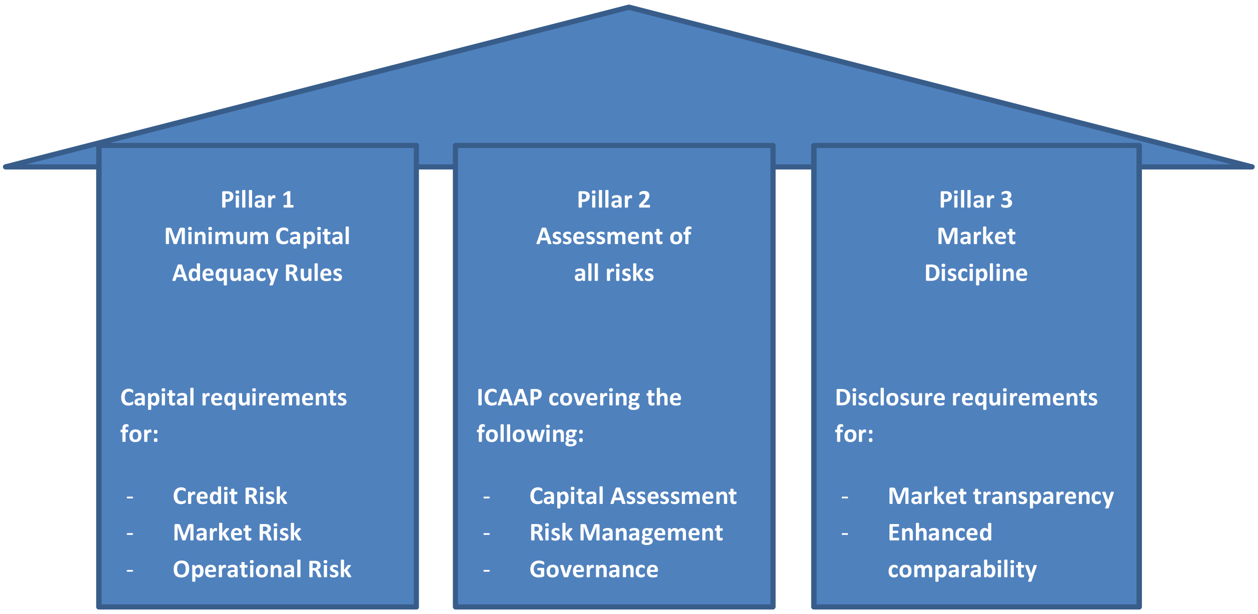
## 1. OVERVIEW

The Prudential Rules issued by the Capital Market Authority (CMA) of Saudi Arabia covers and consists of three main pillars of Capital Adequacy as illustrated below:




This disclosure requirement meets the minimum requirements for the annual market disclosure of information as referred to by the Article 68 of the Prudential Rules (PRs) (the market disclosure is hereinafter referred to as the "Pillar III Disclosure") to be published by all the Authorized persons (APs) licensed for the Dealing, Managing and/or Custody activities.

The purpose of Pillar III Disclosure is for the market participants to assess the key pieces of information on the scope of application, capital, risk exposures, risk assessment processes, and hence the capital adequacy of the APs.

This document has been prepared in accordance with the guidelines issued by the Capital Market Authority (CMA) of Saudi Arabia which supplements the disclosure requirements for the Pillar III Disclosure in the PRs.

This Pillar III Disclosure comprises both the qualitative and quantitative disclosures.

This Pillar III Disclosure has been approved by the Board of Directors of Alistithmar Capital before its publication. The information presented in this Pillar 3 Report is not required to be, and has not been, subject to external audit.

## 2. SCOPE OF APPLICATION

### 2.1 SCOPE OF THE COMPANY

Alistithmar for Financial Securities and Brokerage Company - Alistithmar Capital (the "Company") is a Saudi limited liability company established under the Regulations for Companies in the Kingdom of Saudi Arabia. The Company operates under Commercial Registration No. 1010235995 issued in Riyadh on Rajab 8, 1428 H (corresponding to July 22, 2007). The Company also operates its activities under Authorization License number 11156-37 dated September 25, 2011 (corresponding to 27/10/1432H) issued by the Capital Market Authority (CMA).

The principal activities of the Company are dealing in securities as principal and agent, underwriting, management of investment funds and private investment portfolios on behalf of customers, arrangement, margin loans, murabaha financing, advisory and custody services relating to financial securities.

### 2.2 HOLDING STRUCTURE OF THE COMPANY

The Company's share capital of SR 250 million as at December 31, 2014 consists of 25,000,000 fully paid shares of SR 10 each, and is wholly-owned by The Saudi Investment Bank.

### 2.3 CAPITAL TRANSFERABILITY BETWEEN LEGAL ENTITIES

There are no current or foreseen material or legal impediment to the prompt transfer of capital or repayment of liabilities between the Company and its subsidiaries, as Alistithmar Capital does not have any subsidiaries with a business ownership unless in the case of fund structures in the capacity of the designated fund manager.

**Restrictions by Memorandum and Articles of Association:**

As per Article 10-1(i) of Articles of Association, the Board of Directors of the Company can recommend any sale or transfer of shares of the Company, however the ownership of the company shall not change prior to approval by the Capital Market Authority of Saudi Arabia. Apart from the above, no other restrictions have been imposed by the management on transfer of shares.

**Statutory restriction:**

As per Article 15-1 of the Articles of Association and Article 176 of the Saudi Companies Law, the Company is required to transfer 10% of its net profit to establish and fund the statutory reserves before declaration of dividend until the amount of statutory reserves is equal to the half of the paid up capital of the Company.

**Regulatory restriction:**

The CMA has imposed a restriction that the Company shall continuously possess a capital base which corresponds to not less than the total of the minimum capital requirements in accordance with Chapter 4 to Chapter 16 of Part 3 of the Prudential Rules at any point in time.

## 3. CAPITAL STRUCTURE

### 3.1 GENERAL PRINCIPLE OF CAPITAL ADEQUACY

It is the company's policy to maintain a strong capital base and to utilize it efficiently throughout its activities to optimize the return to shareholders, while maintaining a prudent relationship between the capital base and the underlying risks of the business. In carrying out this policy, the Company has taken into account the supervisory requirements of the Prudential Rules.

The calculation of the Capital Base complies with all the respective chapters under the requirements of Part 2 – Capital Base of the Prudential Rules.

### 3.2 CAPITAL BASE

The capital base of Alistithmar Capital as of end of December 31, 2014, as per the audited financial statements is as follows:

| Capital Base | SAR '000 |
|---|---:|
| **Tier-1 capital** | |
| Paid-up capital | 250,000 |
| Audited retained earnings | 61,695 |
| Share premium | - |
| Reserves (other than revaluation reserves) | 20,951 |
| Tier-1 capital contribution | - |
| Deductions from Tier-1 capital | (11,880) |
| **Total Tier-1 capital** | **320,766** |
| | |
| **Tier-2 capital** | |
| Subordinated loans | - |
| Cumulative preference shares | - |
| Revaluation reserves | 3,160 |
| Other deductions from Tier-2 (-) | - |
| Deduction to meet Tier-2 capital limit (-) | - |
| **Total Tier-2 capital** | **3,160** |
| | |
| **TOTAL CAPITAL BASE** | **323,926** |

## 4. CAPITAL ADEQUACY

### 4.1 PRINCIPLES OF CAPITAL ADEQUACY

The Company's approach in assessing adequacy of its capital to support current and future activities is envisaged around the following principles:

- It has a process for assessing its overall capital adequacy in relation to its risk profile and a strategy for maintaining capital levels
- A review of company's Internal Capital Adequacy Assessment Process (ICAAP) and capital strategies are undertaken by its management at-least annually, as well as monitoring and ensuring compliance to CMA regulations, with appropriate actions being taken when required
- It is possessing a capital base which corresponds to at-least the minimum capital requirements as per the Prudential Rules

As of December 31, 2014, the Company's total capital ratio was 1.69x which corresponds to an excess capital of SAR 132.65 Mn compared to the total minimum capital requirement that was calculated in accordance with Part 3 – Minimum Capital Requirements of the Prudential Rules.

### 4.2 MINIMUM CAPITAL REQUIREMENTS AND CAPITAL RATIO

The minimum capital requirements of Alistithmar Capital as of end of December 31, 2014 as per the audited financial statements are as follows:

| Exposure class | Exposure before CRM | | Net Exposures after CRM | Risk Weighted Assets | Capital Requirement |
|---|---|---|---|---|---|
| ***Credit Risk*** | | | | | |
| *On-balance Sheet Exposures* | | | | | |
| Governments and Central Banks | - | | - | - | - |
| Authorized Persons and Banks | 858 | | 858 | 172 | 24 |
| Corporates | - | | - | - | - |
| Retail | - | | - | - | - |
| Investments | 39,897 | | 39,897 | 85,171 | 11,924 |
| Securitization | - | | - | - | - |
| Margin Financing | 836,512 | | 836,512* | 965,876** | 135,223 |
| Other Assets | 34,428 | | 34,428 | 147,928 | 20,710 |
| **Total On-Balance sheet Exposures** | **911,695** | | **75,183** | **1,199,147** | **167,881** |
| *Off-balance Sheet Exposures* | | | | | |
| OTC/Credit Derivatives | - | | - | - | - |
| Repurchase agreements | - | | - | - | - |
| Securities borrowing/lending | - | | - | - | - |
| Commitments | - | | - | - | - |
| Other off-balance sheet exposures | 1,613 | | 1,613 | 11,520 | 1,613 |
| **Total Off-Balance sheet Exposures** | **1,613** | | **1,613** | **11,520** | **1,613** |
| **Total On and Off-Balance sheet Exposures** | **913,308** | | **76,796** | **1,210,667** | **169,493** |
| **Prohibited Exposure Risk Requirement** | - | | - | - | - |
| **Total Credit Risk Exposures** | **913,308** | | **76,796** | **1,210,667** | **169,493** |
| ***Market Risk*** | **Long** | **Short** | | | |
| Interest rate risks | - | - | | | - |
| Equity price risks | - | - | | | - |
| Risks related to investment funds | - | - | | | - |
| Securitization/re-securitization positions | - | - | | | - |
| Excess exposure risks | - | - | | | - |
| Settlement risks and counterparty risks | - | - | | | - |
| Foreign exchange rate risks | 108,417 | 3 | | | 2,172 |
| Commodities risks. | - | - | | | - |
| **Total Market Risk Exposures** | **108,417** | **3** | | | **2,172** |
| ***Operational Risk*** | | | | | **19,616** |
| | | | | | |
| **Minimum Capital Requirements** | | | | | **188,178** |
| | | | | | |
| **Surplus/(Deficit) in capital** | | | | | **132,645** |
| **Total capital ratio (time)** | | | | | **1.69** |

* The Company has CRM techniques, however as per the regulation, since the capital charge is based on the exposures before CRM, the same has been reported here. However, the company has collaterals to cover the exposures to margin financing.

** The RWA for margin financing exposures have been as per the requirements of the Prudential Rules of CMA

# 5. RISK MANAGEMENT

## 5.1 GENERAL QUALITATIVE DISCLOSURE FOR RISKS

### 5.1.1 CREDIT RISK

Credit risk is the risk of loss due to an obligor's non-payment of an outstanding debt, loan or other line of credit (either the principal or interest (coupon) or both). The principal sources of credit risk for ICAP arise from two potential sources:

1. Margin facilities to corporate clients and retail customers – both conventional and Islamic facilities
2. Proprietary Investments of the Company

With respect to the margin facilities provided by the Company, there is a detailed policy that covers the parameters that should be considered prior to the acceptance of a customer for the provision of margin facilities, rules of disbursement, different controls that need to be in place during the facility period, etc. There are stipulated minimum coverage ratios required for the disbursement of margin facilities depending on the market.

The Risk Management Department is engaged in frequent monitoring of the different limits and controls that are in place for the provision of such facilities. In addition to the minimum coverage ratios, there are controls in terms of maximum limit per customer, tenor limits, margin calls, and various other risk controls in order to minimize the credit risk arising from these facilities.

Margin lending decisions are based on credit scoring models and decision strategies, developed using internal data with behavioral scoring applied. The approval process is reviewed regularly by Board Credit Risk Committee with limit delegations from the Board. Within the company, emphasis is placed on the responsibility for making credit decisions and as such there is a series of delegated approval limits agreed by Board.

In terms of the proprietary investment portfolio, the Company invests only after performing enhanced due diligence on the investment and obtaining appropriate approvals from the Board of the Company through the Board Proprietary Investment Committee. The approval process is very organized and sufficient care is taken while taking those investments moreover they also conform to the Investment Policy guidelines that are approved by the Board.

The company also carries out regular stress tests on the above different aspects to effectively monitor, measure and manage the credit risk that the company is exposed to. The Risk management Manual and the credit policies are all annually reviewed by the Chief Risk Officer who reports independently to the Credit and Risk Committee which is a Board Committee. These are approved by the Board on an annual basis.

Credit risk consumes the largest proportion of the Company's minimum capital requirement. Within the established principles and parameters the company ensures that strict capital discipline is maintained through correct pricing and management of credit risks in relation to the regulatory and economic capital requirements.

Further information on credit risk capital is provided in section 5.2 – Credit Risk Disclosure.

### 5.1.2 MARKET RISK

This is the risk that the value of an investment will decrease due to movements in market factors. The market risk factors considered by the Company are equity risk, interest rate risk, foreign exchange risk, credit spread risk, underwriting risk, commodity risk and settlement risk. The Company has very little market risk given that it does not operate an active trading book. It invests its excess cash in carefully analyzed and selected investment after appropriate due diligence.

The Company does not having an active trading book, however it has established a detailed Investment policy guideline that it should follow which prescribes the trading limits, investment limits, exposure limits, etc. that shall be strictly followed in case of any positions that the Company takes in principal. The Company has a formalized procedure to be followed in case of taking any exposures to investments as Principal. One of the purposes of this procedure was to ensure that the capital adequacy requirements are taken into consideration well before the investment is made. This process is in addition to the formal approval process which requires all such investments taken in principal capacity to be approved by the Board Proprietary Investment Committee having representation of Board members in the Committee.

The monitoring and control of market risk is handled by the risk management function which is responsible for ensuring market risk exposures are measured in accordance with defined policies and reported daily against prescribed control limits.

As noticed in the minimum capital requirements, given the absence of an active trading book, the capital requirements for market risk is very minimal which is only arising from the foreign exchange risk.

Further information on market risk capital is provided in section 5.5 – Market Risk Disclosure.

### 5.1.3 OPERATIONAL RISK

Operational risk is defined as per Basel II regulations, as the risk of direct or indirect losses resulting from human factors, external events and inadequate or failed internal processes and systems. In general, there are four main causes that are identified in standard operational risk definitions. Operational risk events can occur when there are inadequacies or failures due to:

- People (human factors)
- Processes
- Systems
- External events

Even though the above is self-explanatory, the above explicitly means, the person doing the activity making an error, the process that supports the activity is flawed, the system that facilitated the activity is broken, or an external event occurs that disrupts the activity.

In order to manage the operational risks within the Company, it operates a ‘three line of defense’ model as indicated below:

- The first line of defense is business line management. It has the primary responsibility for the identification, management and mitigation of the risks associated with the products and processed of its business. It engages in regular testing and certification of the adequacy and effectiveness of controls and compliance with the company’s policies and procedures

- The second line of defense is the company's Risk Management Department. This department is responsible for identifying the potential sources of risks that can arise as a result of the differing business lines and support functions in the Company. It is also responsible for the preparation and maintenance of the detailed risk register which identified the potential sources of risk and the possible controls that have to be in place in order to mitigate the identified risks
- The third line of defense is Audit. The Company's internal audit is responsible for assessing compliance with the risk register and for providing independent evaluation of the adequacy and effectiveness of the risk control framework. The Head of Internal Audit reports to the Audit Committee which is a Board committee.

In addition, to the above framework, it has been the Company's practice to document detailed policies and procedures, for all business lines and functions within the Company, which shall detail the ways in which things should be carried out to achieve the objectives of the function with minimal errors. The Company's policies and procedures are regularly reviewed by the management and approved by the Board of Directors.

Further information on market risk capital is provided in section 5.6 – Operational Risk Disclosure.

### 5.1.4 INTEREST RATE RISK

This is the risk that a movement in interest rates will impact the profitability of the Company. Interest rate risk arises principally from mismatches between the future yield on assets such as margin loans and their respective funding costs, as a result of changes in interest rates.

In order to manage interest rate risk, the pricing of margin loans are carefully performed taking into account the funding costs in order to minimize the mismatch in interest rate spreads. Risk monitoring is done on a periodic basis to assess this risk and to manage it effectively.

The Company does not engage in any hedging techniques to minimize interest rate risk.

There is no interest rate risk in the trading book as the Company does not hold a proprietary trading book.

### 5.1.5 FOREIGN EXCHANGE RISK

Currency or foreign exchange risk arises from an open position, either overbought (long) or oversold (short), in a foreign currency, creating exposure to a change in the relevant exchange rate.

The Company is not exposed to any Trading Book FX Risk as it does not hold a proprietary trading book.

However the company is exposed to Structural FX risk which arises from non-SAR denominated assets and liabilities in its normal course of business.

### 5.1.6 LIQUIDITY RISK

This is the risk of the Company not having available sufficient resources to enable it to meet its obligations as they fall due or can only secure such resources at excessive cost. The two aspects of liquidity are asset liquidity and funding liquidity.

Funding liquidity risk arises when the necessary liquidity to fund obligations cannot be obtained at the expected terms and when required. Asset liquidity risk arises when the assets are not able to be disposed at its current market value without affecting liquidity of the asset.

When it comes to funding liquidity risk, the Company monitors the liquidity position of the company regularly to meet any commitments in a timely manner. The Company also carries out stress testing to assess the worst case scenario in terms of liquidity crisis with a view to assess the company's ability to maintain an adequate capital position in such a scenario.

The Company also closes monitors the availability of funding lines to meet the commitments.

The Company seeks to maintain a cushion of unencumbered, liquid investment that can be liquidated in times of meeting unexpected cash flows arising from the normal course of business.

### 5.1.7 CONCENTRATION RISK

Concentration risk is the possible losses that shall be incurred arising from heavily lopsided exposure to a particular group of counterparties. In terms of the Company, the possible concentration risks that can lead to a loss of capital are from any of the following sources:

- Concentration of its clients whose defaults will result in a direct loss of capital for the Company
- Concentration of its investment portfolio to a few asset classes or few counterparties or few instruments

It needs to be understood that concentration risk is not a stand-alone risk and is a part of the other risk elements such as credit or market risks. However apart from the above direct loss of capital, potential concentration among the Company's clients in terms of its customers shall mean that the income sources of the Company is concentrated and this indirectly could have an impact on the income of the Company – therefore this is also considered as a source of concentration risk.

All approved borrowing limits are subject to credit analysis and assessment as set out in the policies and procedures and there are concentration limits for the same along with the approval matrix. Exposures are monitored on a regular basis, and are overseen by CEO and the Board Credit and Risk Committee.

Prudent sanctioning of any new lending is a key mitigant. In terms of concentration of margin financing clients, as a control measure in order to mitigate and manage concentration risk, a maximum cap has been placed on the margin commitment that can be provided for any single client.

In terms of monitoring the concentration risk, regular reports are being generated by the Risk Management department to monitor the largest exposures and the concentration of these exposures along with their underlying collaterals in order to assess the capital at loss, if any, despite the required coverage requirements.

Moreover, as per the Prudential Rules issued by the CMA, there is a large exposure limit that has been placed as 25% of the capital base beyond which all such exposures are considered as prohibited exposures. The reporting limit is 10% of the capital base which is regularly monitored on a monthly basis as part of the CAM submissions to the Authority.

### 5.1.8 BUSINESS/ECONOMIC RISK

Business risks implies uncertainty in profits or danger of loss and the events that could pose a risk due to some unforeseen events in future, which causes businesses to fail.

Business risk could arise either due to:

- Internal risks – risks arising from events that may happen within the company; or
- External risks – risks arising from events that happen out of the company

Economic risk is somewhat related to Business risk, as the former is a key External risk that is prone to happen which may impact the running of the company. Explicitly, economic risk can be described as the likelihood that the company will be affected by macroeconomic conditions such as government regulation, exchange rates, or political stability, most commonly in a foreign country.

The key potential business risks are identified as part of the budgeting and forecasting process. The outcome of this process forms the basis for sensitivity analysis of the net income, which is incorporated as part of the annual budget report presented to the Board of Directors for approval. Business risk is covered by the budgeted income. Moreover, the company usually does an ongoing review of its performance against the budget and in addition also takes into account the current market conditions and economic factors and incorporates this in order to revise the forecasted financial statements of the company in order to assess its position against where it was expected to be in the budgets.

In terms of economic risk, the risk management department does a regular stress testing which takes into account some distressed macro-economic conditions in order to assess the impact on the net income of the company.

With respect to managing the risk of key positions within the company, the company has a detailed succession plan for all of the key positions within the company so that there is no disruption in business activity or impact rising from such instances.

### 5.1.9 STRATEGIC RISK

The risk that the medium and long term profitability of the company could be adversely impacted by the failure to either identify and implement the correct strategy or not being able to meet its business objectives, targets or losing the support from its shareholders.

This is somewhat related to the business risk and economic risk elements identified above and are not significantly different from those risks and the factors relating to those. Competition risk could be one of the primary causes of strategic risk.

Competition risk is the risk of intense competition from the competitors. Keeping in view the business cycle of the investment management industry in the Kingdom, the risk of competitors and new entrants is phenomenal.

The strategy department on a regular basis and variations monitors the strategic risks, if any are reported to the Board to refine the Company's strategy in light of market developments.

The Company in an effort to have a clear direction had developed a medium term strategic plan ranging over the next 5 years, which identifies clearly the objectives of the company and how it intends to achieve them.

### 5.1.10 COMPLIANCE RISK

Compliance risk is the current and prospective risk of non-conformance with applicable, laws, rules and regulations set forth by the CMA and other governmental and supervising agencies within the Kingdom of Saudi Arabia, in addition to the best and common practices and ethical standards. These risks also arise in situations where the laws or rules governing the company's products or activities of its clients may be ambiguous or untested. These risks expose the institution to fines, civil money penalties, payment of damages, voiding of contracts and it might reach the cancelation of the investment licenses for major braches. Compliance risk can lead to diminished reputation, reduced franchise value, limited business opportunities, reduced expansion potential, and an inability to enforce contracts.

Compliance, Regulatory and Statutory risks are within the overall responsibilities of the Compliance Department. The Compliance Department is responsible for managing regulatory and compliance risks. The Company measures its vulnerability to loss (on an on-going basis) under potential litigations arising due to various reasons listed above.

The Compliance Committee reports to the Audit Committee, which is a Board committee with its key findings and observations on a regular basis. Moreover, the Compliance department also carries out a regular compliance monitoring program to identify the key compliance issues relating to different business and functional activities.

### 5.1.11 REPUTATION RISK

Reputation risks relate to risks that could damage reputation or standing of the company in the marketplace. Materialization of reputation risk could lead to perceptions of poor corporate governance and inability / lack of commitment in being able to provide valuable services to clients.

Possible sources of reputation risk have been identified as follows:

- Regulatory or legal compliance failure;
- Unethical practice by company employee;
- Failure to deliver minimum standards of service;
- Failure to achieve financial performance targets;
- Poor crisis management;
- Security breach;
- Failure to meet market expectations;
- Ineffective Business Continuity Plans; and
- Inadequate IT services

Reputational risk is not a stand-alone risk and is inherent and derived from any of the other risks that have been detailed above. As these are not stand alone risks, proper and efficient management of the underlying risks which are prone to result in these risks is critical to avoid reputation risk.

## 5.2 CREDIT RISK DISCLOSURE – ADDITIONAL DISCLOSURES

### 5.2.1 PAST DUE LOANS

A loan is considered past due if it is not repaid on the payment due date or maturity date.

### 5.2.2 IMPAIRED LOANS

The Company regularly monitors the past due loans and the duration of such past due exposures. Based on its internal approved policies depending on how long the loan has been past due and the presence of financial collateral, the Company decides to write off the loan amount. However this shall be only done with the approval of the Board Credit and Risk Committee. There are no general provisions being created for the margin loan portfolio given the strong controls in place.

### 5.2.3 CREDIT RATING SCALES AND CREDIT RISK WEIGHTS

The Company for the purpose of assigning ratings uses the three globally recognized credit rating institutions namely:

1. Moody's Investors Service
2. Standard and Poor's Ratings Group
3. Fitch Group

Credit ratings of all exposures are individually determined from the above credit rating agencies and mapped to the exposures assigning a risk weight according to the Prudential Rules. The alignment of alphanumeric scales of each agency to risk buckets is as follows:

| Moody's | Standard & Poor's | Fitch |
|---|---|---|
| Aaa | AAA | AAA |
| Aa1 | AA+ | AA+ |
| Aa2 | AA | AA |
| Aa3 | AA- | AA- |
| A1 | A+ | A+ |
| A2 | A | A |
| A3 | A- | A- |
| Baa1 | BBB+ | BBB+ |
| Baa2 | BBB | BBB |
| Baa3 | BBB- | BBB- |
| Ba1 | BB+ | BB+ |
| Ba2 | BB | BB |
| Ba3 | BB- | BB- |
| B1 | B+ | B+ |
| B2 | B | B |
| B3 | B- | B- |
| Caa1 | CCC+ | CCC+ |
| Caa2 | CCC | CCC |
| Caa3 | CCC- | CCC- |
| Ca | CC | CC |
| C | C | C |
| NR | D | D |
| | NR | NR |

In case of differing ratings by the different rating agencies, as the prudent basis, the minimum of the three available ratings are taken to account for the risks.

The following are the mappings between the credit rating from each credit rating agency and the credit quality steps with respect to non-trading activities. This is in compliance with the Prudential Rules issued by the CMA.

| Credit Quality Step for long term ratings | S&P | Fitch | Moody's |
|---|---|---|---|
| 1 | AAA to AA- | AAA to AA- | Aaa to Aa3 |
| 2 | A+ to A- | A+ to A- | A1 to A3 |
| 3 | BBB+ to BBB- | BBB+ to BBB- | Baa1 to Baa3 |
| 4 | BB+ to BB- | BB+ to BB- | Ba1 to Ba3 |
| 5 | B+ to B- | B+ to B- | B1 to B3 |
| 6 | CCC+ and below | CCC+ and below | Caa1 and below |
| 7 | Non rated | Non rated | Non rated |

| Credit Quality Step for short term ratings | S&P | Fitch | Moody's |
|---|---|---|---|
| 1 | A-1+, A-1 | F1+, F1 | P-1 |
| 2 | A-2 | F2 | P-2 |
| 3 | A-3 | F3 | P-3 |
| 4 | Below A-3 | Below F3 | Not Prime |
| 5 | Non rated | Non rated | Non rated |

The risk weights for the different exposure types are as follows:

| Credit Quality Step | 1 | 2 | 3 | 4 | 5 | 6 | 7 |
|---|---|---|---|---|---|---|---|
| Exposure to government or central banks | 0% | 20% | 50% | 100% | 100% | 150% | 150% |
| Exposure to authorized persons and banks | 20% | 50% | 100% | 100% | 100% | 150% | 150% |
| Exposures to authorized persons, banks and foreign equivalents with an original maturity of three months or less | 20% | 20% | 20% | 50% | 50% | 150% | 150% |
| Exposure to corporates | 20% | 50% | 100% | 200% | 400% | 714% | 714% |
| Exposure to securitization positions | 20% | 50% | 100% | 350% | 714% | 714% | 714% |
| Exposure to re-securitization position | 20% | 50% | 100% | 350% | 714% | 714% | 714% |
| Exposure to investment funds | 20% | 50% | 100% | 100% | 150% | 150% | 150% |

## 5.2.4 CREDIT RISK QUANTITATIVE DISCLOSURES – RISK WEIGHT AND EXPOSURES

| | Exposures after netting and credit risk mitigation | | | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| **Risk Weight** | Govt and Central banks | Administrative bodies and NGO | Authorized person and banks | Margin Financing | Corporates | Retail | Past due items | Investments | Securitization | Other assets | Off balance sheet commitments | **Total Exposure after netting and CRM** | **Total Risk Weighted Assets** |
| 0% | - | - | - | - | - | - | - | - | - | - | - | **-** | **-** |
| 20% | - | - | 858 | - | - | - | - | - | - | - | - | **858** | **172** |
| 50% | - | - | - | - | - | - | - | - | - | - | - | **-** | **-** |
| 100% | - | - | - | 836,512* | - | - | - | - | - | - | - | **836,512*** | **965,876**** |
| 150% | - | - | - | - | - | - | - | 29,046 | - | - | - | **29,046** | **43,568** |
| 200% | - | - | - | - | - | - | - | - | - | - | - | **-** | **-** |
| 300% | - | - | - | - | - | - | - | 1,800 | - | 23,644 | - | **25,444** | **76,332** |
| 400% | - | - | - | - | - | - | - | 9,051 | - | - | - | **9,051** | **36,203** |
| 500% | - | - | - | - | - | - | - | - | - | - | - | **-** | **-** |
| 714% | - | - | - | - | - | - | - | - | - | 10,784 | 1,613 | **12,397** | **88,515** |
| Avg Risk Weight * | - | - | 20% | - | - | - | - | 213.48% | - | 429.68% | 714% | **N/A** | **N/A** |
| Deduct from capital base | - | - | - | - | - | - | - | - | - | - | - | **-** | **-** |

*All of the above figures are in SAR '000*
*The average risk weights have been calculated based on the weighted average weights for the different exposure types under the respective category*

** The Company has CRM techniques, however as per the regulation, since the capital charge is based on the exposures before CRM, the same has been reported here. However, the company has collaterals to cover the exposures to margin financing.*
*** The RWA for margin financing exposures have been as per the requirements of the Prudential Rules of CMA*

### 5.2.5 CREDIT RISK QUANTITATIVE DISCLOSURES –IMPAIRMENTS AND PAST DUE EXPOSURES

Not applicable

There have been no past due exposures as of December 31, 2014. With respect to impairments please refer to section 5.2.2. There have been no impaired assets as of December 31, 2014.

### 5.2.6 CREDIT RISK QUANTITATIVE DISCLOSURES –GEOGRAPHICAL EXPOSURES

| All figures are in SAR '000 | Kingdom of Saudi Arabia | Gulf Cooperation Council |
|---|---|---|
| **On balance sheet exposures** | | |
| Authorized persons and banks | 858 | - |
| Investments | 30,846 | 9,051 |
| Margin Financing | 836,512 | - |
| Other assets | 34,428 | - |
| **Off balance sheet exposures** | 1,613 | - |

### 5.2.7 CREDIT RISK QUANTITATIVE DISCLOSURES –RESIDUAL CONTRACTUAL MATURITY OF CREDIT EXPOSURES

| All figures are in SAR '000 | Less than 3 months | 3 months to 1 year | 1 year to 5 years | More than 5 years | No fixed maturity |
|---|---|---|---|---|---|
| **On balance sheet exposures** | | | | | |
| Authorized persons and banks | - | - | - | - | 858 |
| Investments | - | - | 1,800 | - | 38,097 |
| Margin Financing | 115,709 | 180,476 | - | - | 540,327 |
| Other assets | 14,260 | 6,488 | 1,772 | - | 11,907 |
| **Off balance sheet exposures** | - | - | - | - | 1,613 |

### 5.2.8 CREDIT RISK QUANTITATIVE DISCLOSURES –RECONCILIATION REPORT FOR PROVISIONS AND IMPAIRMENTS

Not applicable

There have been no past due exposures as of December 31, 2014. With respect to impairments please refer to section 5.2.2. There have been no impaired assets as of December 31, 2014

## 5.2.9 CREDIT RISK QUANTITATIVE DISCLOSURES –CREDIT RISK'S RATED EXPOSURE

**Long Term Ratings of Counterparties**

| | Credit step 1 | Credit step 2 | Credit step 3 | Credit step 4 | Credit step 5 | Credit step 6 | Credit step 7 (N/R) |
|---|---|---|---|---|---|---|---|
| On and Off balance sheet exposures | | | | | | | |
| Government and Central Banks | - | - | - | - | - | - | - |
| Authorized Persons and Banks | - | 858 | - | - | - | - | - |
| Corporates | - | - | - | - | - | - | - |
| Retail | - | - | - | - | - | - | - |
| Investments | - | - | - | - | - | - | 39,897 |
| Securitization | - | - | - | - | - | - | - |
| Margin Financing | - | - | - | - | - | - | 836,512 |
| Other Assets | - | - | - | - | - | - | 34,428 |
| Off-balance sheet | - | - | - | - | - | - | 1,613 |
| **Total** | **-** | **858** | **-** | **-** | **-** | **-** | **912,450** |

**Short Term Ratings of Counterparties**

| | Credit step 1 | Credit step 2 | Credit step 3 | Credit step 4 | Credit step 5 (N/R) |
|---|---|---|---|---|---|
| On and Off balance sheet exposures | | | | | |
| Government and Central Banks | - | - | - | - | - |
| Authorized Persons and Banks | - | 858 | - | - | - |
| Corporates | - | - | - | - | - |
| Retail | - | - | - | - | - |
| Investments | - | - | - | - | 39,897 |
| Securitization | - | - | - | - | - |
| Margin Financing | - | - | - | - | 836,512 |
| Other Assets | - | - | - | - | 34,428 |
| Off-balance sheet | - | - | - | - | 1,613 |
| **Total** | **-** | **858** | **-** | **-** | **912,450** |

## 5.3 CREDIT RISK MITIGATION EXPOSURES

### 5.3.1 QUALITATIVE DISCLOSURES

The mitigation of credit risk is an important aspect of its effective management and takes many forms. When it comes to margin financing, the company nevertheless holds a range of collaterals to reduce the risk of loss and maximize the probability of facilities being repaid. The nature and type of assets that can be accepted as collaterals are approved by the Board Credit and Risk Committee.

The main types of collaterals that the Company accepts with respect to margin financing are:

- Cash in any currency that is under immediate control of the company currently or in any future value date
- Securities in local Markets at a value considered fair value at the Company's own assessments
- Securities in GCC and International Markets at a value considered fair value at Company's own assessments
- Bonds or Sukuk in any markets subject to Credit Risk Committee acceptance and approval and evaluation
- Other instruments as approved accepted and evaluated by the Credit and Risk Committee

The Company has a Committee which determines the haircuts on the collaterals on a regular basis. The Company has in place a formalized model that would be an indicative model in determining the haircuts that shall be applied to the stocks for which margin facilities are being provided. The indicative model takes into account in detail different factors which are of key concern in providing margin facility for such stocks.

Margin lending decisions are based on credit scoring models and decision strategies, developed using internal data with behavioral scoring applied. The approval process is reviewed regularly by Board Credit Risk Committee with limit delegations from the Board. Within the company, emphasis is placed on the responsibility for making credit decisions and as such there is a series of delegated approval limits agreed by Board.

## 5.3.2 QUANTITATIVE DISCLOSURES

| | Exposures before CRM | Exposures covered by Guarantee/ Credit derivatives | Exposures covered by Financial collateral | Exposures covered by Netting Agreement | Exposures covered by other eligible collaterals | Exposures after CRM |
|---|---|---|---|---|---|---|
| ***Credit Risk*** | | | | | | |
| *On-balance sheet exposures* | | | | | | |
| Government and Central Banks | - | - | - | - | - | - |
| Authorized Persons and Banks | 858 | - | - | - | - | 858 |
| Corporates | - | - | - | - | - | - |
| Retail | - | - | - | - | - | - |
| Investments | 39,897 | - | - | - | - | 39,897 |
| Securitization | - | - | - | - | - | - |
| Margin Financing | 836,512 | - | 836,512 | - | - | 836,512* |
| Other Assets | 34,428 | - | - | - | - | 34,428 |
| **Total On-Balance sheet exposures** | **911,695** | - | **836,512** | - | - | **911,695** |
| *Off-balance sheet exposures* | - | - | - | - | - | - |
| OTC/Credit Derivatives | - | - | - | - | - | - |
| Exposure in the form of repurchase agreements | - | - | - | - | - | - |
| Exposure in the form of securities lending | - | - | - | - | - | - |
| Exposure in the form of commitments | - | - | - | - | - | - |
| * Other off-balance sheet exposures | 1,613 | - | - | - | - | 1,613 |
| **Total Off-Balance sheet exposures** | **1,613** | - | - | - | - | **1,613** |
| **Total On and Off-Balance sheet exposures** | **913,308** | - | **836,512** | - | - | **913,308** |

** The Company has CRM techniques, however as per the regulation, since the capital charge is based on the exposures before CRM, the same has been reported here. However, the company has collaterals to cover the exposures to margin financing.*

## 5.4 COUNTERPARTY CREDIT RISK (CCR) AND OFF BALANCE SHEET DISCLOSURES

### 5.4.1 QUALITATIVE DISCLOSURES

Counterparty credit risk is the risk that a counterparty to a transaction may default before completing the satisfactory settlement of the transaction.

The company does not have any exposure to any Over-The-Counter (OTC) derivatives.

### 5.4.2 QUANTITATIVE DISCLOSURES

Not applicable, as the company does not have any exposure to any OTC derivatives.

## 5.5 MARKET RISK DISCLOSURES

### 5.5.1 QUALITATIVE DISCLOSURES

This is the risk that the value of an investment will decrease due to movements in market factors. The market risk factors considered by the Company are equity risk, interest rate risk, foreign exchange risk, credit spread risk, underwriting risk, commodity risk and settlement risk. The Company has very little market risk given that it does not operate an active trading book. It invests its excess cash in carefully analyzed and selected investment after appropriate due diligence.

The Company does not having an active trading book, however it has established a detailed Investment policy guideline that it should follow which prescribes the trading limits, investment limits, exposure limits, etc. that shall be followed in case of any positions that the Company takes in principal. The Company has a formalized procedure to be followed in case of taking any exposures to investments as Principal. One of the purposes of this procedure was to ensure that the capital adequacy requirements are taken into consideration well before the investment is made. This process is in addition to the formal approval process which requires all such investments taken in principal capacity to be approved by the Board Proprietary Investment Committee having representation of Board members in the Committee.

The monitoring and control of market risk is handled by the risk management function which is responsible for ensuring market risk exposures are measured in accordance with defined policies and reported daily against prescribed control limits.

As noticed in the minimum capital requirements, given the absence of an active trading book, the capital requirements for market risk is very minimal which is only arising from the foreign exchange risk.

### 5.5.2 QUANTITATIVE DISCLOSURES

The capital requirements for market risk as per the requirements of Pillar 1 of the Prudential Rules as of December 31, 2014 are as follows:

| All figures are in SAR '000 | Capital requirements |
|---|---|
| Equity & Fund Risk | - |
| Interest Rate Risk | - |
| Commodities Risk | - |
| FX Risk | 2,172 |
| Underwriting Risk | - |
| Excess Exposure Risk | - |
| Settlement Risk | - |
| **Total capital requirements** | **2,172** |

The company does not operate a trading book and hence no capital requirements specifically required for the trading book.

## 5.6 OPERATIONAL RISK DISCLOSURE

### 5.6.1 QUALITATIVE DISCLOSURES

Operational risk is defined as per Basel II regulations, as the risk of direct or indirect losses resulting from human factors, external events and inadequate or failed internal processes and systems. In general, there are four main causes that are identified in standard operational risk definitions. Operational risk events can occur when there are inadequacies or failures due to:

- People (human factors)
- Processes
- Systems
- External events

Even though the above is self-explanatory, the above explicitly means, the person doing the activity making an error, the process that supports the activity is flawed, the system that facilitated the activity is broken, or an external event occurs that disrupts the activity.

In order to manage the operational risks within the Company, it operates a 'three line of defense' model as indicated below:

- The first line of defense is business line management. It has the primary responsibility for the identification, management and mitigation of the risks associated with the products and processed of its business. It engages in regular testing and certification of the adequacy and effectiveness of controls and compliance with the company's policies and procedures
- The second line of defense is the company's Risk Management Department. This department is responsible for identifying the potential sources of risks that can arise as a result of the differing business lines and support functions in the Company. It is also responsible for the preparation and maintenance of the detailed risk register which identified the potential sources of risk and the possible controls that have to be in place in order to mitigate the identified risks

- The third line of defense is Audit. The Company's internal audit is responsible for assessing compliance with the risk register and for providing independent evaluation of the adequacy and effectiveness of the risk control framework. The Head of Internal Audit reports to the Audit Committee which is a Board Committee.

In addition, to the above framework, it has been the Company's practice to document detailed policies and procedures, for all business lines and functions within the Company, which shall detail the ways in which things should be carried out to achieve the objectives of the function with minimal errors. The Company's policies and procedures are regularly reviewed the management and approved by the Board of Directors.

The Company follows the Basic Indicator Approach for the calculation of the operational risk capital requirements which is 15% of the income indicator calculated in accordance with Annex 4 of the Prudential Rules. However as stipulated by the Prudential Rules, the requirement for operational risks shall correspond to not less than 25% of the Company's overhead expenses calculated in accordance with Chapter 12 of Part 1 of the Prudential Rules.

### 5.6.2 QUANTITATIVE DISCLOSURES

As per the guidelines in the Prudential Rules, the capital requirement as per the approach stated above is SAR 19.62 Mn as of the year ended 31 December 2014.

## 5.7 LIQUIDITY RISK DISCLOSURE

### 5.7.1 QUALITATIVE DISCLOSURES

Liquidity risk is the risk of not having available sufficient resources to enable it to meet its obligations as they fall due or can only secure such resources at excessive cost. The two aspects of liquidity are asset liquidity and funding liquidity.

- Funding liquidity risk arises when the necessary liquidity to fund obligations cannot be obtained at the expected terms and when required.
- Asset liquidity (or market liquidity) risk arises when the assets are not able to be disposed or transferred into cash without affecting the liquidity of the asset or incurring significant losses

The company has an approved liquidity risk policy in place which is regularly reviewed. The aim of the policy is to describe the policies and guidelines through which the Company manages its cash flow mismatches and its adopted liquidity risk management structure.

The key metrics ICAP uses to measure and limit liquidity risk is on two aspects:

1. Ability to meet commitments
2. Ability to meet the liabilities on its balance sheet

The company regularly monitors the following on a periodic basis as agreed by the management to assess the liquidity risk:

1. Surplus/deficit in availability of funding – in order to assess the ability to meet commitments
2. Residual contractual mismatch –in order to assess the mismatch in maturity of assets and liabilities

For the purpose of assessing the surplus/deficit in availability of funding, stressed scenario of worst case utilization scenarios by all customers is assumed. The stress test scenarios are applied keeping in mind the controls in place as discussed previously.

As part of its liquidity risk policy, the company has identified a series of steps it shall take in order to manage the liquidity risk in case of a liquidity crisis.

Moreover, as part of the same policy, ICAP has also identified a liquidity contingency plan which shall be used to solve an immediate liquidity crisis.

### 5.7.2 QUANTITATIVE DISCLOSURES

Currently the company has an approved credit line from a local bank in Saudi Arabia. As of December 31, 2014 the un-utilized amount of this funding credit line amounted to SAR 657 Mn which the company believes is an appropriate liquidity cushion given the low level of liquidity concerns in the near future given that there are no liquidity run offs expected in the near term.