





بِسْمِ اللَّهِ الرَّحْمَنِ الرَّحِيمِ

## Directors' Report

*The Board of Directors are pleased to submit to shareholders the Annual Report of HSBC Saudi Arabia Limited for the financial year ended 31st December 2016.*

### Introduction

HSBC SAUDI ARABIA LIMITED (HSBC SA), a limited liability company, registered in the Kingdom of Saudi Arabia under Commercial Registration No. 1010221555 dated 27/06/1427H (corresponding to 23/07/2006G) and SAGIA Licence No. 102030104697 dated 17/12/1426H (corresponding to 17/01/2006G), organized and existing under the laws of Saudi Arabia with its principal place of business address at HSBC Building 7267, Main Olaya Street (North), Al Morooj District, Riyadh 12283-2255, Kingdom of Saudi Arabia.

As at 31 December 2016, the Company is owned by the following shareholders in the proportion set out below:

	<b>Number of shares</b>	<b>Percentage contribution</b>	<b>As at 31 December 2016</b>
HSBC Asia Holdings BV (HSBC)	4,900	49%	245,000,000
The Saudi British Bank (SABB)	5,100	51%	255,000,000
<b>Total</b>	<b>10,000</b>	<b>100%</b>	<b>500,000,000</b>

The Company provides full range of securities activities services as per Capital Market Authority Regulations which includes, dealing, arranging, managing, advising and custody services. The range of services provided by the Company covers all investment banking activities such as investment banking advisory, debt and project finance including both conventional and Shariah compliant finance, management of mutual funds, discretionary portfolios and securities services. The Company serves a wide range of clients including but not limited to corporates, non-bank financial institutions and individuals.

The Company on 1 July 2011 acquired all the assets and liabilities together with its business activities of SABB Securities Limited (SASL), a 100% owned subsidiary of SABB. As per the shareholders resolution of SASL a voluntary liquidation is under progress and nearing completion.

### Key financial highlights

<b>Saudi Riyal (millions)</b>	<b>Year</b>				
	<b>2016</b>	<b>2015</b>	<b>2014</b>	<b>2013</b>	<b>2012</b>
Shareholder's Equity	<b>765</b>	865	785	795	731
Investments, Net	<b>615</b>	1,029	902	872	438
Total Assets	<b>1,028</b>	1,168	1,148	1,016	994
Net Income	<b>140</b>	279	229	258	218
Gross Dividend	<b>211</b>	157	192	163	164

## Net Income

---

HSBC SA recorded a net income for the year of SAR 140 million for the year ended 31 December 2016. This was a decrease of SAR 139 million compared to SAR 279 million for the year ended 2015. During 2016, operating income decreased by SAR 180m as management fee income and brokerage income decreased by SAR 109 million and SR 40 million respectively. The above was partly offset by savings in operating expenses of SAR 30 million.

---

## Cash Dividends

The annual net income of the Company is distributed as follows:

1. Amounts for payment of Zakat payable by Saudi shareholders and tax payable by the non-Saudi partner, will be calculated and allocated in line with the rules and regulations in force in the Kingdom of Saudi Arabia. The company will pay such amounts from the net income distributed to these parties.
2. 10% of the net income is transferred to statutory reserves until this reserve equals 30% of the paid up share capital of the Company.
3. Based on the recommendation of the Board and the approval of shareholders at the Ordinary General Meeting dividends will be paid to shareholders in accordance with the number of shares held by each shareholder.
4. Un-distributed net income is carried forward as retained earnings.

The Board of Directors have recommended the distribution of profits as follows:

	<b>SAR '000</b>
Net Income 2016	139,750
Retained earnings from the previous year	227,600
<b>Total</b>	<b>367,350</b>
<b>Distributed as follows:</b>	
Transferred to statutory reserves	13,975
Zakat and Income Tax	33,961
Paid/Proposed Dividend, Net	210,723
<b>Retained earnings for 2016</b>	<b>108,691</b>

## Statutory Payments

The statutory payments for the year were as follows:

	<b>SAR '000</b>
Zakat attributable to the Saudi Shareholders for 2015	2,113
Income tax attributable to non-Saudi shareholder for 2015	38,329
GOSI payments	12,729

**Directors' Report** (continued)**Net Income** (continued)**Related Party Balances and Transactions**

Related parties of the Company comprise of group companies including its affiliates and brokers, its shareholders and directors of HSBC Saudi Arabia Limited. The Company and its related parties transact with each other in the ordinary course of business. The transactions with related parties are undertaken at mutually agreed terms which are approved by the management. ly agreed terms which are approved by the management.

		<u>2016</u>
(a) Due from related parties		
Receivable from mutual funds	1	<b>944,303</b>
Receivable from SABB	2	<b>51,840,760</b>
Receivable from HSBC Plc	3	<b>6,712,695</b>
Receivable from HSBC Middle East Ltd.	4	<b>1,523,441</b>
		<b><u>61,021,199</u></b>
(b) Due to related parties		
Payable to SABB	5	<b>6,719,578</b>
Payable to HSBC Plc	6	<b>3,359,900</b>
Payable to HSBC Middle East Ltd.	7	<b>8,286,035</b>
Payable to Hongkong Shanghai Banking Corporation	8	<b>1,150,017</b>
		<b><u>19,515,530</u></b>

1. This represents management fees receivable from HSBC Saudi Arabia Limited Mutual Funds ("the Mutual Funds") calculated at mutually agreed rate.
2. This mainly represents receivable on account of advisory services and net balance on intercompany transactions with SABB.
3. This mainly represents receivable on account of equity swap commission of SAR 2.8 million and receivable on account of advisory services.
4. This mainly consists of receivable on account of services under service level agreement.
5. This mainly represents payable to SABB for services under service level agreement.
6. This mainly consists of payables on account of services under service level agreement and amounts due on advisory services performed.
7. This mainly consists of payables on account of services under service level agreement and amounts due on advisory services performed.
8. This mainly consists of payables on account of services under agreement.

## Net Income (continued)

### Related Party Balances and Transactions (continued)

The income, expenses and transactions in respect of related parties included in the financial statements are as follows:

<b>Transaction with</b>	<b>Description</b>	<b>2016</b>
The Saudi British Bank (SABB)	Services cost under service level agreement-net	<b>(23,697,780)</b>
	Income from Time deposit	<b>86,111</b>
	Cash and cash equivalents	<b>239,768,181</b>
	Cash at bank on account of swaps	<b>125,571,260</b>
	Arranging Income under service level agreement	<b>47,868,090</b>
	Fees paid for discretionary portfolios service and Mutual Funds	<b>(11,974,887)</b>
Hongkong and Shanghai banking Corporation	Services cost under agreement	<b>(363,998)</b>
HSBC Saudi Arabia Limited Mutual Funds ("the Mutual Funds")	Brokerage and Management Fee income, net	<b>71,854,796</b>
	Realized gain on sale of investments	<b>10,825,187</b>
	Investments in Funds	<b>608,415,378</b>
HSBC Bank Plc.	Income on equity swaps	<b>10,158,420</b>
	Services cost under agreement	<b>(1,125,659)</b>
	Advisory income	<b>3,937,500</b>
HSBC Middle East Ltd.	Cash and cash Equivalents	<b>2,401,511</b>
	Services cost under service level agreement-net	<b>(4,173,424)</b>
	Cash and cash equivalents	<b>4,553,669</b>
Directors Remuneration & Committee members fee		
Key management compensation		<b>(1,481,000)</b>
(Key management personnel of the Company comprise senior executive management)	Salaries & compensations	<b>(6,526,121)</b>
	Allowances	<b>(3,260,777)</b>
	Periodic and annual remuneration	<b>(11,933,240)</b>

### Strategic Future Plans

The Company is in the process of converting its legal status from Limited Liability Company to a Saudi Closed Joint Stock Company. Relevant approvals have been granted by regulatory and governmental authorities for the conversion of its legal status. In addition to the existing two shareholders, three entities which are wholly owned subsidiaries of SABB will become new shareholders in new ownership structure.

HSBC SA's vision is to be the leading investment banking services provider in the Kingdom. To achieve this vision, HSBC SA will continue to focus on the following key strategic objectives:

- Operate within the Risk appetite framework as approved by its Board but recognising the risk appetite of its shareholders HSBC and SABB
- Implementation of HSBC SA International Standards and compliance with all applicable rules and regulations
- Attract, retain and grow talent
- Improve Operational efficiency and enhance organizational effectiveness
- Diversify product offering and embark on digitalisation

**Directors' Report** (continued)**Punishments, Penalties and Regulatory Restrictions**

During 2016, HSBC SA was subject to penalties from the regulator for minor breaches which were subsequently addressed.

**Directors' Remuneration**

Directors' fees during 2016 amounted to SAR 1,355,000. Apart from the directors fee a sum of SAR 126,000 was paid on account of attendance fee.

<b>Details</b>	<i>Executive</i>	<i>Non-executive/ Independent</i>	<i>Detailed remuneration for the six Executives who received the highest compensation from the Company. The CEO and Chief Financial Officer are included as per requirement</i>
<b>SAR' 000</b>	<i>Board Members</i>	<i>Board Members</i>	
Salaries & compensations	-	N/A	<b>6,526,121</b>
Allowances	-	N/A	<b>3,260,777</b>
Periodic and annual remunerations*	-	N/A	<b>11,933,240</b>
Incentive schemes	-	N/A	-
Any compensation or benefits in kind paid on a monthly and annual basis	-	<b>1,481,000</b>	-

\*Bonuses

**Staff Benefits and Schemes**

According to the Labour Law of The Kingdom of Saudi Arabia and the Company's internal policies, staff benefits are due for payment during or at the end of an employee's period of service. The end of service benefit outstanding as at 31 December 2016 amounted to SAR 42.7 million.



## **Board of Directors' Assurance**

---

The Board of Directors assures shareholders and other interested parties that to the best of its knowledge and in all material aspects:

- The Company's books of account were properly prepared
- The Company's internal control system is effective
- It has no evidence on record that might cast significant doubt on the Company's ability to continue as a going concern
- There is no contract or deal the company is part of, where or when there were substantial interests for one of the Board Members, CEO, Chief Financial Officer or any person who has a relationship with them, except for that which was disclosed in the Related Party Transactions in this report
- The Company does not have any affiliate i.e any holding in share capital of any company
- The board members or any person who has a relationship with them did not have any interest, contractual securities or subscription rights in the shares of the company during the year
- The company has not taken any loan during the year

As indicated in their audit report, the Company's auditors, for the purpose of their work on the financial statements, have considered internal controls relevant to the Company's preparation and fair presentation of the financial statements in order to enable them to design audit procedures which are appropriate, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal controls. The Auditors have issued an unqualified audit report on the financial statements of the Company.

## **Accounting Standards**

---

The financial statements have been prepared in accordance with the accounting standards issued by SOCPA. There has been no major deviation in the accounting standards applied at HSBC SA against SOCPA's accounting standards during the financial year ended 31 December 2016.

## **Appointment of External Auditors**

---

In the AGM of the company held on 30 March 2016, the shareholders endorsed the selection of KPMG AIFozan & Partners as external auditors according to the recommendation of the Audit Committee, to audit the Company's annual financial statements for the year ended 31 December 2016.

## **Board of Directors and its Sub-Committees**

---

The Board of Directors of HSBC SA comprises of nine (9) members, who shall be appointed and removed as follows:

- a) Three (3) Managers shall be appointed and removed by HSBC;
- b) Three (3) Managers shall be appointed and removed by SABB; and
- c) Three (3) Managers shall be Independent Managers and shall be appointed and removed with the unanimous consent of both SABB and HSBC.

**Directors' Report** (continued)**Board of Directors**

---

The Board of Directors as at 31 December 2016 comprised of the following:

---

**Mr Mansour Al Bosaily**, NON-EXECUTIVE, CHAIRMAN AND BOARD MEMBER (1ST JANUARY 2015)

Board Member, Saudi Ground Services Company  
Board Member, Saudi Reinsurance Company  
Board Member, National Amlak Company  
Board Member, Jabal Omar Developments Company  
Board Member, United Electronics Company (eXtra)

---

**Mr Majed Najm**, CHIEF EXECUTIVE OFFICER AND BOARD MEMBER HSBC SA, EXECUTIVE (1ST JANUARY 2015)

NIL

---

**Mr David Dew**, NON-EXECUTIVE, BOARD MEMBER (1ST JANUARY 2015)

Board Member and Managing Director of The Saudi British Bank

---

**Mr Georges Elhedery**, NON-EXECUTIVE, BOARD MEMBER (15TH MARCH 2015)

Board Member, HSBC Bank Egypt SAE  
Board Member, The Saudi British Bank  
Board Member, HSBC Bank Middle East Limited

---

**Mr Sridhar Chandrasekharan**, NON-EXECUTIVE, BOARD MEMBER (31ST OCTOBER 2016)

Board Member, HSBC Global Asset Management Limited  
Board Member, Non-Executive, Hang Seng Investment Management Limited

---

**Mr Hamad Al Omar**, INDEPENDENT, BOARD MEMBER (1ST JANUARY 2015)

NIL

---

**Mr Mohammad Alshayea**, INDEPENDENT, BOARD MEMBER (1ST JANUARY 2015)

Board Member, Saudi Ground Services Company  
Board Member, NAJM for Insurance Services

---

**Mr Abdulatif Al Seif**, INDEPENDENT, BOARD MEMBER (15TH MARCH 2016)

NIL

---

**Vacant**

## Board of Directors (continued)

### Board Members who resigned during 2016

**Mr Fahad Al Saif**, NON-EXECUTIVE, BOARD MEMBER (RESIGNED WITH EFFECT FROM 25TH MAY 2016)

NIL

**Mr Mohammad Al Tuwaijri**, NON-EXECUTIVE, BOARD MEMBER (RESIGNED WITH EFFECT FROM 8TH MAY 2016)

Board Member, The Saudi British Bank  
Board Member, HSBC Bank Egypt SAE  
Board Member, Public Pension Agency

**Mr Martin Spurling**, NON-EXECUTIVE, BOARD MEMBER (RESIGNED WITH EFFECT FROM 1ST FEBRUARY 2016)

NIL

Number of Board & Committee meetings attended by each Director during 2016:

No.	Name	Board Meetings	EXCOM Meetings	Audit Committee Meetings	Board Risk Committee Meetings	Nomination & Remuneration Committee Meetings
1	Mr Mansour Al Bosaily	4	-	-	4	7
2	Mr Majed Najm	4	6	-	-	-
3	Mr David Dew	4	6	-	-	1
4	Mr Georges Elhedery	4	4	-	4	6
5	Mr Sridhar Chandrasekharan	-	-	-	-	-
6	Mr Hamad Al Omar	4	-	-	4	-
7	Mr Mohammad Alshayea	4	-	5	-	-
8	Mr Abdulatif Al Seif	4	-	-	-	6
9	Mr Fahad Al Saif	1	-	-	1	-
10	Mr Mohammad Al Tuwaijri	1	-	-	-	-

Dates of the Board Meetings and Attendance:

No.	Date of Meeting	Number of Attendees	Percentage Attendance
1	30 March 2016	9	100%
2	28 June 2016	7 <sup>1</sup>	100%
3	19 October 2016	7	100%
4	14 December 2016	8 <sup>2</sup>	100%

Dates of the Audit Committee Meetings and Attendance:

No.	Date of Meeting	Number of Attendees	Percentage Attendance
1	6 March 2016	3	75%
2	27 March 2016	4	100%
3	26 June 2016	4	100%
4	18 October 2016	3 <sup>3</sup>	100%
5	13 December 2016	3	100%

<sup>1</sup> It should be noted that a Board member resigned on 08 May 2016 and another on 25 May 2016, hence the total strength of the Board dropped to 7 members.

<sup>2</sup> It should be noted that a new Board member was appointed on 31 October 2016, hence the total strength of the Board was increased to 8 members.

<sup>3</sup> It should be noted that a non-board member of Audit Committee resigned on 22 September 2016, hence the total strength of the Audit Committee dropped to 3 members.

**Directors' Report** (continued)**Board of Directors** (continued)

Dates of the Nomination & Remuneration Committee Meetings and Attendance:

<i>No.</i>	<i>Date of Meeting</i>	<i>Number of Attendees</i>	<i>Percentage Attendance</i>
1	4 March 2016	4 <sup>4</sup>	100%
2	10 March 2016	2 <sup>5</sup>	100%
3	4 September 2016	4	100%
4	19 October 2016	4	100%
5	25 October 2016	4	100%
6	5 December 2016	4	100%
7	14 December 2016	4	100%

Dates of EXCOM Meetings and Attendance:

<i>No.</i>	<i>Date of Meeting</i>	<i>Number of Attendees</i>	<i>Percentage Attendance</i>
1	10 January 2016	2 <sup>6</sup>	100%
2	30 March 2016	3 <sup>7</sup>	100%
3	4 May 2016	3	100%
4	24 May 2016	3	100%
5	29 August 2016	3	100%
6	27 November 2016	3	100%

Dates of the Board Risk Committee Meetings and Attendance:

<i>No.</i>	<i>Date of Meeting</i>	<i>Number of Attendees</i>	<i>Percentage Attendance</i>
1	28 March 2016	6	100%
2	27 June 2016	4 <sup>8</sup>	100%
3	18 October 2016	5 <sup>9</sup>	100%
4	13 December 2016	5	100%

<sup>4</sup> It should be noted that REMCOM terms of reference were amended to increase total strength of REMCOM to 4 members.

<sup>5</sup> It should be noted that a REMCOM member resigned in 22 December 2015, hence the total strength of REMCOM membership dropped to 2 members.

<sup>6</sup> It should be noted that due to resignation of an EXCOM member, the total strength of EXCOM membership dropped to 2 members.

<sup>7</sup> It should be noted that new EXCOM member was appointed on 10 March 2016, hence the total strength of EXCOM membership increased from 2 to 3 members.

<sup>8</sup> It should be noted that a Board Risk Committee member resigned on 3 May 2016 and another one on 25 May 2016, hence the total strength of Board Risk Committee dropped from 6 to 4 members.

<sup>9</sup> It should be noted that a new Board Risk Committee member was appointed on 18 August 2016, hence the total strength of Board Risk Committee members increased from 4 to 5 members.

## **Audit Committee**

---

HSBC SA's Audit Committee was formed in 2011 reporting directly to the Board of Directors, and meets minimum four times during the year. The Audit Committee shall consist of at least three members including Non-Executive or Independent Board Members, and non-board members.

The Committee monitors the Company's internal and external audit functions and reviews control & compliance weaknesses and system deficiencies. It is also responsible for ensuring that all financial information is of the highest quality, concentrating on critical business issues, which enable the Company's external auditors and management to focus on those areas of greatest risk to the business.

The Audit Committee during 2016 comprised of the following members:

1. Mr Mohammad Alshayea, (Chairman)
2. Mr Hussain Al-Yami, (Member from outside the Board)
3. Mr James Madsen, (Member from outside the Board)
4. Mr Mark G. Prothero (Member from outside the Board) (resigned on 22 September 2016)

## **Nomination and Remuneration Committee**

---

The Nomination and Remuneration Committee was formed by the Board on 19 July 2011, and meets at least once during the year. The committee consists of three to five members appointed by the Board and reports directly to the Board.

The Committee recommends to the Board of Directors nominations for Board membership, annually reviews the skills and capabilities required of those suitable for Board membership, including the time needed by a Board member for Board business, reviews the structure of the Board and submits the necessary recommendations.

The REMCOM during 2016 comprised of the following members:

1. Mr Abdulatif Al Seif, (Chairman)
2. Mr Mansour Al Bosaily, (Member)
3. Mr Goerges Elhedery, (Member)
4. Mr Ahmed AlSudais, (Member from outside the Board)

## **Executive Committee**

---

The Executive Committee ("EXCOM") is appointed by the Board and reports directly to the Board. The committee consists of the Company's CEO (Chairman) and two other Board Members.

The main task of EXCOM is to assist the Company's CEO, within the authorities entrusted to CEO by the Board, and in handling the matters referred to CEO by the Board. In addition, EXCOM review, inter alia, Business Performance Reports, Financial Markets Reports, Investment Banking Report, Monitoring of AOP Progress Reports and Human Resources Reports etc. and meets six times during the year.

The EXCOM during 2016 comprised of the following members:

1. Mr Majed Najm, (Chairman)
2. Mr David Dew, (Member)
3. Mr Georges Elhedery, (Member) (effective from 15 March 2016)

## Directors' Report (continued)

### Board Risk Committee

---

The Board Risk Committee ("BRC") was formed by the Board to handle risk management affairs. As per its terms of reference, the BRC consists of not less than 3 members including at least one Non-Executive Independent Board Member, and non-board member and reports directly to the Board.

The BRC meets four times a year and supervises and gives advice to the Board on all matters relating to high level risks pertinent to the Company's business in addition to strategic direction of risks across the Company including the drawing up of a risk vision, prioritization and supervision of principal initiatives and overseeing the execution of major transformational risk initiatives.

The BRC during 2016 comprised of the following members:

1. Mr Georges Elhedery (Chairman) (with effect from 15 March 2016)
2. Mr Mansour AlBosaily (Member)
3. Mr Hamad Al Omar (Member)
4. Mr James Madsen (Member from outside the Board)
5. Mr Richard Hinchley (Member from outside the Board) (with effect from 18 August 2016)
6. Mr David Kenney (Member from outside the Board) (resigned with effect from 3 May 2016)
7. Fahad Al Saif (Member) (resigned with effect from 25 May 2016)

### Risk Management

---

The Board of Directors are responsible for the overall risk management approach with HSBC SA and for reviewing its effectiveness.

The Board's designated committee for risk matters is the Board Risk Committee which approves and provides oversight for the Company's risk framework, plans and performance targets which include the establishment of risk appetite statements, risk management strategies, the appointment of senior officers, the delegation of authorities for credit and other risks and the establishment of effective control procedures.

The Chief Risk Officer (CRO) is responsible for managing the risks within the Company. In addition there is a separate Head of Compliance both report directly to the CEO. Their key functions are:

#### Chief Risk Officer:

- Risk Management
- Operational Risk
- Security and Fraud Risk
- HSBC SA Standards

#### Compliance:

- Financial Crime Compliance
- Regulatory Compliance

The Company's strategy, processes and policies are documented with regular reporting through Key Risk Indicator (KRI's) and Limits and escalation to Management and Governance Committees.

The Company operates a three lines of defense model to manage the risk within the business and monitor the effectiveness of controls.

- First Line – management responsibility is with the business and control functions for the risks they are managing – supplemented by Business Risk Control Managers.
- Second Line – Risk stewards and oversight of first line.
- Third Line – Independent Audit Function.

Through the ICAAP process the Board reviews the risks of the Company against the Capital availability. On an ongoing basis the risk profile of the Company is reviewed against the Risk Appetite Statement and also the ICAAP exposures to ensure that the risks remain appropriate.

## Annual Review of the Effectiveness of Internal Control Procedures

---

HSBC SA's management is responsible for implementing and reviewing the effectiveness of the Company's internal control framework as approved by the Board of Directors.

HSBC SA has established clear standards that should be met by employees, departments and the Company as a whole. Systems and procedures are in place within HSBC SA to identify any deviations in control and report on major risks including credit, changes in the market prices of financial instruments, liquidity, operational error, breaches of law or regulations, unauthorised activities and fraud. In addition to an on-going management review, exposure to these risks is subject to monitoring through various management committees that were established to ensure the effectiveness of the Company's control framework and to maintain specific oversight of key risks such as credit, operational, compliance and fraud.

Periodically, strategic plans are prepared for the Company and these are implemented and monitored through annual operating plans that are prepared and adopted by all business and support functions and that set out the key business initiatives and their likely financial effects.

Centralised functional control is exercised over all computer system developments and operations. Common systems are employed for similar business processes wherever practicable.

In addition, management is responsible for setting policies, procedures and standards across all areas of risk, including credit, market, liquidity, operational, IT, accounting, information, legal and regulatory compliance, human resources, reputational and purchasing risks. These policies are subject to ongoing review and are benchmarked to best practice.

The Risk Management function serves as a secondary control maintaining oversight of Credit, Market and Operational risks, as well as other functions such as security and fraud risks. The Compliance function maintains oversight of business operations and management action to ensure conformity with regulatory requirements. The risk management process is fully integrated with the strategic planning, annual operating plan and capital planning cycle. Furthermore, each employee is expected to be accountable for and to manage the risk within his or her assigned responsibilities based on the governance principles adopted by the Company and addressed during training programs.

The systems and procedures for the ongoing identification, evaluation and management of the significant risks faced by HSBC SA were in place throughout the year. These procedures enabled HSBC SA to discharge its obligations under the rules and regulations issued by CMA, the Capital Market Authority.

Operational Risk together with the Risk Management and Compliance functions, forms an integral part of the control environment of HSBC SA. Positioned as an independent control, Operational Risk provides management and, through the Board Risk Committee, Audit Committee and Board, with an independent and objective assessment on whether the framework of risk management, control and governance processes, as designed and represented by management, is adequate and functioning effectively.

Operational Risk accomplishes this by independently reviewing, through a risk-based approach, the design effectiveness and operating efficiency of internal control systems and policies prepared and implemented by business management. Operational Risk also reviews and reports on the adequacy and effectiveness of oversight maintained by support functions such as compliance and risk management departments, to ensure that the Company is operating within its stated risk appetite and in compliance with the regulatory framework.

A dedicated audit team within HSBC SA acts as a third line of defence through reviewing the business and control functions within the Company against local regulations and international best practices. The audit team is independent and reports directly into the Chairman of the Audit committee.

## Directors' Report (continued)

---

### Credit Risk

---

The Company manages exposure to credit risk, which is the risk that one party to a financial instrument will fail to discharge an obligation and cause the other party to incur a financial loss. Credit exposure within HSBC SA principally is from a fiduciary perspective within the Asset Management Business, investment of the Company's capital and on credit commitments associated with the Companies Brokerage.

The Company attempts to control credit risk by monitoring credit exposures, limit transactions with specific counterparties and continually assessing the creditworthiness of counterparties. The Companies risk management policies are designed to identify and set appropriate risk limits and to monitor the risks and adherence to limits.

### Market Risk

---

Market Risk is the risk that the fair value of financial instruments will fluctuate due to changes in market variables such as special commission rates, foreign exchange rates and equity prices. The company classifies exposures to market risk into either trading or non-trading books.

The market risk taken by HSBC SA is limited and is operating under approved market risk limits.

### Market Risk Trading Book

---

The board has set limits for the acceptable level of risks in managing the trading book. Nominal limits have been established covering the product and the daily and monthly Mark to Market Loss referral limits.

Within the trading limits the Board has authorized Equity Underwriting limits to cover IPO's and Rights issues with nominal limits. The nature of the Saudi Market currently is focused on soft underwriting where the Company is not exposed to Equity price risk, although certain transactions (rights issuance) can have hard underwriting limits where the Company would be exposed.

### Market Risk Non Trading Book

---

The Company has deployed its surplus capital in the Company's Asset Management Funds which provided exposure to Saudi and International Money Market and Fixed Income investments resulting in special commission and FX exposure. These operate under nominal limits approved by the Board including MTM Referral Limits.

### Liquidity Risk

---

Liquidity risk is the risk that the Company is unable to meet its payment obligations when they fall due under normal and stress circumstances. Given the nature of HSBC SA activities (ie generally not direct lending) this risk is mitigated via deploying the Companies' surplus capital in Mutual Fund investments. The liquidity risk of Asset Management is covered within the fiduciary risk.

### Fiduciary Risk

---

The risk to HSBC SA of breaching its fiduciary duties where it acts in a fiduciary capacity as Trustee, Investment Manager, Broker (for cash balances maintained at SABB) as mandated by law or regulation. Within HSBC SA this risk is mainly within the Asset Management business where we are investing in funds on behalf of clients.

The risk within Asset Management is primarily managed by the business, with additional limits and controls established with the individual fund prospectus or client mandate – these limits are independently monitored by Risk.



## **Compliance Risk**

---

The risk to HSBC SA in breaching Local Regulatory and International Best Standards in regard to Financial Crime Compliance and Regulatory Compliance. Within HSBC SA this risks exists throughout all areas of the Company.

The risks is primarily managed by the business and through an independent compliance function responsible for providing guidance and independent control and review of the compliance risks within the company.

## **Business Performance**

---

### **Investment Banking**

HSBC SA is the market leader in M&A and IPOs and has consistently maintained its top league-table position throughout 2016, as was the situation in previous years. During 2016, HSBC SA significantly expanded its Investment Banking Advisory capabilities in order to address existing and rapidly growing private and public client demand in the Kingdom. HSBC SA successfully closed two transactions in the Kingdom those being the SAR 600m rights issue of Takween Advanced Industries and the M&A buy-side advisory on behalf of AlTayyar Travel Group in the acquisition of a 30% stake in Thakher by way of issuance of shares. HSBC SA's accomplishments were recognised through multiple awards, including "Best Investment Bank in the Middle East" by Euromoney (wherein the accomplishments of the Saudi franchise played a strong part and found mention in the award statement), and "Best Foreign Investment Bank in Saudi Arabia" by EMEA Finance.

### **Debt Capital Markets and Syndicated Finance**

Debt Capital Markets and Syndicated Finance transactions in 2016 included the inaugural USD 17.5bn triple-tranche Eurobond issuance by the Kingdom where HSBC acted as Joint Global Coordinator, Joint Book runner and Joint Lead Manager; and the debut Sukuk issuance by Bank AlBilad where HSBC SA acted as Joint Lead Manager and Book runner. Deal specific awards in which HSBC SA played a lead role in 2016 included "MENA Deal of the Year" from Trade Finance Awards for the Saudi Aramco USD 10 billion Standby Revolving Credit Facilities for which HSBC was a Global Coordinator.

### **Project and Export Finance**

Key achievements in Project and Export Finance in 2016 included the successful closing of the landmark King Abdullah Port transaction, the first private sector port in the Kingdom. Deal specific awards in which HSBC SA played a lead role included "Best Water Deal in MENA" from IJ Global for the King Khaled International Airport Potable Water and District Cooling projects; and "Best Petrochemicals Deal in MENA", also from IJ Global for the Jazan Air Separation Unit.

### **Asset Management**

The Asset Management business of HSBC SA received the following awards in 2016: "Saudi Asset Manager of the year" award from MENA Fund Manager, "Equities Manager of the year" award from Global ISF and the "Best one year performance" awards for the HSBC GCC equity fund and the HSBC Financial Institution fund from Lipper.

### **Equity Brokerage**

The Equity Brokerage business restructured its Brokerage services by establishing independent Equity sales and execution platforms to better support both Institutional and Retail customer needs. HSBC SA also expanded its foot print by opening two new investment centres thereby increasing its network from ten to twelve. At 31st December 2016 HSBC SA was undertaking significant infrastructure changes to its core brokerage systems to further improve its client offering.

### **Securities Services**

HSBC SA continued its market leadership in the QFI space and maintained its leading position in terms of assets under custody for QFIs. During 2016, its Securities Services business successfully secured a custody and administration mandate from a large asset manager in Saudi Arabia with assets under management in excess of SAR 3 billion.