

بِسْمِ اللَّهِ الرَّحْمَنِ الرَّحِيمِ

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Directors' Report

The Board of Directors (the "Board") is pleased to submit to shareholders the Annual Report of HSBC Saudi Arabia ("HSBC SA") for the financial year ended 31st December 2018. The financial statements, for the year ended 31 December 2018 have been prepared in accordance with the International Financial Reporting Standards ("IFRS"). For years up to and including the year ended 31 December 2017, the Company prepared its financial statements in accordance with SOCPA Standards.

1. Principal activities

HSBC Saudi Arabia is a Closed Joint Stock Company registered in the Kingdom of Saudi Arabia under Commercial Registration No. 1010221555 dated 27/06/1427H (corresponding to 23/07/2006G), 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.

The main activities of the Company are to provide a full range of investment banking services including investment banking advisory, debt capital market and syndicated finance advisory and project and export finance advisory and custody and funds securities services. It also manages mutual funds and discretionary portfolios, and provides brokerage services including margin lending conventional and Shariah compliant overdraft facility for customers to trade in the capital market. The Company serves a wide range of clients including but not limited to corporates, financial institutions, non-bank financial institutions and individuals.

On 01 Rajab 1438H corresponding to 28 March 2017, the Company was converted from a Limited Liability Company to a Closed Joint Stock Company under Royal Decree number M/3 dated 28/01/1437H. All the assets and liabilities of the Limited Liability Company were brought forward to the Closed Joint Stock Company.

Investment Banking Advisory

HSBC SA continues to be one of the leading investment banking platforms in the Kingdom, active across the entire advisory product offering. During 2018, HSBC SA demonstrated the breadth of its M&A offering in a number of industries, having advised the Public Investment Fund (PIF) on an M&A buy side role in its high profile acquisition of a stake in ACWA Power (closed), advised SABIC on its cross-border acquisition of a 25% stake in Clariant (closed), continued to advise Saudi International Petrochemical Company (Sipchem) on its merger with Sahara Petrochemicals Company as the first public merger under the Exchange of Securities Offer (signed) and launched qualification for the Kingdom's first privatization sale process - Saudi Grains Organization (SAGO). On the Equity Capital Markets front, and to add to its leading position in recent years, HSBC SA continued to advance preparation of several issuers for upcoming landmark offerings. In addition, HSBC continued to successfully expand its pipeline of activity, including, as announced, being mandated to act as financial advisor, lead underwriter and bookrunner to Ataa Educational Company on its contemplated IPO on Tadawul.

Debt Capital Markets and Syndicated Finance

HSBC's Debt Capital Markets business further strengthened its market leadership position in Saudi Arabia by maintaining #1 DCM house position in 2018, for a record 8th year in a row. During the year HSBC acted as joint lead manager and bookrunner on an aggregate primary bond supply of around USD 19 billion, for key clients including the Kingdom of Saudi Arabia, SABIC, SEC, and APICORP. HSBC is the only bank to have now acted as an active joint lead manager and bookrunner on all of the KSA's international DCM issuances to date.

On the local front, HSBC acted as a sole arranger and dealer on the establishment of Saudi Real Estate Refinance Company's inaugural SAR 11 billion Saudi-riyal denominated Sukuk Programme, which will act as a catalyst for establishing a fixed rate mortgage market in line with the Kingdom's housing initiatives and Vision 2030 plans. HSBC also acted as a joint lead manager and joint bookrunner on SAR3.5 billion Ma'aden Phosphate Company's debut 7-year Sukuk issuance, which represented the first private sector SAR Sukuk issuance of the year. Within the Syndicated Finance space, HSBC acted as MLA and bookrunner on a number of landmark international bank financings including USD16 billion for KSA, USD11 billion for PIF and USD 2.65 billion for SEC. In the SAR bank market, HSBC through SABB arranged syndicated financings totalling SAR 16.5 billion. HSBC won "Deal of the Year" from The Banker for the Kingdom's USD 9.0 billion dual-tranche 5 and 10-year Sukuk issuance; "Best Refinancing in the Middle East" from EMEA Finance for Mobily's SAR 8 billion refinancing; and "Best Restructuring in the Middle East" for Tasnee's SAR 2.9 billion syndicated Islamic loan facility.

Project and Export Finance

One of the key achievements in Project and Export Finance in 2018 included the successful structuring and arrangement of USD 1.1 billion Shariah compliant financing for Farabi's Integrated Petrochemicals Complex at Yanbu Industrial City. HSBC acted as the financial advisor, mandated lead arranger (through our affiliate SABB), inter-creditor agent, facility agent, onshore security trustee and offshore security trustee.

Asset Management

HSBC SA asset management continued to maintain its strong position during the year in managing local equity mandates for institutional as well as retail and private banking clients. HSBC SA has an eminent position in terms of product offering with a product suite of 19 public funds and a private real estate fund. HSBC SA is also one of the only two Authorised Persons in Saudi Arabia offering an Exchange Traded Fund that is listed on the Saudi Stock Exchange. The business continued to maintain its top position in local equity mutual funds with c.20% market share and delivered strong performance in 2018 across all asset classes. Notably, HSBC Financial Institutions Fund (FIF) was the best performing fund of the year with a YTD return of 31%, HSBC Saudi Freestyle Equity Fund was ranked 1st in the unconstrained (freestyle category), HSBC Saudi Equity Fund (SEF) was ranked 2nd in the conventional balanced peer group of conventional equity strategy, HSBC Saudi Companies Equity Fund (ASF) ranked in the 1st quartile was in the top quartile among the Shariah complaint equity strategy, and HSBC Saudi Equity Income Fund (SSF) was ranked 1st amongst its peers in the Saudi dividend category. HSBC SA won The Saudi Asset Manager of the Year award from MENA Fund Manager in addition to winning another award from Argaam for HSBC Financial Institutions Fund for Top Performing Saudi Equity Fund 2018 for 1 year and 3 year performance. HSBC SA also continued to broaden its product offering to meet client demand and launched a new Shariah compliant Murabaha Fund as a private fund.

Brokerage Services

HSBC SA operates a sizable institutional and retail brokerage business, and during 2018 maintained its status as the leading brokerage house by market share as compared to all its internationally-linked peers operating in Saudi Arabia. The brokerage division offers a comprehensive range of trading services to both retail and institutional investors (domestic and foreign). The brokerage services are seamlessly delivered through multiple channels that include 12 Investment Centers, On-line channels such as HSBC Tadawul and HSBC Mubasher, online platforms to facilitate KYC and onboarding processes, centralized Call Centre and dedicated market access channels for its institutional clients. The business is ably supported by research capabilities providing timely and comprehensive sector and company research. In addition, the company offers to its customer's margin lending overdraft facility to trade in the local capital market.

Securities Services

HSBC SA is a leading custodian in the market, offering custody and administration services to local and foreign institutional investors. HSBC SA played a pivotal role in facilitating foreign institutions obtain Qualified Foreign Investor (QFI) status and is a market leader with QFI assets of over USD 6 billion whilst the overall assets under custody have crossed the USD 100b mark. The business is well positioned for servicing the incremental volumes envisaged post the inclusion in the MSCI and FTSE EM indices expected in various phases during 2019. HSBC SA was recognised as "Best sub-custodian in Saudi Arabia", by 'The Asset' magazine and 'Global Finance'

Margin Lending

HSBC SA offers margin lending facilities both conventional and Sharia compliant products to its customers to trade in the Saudi stock exchange (Tadawul) local equities. It is a fully secured overdraft facility collateralised against equity securities purchased by the borrowers using these funds. The facilities are reviewed at least on an annual basis. During the year, the company increased its margin lending portfolio by around 14% to SAR 814.9m from SAR 716.1m last year.

Directors' Report (continued)

2. Strategic Focus

HSBC SA's vision is to be the best investment banking services provider in the Kingdom, focusing on the needs of its customers and contributing to the success of Vision 2030, thereby delivering long-term sustainable value to all its stakeholders. To achieve the mission, HSBC SA will continue to focus on the following key strategic objectives;

- Offer seamless customer experience and treat our customers fairly;
- Simplify the organisation and enhance customer service capabilities;
- Expand product capabilities and gain market share with new offering targeting retail and Institutional clients;
- Leverage from potential growth from Inclusion to MSCI and FTSE EM in 2019;
- Embark on digitalization and technology initiatives;
- Contribute to the success of the Saudi Vision 2030;
- Maintain continued market leadership in Investment Banking and Securities Services;
- Grow and compete for leadership in Institutional Brokerage;
- Attract, retain and grow talent.

People

People are core to the success of HSBC SA's strategy to build 'The Best Place to Work' Accordingly HSBC SA has built a leading employer brand in the market to attract, engage, develop and retain talent. Our talent pursues customer satisfaction, constantly innovates product solutions, lives the strong risk management culture along with driving alignment with our values of being Open, Dependable, Connected and Working together aspiring for HSBC SA to be the Leading Investment banking services provider in the Kingdom. Accordingly HSBC SA has built a leading employer brand in the market to attract, engage, develop and retain talent, which is built on management ethos towards prioritizing People, an internationally-connected professional environment, top class training and career development structure. Developing the Saudi workforce has continued to be a priority representing around 80%, including diversity agenda with Saudi women representing around 24% of the work force.

During the year, HSBC SA successfully implemented a number of programs, notably Global graduate Training Program that includes training and opportunity to work with experts in the HSBC Group, Youth for Saudi program's run in partnership with HSBC giving opportunity to work with specialized experts in HSBC for period of 18 months in the United Arab Emirates, United Kingdom and Hong Kong. In addition, HSBC SA offers JODP programs, short term intern placements for university students with overall objective to identify, train and develop the best in class Saudi talent and support KSA vision 2030

HSBC SA Human Resources function (HR) reports directly to the CEO and regularly reports to the Board nominated committees on the direction, initiatives and success of HSBC SA's People Strategy. HR governs all policies and procedures related to the recruiting, training, career development, performance assessment, succession planning and reward of HSBC SA employees.

A career with HSBC SA offers the opportunity to enhance performance, experience and skills sets through its international connectivity with HSBC group and that forms a leading global career proposition in the Kingdom. All HSBC SA employees are eligible to apply and undertake development assignments across the HSBC group along with having the opportunity to network with HSBC colleagues around the world to benchmark processes and initiatives in many fields such as customer service, technological solutions, risk management practices, capability enhancement and people management.

Strategic Focus *(continued)*

3. Best in Class: Industry Awards

HSBC SA received recognition in 2018 as follows:

- “Best Investment Bank in Saudi Arabia” by Euromoney
- “Best Foreign Investment Bank in Saudi Arabia” by EMEA
- “Best sub-custodian in Saudi Arabia” by The Asset magazine
- “Best sub-custodian in Saudi Arabia” by Global Finance
- “Saudi Asset Manager for 2018” by MENA FM Performance Awards

4. Corporate social responsibility

In line with its core values, HSBC SA remains committed to the community where it operates. Within this framework, HSBC SA is making efforts to serve the community by providing a range of activities that serve and benefit the various community groups in Saudi Arabia that stand in need of support and assistance. HSBC SA is making all efforts to promote a social responsibility culture and instill the spirit of volunteer activities by involving HSBC SA staff members.

During 2018, HSBC SA successfully conducted and organised a number of CSR activities, including a blood drive donation with King Faisal Hospital, winter cloths bags that were given to families in need during the winter, Ramadan food gift basket where staff participated in distributing these baskets to families in need. In addition, the awareness campaigns were run on breast cancer, diabetes and No smoking day awareness.

5. Financial results and Segment performance highlights

Key financial highlights

Saudi Riyal (millions)	2018	2017**	2016	2015	2014
Shareholder’s Equity	780	775	765	865	785
Investments, Net	181	242	615	1,029	902
Loans and Advances*	814	716	-	-	-
Total Assets	1,350	1,177	1,028	1,168	1,148
Total Liabilities	569	401	262	302	363
Net Income**	145	150	140	279	229
Gross Dividend	112	104	211	157	192

*Relates to margin lending portfolio launched in 2017

** Net Income for the period 01 January 2017 to 31 December 2017 is as per IFRS restatement.

Net income

HSBC SA recorded a net income of SAR 145 million for the year 2018. HSBC SA’s total income for 2018 was SAR 409 million. In 2018, the company generated strong revenue growth in securities services mainly custody and fund services along with Institutional brokerage business. HSBC SA’s total operating expenses for 2018 were SAR 264 million which includes one off release of operational loss provision amounting to SAR 30.5 million.

Balance sheet

During the year, the company growth in balance sheet was mainly driven by increase in Margin lending portfolio balance that increased from SAR 716m to SAR 815m. The company increased its overall borrowing in the form of short term loans to SAR 325m compared to SAR 150m in 2017. During 2018, the company obtained a short term revolving loan facility from SABB amounting to SAR 275 million and a further SAR 50m short term loan facility from local bank. As part of its balance sheet management, the company liquidated part of its investment in units of Saudi Riyal Trading Fund and further invested SAR 70m as seed capital in the new Enhanced Murabaha Private fund. The end of services balances are based on the actuary valuation carried out by an independent consultant.

HSBC SA generates its operating income from activities in the Kingdom of Saudi Arabia and has no branches, subsidiaries or associates established or operating outside the Kingdom of Saudi Arabia. The company’s performance by business segments is summarized in the below table.

Directors' Report (continued)

SAR' 000	<i>Advisory Services</i>	<i>Brokerage</i>	<i>Asset Management</i>	<i>Securities Services</i>	<i>Margin Lending</i>	<i>Others</i>	<i>Total</i>
Revenue	67,672	85,843	99,430	114,425	39,186	2,667	409,223
Expenses	80,140	84,687	71,907	47,832	10,029	(30,585)	264,010

Related Party Balances and Transactions

Related parties of the Company comprise of group companies including its affiliates and brokers and its shareholders. 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.

	Notes	As at 31/12/2018
Due from related parties		
Receivable from SABB	1	5,256,300
Receivable from affiliates	2	8,948,500
		<u>14,204,800</u>
Due to related parties		
Payable to SABB	3	6,942,453
Payable to affiliates	4	20,375,433
		<u>27,317,886</u>

Notes:

- 1 This mainly represents receivable on account of advisory services and net balance on intercompany transactions with SABB.
- 2 This mainly represents receivable from an HSBC entity on account of commission earned from equity swap arrangements with foreign counter parties pursuant to Capital Market Authority (CMA) circular dated 21 August 2008, as explained in note 17.
- 3 This mainly represents payable to SABB for DPM profit sharing.
- 4 This mainly consists of payable to HSBC entities.

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

Transaction with	Income Statement	For the year end 31/12/2018
The Saudi British Bank (SABB)	Services cost under service level agreement-net	<u>22,499,616</u>
	Arranging/advisory income under service level agreement	<u>9,858,250</u>
	Income from Time deposit	<u>167,215</u>
	Special commission income on deposit	<u>42,279,427</u>
	Fees paid for discretionary portfolios service and mutual funds	<u>6,024,877</u>
	Special commission expense on short term loan facility	<u>9,877,638</u>
	HSBC Saudi Arabia Mutual Funds (“the Mutual Funds”)	Brokerage income, net
	Asset management fee from funds	<u>69,983,351</u>
	Realized gain on sale of investments – FVTPL	<u>2,188,518</u>
HSBC entities	Brokerage income on equity swaps	<u>18,016,088</u>
	Service cost under service level agreement	<u>6,654,674</u>
	Arranging/advisory income under service level agreement	<u>3,093,750</u>
Directors remuneration & Committee members Fee		<u>1,394,000</u>
Key management compensation	Salaries & compensations	<u>7,680,628</u>
	Allowances	<u>3,344,016</u>
	Periodic and annual remuneration	<u>9,680,000</u>

Short Term Loans

	Notes	2018
Short-term from SABB and other local bank	1	325,000,000
Accrued commission expense	2	1,215,177
Total		<u>326,215,177</u>

- 1 This represents short-term loan from SABB and other local commercial bank carrying a commission rate at agreed commercial rate. This facility arrangement includes certain covenants, which the Company was in compliance with during the year ended 31 December 2018.
- 2 This represents accrued commission expense on short-term loans on based of spread over 3 months SAIBOR.

Directors' Report (continued)

6. 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 and the Head of Compliance is responsible for regulatory and Financial Crime compliance. The CRO and Head of Compliance report to the CEO and operate under the guidance and supervision of the Board Risk Committee and Audit Committee respectively. Their key functions are:

Chief Risk Officer:

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

Compliance

- Regulatory Compliance
- Financial Crime 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)

Risk Management (continued)

Credit Risk

Credit risk 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 risk exposure within the company principally is receivables from advisory services rendered, margin lending, cash with Banks, and Investments in HSBC Funds.

The Company manages its credit risk by monitoring credit exposures, establishing limits for transactions with specific counterparties and continually assessing the creditworthiness of counterparties. The Company's risk management policies are designed to identify and set appropriate risk limits and to monitor the risks and adherence to limits on a continuous basis.

Concentrations of credit risk arises when a number of counterparties are engaged in similar business activities, related group of counterparties, or have similar economic features that would cause their ability to meet contractual obligations to be similarly affected by changes in economic, political or other conditions. Concentrations of credit risk indicate the relative sensitivity of company's performance to developments affecting these counterparties.

The Company seeks to mitigate its overall credit risk exposure through sound risk strategies, establish credit limits, segment diversification and ensures there are sound internal control.

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. Daily forward looking liquidity monitoring and assessment is in place. Stress tests are also undertaken on liquidity. Liquidity needs are funded by a mixture of own capital, and wholesale bank funding. Excess liquidity is invested 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.

Risk Management *(continued)*

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 are 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.

Cyber Security Risk

Cyber security risk is a subset of information security and HSBC continues to strengthen and significantly invest in our ability to prevent, detect and respond to the ever-increasing and sophisticated threat of cyber-attacks.

Shariah Risk

Shariah Risk is the risk of financial loss, regulatory sanction and/or reputational damage to the Company as a result of failure to comply with the directions, guidelines and conditions issued by relevant Shariah Committees and/or relevant regulators in respect of the development, execution, delivery and marketing of Shariah Compliant Products. Shariah Risk also includes failure to comply with any conditions of approval/interpretations/directions provided by the relevant Shariah Function in respect of any Shariah Compliant Products or processes.

Directors' Report (continued)**7. Legal Entity Structure**

The share capital of the Company was SAR 500 million divided into 10,000 shares of SAR 50,000 each. The shareholders and their respective holdings were as follows:

	Number of shares	% of contribution	As at 28 March 2017
HSBC Asia Holdings BV	4,900	49%	245,000,000
The Saudi British Bank ('SABB')	5,100	51%	255,000,000
Total	10,000	100%	500,000,000

On 29 March 2017, the legal formalities in respect of the incorporation were completed and the Company obtained its revised commercial registration certificate. The share capital of the Company was split from 10,000 shares of SAR 50,000 each into 50 million shares of SAR 10 each. The revised shareholding is as follows:

	Number of shares	% of contribution	As at 31 December 2017
HSBC Asia Holdings BV	24,500,000	49%	245,000,000
The Saudi British Bank ('SABB')	25,497,000	50.994%	254,970,000
Arabian Real Estate Company Limited	1,000	0.002%	10,000
SABB Insurance Agency Limited	1,000	0.002%	10,000
SABB Real Estate	1,000	0.002%	10,000
Total	50,000,000	100%	500,000,000

8. Corporate Governance**Corporate governance principles**

HSBC SA is aware of the positive impact associated with the adoption of prudent Corporate Governance Principles and Standards and that such adoption will lead to observance of professional and ethical standards in the company's dealings as well as transparency and disclosure which will contribute to the furthering and improvement of its efficiency and relations with all interested parties. It is also believed that the adoption of this approach will enhance investors' confidence both in the HSBC SA and in the Saudi Securities Business in the Kingdom.

HSBC SA's Bylaws and the HSBC SA Governance Document, provide for disclosure policies and procedures, formation of the Board and Sub-committees, responsibilities of the Board of Directors, policy regulating relationships with stakeholders, shareholders' rights and attendance of meetings.

Corporate Governance *(continued)*

Board of Directors

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

- Three (3) Directors shall be appointed and removed by HSBC;
- Three (3) Directors shall be appointed and removed by SABB; and
- Three (3) Directors shall be Independent Directors and shall be appointed and removed with the unanimous consent of both SABB and HSBC.
- The current Board was elected on 16 February 2017 for a term of three years.

Profile of the Board of Directors as at 31 December 2018 comprised of the following:

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

Board Member, Saudi Ground Services Company
Board Member, Saudi Reinsurance Company
Board Member, Amlak International 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 (EFFECTIVE FROM 1ST JANUARY 2015)
NIL

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

Board Member, The Saudi British Bank
Board Member, HSBC Bank Middle East

Mr Georges Elhedery, NON-EXECUTIVE, (EFFECTIVE FROM 15TH MARCH 2016)

Board Member, HSBC Bank Middle East Limited
Board Member, HSBC Bank Middle East Holdings BV
Board Member, HSBC Bank Egypt SAE
Board Member, HSBC (Turkey) Bank A.S.
Board Member, The Saudi British Bank

Mr Sridhar Chandrasekharan, NON-EXECUTIVE, BOARD MEMBER (EFFECTIVE FROM 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 (EFFECTIVE FROM 1ST JANUARY 2015)

NIL

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

Board Member, Saudi Ground Services Company
Board Member, NAJM for Insurance Services
Board Member, SABB Takaful (JSC)
Board Member, The General Authority for Competition

Mr. Naif Alabdulkareem, NON-EXECUTIVE, BOARD MEMBER (7 FEBRUARY 2018)

Board Member, SABB Takaful (JSC)
Board Member, Saudi Credit Bureau (SIMAH)

Board Members who resigned during 2018

Mr. Abdulatif Al seif, INDEPENDENT, BOARD MEMBER (RESIGNED WITH EFFECT FROM 29 MARCH 2018)

Board Member, Al Rajhi Bank

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

Number of Board & Committee meetings attended by each Director during 2018:

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

Dates of the Board Meetings and Attendance:

<i>No.</i>	<i>Date of Meeting</i>	<i>Number of Attendees</i>	<i>Percentage Attendance</i>
1	27 March 2018	9	100%
2	1 May 2018	8	100%
3	6 June 2018	6	75%
4	25 September 2018	7	87.5%
5	22 November 2018	8	100%

Board committees**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 reviews matters relating to financial reporting and the effectiveness of internal control and financial control systems. It also safeguards the independence of the company's internal audit function and oversees its performance as well as monitoring the effectiveness of the external auditor.

The Audit Committee during 2018 comprised of the following members:

- Mr. Mohammad Alshayea, (Chairman)
- Mr. Hussain Al-Yami, (Member from outside the Board)
- Mr. Mr. Rob Underwood, (Member from outside the Board)
- Mr. Sami AlMahaid, (Member from outside the Board)
- Ms. Sonali Goiporia, (Member from outside the Board)

<i>No.</i>	<i>Date of Meeting</i>	<i>Number of Attendees</i>	<i>Percentage Attendance</i>
1	7 March 2018	3	75%
2	4 June 2018	4	80%
3	9 September 2018	4	80%
4	20 November 2018	5	100%

Board committees *(continued)*

Nomination and Remuneration Committee

The Nomination and Remuneration Committee (“NRC”) 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 Committee sets the overarching principles, parameters and governance framework of the company’s remuneration policy and the remuneration of executive directors and other senior company employees. It regularly reviews the effectiveness of the remuneration policy in the context of effective risk management.

The NRC during 2018 comprised of the following members:

- Mr. Abdulatif Al Seif, (Chairman)
- Mr. Mansour Al Bosaily, (Member)
- Mr. Georges Elhedery, (Member)
- Mr. Ahmed AlSudais, (Member from outside the Board)
- Mr. Faisal Jadu, (Member from outside the Board)

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	15 March 2018	3	75%
2	10 September 2018	4	100%
3	22 November 2018	4	100%

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 reviews, inter alia, Business Performance Reports, Financial Markets Reports, business performance reports and analysis, progress against financial and strategic objectives, reviews business challenges and other key operational matters of the company.

The EXCOM during 2018 comprised of the following members:

- Mr. Majed Najm, (Chairman)
- Mr. David Dew, (Member)
- Mr. Georges Elhedery, (Member)

Dates of EXCOM Meetings and Attendance

<i>No.</i>	<i>Date of Meeting</i>	<i>Number of Attendees</i>	<i>Percentage Attendance</i>
1	2 February 2018	3	100%
2	26 April 2018	3	100%
3	3 June 2018	3	100%
4	2 August 2018	3	100%
5	28 October 2018	3	100%
6	20 November 2018	3	100%

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 undertakes oversight of enterprise risk management, risk governance and internal control systems (other than internal financial control systems). The BRC 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 and overseeing the execution of major transformational risk initiatives.

The BRC during 2018 comprised of the following members:

- Mr. Sridhar Chandrasekharan (Chairman)
- Mr. Mansour AlBosaily (Member)
- Mr. Hamad Al Omar (Member)
- Mr. Richard Hinchley (Member from outside the Board)
- Mr. Rob Underwood (Member from outside the Board)

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	8 March 2018	5	100%
2	5 June 2018	5	100%
3	10 September 2018	4	80%
4	22 October 2018	5	100%

Dividends

In accordance with the Company's Articles of Association, the Company's dividend distribution policy is in compliance with the provisions of the Company by laws. The annual net income of the Company is distributed as follows:

- 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.
- 10% of the net income is transferred to statutory reserves until this reserve equals 30% of the paid up share capital of the Company.
- 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.
- Un-distributed net income is carried forward as retained earnings.

Distribution of profits as per the Company's dividend distribution policy is as follows:

	<i>SAR '000s</i>
Net Income 2018	123,557
Retained earnings from the previous year	127,536
Total	251,093
Distributed as follows:	
Paid / Proposed Dividend, Net	112,692
Zakat and Income Tax	2,385
Retained earnings for 2018	136,016

Accounting Standards

The Company's financial statements for the year ended 31 December 2018 have been prepared in accordance with International Financial Reporting Standards ("IFRS"). The notes to the financial statements include reconciliations required under IFRS, First-time Adoption of International Financial Reporting Standards.

9. Statutory payments

Statutory payments payable by the company during 2018 consist of Zakat payable by Saudi shareholders, tax payable by the foreign partner, and the amounts payable to The General Organisation for Social Insurance (GOSI) which represents staff insurance contributions.

The statutory payments for the year 2018 were as follows:

	SAR '000
Zakat attributable to the Saudi Shareholders for 2017	990
Income tax attributable to non-Saudi shareholder for 2017	16,459
GOSI payments	12,255

10. Remuneration Report

Directors' fees for their membership of the Board and participation in the Company's operations, during 2018 amounted to SAR 1,394,000 including SAR 105,000 in attendance fees at Board meetings and Board Committees, namely: Executive Committee, Audit Committee, Nomination and Remuneration Committee and Board Risk Committee. The compensation is paid towards the end of the year.

During 2018, none of the board or committee members have assumed any work of technical or advisory role, and therefore they did not obtain any consideration or special benefits in this respect.

The following table shows details of remuneration paid to Board members and senior executives of HSBC SA during the year:

<i>2018 SAR' 000</i>	<i>Salaries and Remuneration</i>	<i>Allowances</i>	<i>Annual and Periodic Bonuses</i>	<i>Incentive Schemes</i>	<i>Any Remuneration or other benefits in kind paid monthly or annually</i>
Board of Directors	-	-	-	-	-
Executive Board Members	-	-	-	-	-
Non-Executive / Independent Board Members	-	-	-	-	1,394
Top senior executives (including CEO and CFO)	7,680	3,344	9,680	-	-

Directors' Report (continued)

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 2018 based on independent actuary valuation amounted to SAR 48.9 million.

11. Board of Directors Assurance

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

- Proper books of account have been maintained.
- The system of internal controls is sound in design and has been effectively implemented.
- It has no evidence that suggests the Company's inability to continue as a going concern.

12. Internal control

The Board is responsible for maintaining and reviewing the effectiveness of risk management and internal control systems, and for determining the aggregate level and types of risks the company is willing to take in achieving its strategic objectives. To meet this requirement, procedures have been designed to provide effective internal control; for safeguarding assets against unauthorised use or disposal; for maintaining proper accounting records; and for ensuring the reliability and usefulness of financial information used within the business or for publication. These procedures can only provide reasonable assurance against material mis-statement, errors, losses or fraud.

The key risk management and internal control procedures include the following:

- HSBC SA standards outlines the core principles within which the Company and its employees must operate in conducting its business.
- Delegation of authority within the limits set by the Board. The Chief Executive has been delegated authority limits and powers within which to manage the day-to-day affairs of the company.
- Risk identification and monitoring. Systems and procedures are in place to identify, assess, control and monitor the material risk types facing HSBC SA. Our risk measurement and reporting systems are designed to help ensure that risks are captured with all the attributes necessary to support well-founded decisions,
- Changes in market conditions/practices: processes are in place to identify new risks arising from changes in market conditions/practices or customer behaviours, which could expose HSBC SA to heightened risk of loss or reputational damage.
- Strategic plans: A business strategy for 2018 is in place. The strategy outlines the risk appetite of HSBC SA and sets out the key business initiatives and the likely financial effects of those initiatives.
- Responsibility for risk management: All employees are responsible for identifying and managing risk within the scope of their role as part of the three lines of defense model, which is an activity-based model to delineate management accountabilities and responsibilities for risk management and the control environment. Governance is in place to provide oversight of, and advice to the Board on material risk related matters effected through the Board sub-committees and management committees which oversee the effectiveness of risk management and report to the Board sub-committees.

HSBC SA's management is responsible for establishing and maintaining an adequate and effective framework of internal control which encompasses the policies as approved by the Board. HSBC SA's management has put in place an internal control framework to ensure compliance with applicable laws and regulations, internal policies with respect to conduct of business, maintenance of proper records and processes and quality of external and internal reporting.

HSBC SA has implemented a 'Three Lines of Defence' model for managing its risks. Business management, as the First Line of Defence, is responsible for setting policies, procedures and standards across all areas under their responsibility. Functional management is also responsible for implementing effective monitoring mechanisms to detect and prevent deviations or breaches from established policies and regulatory requirements.

The Second Line of Defence comprises various risk management and control functions which maintain oversight of credit, market, legal, compliance, information technology, financial control, reputational risks as well as other operational risks relating to business continuity, security and fraud. Risks are analysed qualitatively as well as by quantitative methods and reported to the Board and sub-committees through HSBC SA's management committees.

Internal Audit (INA) represents the independent ‘Third Line of Defence’ and reviews the design and operating effectiveness of the HSBC SA internal control framework and policies established by business and functional Risk Owners to provide independent and objective assurance that HSBC SA is operating within its stated risk appetite and in compliance with the regulatory framework. The Head of Internal Audit reports to the Audit Committee (AUCOM) on all audit related matters. The executive management is responsible for ensuring that Management Action Plans provided to the INA function are implemented within an appropriate and agreed timetable.

During 2018, INA conducted a number of reviews across HSBC SA in accordance with the approved Internal Audit Plan and identified certain weaknesses in the internal control framework. The Management is actively remediating these weaknesses in line with agreed action plans that include long term IT solutions. The Audit Committee actively monitors the adequacy and effectiveness of the internal control framework to provide reasonable assurance that all identified weaknesses are being remediated and that the internal control framework of HSBC SA remains effective.

13. Penalties

The Company applies in form and spirit all capital market laws, rules and regulations issued by the regulators in its day to day business. Through the establishment of three lines of defence it ensures that the application of regulations is robust and sustainable in the businesses and functions.

During 2018, HSBC SA was subject to penalties of SR 50,000 from the regulator for minor breaches which were subsequently addressed.

14. HSBC SA General Meetings

In 2018, the Annual General meeting of the company was held on 6th June 2018.

15. Appointment of external auditors

The Annual General Assembly meeting of HSBC SA was held on 6th June 2018, endorsed the selection of KPMG Al Fozan & Partners according to the recommendation of the Audit Committee, to audit HSBC SA’s annual financial statements and review quarterly interim financial statements for the year ended 31 December 2018 and the determination of their remuneration.

16. Board of Directors Approval

The financial statements were approved by the Board of Directors 28 March 2019.