HSBC Saudi Arabia

Pillar 3 Disclosures (31 December 2019)

HSBC

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Pillar 3 Disclosures (31 December 2019) (continued)

1. Introduction

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.

The report has been prepared in accordance to meet the minimum disclosure requirement as set out in Article 68 (Annex 10) of the CMA Prudential Rules relating to Pillar III Disclosure and Reporting requirements. In accordance with the capital adequacy framework issued by CMA, the prudential rules comprises of three pillars as summarised below:

Pillar I includes the company's minimum capital requirements as per risk based approach;

- Credit risk in the company arises from receivables from advisory services, margin lending, cash balances held with banks, and Investments in HSBC Funds.
- Market Risk in the company arises from Special commission/Interest rate risk, equity price risk and liquidity risk.
- Operational Risk, company has applied Expenditure based approach for 2019.

Pillar II includes the company's Internal Capital Adequacy Assessment Process (ICAAP) pursuant to Annex. 9 of the CMA prudential rules and ensures that there is governing body oversight; sound capital assessment; comprehensive assessment of risks; monitoring and reporting; and internal control review.

Pillar III includes the company's disclosure and reporting framework that enhances market discipline, transparency and enables comparability and includes information regarding the calculation of capital base, minimum capital requirements and large exposures in accordance with the capital adequacy model.

2. Capital Structure

The authorized, issued and fully paid share capital of the Company consists of 50 million shares of
SAR 10 each. As at 30 September 2019, the Company is owned by the following shareholders in the proportion set out below:

	Number of shares	*% of contribution*	*As at 30 September 2019*
HSBC Asia Holdings BV	24,500,000	49.00%	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**

Effective 01 October 2019, the ownership structure of the Company has been changed as follows:

	Number of shares	*% of contribution*	*As at 30 September 2019*
HSBC Asia Holdings BV	25,500,000	51.00%	255,000,000
The Saudi British Bank ('SABB')	24,500,000	49.00%	245,000,000
Total	**50,000,000**	**100%**	**500,000,000**

2. Capital Structure *(continued)*

Tier 1 and 2 Tier Capital

Capital Base ***SAR '000***	***2019***	*2018*
Tier-1 capital		
Paid-up capital	**500,000**	500,000
Audited retained earnings	**261,071**	136,015
Other reserves	**(4,835)**	(5,314)
Statutory Reserve	**150,000**	150,000
Deductions from Tier-1 capital	**(8,633)**	(8,026)
Total Tier-1 capital	**897,603**	772,675
Tier-2 capital	**-**	-
Total Tier-2 capital	**897,603**	772,675

Total Capital Base

Paid-up capital: The authorized, issued and fully paid share capital of the Company consists of 50 million shares of SAR 10 each.

Statutory Reserve: In accordance with Article 176 of the Saudi Arabian Regulations for Companies, the Company is required to transfer 10% of net income to a statutory reserve until such reserve equals 30% of the paid up capital as a minimum. This reserve is not available for distribution. As the company's cumulative transfers to statutory reserves had reached the 30% of the total paid up capital, the company was not required to make any transfers to the statutory reserve during this year.

Retained Earnings: This constitutes undistributed profits relating to prior years if any and profit for the current year 2018 net of any deductions relating to zakat, income tax and statutory reserves.

Other Reserves: The balances pertain to adjustments made for the recognition of deferred tax asset and re-measurement of the end of service benefits resulting from the Company's adoption of IFRS.

3. Capital Adequacy

HSBC SA as of 31 December 2019 is maintaining a strong capital adequacy ratio of 2.47 and is reasonably well capitalised in accordance with the capital adequacy guidelines defined under Pillar 1. As at 31 December 2019, total Pillar 1 minimum capital requirement was SAR 364 million, whilst total available capital was SAR 897.6 million resulting in a surplus capital of SR 533.5 m. HSBC SA is fully committed to maintain adequate levels of capital in line with the overall risks taken by the company. HSBC SA has ensured that capital levels are maintained above the levels required by CMA and is fully committed to meet the capital requirements as regulated by CMA going forward.

HSBC SA capital adequacy as of 31st December 2019 is as below

HSBC SA Capital Summary SAR 000	December 2019
Total capital available HSBC SA	**897,603**
Capital Required - Market Risk	14,452
Capital Required - Credit Risk	267,329
Capital Required - Operational Risks	82,278
Total Minimum Capital Requirement	**364,059**
Surplus Capital	**533,544**
Capital Ratio (times)	**2.47**

4. Risk Management

HSBC SA through its risk management and governance framework seeks to maintain a conservative and consistent approach to risk, helping to ensure we protect customers' and support economies. By carefully aligning our risk appetite to our strategy, we aim to deliver sustainable long-term shareholder returns.

All employees are responsible for the management of risk, with the ultimate accountability residing with the Board. We have a strong risk culture, which is embedded through clear and consistent communication and appropriate training for all employees. A comprehensive risk management framework is applied throughout the company, with governance and corresponding risk management tools. This framework is underpinned by our risk culture and reinforced by the HSBC values and required conduct outcomes. The Risk function oversees the framework and is led by the Chief Risk Officer and it is independent from the businesses, including our sales and trading functions, to provide challenge, appropriate oversight and balance in risk/reward decisions.

4.1 Risk Framework:

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

- The company's risk appetite defines the desired forward-looking risk profile, and informs the strategic and financial planning process. It is articulated in our risk appetite statement, which is approved by the Board. Key elements include:
  - risks that we accept as part of doing business, such as credit risk and market risk;
  - risks that we incur as part of doing business, such as operational risk, which are actively managed to remain below an acceptable tolerance; and
  - risks for which we have zero tolerance, such as knowingly engaging in activities where foreseeable reputational risk and misconduct has not been considered

  Internal stress tests are an important element in our risk management and capital management frameworks. They include potential adverse macroeconomic, geopolitical and operational risk events, and other potential events that are specific to HSBC SA. Stress testing analysis helps management understand the nature and extent of vulnerabilities to which the bank is exposed. We operate a comprehensive stress testing programme as part of the ICAAP, taking part in CMA's as well as our own stress tests.

  Our Internal Capital Adequacy Assessment Process (ICAAP) is based on the following key elements:
  - Framework to assess capital adequacy, process and governance and the risks included in the ICAAP assessment;
  - The company's legal, operating and governance structures;
  - The company's strategy and approach to risk and capital management;
  - Assessment of capital adequacy in light of the financial projections over a 3 year horizon;
  - Stress testing including reverse stress testing.
- Our top and emerging risks framework helps enable us to identify current and forward-looking risks so that we may take action to either prevent them materialising or limit their effect. Top risks are those that may have a material impact on the financial results, reputation or business model of the company in the year ahead. Emerging risks are those that have large unknown components and may form beyond a one-year horizon. If these risks occurred, they could have a material effect on the company.

4. Risk Management *(continued)*

- HSBC SA standards and policies outline the core principles within which the Company and its employees must operate in conducting its business.
- 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,

HSBC SA has implemented a 'Three Lines of Defence' model for managing its risks.

First Line of Defence: Business management 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.

Second Line of Defence: It 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.

Third Line of Defence: Internal Audit (INA) represents the independent 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.

4.2 Corporate Governance

HSBC SA is committed to high standards of corporate governance. We have a comprehensive range of policies and systems in place to ensure that the company is well-managed, with effective oversight and control.

The Board aims to promote HSBC SA's long-term success, deliver sustainable value to shareholders and promote a culture of openness and debate. Led by the non-executive Chairman, it sets the company's strategy and risk appetite. It also approves capital and operating plans for achieving strategic objectives on the recommendation of management. In exercising its duty to promote the success of the Company, the Board is responsible for overseeing the management of HSBC SA and, in so doing, may exercise its powers, subject to all local relevant laws, regulations and the committee's articles of association. The Board is committed to effective engagement with all of its stakeholders. The Board receives reports from management on various issues, which it takes into account in discussions and decision making. Certain matters, including the review and approval of annual operating plans, risk appetite, performance targets, credit or market risk limits and any substantial change in balance sheet management policy, require Board approval before implementation.

The Board regularly reviews reports on performance against financial and other strategic objectives, key business challenges, risk, business developments and relationships with its stakeholders.

HSBC SA Board and Sub-Committees			
Risk Committee Consisting of 5 Members including non-executive or independent board members, and non-board members.	**Audit Committee** Consisting of 5 Members including non-executive or independent board members, and non-board members	**Executive Committee** Consisting of 3 Members from the board	**Nomination & Remunaration Committee** Consisting of 4 Members from non-executive or independent board members, and non-board members
Chairman: HSBC Nominated	**Chairman: Independent Director**	**Chairman: CEO HSBC SA**	**Chairman: Independent Director**

HSBC's Board and its committees are subject to regular, independent evaluation of their effectiveness. All Board members also undergo regular performance reviews. In the case of executive directors, this helps determine the level of variable pay they receive each year. In addition, the Board is directly accountable to our shareholders. Shareholders vote at each Annual General Meeting on whether to re-elect individual directors. Committees are smaller groups delegated by the full Board to provide advice on and oversight of the Company's different activities. Each standing committee is chaired by a non-executive Board member and has a remit to cover specific topics.

Board Risk Committee

The Board Risk Committee ("BRC") 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.

Audit Committee

It reviews matters relating to financial reporting and the effectiveness of internal 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.

Nomination and Remuneration Committee

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.

Executive Committee

The Executive Committee ("EXCOM") is appointed by the Board and reports directly to the Board. 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.

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. As part of the risk governance and internal control framework, the management has established various committees such as Risk Management Committee. HSBC Compliance Committee, Management Committee, Asset Liability Committee, Shariah Committee and Operations Risk Working Group to ensure compliance with applicable laws and regulations, internal policies and procedures, and quality of external and internal reporting.

4. Risk Management *(continued)*

4.3 Risk Appetite Statement

HSBC SA Risk Appetite framework includes the following;

Risk Matric Category	Risk Components Monitored
Earnings	Return on Equity, cost efficiency and dividend pay-outs
Capital and Liquidity	Capital and Liquidity ratios
Risk Categories & Diversification	Limits established for Operations risk, Reputation, Credit, Fiduciary and Information risk
Financial Crime Compliance	Exceptions in KYC, AML, Sanctions, Suspicious activity etc.
Regulatory compliance	Sets targets and limits covering customer conduct, sales quality, product due diligence and compliance conduct
FCC and RC Audit Issues	Sets limits on High risk audit points
Trainings	Monitors mandatory FCC and RC training of staff and other mandatory

5. 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 measuring and 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 monitor 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. Procedures for identifying and recording and monitoring all large exposures are managed as per thresholds defined by the regulator. The company has defined large exposures as an exposure to a counterparty or group of connected counterparties that exceeds 10% of the capital base.

The company had invested part of its surplus capital into HSBC Funds after performing adequate due diligence and approvals of the Board.

Credit Risks	**267,329**
Exposures to government, central banks	112
Exposures to corporates, admin bodies, NPO	54,346
Exposures to APs, banks	14,877
Investment funds	13,102
Margin financing	155,744
Other on-balance sheet exposures	23,150
Off-balance sheet commitments	5,998

5. Credit Risk *(continued)*

Impairment of financial assets (Expected credit losses)

IFRS 9 requires the Company to record an allowance for ECL for all loans and other debt financial assets not held at FVTPL. The allowance is based on the ECL associated with the probability of default in the next twelve months unless there has been a significant increase in credit risk since origination.

The Company considers a financial asset to be in default when:

- The borrower is unlikely to pay its credit obligations to Company in full, or
- The borrower is past due more than 90 days on any material credit obligation to Company.

In assessing whether a borrower is in default the Company considers indicators that are:

- Qualitative- e.g. breaches of covenant;
- Quantitative- e.g. overdue status and non-payment on another obligation of the same issuer to Company;

Advisory Income Receivable

	As at 31 December 2019	*As at 31 December 2018*
Gross advisory income receivable	**16,824,137**	34,110,548
Less: Allowance for impairment	**(7,261,815)**	(5,325,345)
	9,562,322	28,785,203

These advisory income receivables are expected to be settled in short term, thus do not contain any financing component.

Receivable Against Margin Lending

	As at 31 December 2019	*As at 31 December 2018*
Gross receivable against margin lending	**742,408,348**	816,085,684
Less: Allowance for impairment for expected credit losses	**(769,733)**	(1,113,294)
	741,638,615	814,972,390

The Company extends margin financing facilities to its customers to invest in the Saudi stock exchange (Tadawul) who wish to actively trade on a leveraged basis, secured by the tradable securities. The facilities are reviewed at least on an annual basis.

6. 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 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 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 provide exposure to Saudi and International Money Market and Fixed Income investments. The company non trading book is operated within the nominal limits approved by the Board including MTM Referral Limits.

Equity price risk refers to the risk of decrease in fair values of equity securities held by the Company. Currently the Company does not have any investments in equity securities, however, there are investments in mutual funds where underlying assets are equity securities. The net asset value of these mutual funds are subject to equity price risk. Since these mutual funds' investments are highly liquid due to its open ended nature, management is able to minimize the risk while monitoring the net asset value changes due to fluctuations in equity price indices.

Foreign exchange rate risk

Foreign exchange rate risk arises when the actual or forecasted assets in a foreign currency are either greater or less than the liability in that currency. The Company's foreign currency transactions are primarily denominated in USD. The rate of exchange for conversion of the Saudi Riyal to the US Dollar is pegged, on the basis of which the management believes that the Company is not significantly exposed to risk of fluctuation in foreign exchange rates.

Special commission rate risk

Special commission/Interest rate risk is the uncertainty of future earnings resulting from fluctuations in special commission or Interest rates. The risk arises when there is a mismatch in assets and liabilities, which are subject to rate movements within a specified period. The most important source of such risk is the Company's difference in company's borrowing rates and the lending rates offered on margin lending facilities, where fluctuations in the rates, if any, are reflected in the results of its operations. Management monitors the change in the special commission rate and believes that the net special commission rate risk to the Company is not significant.

Capital requirements for market risk of the company as of 31st December 2019 are indicated below;

Market Risks	**14,452**
Fund Risk	12,607
FX Risk	**1,845**

7. Operational Risk

Operational risk is defined as the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events, including legal risk. Operational risk is relevant to every aspect of the Company's business and covers a wide spectrum of risks.

It is HSBC SA's strategy to manage operational risks in a cost effective manner, within targeted levels consistent with the company's risk appetite. The company's Operational Risk Management Framework ensures minimum standards of governance and organization over operational risk and internal control and covers all its businesses and operations.

Strong risk management and internal control are core elements of HSBC SA's strategy and all staff are responsible for managing and mitigating operational risks in their core operations.

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.

Operational Risk has specific responsibilities in relation to the operational risk framework. These are:

- Set the Operational Risk framework and policy and oversee their implementation across HSBC SA.
- Provide quality assurance and challenge of risk and control assessments, internal control monitoring plans, the results of control monitoring activity conducted by the First Line and of the completeness of second line oversight of the business and functions.
- Provide independent oversight of HSBC SA's operational risk profile, identify emerging risks and gaps and carry out specific reviews of key risk issues.
- Flag breaches of risk appetite and unacceptable delays in resolving control issues to the appropriate governance committees.

Operations Risk capital requirements of the company as of 31st December 2017 are indicated below;

The company applied the Basic Indictor Approach as per which the income indicator consists of the average of operating income for the last three audited annual financial statements on which a risk charge of 15% is applied to arrive at the capital requirement.

Operational Risks	***Year -3***	***Year -2***	***Year -1***			
Basic Indicator Approach	**2017**	**2018**	**2019**	**Average**	**Risk charge (%)**	**Capital requirements (SAR '000)**
Operating income (SAR '000)	392,151	409,223	625,868	475,747	15	**71,362**
Expenditure-based approach	-	-	-	-	-	-
Overhead expenses (SAR '000)	-	-	329,111	-	25	**82,278**
Total Operational Risks						**82,278**

8. Liquidity Risk

Liquidity risk is the risk that the Company will be unable to meet its net funding requirements. Liquidity risk can arise from market disruptions or credit downgrades, which may cause certain sources of funding to dry up immediately.

Management monitors the maturity profile of the Company's assets and liabilities based on the remaining year at the balance sheet date to the contractual maturity date to ensure that adequate liquidity is maintained. All liabilities other than end of service benefits and long-term loans are contractually payable on a current basis.

In addition to the operational profits, the main source of funds for HSBC SA is its capital and undistributed profits. The Company has established a short term revolving loan facility from and other local commercial bank carrying commission rate at agreed commercial rate. In the case of HSBC SA liquidity risk may arise by an inability to sell a financial instrument in the market on a timely basis. Within HSBC SA one of the main liquidity risk is of a fiduciary basis within Asset Management.

With the advent of the market change to a two day settlement cycle, the company has set settlement limits for both its Custody and Brokerage activities on a per counterparty basis, these limits generate liquidity risk in the advent of client defaults or delayed trades. Such instances historically are very limited. HSBC SA has sufficient committed credit lines in place to match liquidity settlement risk on these lines. These are further ring fenced by our Settlement agent who guarantees to Tadawul all HSBC SA market trade settlements.

The company has established a liquidity management process for Margin lending product is to ensure that the company has access to adequate level of funding at all times to meet the cash flow requirements driven by changes in utilization levels and to fully mitigate any liquidity and reputation risks for the company.

The liquidity ratio of HSBC SA as at 31 Dec 2019 is 2.49. The ratio has been computed as current asset divided by current liabilities.

9. 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

The fiduciary risk in asset management can arise from market risk, liquidity risk, credit risk, and product design and product suitability amongst others. The risk is managed through internal controls exercised primarily through the following committees:

Committee	Objective
Investment Committee	The primary objective of the Investment Committee is to govern and manage the investment strategies to ensure all strategies are aligned to the investment objective of the product/service. Additionally the committee ensures that investment process followed by HSBC SA complies with the standards required by both CMA regulations and HSBC best practices
Performance Review Committee	To review performance of Funds and Discretionary Portfolios and ensure consistency of performance across portfolios following similar strategies.
Product Approval Committee	Oversee initiatives to develop or distribute new products.
Fund Board	The fund board oversees the management and operations of the fund on behalf of the funds' unit holders. Among other things, the fund board oversees the performance of the fund, approve the fees paid to the service providers, and oversee the fund's compliance to the regulations.
Retail Banking Oversight Committee	The committee oversee the wealth activities related to retail clients with the prime objective of ensuring the sales monitoring, sales quality control and Client servicing.

In addition, a business risk control team is part of the first line of defence integrated within the asset management business and t keeps the business head apprised of any emerging risk and / or any issues that need to be addressed.

Control departments including compliance and risk management also oversee the operations of the business with the risk management committee. The risk department in particular monitors the management of all investment funds and portfolios with daily reports generated to identify any breaches against regulatory requirements, client imposed restrictions or Management Action Triggers (MAT) that generally specify the maximum deviation of a portfolio's performance compared to its benchmark.

10. Compliance Risk

It is the risk to HSBC SA in breaching Local Regulatory and International Best Standards in regard to Financial Crime Compliance and Regulatory Compliance. As any business operating in such regulated environment, this risk exists throughout all areas of the Company.

HSBC SA applied "Three Line of Defence" approach to manage risks. Therefore, compliance risk among other risks is owned by business as first line of defence and is being monitored through an independent compliance function which is responsible for providing guidance and independent control and review of the compliance risks within the company as a second line of defence while Audit function which conducts regular reviews acts as the third line of defence.

HSBC SA has implemented a strong internal control structure to ensure full compliance with all directives issued by CMA. Frequent reviews are conducted and business owners certify on an annual basis their compliance with existing regulatory requirements.

11. Other Risks

HSBC SA continues identifying risks that will adversely impact on present and future operations of the Company. Issues are addressed in a proactive manner with respect to risk assessment and management to ensure compliance with local regulatory requirements.

App II: Disclosure on Capital Base	**2019**	**2018**
Tier-1 Capital	**SAR'000**	**SAR'000**
Paid-up capital	500,000	500,000
Audited retained earnings	261,071	136,015
Share premium	-	-
Reserves (other than revaluation reserves)	150,000	150,000
Other Reserves	(4,835)	(5,314)
Tier-1 capital contribution	-	-
Deductions from Tier-1 capital	(8,633)	(8,026)
Total Tier-1 capital	**897,603**	**772,675**
Tier-2 capital		
Subordinated loans	-	-
Cumulative preference shares	-	-
Revaluation reserves	-	-
Other deductions from Tier-2 (-)	-	-
Deduction to meet Tier-2 capital limit (-)	-	-
Total Tier-2 capital	-	-
Total Capital Base	**897,603**	**772,675**

Pillar 3 Disclosures (31 December 2019) (continued)

App II: Disclosure on Capital Adequacy 2019

Exposure Class	Exposures before CRM SAR'000		Net Exposures after CRM SAR'000	Risk Weighted Assets SAR'000	Capital Requirement SAR'000
Credit Risk					
On-balance Sheet Exposures		-	-	-	-
Governments and Central Banks		3,988	-	798	112
Authorised Persons and Banks		531,320	-	106,264	14,877
Corporates		58,273	-	388,185	54,346
Retail		-	-	-	-
Investments		231,741	-	93,585	13,102
Securitisation		-	-	-	-
Margin Financing		741,639	-	1,112,459	155,744
Other Assets		39,430	-	165,361	23,150
Total On-Balance sheet Exposures		**1,606,391**	**-**	**1,866,651**	**261,331**
Off-balance Sheet Exposures		-	-	-	-
OTC/Credit Derivatives		-	-	-	-
Repurchase agreements		-	-	-	-
Securities borrowing/lending		-	-	-	-
Commitments		6,000	-	42,840	5,998
Other off-balance sheet exposures		-	-	-	-
Total Off-Balance sheet Exposures		**6,000**	**-**	**57,120**	**5,998**
Total On and Off-Balance sheet Exposures		1,612,391	**-**	1,909,491	267,329
Prohibited Exposure Risk Requirement		**-**	**-**	**-**	-
Total Credit Risk Exposures		**1,612,391**	**-**	**1,909,491**	**267,329**
Market Risk	*Long Position*	*Short Position*			
Interest rate risks	-	-	-	-	-
Equity price risks	-	-	-	-	-
Risks related to investment funds	78,793	-	-	-	21,607
Securitisation/resecuritisation positions	-	-	-	-	-
Excess exposure risks	-	-	-	-	-
Settlement risks and counterparty risks	-	-	-	-	-
Foreign exchange rate risks	187,440	(112,682)	-	-	1,845
Commodities risks.	-	-	-	-	-
Total Market Risk Exposures	**266,233**	**(112,682)**	**-**	**-**	**14,452**
Operational Risk					**82,278**
Minimum Capital Requirements					**364,059**
Surplus/(Deficit) in capital					**533,544**
Total Capital ratio (time)					**2.47**

App II: Disclosure on Capital Adequacy 2018

Exposure Class	Exposures before CRM SAR'000	Net Exposures after CRM SAR'000	Risk Weighted Assets SAR'000	Capital Requirement SAR'000
Credit Risk				
On-balance Sheet Exposures	-	-	-	-
Governments and Central Banks	1,689	-	338	47
Authorised Persons and Banks	236,2125	-	47,243	6,614
Corporates	37,870	-	225,804	31,613
Retail	-	-	-	-
Investments	181,559	-	235,919	33,029
Securitisation	-	-	-	-
Margin Financing	814,972	-	1,222,458	171,144
Other Assets	64,484	-	330,747	46,305
Total On-Balance sheet Exposures	1,336,789	-	2,062,509	288,751
Off-balance Sheet Exposures	-	-	-	-
OTC/Credit Derivatives	-	-	-	-
Repurchase agreements	-	-	-	-
Securities borrowing/lending	-	-	-	-
Commitments	-	-	-	-
Other off-balance sheet exposures	6,000	-	42,840	5,998
Total Off-Balance sheet Exposures	6,000	-	42,840	5,998
Total On and Off-Balance sheet Exposures	1,342,789	-	2,105,349	294,749
Prohibited Exposure Risk Requirement	-	-	-	-
Total Credit Risk Exposures	**1,342,789**	**-**	**2,105,349**	**294,749**

Market Risk	*Long Position*	*Short Position*			
Interest rate risks	-	-	-	-	-
Equity price risks	-	-	-	-	-
Risks related to investment funds	7,263	-	-	-	1,162
Securitisation/resecuritisation positions	-	-	-	-	-
Excess exposure risks	-	-	-	-	-
Settlement risks and counterparty risks	-	-	-	-	-
Foreign exchange rate risks	90,038	(198)	-	-	1,975
Commodities risks.	-	-	-	-	-
Total Market Risk Exposures	**97,301**	**(198)**	**-**	**-**	**3,137**

Operational Risk	**66,003**
Minimum Capital Requirements	**363,889**
Surplus/(Deficit) in capital	**408,786**
Total Capital ratio (time)	**2.12**

Pillar 3 Disclosures (31 December 2019) (continued)

App III: Disclosure on Credit Risk's Risk Weight - 2019

	Exposures after netting and credit risk mitigation												
Risk Weights	*Governments and central banks* **SAR'000**	*Administrative bodies and NPO* **SAR'000**	*Authorised persons and banks* **SAR'000**	*Margin Financing* **SAR'000**	*Corporates* **SAR'000**	*Retail* **SAR'000**	*Past due items* **SAR'000**	*Investments* **SAR'000**	*Securitisation* **SAR'000**	*Other assets* **SAR'000**	*Off-balance sheet commitments* **SAR'000**	*Total Exposure after netting and Credit Risk Mitigation* **SAR'000**	*Total Weighted Assets* **SAR'000**
0%	-	-	-	-	-	-	-	-	-	28	-	2,838	**-**
20%	3,988	-	531,320	-	-	-	-	16,329	-	-	-	139,580	**110,327,40**
50%	-	-	-	-	4,199	-	-	92,549	-	-	-	124,946	**48,374.03**
100%	-	-	-	-	-	-	-	44,069	-	-	-	35,516	**44,069**
150%	-	-	-	741,639	-	-	-	-	-	-	-	784,904	**1,112,458.50**
200%	-	-	-	-	-	-	-	-	-	-	-	-	**-**
300%	-	-	-	-	-	-	-	-	-	28,012	-	39,456	**84,036**
400%	-	-	-	-	-	-	-	-	-	-	-	-	**-**
500%	-	-	-	-	-	-	-	-	-	-	-	-	**-**
714% (include prohibited exposure)	-	-	-	-	54,074	-	-	-	-	11,390	6,000	71,464	**510,250**
Average Risk Weight	-	-	-	-	-	-	-	-	-	-	-	-	**125%**
Deduction from Capital Base	-	-	-	-	-	-	-	-	-	-	-	-	**267,332**

App III: Disclosure on Credit Risk's Risk Weight - 2018

	Exposures after netting and credit risk mitigation												
Risk Weights	*Governments and central banks* **SAR'000**	*Administrative bodies and NPO* **SAR'000**	*Authorised persons and banks* **SAR'000**	*Margin Financing* **SAR'000**	*Corporates* **SAR'000**	*Retail* **SAR'000**	*Past due items* **SAR'000**	*Investments* **SAR'000**	*Securitisation* **SAR'000**	*Other assets* **SAR'000**	*Off-balance sheet commitments* **SAR'000**	*Total Exposure after netting and Credit Risk Mitigation* **SAR'000**	*Total Weighted Assets* **SAR'000**
0%	-	-	-	-		-	-	-	-	38	-	38	-
20%	1,689	-	236,215	-	-	-	-	-	-	-	-	237,904	47,580,80
50%	-	-	-	-	6,715	-	-	18,997	-	-	-	25,712	12,856.15
100%	-	-	-	-	-	-	-	16,302	-	-	-	16,302	16,302
150%	-	-	-	814,972	-	-	-	138,709	-	-	-	953,681	1,430,522
200%	-	-	-	-	-	-	-	-	-	40,803	-	-	-
300%	-	-	-	-	-	-	-	-	-	-	-	40,803	122,409
400%	-	-	-	-	-	-	-	-	-	-	-	-	-
500%	-	-	-	-	-	-	-	-	-	-	-	-	-
714% (include prohibited exposure)	-	-	-	-	31,155	-	-	288	-	29,179	6,000	66,622	475,680
Average Risk Weight	-	-	-	-	-	-	-	-	-	-	-	-	157%
Deduction from Capital Base	-	-	-	-	-	-	-	-	-	-	-	-	294,749

Pillar 3 Disclosures (31 December 2019) (continued)

App IV: Disclosure on Credit Risk's Rated Exposure - 2019

Exposure Class	Long term Ratings of counterparties							
	Credit quality step	1	2	3	4	5	6	Unrated
	S&P	AAA TO AA-	A+ TO A-	BBB+ TO BBB-	BB+ TO BB-	B+ TO B-	CCC+ and below	Unrated
	Fitch	AAA TO AA-	A+ TO A-	BBB+ TO BBB-	BB+ TO BB-	B+ TO B-	CCC+ and below	Unrated
	Moody's	Aaa TO Aa3	A1 TO A3	Baa1 TO Baa3	Ba1 TO Ba3	B1 TO B3	Caa1 and below	Unrated
	Capital Intelligence	AAA	AA TO A	BBB	BB	B	C and below	Unrated
On and Off-balance-sheet Exposures								
Governments and Central Banks				3,988				
Authorised Persons and Banks			440,299	91,021				
Corporates				4,199				54,074
Retail								
Investments								
Securitisation								
Margin Financing								741,639
Other Assets								
Total			**440,299**	**99,208**				**795,713**

App IV: Disclosure on Credit Risk's Rated Exposure - 2018

Exposure Class	Long term Ratings of counterparties							
	Credit quality step	1	2	3	4	5	6	Unrated
	S&P	AAA TO AA-	A+ TO A-	BBB+ TO BBB-	BB+ TO BB-	B+ TO B-	CCC+ and below	Unrated
	Fitch	AAA TO AA-	A+ TO A-	BBB+ TO BBB-	BB+ TO BB-	B+ TO B-	CCC+ and below	Unrated
	Moody's	Aaa TO Aa3	A1 TO A3	Baa1 TO Baa3	Ba1 TO Ba3	B1 TO B3	Caa1 and below	Unrated
	Capital Intelligence	AAA	AA TO A	BBB	BB	B	C and below	Unrated
On and Off-balance-sheet Exposures								
Governments and Central Banks			1,689					
Authorised Persons and Banks		236,215						
Corporates			6,715					31,155
Retail								
Investments			18,997	16,302				138,997
Securitisation								
Margin Financing								814,972
Other Assets								70,020
Total		**236,215**	**27,401**	**16,302**				1,055,144

**Short term rating of counterparties is not applicable*

App V: Disclosure on Credit Risk Mitigation (CRM) - 2019

Exposure Class	*Exposures before CRM*	*Exposures covered by Guarantees/ 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						
Governments and Central Banks	3,988					3,988
Authorised Persons and Banks	531,320					531,320
Corporates	58,273					58,273
Retail						-
Investments	231,741					231,741
Securitisation						-
Margin Financing	741,639					-
Other Assets	39,430		(741,639)			39,430
Total On-Balance sheet Exposures	**1,606,391**		**(741,639)**			**864,752**
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	6,000					6,000
Total Off-Balance sheet Exposures	**6,000**	-	**-**	-	-	6,000
Total On and Off-Balance sheet Exposures	**1,612,391**	-	**(741,639)**	-	-	**870,752**

Pillar 3 Disclosures (31 December 2019) (continued)

App V: Disclosure on Credit Risk Mitigation (CRM) - 2018

Exposure Class	*Exposures before CRM*	*Exposures covered by Guarantees/ 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						
Governments and Central Banks	1,689					1,689
Authorised Persons and Banks	236,215					236,215
Corporates	37,870					37,870
Retail						-
Investments	181,559					181,559
Securitisation						-
Margin Financing	814,972					-
Other Assets	70,020		(814,972)			70,020
Total On-Balance sheet Exposures	**1,342,325**		**(814,972)**			**527,353**
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	6,000					6,000
Total Off-Balance sheet Exposures	**6,000**	-	**-**	-	-	6,000
Total On and Off-Balance sheet Exposures	**1,348,325**	-	**(814,972)**	-	-	**533,353**

App VI - Contractual Maturity Break down as at 31 Dec. 2019

Assets	*Within 3 months*	*3 to 12 months*	*No fixed maturity*	**SAR'000** *Total*
Cash and cash equivalents	-	-	457,980,727	457,980,727
Investments - fair value through profit or loss	-	-	231,739,849	231,739,849
Advisory income receivable	9,562,322	-	-	9,562,322
Receivable against portfolio management	3,122,021	-	-	3,122,021
Receivable against margin lending	-	741,638,615	-	741,638,615
Due from related parties	86,006,675		-	86,006,675
Total	**98,691,018**	**741,638,615**	**689,720,576**	**1,530,050,209**
Liabilities and Shareholders' equity				
Due to related parties	22,689,391	-	-	22,689,391
Short term loans	225,720,047	-	-	225,720,047
Accrued expenses and other liabilities	278,668,935	67,463,137	-	346,132,072
End of service benefits	-	-	49,186,585	49,186,585
Total	**527,078,373**	**67,463,137**	**49,186,585**	**643,728,095**
Maturity gap	**(428,387,355)**	**674,175,478**	**640,533,991**	**886,322,114**
Cumulative maturity gap	**(428,387,355)**	**245,788,123**	**886,322,114**	**-**

App VI - Contractual Maturity Break down as at 31 Dec. 2018

Assets	*Within 3 months*	*3 to 12 months*	*No fixed maturity*	**SAR'000** *Total*
Cash and cash equivalents	-	-	229,709,388	229,709,388
Investments - fair value through profit or loss	-	-	181,559,495	181,559,495
Advisory income receivable	28,785,203	-	-	28,785,203
Receivable against portfolio management	2,530,946	-	-	2,530,946
Receivable against margin lending	-	814,972,390	-	814,972,390
Due from related parties	14,204,800	-	-	14,204,800
Total	**45,520,949**	**814,972,390**	**411,268,883**	**1,271,762,222**
Liabilities and Shareholders' equity				
Due to related parties	27,317,886	-	-	27,317,886
Short term loans	326,215,177	-	-	326,215,177
Accrued expenses and other liabilities	68,700,000	64,246,006	-	132,946,006
End of service benefits	-		48,942,303	48,942,303
Total	**422,233,063**	**64,246,006**	**48,942,303**	**535,421,372**
Maturity gap	**(376,712,114)**	**750,726,384**	**362,326,580**	**736,340,850**
Cumulative maturity gap	**(376,712,114)**	**374,014,270**	**736,340,850**	**-**

Pillar 3 Disclosures (31 December 2019) (continued)

Glossary of Terms

Acronym	***Definition***	***Acronym***	***Definition***
AML	Anti –Money Laundering	HSBC	HSBC Group Plc
APR	Authorised Persons Regulation	HSBC SA	HSBC Saudi Arabia
AUCOM	Audit Committee	HCC	HSBC Compliance Committee
BOARD	HSBC SA Board of Directors	HSS	HSBC Securities services
BRCM	Business Risk Control Manager	ICAAP	Internal Capital Adequacy Assessment Process
CMA	Capital Markets Authority	KRIs	Key Risk Indicators
CEO	Chief Executive Officer	MAT	Management Attention Limits
CRO	Chief Risk Officer	MTM	Market to Market – Market Risk
DPM	Discretionary Portfolio Management	AOP	Annual operation plan
FCC	Financial Crime Compliance	RAS	Risk Appetite Statement
RWAs	Risk Weighted Assets	RC	Regulatory Compliance
SABB	The Saudi British Bank	RMC	Risk Management Committee