

**HSBC SAUDI EQUITY INCOME FUND**  
**Managed by HSBC Saudi Arabia**  
**FINANCIAL STATEMENTS**  
**For the year ended 31 December 2018**  
together with the  
**INDEPENDENT AUDITORS' REPORT**



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Licence No. 46/11/323 issued 11/3/1992

## Independent auditor's report

To the unitholders of HSBC Saudi Equity Income Fund

### Opinion

We have audited the financial statements of **HSBC Saudi Equity Income Fund** ("the Fund"), managed by HSBC Saudi Arabia ("the Fund Manager"), which comprise of the statement of financial position as at 31 December 2018, the statements of comprehensive income, changes in net assets (equity) attributable to the unitholders and cash flows for the year then ended, and notes to the financial statements, comprising significant accounting policies and other explanatory information.

In our opinion, the accompanying financial statements present fairly, in all material respects, the financial position of the Fund as at 31 December 2018, and its financial performance and its cash flows for the year then ended in accordance with the International Financial Reporting Standards ("IFRS") as endorsed in the Kingdom of Saudi Arabia and other standards and pronouncements issued by the Saudi Organization for Certified Public Accountants ("SOCPA").

### Basis for opinion

We conducted our audit in accordance with the International Standards on Auditing ("ISA") that are endorsed in the Kingdom of Saudi Arabia. Our responsibilities under those standards are further described in the *Auditors' responsibilities for the audit of the financial statements* section of our report. We are independent of the Fund in accordance with the professional code of conduct and ethics that are endorsed in the Kingdom of Saudi Arabia that are relevant to our audit of the financial statements, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

### Responsibilities of the Fund Manager and those charged with governance for the financial statements

The Fund Manager is responsible for the preparation and fair presentation of the financial statements in accordance with IFRS that are endorsed in the Kingdom of Saudi Arabia and other standards and pronouncements issued by SOCPA, and compliance with the applicable provisions of the Investment Funds Regulations issued by the Capital Market Authority, the Fund's Terms and Conditions and the Information Memorandum and for such internal control as the Fund Manager determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the Fund Manager is responsible for assessing the Fund's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the Fund Manager either intends to liquidate the Fund or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Fund's financial reporting process.

# Independent auditors' report

To the unitholders of HSBC Saudi Equity Income Fund (continued)

## Auditors' responsibilities for the audit of the financial statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. 'Reasonable assurance' is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISA that are endorsed in the Kingdom of Saudi Arabia will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

As part of an audit in accordance with ISA that are endorsed in the Kingdom of Saudi Arabia, we exercise professional judgement and maintain professional scepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error; design and perform audit procedures responsive to those risks; and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Fund's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the Fund Manager.
- Conclude on the appropriateness of the Fund Manager's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Fund's ability to continue as a going concern. If we conclude that a material uncertainty exists, then we are required to draw attention in our auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Fund to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit of **HSBC Saudi Equity Income Fund** ("the Fund").

**For KPMG Al Fozan & Partners**  
**Certified Public Accountants**

**Dr. Abdullah Hamad Al Fozan**  
License No. 348

28 Rajab 1440H  
Corresponding to: 4 April 2019



**HSBC SAUDI EQUITY INCOME FUND**  
**(An open-ended mutual fund)**  
**Statement of financial position**  
**As at 31 December 2018**  
(Amounts in Saudi Arabian Riyal)

	<i>Note</i>	<i>31 December</i> <b>2018</b>	<i>31 December</i> <b>2017</b>	<i>1 January</i> <b>2017</b>
<b>ASSETS</b>				
Cash and cash equivalents	<i>10</i>	<b>4,669,336</b>	4,493,334	2,893,229
Investments at fair value through profit or loss	<i>11</i>	<b>239,444,442</b>	215,104,533	238,893,136
Receivables and advances		<b>391,280</b>	58,902	310,041
<b>TOTAL ASSETS</b>		<b>244,505,058</b>	219,656,769	242,096,406
<b>LIABILITIES</b>				
Accrued expenses	<i>13</i>	<b>473,513</b>	60,666	55,883
Dividend Payable		<b>3,062,942</b>	2,332,329	1,376,412
<b>TOTAL LIABILITIES</b>		<b>3,536,455</b>	2,392,995	1,432,295
<b>NET ASSETS (EQUITY) ATTRIBUTABLE TO THE UNITHOLDERS</b>				
		<b>240,968,603</b>	217,263,774	240,664,111
Units in issue (numbers)		<b>2,463,153</b>	2,478,011	2,541,803
Net asset (equity) value per unit – Dealing	<i>18</i>	<b>97.83</b>	87.68	94.68
Net asset (equity) value per unit - IFRS	<i>18</i>	<b>97.83</b>	87.68	94.68

The accompanying notes 1 to 23 form integral part of the financial statements.

The financial statements and accompanying disclosures in the report are approved on behalf of the Fund Board based on the authorization issued on 28 Rajab 1440H (corresponding to 4 April 2019) by:

**Waleed H AlRashed**  
General Manager Asset Management

**Chistie K Moinuddin**  
Chief Financial Officer

**HSBC SAUDI EQUITY INCOME FUND**  
**(An open-ended mutual fund)**  
**Statement of comprehensive income**  
**For the year ended 31 December**  
(Amounts in Saudi Arabian Riyal)

	<i>Note</i>	<u>2018</u>	<u>2017</u>
<b>INVESTMENT INCOME</b>			
Net gains / (losses) from investments at fair value through profit or loss	12	27,308,721	(14,884,804)
Dividend income		12,628,648	11,834,745
<b>TOTAL INCOME</b>		<u>39,937,369</u>	<u>(3,050,059)</u>
<b>EXPENSES</b>			
Management fees	14	4,309,470	3,896,887
Other expenses		2,934	7,713
<b>TOTAL EXPENSES</b>		<u>4,312,404</u>	<u>3,904,600</u>
<b>NET INCOME / (LOSS) FOR THE YEAR</b>		<u>35,624,965</u>	<u>(6,954,659)</u>
Other comprehensive income for the year		--	--
<b>TOTAL COMPREHENSIVE INCOME / (LOSS) FOR THE YEAR</b>		<u>35,624,965</u>	<u>(6,954,659)</u>

The accompanying notes 1 through 23 form an integral part of the financial statements.

The financial statements and accompanying disclosures in the report are approved on behalf of the Fund Board based on the authorization issued on 28 Rajab 1440H (corresponding to 4 April 2019) by:

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**Waleed H AlRashed**  
General Manager Asset Management

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**Chistie K Moinuddin**  
Chief Financial Officer

**HSBC SAUDI EQUITY INCOME FUND**  
**(An open-ended mutual fund)**  
**Statement of changes in net assets (equity) attributable to the unitholders**  
**For the year ended 31 December**  
(Amounts in Saudi Arabian Riyal)

	<u>2018</u>	<u>2017</u>
<b>Net assets (equity) attributable to unit holders at beginning of the year</b>	217,263,774	240,664,111
<b>Net income / (loss) for the year</b>	35,624,965	(6,954,659)
<b>Dividends paid during the year</b>	21 (10,755,394)	(10,649,081)
<i>Contributions and redemptions by the Unitholders:</i>		
Proceeds from issuance of units	9,185,393	441,311
Payments for redemption of units	(10,350,135)	(6,237,908)
Net change from unit transactions	(1,164,742)	(5,796,597)
<b>Net assets value (equity) at end of the year</b>	240,968,603	217,263,774

**UNIT TRANSACTIONS:**

Transactions in units for the year ended 31 December are summarised as follows:

	<u>2018</u>	<u>2017</u>
	<i>(In numbers)</i>	
<b>Units at beginning of the year</b>	2,478,011	2,541,803
Units issued during the year	93,039	4,850
Units redeemed during the year	(107,897)	(68,642)
Net decrease in units	(14,858)	(63,792)
<b>Units as at end of the year</b>	2,463,153	2,478,011

The accompanying notes 1 through 23 form an integral part of the financial statements.

**HSBC SAUDI EQUITY INCOME FUND**  
**(An open-ended mutual fund)**  
**Statement of cash flows**  
**For the year ended 31 December**  
(Amounts in Saudi Arabian Riyal)

	<i>Note</i>	<u>2018</u>	<u>2017</u>
<b>CASH FLOW FROM OPERATING ACTIVITIES</b>			
Net income / (loss) for the year		<b>35,624,965</b>	(6,954,659)
<i>Adjustment to reconcile net income to net cash from operating activities:</i>			
Unrealized (gains) / losses on investments at fair value through profit or loss	12	<u>(44,624,111)</u>	<u>6,963,640</u>
		<b>(8,999,146)</b>	8,981
<b>Net change in operating assets and liabilities</b>			
Decrease in investments at fair value through profit or loss		<b>20,284,204</b>	16,824,963
(Increase) / decrease in receivables and advances		<b>(332,378)</b>	251,139
Increase in accrued expenses	13	<b>412,846</b>	4,783
Increase in dividend payable		<b>730,612</b>	955,917
<b>Net cash generated from operating activities</b>		<u><b>12,096,138</b></u>	<u>18,045,783</u>
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>			
Proceeds from issuance of units		<b>9,185,393</b>	441,311
Payments for redemption of units		<b>(10,350,135)</b>	(6,237,908)
Dividend distributed during the year	21	<b>(10,755,394)</b>	(10,649,081)
<b>Net cash used in financing activities</b>		<u><b>(11,920,136)</b></u>	<u>(16,445,678)</u>
<b>Net increase in cash and cash equivalents</b>		<b>176,002</b>	1,600,105
Cash and cash equivalents at beginning of the year	10	<b>4,493,334</b>	2,893,229
<b>Cash and cash equivalents at end of the year</b>		<u><b>4,669,336</b></u>	<u>4,493,334</u>

The accompanying notes 1 through 23 form an integral part of the financial statements.

**HSBC SAUDI EQUITY INCOME FUND**  
**(An open-ended mutual fund)**  
**Notes to the financial statements**  
**For the year ended 31 December 2018**  
(Amounts in Saudi Arabian Riyal)

**1 GENERAL**

HSBC Saudi Equity Income Fund (“the Fund”), formerly HSBC Saudi Equity Trading Fund, is an open-ended mutual investment fund created through an the agreement between HSBC Saudi Arabia (“the Fund Manager”) and the investors (“the Unitholders”).

The objective of the Fund is to seek capital appreciation and returns from investments in Shariah compliant equities of companies listed on Tadawul (Saudi Stock Market) over the long term.

The Fund is managed by the Fund Manager who also acts the administrator of the Fund. Albilad Capital has been appointed as the custodian of the Fund. All income is reinvested in the Fund and is reflected in the unit price. The Fund distributes income, subject to the approval of the Fund Board, on a semi-annual basis.

**2 REGULATING AUTHORITY**

The Fund is governed by the Investment Fund Regulations (“the Regulations”) detailing requirements for all investments funds operating within the Kingdom of Saudi Arabia and published by the Capital Market Authority (“the CMA”) on 3 Dhul Hijja 1427H (corresponding to 24 December 2006). The Regulations were further amended on 16 Sha’aban 1437H (corresponding to 23 May 2016) (“the Amended Regulations”). The Fund Manager believes that the Amended Regulations was effective since 6 Safar 1438H (corresponding to 6 November 2016).

During the year ended 31 December 2018, the Fund Manager has made certain revisions to the Terms and Conditions of the Fund. The main change in the Terms and Conditions relates to the change in the custodianship. The Fund updated its Terms and Conditions which were approved by the CMA on 20 Muharram 1440H (corresponding to 30 September 2018).

**3 SUBSCRIPTION/ REDEMPTION (DEALING DAY AND VALUATION DAY)**

The Fund is open for subscriptions/ redemptions of units twice weekly on Sunday and Tuesday (each being a “Dealing Day”). The value of the Fund’s portfolio is determined twice weekly on Monday and Wednesday (each being a “Valuation Day”). The net asset value of the Fund for the purpose of purchase or sale of units is determined by dividing the net value of assets (fair value of fund assets minus fund liabilities) by the total number of outstanding fund units on the relevant Valuation Day.

**4 BASIS OF PREPARATION**

The financial statements have been prepared in accordance with the International Financial Reporting Standards (“IFRS”) as endorsed in the Kingdom of Saudi Arabia and other standards and pronouncements issued by Saudi Organization for Certified Public Accountants (“SOCPA”) and to comply with the applicable provisions of the Investment Fund Regulations issued by the Capital Market Authority, the Fund’s Terms and Conditions and the Information Memorandum.

For all periods up to and including the year ended 31 December 2017, the Fund prepared its financial statements in accordance with the generally accepted accounting standards as issued by Saudi Organization of Certified Public Accountants (“SOCPA”). The financial statements for the year ended 31 December 2018 are the first financial statements of the Fund prepared in accordance with IFRS and IFRS 1 “First-time Adoption of International Financial Reporting Standards” has been applied.

An explanation of how the transition to IFRS has affected the reported financial position, financial performance and cash flows of the Fund is provided in note 19.



**HSBC SAUDI EQUITY INCOME FUND**  
**(An open-ended mutual fund)**  
**Notes to the financial statements**  
**For the year ended 31 December 2018**  
(Amounts in Saudi Arabian Riyal)

**5 FUNCTIONAL AND PRESENTATION CURRENCY**

The financial statements are presented in Saudi Riyal (“SR”), which is also the Fund’s functional currency.

**6 BASIS OF MEASUREMENT**

The financial statements have been prepared on a historical cost basis, (except for investments at fair value through profit or loss, “FVTPL” which are stated at their fair value) using the accrual basis of accounting.

The Fund Manager has made an assessment of the Fund’s ability to continue as a going concern and is satisfied that the Fund has the resources to continue in business for the foreseeable future. Furthermore, the Fund Manager is not aware of any material uncertainties that may cast significant doubt upon the Fund’s ability to continue as a going concern. Therefore, the financial statements continue to be prepared on the going concern basis.

The financial statement accounts in the statement of financial position have been presented in the order of liquidity.

**7 USE OF JUDGEMENTS AND ESTIMATES**

Preparation of the financial statements in conformity with IFRS requires the use of certain critical accounting judgements, estimates and assumptions that affect the reported amounts of assets and liabilities. It also requires management to exercise its judgment in the process of applying the Fund’s accounting policies. Such judgements, estimates and assumptions are continually evaluated and are based on historical experience and other factors, including obtaining professional advices and expectations of future events that are believed to be reasonable under the circumstances.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to estimates are recognized prospectively.

**8 SIGNIFICANT ACCOUNTING POLICIES**

The principal accounting policies applied in the preparation of the financial statements are set out below. These policies have been consistently applied to all the years presented, unless otherwise stated. Where policies are applicable only after or before 1 January 2018, those policies have been particularly specified.

***Foreign currency translation***

Transactions in foreign currencies are translated into Saudi Riyal at the exchange rate at the dates of the transactions. Foreign exchange gains and losses arising from translation are included in statement of comprehensive income. Monetary assets and liabilities denominated in foreign currencies are retranslated into Saudi Riyal at the exchange rate at the reporting date. Non-monetary assets and liabilities that are measured at fair value in foreign currencies are also translated into Saudi Riyal at the exchange rate at the reporting date.

Foreign currency differences arising on retranslation are recognised in profit or loss as net foreign exchange gain / (loss), except for those arising on financial instruments at FVTPL, which are recognised as a component of net gain / (loss) from financial instruments at FVTPL.

***Net Asset Value (Equity)***

Net assets value (equity) per unit, as disclosed in the statement of financial position is calculated by dividing the net assets of the Fund by the numbers of units in issue at the year end.

**HSBC SAUDI EQUITY INCOME FUND**  
**(An open-ended mutual fund)**  
**Notes to the financial statements**  
**For the year ended 31 December 2018**  
(Amounts in Saudi Arabian Riyal)

**8 SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

***Subscription and redemption of units***

Units subscribed and redeemed are recorded at net asset value (equity) per unit on the Valuation Day for which the subscription request and redemption applications are received.

***Trade date accounting***

All purchases and sales of financial assets are recognized and derecognized on the trade date, i.e. the date that the Fund commits to purchase or sell the assets. Purchases or sales of financial assets require delivery of those assets within the timeframe generally established by regulation or convention in the market place.

***Revenue recognition***

***Dividend income***

Dividend income is recognized in profit or loss on the date on which the right to receive payment is established. For quoted equity securities, this is usually the ex-dividend date. For unquoted equity securities, this is usually the date on which the shareholders approve the payment of a dividend. Dividend income from equity securities designated as at FVTPL is recognized in the statement of comprehensive income in a separate line item.

***Net gain / (losses) from investments at FVTPL***

Net gains / (losses) from investments at FVTPL includes all realized and unrealized fair value changes and foreign exchange differences (if any), but excludes interest and dividend income, and dividend expense on securities sold short.

Net realized gain from investments at FVTPL is calculated using the weighted average cost method.

***Fund management fees***

Fund management fees are charged at rates agreed with the Fund Manager. These charges are calculated on each Valuation Day at an annual percentage of the Fund's net assets value. These expenses are charged to the statement of income.

***Zakat and income tax***

Under the current system of taxation in Kingdom of Saudi Arabia the Fund is not liable to pay any tax. Zakat and income tax are considered to be the obligation of the Unitholders and are not provided in the accompanying financial statements.

The Value Added Tax (VAT) applicable for fees and expenses are recognized in the statement of comprehensive income.

***Fair value measurement***

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date in the principal or, in its absence, the most advantageous market to which the Fund has access at that date. The fair value of a liability reflects its non-performance risk.

When available, the Fund measures the fair value of an instrument using the quoted price in an active market for that instrument. A market is regarded as active if transactions for the asset or liability take place with sufficient frequency and volume to provide pricing information on an on-going basis. The Fund measures instruments quoted in an active market at a mid-price, because this price provides a reasonable approximation of the exit price.

If there is no quoted price in an active market, then the Fund uses valuation techniques that maximize the use of relevant observable inputs and minimize the use of unobservable inputs. The chosen valuation technique incorporates all of the factors that market participants would take into account in pricing a transaction.

**HSBC SAUDI EQUITY INCOME FUND**  
**(An open-ended mutual fund)**  
**Notes to the financial statements**  
**For the year ended 31 December 2018**  
(Amounts in Saudi Arabian Riyal)

**8. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

*Fair value measurement (continued)*

The Fund recognizes transfers between levels of the fair value hierarchy as at the end of the reporting year during which the change has occurred.

*Financial assets and financial liabilities*

*Policy applicable before 1 January 2018*

*Investments held for trading*

Investment securities purchased for trading are initially recognized at cost on the trade date and are subsequently measured at their market values. The unrealized gains and losses from revaluation of investments held for trading and realized gains and losses from sale of investments held for trading are recognized in the statement of comprehensive income.

*Financial liabilities*

The Fund classifies its financial liabilities at amortised cost. All financial liabilities are recognized initially at fair value less any directly attributable transaction costs. Subsequent to initial recognition, these are measured at amortized cost using the effective interest method.

*Policy applicable from 1 January 2018*

*Recognition and initial measurement*

Financial assets and financial liabilities at FVTPL are initially recognized on the trade date, which is the date on which the Fund becomes a party to the contractual provisions of the instrument. Other financial assets and financial liabilities are recognized on the date on which they are originated.

Financial assets at FVTPL are initially recognized at fair value, with transaction costs recognized in statement of comprehensive income. Financial assets not at FVTPL are initially recognized at fair value plus transaction costs that are directly attributable to their acquisition or issue.

*Financial assets*

*Classification*

On initial recognition, a financial asset is classified as measured at: amortized cost, fair value through other comprehensive income (FVOCI) or fair value through profit or loss (FVTPL).

A financial asset is measured at amortized cost if it meets both of the following conditions and is not designated as at FVTPL:

- the asset is held within a business model whose objective is to hold assets to collect contractual cash flows; and
- the contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

A debt instrument is measured at FVOCI only if it meets both of the following conditions and is not designated as at FVTPL:

- the asset is held within a business model whose objective is achieved by both collecting contractual cash flows and selling financial assets; and
- the contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

**HSBC SAUDI EQUITY INCOME FUND**  
**(An open-ended mutual fund)**  
**Notes to the financial statements**  
**For the year ended 31 December 2018**  
(Amounts in Saudi Arabian Riyal)

**8 SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

*Financial assets (continued)*

On initial recognition of an equity investment that is not held for trading, the Fund may irrevocably elect to present subsequent changes in fair value in other comprehensive income. This election is made on an investment-by-investment basis.

All other financial assets are classified as measured at FVTPL.

*Business model assessment*

The Fund makes an assessment of the objective of a business model in which an asset is held at a portfolio level because this best reflects the way the business is managed and information is provided to management. The information considered includes:

- the stated policies and objectives for the portfolio and the operation of those policies in practice. In particular, whether management's strategy focuses on earning contractual commission revenue, maintaining a particular interest rate profile, matching the duration of the financial assets to the duration of the liabilities that are funding those assets or realizing cash flows through the sale of the assets;
- how the performance of the portfolio is evaluated and reported to the Fund's managers;
- the risks that affect the performance of the business model (and the financial assets held within that business model) and how those risks are managed;
- how managers of the business are compensated – e.g. whether compensation is based on the fair value of the assets managed or the contractual cash flows collected; and
- the frequency, volume and timing of sales in prior periods, the reasons for such sales and its expectations about future sales activity. However, information about sales activity is not considered in isolation, but as part of an overall assessment of how the Funds' stated objective for managing the financial assets is achieved and how cash flows are realized.

Financial assets that are held for trading or managed and whose performance is evaluated on a fair value basis are measured at FVTPL because they are neither held to collect contractual cash flows nor held both to collect contractual cash flows and to sell financial assets.

*Assessment whether contractual cash flows are solely payments of principal and interest*

For the purposes of this assessment, 'principal' is defined as the fair value of the financial asset on initial recognition. 'Commission / Interest' is defined as consideration for the time value of money and for the credit risk associated with the principal amount outstanding during a particular period of time and for other basic lending risks and costs (e.g. liquidity risk and administrative costs), as well as profit margin.

In assessing whether the contractual cash flows are solely payments of principal and interest, the Fund considers the contractual terms of the instrument. This includes assessing whether the financial asset contains a contractual term that could change the timing or amount of contractual cash flows such that it would not meet this condition. In making the assessment, the Fund considers:

- contingent events that would change the amount and timing of cash flows;
- leverage features;
- prepayment and extension terms;
- terms that limit the Fund's claim to cash flows from specified assets (e.g. non-recourse asset arrangements); and
- features that modify consideration of the time value of money – e.g. periodical reset of interest rates.

*Reclassifications*

Financial assets are not reclassified subsequent to their initial recognition, except in the year after the Fund changes its business model for managing financial assets.

**HSBC SAUDI EQUITY INCOME FUND**  
**(An open-ended mutual fund)**  
**Notes to the financial statements**  
**For the year ended 31 December 2018**  
(Amounts in Saudi Arabian Riyal)

**8 SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

*Financial assets (continued)*

***Derecognition***

The Fund derecognizes a financial asset when the contractual rights to the cash flows from the financial asset expire, or it transfers the rights to receive the contractual cash flows in a transaction in which substantially all of the risks and rewards of ownership of the financial asset are transferred or in which the Fund neither transfers nor retains substantially all of the risks and rewards of ownership and it does not retain control of the financial asset.

On derecognition of a financial asset, the difference between the carrying amount of the asset (or the carrying amount allocated to the portion of the asset derecognized) and the sum of (i) the consideration received (including any new asset obtained less any new liability assumed) and (ii) any cumulative gain or loss that had been recognized in OCI is recognized in profit or loss. Transactions in which the Fund neither retains nor transfers substantially all of the risks and rewards of ownership of a financial asset and it retains control over the asset, the Fund continues to recognize the asset to the extent of its continuing involvement, determined by the extent to which it is exposed to changes in the value of the transferred asset.

***Offsetting***

Financial assets and financial liabilities are offset and the net amount presented in the statement of financial position when, and only when, the Fund currently has a legally enforceable right to set off the amounts and it intends either to settle them on a net basis or to realize the asset and settle the liability simultaneously.

Income and expenses are presented on a net basis only when permitted under IFRS, or for gains and losses arising from a Fund of similar transactions such as in the Fund's trading activity.

***Cash and cash equivalents***

Cash and cash equivalents comprise deposits with banks and highly liquid financial assets with maturities of three months or less from the date of acquisition that are subject to an insignificant risk of changes in their fair value and are used by the Fund in the management of short-term commitments, other than cash collateral provided in respect of derivatives and securities borrowing transactions.

***Redeemable units***

The redeemable units are as equity instruments as they meet certain strict criteria. Those criteria include:

- the redeemable units must entitle the holder to a pro-rata share of net assets;
- the redeemable units must be the most subordinated class and class features must be identical;
- there must be no contractual obligations to deliver cash or another financial asset other than the obligation on the issuer to repurchase; and
- the total expected cash flows from the redeemable units over its life must be based substantially on the profit or loss of the issuer.

**HSBC SAUDI EQUITY INCOME FUND**  
**(An open-ended mutual fund)**  
**Notes to the financial statements**  
**For the year ended 31 December 2018**  
(Amounts in Saudi Arabian Riyal)

**9 STANDARDS ISSUED BUT NOT YET EFFECTIVE**

A number of amendments and standards are effective for the period beginning on or after 1 January 2019 and earlier application is permitted; however, the Fund has not early applied these new amendments and standards in preparing the financial statements as these do not have material impact on the Fund's financial statements.

**10 CASH AND CASH EQUIVALENTS**

Cash and cash equivalents balance comprise of cash with banks who have investment grade credit ratings, as rated by the international rating agencies.

**11 INVESTMENTS AT FAIR VALUE THROUGH PROFIT OR LOSS**

Investments comprise the following sector exposures as at statement of financial position:

<i>Sector</i>	<i>31 December 2018</i>		<i>31 December 2017</i>		<i>1 January 2017</i>	
	<i>Cost</i>	<i>Fair value</i>	<i>Cost</i>	<i>Fair value</i>	<i>Cost</i>	<i>Fair value</i>
Materials	<b>76,366,614</b>	<b>91,377,420</b>	66,931,301	75,787,916	98,108,716	100,674,389
Banks	<b>48,359,621</b>	<b>60,138,830</b>	37,271,144	37,041,153	8,961,192	8,780,929
Telecommunication Services	<b>15,923,115</b>	<b>24,731,930</b>	16,061,181	18,641,844	16,985,872	21,588,921
Retailing	<b>14,177,576</b>	<b>23,042,896</b>	13,663,638	16,303,820	14,090,312	13,229,646
Real Estate Mgmt. & Dev.	<b>21,561,820</b>	<b>19,505,497</b>	13,159,424	12,616,418	13,159,424	15,381,753
Commercial & Prof. Services	--	--	26,420,306	16,176,443	26,420,306	20,796,268
Transportation	<b>7,179,477</b>	<b>7,254,208</b>	14,036,007	11,371,675	14,036,007	19,138,897
Capital Goods	--	--	6,276,712	6,476,422	17,484,508	15,398,202
Health Care Equip. & Svc.	--	--	4,815,099	5,270,129	4,815,099	4,951,407
Insurance	--	--	10,445,362	10,329,437	--	--
Diversified Financials	--	--	6,677,385	5,089,276	--	--
Energy	--	--	--	--	8,703,420	11,587,293
Food & Beverage	<b>11,905,131</b>	<b>13,393,661</b>	--	--	9,817,663	7,365,431
<b>Total</b>	<b>195,473,354</b>	<b>239,444,442</b>	215,757,559	215,104,533	232,582,519	238,893,136

**12 NET GAIN / (LOSS) FROM INVESTMENTS AT FAIR VALUE THROUGH PROFIT OR LOSS**

	<i>2018</i>	<i>2017</i>
Realised loss during the year	<b>(17,315,390)</b>	(7,921,164)
Unrealised gain / (loss) during the year	<b>44,624,111</b>	(6,963,640)
<b>Total</b>	<b>27,308,721</b>	(14,884,804)

Realized gain on investments at FVTPL is calculated based on weighted average cost of securities.

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**13 ACCRUED EXPENSES**

Accrued expenses include management fee payable (inclusive of VAT) to the Fund Manager.

**14 TRANSACTIONS WITH RELATED PARTIES**

Parties are considered to be related if one party has the ability to control the other party or exercise significant influence over the other party in making financial or operational decisions. In considering each possible related party relationship, attention is directed to the substance of the relationship, not merely the legal form

Related parties of the Fund comprise HSBC Saudi Arabia (being the Fund Manager, custodiana and administrator of the Fund), the Fund Board and The Saudi British Bank (“SABB”) (being significant shareholder of the Fund Manager).

In the ordinary course of its activities, the Fund transacts business with related parties. Related party transactions are governed by limits set by the regulations issued by CMA. All the related party transactions are undertaken at mutually agreed prices and approved by the Fund Manager. These transactions were carried out on the basis of approved terms and conditions of the Fund

The Fund Manager charges to the Fund on each Valuation Day, management fees at a rate of 1.7% of Net assets value (2017: 1.7% of Net assets value). All Fees and expenses related to the management of the Fund including but not limited to custody, administration, audit, regulatory and index fees, etc., are included in the management fee.

Subscription fee up to 2% is not considered in the financial statement of the Fund, as investment to the Fund are always net of subscription fees.

During the year, the Fund entered into the following transactions with related parties in the ordinary course of business.

Related party	Nature of transactions	Amount of transaction during the year		Payable	
		<u>2018</u>	<u>2017</u>	<u>2018</u>	<u>2017</u>
HSBC Saudi Arabia (Fund Manager)	Fund management fee	<b>4,309,470</b>	3,896,887	<b>473,513</b>	60,666
SABB	Cash and cash equivalents	--	--	--	4,493,334

Board member compensation and other expenses such as custodian fee and administration fee during the year has been borne and paid by HSBC Saudi Arabia (*“the Fund Manager”*).

No special commission is receivable against the cash balances in the respective bank accounts with the related parties.

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**15. CLASSIFICATION OF FINANCIAL ASSETS AND FINANCIAL LIABILITIES**

The table below sets out the classifications of the carrying amounts of the Fund's financial assets and financial liabilities into categories of financial instruments:

<u>31 December 2018</u>	<u>Amortized cost</u>	<u>FVTPL</u>
Cash and cash equivalents	4,669,336	--
Investments	--	239,444,442
Receivables and advances	391,280	--
<b>Total financial assets</b>	<b>5,060,616</b>	<b>239,444,442</b>
Accrued expenses	473,513	--
Dividend payable	3,062,942	--
<b>Total financial liabilities</b>	<b>3,536,455</b>	<b>--</b>
	<i>Loans and receivables / Amortized cost</i>	<i>Held for trading</i>
<u>31 December 2017</u>	<u>Amortized cost</u>	<u>Held for trading</u>
Cash and cash equivalents	4,493,334	--
Investments	--	215,104,533
Receivables and advances	58,902	--
<b>Total financial assets</b>	<b>4,552,236</b>	<b>215,104,533</b>
Accrued expenses	60,666	--
Dividend payable	2,332,329	--
<b>Total financial liabilities</b>	<b>2,392,995</b>	<b>--</b>
	<i>Loans and receivables / Amortized cost</i>	<i>Held for trading</i>
<u>1 January 2017</u>	<u>Amortized cost</u>	<u>Held for trading</u>
Cash and cash equivalents	2,893,229	--
Investments	--	238,893,136
Receivables and advances	310,041	--
<b>Total financial assets</b>	<b>3,203,270</b>	<b>238,893,136</b>
Accrued expenses	55,883	--
Dividend payable	1,376,412	--
<b>Total financial liabilities</b>	<b>1,432,295</b>	<b>--</b>



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**16. FINANCIAL RISK MANAGEMENT**

The Fund has exposure to the following risks from financial instruments:

- credit risk;
- liquidity risk;
- market risks; and
- operational risk

This note presents information about the Fund's objectives, policies and processes for measuring and managing risk, and the Fund's management of capital.

***Risk management framework***

The Fund maintains positions in non-derivative financial instruments in accordance with its investment management strategy. The Fund's investment portfolio comprises of listed equities.

The Fund's investment manager has been given discretionary authority to manage the assets in line with the Fund's investment objectives. Compliance with the target asset allocations and the composition of the portfolio are monitored by the Fund Board. In instances where the portfolio has diverged from target asset allocations, the Fund's investment manager is obliged to take actions to rebalance the portfolio in line with the established targets, within prescribed time limits.

***Credit risk***

Credit risk is the risk that a counterparty to a financial instrument will fail to discharge an obligation or commitment that it has entered into with the Fund, resulting in a financial loss to the Fund.

The Fund is exposed to credit risk on its bank balance and balance held in trading account. For risk management reporting purposes, the Fund considers and aggregates all elements of credit risk exposure such as individual obligor default risk, country risk and sector risk.

The Fund's policy over credit risk is to minimize its exposure to counterparties with perceived higher risk of default by dealing only with counterparties that meet the certain credit standards.

Credit risk is monitored on a regular basis by the Fund Manager to ensure it is in line with the investment guidelines of the Fund Board.

The Fund's activities may give rise to settlement risk. 'Settlement risk' is the risk of loss due to the failure of an entity to honor its obligations to deliver cash, securities or other assets as contractually agreed.

For all of transactions, the Fund mitigates this risk by conducting settlements through a regulated broker to ensure that a trade is settled only when both parties have fulfilled their contractual settlement obligations.

The table below shows the maximum exposure to credit risk for the component of the statement of financial position:

	<i>31 December 2018</i>	<i>31 December 2017</i>	<i>1 January 2017</i>
Cash and cash equivalents	<b>4,669,336</b>	4,493,334	2,893,229
Receivables and advances	<b>391,280</b>	58,902	310,041
<b><i>Total exposure to credit risk</i></b>	<b><u>5,060,616</u></b>	<u>4,552,236</u>	<u>3,203,270</u>

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**16 FINANCIAL RISK MANAGEMENT (CONTINUED)**

***Credit risk (continued)***

The Fund does not have a formal internal grading mechanism. Credit risk is managed and controlled by monitoring credit exposures, limiting transactions with specific counterparties and continually assessing the creditworthiness of counterparties. Credit risks are generally managed on the basis of external credit ratings of the counterparties.

**Analysis of credit quality**

The Fund's cash and cash equivalents are held with The Saudi British Bank and Bank Albilad, which are rated A1 and A3 (2017: A1 and A3) respectively based on Moody's ratings.

**Allowance for expected credit loss**

The Fund does not have any impairment of assets, so no impairment allowance is provided in the financial statements. Financial instruments such as, cash and cash equivalents and Receivables and Advances are of short term in nature and have limited credit exposure.

***Liquidity risk***

Liquidity risk is the risk that the Fund will encounter difficulty in releasing funds to meet commitments associated with financial liabilities.

The Fund's Terms and Conditions provide for the subscriptions and redemptions of units throughout the week and it is, therefore, exposed to the liquidity risk of meeting unitholders redemptions. However the fund is allowed to borrow in order to satisfy redemptions. The Fund's securities are considered to be readily realizable as they are all listed on Saudi stock markets. The Fund Manager monitors the liquidity requirements on a regular basis and seeks to ensure that sufficient funds are available to meet any commitments as they arise.

***Market risk***

Market Risk is the risk that changes in market prices – such as foreign exchange rates and equity prices – will affect the Fund's income or the fair value of its holdings in financial instruments.

The Fund's strategy for the management of market risk is driven by the Fund's investment objective as per the Fund's Terms and Conditions. The Fund's market risk is managed on a timely basis by the investment manager in accordance with the policies and procedures in place. The Fund's market positions are monitored on a timely basis by the fund manager.

**Equity price risk**

Equity price risk is the risk that the value of financial instruments will fluctuate because of changes in market prices.

The Fund's investments are susceptible to market price risk arising from uncertainties about future prices. The Fund Manager manages this risk through diversification of its investment portfolio in terms of geographical distribution and industry concentration.

**Sensitivity analysis**

The table below sets out the effect on net assets attributable to Unitholders of a reasonably possible weakening / strengthening in the individual equity market prices of 5% at reporting date. The estimates are made on an individual investment basis. The analysis assumes that all other variables, in particular interest and foreign currency rates, remain constant.

	<u>2018</u>		<u>2017</u>	
<b><i>Net gain / (loss) on investments held at FVTPL</i></b>	<b>+ 5%</b>	<b>11,972,222</b>	+ 5%	10,755,227
	<b>- 5%</b>	<b>(11,972,222)</b>	- 5%	(10,755,227)

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**16 FINANCIAL RISK MANAGEMENT (CONTINUED)**

*Market risk (continued)*

Currency risk

Currency risk is the risk that the value of a financial instrument will fluctuate due to a change in foreign exchange rates. The Fund is not subject to currency risks as all the assets and liabilities of the Fund are denominated in local currency. The investment risks of the fund are included in the Terms and Conditions detailed on the website of the Fund Manager at [www.hsbcSaudi.com](http://www.hsbcSaudi.com). The Terms and Conditions do not form part of the financial statements.

*Operational risk*

Operational risk is the risk of direct or indirect loss arising from a wide variety of causes associated with the processes, technology and infrastructure supporting the Fund's activities with financial instruments, either internally within the Fund or externally at the Fund's service providers, and from external factors other than credit, market and liquidity risks such as those arising from legal and regulatory requirements and generally accepted standards of investment management behavior.

The Fund's objective is to manage operational risk so as to balance limiting of financial losses and damage to its reputation with achieving its investment objective of generating returns to unitholders.

The primary responsibility for the development and implementation of control over operational risks rests with the Risk Management Team. This responsibility is supported by the development of overall standard for the management of operational risk, which encompasses the controls and processes at the service providers and the establishment of service levels with the service providers, in the following areas:

- documentation of controls and procedures
- requirements for
  - appropriate segregation of duties between various functions, roles and responsibilities;
  - reconciliation and monitoring of transactions; and
  - periodic assessment of operational risks faced,
- the adequacy of controls and procedures to address the risks identified;
- compliance with regulatory and other legal requirements;
- development of contingency plans;
- training and professional development;
- ethical and business standards; and
- risk mitigation, including insurance if this is effective

**17 FAIR VALUES OF FINANCIAL INSTRUMENTS**

The Fund measures certain financial instruments at fair value at each statement of financial position date.

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The fair value measurement is based on the presumption that the transaction to sell the asset or transfer the liability takes place either:

- In the principal market for the asset or liability; or
- In the absence of a principal market, in the most advantageous market for the asset or liability.

The principal or the most advantageous market must be accessible by the Fund. The fair value of an asset or a liability is measured using the assumptions that market participants would use when pricing the asset or liability, assuming that market participants act in their economic best interest. The Fund uses valuation techniques that are appropriate in the circumstances and for which sufficient data are available to measure fair value, maximising the use of relevant observable inputs and minimising the use of unobservable inputs. Changes in assumptions about these factors could affect the fair value of financial instruments.

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**17 FAIR VALUES OF FINANCIAL INSTRUMENTS (CONTINUED)**

Valuation models

The fair values of financial instruments that are traded in active markets are based on prices obtained directly from an exchange on which the instruments are traded or obtained from a broker that provides an unadjusted quoted price from an active market for identical instruments. For all other financial instruments, the Fund determines fair values using other valuation techniques.

For financial instruments that trade infrequently and have little price transparency, fair value is less objective and requires varying degrees of judgment depending on liquidity, uncertainty of market factors, pricing assumptions and other risks affecting the specific instrument.

The Fund measures fair values using the following fair value hierarchy that reflects the significance of the inputs used in making the measurements.

Level 1: Inputs that are quoted market prices (unadjusted) in active markets for identical instruments.

Level 2: Inputs other than quoted prices included within Level 1 that are observable either directly (i.e. as prices) or indirectly (i.e. derived from prices). This category includes instruments valued using: quoted market prices in active markets for similar instruments; quoted prices for identical or similar instruments in markets that are considered less than active; or other valuation techniques in which all significant inputs are directly or indirectly observable from market data.

Level 3: Inputs that are unobservable. This category includes all instruments for which the valuation technique includes inputs not based on observable data and the unobservable inputs have a significant effect on the instrument's valuation. This category includes instruments that are valued based on quoted prices for similar instruments but for which significant unobservable adjustments or assumptions are required to reflect differences between the instruments.

The Fund values equity securities that are traded on an approved stock exchange at their last reported prices. To the extent that equity securities are actively traded and valuation adjustments are not applied, they are categorized in Level 1 of the fair value hierarchy, hence the Fund's assets recorded at fair value have been categorized based on fair value hierarchy Level 1.

Fair value hierarchy – Financial instruments measured at fair value

The table below analyses financial instruments measured at fair value at the reporting date by the level in the fair value hierarchy into which the fair value measurement is categorized. The amounts are based on the values recognised in the statement of financial position.

	Carrying value	31 December 2018			Total
		-----Fair value-----			
		Level 1	Level 2	Level 3	
Investments at FVTPL	239,444,442	239,444,442	--	--	239,444,442
Total	239,444,442	239,444,442	--	--	239,444,442

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**17 FAIR VALUES OF FINANCIAL INSTRUMENTS (CONTINUED)**

	Carrying value	31 December 2017			
		-----Fair value-----			
		Level 1	Level 2	Level 3	Total
Held for trading investment	215,104,533	215,104,533	--	--	215,104,533
<b>Total</b>	<b>215,104,533</b>	<b>215,104,533</b>	<b>--</b>	<b>--</b>	<b>215,104,533</b>

  

	Carrying value	1 January 2017			
		-----Fair value-----			
		Level 1	Level 2	Level 3	Total
Held for trading investments	238,893,136	238,893,136	--	--	238,893,136
<b>Total</b>	<b>238,893,136</b>	<b>238,893,136</b>	<b>--</b>	<b>--</b>	<b>238,893,136</b>

During the year, there has been no transfer in fair value hierarchy for the financial assets held at fair value through profit or loss.

Other financial instruments include items such as, cash and cash equivalents, receivable and advances, accrued expenses and dividend payable. These are short-term financial assets and financial liabilities whose carrying amounts approximate fair value, because of their short-term nature and the high credit quality of counterparties.

**18 LAST VALUATION DAY**

The last valuation day of the year was 31 December 2018 (2017: 31 December 2017) and the dealing net assets value on this day was SR 97.83 per unit (2017: 87.68). The IFRS net assets value per unit on 31 December 2018 was SR 97.83.

**19 EXPLANATION OF TRANSITION TO IFRS**

As stated in note 4, these are the Fund's first financial statements prepared in accordance with IFRS as endorsed in the Kingdom of Saudi Arabia and other standards and pronouncements issued by SOCPA.

The accounting policies set out in note 8 have been applied in preparing the financial statements for the year ended 31 December 2018, the comparative information presented in the financial statements for the year ended 31 December 2017 and in the preparation of an opening IFRS statement of financial position at 1 January 2017 (the Fund's date of transition) except for IFRS 9 as disclosed in note 20.

The transition from previous GAAP i.e. generally accepted accounting standards in the Kingdom of Saudi Arabia as issued by SOCPA to IFRSs as endorsed in the Kingdom of Saudi Arabia had no significant impact on the Fund's financial position, comprehensive income, and statement of changes in net assets attributable to the Unitholders and cash flows and hence no further reconciliation statements have been provided.

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**20 IMPACT OF CHANGE IN ACCOUNTING POLICIES**

Adoption of IFRS 9 “Financial Instruments” (IFRS 9)

The Fund has adopted IFRS 9 with date of transition of 1 January 2018, opting to apply exemption allowed under IFRS 1 “First-time Adoption of International Financial Reporting Standards” from retrospective application. Accordingly, comparative information has been presented under the previous GAAP.

The assessment relating to determination of business model within which a financial instrument is held and classification and measurements of all of the Fund’s financial instruments have been made based on the facts and circumstances that existed at the date of transition.

As all of the Fund’s investments are either held for trading and/or managed and evaluated on a fair value basis, they have remained classified as fair value through profit or loss (FVTPL) upon adoption of IFRS 9. Therefore, transition to IFRS 9 has not resulted in any change to the classification or measurement of investments, in the current year. Accordingly, no separate reconciliation statement is prepared to reconcile the financial position balances from previous GAAP to IFRS 9.

The following table shows the original measurement categories in accordance with previous GAAP and the new measurement categories under IFRS 9 for the Fund’s financial instruments as at 1 January 2018:

	<b>Classification under previous GAAP</b>	<b>New classification under IFRS 9</b>	<b>Original carrying value under previous GAAP</b>	<b>New carrying value under IFRS 9</b>
<b><i>Financial assets</i></b>				
Cash and cash equivalents	Loans and receivables	Amortized cost	4,493,334	4,493,334
Receivables and advances	Loans and receivables	Amortized cost	58,902	58,902
Investments	Held for Trading	FVTPL	215,104,533	215,104,533
<b><i>Financial liabilities</i></b>				
Accrued expenses	Amortized cost	Amortized cost	60,666	60,666
Dividend payable	Amortized cost	Amortized cost	2,332,329	2,332,329

**21 DIVIDEND DISTRIBUTION**

In accordance with the terms & conditions of the Fund, the Fund Board made the following dividend distributions out of the fund during the year:

	<b>2018</b>	<b>2017</b>
1 <sup>st</sup> dividend at a rate of SR 1.25 (2017: SR 1.25) per unit	3,058,444	3,160,436
2 <sup>nd</sup> dividend at a rate of SR 3.1 (2017: SR 3.00) per unit	7,696,950	7,488,645
	<b>10,755,394</b>	<b>10,649,081</b>

**22 SUBSEQUENT EVENT**

There were no events subsequent to the statement of financial position date which require adjustments of or disclosure in the financial statements or notes thereto.

**23 APPROVAL OF FINANCIAL STATEMENTS**

The financial statements were approved by the Fund Manager on 28 Rajab 1440H (corresponding to 4 April 2019).