

GIB Capital LLC

# Pillar III Disclosures

Year ended 31 December 2016

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## 1. OVERVIEW

GIB Capital LLC (hereinafter referred to as “**GIBC**” or “**the Company**”) is a limited liability company registered in the Kingdom of Saudi Arabia under commercial registration number 1010244294 dated 6 Safar 1429H (corresponding to 14 February 2008G) with a paid up capital of SAR 200 million.

GIBC is authorised by the Capital Market Authority (“**CMA**”) under license number 07078-37 dated 8 Rajab 1428H (corresponding to 22 July 2007G) to provide a full range of financial services including dealing as a principal, underwriting, managing, arranging, advising and acting as custodian of financial securities.

The Pillar III disclosures relate to GIBC for the year ended 31 December 2016 and are being made in line with CMA’s Prudential Rules. GIBC believes that these disclosures will enable readers to assess the Company’s capital, risk exposures, risk assessment processes and consequently its capital adequacy and promote comparability among Authorised Persons (APs).

## 2. SCOPE OF APPLICATION

### 2.1 Pillar I – Minimum capital requirements

Pillar I describes the minimum capital requirements for credit, market and operational risks. Various approaches are available to determine the minimum capital requirements under Pillar I. The choice of an appropriate approach will depend on the capability of the systems and its suitability to the AP’s business. The Company calculates the minimum capital requirements for credit, market and operational risks as per the provisions of Part 3 of the Prudential Rules.

GIBC applies the standardised approach to calculate the capital required for credit risk. The capital requirements for market risk is calculated separately for each category within this risk type (i.e. interest rate, equity price and foreign exchange) and then aggregated. As a starting point, GIBC uses the basic indicator approach to determine capital required for its operational risks. This approach calculates capital at 15% of the average operating income for the last three years. However, to meet the provisions of the Prudential Rules, GIBC ensures that the capital required for operational risk is maintained at least at 25% of its overhead expenses as laid down under the expenditure based approach.

### 2.2 Pillar II – Internal Capital Adequacy Assessment Process (ICAAP)

Pillar II requires all APs to conduct an assessment of all risks faced by them in their business with a view to ensuring that they hold adequate capital against these risks, after taking into account appropriate risk mitigants. This assessment has to be comprehensive, done annually and should be commensurate with the nature, scale and complexity of the AP’s activities. The range of risks covered in this assessment include liquidity, concentration, reputation and strategic and goes beyond the Pillar I requirement of credit, market and operational risks. Such assessment will usually be documented in an ICAAP which has to be filed with CMA on an annual basis.

### 2.3 Pillar III – Disclosure and reporting

This part of the Prudential Rules requires a comprehensive and consistent disclosure and reporting framework that allows for comparison among APs while enhancing the risk management practices. This part shows the calculation of capital base, minimum capital requirements and large exposures in accordance with the capital adequacy model and is consistent with the capital adequacy information reported in the notes to the Company’s audited financial statements. The qualitative and quantitative information presented here are in accordance with the regulations currently in force and have been reviewed and validated by the senior management. This document has been approved by GIBC Board of directors.

In line with CMA requirements, GIBC publishes its Pillar III disclosures on its website [www.gibcapital.com](http://www.gibcapital.com).

### 2.4 Material or legal impediments

Since GIBC does not have any subsidiaries there are no material or legal impediments to the prompt transfer of capital or repayment of liabilities. Accordingly, the figures presented in this report are on a Company only basis.

## 3. CAPITAL STRUCTURE

The Company’s capital structure is typically divided into Tier 1 capital and Tier 2 capital from a regulatory perspective. While the Tier 1 capital comprises paid up share capital, reserves (excluding revaluation reserve) and audited retained earnings, the Tier 2 capital usually consists of subordinated loan and is limited to an amount equivalent to 50% of Tier 1 capital.

The Company’s capital base as of 31 December 2016 is summarised in the table below:

Description	SAR ‘000
<b>Tier 1 Capital</b>	
Paid up capital	200,000
Reserves (excluding revaluation reserve)	3,768
Retained earnings	13,165
Unrealised loss on investments held for trading	(166)
<b>Total Tier 1 Capital (a)</b>	<b>216,767</b>
<b>Tier 2 Capital</b>	
<b>Total Tier 2 Capital (b)</b>	<b>-</b>
<b>TOTAL CAPITAL BASE (a) + (b)</b>	<b>216,767</b>

The Company repaid its subordinated loan in 2016 and hence does not have Tier 2 Capital at the year end.

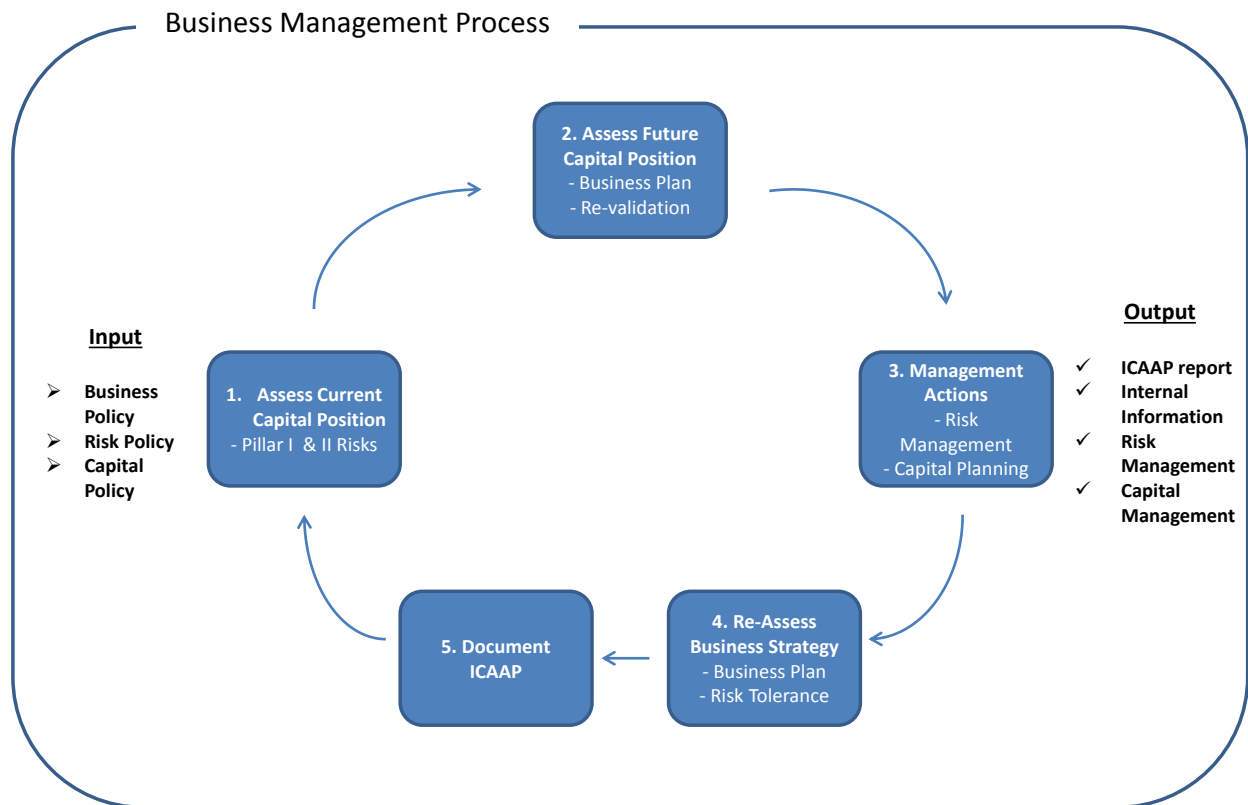
#### 4. CAPITAL ADEQUACY

GIBC assesses its capital adequacy at all times in line with CMA’s Prudential Rules. This assessment takes into account the inherent risks in GIBC’s nature of business as well as its current and future business activity levels.

GIBC strives to maintain a balanced capital base that is consistent with its business operations, growth plans and to address potential extreme stress conditions. The regulatory requirements for capital adequacy always underpin GIBC’s assessment of its capital base.

In line with section 2.2 above, GIBC has developed an ICAAP framework that supports its capital adequacy assessment. The framework takes into account the risk profile of the Company both from a regulatory perspective and its internal risk exposure and appetite. The ICAAP describes the Company’s assessment of the level of capital that the Company’s Board considers adequate to cover the various risks to which the Company is, and could be, exposed in the short to medium term. This assessment takes into account the Company’s forecasted activity and financial position over a three year horizon. Material risks are identified and assessed in accordance with the Prudential Rules as well as through extensive management discussions. The ICAAP framework forms a critical part of the Company’s strategic decision making and risk management process.

The Company’s ICAAP process follows four primary steps:



The Company's ICAAP is reviewed in detail by the senior management for adequacy of capital and approved by the Board of Directors on an annual basis. This review process resulted in the Company increasing its share capital, during 2014, by SAR 140 million (Tier 1 capital) and, initially, also having a subordinated loan facility of SAR 150 million in place. The subordinated loan which was reduced to SAR 100 million in 2015, has since been fully repaid before the end of 2016. The surplus in capital base of SAR 187 million, as described subsequently, enhances GIBC's equity underwriting capabilities as well as its ability to increase its exposure to investments held for trading portfolio.

The Company's capital adequacy assessment also includes the provision of buffers to address additional capital requirements for non-specific, unexpected and unidentified risks. They also relate to growth and new initiatives expected to be pursued to reach the set strategic goals. The introduction of new products and services generally take account of increased exposure to new markets, products and added complexity, leading to additional capital requirement.

As shown below, at 31 December 2016, GIBC is well capitalised with a capital adequacy ratio of 7.29x (versus a CMA minimum capital ratio requirement of 1.0x) and a surplus capital over the minimum requirement in line with CMA regulations of SAR 187 million.

The table below summarises the Company's capital adequacy position as of 31 December 2016:

Description	SAR '000
Tier 1 capital	216,767
Tier 2 capital	-
<b>Total capital base (a)</b>	<b>216,767</b>
Capital required for credit risk	21,366
Capital required for market risk	42
Capital required for operational risk	8,325
<b>Minimum capital requirement (b)</b>	<b>29,732</b>
<b>Total capital ratio</b>	<b>7.29x</b>
<b>Surplus in capital base (a) – (b)</b>	<b>187,035</b>

## 5. RISK MANAGEMENT

The management of risk is an essential element of the Company's business. A key tenet of the risk management culture of GIBC (and Gulf International Bank B.S.C. ["GIB" or "the parent bank"], the Group to which the Company belongs) is the clear segregation of duties and reporting lines between personnel transacting business and personnel processing those business activities. The GIBC and GIB Group's risk management is underpinned by their ability to identify, measure, aggregate and manage the different types of risk they face. In addition to its own processes, the Company adheres to the GIB Group risk management practices to effectively manage its risks.

### 5.1 Risk management strategy and processes

The Company maintains a prudent and disciplined approach to risk taking by maintaining a set of policies and processes applied throughout the Company's activities, under a Corporate Policy Manual, with an appropriate framework of governance and oversight. The Company management reports to the Board of Directors, which is the highest Governing Body. The Company actively promotes a culture of sound risk management at all levels by employing professional, qualified and suitably experienced people with appropriate skills and by providing appropriate training.

The Company's primary asset is a bank deposit maintained with the parent bank with minimal investment exposures. To manage these exposures, the Company has in place suitable strategies and processes to maintain adequate capital, considering the nature and projected level of the risk exposure. The operations of the Company are subject to regular independent review by Internal Audit, which is outsourced to GIB through a service level agreement, and the Audit Committee.

The Company's management regularly and methodically addresses the risk surrounding its business activities by continuously focusing on its client base. It places emphasis on creating a risk awareness culture and considers this to be a highly effective way to minimize unexpected losses and by maintaining a highly client focused approach in its business dealings. Regular and pro-active consultation with regulators reinforces this risk management approach in which the reputational risk is considered to be the most significant risk element.

The risk management control process is managed on a global basis by the GIB Group and is based on a detailed structure of the Group's policies and procedures and comprehensive risk management for the identification, control, monitoring and reporting of risks. The risk management framework is guided by an evaluation of risk appetite (expressed in terms of business), risk oversight, independent of business units and a thorough risk assessment.

Key Strategy and Investment Policies are documented and approved by the Board of Directors. The Strategy and Policies, among others, include:

- The overall governance structure
- Key roles and responsibilities

- Key risk management processes
- The authorities for entering into this risk

As part of the risk management process, the Company's management is required to obtain the prior approval of the GIB Group Investment Committee plus the GIBC Chairman (together "**the GIBC Investment Committee**") before underwriting any equity exposure or buying a 'held for trading' investment. As part of this approval process the GIBC Investment Committee provides clear guidelines for the holding period, exposure limits and a portfolio management plan for subsequent unwinding of these exposures. The Company's management is required to update the GIBC Investment Committee on a regular basis about these exposures in case there are deviations to the approval terms.

Further, there are two support units which follow up on the implementation of the Company's overall risk management process. They are Internal Audit and Compliance.

#### **Internal Audit**

The role of Internal Audit is to provide independent assurance to the Company's Board of Directors on the effectiveness of the risk management, control and governance processes as dictated by the GIB Group. It does this by carrying out a series of risk based audits, which are designed to cover all the material risks that arise from the Company's activities and to provide assurance that the Company's assets are safeguarded. This involves ensuring that controls are in place and working effectively in accordance with Company policies and procedures as well as with laws and regulations. In addition, when required, Internal Audit performs special investigations and may, from time to time, undertake work requested by regulators. The Audit Committee approves the annual audit plan and also receives regular reports of the results of audit work.

The Internal Audit personnel belonging to the GIB Group, the outsourced service provider, report to the Group Chief Auditor.

#### **Compliance**

The Company has a formally structured Compliance function which reports into the Chief Executive Officer. A formal risk based assessment of regulatory and compliance risks forms the basis of the annual Compliance Monitoring Plan, which identifies the risks to be monitored, and with frequency of monitoring determined by an assessment of the probability and likely impact of those risks occurring.

The Company's policy is to maintain a strong capital base so as to maintain creditor and market confidence and to sustain future business development. The Company manages its capital structure and makes adjustments to the structure taking account of changes in economic conditions and strategic business plans approved by the Board of Directors. The capital structure may be adjusted through the issuance of new shares or dividend payout.



## 5.2 Major risk types

The major risks associated with the Company's business activities are credit, market, operational and liquidity risk. These risks together with a commentary on the way in which the risks are managed and controlled are set out in the following sections, based on the Basel 2 Pillars in which the risks are addressed.

## 5.3 Credit risk, Credit risk mitigation and Off-Balance Sheet exposure

Credit risk is the risk of loss resulting from fluctuations in the credit standing of issuers of securities, counterparties and any debtors to which APs are exposed. The Company uses the Standardised approach to measure its capital requirements for credit risk.

Credit risk arises principally on cash balance at bank, short term deposits and accounts receivable.

The management believes that the Company has no significant exposure to credit risk in respect of short term deposits and cash balance at bank as these amounts are kept with GIB Saudi Arabian operations ("GIB – KSA") and the ultimate exposure is to the parent bank which has a high credit rating from international rating agencies. The credit risk with respect to accounts receivable is limited as these balances are spread among multiple customers.

The Company, as part of its ongoing business, deals with high profile corporations. Most of the accounts receivable are being actively followed up with the clients and do not constitute a significant risk based on their relatively strong financial position and track record. Of the Company's accounts receivable at the balance sheet date, significant amount have been realised subsequent to the year end.

**Impairment and provision assessment:** At each reporting period, GIBC assesses impairments and the need for provisions. Financial assets and other non-current assets are reviewed for impairment losses whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss, if any, is determined and recognized based on the difference between the net carrying amount and the recoverable amount of the asset. During the year, the Company did not assess a requirement for further provision charge against accounts receivable. The opening balance was maintained throughout the year resulting in a provision balance of SAR 1.5 million at 31 December 2016.

The Company follows CMA guidelines in classifying its credit risk exposures, assigning credit risk weightings, rating its credit risk exposures and applying credit risk mitigation factors to determine the related capital requirement.

As per the above guidelines, a substantial part of the Company's credit risk exposures at 31 December 2016, represented by cash balance at bank and short term deposits (i.e. exposures to Authorised Persons and Banks), are weighted at 20% in line with them being credit rated exposures. However, the Company's accounts receivable are Unrated and the capital risk charge for this exposure is also calculated in accordance with CMA guidelines.

In accordance with the CMA guidelines, most of the Company's credit exposures at 31 December 2016 are considered having a rating of 2 in the credit quality step with the remaining exposures being Unrated. GIBC does not have any exposures covered by financial collateral, guarantees or netting agreements as of 31 December 2016. Accordingly, the Company does not claim any reduction in credit risk capital requirements for credit risk mitigation items. Further, the Company does not have any off-balance sheet exposures at 31 December 2016.

The table below summarises the Company's credit risk exposures by rating category and shows the related capital required (at 14% of RWA) at 31 December 2016.

Exposure class (Rating per CMA credit quality step)	Balance sheet exposure (SAR '000)	Risk weighting	Risk Weighted Assets (RWA) (SAR '000)	Capital requirement for credit risk (SAR '000)
Authorised Persons and Banks * (2)	208,402	20%	41,680	5,835
Corporates (Unrated)	10,895	714%	77,790	10,891
Other Assets (Unrated)	11,047	300%	33,141	4,640
<b>TOTAL</b>	<b>230,344</b>		<b>152,612</b>	<b>21,366</b>

\* The exposure to this counterparty is rated by Fitch (A-), Moody's (Baa1) and Capital Intelligence (A-).

#### **5.4 Market Risk**

Market risk is the risk that the fair value or future cash flows of a financial instrument may fluctuate due to changes in market variable such as interest rates, equity prices and foreign exchange rates. The Company assesses the capital requirement for each element of market risk and then aggregates them to come up with the total capital requirement for market risk.

The Company's primary asset, short-term deposits have short tenures and carry rates of interest approximating market rates and therefore, the Company is not exposed to any significant interest rate risk.

The equity price risk arises from exposures to changes in the price and volatility of individual equities or equity indices. The Company's equity risk arises from the trading positions taken as part of the investments held for trading. The management believes that the Company has no significant exposure to equity risk in respect of trading securities as these are investments in highly liquid stocks with a short-term holding period.

At 31 December 2016, GIBC's only exposure to equity risk is in the form of its shareholding in L'azurde Company (no exposure at 31 December 2015). On an overall basis, this is an insignificant exposure on the balance sheet. The amount of exposure at the year-end was SAR 235 thousand requiring a capital charge of SAR 42 thousand. This exposure is regularly marked-to-market and the fair value changes are reflected in the income statement.

#### **5.5 Operational Risk**

Operational risk is the risk of loss resulting from inadequate or failed processes, people or systems, inaccuracy and improper disclosure of data, including legal and information security risk. The management believes that operational risks for the Company is managed and mitigated by ensuring appropriate controls and systems are in place throughout the Company.

The Company, under an SLA, outsourced a range of its operational activities including Finance, Operations, Human Resources administration, Internal Audit, Administration and certain IT support services to GIB Group, and benefits from the parent bank's expertise in these areas.

For determining the capital requirement for operational risks, GIBC uses the basic indicator approach which calculates capital at 15% of the average operating income for the last three years. However, in accordance with the Prudential Rules, GIBC ensures that the capital requirement for operational risk is maintained at least at 25% of its overhead expenses as laid down under the expenditure based approach.

The calculation of the Company's capital requirement for operational risk is shown in the tables below:

Basic Indicator Approach (BIA)	Base Year	Gross operating income (SAR '000)	Average gross operating income (SAR '000)	Risk capital charge (%)	Capital required (SAR '000)
For the year 2016	2014	22,820	29,418	15%	4,413
	2015	39,011			
	2016	26,424			

Expenditure Based Approach (EBA)	Base Year	Overhead expenses (SAR '000)	Risk capital charge (%)	Capital required (SAR '000)
For the year 2016	2016	33,298	25%	8,325

<b>Capital requirement for Operational Risk for 2016 (SAR '000) (Higher of Basic Indicator Approach and Expenditure Based Approach)</b>	<b>8,325</b>
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## 5.6 Liquidity Risk

Liquidity risk is the risk that sufficient funds are not available to meet the Company's financial obligations on a timely basis as they fall due. The risk arises from the timing differences between the maturity profiles of the Company's assets and liabilities.

Given the short term nature of the Company's assets, the Management believes that the Company does not have any significant exposure to liquidity risk. Based on scenarios with a potential liquidity shortfall, the Company has determined the liquidity risk to be minimal given the nature and size of its obligations.

As of the year end, the Company has short term deposits amounting to SAR 205 million maturing in periods up to May 2017 that is more than sufficient to cover any financial obligation that may fall due.