



Risk Assessment Report 2023

SICO Saudi REIT

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1. FUND DETAILS

Name of the Fund	SICO Saudi REIT
Fund Manager	SICO Capital
Type	Sharia-Compliant Closed-Ended Real Estate Investment Fund
Objective	Provide regular income to unitholders by investing in structurally developed income-generating real estate assets of no less than 75% of the total value of the fund. In addition, the Fund may invest in real estate outside the Kingdom of Saudi Arabia up to a maximum of 25% of the Fund's total assets.
Tenure	99 years
Risk Level	High

Key Risks	Description	Mitigation
<p>2. MARKET RISK</p>	<p>Market risk refers to the risk of loss resulting from adverse movements in market prices of Real Estate assets due to various factors including the sector risk, supply & demand, economic conditions, inflation, interest rates etc.</p>	<p>Market risk is mitigated through a number of actions including:</p> <ul style="list-style-type: none"> • Regularly evaluating the sector & geography dynamics to identify the risks affecting the valuation and tenancy. • Regular monitoring of macro-economic changes and regulatory trends and taking proactive steps to minimize the impact. • Regular review of valuations by independent evaluators to assess the future trend and its impact on the fund prices. • Interest rate risk is discussed separately in the ensuing paragraphs.
<p>3. COMMERCIAL REAL ESTATE MARKET RISK</p>	<p>Commercial real estates are more volatile than residential properties. Worsening economic conditions can more quickly affect the valuation, rental yields and tenants' ability to make timely payments.</p>	<p>All of the Fund's assets are commercial real estate. The Fund Manager constantly monitors the emerging negative trends to take action to mitigate these risks. The fund manager should also look for opportunities to diversify the portfolio in-line with the Fund's Terms and Conditions as soon as signs of economic weakness appear.</p>

<p>4. CREDIT RISK</p>	<p>The Fund is exposed to credit risks from the tenants and other debtors including banks used for money market placements.</p>	<p>Thorough due diligence is done for selection of credit worthy tenants. Rental contracts have punitive clauses for late payments and provide sound basis for legal actions in case of defaults.</p> <p>For rent receivables, the fund manager regularly monitors outstanding dues and follows up with tenants for payments.</p> <p>Excess cash is managed as follows:</p> <ul style="list-style-type: none"> • Deal with reputable financial counterparties. • Regularly monitor credit exposures and • Periodic credit assessment of counterparties.
<p>5. LIQUIDITY RISK</p>	<p>Liquidity risk primarily arises in two forms: 1) Fund’s inability to meet its financial obligations. 2) fund’s inability to convert assets into cash without a loss of capital or income in the process</p>	<p>Following are some of the actions that the fund manager takes to manage the liquidity risk of the fund:</p> <ul style="list-style-type: none"> • Regular monitoring of cash balances vis a vis maturing liabilities and expenses ensuring sufficient funds to honor these obligations. • Monitoring of liquidity and debt service Coverage Ratio. • As of 31 December 2023, the fund has adequate liquidity to service its debt and meet other obligations.

<p>6. INTEREST RATE RISK</p>	<p>As the Fund is leveraged using a floating rate facility (SAIBOR 3 Months+ 2.25% (reduced to 1.90) in 2024), any increase in SAIBOR would result in higher interest expenses and consequently lower total returns available to the Unitholders.</p>	<p>Fund has obtained Islamic financing amounting to SAR 149.89 Mn from a local Bank, which has a variable financing cost. Any increase in SAIBOR will have a negative impact on fund's NAV. In case of 100 bps increase in SAIBOR, financial costs will increase by around SAR 1.5 Mn.</p> <p>Fed rate hikes have now come to a halt with an expected decrease in coming months, this will have a positive impact on the Fund. However, in future Interest rate hedging may be considered to avoid the risk of rising interest rates depending upon the cost of hedging.</p> <p>Fund manager should regularly review the interest rate outlook and take actions to mitigate the interest rate risk.</p>
<p>7. COUNTRY RISK</p>	<p>The risk that new government policies and political & social instability, could negatively impact the Fund's performance and/ or its liquidity.</p>	<p>The Fund is fully invested in Saudi Arabia. Fund manager closely monitors Kingdom's real estate policies, regulatory/tax landscapes to respond appropriately as needed.</p>
<p>8. REGULATORY COMPLIANCE RISK</p>	<p>This risk entails risk of not complying with the rules of the various regulators as applicable to the fund specially CMA, Tadawul, MOCI etc.</p>	<p>The fund strictly complies with all applicable regulations. SICO Capital's Compliance function presents regular reports to the Fund Board.</p>

9. CONCENTRATION RISK

Excessive concentration of real estate type, sector, or geographic location.

The Fund has invested in four Real Estate assets, three of which are located in Makkah and one in Riyadh.

The Fund is highly concentrated in terms of sector exposure (Hospitality Sector) & geography exposure.

The Fund Manager is working continuously to diversify fund's portfolio in terms of sector and location. In order to achieve this, investment objective of the fund was changed to allow it to invest anywhere in the Kingdom of Saudi Arabia without any limitation. The fund was initially mandated to invest at least 55% of the assets in the holy cities of Makkah and Medina. The Fund has acquired a high-end office complex in Riyadh, known as the I-Offices at a net price SR 135 million.

The Fund has unutilized credit facility of SAR 475 Mn with one of Saudi Banks which gives the Fund the flexibility in acquiring new assets.

Below is a comparison of exposure to various sectors during the last 3 years as % of the market value of the portfolio. Fund Manager shall continue its effort to further diversify the portfolio.

Assets	Concentration		
	2023	2022	2021
Hotels	72%	74%	79%
Offices	28%	26%	21%

10.OCCUPANCY RISK.

Risk of Non-renewal of lease agreements, early termination of lease agreements, risk of delay in finding the new tenant, renewal at lower than current lease rate affecting the rental income of the fund.

To mitigate this risk tenants' agreement shall have the provision of advance notice by either party before terminating the contract. During such period, an alternative tenant could be searched.

In some cases, the Fund Manager may accept the renewal at lower than the expiring lease rate due to adverse market conditions. Any significant impact arising due to such renewals shall be disclosed to the market.

Before any upcoming lease expiry, the fund manager should start assessing the existing lease terms and other options of leasing at better rates. In case of risk of vacation or non-renewal from tenant's part, search for the new tenant should start well in advance using internal efforts and external agents as appropriate. There should be a policy to assess available options at least 3 months before the lease expiry.

Current occupancy;

In March 2023, all three properties were leased to Moro International Company until 31 December 2023, thus allowing the Fund Manager to re-assess the leasing rates for these properties prior to the Ramadan and Hajj Season of the Hijri Year 1445, in-line with the prevailing market conditions. Lease renewals of these properties have been renewed for another 2 years up to 31 Dec 2025.

I-Offices property is fully occupied with 3 tenants with annual gross rental income of SR 10.45 million.

11. STRUCTURAL DAMAGE RISK	Any adverse event leading to structural damage to property can impact the income generating potential of the property leading to negative impact on the valuation.	Preventative maintenance and inspection should be carried out at regular intervals to ensure that properties are kept in good conditions.
12. RISK OF NOT UTILIZING MARKET OPPORTUNITIES	Fund Manager's inability to identify good market opportunities may lead to negative effect on fund's capacity to achieve desired returns.	Fund Manager should regularly study the market with access to reputable research reports for new investment opportunities that meet the fund's objective. The Fund currently has an approved credit line with one of the Saudi Banks that can be utilized to close attractive deals that becomes available.
13. NEW ACQUISITION - GENERAL RISK:	In order to continue achieving the target return of the fund it is important to acquire profitable and undervalued properties. The due diligence should include a through project cash flow analysis, financial conditions of tenants, financing cost of acquisition, exit strategy etc.	The Fund Manager should conduct a thorough feasibility study and legal & financial due diligence before acquiring any investment by analyzing the economic conditions of the target market vis a vis the Fund's ability to achieve its investment objectives. Fund manager should also consider various financing options for new acquisitions taking into account the current interest rate outlook.
14. DISTRIBUTIONS VOLATILITY RISK	The risk of inability or failure to periodic or targeted future distribution obligations as per fund's Terms & Conditions (T&C).	The Fund Manager should conduct regular meeting with property agents and operators to closely monitor the performance of the assets and take prompt actions to ensure the Fund meets its performance targets.

	The REIT has a policy of distributing annually at least 90% of its net profit not including profit resulting from the sale of the real estate assets and other investments.	The fund manager should review the periodic financials as well as the projected financials, if available to assess the actual profits vs targets.
15. PROPERTY MANAGER RISK	Risk of early termination of the property manager's contract may affect the property operations and performance.	The Fund manager should consider having provision of at least 3 months advance notice by either party before terminating the services. During this period, alternative arrangement can be made.
16. DEPENDENCE ON KEY PERSONNEL	Risk of losing a key real estate team member in general (whether through resignation or otherwise).	The Fund manager ensures that Real Estate unit is staffed with seasoned professionals. Any vacancies are timely filled with suitable replacement staff.
17. CONFLICTS OF INTEREST RISK	Risk of conflict of interest between the fund manager and unit holder/s	Compliance as an independent function should continuously monitor for conflict of interest cases and report the same as per applicable regulations.
18. Operational RISK	Operational risk is the losses arising from a variety of internal and external factors including failure of controls or processes, technology, disruptions and disasters.	Fund Manager should manage operational risks by establishing appropriate controls and processes covering all aspects of Fund/property operations. This includes timely renewal of insurance coverages, compliance with best real estate practices and for key activities that require subject matter expert fund manager should consider outsourcing it to reputable service providers with strong track record.
19. FUND MANAGER RISK	Unitholders may not be provided the opportunity to participate in the Fund's decision-making or approval process in line with the fund	The Fund Manager should set-up systems and controls to ensure full participation of unit holders in the approval or decision-making process as required by the T&C and regulations. The Fund should comply with the regulations at all times and the investment team should act in the best

	T&C or regulations. This may have an impact on the performance of the fund	interest of unitholders putting all efforts to achieve the Fund's growth aspirations.
20. RISK OF INVESTMENTS UNDERPERFORMANCE	The risk that the underlying assets will not perform as expected due to idiosyncratic factors such as, tenants' delinquency, higher CAPEX or higher vacancy rates.	<p>In order to mitigate such risks, Fund Manager to follow a number of strategies including:</p> <ul style="list-style-type: none"> • Sign long term contracts with tenants with provisions for contractual increase in the rent. Ensure financially sound and diversified tenant mix • Closely monitor the performance of the underlying assets and regularly meet with the property managers/operator to monitor any issues/ events that might lead to asset's underperformance.
21. REAL ESTATE VALUATION RISKS	Risk of Incorrect valuation of the properties resulting in financial and reputational losses.	Valuations are done by taking the average of two independent valuers accredited by the Saudi Authority for Accredited Valuers (TAQEEM). The methodology takes into consideration a number of factors, including the area, sector, geography and type of the property together with economic outlook and trends.
22. DEVELOPMENT RISK	The Risk associated with real estate development projects include: the risk of inexperienced developers and project monitoring team resulting in costs & time overrun resulting in financial and reputational implications.	For development projects, the Fund has a CAP of 25% of fund assets and currently there are no projects under development. Project development is a high-risk activity starting with the selection of a reputable and experienced developer. The Fund Manager should embark upon a development project only after all necessary technical, financial and legal due diligence and market study.

<p>23.LEVERAGE RISK</p>	<p>The risk that the Fund may not be able to meet some of the bank financing covenants or misses the repayment schedule, which triggers an event of default.</p>	<p>The Fund Manager should closely monitor:</p> <ul style="list-style-type: none"> • Debt repayment commitments and ensure availability of funds by assessing projected cash flows from each property and for the total fund on a regular basis. • Compliance with all debt covenants. As of 31 December 2023, the fund is compliant with all debt covenants. <p>Any new funding from the bank should be properly analyzed and pricing from different banks should be obtained before going ahead with any bank financing.</p>
<p>24.LITIGATION RISK</p>	<p>The Fund is exposed to the possibility of contractual disputes, legal notices and lawsuits with third parties due to the nature of its activities. In such cases, the fund will bear legal fees in addition to the amounts of settlement or judgements, which would reduce the fund’s income and the cash available for distribution to unitholders.</p> <p>The fund manager and others are entitled to be compensated from the fund for any liability incurred by them in performing their duties for fund as per the T&C and regulations.</p>	<p>The Fund Manager takes all possible and available actions including legal procedures to protect the interests of unit holders.</p> <p>In Q4 2022, the Fund Manager initiated legal proceedings against the previous Master Tenant of Eskan Hospitality Towers 4, 5 and 6 (known as Eskan Company for Development). The Fund Manager executed 4 promissory notes in the amount of SR 18,325,000 pertaining to uncollected rent for Eskan 4 and Eskan 6 assets that was due in 2022. The relevant courts deemed the promissory notes void and cancelled them accordingly.</p> <p>In Q4 2022 as well, Eskan Company filed two legal cases against the fund, to claim back rent paid by Eskan to the fund during 2020, 2021 and 2022 pertaining to Eskan 4 and Eskan 6 assets. The relevant courts ruled in favor of Eskan Company where Eskan Company currently holds execution orders to claim c.a. SR 16 Million.</p>

		Fund manager is taking steps to minimize the adverse implications of these cases on the fund performance.

25. CONCLUSION

Investment in the real estate funds are categorized as high risk. The Fund manager takes steps to mitigate these risks however, these cannot be eliminated. The above listed risks are not exhaustive as there may be other risks and un-certainties that are not currently known to the Fund Manager or the Fund Manager may consider to be currently insignificant and which may have a negative impact on the Fund's income or valuation. No guarantees can be made that the Fund will be able to achieve the investment objective or that investors will receive a return on their capital.