SEDCO Capital REIT Fund

Risk Assessment – Annual Report 2024

December 2024

Risk Assessment

The Fund's activities expose it to a variety of different risk factors that are exogenous such as market risk, credit risk, and liquidity risk as well as operational process-related risks. Furthermore, there are risks related to the asset class REITs as such.

The Fund's overall risk management program focuses on the unpredictability of financial markets and seeks to minimize potential adverse effects on the Fund's financial performance.

Consequently, the risk assessment process focuses on the most significant risk factors, which include but are not limited to:

Main Risks	Description	Assessment
Market Risk	Market Risk arises from external factors such as macroeconomic conditions, competition, supply & demand, political changes, FX etc.	The Manager monitors on a regular basis the fluctuation and changes in the overall economic environment, local real estate markets including cap rates, inflation rate, taxes, valuations, competition from other available premises and various other factors. Given these factors, the Manager believes that the impact of current market factors is mitigated through diversification of assets that adds stability to the portfolio while reducing vulnerability to economic fluctuations. Additionally, vacancy risks are managed through a proactive asset management approach. Market research is conducted to avoid any economic constraints as much as possible. Given current trends and changes in demand patterns of the real estate sector, the Manager highlights the following points: 1) The wider acceptance of work from home could have implications for the office market and may lower demand for office space and related services 2) The rising interest rates over the last years have led to widening cap rates and may impact market dynamics for buy/sale transactions and leasing. Manager also recognizes that the Saudi government is actively supporting the real estate sector through various reforms and initiatives aimed at facilitating investment. In result, the volume of investment and development witnessed notable increases, indicating vigorous market activity. Therefore, the future supply/demand situation is to be closely monitored by the Manager. Several approaches to mitigate this risk are under consideration including diversification of property types, stakeholder engagement, sustainability/
Risks related to the use of debt	The use of debt results in risks such as challenges with (extended) periods of high interest/profit rate levels, and leverage related to refinancing risks. Profit/interest rate risk is the potential for financial loss arising from increases in profit/interest rates and ultimately adversely impacting the financing terms of the Fund.	The Manager uses debt with the objective to enhance investor returns. Based on the expected trend of profit/interest rates, the Manager may consider other financial instruments to manage/hedge this risk. Leveraging may also further exacerbate any losses. Additionally, while increasing profit/interest rates may be a challenge, which can impact cap rates, real estate investments may nevertheless perform in a rising rate environment due to variety of factors, such as increasing rent revenue, demand, and prices.
Credit Risk	Credit risk arises from the possibility that tenants may experience financial difficulty and be unable to fulfill their lease commitments.	Credit risk is mitigated by industrial and geographical diversification, diversity both in its tenant mix and asset mix and by conducting tenant credit assessments. For new leases, credit evaluation is performed and on an ongoing basis, tenant credit and arrears are closely monitored by the Manager.

Risk Assessment – Cont.

Main Risks	Description	Assessment
Completion Risk	Risk associated with development projects underway include construction delays and their impact on financial performance, cost overruns which could impact the profitability and/or financial viability of a project; and the inability to meet revenue projections upon completion. Delays may result in legal risk.	This risk is somewhat mitigated due to the limit that the Fund can invest only up to 25% of the value of its assets in real estate development. The Manager also aims to mitigate this risk through management of the contractual framework of the properties.
Operational Risk	Risk of loss resulting from failure of internal processes, operational procedures, external events, loss of key personnel, service provider and counterparty risk as well as business continuity risk.	The Manager has in place a monitoring framework to manage the day-to-day activities and mitigate operational risks. These include periodic meetings to identify potential operational risks, reviewing and resolving operational issues. Internal audits are also carried out periodically to review compliance with processes, and to identify and rectify any lapses in procedures. A business continuity plan is in place to mitigate the business continuity risk of interruptions or catastrophic loss to its operations. Service providers and counterparty performance is regularly monitored. Moreover, Manager's ability to uphold a robust reputation and foster strong relationships with other service providers ensures that the Manager has reliable support available whenever needed.
Liquidity Risk	Liquidity Risk has many dimensions such as the risk of being unable to meet any payment obligations for exiting properties according to plan.	Cash flow generated from operating the property portfolio represents the primary source of liquidity used to service the interest on debt, fund general and administrative expenses. Therefore, the Manager ensures that there are adequate funds to repay obligation in a timely and cost-effective manner. Additionally, the Fund Manager also has a cash management process, in which he has the option to utilize any excess cash for short-term deposits. Any decline in liquidity in the Saudi real estate market may affect valuations. Any exit below acquisition cost (including transaction cost) can lower the returns.
Regulatory Risk	Fund operates within guidelines as set out in the "Real Estate Investment Funds Regulations" from Capital Market Authority. There can be further regulatory risk related to real estate market or public policy. Examples include new taxation, building code requirements, energy efficiency standards, Operational improvement requirements, etc. Changing regulations can add substantial time, risk, and cost to completing development projects and can also impose new and often burdensome operating restrictions on existing properties.	The Manager has implemented processes to monitor regulatory requirements in all fund management functions, such as Compliance department aim to provide another layer of assurance that proper controls are in place to avoid any non-compliance.

Risk Assessment – Cont.

Main Risks	Description	Assessment
Legal Risk	Risks involved in legal arrangements, contracts, agreements and obligations.	The Manager has dedicated Legal and Compliance departments, who are responsible to provide guidance to ensure that all regulatory and compliance matters are adhered to. Regarding legal suits, any adverse ruling may potentially have a negative financial impact on the Fund.
Risk of crimes such as cyber security risks	Crimes such as cyber security incident includes any material adverse event that threatens the confidentiality, integrity and/or availability of SC's information resources and may result in financial losses.	The Manager has implemented processes, procedures, and controls to help mitigate these risks. However, these measures, as well as its increased awareness of a risk of a cyber-incident, do not guarantee that its financial results would not be negatively impacted by the occurrence of any such event.
Valuation Risk	Risk that the valuation is notably incoherent from actual market prices.	Two independent appraisals are performed for asset valuations. The 3rd party Valuers are accredited by TAQEEM (i.e., Saudi Authority for Accredited Valuers). The Fund Manager uses the average of the two independent Valuers for reporting purpose. In case of any material contradiction between the two Valuers, the Fund Manager assigns third Valuer.
Capital Deployment Risk and Reinvestment Risks	Risk of delay in capital deployment.	There is notable risk mitigation currently since the Fund has largely deployed its capital. Nevertheless, any actions such as portfolio rebalancing may create future deployment and/or reinvestment risks.
General Risks Related to the Asset Class REIT	General risks of the asset class include among other aspects volatility of the share price, potential deviations between net asset value and the share price in the market, potential drop in share price and liquidity risks.	The market price of the Units may be affected by changes in general market conditions, fluctuations in the markets for equity securities and numerous other factors beyond the control of the Manager.
Environmental, Social and Governance (ESG) Risks, in Particular Climate Risk	Environmental, Social, and Governance (ESG) risks refer to the three factors in measuring the sustainability and societal impact of an investment. ESG criteria can help to better determine the future financial performance of companies (return and risk). Any environmental issues of properties, such as the use of hazardous materials, could adversely impact its value. As part of ESG risks, climate risks may result in increased exposure to loss as assets become less liquid, generate lower income or may be subject to environmental regulation. Additionally, Climate change could make insurance prohibitively expensive. New regulations for mitigating carbon emissions may cause future capital expense requirements and/or decrease real estate market values.	The Manager assesses ESG risks in the analysis of investment opportunities and in its monitoring according to its responsible investment policy. In the Manager's experience, ESG assessment can complement traditional financial analysis and due diligence. The Manager has implemented processes, procedures and controls to help mitigate these risks. However, these measures, as well as its increased awareness of ESG risks, do not guarantee that its financial results will not be negatively impacted by the occurrence of any such event.

Risk Assessment – Cont.

Main Risks	Description	Assessment
Risks Related to Geopolitical Events, Natural Catastrophes, Terrorism and Health Pandemics	Geopolitical events, instability, terrorism, natural catastrophes and events such as health pandemic may negatively impact assets from valuation as well as income perspective.	The escalation of geopolitical conflicts may be reflected in the risk premia of global risk assets and thus may impact the Fund, too. Given the fact that these events are highly uncertain and unpredictable and therefore the Fund as well as the Manager may be negatively impacted by the occurrence of any such event.
Property Management Risk	Risk of lower income (i.e., return on investment) due to inappropriate or insufficient property management, resulting in high vacancy rates, high operating expenses and below market rental income etc.	Manager recognizes that management is essential to success in real estate investment and therefore, mitigates this risk by engaging suitable, qualified, and experienced property managers when outsourcing is done. In this regard, roles & responsibilities are clearly defined and agreed through legal documentation i.e., agreements, contracts etc. The Manager has implemented necessary processes to mitigate insufficiencies related to property management. Particularly, increasing energy costs may bring heightened focus on the energy efficiency of buildings, because of the impact on tenants' bills.
Inflationary Pressure / Supply chain issues	Risk that production and supply chain bottlenecks likely to lead to unexpected inflation level.	While inflation is a risk factor, there is some mitigation of inflation through rent escalations in lease agreements. Based on historical data, REITs provide reasonable protection against inflation because rents are not as sticky as other prices. The alleviation of pandemic restrictions may ease some supply chain bottlenecks that have been a cause of inflation.
Concentration Risk	Risk of a scenario where too much investment capital has been put into a single property type or geographical location.	Manager recognizes portfolio diversification to manage concentration risk involves spreading investment capital across different property types as well as different geographical locations. Tenant diversification is an important factor considered by the Manager. This practice can reduce concentration risk and reduce exposure to market volatility or asset devaluations.

Risk Assessment – Cont.

Main Risks	Description	Assessment
Risk of Global Recession	Risk of a regional or global recession and a string of financial crises in emerging market and developing economies that would do them lasting harm.	While such factors are beyond the control of the Manager, the proactive action plan to be in place for any potential slowing of businesses.
Technological Disruption and Artificial intelligence (AI) productivity boost	Risks to disrupt traditional real estate practices by streamlining processes, reducing costs, and increasing efficiency. AI may the impact real estate due to certain infrastructure requirements such as data centers as well as elevated energy supply. This disruption may also lead to job displacement and market consolidation, impacting real estate professionals and smaller businesses. Additionally, the adoption of AI in real estate may widen economic disparities by favoring larger firms and investors with access to advanced AI technologies and data analytics capabilities.	Manager recognizes that the greater and more rapid the investment in new technologies, the greater the potential impact on productivity. However, changes in productivity tended to be signaled a few years in advance. Therefore, any development in this area is to be closely monitored by the Manager.

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For more information

+966 12 690 6555

P.O. Box 13396, Jeddah 21493, Kingdom of Saudi Arabia

www.sedcocapital.com

+966 12 690 6599

License No. 11157-37

info@sedcocapital.com