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شركة آر إس إم المحاسبون المتحدون للإستشارات المهنية
RSM Allied Accountants Professional Services Co.

MUSHARAKA REIT FUND
(Managed by Musharaka Capital Company)

**FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2022
AND INDEPENDENT AUDITOR'S REPORT**

MUSHARAKA REIT FUND
(Managed by Musharaka Capital Company)

Financial statements for the year ended 31 December 2022 and independent auditor's report

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INDEPENDENT AUDITOR'S REPORT

To the Unitholders Musharaka REIT Fund

Report on the audit of the financial statements

Opinion

We have audited the financial statements of Musharaka REIT Fund (the "Fund"), managed by Musharaka Capital Company (the "Fund Manager"), which comprise the statement of financial position as at 31 December 2022, and the statements of profit or loss and other comprehensive income, changes in net assets attributable to unit holders and cash flows for the year then ended and notes to the financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying financial statements present fairly, in all material respects, the financial position of the Fund as at 31 December 2022, and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards ("IFRS") that are endorsed in the Kingdom of Saudi Arabia and other standards and pronouncements issued by the Saudi Organization for Chartered and Professional Accountants ("SOCPA").

Basis for Opinion

We conducted our audit in accordance with International Standards on Auditing that are endorsed in the Kingdom of Saudi Arabia. Our responsibilities under those standards are further described in the "Auditor's Responsibilities for the Audit of the Financial Statements" section of our report. We are independent of the Fund in accordance with the International Code of Ethics for Professional Accountants (including International Independence Standards) that are endorsed in the Kingdom of Saudi Arabia that is relevant to our audit of the financial statements, and we have fulfilled our other ethical responsibilities in accordance with this Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Key Audit Matters

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the financial statements of the current year. These matters were addressed in the context of our audit of the financial statements as a whole, and in forming our opinion there on, and we do not provide a separate opinion on these matters.

Independent auditor's report to the unitholders of Musharaka REIT Fund (continued)

Impairment of investment properties	
Key audit matter	How our audit addressed the key audit matter
<p>As at 31 December 2022, the carrying value of the Fund's investment properties amounted to SR 1.3 billion.</p> <p>At the end of each reporting period, the Fund Manager assesses whether there is any indication that investment properties may be impaired.</p> <p>As part of the assessment of impairment on its investment properties, the Fund uses valuations carried out by third party valuers to ascertain the fair value of these properties.</p> <p>We considered this as a key audit matter as the assessment for impairment involves significant judgement that could have a material impact on the financial statements of the Fund."</p> <p>Refer to Note 2.15 of the financial statements on the accounting policy for impairment of non-financial assets and Note 10 for the disclosures on investment properties.</p>	<p>We have performed the following as part of our audit:</p> <ul style="list-style-type: none"> • Reviewed management assessment for the existence of impairment indicators on investment properties; • Assessed the independence, professional qualifications, competence and experience of the Fund's independent valuers engaged; • Met with the Fund's independent valuers to understand the assumptions and methodologies used in valuing the investment properties and the market evidence used by them to support their assumptions; • Agreed the specific details (area, location etc.) of the investment properties as per the valuation reports with the Fund records and title deeds of the investment properties; • Compared the recoverable amount of the investment properties as per the Valuation Report to their carrying values to determine whether the recognition of any impairment loss is required; and • Assessed the appropriateness and adequacy of the accounting treatment and policies used and disclosures made in the Fund's financial statements including disclosure of key assumptions and judgments

Other matter

The financial statements of the Fund for the year ended 31 December 2021 were audited by another auditor who expressed unmodified opinion on those financial statements dated 29 March 2022.

Responsibilities of Management and Those Charged with Governance for the Financial Statements

Fund Manager is responsible for the preparation and fair presentation of these financial statements in accordance with IFRS, that are endorsed in the Kingdom of Saudi Arabia and other standards and pronouncements issued by SOCPA, and the Fund terms and conditions, and for such internal control as Fund manager determines is necessary to enable the preparation of financial statements that are free of material misstatement, whether due to fraud or error.

In preparing the financial statements, management is responsible for assessing the Funds'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 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 i.e. Board of Directors, are responsible for overseeing the Fund's financial reporting process.

Independent auditor's report to the unitholders of Musharaka REIT Fund (continued)**Auditor's 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 International Standards on Auditing 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 the 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 International Standards on Auditing that are endorsed in the Kingdom of Saudi Arabia, we exercise professional judgement and maintain professional skepticism 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 the one resulting from error, as fraud may involve collusion, forgery, intentional omission, 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 internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of 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 Funds's ability to continue as a going concern. If we conclude that a material uncertainty exists, 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.

RSM Allied Accountants Professional Services

Mohammed Bin Farhan Bin Nader
License No. 435

Al-Khobar, Saudi Arabia
30 March 2023 (corresponding to 8th Ramadan, 1444H)



MUSHARAKA REIT FUND

(Managed by Musharaka Capital Company)

Statement of profit or loss and other comprehensive income

(All amounts in Saudi Riyals unless otherwise stated)

	Note	For the year ended 31 December	
		2022	2021
Rental revenue	4	100,616,509	88,784,030
Finance income	7	11,596,685	11,911,540
Total income		112,213,194	100,695,570
Depreciation	10	(28,689,703)	(23,529,595)
Fund management fee	5	(15,780,449)	(16,629,524)
Other operating expenses	6	(13,668,354)	(7,818,848)
Impairment loss on investment properties	10	(8,439,546)	(4,704,234)
Allowance for expected credit losses	12	(5,050,770)	116,394
Total expenses		(71,628,822)	(52,565,807)
Total income from operations		40,584,372	48,129,763
Unrealised gain at investments in fair value through profit or loss	14	30,000	63,100
Finance costs	8	(32,282,156)	(17,184,509)
Finance income on short-term murabha deposit	15	288,750	
Other income	17	320,000	820,000
Profit before zakat		8,940,966	31,828,354
Zakat	9	1,959,473	(1,959,473)
Profit for the year		10,900,439	29,868,881
Other comprehensive income		-	-
Total comprehensive income for the year		10,900,439	29,868,881
Weighted average number of units outstanding		88,000,000	88,000,000
Basic and diluted earnings per unit		0.12	0.34

The accompanying notes form an integral part of these financial statements.

MUSHARAKA REIT FUND
(Managed by Musharaka Capital Company)

Statement of financial position
(All amounts in Saudi Riyals unless otherwise stated)

	Note	As at 31 December	
		2022	2021
Assets			
Investment properties	10	1,334,991,726	1,108,922,475
Net investment in finance leases	11	219,945,398	230,425,626
Lease rental receivables	12	26,705,723	35,516,432
Prepayments and other assets	13	3,718,823	3,489,350
Investments carried at fair value through profit or loss	14	5,312,150	5,282,150
Short-term murabaha deposit	15	35,000,000	-
Cash at banks		31,486,197	58,135,003
Total assets		1,657,160,017	1,441,771,036
Liabilities			
Borrowings	16	657,438,425	405,265,264
Lease liabilities	17	139,419,106	142,220,187
Unearned rental revenue	18	15,595,152	17,855,057
Accrued expenses and other liabilities	19	20,370,576	5,836,612
Accrued fund management fee	20	7,466,719	9,864,843
Zakat provision	9	-	1,959,473
Total liabilities		840,289,978	583,001,436
Net assets attributable to unit holders		816,870,039	858,769,600
Units in issue		88,000,000	88,000,000
Per unit value (Saudi Riyals)		9.28	9.76

The accompanying notes form an integral part of these financial statements.

MUSHARAKA REIT FUND

(Managed by Musharaka Capital Company)

Statement of changes in net assets attributable to unitholders

(All amounts in Saudi Riyals unless otherwise stated)

	For the year ended 31 December	
	2022	2021
Net assets attributable to unitholders at 1 January	858,769,600	881,700,719
Change from operations		
Total comprehensive income for the year	10,900,439	29,868,881
Dividends (Note 23)	(52,800,000)	(52,800,000)
	(41,899,561)	(22,931,119)
Net assets attributable to unitholders at 31 December	816,870,039	858,769,600

The accompanying notes form are an integral part of these financial statements.

MUSHARAKA REIT FUND

(Managed by Musharaka Capital Company)

Statement of cash flows

(All amounts in Saudi Riyals unless otherwise stated)

	Note	For the year ended 31 December	
		2022	2021
Cash flow from operating activities			
Profit for the year		8,940,966	31,828,354
Adjustment for:			
Depreciation and amortization	10	28,689,703	23,529,595
Impairment loss on investment properties	10	8,439,546	4,704,234
Allowance for expected credit losses	12	5,050,770	(116,394)
Unrealised gain on investments carried at fair value through profit or loss	14	(318,750)	(63,100)
Finance costs	8	32,282,156	17,184,509
Finance income	7	(11,596,685)	(11,911,540)
Rent concession on lease liabilities	17	(320,000)	(820,000)
Changes in operating assets and liabilities:			
Decrease (increase) in lease rental receivables		8,810,709	(24,516,382)
(Increase) decrease in prepayments and other assets		(229,473)	355,825
Increase in unearned rental revenue		2,259,905	10,586,520
Increase in accrued fund management fee	20	2,398,124	1,063,800
Decrease in accrued expenses and other liabilities	19	(14,533,964)	(1,140,617)
Cash generated from operations		69,873,007	50,684,804
Finance cost paid	17	(13,866,828)	(9,666,340)
Net cash inflow from operating activities		56,006,179	41,018,464
Cash flow from investing activities			
Additions to investment properties	10	(260,291,493)	(95,926,251)
Finance income received	11	22,076,913	28,745,912
Placement of short-term murabaha deposit	15	(35,000,000)	-
Net cash outflow from investing activities		(273,214,580)	(67,180,339)
Cash flow from financing activities			
Proceeds from borrowings	16	254,879,595	101,627,757
Repayment of lease liabilities	17	(11,520,000)	(10,170,000)
Dividends paid	23	(52,800,000)	(52,329,920)
Net cash inflow from financing activities		190,559,595	39,127,837
Net change in cash at banks		(26,648,806)	12,965,962
Cash at banks at beginning of year		58,135,003	45,169,041
Cash at banks at end of year		31,486,197	58,135,003
Non-cash financing activity			
Amortization of loan arrangement fee	8	2,633,765	1,977,359
Additions to right-of-use assets and lease liabilities	10, 17	2,907,007	-

The accompanying notes form an integral part of this financial information.

MUSHARAKA REIT FUND

(Managed by Musharaka Capital Company)

Notes to the financial statements for the year ended 31 December 2022

(All amounts in Saudi Riyals unless otherwise stated)

1 GENERAL INFORMATION

Musharaka REIT Fund (the “Fund”) is a closed-ended Shari’ah-compliant real estate investment traded fund incorporated in the Kingdom of Saudi Arabia in compliance with the Real Estate Investment Funds Regulations and Real Estate Investment Traded Funds Instructions issued by the board of the Capital Market Authority (“CMA”).

The Fund is listed and traded in the Saudi Stock Exchange (“Tadawul” or “Saudi exchange”) and is managed by Musharaka Capital Company (the “Fund Manager”).

The registered address of the Fund Manager is P.O.Box 712, Al Khobar 31952, Kingdom of Saudi Arabia.

The offering of the units of the Fund has been approved by the CMA on 23 Ramadan 1438 H (corresponding to 17 July 2017) and started its operations on 25 Dhul Qadah 1438H (corresponding to 17 August 2017). The Fund's term is 99 years and is extendable for additional two years at the discretion of the Fund Manager after obtaining CMA approval.

During 2021, the Fund’s board of directors and Capital Market Authority (“CMA”) issued approval for a change in the terms and conditions of the Fund converting the Fund into a closed-ended Traded Real Estate Investment Fund that takes the form of a special purpose entity.

The primary investment objective of the Fund is to invest in developed properties that are qualified to generate periodic rental income and distribute at least 90% of the Fund's net profit as cash dividends to the unit holders annually.

2 BASIS OF PREPARATION SIGNIFICANT ACCOUNTING POLICIES

2.1 Basis of preparation

These financial statements of fund have been prepared in accordance with the International Financial Reporting Standards (“IFRS”) that are endorsed in the Fund the Kingdom of Saudi Arabia and other standards and pronouncements issued by the Saudi Organization for Chartered and Professional Accountants (“SOCPA”).

2.2 Historical cost convention

The financial statement have been prepared on a historical cost basis except for investments carried at fair value through profit or loss (“FVTPL”).

2.3 Functional and presentation currency

Items included in the financial statement of the Fund are measured using the currency of the primary economic environment in which the Fund operates (the “functional currency”). The financial statements are presented in Saudi Arabian Riyals (“Saudi Riyals”) which is the Fund’s functional currency.

MUSHARAKA REIT FUND

(Managed by Musharaka Capital Company)

Notes to the financial statements for the year ended 31 December 2022 (continued)

(All amounts in Saudi Riyals unless otherwise stated)

2 BASIS OF PREPARATION SIGNIFICANT ACCOUNTING POLICIES (continued)

2.4 New and amended Standards adopted by the Company

The Fund has applied the following standards and amendments for the first time for its reporting period commencing on or after 1 January 2022:

- Interest Rate Benchmark Reform phase 2 - amendments to IFRS 9 'Financial instruments', IAS 39 'Financial instruments: Recognition and Measurement', IFRS 7 'Financial Instruments: Disclosures', IFRS 4 'Insurance Contracts' and IFRS 16 'Leases', address the financial reporting impacts due to the interest rate benchmark reform, including the replacement of an IBOR benchmark rate with an alternative benchmark rate. Phase 2 is effective for financial reporting periods beginning on or after January 1, 2021;
- Covid-19-Related Rent Concessions - amendment to IFRS 16 'Leases', which extends the practical relief provided to lessees from performing lease modification accounting on a COVID-19-related rent concession when certain criteria are met. The amendment is applicable for lease payments due on or before 30 June 2021, and
- Lessor forgiveness of lease payment (IFRS 9 and IFRS 16)

No material impact was identified upon adoption of the new and amended standards.

2.5 Standards issued but not yet effective

Certain new accounting standards, amendments and interpretations have been published that are mandatory for 31 December 2023 reporting periods and have not been early adopted by the Fund. The management is in process of assessing the impact of new standards and interpretation on its financial statements.

2.6 Rental revenue

Rental income arising from operating leases on investment properties is recognised, net of discount, in accordance with the terms of lease contracts over the lease term on a straight-line basis over the non-cancellable period of lease.

2.7 Earnings per unit

Earnings per unit ("EPU") is calculated by dividing the total comprehensive income attributable to unit holders of the Fund by the weighted average number of units outstanding during the year.

2.8 Investment properties

Investment property is the property which is held (by owner or lessee under finance lease) either to earn rental income or for capital appreciation or for both. Investment property is initially measured at cost and are stated subsequently at cost less accumulated depreciation and impairment in value, if any. Freehold land is not depreciated. The cost of investment property is depreciated on a straight-line basis over estimated useful lives of the assets.

An investment property is derecognized on sale or disposal when permanently withdrawn or when transferred to inventory properties. Any gain or loss arising from de-recognition of the property is recognized in the profit or loss immediately.

Investment properties also include properties under construction for future use as investment properties. These are carried at fair value, or at cost where fair value cannot be reliably determined and the construction is incomplete.

2 BASIS OF PREPARATION SIGNIFICANT ACCOUNTING POLICIES (continued)

2.9 Leases

At the inception of the contract, the Fund assesses whether a contract is or contains a lease. The Fund recognises a Right of Use ("RoU") asset and a corresponding lease liability with respect to all lease agreements in which it is the lessee, except for short-term leases (defined as leases with a lease term of twelve months or less) and leases of low value assets. For these leases, the Fund recognises the lease payments as an operating expense on a straight-line basis over the term of the lease unless another systematic basis is more representative of the time pattern in which economic benefits from the leased asset are consumed.

Lease liabilities

The lease liability is initially measured at the net present value of the lease payments that are not paid at the commencement date. The lease payments are discounted using the interest rate implicit in the lease. If that rate cannot be readily determined, which is generally the case for leases in the Fund, the lessee's incremental borrowing rate is used, being the rate that the individual lessee would have to pay to borrow the funds necessary to obtain an asset of similar value to the RoU asset in a similar economic environment with similar terms, security and conditions.

To determine the incremental borrowing rate, the Fund:

- where possible, uses recent third-party financing received by the individual lessee as a starting point, adjusted to reflect changes in financing conditions since third party financing was received;
- uses a build-up approach that starts with a risk-free interest rate adjusted for credit risk for leases held by the individual lessee, which does not have recent third-party financing, and
- makes adjustments specific to the lease, for example term, country, currency and security.

Right-of-use (RoU) assets

The RoU assets comprise the initial measurement of the corresponding lease liability, lease payments made at or before the commencement day and any initial direct costs. They are subsequently measured at cost less accumulated depreciation and impairment losses, if any.

RoU assets are depreciated over the shorter period of the lease term or the economic useful life of the underlying asset. If a lease transfer's ownership of the underlying asset or the cost of the RoU asset reflects that the Company expects to exercise a purchase option, the related RoU asset is depreciated over the useful life of the underlying asset. The depreciation starts at the commencement date of the lease.

The RoU assets are presented as a separate line in the statement of financial position.

The Fund determines whether a RoU asset is impaired and accounts for any identified impairment loss.

Variable rents that do not depend on an index or rate are not included in the measurement the lease liability and the RoU asset. The related payments are recognised as an expense in the period in which the event or condition that triggers those payments occurs and are included in the profit or loss.

Net investment in finance lease

Net investment in finance lease includes gross investment in finance lease and related unearned income (if any).

Gross investments in finance lease include the total of future lease payments on finance leases (lease receivables), plus estimated residual amounts receivable. The difference between the lease receivables and the cost of the leased asset is recorded as unearned lease finance income and for presentation purposes, is deducted from the gross investment in finance leases.

MUSHARAKA REIT FUND

(Managed by Musharaka Capital Company)

Notes to the financial statements for the year ended 31 December 2022 (continued)

(All amounts in Saudi Riyals unless otherwise stated)

2 BASIS OF PREPARATION SIGNIFICANT ACCOUNTING POLICIES (Continued)

2.10 Cash and cash equivalents

Cash and cash equivalents include cash in hand and with banks and other short-term highly liquid investments, if any, with original maturities of three months or less from the purchase date.

2.11 Borrowings

Borrowings are initially recognised at the fair value (being proceeds received), net of eligible transaction costs incurred, if any. Subsequent to initial recognition, long-term borrowings are measured at amortised cost using the effective interest rate method. Any difference between the proceeds (net of transaction costs) and the redemption amount is recognised in profit or loss over the period of the borrowings using the effective interest rate method.

Borrowings are removed from the statement of financial position when the obligation specified in the underlying contract is discharged, cancelled or expired. The difference between the carrying amount of a financial liability that has been extinguished or transferred to another party and the consideration paid, including any non-cash assets transferred or liabilities assumed, is recognised in profit or loss as other income or financial costs.

Borrowings are classified as current liabilities unless the Fund has an unconditional right to defer settlement of the liability for at least twelve months after the reporting period.

General and specific borrowing costs that are directly attributable to the acquisition, construction or production of qualifying assets are capitalised during the period of time that is required to complete and prepare the asset for its intended use or sale. Qualifying assets are assets that necessarily take a substantial period of time to get ready for their intended use or sale. Investment income earned on the temporary investment of specific borrowings pending their expenditure on qualifying assets is deducted from the borrowing costs eligible for capitalisation. Other borrowing costs are expensed in the period in which they are incurred.

2.12 Net assets value per unit

The net assets value (NAV) per unit as disclosed on the statement of financial position is calculated by dividing the net assets of the Fund by the number of units outstanding at the period end.

2.13 Dividends

Dividends are recognised when declared during the financial year and no longer at the discretion of the Fund. Unpaid dividends to the unit holders are recognized as a liability in the financial statements in the period in which the dividends are declared by the Fund's Board.

2.14 Financial instruments

2.14.1 Financial assets

(i) Classification

Financial assets at amortised cost

Financial assets at amortised cost are subsequently measured using the effective interest (EIR) method and are subject to impairment. Gains and losses are recognised in profit or loss when the asset is derecognised, modified or impaired.

The Fund's financial assets at amortised cost includes lease receivables, investment in finance lease and cash and cash equivalents.

The Fund classifies its financial assets as measured at amortised cost as such assets are held for collection of contractual cash flows where those cash flows represent solely payments of principal and interest.

MUSHARAKA REIT FUND

(Managed by Musharaka Capital Company)

Notes to the financial statements for the year ended 31 December 2022 (continued)

(All amounts in Saudi Riyals unless otherwise stated)

2 BASIS OF PREPARATION SIGNIFICANT ACCOUNTING POLICIES (Continued)

2.14 Financial instruments (continued)

2.14.1 Financial assets (continued)

(i) Classification (continued)

Financial assets at fair value through profit or loss

Financial assets are classified as investments at fair value through profit or loss if they are acquired for the purpose of selling or repurchasing them in the near term. The Fund designated its holding in a local quoted securities portfolio as financial assets at fair value through profit or loss. Such investments are carried in the statement of financial position at fair value with net changes in fair value presented in the statement of profit or loss.

(ii) Recognition and derecognition

At initial recognition, the Fund measure financial assets at its fair value plus, in the case of a financial asset not at fair value through profit or loss, transactions costs that are directly attributable to the acquisition of financial asset. Transactions cost of financial assets carried at fair value through profit or loss are expensed in profit or loss.

The Fund derecognizes a financial asset when the contractual cash flows from the asset expire or it transfers its rights to receive contractual cash flows on the financial asset in a transaction in which substantially all the risks and rewards of ownership are transferred. Any interest in transferred financial assets that is created or retained by the Fund is recognized as a separate asset or liability.

(iii) Measurement

Subsequent measurement of financial assets depends on the Fund's business model for managing the assets and the cash flow characteristics of the assets. Assets that are held for collection of contractual cash flows where those cash flows represent solely payment of principal and interest are measured at amortised cost. A gain or loss on a financial instrument that is subsequently measured at amortized cost and is not part of the hedging relationship is recognized in profit or loss when the asset is derecognized or impaired. Interest income from these financial assets is calculated using the effective interest rate method.

Currently, the Fund does not hold any equity instruments, therefore the related accounting policies are not presented.

2.14.2 Financial liabilities

All financial liabilities are recognised at the time when the Fund becomes a party to the contractual provisions of the instrument. Financial liabilities are recognized initially at fair value less any directly attributable transaction cost. Subsequent to initial recognition, these are measured at amortized cost using the effective interest method.

A financial liability is derecognized when the obligation under the liability is discharged or cancelled or expired. Where an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is treated as a derecognition of the original liability and the recognition of a new liability, and the difference in respective carrying amounts is recognised in the profit or loss.

2.14.3 Offsetting financial assets and liabilities

Financial assets and liabilities are offset and net amounts are reported in the financial statements, when the Fund has a legally enforceable right to set off the recognized amounts and intends either to settle on a net basis, or to realize the assets and liabilities simultaneously.

MUSHARAKA REIT FUND

(Managed by Musharaka Capital Company)

Notes to the financial statements for the year ended 31 December 2022 (continued)

(All amounts in Saudi Riyals unless otherwise stated)

2 BASIS OF PREPARATION SIGNIFICANT ACCOUNTING POLICIES (Continued)

2.15 Impairment of financial and non-financial assets

2.15.1 Impairment of non-financial assets

The Fund assesses at each reporting date whether there is an indication that a non-financial asset may be impaired. If any indication exists, or when annual impairment testing for an asset is required, the Fund estimates the asset's recoverable amount. An asset's recoverable amount is the higher of an asset's or cash-generating unit's fair value less costs to sell and its value in use and is determined for an individual asset, unless the asset does not generate cash inflows that are largely independent of those from other assets or Fund's of assets. Where the carrying amount of an asset exceeds its recoverable amount, the asset is considered impaired and is written down to its recoverable amount. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. In determining fair value less costs to sell, an appropriate valuation model is used. These calculations are corroborated by valuation multiples, quoted share prices for publicly traded entities or other available fair value indicators.

Impairment losses from continuing operations are recognised in profit or loss in those expense categories consistent with the function of the impaired asset.

2.15.2 Impairment of financial assets

The Fund recognises an allowance for expected credit losses (ECLs). ECLs are recognised in two stages. For credit exposures for which there has not been a significant increase in credit risk since initial recognition, ECLs are provided for credit losses that result from default events that are possible within the next 12-months (a 12-month ECL). For those credit exposures for which there has been a significant increase in credit risk since initial recognition, a loss allowance is required for credit losses expected over the remaining life of the exposure, irrespective of the timing of the default (a lifetime ECL).

For rent receivables the Fund applies a simplified approach in calculating ECLs. Therefore, the Fund has established a provision matrix that is based on its historical credit loss experience, adjusted for forward-looking factors specific to the tenants and the economic environment. Collateralized debts are assessed by management for Expected Credit Loss (ECL) on an individual basis, whereby the debt is assessed in conjunction with underlying collateralization upon which ECL is calculated.

2.16 Financial income and cost

Financial income is measured using the effective interest rate, which is the rate that exactly discounts the estimated future cash receipts through the expected life of the financial asset or a shorter period, where appropriate, to the net carrying amount of the financial asset.

Finance income is recognised as the interest accrues using the effective interest method.

3 SIGNIFICANT ACCOUNTING JUDGEMENTS, ESTIMATES AND ASSUMPTIONS

The preparation of this financial statements requires management to make judgments, estimates and assumptions that affect the reported amounts of revenues, expenses, assets and liabilities, and the accompanying disclosures and the disclosure of contingent liabilities at the reporting date. Uncertainty about these assumptions and estimates could result in outcomes that require a material adjustment to the carrying amount of the assets or liabilities affected in future years.

Estimates and their underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the period in which the estimates are revised.

MUSHARAKA REIT FUND

(Managed by Musharaka Capital Company)

Notes to the financial statements for the year ended 31 December 2022 (continued)

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3 SIGNIFICANT ACCOUNTING JUDGEMENTS, ESTIMATES AND ASSUMPTIONS (Continued)

The key judgments, estimates and assumptions that have a significant impact on the financial statements of the Fund are discussed below:

Valuation of investment properties

The Fund hires the services of third parties to obtain estimates of the market value of investment properties using recognised valuation techniques for the purposes of their impairment review and disclosures in the financial statements. The key assumptions used to determine fair values of investment properties are disclosed in Note 8.

Useful lives of investment properties

The Fund Manager determines the estimated useful lives of its investment properties for calculating depreciation. This estimate is determined after considering the expected usage of the property or physical wear and tear. The Fund Manager periodically reviews estimated useful lives and the depreciation method to ensure that the method and period of depreciation are consistent with the expected pattern of economic benefits from such assets.

Impairment of financial assets held at amortised cost

The Fund uses a provision matrix to calculate Expected Credit Losses ("ECLs") for lease receivables. The provision rates are based on days past due for groupings of various customer segments that have similar loss patterns (i.e., by customer type, and coverage by guarantees and other forms of credit insurance).

The provision matrix is initially based on the Fund's historically observed default rates. The calculation reflects the probability-weighted outcome, the time value of money and reasonable and supportable information that is available at the reporting date about past events, current conditions and forecasts of future economic conditions. At every reporting date, the historically observed default rates are updated and changes in the forward looking estimates are analysed.

The assessment of the correlation between historically observed default rates, forecast economic conditions and ECLs is a significant estimate. The amount of ECLs is sensitive to changes in circumstances and forecast economic conditions. The Fund's historical credit loss experience and forecast of economic conditions may also not be representative of customer's actual default in the future. The information about the ECLs on the lease receivables is disclosed in Note 12.

4 RENTAL REVENUE

During the year ended 31 December 2022, the Fund has earned revenue of Saudi Riyals 112.2 million (2021: Saudi Riyals 100.7 million) from rentals of investment properties, that is recorded on an accrual basis in accordance with the terms of the corresponding contracts. Revenue also includes, rental revenue amounting to Saudi Riyals 8.5 million (2021: Saudi Riyals 13.4 million) earned through related party, (also see Note 20).

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5 FUND MANAGEMENT FEE

The Fund is managed and administered by the Fund Manager. For these services, the Fund calculates the management fee, as set out in the Fund's terms and conditions, at an annual rate of 1.2% of the Fund's total assets after deducting accrued fee and expenses. For the year ended 2022 management fee amounted to Saudi Riyals 15.7 million (2021: Saudi Riyals 16.6 million).

6 OTHER OPERATING EXPENSES

		2022	2021
	Note		
Properties maintenance expenses	6.1	7,624,784	1,270,142
Manpower expenses	6.1	2,442,183	-
Fees and subscriptions		901,091	2,533,932
Property management fee		899,168	1,237,571
Valuation fee		434,826	268,130
Board of director's fee		30,000	30,000
Others		1,336,302	2,479,073
		13,668,354	7,818,848

6.1 This represent the expenses incurred on residential properties, commercial properties and hotel apartments i.e. maintenance, utilities, and other miscellaneous operating expenses, such properties are managed by the Fund, which were previously leased and managed by third parties.

7 FINANCE INCOME

	2022	2021
Finance income on investment in finance leases (Note 11)	11,596,685	11,911,540

8 FINANCE COST

		2022	2021
	Note		
Finance cost on borrowings (Note 16)		23,516,480	8,950,014
Finance cost on lease liabilities (Note 17)		6,131,911	6,371,246
Amortization of loan arrangement fee	8.1	2,633,765	1,863,249
		32,282,156	17,184,509

8.1 Loan arrangement fee constitutes administrative and consultancy fee on the unavailed loan facility arrange by the Fund. Such arrangement fee for the loan is amortized over the loan term once the loan facilities are withdrawn.

9 ZAKAT PROVISION

During 2021, zakat provision amounting to Saudi Riyals 1.96 million was recognized in the books of accounts by the Fund manager, and the registration process with the ZATCA was initiated. However, based on the ZATCA resolution no 29791 (the "Resolution") issued in 2022, such provision was reversed. The Resolution stated that investment funds are not required to pay any zakat and are only required to be registered with the ZATCA. The Resolution further explained that the unitholders are responsible to pay the zakat in lieu of their investments in funds without any liability on part of the funds.

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10 INVESTMENT PROPERTIES

		2022	2021
Owned investment properties	Note 10.1	1,247,386,713	1,016,931,494
Right of use assets	10.2	87,605,013	91,990,981
		<u>1,334,991,726</u>	<u>1,108,922,475</u>

10.1 Owned investment properties

	Land	Buildings	Furniture and fixtures	Leasehold improvements	Total
2022					
<u>Cost</u>					
At 1 January	563,786,444	473,270,581	66,561,648	-	1,103,618,673
Additions during the year	76,135,145	177,371,107	-	6,785,241	260,291,493
At 31 December	<u>639,921,589</u>	<u>650,641,688</u>	<u>66,561,648</u>	<u>6,785,241</u>	<u>1,363,910,166</u>
<u>Accumulated depreciation and impairment</u>					
At 1 January	11,786,649	51,501,002	23,399,528	-	86,687,179
Charge for the period		14,744,209	6,652,519		21,396,728
Impairment charge for the year	7,692,167	747,379	-	-	8,439,546
At 31 December	<u>19,478,816</u>	<u>66,992,590</u>	<u>30,052,047</u>	<u>-</u>	<u>116,523,453</u>
Net book value at 31 December	<u>620,442,773</u>	<u>583,649,098</u>	<u>36,509,601</u>	<u>6,785,241</u>	<u>1,247,386,713</u>

	Land	Buildings	Furniture and fixtures	Leasehold improvements	Total
2021					
<u>Cost</u>					
At 1 January	529,376,947	424,184,388	52,678,780	-	1,006,240,115
Additions during the year	34,409,497	49,086,193	13,882,868	-	97,378,558
At 31 December	<u>563,786,444</u>	<u>473,270,581</u>	<u>66,561,648</u>	<u>-</u>	<u>1,103,618,673</u>
<u>Accumulated depreciation and impairment</u>					
At 1 January	7,082,415	40,660,071	17,750,589	-	65,493,075
Charge for the year	-	10,840,931	5,648,939	-	16,489,870
Impairment charge for the year	4,704,234	-	-	-	4,704,234
At 31 December	<u>11,786,649</u>	<u>51,501,002</u>	<u>23,399,528</u>	<u>-</u>	<u>86,687,179</u>
Net book value at 31 December	<u>551,999,795</u>	<u>421,769,579</u>	<u>43,162,120</u>	<u>-</u>	<u>1,016,931,494</u>

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10 INVESTMENT PROPERTIES (continued)

10.1 Owned investment properties (continued)

Owned investment properties comprise the Fund's investments in various residential compounds, warehousing facilities, showrooms, retail, hotels, hotel apartments, commercial and administrative buildings located within the Kingdom of Saudi Arabia except for one warehouse in the United Arab Emirates ("UAE").

Investment properties as of 31 December 2022 with a net book value of Saudi Riyals 1,145.56 million (31 December 2021: Saudi Riyals 799.54 million) are pledged as security against borrowings obtained from Bank Al Rajhi (also see Note 16).

In accordance with Article 22 of the Real Estate Investments Funds Regulations issued by CMA in the Kingdom of Saudi Arabia, the Fund Manager evaluates the Fund's assets based on valuations carried out by two independent evaluators.

Additions during 2022 represent the acquisition of Verdun Tower in Riyadh, by the Fund with a total investment of Saudi Riyals 253.5 million (Saudi Riyals 76.1 million related to land and Saudi Riyals 177.3 million related to Building), including acquisition costs.

The fair values of the properties are based on valuations performed by the following independent valuers accredited by the Saudi Authority for Accredited Valuers:

- Olaat Valuation Company;
- Abaad Real Estate Valuation;
- ValuStrat consulting;
- Sima and partner property valuation; and
- JLL Valuation

As at 31 December 2022, the average valuation of the above investment properties amounted to Saudi Riyals 1,351.20 million (31 December 2021: Saudi Riyals 1,063.56 million). Key assumptions used for the valuation of investment properties include discount rate at 8% to 11% (31 December 2021: 8% to 10%) and income Cap rate ranging from 7.5% to 8.5% (31 December 2021: 8% to 10%). Based on the valuation as of 31 December 2022, the Fund has recognized an impairment loss amounting to Saudi Riyals 8.4 million (31 December 2021: 4.7 million) on such properties.

Fair value hierarchy

The fair value of investment properties is classified in the level - 2 of fair value hierarchy, as the valuation is carried out with reference to the observable market data, among other factors.

Any significant movement in the assumptions used for fair valuation of investment properties such as discount rates, yield, rental growth, occupancy rate etc. would result in significantly lower/higher fair value of those assets.

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Notes to the financial statements for the year ended 31 December 2022 (continued)

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10 INVESTMENT PROPERTIES (continued)**10.2 Right of use assets**

	Land	Buildings	Total
2022			
Cost			
At 1 January	58,403,266	58,430,976	116,834,242
Additions during the year	2,907,007	-	2,907,007
At 31 December	61,310,273	58,430,976	119,741,249
Accumulated depreciation			
At 1 January	12,709,490	12,133,771	24,843,261
Charge for the year	3,755,555	3,537,420	7,292,975
At 31 December	16,465,045	15,671,191	32,136,236
Net book value at 31 December	44,845,228	42,759,785	87,605,013
2021			
Cost			
At 1 January and 31 December	58,403,266	58,430,976	116,834,242
Accumulated depreciation			
At 1 January	9,206,934	8,596,602	17,803,536
Charge for the year	3,502,556	3,537,169	7,039,725
At 31 December	12,709,490	12,133,771	24,843,261
Net book value at 31 December	45,693,776	46,297,205	91,990,981

The Fund has acquired right of use ("ROU") for certain commercial properties, i.e. land and building for a term ranging from 15.5 to 16.5 years.

The fair values of the ROU are based on valuations performed by Olaat Valuation Company and Abaad Real Estate Valuation (31 December 2021: Olaat Valuation Company and Abaad Real Estate Valuation,) all are independent valuers accredited by the Saudi Authority for Accredited Valuers.

As at 31 December 2022, the average valuation of the buildings amounted to Saudi Riyals 62.3 million (31 December 2021: Saudi Riyals 66.5 million) calculated by allocating the overall average valuation of the acquired right-of-use for buildings amounting to Saudi Riyals 126.1 million (31 December 2021: Saudi Riyals 134.4 million) to the remaining area after the derecognition of the portion of buildings that was derecognised on finance lease arrangements. Key assumptions used for the valuation of the ROU include discount rate ranging from 9.5% to 12% (31 December 2021: 7.5% to 12%).

Fair value hierarchy

The fair value of investment properties is classified in the level-2 of fair value hierarchy.

Any significant changes in the assumptions used for fair valuation of investment properties such as discount rates, yield, rental growth, vacancy rate etc. would result in significantly lower/higher fair value of those assets.

MUSHARAKA REIT FUND

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Notes to the financial statements for the year ended 31 December 2022 (continued)

(All amounts in Saudi Riyals unless otherwise stated)

11 NET INVESTMENT IN FINANCE LEASES

Net investment in finance leases consists of:

	2022	2021
Gross investment in finance leases	334,727,768	356,804,687
Less: Unearned finance income	(114,782,370)	(126,379,061)
	<u>219,945,398</u>	<u>230,425,626</u>

The maturity analysis of investment in finance leases as at 31 December 2022 is as follows:

	Less than one year	Two to five years	More than five years	Total
Gross lease receivables	20,822,533	101,396,000	212,509,235	334,727,768
Finance income	(11,048,135)	(43,473,230)	(60,261,005)	(114,782,370)
	<u>9,774,398</u>	<u>57,922,770</u>	<u>152,248,230</u>	<u>219,945,398</u>

The maturity analysis of investment in finance lease as at 31 December 2021 is as follows:

	Less than one year	Two to five years	More than five years	Total
Gross lease receivables	22,753,525	86,525,469	247,525,693	356,804,687
Finance income	(9,674,608)	(41,980,469)	(74,723,984)	(126,379,061)
	<u>13,078,917</u>	<u>44,545,000</u>	<u>172,801,709</u>	<u>230,425,626</u>

Net investment in finance lease does not include any receivable balances which are either past due or impaired.

12 LEASE RENTAL RECEIVABLES

		2022	2021
Lease receivables:	Note		
- Billed		35,273,665	40,621,109
- Unbilled		3,757,566	3,004,909
Total receivables	12.1	<u>39,031,231</u>	43,626,018
Less: allowance for expected credit losses	12.2	<u>(12,325,508)</u>	(8,109,586)
		<u>26,705,723</u>	<u>35,516,432</u>

12.1 An aged analysis of lease receivables as at 31 December 2022 and 31 December 2021 is as follows:

	Neither past due nor impaired	< 180 days	181-270 days	270-365 days	> 365 days	Total
At 31 December 2022	3,757,566	12,700,930	2,526,684	12,958,236	7,087,815	39,031,231
At 31 December 2021	3,004,909	25,907,518	1,784,617	6,301,667	6,627,307	43,626,018

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12 LEASE RENTAL RECEIVABLES (continued)

12.2 Movement in allowance for expected credit losses is as follows:

	2022	2021
At the beginning of the year	8,109,586	8,888,208
Provision charged during the year	5,050,770	(116,394)
Written - off during the year	(834,848)	(662,228)
At the end of year	<u>12,325,508</u>	<u>8,109,586</u>

Lease rental receivables include certain amounts that are past due but not impaired. Based on historical experience, it is expected that all receivables for lease contracts that have not been fully impaired will be collected. Further, the Fund also has other guarantees in the form of promissory notes issued for such parties.

13 PREPAYMENTS AND OTHER ASSETS

	Note	2022	2021
Deferred loan arrangement fee	13.1	-	3,489,350
Prepaid expenses and other assets		2,985,559	-
Value added tax (VAT) receivable		733,264	-
		<u>3,718,823</u>	<u>3,489,350</u>

13.1 Deferred loan arrangement fee constitutes administrative and consultancy fee on the unavailed loan facility.

14 INVESTMENTS CARRIED AT FAIR VALUE THROUGH PROFIT OR LOSS

During 2020, the Fund made an investment in Musharaka Murabaha and Sukuk Fund which is an open-ended investment fund, managed by Musharaka Capital Company. The Fund recognised this investment at fair value through profit or loss ("FVTPL").

15 SHORT TERM MURABAHA DEPOSIT

Short-term Murabaha deposit represent amounts invested by the Fund in Murabaha deposits held with a local financial institution, and have an original maturity of more than 3 months from the placement date with a profit rates 4.5% (31 December 2021: Nil) per annum. As at year end, accrued finance income on such deposit amounted to Saudi Riyals 0.3 million (31 December 2021: Nil).

16 BORROWINGS

	2022	2021
Long-term loan	668,556,977	413,676,688
Less: transaction costs	(11,118,552)	(8,411,424)
	<u>657,438,425</u>	<u>405,265,264</u>

MUSHARAKA REIT FUND

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Notes to the financial statements for the year ended 31 December 2022 (continued)

(All amounts in Saudi Riyals unless otherwise stated)

16 BORROWINGS (continued)

During 2018, the Fund entered into a Sharia compliant borrowing arrangement facility, with a local commercial bank in the form of long-term loans with a total facility limit of Saudi Riyals 400 million to finance the acquisition of income generating assets. Further, during 2021, the Fund has increased its credit facility limit from Saudi Riyals 400 million to Saudi Riyals 1 billion. These facilities carry interest at SIBOR (6 months) plus margin, which is commensurate with the market rate, and is repayable on a single lumpsum payment after seven years from the date of withdrawal (28 June 2018). Interest is payable on a semi-annual basis.

The Fund has withdrawn Saudi Riyals 668.55 million till 31 December 2022 (31 December 2021: Saudi Riyals 413.67 million) for the purpose of acquiring investment properties. The loan is secured by a mortgage on certain investment properties (see Note 10).

17 LEASE LIABILITIES

	2022	2021
Gross lease liabilities	183,026,283	191,716,280
Less: finance charges not yet due	(43,607,177)	(49,496,093)
	<u>139,419,106</u>	<u>142,220,187</u>
	2022	2021
At 1 January	142,220,187	146,838,941
Addition	2,907,007	-
Finance cost for the year	6,131,912	6,371,246
Rent concession	(320,000)	(820,000)
Payments	(11,520,000)	(10,170,000)
At 31 December	<u>139,419,106</u>	<u>142,220,187</u>

Lease liabilities represents present value of minimum lease payments for land lease. During the year ended 31 December 2022, the Fund received concession on one of the land parcels carried under lease arrangements for an amount of Saudi Riyals 320,000 (2021: Saudi Riyals 820,000) and has been recognised as other income.

The maturity analysis of lease liabilities as at 31 December 2022 is as follows:

	Less than one year	Two to five years	More than five years	Total
Principal amount of lease liabilities	14,986,735	52,888,000	115,151,548	183,026,283
Finance cost not yet due	(6,334,077)	(19,949,074)	(17,324,026)	(43,607,177)
	<u>8,652,658</u>	<u>32,938,926</u>	<u>97,827,522</u>	<u>139,419,106</u>

The maturity analysis of lease liabilities as at 31 December 2021 is as follows:

	Less than one year	Two to five years	More than five years	Total
Principal amount of lease liabilities	19,210,000	51,106,000	121,400,280	191,716,280
Finance cost not yet due	(4,819,816)	(21,847,940)	(22,828,337)	(49,496,093)
	<u>14,390,184</u>	<u>29,258,060</u>	<u>98,571,943</u>	<u>142,220,187</u>

MUSHARAKA REIT FUND

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Notes to the financial statements for the year ended 31 December 2022 (continued)

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18 UNEARNED RENTAL REVENUE

This represent rental income received in advance and receivable in respect of operating leases of investment properties.

19 ACCRUED EXPENSES AND OTHER LIABILITIES

	2022	2021
Accrued finance costs	11,169,956	2,231,893
Property operating expenses	4,694,914	-
Security deposits	3,253,136	1,114,347
Accrued expenses	432,469	2,086,728
Other	820,101	403,644
	<u>20,370,576</u>	<u>5,836,612</u>

20 RELATED PARTIES TRANSACTIONS AND BALANCES

Related parties represent the Fund Manager, Al-Inma Investment Company (Custodian), the unitholders, the Fund's Board and the Fund Sharia Committee.

The following table represents details of transactions that have been entered into with the related parties:

a) Related parties transactions

Related party	Nature of transaction with related party	2022	2021
Fund Manager	Management fees	15,780,449	16,629,524
	Commission on purchase of investment property	2,350,000	855,000
	Loan arrangement fee	-	1,444,500
Fund Board	Board of Directors remunerations	30,000	30,000
Sharia Committee	Sharia Committee remunerations	33,000	33,000
Custodian	Custody fee	100,000	100,000
Units holder	Rental revenue	8,580,822	13,481,532

The Fund Manager's investment in the Fund at 31 December 2022 is 4.64 million units (31 December 2021 is 4.64 million units)

b) Due to related parties

Related party	2022	2021
Fund Manager (accrued management fee)	7,466,719	9,864,843
Custodian (presented under accrued expenses)	141,667	191,667
	<u>7,608,386</u>	<u>10,056,510</u>

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Notes to the financial statements for the year ended 31 December 2022 (continued)

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20 RELATED PARTIES TRANSACTIONS AND BALANCES (continued)

The basis and term of payment as per terms and conditions of the Fund approved by CMA as follows:

Type of fee	Basis and rate	Payment term
Management fees	1.2% of the total assets after deducting accrued fees and expenses	Every six (6) months
Board of Directors remuneration	Saudi Riyals 5,000 per meeting only payable to the independent members, maximum up to Saudi Riyals 80,000 per annum for all members.	After the meeting of the Board of Directors
Sharia Committee remuneration	Saudi Riyals 33,000 per annum	Every six (6) months
Custody fees	Saudi Riyals 100,000 per annum	Annually
Debt arrangement fees	Up to 1.5% of the arranged facility	Upon arrangement

21 FINANCIAL RISK MANAGEMENT

The Fund's activities expose it to a variety of financial risks: market risk (including currency risk, fair value and cash flow interest rate risks and price risk), credit risk and liquidity risk. 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.

Risk management is carried out by senior management under policies approved by the Board of Directors. Senior management identifies, evaluates and controls financial risks in close co-operation with the Fund's operating units. The most important types of risk are credit risk, currency risk and fair value and cash flow interest rate risks.

The Board of Directors has overall responsibility for establishment and oversight of the Fund's risk management framework. The executive management team is responsible for developing and monitoring the Fund's risk management policies. The team regularly meets and any changes and compliance issues are reported to the Board of Directors.

Risk management systems are reviewed regularly by the executive management team to reflect changes in market conditions and the Fund's activities. The Fund, through its training and management standards and procedures, aims to develop a disciplined and constructive control environment in which all employees understand their roles and obligations.

The Board of Directors oversees compliance by management with the Fund's risk management policies and procedures, and reviews the adequacy of the risk management framework in relation to the risks faced by the Fund.

Financial instruments carried on the statement of financial position include cash and cash equivalents, trade and other receivables, investments, borrowings, accounts payable and other current liabilities. The particular recognition methods adopted are disclosed in the individual policy statements associated with each item.

Financial asset and liability are offset and net amounts reported in the financial statements, when the Fund has a legally enforceable right to set off the recognized amounts and intends either to settle on a net basis, or to realize the asset and liability simultaneously.

MUSHARAKA REIT FUND

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Notes to the financial statements for the year ended 31 December 2022 (continued)

(All amounts in Saudi Riyals unless otherwise stated)

21 FINANCIAL RISK MANAGEMENT (continued)

Market risk

Market risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market prices. Market risk comprises three types of risk: interest rate risk, currency risk and other price risk.

Fair value and cash flow Interest rate risk

Fair value and cash flow interest rate risks are the exposures to various risks associated with the effect of fluctuations in the prevailing interest rates on the Fund's financial positions and cash flows. The Fund's interest rate risks arise mainly from its borrowings, which are at floating rate of interest and are subject to re-pricing on a regular basis. Management monitors the changes in interest rates. The interest rate profile of the Fund's interest-bearing financial instruments as reported to the management of the Fund is as follows:

If Saudi Interbank Offered Rate ("SIBOR") had been 1% higher or lower with all other variables held constant, the impact on the equity and profit before zakat for the year ended 31 December 2022 would have been Saudi Riyals 2.1 million (2021: Saudi Riyals 2.1 million).

Currency risk

Currency risk is the risk that the value of a financial instrument will fluctuate due to changes in foreign exchange rates. The Fund's transactions are principally in Saudi Riyals and US Dollars. The Fund's management monitors such fluctuations and manages its effect on the financial statements accordingly.

Price risk

The risk that the value of a financial instrument will fluctuate as a result of changes in market prices, whether those changes are caused by factors specific to the individual instrument or its issuer or factors affecting all instruments traded in the market.

Credit risk

Credit risk is the risk that one party to a financial instrument will fail to discharge an obligation and cause the other party to incur a financial loss. The Fund has no significant concentration of credit risk. To reduce exposure to credit risk the Fund has developed a formal approval process whereby credit limits are applied to its customers. The management also continuously monitors the credit exposure towards the customers and makes provision against those balances considered doubtful of recovery. To mitigate the risk, the Fund has a system of assigning credit limits to its customers based on an extensive evaluation based on customer profile and payment history. Outstanding customer receivables are regularly monitored.

The Fund's gross maximum exposure to credit risk at the reporting date is as follows:

	2022	2021
Financial assets		
Investments carried at fair value through profit or loss	5,312,150	5,282,150
Net investment in finance leases	219,945,398	230,425,626
Lease receivables	26,705,723	35,516,432
Prepayments and other assets	3,718,823	3,489,350
Short-term Murabaha deposit	35,000,000	-
Cash and cash equivalents (excluding cash in hand)	31,486,197	58,135,003
	<u>322,168,291</u>	<u>332,848,561</u>

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21 FINANCIAL RISK MANAGEMENT (continued)

Provisioning policy

The Fund allocates each exposure to a credit risk grade-based credit risk characteristics and the days past due. The expected loss rates are based on the payment profiles of the customers on due dates.

The loss allowances is measured on lifetime ECLs: ECLs result from all possible default events over the expected life of a financial instrument.

Liquidity risk

Liquidity risk is the risk that an enterprise will encounter difficulty in raising funds to meet commitments associated with financial instruments. Liquidity risk may result from an inability to sell a financial asset quickly at an amount close to its fair value. Liquidity risk is managed by monitoring on a regular basis that sufficient funds are available through committed credit facilities to meet any future commitments.

2022	Carrying amount	Total	Contractual cash flows		
			Less than 1 year	1 year to 5 years	More than 5 years
<i>Non-derivative financial liabilities</i>					
Borrowings	657,438,425	668,556,977	-	343,612,728	324,944,249
Lease liabilities	139,419,106	183,026,283	14,986,735	52,888,000	115,151,548
Unearned rental revenue	15,595,152	15,595,152	15,595,152	-	-
Accrued fund management fees	7,466,719	7,466,719	7,466,719	-	-
Accrued expenses and other liabilities	20,370,576	20,370,576	20,370,576	-	-
	<u>840,289,979</u>	<u>895,015,708</u>	<u>58,419,183</u>	<u>396,500,728</u>	<u>440,095,797</u>

It is not expected that the cash flows included in the maturity analysis could occur significantly earlier, or at significantly different amount.

2021	Carrying amount	Total	Contractual cash flows		
			Less than 1 year	1 year to 5 years	More than 5 years
<i>Non-derivative financial liabilities</i>					
Borrowings	405,265,264	413,676,688	-	212,614,003	201,062,685
Lease liabilities	142,220,187	191,716,280	19,210,000	51,106,000	121,400,280
Unearned rental revenue	17,855,057	17,855,057	17,855,057	-	-
Accrued fund management fees	9,864,843	9,864,843	9,864,843	-	-
Accrued expenses and other liabilities	5,836,612	5,836,612	5,836,612	-	-
	<u>581,041,963</u>	<u>638,949,480</u>	<u>52,766,512</u>	<u>263,720,003</u>	<u>322,462,965</u>

Capital risk management

The Fund's objective when managing capital is to safeguard the Fund's ability to continue as a going concern so that it can continue to provide returns for shareholders and benefits for other stakeholders; and to maintain a strong capital base to support the sustained development of its businesses.

MUSHARAKA REIT FUND
(Managed by Musharaka Capital Company)

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21 FINANCIAL RISK MANAGEMENT (continued)

Fair value of assets and liabilities

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.

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 market price, because this price 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. The Fund recognizes transfer between levels of fair value at the end of the reporting period during which the change has occurred.

The fair value hierarchy has the following levels:

Level 1 - quoted (unadjusted) market price in active markets for identical assets or liabilities;

Level 2 - valuation techniques for which the lowest level input that is significant to the fair value measurement is directly or indirectly observable; and

Level 3 - valuation techniques for which the lowest level input that is significant to the fair value measurement is unobservable.

The following table shows the carrying amounts and fair values of financial assets and financial liabilities, including their levels in the fair value hierarchy. It does not include fair value information for financial assets and financial liabilities not measured at fair value if the carrying amount is a reasonable approximation of fair value.

	As at 31 December 2022						
	Carrying Amount			Fair value			
	Fair value	Amortized cost	Total	Level 1	Level 2	Level 3	Total
Financial assets							
Investments at fair value through profit or loss	5,312,150	-	5,312,150	5,312,150	-	-	5,312,150
Net investment in finance leases	-	219,945,398	219,945,398	-	-	-	-
Lease rental receivables	-	26,705,723	26,705,723	-	-	-	-
Prepayments and other assets	-	3,718,823	3,718,823	-	-	-	-
Short-term Murabha deposit	-	35,000,000	35,000,000	-	-	-	-
Cash at banks	-	31,486,197	31,486,197	-	-	-	-
	5,312,150	316,856,141	322,168,291	5,312,150	-	-	5,312,150

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Notes to the financial statements for the year ended 31 December 2022 (continued)

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21 FINANCIAL RISK MANAGEMENT (continued)**Financial liabilities**

Borrowings	668,556,977	668,556,977	668,556,977	-	-	-	-
Lease liabilities	-	139,419,106	139,419,106	-	-	-	-
Unearned rental revenue	-	15,595,152	15,595,152	-	-	-	-
Accrued fund management fees	-	7,466,719	7,466,719	-	-	-	-
Accrued expenses and other liabilities	-	20,370,576	20,370,576	-	-	-	-
	668,556,977	851,408,530	851,408,530	-	-	-	-

As at 31 December 2021

	Carrying Amount			Fair value			Total
	Fair value	Amortized cost	Total	Level 1	Level 2	Level 3	
Financial assets							
Investments at fair value through profit or loss	5,282,150	-	5,282,150	5,282,150	-	-	5,282,150
Net investment in finance leases	-	230,425,626	230,425,626	-	-	-	-
Lease receivable	-	35,516,432	35,516,432	-	-	-	-
Prepayments and other assets	-	3,489,350	3,489,350	-	-	-	-
Cash at banks	-	58,135,003	58,135,003	-	-	-	-
	5,282,150	327,566,411	332,848,561	5,282,150	-	-	5,282,150

Financial liabilities

Borrowings	413,676,688	-	413,676,688	413,676,688	-	-	413,676,688
Lease liabilities	-	142,220,187	142,220,187	-	-	-	-
Unearned rental revenue	-	17,855,057	17,855,057	-	-	-	-
Accrued fund management fees	-	9,864,843	9,864,843	-	-	-	-
Accrued expenses and other liabilities	-	5,836,612	5,836,612	-	-	-	-
	413,676,688	175,776,699	589,453,387	413,676,688	-	-	413,676,688

Measurement of fair values

The valuation of public traded investment classified under level 1 is based upon the closing market price of that security as of the valuation date, less a discount if the security is restricted. The fair value of level 2 fixed-income investment and funds are taken from reliable and third-party sources. Fair values of other investments classified in Level 3 are, where applicable, determined based on discounted cash flows.

Cash and cash equivalents, receivables from related parties and the financial liabilities except employee benefit obligations are measured at amortised cost.

MUSHARAKA REIT FUND

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22 MATURITY ANALYSIS OF ASSETS AND LIABILITIES

Non-current portion of net investment in finance leases (Note 11), long term loan and non-current portion of lease liabilities (Note 17) are expected to be realized after twelve (12) months from the reporting date. All other financial assets and liabilities are of a current nature.

23 DIVIDENDS

During 2022, the Fund paid dividends of Saudi Riyals 52.8 million (2021: Saudi Riyals 52.8 million). As per the terms and conditions of the Fund, it aims to distribute cash dividend, at least once annually, not less than 90% of the net profit.

24 SUBSEQUENT EVENTS

On 23 Jan 2023, the Fund's Board approved to distribute dividends with regards to the year ended 31 December 2022, amounting to Saudi Riyals 0.2 per unit, totaling to Saudi Riyals 17.6 million to its unitholders.

25 APPROVAL OF THE FINANCIAL STATEMENTS

The financial statements were approved by the Fund's Board on 30 March 2022 (corresponding to 8th Ramadan, 1444H).