OMAN ARAB BANK

ANNUAL REPORT 2013

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FINANCIAL HIGHLIGHTS

Financial Highlights

	2013	2012	2011	2010	2009
	RO '000	RO '000	RO '000	RO '000	RO '000
Total Assets	1,456,355	1,370,409	1,114,665	953,655	858,891
Deposits	1,149,153	1,031,144	909,660	769,761	696,072
Net Loans	1,076,291	934,814	829,845	660,346	565,557
Shareholders' Equity	187,152	172,511	148,956	125,831	111,481
Net Profit	25,023	25,270	23,205	23,170	23,081
Net interest income	42,452	40,967	36,480	33,357	30,778
Other operating income	21,376	19,861	18,895	18,175	17,768
Net operating income	63,828	60,828	55,375	51,532	48,546
Operating expenses	(33,798)	(28,542)	(25,347)	(21,970)	(20,541)
Provision for loan impairment	(6,351)	(5,727)	(6,173)	(4,562)	(4,325)
Release/recovery from provision for loan impairment	4,999	2,284	2,667	1,742	2,459
Taxation	(3,655)	(3,573)	(3,317)	(3,572)	(3,058)
Net Profit after taxation	25,023	25,270	23,205	23,170	23,081
Dividend	11,600	11,600	18,000	17,000	15,000
Total Assets	1,456,355	1,370,409	1,114,665	953,655	858,891
Gross Loans and advances	1,110,606	966,335	857,000	682,349	583,404
Provision for loan impairment	(34,315)	(31,521)	(27,155)	(22,003)	(17,847)
Net Loans and advances	1,076,291	934,814	829,845	660,346	565,557
Non-performing loans	36,613	26,087	24,446	20,953	15,787
Customer deposits	1,149,153	1,031,144	909,660	769,761	696,072
Shareholders' funds	187,152	172,511	148,956	125,831	111,481
Share Capital	116,000	116,000	100,000	85,000	75,000
Ratios					
1. Profitability					
Return on shareholders' funds	13.91%	15.72%	16.89%	19.53%	22.86%
Return on Total Assets	1.77%	2.03%	2.24%	2.56%	2.82%
Cost to income	52.95%	46.92%	45.77%	42.63%	42.31%
2. Capital					
Capital Adequacy (BIS standard)	16.52%	16.91%	13.69%	14.49%	13.44%
Shareholders' funds to Total Assets	12.85%	12.59%	13.36%	13.19%	12.98%
3. Asset Quality					
Non-performing loans to Total loans	3.30%	2.70%	2.85%	3.07%	2.71%
Provision coverage	93.72%	120.83%	111.08%	105.01%	113.05%
4. Liquidity					
Net loans to customer deposits	93.66%	90.66%	91.23%	85.79%	81.25%
Net loans to Total Assets	73.90%	68.21%	74.45%	69.24%	65.85%
Liquid Assets to Customer Deposits	26.19%	36.08%	25.92%	32.70%	36.80%
5. Others					
Dividend rate	10.00%	10.00%	18.00%	20.00%	20.00%
Dividends per share in RO	0.010	0.010	0.180	0.200	0.200
Basic Earnings per share in RO	0.022	0.022	0.023	0.027	0.031

CORPORATE GOVERNANCE REPORT

Deloitte.

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TO THE SHAREHOLDERS OF
OMAN ARAB BANK SAOC

We have performed the procedures prescribed in Capital Market Authority (CMA) Circular No. 16/2003 dated 29 December 2003 with respect to the accompanying corporate governance report of **Oman Arab Bank SAOC** and its application of corporate governance practices in accordance with CMA Code and additional regulations and disclosures with except for the meeting intervals where the Bank follows its own meeting schedule. Our engagement was undertaken in accordance with the International Standards on Related Services applicable to agreed-upon procedures engagements. The procedures were performed solely to assist you in evaluating the Bank's compliance with the code as issued by the CMA.

We report our findings as below:

We found that the Bank's corporate governance report fairly reflects the bank's application of the provisions of the code and is free from any material misrepresentation.

Because the above procedures do not constitute either an audit or a review made in accordance with International Standards on Auditing or International Standards on Review Engagements, we do not express any assurance on the corporate governance report.

Had we performed additional procedures or had we performed an audit or review of the corporate governance report in accordance with International Standards on Auditing or International Standards on Review Engagements, other matters might have come to our attention that would have been reported to you.

Our report is solely for the purpose set forth in the first paragraph of this report and for your information and is not to be used for any other purpose. This report relates only to the accompanying corporate governance report of **Oman Arab Bank SAOC** to be included in its annual report for the year ended 31 December 2013 and does not extend to any financial statements of **Oman Arab Bank SAOC**, taken as a whole.

Deloitte

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سلطنة عمان
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Deloitte & Touche (M.E.)& Co. LLC

Deloitte & Touche (M.E.) & Co. LLC
Muscat, Sultanate of Oman
23 January 2014

CORPORATE GOVERNANCE REPORT

OAB's approach to corporate governance

Framework and Approach to corporate governance and responsibility

The Board is committed to maintaining the highest standards of corporate governance.

The Board believes that corporate governance is about having a set of values and behaviors that governs the Bank's everyday activities - values and behaviors that ensure transparency, fair dealing and protection of the interest of the Bank's stakeholders namely customers, shareholders, employees and the community. In line with this belief, the Board's approach is to consider corporate governance within the broader framework of corporate responsibility and regulatory oversight.

The business case for good governance is compelling. A Bank's level of governance and responsibility has emerged as a significant indicator of its overall health as a business. The genuine commitment to good governance is fundamental to the sustainability of the Bank's business and its performance.

In pursuing its commitment to best practice governance standards, the Board will continue to:

- review and improve our governance practices;
- monitor global developments in best corporate governance practice, in particular developments from the United States Sarbanes- Oxley Act 2002; and
- contribute wherever we can to local debates on what represents best corporate governance practice.

Our Governance Standards – Principles and Processes

We believe that the best approach is to be guided by the principles and practices that are in our stakeholders' interests. However, as a minimum we ensure full compliance with legal requirements, in particular to the letter and spirit of the local governance practices issued by the Capital Market Authority (CMA), guidelines issued by the Central Bank of Oman and the Corporate Governance regulations issued by the Ministry of Commerce and Industry for closed joint stock companies.

What is in this statement?

This corporate governance statement is divided in two Parts. Part 1 discusses the broad principles of corporate governance adopted by the Bank. Part 2 provides specific disclosures.

In the Directors' opinion, Part 1 and Part 2 together as a minimum comply with the requirements of the Code of Corporate Governance issued by the CMA.

Date of this statement

This statement reflects the Bank's corporate governance policies and procedures as at 31 December 2013.

Corporate Governance - Part 1

In this part we set out the following contents as required under the Code of Corporate Governance issued by CMA:

1. The Board – putting governance into practice
2. Board Committees and their role
3. Audit governance and independence
4. Executive pay and reward scheme
5. Controlling and managing risk
6. Communication with Shareholders, regulators and wider market

1. The Board – putting governance into practice

Role of the Board

The Board of Directors is accountable to the shareholders. The Board's specific responsibilities include:

- ensuring our business is conducted ethically and transparently;
- providing strategic direction and approving corporate strategies;
- ensuring maintenance of adequate risk management controls and reporting mechanisms;
- monitoring management and financial performance;
- reviewing and approving the Bank's quarterly and annual financial reports;
- approving the business plan and budgets;
- selecting and evaluating the Chief Executive Officer (CEO) and senior management;
- planning for executive succession; and
- setting Chief Executive Officer's remuneration and recommending the Directors' remuneration to the shareholders for approval in the Annual General Meeting.

Board size and Composition

The Directors of the Bank are elected by the two major shareholders namely OMINVEST and Arab Bank Plc Jordan subject to the limits imposed by our constitution. The Bank's constitution requires a minimum of seven and a maximum of nine Directors. In accordance with the Central Bank of Oman's regulations, we do not have an executive Director in the Board.

Currently, there are seven non-executive Directors, of whom two are independent Directors and two are nominated Directors representing OMINVEST and Arab Bank Plc.

The current composition of the Board and Board Committees is set out in Part 2.

Selection and Role of the Chairman

The Chairman is a non-executive Director, appointed by the Board. The Chairman's role includes:

- ensuring that, when all Board members take office, they are fully briefed on the terms of their appointment, their duties and responsibilities;
- providing effective leadership on formulating the Board's strategy;
- representing the views of the Board to the public;
- ensuring that the Board meets at regular intervals throughout the year, and that minutes of meetings accurately record decisions taken and, where appropriate, the views of individual Directors; and
- reviewing the contributions made by the Board members.

<u>**Corporate Governance - Part 1 (continued)**</u>

1. The Board – putting governance into practice (continued)

Board Independence

Having an independent Board is a key to good corporate governance. The Bank has structures and procedures in place to ensure that the Board operates independently of executive management. These include appointing an independent, non-executive Director as chairman and ensuring that there are non-executive Directors who can bring special professional expertise to the Board. All the existing Directors meet the criteria of 'independent director' as defined by Article 1 of the CMA code of corporate governance issued under circular no. 11/2002 dated June 2002. The CMA has amended the definition of 'independent director' in the circular issued on 24 October 2012 and the Bank will ensure compliance with the new definition during 2013.

Meetings of the Board and their Conduct

The Board meets formally at least four times a year. In addition, it meets whenever necessary to deal with specific matters needing attention between the scheduled meetings. Meeting agendas are established by the Chairman in consultation with the CEO to ensure adequate coverage of financial, strategic and major risk areas throughout the year. Copies of Board papers are circulated in advance of meetings.

Meetings attended by the Directors for the past financial year are reported in Part 2.

Attendance at Annual General Meeting

The Directors attend, and are available to answer questions at, the Annual General Meeting.

Avoidance of Conflicts of Interest of Directors

In accordance with the constitution of the Bank, any Director with a material personal interest in a matter being considered by the Board must not be present when the matter is being considered, and may not vote on the matter.

Expertise of our Board

The Board has a broad range of expertise and experience to meet its objectives. The current Board composition is set out in Part 2, with details of each member's expertise and experience and other current Directorships, is set out in the annual report.

Succession Planning

The Board is responsible for CEO succession planning taking into account the skills and experience required.

Nomination and Appointment of New Directors

Recommendations for nominations of new Directors are made by the shareholders. When Directors are nominated, the shareholders assesses them against a range of criteria including background, experience, professional skills, personal qualities, whether their skills and experience will augment the existing Board, and their availability to commit themselves to the Board's activities. If these criteria are met then the shareholders appoint a new Director.

When appointed to the Board, all new Directors receive an induction appropriate to their experience to familiarize them with matters relating to the Bank's business, strategy and current issues before the Board.

The Board is appointed for a period of three years. The term of the current Board expires in March 2016.

Corporate Governance - Part 1 (continued)

Review of Board Performance

The Board regularly reviews its overall performance, as well as the performance of individual Directors.

1. The Board – putting governance into practice

Board Access to Information

The Board needs high quality, unfiltered information on which to base decisions. All Directors have unrestricted access to the Bank's records and information, and receive regular detailed financial and operational reports from senior management to enable them to carry out their duties.

2. Board Committees

We currently have three Board Committees whose powers are governed by the relevant Committee's terms of reference, as approved by the Board. The three Board Committees are: Executive Committee, Audit and Risk Management Committee and Selection and Remuneration Committee. Other committees may be established from time to time to consider matters of special importance.

Operation of the Committees

The Board Committees meet at least quarterly and at any other times as necessary. Each committee is entitled to the resources and information it requires, including direct access to employees and advisers. Senior managers and other employees are invited to attend committee meetings as necessary. All Directors receive minutes of the committee meetings and can attend all committee meetings.

Composition and Independence of the Committees

Committee members are chosen for the skills, experience and other qualities they bring to the committees. All committees are currently composed of only non-executive Directors. In addition, the Chief Internal Auditor is the secretary of the Audit and Risk Management Committee.

How the Committees report to the Board

Minutes of every meeting of the Board Committees are included in the agenda for the first full Board meeting scheduled to be held after the committee meeting. When necessary the chairman of the respective committee may also provide a verbal report.

Brief Terms of Reference of Board Committees

a) Board Executive Committee

The Board Executive Committee:

- reviews and approves policies with regard to credit risk limits and controls
- reviews and approves credit facilities above the executive management's approval limits,
- reviews and approves expenses or capital expenditures above executive managements approval limits,
- considers matters of special importance as delegated by the Board.

Corporate Governance - Part 1 (continued)

b) Board Audit and Risk Management Committee

The Board Audit and Risk Management Committee oversee all matters concerning:

- Integrity of the financial statements.
- Compliance with legal and regulatory requirement.
- Ensuring that Bank has an effective risk management system and clear policies and procedures for reporting, taking action and documenting breaches of laws including fraud and theft.
- Reviewing and recommending risk management policies and controls to Board.
- Review and recommendation to the Board the terms of engagement of our external auditors.
- Performance of the internal audit function.
-

2. Board Committees

c) Board Selection and Remuneration Committee

The Board Selection & Remuneration Committee oversees all matters concerning:

- Recommending the appointment of Chief Executive Officer to the Board.
- Ensuring independence of the Board members and avoidance of conflict of interest.
- Approving the appointment of executive management team based on recommendation by Chief Executive Officer except the appointment of Chief Audit Executive, Head of Compliance, Head of Risk Management, and Legal Counsel who will be appointed directly by the Board or its committees
- Recommending remuneration of the Chief Executive Officer to the Board including the salary and other benefits.
- Approving remuneration of executive management team include the salaries and other benefits.
- Ensuring that the Bank has a proper compensation policy, reviewing and recommending amendments in policy to the Board.
- Reviewing and monitoring the human resource plan and align the plan to achieve the Bank's strategies.
- Ensuring that the Bank has proper training, career development and succession plans.
- Reviewing and monitoring the "Omanisation" plan and identifying the positions that should be occupied by Omanis with the time table to achieve the plan.

Integrity of the Financial Statements

The Committee considers whether the accounting methods applied by management are consistent and comply with accounting standards and concepts. The committee reviews and assesses any significant estimates and judgments in the financial reports and monitors the methods used to account for unusual transactions. In addition it assesses the processes used to monitor and ensure compliance with laws, regulations and other requirements relating to external reporting of financial and non-financial information.

Internal Audit Function

The committee supervises the Internal Audit function. It reviews the Internal Audit responsibilities, budget, plan and staffing. The Committee also reviews significant reports prepared by Internal Audit and management responses and the committee meets separately with the Head of Internal Audit.

Corporate Governance - Part 1 (continued)

Composition of the Committee and Meetings

The current committee memberships together with dates of meetings held are set out in Part 2.

3. Audit Governance and Independence

The Board is committed to three basic principles:

- the Bank must produce true and fair financial reports;
- the Bank must have independent auditors who serve shareholder interests by ensuring shareholders know the Bank's true financial position; and
- the accounting and auditing standards are comprehensive and relevant and comply with applicable accounting standards and policies.

Engagement of Auditors

The Bank's independent external auditors are Deloitte & Touché M.E. for the financial year ended at 31 December 2013. They were appointed by shareholders at the Annual General Meeting held on 28 March 2013.

Certification and Discussions with Auditors on Independence

The Board Audit and Risk Management Committee require the Bank's external auditors to confirm that they maintained their independence at the commencement and during the audit. Board Audit and Risk Management Committee also meets with the external auditors to discuss their audit and any concerns they may have.

Rotation of External Auditors

Subject to applicable regulatory requirements, the Bank will require rotation of the external auditor every four years and a minimum two years' 'cooling off' period before an auditor is reappointed.

Restrictions on Non-Audit Work by the Audit Firm

The Bank's external auditors will not be able to carry out the following types of non-audit work for the Bank:

- preparation of accounting records and financial statements;
- IT systems design and implementation;
- valuation services and other corporate finance activities;
- internal audit services;
- temporary senior staff assignments, management functions;
- broker or dealer, investment adviser or investment banking;
- legal services; and
- litigation services.

For all other non-audit related services that are required, if our external audit firm were selected then the need for that will be assessed and approved by the Audit and Risk Management Committee.

Attendance at Annual General Meeting

The Bank's auditors attend, and are available to answer questions at, the Annual General Meeting.

Corporate Governance - Part 1 (continued)

4. Executive Pay and Reward Schemes

Overview

The Bank's goal in rewarding the CEO and other executives is to provide base pay plus performance-linked rewards and other benefits that will attract and retain key executives. The Bank's policy is to provide individual performers with a level of income that:

- recognizes the market value of each position in a competitive market;
- rewards the individual's capabilities and experience;
- recognizes the performance of individuals; and
- assists in executive retention.

To do this, the Bank has designed a fair and transparent structure for rewarding the Bank's executives that matches comparable remuneration in the marketplace.

Who decides how individuals should be paid and rewarded?

The Board recommends the remuneration and the sitting fee for individual Directors to be approved in the Annual General meeting. The remuneration of the CEO is recommended by the Board Selection and Remuneration Committee and approved by the Board of Directors.

The CEO recommends the pay and reward packages for key senior management staff consistent with the market practice and this is approved by the Board Selection and Remuneration Committee.

Fees paid to each Director during the 12 month period ended 31 December 2013 together with pay and rewards for the Bank's key management personnel are set out in Part 2.

5. Controlling and Managing Risk

Approach to Risk Management

Risk is inherent in Banking business. Risk management is a strategic issue in today's competitive environment. Taking and managing risk are central to the Bank's business and to building shareholder value. To do this effectively the Bank needs to optimize its level of risk. The Bank's risk approach links its vision and values, objectives and strategies, and procedures and training.

The Bank recognizes three main types of risk:

- Credit risk, being the risk of financial loss from the failure of customers to honor fully the terms of their contract with us;
- Market risk, being the risk to earnings from changes in market factors such as interest and foreign exchange rates, or liquidity and funding profiles; and
- Operational risk, being the risk of unexpected financial, reputation or other damage arising from the way our organization pursues its business objectives.

We recognize that these risk categories are interlinked and therefore we take an integrated approach to managing them. We have comprehensive risk principles that apply to each category of risk.

Corporate Governance - Part 1 (continued)

Approach to Risk Management (continued)

The risk management function aims at ensuring that:

(a) the Bank operates its key risk activities within acceptable risk/reward parameters through establishment as well as maintenance of policies and procedures

(b) the trend and quality of risk is adequately monitored and controlled; and

(c) all the attendant risks are adequately monitored.

Risk Management Roles and Responsibilities

The Board is responsible for approving and reviewing the Bank's risk management strategy and policy. Executive management is responsible for implementing the Board-approved risk management strategy and developing policies, controls, processes and procedures to identify and manage risks in all of our activities.

In order to effectively manage various risks in the business, the Bank has set up a Risk Management department. The head of this department is responsible for independently evaluating and managing the risks. He reports directly to the CEO and also reports to the Board Audit & Risk Management Committee.

Internal Review and Risk Evaluation

Based on Board approved policies the Bank has established appropriate procedures to manage and monitor the risks. Broadly the Asset and Liability Committee is responsible for monitoring market risks arising from the Bank's core lending and deposit-taking activities. Similarly, the Investment management Committee is responsible for monitoring market risk and related credit and operational risk exposures arising from trading activity. Internal Audit is responsible for independently evaluating the adequacy and effectiveness of management's control of operational risk.

6. Communication with Shareholders, Regulators and Wider Market

The Bank is committed to giving all shareholders comprehensive and equal access to information about the Bank's activities, and to fulfilling our continuous disclosure obligations to the broader market including the regulatory authorities namely Central Bank of Oman, Capital Market Authority and Muscat Securities Market.

The Bank's website includes annual reports, quarterly financial statements, briefings and presentations given by CEO and other executives, public announcements and economic updates. Further details on means of communications, including website address, are set out in Part 2.

Corporate Governance - Part 2

In this part, we set out the disclosures specifically required under Annexure 4 of the Code of Corporate Governance issued by CMA. The contents are as follows:

1. Board of Directors
2. Board Committees
3. Process of nomination of Directors
4. Remuneration matters
5. Details of non-compliance by the Bank
6. Means of communication with the shareholders and investors
7. Cash dividend policy
8. Market price data
9. Profile of the statutory auditors
10. Areas of non-compliance with the provisions of Corporate Governance

1. Board of Directors

The current composition of the Board and Board Committees are set out in table 1, with further details on each Director provided in the annual report.

2. Board Committees

There are three Board Committees. The terms of references of the Committees are set out in Part 1.

Table 1

Director	Board Membership	Appointed as Director from	Shareholder Representation	Committee Membership		
				Executive Committee	Audit and Risk Management Committee	Selection and Remuneration Committee
Rashad Bin Muhammed Al Zubair	Chairman Chairman of Executive Committee	October 1989	OMINVEST	√	-	-
Riad Kamal	Deputy Chairman.	August 2012	Arab Bank Plc	-	-	-
Amin R Husseini	Director	May 2010		√	√	√
Randa Sadik	Director	June 2010		√	-	-
Hani Bin Muhammed Al Zubair	Director Independent	June 1999		-	√	-
Said Zaki(*)	Director Chairman of Audit & Risk Management Committee	February 1997		√	√	√
Mulham Bashir Al Jaraf	Director Chairman of Selection & Remuneration Committee Independent	September 2007		√	-	√

* - Mr. Said Zaki passed away on 5th December 2013. A new director will be appointed in his place during January 2014.

Corporate Governance - Part 2 (continued)

2. Board Committees (continued)

The members of the Committees together with the number of meetings held in 2013 and attended by each member are set out in the Table 2.

Table 2

Directors' attendance record

Director	Board Meetings (Note 1)		Executive Committee (Note 2)		Audit and Risk Management Committee (Note 3)		Selection and Remuneration Committee (Note 5)	
	No. of meetings held	No. of meetings attended	No. of meetings held	No. of meetings attended	No. of meetings held	No. of meetings attended	No. of meetings held	No. of meetings attended
Rashad Bin Muhammed Al Zubair	4	4	4	4	-	-	-	-
Riad Kamal	4	4	-	-	-	-	-	-
Hani Bin Muhammed Al Zubair	4	4	-	-	7	5	-	-
Said Zaki	4	3	4	3	7	6	2	2
Amin R Husseini	4	4	4	4	7	7	2	2
Randa Sadik	4	4	4	3	-	-	-	-
Mulham Bashir Al Jaraf	4	3	4	3	-	-	2	2

Note 1 Board meetings were held on 28 March, 21 April, 24 July, and 15 December during the year 2013

Note 2 Executive Committee meetings were held on 21 January, 4 February, 18 June, and 28 October during the year 2013

Note 3 Audit and Risk Management Committee meetings were held on 21 January, 18 March, 10 April, 21 July, 24 October, 20 November and 16 December during the year 2013

Note 4 Selection and Remuneration Committee meetings were held on 21 January and 21 July 2013.

3. Process of nomination of Directors

The nomination process is explained in Part 1 paragraph 1.

Corporate Governance - Part 2 (continued)

4. Remuneration Matters

The processes and procedures of the Bank to reward and remunerate the Directors and senior executives are set out in Part 1, paragraph 4. The Directors' remuneration is governed as set out in the Memorandum of Association of the Bank, the Commercial Companies Law, regulations issued by the Capital Market Authority and regulations issued by the Central Bank of Oman.

The Annual General Meeting approves the remuneration and the sitting fees for the Board of Directors and its sub-committees provided that such fees shall not exceed 5% of the annual net profit (subject to specified deductions) and subject to an overall limit of RO 200,000. The sitting fees for each Director shall not exceed RO 10,000 in one year.

In the Annual General Meeting held on 28 March 2013 the shareholders approved the Directors' remuneration as well as the sitting fees of RO 500 per meeting for 2013. The remuneration and sitting fees for 2012 were paid during 2013. A resolution to approve the proposed remuneration of RO 64,500 and sitting fees of RO 33,500 for 2013 will be presented in the upcoming Annual General Meeting of the shareholders. The remuneration and sitting fees paid to each Director for 2012 was as follows:

Table 3

Director's Name	Remuneration RO	Sitting fees RO	Total RO
Rashad Bin Muhammed Al Zubair	14,500	6,000	20,500
Abdel Hamid Shoman *	7,000	1,000	8,000
Riad Kamal	3,000	1,000	4,000
Hani Bin Muhammed Al Zubair	8,000	4,000	12,000
Said Zaki	8,000	9,500	17,500
Amin R Husseini	8,000	10,000	18,000
Randa Sadik	8,000	1,500	9,500
Mulham Bashir Al Jaraf	8,000	4,500	12,500
Total	**64,500**	**37,500**	**102,000**

The remuneration paid to the key management personnel of the Bank for 2013 is RO 1,482,529 (2012: RO 1,466,354)

No stock options are available to Directors or the executives of the Bank. The Executives are required to provide 30-60 days notice should they wish to resign. No severance fees are payable to the key management personnel in the event of termination of employment.

Corporate Governance - Part 2 (continued)

5. Non-Compliance of Corporate Governance and Penalties

During the year, the Bank complied with all requirements of the regulatory authorities, CMA and Muscat Securities Market including Central Bank of Oman. There were no penalties or strictures imposed by any statutory/regulatory authority on the Bank for non-compliance during the last three years.

6. Means of Communicating with the Shareholders

We confirm the following:

a) Half-yearly results were sent to the shareholders.
b) Quarterly results and the annual report are posted on the Bank website www.oman-arabbank.com.
c) The website displays all official Bank information releases.
d) Management Discussion and Analysis (MD&A) forms part of the annual report.

Our policy with regard to communication with shareholders, regulators and wider market is set out in Part 1, paragraph 6.

7. Acknowledgment by the Board

The Board of Directors acknowledges its responsibilities and confirms that:

i. The audited financial statements of the Bank have been prepared in accordance with the International Financial Reporting Standards (“IFRS”), the requirements of the Commercial Companies Law of 1974, as amended and the disclosure requirements of the Central Bank of Oman.

ii. The Bank will be able to carry on its operations successfully in the foreseeable future.

iii. The Bank has adequate internal controls and procedures which are reviewed regularly through internal audit and overseen by the Audit Committee of the Board.

8. Dividend Policy

The Bank’s Dividend Policy complies with CBO’s guidance and adopted to achieve:

1. Establish provisions that support the Bank's financial position.
2. Pay cash dividend to the shareholders appropriate to their investment.
3. Retain sufficient provisions that support the future growth of the Bank operations and strengthen its position in case of any unexpected crisis.
4. Strike a balance between the retention of some earnings appropriate to the economic conditions and the understandable desire of shareholders for immediate and high returns.

Corporate Governance - Part 2 (continued)

9. Market Price Data

The Bank is a closed joint stock company and its shares therefore are not listed for trading on the Muscat Securities Market.

The two single largest shareholders of Oman Arab Bank are OMINVEST and Arab Bank Plc Jordan who hold 50.99 % and 49 % of the share capital respectively. OMINVEST is a public joint stock company listed at the Muscat Securities Market and Arab Bank Plc is a publicly held company and is listed at the Amman Stock Exchange, Jordan.

10. Profile of the Statutory Auditors

Deloitte refers to one or more of Deloitte Touche Tohmatsu Limited, a UK private company limited by guarantee, and its network of member firms.
Deloitte provides audit, tax, consulting, and financial advisory services to public and private clients spanning multiple industries. With a globally connected network of member firms in more than 150 countries, Deloitte brings world-class capabilities and high-quality service to clients, delivering the insights they need to address their most complex business challenges. Deloitte's more than 200,000 professionals are committed to becoming the standard of excellence.

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11. Audit fees

The Bank paid RO 23,550 to the external auditors for their audit and related services for the year ended 2013.

12. Areas of Non-Compliance with the Provisions of Corporate Governance

None

MANAGEMENT DISCUSSION AND ANALYSIS

MANAGEMENT DISCUSSION AND ANALYSIS

Industry Structure and Development

The banking industry in Oman is governed by the Banking Law issued by Royal Decree 114/2000, and the regulations issued by the banking regulatory authority, the Central Bank of Oman (CBO). In addition the banks must also comply with the requirements of the Commercial Companies Law of 1974, as amended, and the Capital Market Authority.

A summary of the banking sector performance for the year 2013 based on the latest publications and statistics issued by the Central Bank of Oman is as follows:

1. The total assets of the commercial banks increased by 7.2% from 2012 to reach RO 22.3 billion at 31 December 2013.
2. Loans and advances recorded a growth of 6% reaching RO 15.2 billion at 31 December 2013 from RO 14.3 billion at 31 December 2012.
3. Customer deposits increased by 10% to RO 15.6 billion at December 31 2013 from RO 14.2 billion at December 31 2012. The private sector deposits constituted 71% of the total customer deposits at December 2013 compared to 65% at December 2012.
4. Average deposit interest rate on Rial Omani deposits was around 1.17% and the interest rate on foreign currency deposits was around 0.9% as at December 2013. During 2013 the average interest rate on Rial Omani and foreign currency term deposits decreased by 0.2%.
5. Average Rial Omani lending rates decreased to 5.4% at December 2013 from 5.7% at December 2012 due to the surplus liquidity and increased competition among the local banks while average US Dollar rates decreased by 0.1% reaching 2.3% at December 2013.

Opportunities and threats

The Oman Government Budget for 2014 based on the oil price of USD 85 per barrel provides for an expenditure of RO 13.5 Billion of which RO 3.2 Billion will be for investments in oil and gas industry while RO 9 Billion is allocated for social requirements like education, health, housing and training. The infrastructure projects like the expansions at Duqum port with Special Economic Zone, Airports expansion at Muscat and Salalah, New airports at Sohar will continue as planned. The Railway Project in Oman which is expected to provide a boost to jobs and economic development is being pursued actively by the Government of Oman. The Preliminary Design Consultancy services contract has been tendered and the project is planned for completion by 2018. The Small and Medium Enterprise (SME) Fund has been established with a targeted capital of RO 100 Million of which the tranches of RO 20 Million raised each year starting from 2014. This will be used for funding the SME entities for working capital as well as other financial requirements. The CBO has also set a minimum level of 5% of total loans for the SME sector for the commercial banks. The planned government expenditure is expected to provide adequate business opportunities for the banks, especially in financing for working capital and equipment. The projects will also increase the business opportunities for sub-contractors. The increased employment of Omanis in the various projects and the companies under SME sector will provide a wider market for personal lending.

The Rial Omani lending rates reduced by 0.25% in 2013 while the foreign currency rates reduced marginally by 0.08%. The Rial Omani time deposit rates also decreased by 0.25% in 2013 due to the surplus liquidity. A further reduction in the interest rate ceiling of personal loans from 7% in 2012 to 6% during 2013 and increase competition are likely to tighten the interest margin in 2014. The interest rate on Central Bank CD is expected to remain at around 0.13%.

MANAGEMENT DISCUSSION AND ANALYSIS (CONTINUED)

The impact of Islamic Banking in the market has not been significant during 2013 as this is the first year of operation for the Islamic Banks and the windows. There would be both opportunities and threats from the Islamic Banking as it matures and the customers understand better the products or services offered.

Analysis and performance of segments

Analysis and performance of segments Segmental performance analysis forms part of the financial statements and are provided in notes to the financial statements.

Economic Outlook

OAB operates only in Oman and changes in the Oman economy have a direct impact on OAB's performance. Oman is expected to record a real growth of around 5% in GDP for 2013 while the nominal GDP growth would be around 2%. Inflation in GCC countries has generally remained low and even decelerated in some countries despite healthy activity levels and increased credit growth. Inflation in Oman was at 1.4% up to October 2013 and is expected to be around the same level for the full year. Oman's projected revenue for 2014 is at RO 11.7 billion which is a growth of 5% from 2012. Non-oil revenues is budgeted at 17% of the total revenue. Average crude oil price of USD 85 per barrel has been assumed for 2014 budget which was the same basis for the 2013 budget. A deficit of RO 1.8 Billion has been budgeted for 2014. But with the oil price expected at above USD 100 per barrel for 2014 there could be a budget surplus.

The actual oil price during 2013 was at an average of USD 105.5 per barrel which declined by 3.7% from USD 109 per barrel for 2012. However the oil production for 2013 increased by 2.3% with daily production at 942,000 barrels per day compared to the 919,000 barrels per day for 2012.

The stable economic and political environment of Oman has provided confidence to local investors while the foreign investors are guided by the regional perspective. The trading volumes in MSM during 2013 improved by 88% as compared to 2012 with increased turnover in the banking, industry and service sectors along with Oman Government Bond issues. The MSM 30 Index closed at 6,798 points, which is 18% up from 5,760 points at December 31 2012.The IPOs of SembCorp, Sharqia Desalination Co. and the Takaful companies contributed to the increased activity in MSM. MSM remains an attractive market for investors in GCC region with high dividend yields. The privatization of Omantel and issues of power companies - Al Suwaidi Power Co and Al Batinah Power Co will add to the liquidity in the MSM during 2014.

Internal control systems and their adequacy

Management of OAB has established and maintains internal controls supplemented by a program of internal audits. The internal controls are designed to provide reasonable assurance that assets are safeguarded and transactions are executed, recorded and reported in accordance with management's intentions and authorizations and to comply with applicable laws and regulations. The internal control system includes an organizational structure that provides appropriate delegation of authority and segregation of duties, established policies and procedures, and comprehensive internal audit and loan review programs.

To enhance the reliability of internal controls, management recruits and trains qualified personnel, and maintains sound risk management practices. There are inherent limitations in any internal control, including the possibility of human error and the circumvention or overriding of controls. Accordingly, even effective internal controls can provide only reasonable assurance with respect to financial statement preparation. Further, because of changes in conditions, the effectiveness of internal controls may vary over time.

MANAGEMENT DISCUSSION AND ANALYSIS (CONTINUED)

The Internal Audit Department of OAB reviews, evaluates, monitors and makes recommendations on policies and procedures, which serves as an integral, but independent component of internal control.

OAB's financial reporting and internal controls are under the general oversight of the Board of Directors, acting through the Audit and Risk Management Committee. The Audit and Risk Management Committee is composed entirely of independent non-executive directors. The Audit Committee meets periodically with management, internal auditors and external auditors to determine that each is fulfilling its responsibilities and to support actions to identify measure and control risks and augment internal controls.

Discussion on financial and operational performance

1. **Net profit**

   Net profit for the year ended 31 December 2013 is RO 25 million, which is 1% lower than the previous year. The operating profit at RO 30 million is 7% lower than previous year. The significant changes in income and expenses during 2013 are as follows:

   - Growth in net interest from 2012 is 4% as the interest income increased by 6% while the interest expense increased by 17%. The growth in loans during the last during the year by 14% is much higher than the growth of all banks in Oman. But the growth in interest income is lower compared to 2012. The decrease in the interest rate ceiling on personal loans from 7% to 6% as well as high liquidity and competition from local banks contributed to reduced yield on loans. The increase in interest expense from 2012 is mainly due to the interest on the subordinated bonds issued during April 2012.The interest rate on term deposits reduced marginally during the year while the higher volume of deposits resulted in the increased interest expense.
   - Other operating income increased by 3% during the year. The commission income from trade finance activities increased with greater project related activities in Oman. But the lack of growth in income from personal loans as well as the lower income from the Bank’s smart cards resulted in the decline of total commission income. The recovery in the stock markets across the region including MSM provided for the increased realized and unrealized gains from the Bank’s own investments. The gains were from shares in oil, power and services sectors. All GCC markets ended 2013 with a significant positive growth in index. MSM-30 index also performed very well compared to previous year ending 18% higher than 2012. The dividend income in 2013 has been significantly higher than 2012 with increased dividends from telecom, power and oil companies. The fee income from the investment banking increased by 62% with the increased trading volumes and growth in the indices. The Bank also gained on the fee income from managing the major IPO during the year by Sembcorp, Salalah and Sharqiyah Desalination Co. in addition to rights issues by Muscat Finance co. and Galfar Engineering Co.
   - Operating expenses at RO 33 million increased by 15% mainly due to the increased salary costs as a result of promotions and increments combined with the increase in number of staff from 1,002 at December 2012 to 1,137 at December 2013. The fees paid to CBO for the BDIS was higher due to the growth in deposits. The advertisement and promotion costs were higher than the previous year with a higher prize money for the Bank’s Hassad savings deposits. In addition the depreciation on the new Head office also contributed to the increase in costs.

MANAGEMENT DISCUSSION AND ANALYSIS (CONTINUED)

- The Earnings per share remains at RO 0.022 at December 31 2013 which is the same as at December 31 2012. The share capital also remains at the same level of RO 116 million at 100 baizas per share.

2. Assets

The total assets of the Bank at 31 December 2013 have increased by 6% to RO 1.46 Billion from RO 1.37 Billion at 31 December 2012. The significant changes are as follows:

Certificates of Deposit

The investments in Central Bank Certificates of Deposit are at RO 100 million at December 2013 reflecting the surplus liquidity prevailing in the market.

Loans and advances

Gross loans increased by RO 109 million (13%) during 2013 from RO 857 million at December 31 2012 to RO 966 million at December 31 2013. The personal loans increased by 15% while the corporate loans increased by 11%.

Non-performing loans increased to RO 36.6 million, which is 3.3% of the total loans at December 31 2013 from 2.7% at December 31 2012 mainly due to the classification of certain corporate loans, which were given under the Government Soft Loan scheme. The principal amount of these loans are guaranteed and a part of the interest is paid by the Government of Oman. The total provision coverage is at December 31 2013 is 94% of the non-performing assets as compared to 121% at December 31 2012.

The specific provision is at 54% of the Non-performing loans as the provision requirement is lower after considering the collaterals available for these loans. The provision levels were considered adequate and have been determined in accordance with the Central Bank of Oman and International Financial Reporting Standards.

3. Liabilities

The customer deposits constitute 79% of the liabilities. The savings deposits grew by 12% and the current accounts increased by 17% from previous year contributing to the total increase of 11% in customer deposits. The Bank issued subordinated bonds of RO 50 million in April 2012 to provide additional capital to fund the Bank’s growth. The loans are funded entirely from the customers’ deposits.

4. Shareholders' funds

Shareholders’ funds increased to RO 198.75 million from RO 184.11 million in the previous year. The paid-up share capital was increased to RO 116 million in March 2012. During 2013 the capital of RO 11 million was assigned to the Bank’s Islamic Banking window, which commenced operations from July 14 2013.

MANAGEMENT DISCUSSION AND ANALYSIS (CONTINUED)

5. Capital adequacy

Capital adequacy ratio calculated in accordance with the guidelines issued by Bank for International Settlement (BIS) is 16.52% (2012: 16.91%). The details of the calculation and the Bank's policy for capital management are provided in notes to the financial statements and the disclosure as per Pillar 3 of the Basel II guidelines.

6. Human Resources

Omanisation at 31 December 2013 was 93.31% (2012: 92.81%), which is higher than the minimum regulatory requirement of 90%. We provide the following as additional information regarding the number of years completed by staff.

	Below 3 Years	**4 to 6 Years**	**7 to 9 Years**	**10 to 14 Years**	**15 Years and above**	**Total**
Staff Numbers	452	234	73	104	274	1,137

Events after end of financial year

We are not aware of any matter or circumstance that has arisen since 31 December 2013 which has significantly affected, or may significantly affect the operations of the Bank.

Date of the statement 15 February 2014

FINANCIAL STATEMENTS

Deloitte.

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Independent auditor's report to the shareholders of Oman Arab Bank SAOC

Report on the financial statements

We have audited the accompanying financial statements of **Oman Arab Bank SAOC** ("the Bank"), which comprise of the statement of financial position as at 31 December 2013, and the statements of profit or loss and other comprehensive income, changes in equity and cash flows for the year then ended, and a summary of significant accounting policies and other explanatory information as set out on pages 3 to 65.

Board of Director's responsibility for the financial statements

Board of Director's is responsible for the preparation and fair presentation of these financial statements in accordance with International Financial Reporting Standards, and the relevant disclosure requirements of the Commercial Companies Law of 1974, as amended, and the Rules and Guidelines on disclosure issued by the Capital Market Authority and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the Bank's preparation and fair presentation of the financial statements 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 Bank's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Deloitte.

Independent auditor's report to the shareholders of Oman Arab Bank SAOC (continued)

Opinion

In our opinion, the financial statements present fairly, in all material respects, the financial position of **Oman Arab Bank SAOC** as of 31 December 2013, and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

Report on other legal and regulatory requirements

Also, in our opinion, the financial statements comply, in all material respects, with the relevant disclosure requirements of the Commercial Companies Law of 1974, as amended, and the Rules and Guidelines on disclosure issued by the Capital Market Authority.

Other matter

The financial statements of the Bank for the year ended 31 December 2012 were audited by another auditor who expressed an unmodified opinion on those statements on 24 February 2013.

Deloitte & Touche

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Deloitte & Touche (M.E.)& Co. LLC

Deloitte & Touche (M.E.) & Co. LLC
Muscat, Sultanate of Oman
23 January 2014

Signed by
Alfred Strolla
Partner

Statement of financial position
at 31 December 2013

	Notes	2013 RO'000	2012 RO'000
ASSETS			
Cash and balances with the Central Bank of Oman	7	**116,939**	149,893
Certificates of deposit	8	**100,000**	90,000
Due from banks	9	**50,893**	102,829
Loans and advances to customers	10	**1,076,291**	934,814
Investment securities	11	**53,437**	40,867
Other assets	12	**31,985**	30,227
Property and equipment	13	**26,810**	21,779
Total assets		**1,456,355**	1,370,409
LIABILITIES			
Due to banks	14	**3,862**	59,709
Deposits from customers	15	**1,149,153**	1,031,144
Other liabilities	16	**50,896**	41,595
Subordinated Bonds	17	**50,000**	50,000
Taxation	18	**3,692**	3,850
Total liabilities		**1,257,603**	1,186,298
EQUITY			
Share capital	19	**116,000**	116,000
Legal reserve	20	**27,627**	25,125
General reserve	21	**20,819**	19,568
Subordinated debt reserve	22	**20,000**	10,000
Cumulative changes in fair value		**1,364**	146
Retained earnings		**12,942**	13,272
Total equity		**198,752**	184,111
Total equity and liabilities		**1,456,355**	1,370,409
Contingent liabilities and commitments	34	**945,914**	1,054,572

The financial statements were authorised for issue by the Board of Directors on 23 January 2014 and signed by:

Rashad Muhammed Al Zubair
Chairman

Bishara S. Qafiti
Acting Chief Executive Officer

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

Statement of profit or loss and other comprehensive income for the year ended 31 December 2013

	Notes	2013 RO'000	2012 RO'000
Interest income	24	53,610	50,516
Interest expense	25	(11,158)	(9,549)
Net interest income		42,452	40,967
Fee and commission income - net	26	14,417	14,245
Investment income	27	2,308	1,441
Other operating income	28	4,651	4,175
Total income		63,828	60,828
Operating expenses	29	(33,798)	(28,542)
Allowance for loan impairment	10(a)	(6,351)	(5,727)
Recoveries / release from allowance for loan impairment	10(a)	4,999	2,284
Profit before tax		28,678	28,843
Income tax expense	18	(3,655)	(3,573)
Profit for the year		25,023	25,270
Other comprehensive income, net of income tax			
Items that may be reclassified subsequently to profit or loss:			
Net movement in unrealised gain on available-for-sale financial investments		1,218	(115)
Total comprehensive income for the year		26,241	25,155
Earnings per share:			
Basic and diluted	30	RO 0.022	RO 0.022

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

Statement of changes in equity
for the year ended 31 December 2013

	Notes	Share capital	Legal reserve	General reserve	Subordinated debt reserve	Cumulative changes in fair value	Retained earnings	Total
		RO'000	RO'000	RO'000	RO'000	RO'000	RO'000	RO'000
At 1 January 2013		116,000	25,125	19,568	10,000	146	13,272	184,111
Profit for the year		-	-	-	-	-	25,023	25,023
Other comprehensive income		-	-	-	-	1,218	-	1,218
Total comprehensive income for the year		-	-	-	-	1,218	25,023	26,241
Transfer to legal reserve	20	-	2,502	-	-	-	(2,502)	-
Transfer to general reserve	21	-	-	1,251	-	-	(1,251)	-
Transfer to subordinated debt reserve	22	-	-	-	10,000	-	(10,000)	-
Dividend paid relating to 2012	23	-	-	-	-	-	(11,600)	(11,600)
At 31 December 2013		116,000	27,627	20,819	20,000	1,364	12,942	198,752

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

Statement of changes in equity
for the year ended 31 December 2013 (continued)

	Notes	Share capital RO'000	Legal reserve RO'000	General reserve RO'000	Subordinated debt reserve RO'000	Cumulative changes in fair value RO'000	Retained earnings RO'000	Total RO'000
At 1 January 2012		100,000	22,598	18,304	-	261	1,793	160,956
Profit for the year		-	-	-	-	-	25,270	25,270
Other comprehensive income		-	-	-	-	(115)	-	(115)
Total comprehensive (expense) / income for the year		-	-	-	-	(115)	25,270	25,155
Issue of share capital	19	10,000	-	-	-	-	-	10,000
Issue of bonus shares	19	6,000	-	-	-	-	(6,000)	-
Transfer to legal reserve	20	-	2,527	-	-	-	(2,527)	-
Transfer to general reserve	21	-	-	1,264	-	-	(1,264)	-
Transfer to subordinated debt reserve	22	-	-	-	10,000	-	(10,000)	-
Dividend paid relating to 2011	23	-	-	-	-	-	(12,000)	(12,000)
At 31 December 2012		116,000	25,125	19,568	10,000	146	13,272	184,111

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

Statement of cash flows
for the year ended 31 December 2013

	Notes	2013 RO'000	2012 RO'000
Operating activities			
Profit before tax		**28,678**	28,843
Adjustments:			
Depreciation	**13**	**2,337**	1,916
Allowance for loan impairment and reserved interest	**10(a)**	**6,351**	5,727
Recoveries/release from allowance for loan impairment	**10(a)**	**(4,999)**	(2,284)
Income from held-to-maturity investments	**11**	**(745)**	(567)
Profit on sale of property and equipment	**13**	**(49)**	(17)
Profit on sale of available-for-sale investments	**11**	**(966)**	115
Change in the fair value of financial assets at fair value through profit or loss	**27**	**(607)**	(150)
Operating profit before changes in operating assets and liabilities		**30,000**	33,583
Changes in operating assets and liabilities			
Loans and advances		**(142,829)**	(108,412)
Financial assets at fair value through profit or loss		**864**	3,510
Other assets		**(1,758)**	(5,594)
Deposits from customers		**118,009**	121,484
Other liabilities		**9,301**	8,783
Cash from operations		**13,587**	53,354
Tax paid		**(3,813)**	(3,282)
Net cash generated from operating activities		**9,774**	50,072
Investing activities			
Held-to-maturity investments matured	**11**	**-**	13,387
Purchase of held-to-maturity investments	**11**	**(4,213)**	(18,835)
Purchase of investment available-for-sale	**11**	**(20,727)**	(4,293)
Proceeds from sale of investment available-for-sale		**14,297**	1,673
Income from maturing of held-to-maturity investments		**745**	567
Purchase of property and equipment	**13**	**(7,641)**	(8,681)
Proceeds from sale of property and equipment		**322**	19
Net cash used in investing activities		**(17,217)**	(16,163)
Financing activities			
Proceeds from issue of share capital	**19**	**-**	10,000
Proceeds from issue of subordinated bond	**22**	**-**	50,000
Dividends paid		**(11,600)**	(12,000)
Net cash used in financing activities		**(11,600)**	48,000
Net changes in cash and cash equivalents		**(19,043)**	81,909
Cash and cash equivalents at the beginning of the year		**282,513**	200,604
Cash and cash equivalents at the end of the year	**32**	**263,470**	282,513

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

Notes to the financial statements
for the year ended 31 December 2013

1. Legal status and principal activities

Oman Arab Bank SAOC ("the Bank" or "OAB") was incorporated in the Sultanate of Oman on 1 October 1984 as a closed joint stock company. It is principally engaged in commercial and investment banking activities through a network of branches in the Sultanate of Oman. The Bank operates in Oman under a banking licence issued by the Central Bank of Oman and is covered by its deposit insurance scheme. The registered address of the bank is Muttrah Business District, P O Box 2010, Ruwi, Postal Code 112, Muscat, and Sultanate of Oman. During the year the Bank has obtained the license from Central Bank of Oman for the Islamic Banking window under the name – "Al Yusr", which has commenced operations from 14 July 2013 and has assigned Ro 11 million as capital for Al Yusr.

Notes to the financial statements
for the year ended 31 December 2013 (continued)

2. Summary of significant accounting policies

2.1 Statement of compliance

These financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS"), the applicable regulations of the Central Bank of Oman, and the applicable requirements of the Commercial Companies Law of 1974, as amended and the Capital Market Authority of the Sultanate of Oman.

2.2 Basis of preparation

The financial statements are prepared under the historical cost convention, modified to include the measurement at fair value of the financial assets classified as available for sale and fair value through profit or loss and the derivative contracts.

The preparation of financial statements in conformity with IFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgment in the process of applying the Bank's accounting policies. The areas involving a higher degree of judgment or complexity, or areas where assumptions and estimates are significant to the financial statements are disclosed in note 3.

The Bank presents its statement of financial position in order of liquidity. An analysis regarding recovery or settlement within 12 months after the reporting date (current) and more than 12 months after the reporting date (non–current) is presented in note 35.

2.3 Financial instruments – initial recognition and subsequent measurement

The Bank classifies its financial assets in the following categories: financial assets at fair value through profit or loss, loans and advances, due from banks, held-to-maturity investments and available-for-sale investments. Management determines the classification of its investments at initial recognition.

The Bank classifies its financial liabilities into deposits and due to banks.

2.3.1 Date of recognition

All financial assets and liabilities are initially recognised on the trade date, i.e., the date that the bank becomes a party to the contractual provisions of the instrument. This includes "regular way trades": purchases or sales of financial assets that require delivery of assets within the time frame generally established by regulation or convention in the market place.

2.3.2 Initial measurement of financial instruments

The classification of financial instruments at initial recognition depends on the purpose and the management's intention for which the financial instruments were acquired and their characteristics. All financial instruments are measured initially at their fair value plus transaction costs, except in the case of financial assets and financial liabilities recorded at fair value through profit or loss.

Notes to the financial statements for the year ended 31 December 2013 (continued)

2. Summary of significant accounting policies (continued)

2.3 Financial instruments – initial recognition and subsequent measurement (continued)

2.3.3 Financial assets at fair value through profit or loss

Financial assets at fair value through profit or loss comprise financial securities held-for-trading which are acquired principally for the purpose of selling in the short-term and instruments so designated by management upon inception. Financial assets at fair value through profit or loss are initially recognised at fair value and transaction costs are expensed in the statement of comprehensive income. Unrealised gains or losses arising from changes in fair value are included in the statement of comprehensive income in the period in which they arise. Derivatives are also categorised as held for trading unless they are designated as hedging instruments.

Management may only designate an instrument at fair value through profit or loss upon initial recognition when the following criteria are met, and designation is determined on an instrument-by-instrument basis:

- The designation eliminates or significantly reduces the inconsistent treatment that would otherwise arise from measuring the assets or liabilities or recognising gains or losses on them on a different basis.
- The assets and liabilities are part of a group of financial assets, financial liabilities or both, which are managed and their performance evaluated on a fair value basis, in accordance with a documented risk management or investment strategy.
- The financial instrument contains one or more embedded derivatives, which significantly modify the cash flows that would otherwise be required by the contract.

2.3.4 Available-for-sale investments

Available-for-sale investments include equity and debt securities. Equity investments classified as available-for-sale are those which are neither classified as held for trading nor designated at fair value through profit or loss. Debt securities in this category are intended to be held for an indefinite period of time and may be sold in response to needs for liquidity or in response to changes in the market conditions.

The Bank has not designated any loans or receivables as available-for-sale. After initial measurement, available-for-sale financial investments are subsequently measured at fair value.
Unrealised gains and losses are recognised directly in equity (Other comprehensive income) in the cumulative changes in fair value. When the investment is disposed of, the cumulative gain or loss previously recognised in equity is recognised in the income statement in Other operating income. Where the Bank holds more than one investment in the same security, they are deemed to be disposed of on a first–in first–out basis. Interest earned whilst holding available-for-sale financial investments is reported as interest income using the EIR. Dividends earned whilst holding available-for-sale financial investments are recognised in the income statement as other operating income when the right of the payment has been established. The losses arising from impairment of such investments are recognised in the income statement in 'Impairment losses on financial investments' and removed from the cumulative changes in fair value.

Notes to the financial statements
for the year ended 31 December 2013 (continued)

2. Summary of significant accounting policies (continued)

2.3 Financial instruments – initial recognition and subsequent measurement (continued)

2.3.5 Financial investments held-to-maturity

Held-to-maturity investments are non-derivative financial assets with fixed or determinable payments and fixed maturities that the Bank's management has the positive intention and ability to hold to maturity. In the case where the Bank sells more than an insignificant amount of held-to-maturity assets, the entire category would be tainted and reclassified as available-for-sale. Held-to-maturity investments are initially recognised at fair value plus transaction costs. These are subsequently carried at amortised cost using the effective interest method.

2.3.6 Loans and advances to customers and due from banks

Loans and receivables to customers and due from banks are non-derivative financial assets with fixed or determinable repayments that are not quoted in an active market. They arise when the bank provides money directly to a debtor with no intention of trading the receivable. Loans and receivables are recognised when cash is advanced to customers and are carried at amortised cost using the effective interest method.

2.3.7 Fair value measurement principles

Regular purchases and sales of financial assets are recognised on the trade-date – the date on which the Bank commits to purchase or sell the asset. Investments are initially recognised at fair value plus transaction costs for all financial assets not carried at fair value through profit or loss. Financial assets carried at fair value through profit or losses are initially recognised at fair value, and transaction costs are expensed in the statement of comprehensive income. The fair value of financial instruments is based on their quoted market bid price at the reporting date without any deduction for transaction costs. If a quoted market price is not available, the fair value of the instrument is estimated based on discounted cash flow and other valuation techniques. The fair value of derivatives that are not exchange-traded is estimated at the amount that the bank would receive or pay to terminate the contract at the reporting date taking into account current market conditions and the current creditworthiness of the counter-parties.

2.3.8 Derecognition of financial assets and liabilities

A financial asset (or, where applicable a part of a financial asset or part of a group of similar financial assets) is derecognised when:

- The rights to receive cash flows from the asset have expired; or
- The Bank has transferred its rights to receive cash flows from the asset or has assumed an obligation to pay the received cash flows in full without material delay to a third party under a 'pass-through' arrangement; and either:
  - the Bank has transferred substantially all the risks and rewards of the asset, or
  - the Bank has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset.

A financial liability is derecognised when the obligation under the liability is discharged or cancelled or expires. 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 the respective carrying amounts is recognised in profit or loss.

Notes to the financial statements
for the year ended 31 December 2013 (continued)

2. Summary of significant accounting policies (continued)

2.3 Financial instruments – initial recognition and subsequent measurement (continued)

2.3.9 Impairment of financial assets

The Bank assesses at each reporting date whether there is objective evidence that a financial asset or a group of financial assets is impaired. A financial asset or a group of financial assets is impaired and an impairment loss is incurred if, and only if, there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the asset (a 'loss event') and that loss event (or events) has an impact on the estimated future cash flows of the financial asset or group of financial assets that can be reliably estimated. Objective evidence that a financial asset or group of assets is impaired includes observable data that comes to the attention of the Bank about the following loss events as well as considering the guidelines issued by the Central Bank of Oman:

- significant financial difficulty of the issuer or obligor;
- a breach of contract, such as a default or delinquency in interest or principal payments;
- the Bank granting to the borrower, for economic or legal reasons relating to the borrower's financial difficulty, a concession that the lender would not otherwise consider;
- it becoming probable that the borrower will enter bankruptcy or other financial reorganisation;
- the disappearance of an active market for that financial asset because of financial difficulties; or
- observable data indicating that there is a measurable decrease in the estimated future cash flows from a group of financial assets since the initial recognition of those assets, although the decrease cannot yet be identified with the individual financial assets in the group, including adverse changes in the payment status of borrowers in the Bank, or national or local economic conditions that correlate with defaults on the assets in the Bank.

The Bank first assesses whether objective evidence of impairment exists individually for financial assets that are individually significant, and individually or collectively for financial assets that are not individually significant. If the Bank determines that no objective evidence of impairment exists for an individually assessed financial asset, whether significant or not, it includes the asset in a group of financial assets with similar credit risk characteristics and collectively assesses them for impairment. Assets that are individually assessed for impairment and for which an impairment loss is or continues to be recognised are not included in a collective assessment of impairment.

(a) Assets carried at amortised cost

If there is objective evidence that an impairment loss on loans and receivables or held-to-maturity investments carried at amortised cost has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future credit losses that have not been incurred) discounted at the financial asset's original effective interest rate. The carrying amount of the asset is reduced through the use of an allowance account and the amount of the loss is recognised in the statement of comprehensive income. If a loan or held-to-maturity investment has a variable interest rate, the discount rate for measuring any impairment loss is the current effective interest rate determined under the contract.

Notes to the financial statements
for the year ended 31 December 2013 (continued)

2. Summary of significant accounting policies (continued)

2.3 Financial instruments – initial recognition and subsequent measurement (continued)

2.3.9 Impairment of financial assets (continued)
(a) Assets carried at amortised cost (continued)
The calculation of the present value of the estimated future cash flows of a collateralised financial asset reflects the cash flows that may result from foreclosure less costs for obtaining and selling the collateral, whether or not foreclosure is probable.

Future cash flows in a group of financial assets that are collectively evaluated for impairment are estimated on the basis of the contractual cash flows of the assets in the Bank and historical loss experience for assets with credit risk characteristics similar to those in the Bank. Historical loss experience is adjusted on the basis of current observable data to reflect the effects of current conditions that did not affect the period on which the historical loss experience is based and to remove the effects of conditions in the historical period that do not exist currently.

The methodology and assumptions used for estimating future cash flows are reviewed regularly by the Bank to reduce any differences between loss estimates and actual loss experience. When a loan is uncollectible, it is written off against the related allowance for loan impairment. Such loans are written off after all the necessary procedures have been completed and the amount of the loss has been determined. If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised, the previously recognised impairment loss is reversed by adjusting the allowance account. The amount of the reversal is recognised in the statement of comprehensive income.

(b) Available-for-sale financial investments
For available-for-sale financial investments, the Bank assesses at each reporting date whether there is objective evidence that an investment or a group of investments is impaired.

In the case of equity investments classified as available-for-sale, objective evidence would include a significant or prolonged decline in the fair value of the investment below its cost. The determination of what is 'significant' or 'prolonged' requires judgement. Where there is evidence of impairment, the cumulative loss – measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that investment previously recognised in the statement of comprehensive income – is removed from equity and recognised in the statement of comprehensive income. Impairment losses on equity investments are not reversed through the statement of comprehensive income; increases in their fair value after impairment are recognised directly in equity.

In the case of debt instruments classified as available-for-sale, impairment is assessed based on the same criteria as financial assets carried at amortised cost. Interest continues to be accrued at the original effective interest rate on the reduced carrying amount of the asset and is recorded as part of 'Interest income'. If, in a subsequent year, the fair value of a debt instrument increases and the increase can be objectively related to an event occurring after the impairment loss was recognised in the statement of comprehensive income, the impairment loss is reversed through the statement of comprehensive income.

(c) Renegotiated loans
Loans that are either subject to collective impairment assessment or individually significant and whose terms have been renegotiated are no longer considered to be past due but are treated as new loans. In subsequent years, the asset is considered to be past due and disclosed only if renegotiated.

Notes to the financial statements
for the year ended 31 December 2013 (continued)

2. Summary of significant accounting policies (continued)

2.3 Financial instruments – initial recognition and subsequent measurement (continued)

2.3.10 Islamic banking

Murabaha to the purchase orderer
Murabaha to the purchase orderer represents the sale of goods at cost plus an agreed profit. Murabaha receivables consist of deferred sales transaction agreements and are stated net of deferred profits, any amounts written off and provision for impairment, if any. Promise made in the Murabaha to the purchase orderer is not obligatory upon the customer.

Ijarah Muntahia Bittamleek
Ijarah Muntahia Bittamleek is a lease whereby the legal title of the leased asset passes to the lessee at the end of the Ijarah (lease term), provided that all Ijarah installments are settled. Assets under Ijarah Muntahia Bittamleek are initially recorded at cost and subsequently depreciated at rates calculated to write off the cost of each asset over its useful life to its residual value.

Musharaka
Musharaka contracts represents a partnership between the Window and a customer whereby each party contributes to the capital in equal or varying proportions to establish a new project or share in an existing one, and whereby each of the parties becomes an owner of the capital on a permanent or declining basis and shall have a share of profits or losses. These are stated at the fair value of consideration given less any amounts written off and provision for impairment, if any.

Diminishing Musharaka
Diminishing Musharaka is a form of partnership where two or more persons jointly own a tangible asset in an agreed proportion and one of the partners undertakes to buy the ownership rights of other partner by way of periodical payments till the title of such tangible assets completely transferred to the purchasing partner.

Mudaraba
A contract between two parties, whereby one party provides the funds (Rab Al Mal) and the other party (the Mudarib) invest the funds in an asset, project or particular activity and any generated profits are distributed between the parties according to the profit shares that were pre-agreed upon in the contract. The Mudarib is responsible for losses caused by his misconduct, negligence or violation of the terms and conditions of the Mudarib; otherwise, losses are borne by Rab Al Mal. The Mudaraba capital of Mudaraba is paid to the Mudarib or placed under his disposition.

Wakalah
A contract between two parties whereby one party (the principal: Muwakkil) appoints the other party (the agent: Wakil) to invest certain funds according to terms and conditions of the Wakalah for a fixed fee in addition to any profit exceeding the expected profits as an incentive for the Wakil for the good performance. Any losses as a result of the misconduct or negligence or violation of the terms and conditions of the Wakalah are borne by the Wakil; otherwise, they are borne by the principal.

Qard Hassan
A non-profit bearing loan enables the borrower to use the borrowed amounts for a specific period of time, at the end of which the same borrowed amounts would be repaid free of any charges of profits.

Notes to the financial statements
for the year ended 31 December 2013 (continued)

2. Summary of significant accounting policies (continued)

2.4 Cash and cash equivalents

For the purposes of the cash flow statement, cash and cash equivalents comprise balances with less than three months' maturity from the date of acquisition, including: cash and non-restricted balances with the Central Bank of Oman, treasury bills and other eligible bills, loans and advances to banks, amounts due from other banks, amounts due to other banks and short-term government securities.

2.5 Offsetting of financial instruments

Financial assets and financial liabilities are offset and the net amount reported in the statement of financial position only when there is a legally enforceable right to offset the recognised amounts and there is an intention to settle on a net basis, or to realise the assets and settle the liability simultaneously. Income and expenses are not offset in the statement of comprehensive income unless required or permitted by any accounting standard or interpretation, and as specifically disclosed in the accounting policies of the Bank.

2.6 Property and equipment

Property and equipment are initially recorded at cost and are subsequently carried at cost less accumulated depreciation and accumulated impairment losses, if any. Depreciation on the assets except land is calculated using the straight-line basis to allocate their cost over the estimated useful lives, as follows:

Building	25 years
Equipment, furniture and fixtures	5 years
Motor vehicles	5 years

The assets' residual values and useful lives are reviewed at each reporting date to assess whether they are recorded in excess of their recoverable amount, and where carrying values exceed this recoverable amount, assets are written down to their recoverable amount. Gains and losses on disposal of property and equipment are determined by reference to their carrying amount and are taken into account in determining operating profit. Repairs and renewals are charged to the statement of comprehensive income when the expense is incurred. Subsequent expenditure is capitalised only when it increases the future economic benefits embodied in the item of property and equipment. All other expenditure is recognised in the statement of comprehensive income as an expense as incurred.

2.7 Impairment of non-financial assets

The Bank assesses at each reporting date whether there is an indication that an asset may be impaired. If any indication exists, or when annual impairment testing for an asset is required, the Bank estimates the asset's recoverable amount. An asset's recoverable amount is the higher of an asset's fair value less costs to sell and its value in use. 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.

Notes to the financial statements
for the year ended 31 December 2013 (continued)

2. Summary of significant accounting policies (continued)

2.7 Impairment of non-financial assets (continued)

An assessment is made at each reporting date as to whether there is any indication that previously recognised impairment losses may no longer exist or may have decreased. If such indication exists, the Bank estimates the asset's recoverable amount. A previously recognised impairment loss is reversed only if there has been a change in the assumptions used to determine the asset's recoverable amount since the last impairment loss was recognised. The reversal is limited so that the carrying amount of the asset does not exceed its recoverable amount, nor exceeds the carrying amount that would have been determined, net of depreciation, had no impairment loss been recognised for the asset in prior years. Such reversal is recognised in the statement of comprehensive income.

2.8 Collateral pending sale

The Bank occasionally acquires real estate in settlement of certain loans and advances. Real estate is stated at the lower of the net realisable value of the related loans and advances and the current fair value of such assets. Gains or losses on disposal, and unrealised losses on revaluation, are recognised in the statement of comprehensive income.

2.9 Borrowings

Borrowings are recognised initially at fair value, being their issue proceeds (fair value of consideration received) net of transaction costs incurred. Borrowings are subsequently stated at amortised cost; any difference between the proceeds, net of transaction costs, and the redemption value is recognised in the statement of comprehensive income over the period of the borrowings using the effective interest method.

Fees paid on the establishment of loan facilities are recognised as transaction costs of the loan to the extent that it is probable that some or all of the facility will be drawn down. In this case, the fee is deferred until the draw-down occurs. To the extent there is no evidence that it is probable that some or all of the facility will be drawn down, the fee is capitalised as a pre-payment for liquidity services and amortised over the period of the facility to which it relates.

2.10 Employee terminal benefits

End of service benefits are accrued in accordance with the terms of employment of the Bank's employees at the reporting date, having regard to the requirements of the Oman Labour Law 2003 as amended. Employee entitlements to annual leave and leave passage are recognised when they accrue to employees and an accrual is made for the estimated liability arising as a result of services rendered by employees up to the reporting date. These accruals are included in other liabilities.

Contributions to a defined contribution retirement plan for Omani employees in accordance with the Omani Social Insurance Law 1991 are recognised as an expense in the statement of comprehensive income as incurred.

Notes to the financial statements
for the year ended 31 December 2013 (continued)

2. Summary of significant accounting policies (continued)

2.11 Provisions

A provision is recognised in the statement of financial position when the Bank has a legal or constructive obligation as a result of a past event; it is probable that an outflow of economic benefits will be required to settle the obligation; and the amount has been reliably estimated. If the effect is material, provisions are determined by discounting the expected future cash flows at a rate that reflects current market assessments of the time value of money and, where appropriate, the risks specific to the liability.

2.12 Taxation

Income tax on the profit or loss for the year comprises current and deferred tax. Income tax is recognised in the statement of comprehensive income except to the extent that it relates to items recognised directly to equity, in which case it is recognised in equity.

Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantially enacted at the reporting date, and any adjustment to tax payable in respect of previous years.

Deferred tax is calculated using the liability method, providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. The amount of deferred tax provided is based on the expected manner of realisation or settlement of the carrying amount of assets and liabilities, using tax rates enacted or substantially enacted at the reporting date.

A deferred tax asset is recognised only to the extent that it is probable that future taxable profits will be available against which the asset can be utilised. Deferred tax assets are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

2.13 Interest income and expense

Interest income and expense are recognised in the statement of comprehensive income for all instruments measured at amortised cost using the effective interest method, unless collectability is in doubt. The effective interest method is a method of calculating the amortised cost of a financial asset or a financial liability and of allocating the interest income or interest expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument or, when appropriate, a shorter period to the net carrying amount of the financial asset or financial liability. When calculating the effective interest rate, the Bank estimates cash flows considering all contractual terms of the financial instrument but does not consider future credit losses. The calculation includes all fees and points paid or received between parties to the contract that are an integral part of the effective interest rate, transaction costs and all other premiums or discounts.

Notes to the financial statements
for the year ended 31 December 2013 (continued)

2. Summary of significant accounting policies (continued)

2.14 Fee and commission income

Fees and commissions are generally recognised on an accrual basis when the service has been provided. Loan commitment fees for loans that are likely to be drawn down are deferred (together with related direct costs) and recognised as an adjustment to the effective interest rate on the loan. Loan syndication fees are recognised as revenue when the syndication has been completed and the Bank retained no part of the loan package for itself or retained a part at the same effective interest rate for the other participants. Portfolio and other management advisory and service fees are recognised based on the applicable service contracts, usually on a time-apportionment basis. Asset management fees related to investment funds are recognised pro-rata over the period the service is provided. The same revenue recognition criteria are applied for custody services that are continuously provided over an extended period of time.

2.15 Dividend income

Dividend income is recognised when the right to receive payment is established.

2.16 Fiduciary assets

Assets held in trust or in a fiduciary capacity are not treated as assets of the Bank and, accordingly, are not included in these financial statements.

2.17 Derivative financial instruments

Derivatives are initially recognised at fair value on the date on which a derivative contract is entered into and are subsequently remeasured at their fair value. Fair values are obtained from quoted market prices in active markets, including recent market transactions. All derivatives are carried as assets when fair value is positive and as liabilities when fair value is negative.

2.18 Financial guarantees contracts

Financial guarantees are contracts that require the issuer to make specified payments to reimburse the beneficiary for a loss incurred because the debtor fails to make payments when due, in accordance with the terms of the debt. Such guarantees are given to banks, financial institutions or other entities on behalf of the customers.

Financial guarantees are initially recognised in the financial statements at fair value on the date the guarantee was issued. Subsequent to initial recognition, the Bank's liabilities under such guarantees are measured at the higher of initial measurement, less amortisation calculated to recognise in the statement of comprehensive income the fee income earned on the straight line basis over the life of the guarantee and the best estimate of the expenditure required to settle any financial obligation arising at the reporting date. These estimates are determined based on experience of similar transactions and history of past losses, supplemented by the judgment of management. Any increase in the liability relating to guarantees is taken to the statement of comprehensive income.

Notes to the financial statements
for the year ended 31 December 2013 (continued)

2. Summary of significant accounting policies (continued)

2.19 Dividends on shares

Dividends on shares are recognised as a liability and deducted from equity when they are approved by the Bank's shareholders. Dividends for the year that are approved after the reporting date are disclosed as an event after the reporting date.

2.20 Foreign currencies

(a) Functional and presentation currency

Items included in the financial statements of the Bank are measured and presented in Rial Omani being the currency of the primary economic environment in which the Bank operates.

(b) Transactions and balances

Transactions in foreign currencies are translated into Rial Omani and recorded at the foreign exchange rate ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies, which are stated at historical cost, are translated into Rial Omani at the foreign exchange rate ruling at the reporting date. Foreign exchange differences arising on translation are recognised in the statement of comprehensive income. Non-monetary assets and liabilities denominated in foreign currencies, which are stated at historical cost, are translated into Rial Omani at the foreign exchange rate ruling at the date of the transaction.

Changes in the fair value of monetary securities denominated in foreign currency classified as available-for-sale are analysed between translation differences resulting from changes in the amortised cost of the security and other changes in the carrying amount of the security. Translation differences related to changes in amortised cost are recognised in profit or loss, and other changes in carrying amount are recognised in equity. Translation differences on non-monetary financial assets and liabilities such as equities held at fair value through profit or loss are recognised in profit or loss as part of the fair value gain or loss. Translation differences on non-monetary financial assets such as equities classified as available-for-sale are included in the fair value reserve in equity.

2.21 Directors' remuneration

The Directors' remuneration is governed as set out in the Memorandum of Association of the Bank, the Commercial Companies Law, regulations issued by the Capital Market Authority and regulations issued by the Central Bank of Oman.

The Annual General Meeting shall determine and approve the remuneration and the sitting fees for the Board of Directors and its sub-committees provided that such fees shall not exceed 5% of the annual net profit after deduction of the legal reserve and the optional reserve and the distribution of dividends to the shareholders provided that such fees shall not exceed RO 200,000. The sitting fees for each director shall not exceed RO 10,000 in one year.

2.22 Segment reporting

The Bank's segmental reporting is based on the following operating segments: Retail banking, Corporate banking, Investment banking, and support and unallocated functions. The segment information is set out in note 39.

Notes to the financial statements
for the year ended 31 December 2013 (continued)

3. Critical accounting estimates and judgments in applying accounting policies

The key assumptions concerning the future and other key sources of estimating uncertainty at the reporting date, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are discussed below:

3.1 Going concern

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

3.2 Impairment losses on loans and advances

The Bank reviews its loan portfolios to assess impairment at least on a quarterly basis. In determining whether an impairment loss should be recorded in the statement of comprehensive income, the Bank makes judgments as to whether there is any observable data indicating that there is a measurable decrease in the estimated future cash flows from a portfolio of loans before the decrease can be identified with an individual loan in that portfolio. This evidence may include observable data indicating that there has been an adverse change in the payment status of borrowers in a group, or national or local economic conditions that correlate with defaults on assets in the group. Management uses estimates based on historical loss experience for assets with credit risk characteristics and objective evidence of impairment similar to those in the portfolio when scheduling its future cash flows and in line with the Central Bank of Oman guidelines in this respect. The methodology and assumptions used for estimating both the amount and timing of future cash flows are reviewed regularly to reduce any differences between loss estimates and actual loss experience.

3.3 Held-to-maturity investments

The Bank follows the guidance of IAS 39 on classifying non-derivative financial assets with fixed or determinable payments and fixed maturity as held-to-maturity. This classification requires significant judgment. In making this judgment, the Bank evaluates its intention and ability to hold such investments to maturity. If the Bank fails to keep these investments to maturity other than for the specific circumstances – for example, selling an insignificant amount close to maturity – it will be required to reclassify the entire class as available-for-sale. In such situations, the investments would therefore be measured at fair value and not at amortised cost.

3.4 Fair value of financial instruments

Where the fair values of financial assets and financial liabilities recorded on the statement of financial position cannot be derived from active markets, they are determined using a certain valuation techniques, derived from observable market data where possible. Where observable market data are not available, judgment is used to establish fair values.

Notes to the financial statements
for the year ended 31 December 2013 (continued)

3. Critical accounting estimates and judgments in applying accounting policies (continued)

3.5 Impairment of available-for-sale investments

The Bank reviews its debt securities classified as available-for-sale investments at each reporting date to assess whether they are impaired. This requires similar judgment as applied to the individual assessment of loans and advances.

The Bank also records impairment charges on available-for-sale equity investments when there has been a significant or prolonged decline in the fair value below their cost. The determination of what is ‘significant’ or ‘prolonged’ requires judgment. In making this judgment, the Bank evaluates, among other factors, historical share price movements and duration and extent to which the fair value of an investment is less than its cost.

3.6 Taxes

The Bank establishes provisions, based on reasonable estimates, for possible consequences of finalisation of tax assessments. The amount of such provisions is based on factors such as experience of previous tax assessments and interpretations of tax regulations by the Bank and the responsible tax authority.

Notes to the financial statements
for the year ended 31 December 2013 (continued)

4. Adoption of new and revised International Financial Reporting Standards (IFRSs)

For the year ended 31 December 2013, the Bank has adopted all the new and revised standards and interpretations issued by the International Accounting Standards Board (IASB) and the International Financial Reporting Interpretations Committee (IFRIC) of the IASB that are relevant to its operations and effective for the period beginning on 1 January 2013.

4.1 Standards and Interpretations adopted with no effect on the financial statements

The following new and revised Standards and Interpretations have been adopted in these financial statements. Their adoption has not had any significant impact on the amounts reported in these financial statements but may affect the accounting for future transactions or arrangements.

Amendments to IFRS 7 Disclosures - Offsetting Financial Assets and Financial Liabilities	The amendments to IFRS 7 require entities to disclose information about rights of offset and related arrangements (such as collateral posting requirements) for financial instruments under an enforceable master netting agreement or similar arrangement.
IFRS 10: Consolidated Financial Statements	IFRS 10 replaces the parts of IAS 27 Consolidated and Separate Financial Statements that deal with consolidated financial statements and SIC-12 Consolidation - Special Purpose Entities. IFRS 10 changes the definition of control such that an investor has control over an investee when a) it has power over the investee, b) it is exposed, or has rights, to variable returns from its involvement with the investee and c) has the ability to use its power to affect its returns. All three of these criteria must be met for an investor to have control over an investee. Previously, control was defined as the power to govern financial and operating policies of the entity so as to obtain benefits from its activities.
IFRS 11: Joint arrangements	IFRS 11, replaces IAS 31 Interest in Joint Ventures and guidance contained in a related interpretations. IFRS 11, deals with how a joint arrangement of which two or more parties have joint control should be classified and account for. Under IFRS 11, investments in joint arrangements are classified either as joint operations or joint ventures, based on rights and obligation of parties to the arrangements by considering the structure, the legal form of the arrangement, the contractual terms agreed by the parties to the arrangement, and when relevant, other facts and circumstances.
IFRS 12: Disclosure of Interests in Other Entities	IFRS 12 is a new disclosure standard and is applicable to entities that have interests in subsidiaries, joint arrangements, associates and/or unconsolidated structured entities. In general, the application of IFRS 12 has resulted in more extensive disclosures in the consolidated financial statements.

Notes to the financial statements
for the year ended 31 December 2013 (continued)

4. Adoption of new and revised International Financial Reporting Standards (IFRS) (continued)

4.1 Standards and Interpretations adopted with no effect on the financial statements (continued)

IFRS 13: Fair Value Measurement	IFRS 13 establishes a single source of guidance for fair value measurements and disclosures about fair value measurements. The scope of IFRS 13 is broad; the fair value measurement requirements of IFRS 13 apply to both financial instrument items and non- financial instrument items for which other IFRSs require or permit fair value measurements and disclosures about fair value measurements, except for share-based payment transactions that are within the scope of IFRS 2 Share-based Payment, leasing transactions that are within the scope of IAS 17 Leases, and measurements that have some similarities to fair value but are not fair value (e.g. net realisable value for the purposes of measuring inventories or value in use for impairment assessment purposes).
Amendments to IAS 1 Presentation of Items of Other Comprehensive Income	The amendments introduce new terminology, whose use is not mandatory, for the statement of comprehensive income and income statement. Under the amendments to IAS 1, the ‘statement of comprehensive income’ is renamed as the ‘statement of profit or loss and other comprehensive income’ [and the ‘income statement’ is renamed as the ‘statement of profit or loss’]. The amendments to IAS 1 retain the option to present profit or loss and other comprehensive income in either a single statement or in two separate but consecutive statements. However, the amendments to IAS 1 require items of other comprehensive income to be grouped into two categories in the other comprehensive income section: (a) items that will not be reclassified subsequently to profit or loss and (b) items that may be reclassified subsequently to profit or loss when specific conditions are met. Income tax on items of other comprehensive income is required to be allocated on the same basis - the amendments do not change the option to present items of other comprehensive income either before tax or net of tax. The amendments have been applied retrospectively, and hence the presentation of items of other comprehensive income has been modified to reflect the changes. Other than the above mentioned presentation changes, the application of the amendments to IAS 1 does not result in any impact on profit or loss, other comprehensive income and total comprehensive income.
Annual Improvements 2009-2011 Cycle	Makes amendments to the following standards: IAS 1 - Clarification of the requirements for comparative information IAS 16 - Classification of servicing equipment IAS 32 - Clarify that tax effect of a distribution to holders of equity instruments should be accounted for in accordance with IAS 12 Income Taxes IAS 34 - Clarify interim reporting of segment information for total assets in order to enhance consistency with the requirements in IFRS 8 Operating Segments.

Notes to the financial statements
for the year ended 31 December 2013 (continued)

4. Adoption of new and revised International Financial Reporting Standards (IFRS) (continued)

4.1 Standards and Interpretations adopted with no effect on the financial statements (continued)

IAS 19 Employee Benefits (as revised in 2011)	IAS 19 (as revised in 2011) changes the accounting for defined benefit plans and termination benefits. The most significant change relates to the accounting for changes in defined benefit obligations and plan assets. The amendments require the recognition of changes in defined benefit obligations and in the fair value of plan assets when they occur, and hence eliminate the ‘corridor approach’ permitted under the previous version of IAS 19 and accelerate the recognition of past service costs. All actuarial gains and losses are recognised immediately through other comprehensive income in order for the net pension asset or liability recognised in the consolidated statement of financial position to reflect the full value of the plan deficit or surplus. Furthermore, the interest cost and expected return on plan assets used in the previous version of IAS 19 are replaced with a ‘net interest’ amount under IAS 19 (as revised in 2011), which is calculated by applying the discount rate to the net defined benefit liability or asset. These changes have had an impact on the amounts recognised in profit or loss and other comprehensive income in prior years (see the tables below for details). In addition, IAS 19 (as revised in 2011) introduces certain changes in the presentation of the defined benefit cost including more extensive disclosures.

4.2 Standards and Interpretations in issue not yet effective

At the date of authorisation of these consolidated financial statements, the following new and revised Standards and Interpretations were in issue but not yet effective:

	Effective for annual periods beginning on or after
New IFRS and relevant amendments **Financial Instruments**	
IFRS 9: *Financial Instruments* (as revised in 2010 *to include requirements for the classification and measurement of financial liabilities and incorporate existing derecognition requirements)*	January 2015
Consolidation, joint arrangements, associates and disclosures	
Amendment to IFRS 10 Consolidated Financial Statements, IFRS 12 Disclosure of Interests in Other Entities and IAS 27 Separate Financial Statements, to *provide 'investment entities' (as defined) an exemption from the consolidation of particular subsidiaries and instead require that an investment entity measure the investment in each eligible subsidiary at fair value through profit or loss in accordance with IFRS 9 Financial Instruments or IAS 39 Financial Instruments: Recognition and Measurement.*	January 2014

Notes to the financial statements for the year ended 31 December 2013 (continued)

4. Adoption of new and revised International Financial Reporting Standards (IFRS) (continued)

4.2 Standards and Interpretations in issue not yet effective (continued)

Amendments to IFRSs	Effective for annual periods beginning on or after
IAS 32 : Financial instruments: presentation, *Offsetting Financial Assets and Financial Liabilities: to clarify certain aspects because of diversity in application of the requirements on offsetting, focused on four main area (a) the meaning of 'currently has a legally enforceable right of set-off'(b) the application of simultaneous realisation and settlement (c) the offsetting of collateral amounts (d) the unit of account for applying the offsetting requirements*	January 2014
IAS 36: impairment of assets, *Recoverable Amount Disclosures for Non-Financial Assets to reduce the circumstances in which the recoverable amount of assets or cash-generating units is required to be disclosed, clarify the disclosures required, and to introduce an explicit requirement to disclose the discount rate used in determining impairment (or reversals) where recoverable amount (based on fair value less costs of disposal) is determined using a present value technique.*	January 2014
IAS 39: Financial Instruments: Recognition and Measurement, *Novation of Derivatives and Continuation of Hedge Accounting' makes it clear that there is no need to discontinue hedge accounting if a hedging derivative is novated, provided certain criteria are met.* *A novation indicates an event where the original parties to a derivative agree that one or more clearing counterparties replace their original counterparty to become the new counterparty to each of the parties. In order to apply the amendments and continue hedge accounting, novation to a central counterparty (CCP) must happen as a consequence of laws or regulations or the introduction of laws or regulations.*	January 2014

The directors anticipate that the adoption of these Standards and Interpretations in future periods will have no material impact on the financial statements of the Bank's in the period of initial application. The adoption of these standards and interpretations has not resulted in changes to the Bank's accounting policies and has not affected the amounts reported for the current or prior periods except for IFRS 9: Financial Instruments 9. IFRS 9 introduces new requirements for the classification and measurement of financial assets, new criteria for amortised cost measurement, a new measurement category - fair value through other comprehensive income, impairment assessment only for amortised cost assets, eliminates the category available-for-sale assets, eliminates held-to-maturity assets and tainting rules, eliminates embedded derivatives in financial assets and eliminates unquoted equity investments measured at cost less impairment. The management is currently assessing this standard which may have an impact on the financial statements of the Bank as described above.

Notes to the financial statements
for the year ended 31 December 2013 (continued)

5. Financial risk management

The Bank's activities expose it to a variety of financial risks and those activities involve the evaluation, analysis, acceptance and management of risk or combination of risks. As taking risk is core to the financial business and operational risks are an inevitable consequence of any business, the Bank's aim is to achieve an appropriate balance between risk and return while minimising the potential adverse effects on the financial performance.

The Board of Directors defines risk limits and sets suitable policies in this regard for management of credit risk, liquidity risk as well as market risk in both the trading and the banking book of the Bank. Risk Management is carried out by the Risk Management Department in accordance with documented policies approved by the Board of Directors.

The principal types of risks that the Bank faces are credit risk, liquidity risk, market risk (price risk, interest rate risk and currency risk) and operational risk.

5.1 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. Credit exposures arise principally from lending activities, investment activities and other assets in the Bank’s asset portfolio. There is also credit risk in off-balance sheet financial instruments, such as loan commitments and financial guarantees.

The Bank attempts to control credit risk by monitoring credit exposures, limiting transactions with specific counterparties, and continually assessing the creditworthiness of counterparties. Concentrations of credit risk arise when a number of counterparties are engaged in similar business activities, or have similar economic features that would cause their ability to meet contractual obligations to be similarly affected by changes in economic, political or other conditions. Concentrations of credit risk indicate the relative sensitivity of the Bank’s performance to developments affecting a particular industry or geographic location. The details of concentrations of credit risk based on counterparties by industry are disclosed in Note 10(b) and the geographical concentration is disclosed in Note 37.

The credit risk management and control are centralised in the credit risk management team which is divided into corporate, financial institutions and retail groups. The credit risk in corporate and financial institutions portfolio is primarily managed by the Credit Department while the Retail Banking Department manages the credit risk in the retail portfolio. The Risk Management Department reviews the credit risk independently and directly reports to the Audit and Risk Management Committee of the Board of Directors. The Bank's assessment of probability of default of individual counterparties is mainly linked with the number of days the borrower was in default as defined by the Central Bank of Oman (CBO) circular number BM 977 dated 25 September 2004. In addition, the Bank assesses the adequacy of the security and financial performance of the borrowers in further downgrading the classification.

Notes to the financial statements
for the year ended 31 December 2013 (continued)

5. Financial risk management (continued)

5.1 Credit risk (continued)

The Bank rates its customers into the following categories:

Bank's rating	Past due days	
	Retail loans	**Commercial loans**
Standard loans	0 - 60 days	0 - 60 days
Special mention loan	60 - 90 days	60 - 90 days
Substandard loan	90 - 180 days	90 - 270 days
Doubtful loans	180 - 365 days	270 - 630 days
Loss	365 days and over	630 days and over

5.1.2 Risk mitigation policies

The Bank manages, limits and controls concentrations of credit risk – in particular, to individual counterparties and groups, and to industries and countries.

The Bank structures the levels of credit risk it undertakes by placing limits on the amount of risk accepted in relation to one borrower, or groups of borrowers, and to geographical and industry segments. Such risks are monitored and reviewed periodically by the Management Credit Committee, Audit and Risk Management committee of the Board of Directors and the Executive Committee of the Board of Directors.

The exposure to any one borrower including banks and brokers is further restricted by sub-limits covering on- and off-balance sheet exposures. Exposure to credit risk is also managed through regular analysis of the ability of borrowers and potential borrowers to meet interest and capital repayment obligations and by changing these lending limits where appropriate.

Some other specific control and mitigation measures are outlined below.

(a) Collateral

The Bank employs a range of policies and practices to mitigate credit risk. The most traditional of these is the taking of security for funds advanced, which is common practice. The Bank implements guidelines on the acceptability of specific classes of collateral or credit risk mitigation. The principal collateral types for loans and advances are:

- charges over business assets such as premises, inventory and accounts receivable
- lien on fixed deposits
- cash margins
- mortgages over residential and commercial properties
- pledge of marketable shares and securities

Notes to the financial statements
for the year ended 31 December 2013 (continued)

5. Financial risk management (continued)

5.1 Credit risk (continued)

5.1.2 Risk mitigation policies (continued)

(a) Collateral (continued)

Longer-term finance and lending to corporate entities are generally secured. The housing loans are secured by mortgage over the residential property. Credit cards and similar revolving credit facilities are unsecured. Additionally, in order to minimise the credit loss the Bank seeks additional collateral from the counterparty as soon as impairment indicators are noticed for the relevant individual loans and advances.

(b) Assessment of the financial capabilities of the borrowers

The borrowers with balances above the limit specified are subject to the review of their audited financial statements. The Bank assesses the financial performance of the borrowers by reviewing key performance ratios, including solvency and liquidity ratios. The annual reviews are performed by the relationship managers and are also reviewed by the Risk Management Department.

(c) Credit-related commitments

The primary purpose of these instruments is to ensure that funds are available to a customer as required. Guarantees and standby letters of credit carry the same credit risk as loans. Documentary and commercial letters of credit – which are written undertakings by the Bank on behalf of a customer authorising a third party to draw drafts on the Bank up to a stipulated amount under specific terms and conditions – are collateralised by the underlying shipments of goods to which they relate and therefore carry less risk than a direct loan.

Commitments to extend credit represent unused portions of authorisations to extend credit in the form of loans, guarantees or letters of credit. With respect to credit risk on commitments to extend credit, the Bank is potentially exposed to loss in an amount equal to the total unused commitments. However, the likely amount of loss is less than the total unused commitments, as most commitments to extend credit are contingent upon customers maintaining specific credit standards.

The Bank monitors the term to maturity of credit commitments because longer-term commitments generally have a greater degree of credit risk than shorter-term commitments. The concentration of credit related commitments by industry sector at the year-end is set out in Note 10(b).

An analysis of the loans and advances, other than government soft loans, for which collaterals or other credit enhancements are held is as follows:

Notes to the financial statements
for the year ended 31 December 2013 (continued)

5. Financial risk management (continued)

5.1 Credit risk (continued)
5.1.2 Risk mitigation policies (continued)
5.1.2 Credit-related commitments (continued)

	Performing loans (neither past due nor impaired) RO'000	Loans past due and not paid RO'000	Non performing loans RO'000	Gross loans RO'000
Loans and advances with collateral available	**184,583**	**13,462**	**21,096**	**219,141**
Loans and advances with guarantees available	**97,630**	**-**	**9,250**	**106,880**
At 31 December 2013	**282,213**	**13,462**	**30,346**	**326,021**
At 31 December 2012	319,837	7,061	25,448	352,346

5.1.3 Impairment and provisioning policy

Impairment allowance are recognised for financial reporting purposes only for losses that have been incurred at the reporting date based on objective evidence of impairment. Objective evidence that a financial asset or group of assets is impaired includes observable data that comes to the attention of the Bank about the loss events as well as considering the guidelines issued by the Central Bank of Oman.

The Bank's credit policy requires the review of individual financial assets on a quarterly basis or earlier when individual circumstances require. Impairment allowances on individually assessed accounts are determined by an evaluation of the incurred loss at the reporting date on a case-by-case basis, and are applied to all individually significant accounts. The assessment normally encompasses collateral held (including re-confirmation of its enforceability) and the anticipated receipts for that individual account.

Collectively assessed impairment allowances are provided for: (i) portfolios of homogenous assets that are individually not significant; and (ii) losses that have been incurred but have not yet been identified, by using the available historical experience and experienced judgment. The critical estimates used in determining the provision for impairment are explained in Note 3.2.

Notes to the financial statements for the year ended 31 December 2013 (continued)

5. Financial risk management (continued)

5.1 Credit risk (continued)

5.1.4 Maximum exposure to credit risk before collateral held or other credit enhancements

	2013 RO' 000	2012 RO' 000
Items on the statement of financial position		
Certificates of deposit (note (d))	**100,000**	90,000
Due from banks – Money market placements	**50,893**	102,829
Loans and advances		
Corporate loans	**682,179**	563,890
Personal loans	**428,427**	402,445
Other assets	**30,497**	28,749
Investment in securities		
Government Development Bonds	**32,073**	27,860
	1,324,069	1,215,773
Off-Balance sheet items		
Financial guarantees	**89,681**	85,183
Undrawn loan commitments	**770**	8,088
	90,451	93,271

The above table represents the worst case scenario of credit risk exposure to the Bank at 31 December 2013 and 31 December 2012 without taking into account the collateral held or other credit enhancements. Management is confident that the Bank has suitable policies to measure and control the credit risk. In addition credit risk is mitigated through collaterals in the form of mortgages and guarantees wherever required.

a) 100% (2012 – 76.7%) of the inter-bank money market placements are with banks rated investment grade and above based on the ratings assigned by External Credit Rating Agencies.

b) Loans and advances represent 74% (2012 – 68%) of the total on-balance sheet items. Of the total loans and advances 95% (2012 – 95%) are neither past due nor impaired.

c) The impaired loans have increased from 2.7% at 31 December 2012 to 3.3% at 31 December 2013. The impaired personal loans constitute 0.90% of the total loans at 31 December 2013 compared to 0.98% at 31 December 2012.

d) Certificates of deposit which represent 6.8% (2012 – 6.6%) of the total on-balance sheet items are placed with the Central Bank of Oman.

Notes to the financial statements
for the year ended 31 December 2013 (continued)

5. Financial risk management (continued)

5.1 Credit risk (continued)

5.1.5 Loans and advances and due from banks

Loans and advances and due from banks are summarised as follows:

31 December 2013

	Loans and advances RO' 000	Due from banks RO' 000	Total RO' 000
Neither past due nor impaired	**1,053,174**	**50,893**	**1,104,067**
Special Mention loans	**7,357**	**-**	**7,357**
Past due but not impaired	**13,462**	**-**	**13,462**
Impaired	**36,613**	**-**	**36,613**
Gross loans and advances	**1,110,606**	**50,893**	**1,161,499**
Less: allowance for loan impairment and contractual interest not recognized	**(34,315)**	**-**	**(34,315)**
Net loans and advances	**1,076,291**	**50,893**	**1,127,184**

31 December 2012

	Loans and advances RO' 000	Due from banks RO' 000	Total RO' 000
Neither past due nor impaired	922,749	102,829	1,025,578
Special mention loans	10,438	-	10,438
Past due but not impaired	7,061	-	7,061
Impaired	26,087	-	26,087
Gross loans and advances	966,335	102,829	1,069,164
Less: allowance for loan impairment and contractual interest not recognized	(31,521)	-	(31,521)
Net loans and advances	934,814	102,829	1,037,643

a) The total impairment provision for loans and advances is RO 34,315 thousand (2012 - RO 31,521 thousand) of which RO 19,674 thousand (2012 - RO 18,152) represents the individually impaired loans and the remaining amount of RO 14,641 thousand (2012 – RO 13,369 thousand) represents the collective impairment provision made on a portfolio basis.

Notes to the financial statements
for the year ended 31 December 2013 (continued)

5. Financial risk management (continued)

5.1 Credit risk (continued)

5.1.5 Loans and advances and due from banks

b) The break-up of the loans and advances to customers in respect of the risk ratings adopted by the Bank are:

31 December 2013

	Retail loans 2013 RO' 000	Corporate loans 2013 RO' 000	Total 2013 RO' 000
Standard loans	**417,334**	**649,302**	**1,066,636**
Special mention loans	**1,077**	**6,280**	**7,357**
Substandard loans	**1,110**	**5,155**	**6,265**
Doubtful loans	**1,484**	**1,533**	**3,017**
Loss	**7,422**	**19,909**	**27,331**
	428,427	**682,179**	**1,110,606**

31 December 2012

Standard loans	392,587	537,223	929,810
Special mention loans	399	10,039	10,438
Substandard loans	769	198	967
Doubtful loans	1,075	1,614	2,689
Loss	7,615	14,816	22,431
	402,445	563,890	966,335

c) Age analysis of loans and advances past due but not impaired:

	2013 RO' 000	2012 RO' 000
Past due up to 30 days	**1,520**	339
Past due 30-60 days	**7,181**	1,428
Past due 60-89 days	**4,761**	5,294
Total	**13,462**	7,061
Fair value of collateral	**5,535**	6,226

d) Loans and advances individually impaired

	2013	2012
Individually impaired loans	**36,613**	26,087
Fair value of collateral	**15,561**	19,222

Notes to the financial statements
for the year ended 31 December 2013 (continued)

5. Financial risk management (continued)

5.1 Credit risk (continued)

5.1.6 Loans and advances renegotiated

These arrangements include extended payment arrangements, deferral of payments and modification of interest rates. Following restructuring, a previously past due loan account is reclassified as a normal loan and managed with other similar loans which are neither past due nor impaired. The restructuring arrangements are based on the criteria and indicators which in the judgement of the management will indicate that the payment will most likely continue.

The total restructured loans at 31 December 2013 amounted to RO 6,060 thousand (2012 - RO 5,473 thousand).

5.1.7 Debt securities

The Bank's investments in debt securities are mainly in Government Development Bonds or Certificates of deposit denominated in Rial Omani issued by the Government of Oman. The Bank also invests in debt securities issued by other banks based on their individual external credit rating. These investments are made to deploy the surplus liquid funds with maximum return.

5.1.8 Repossessed collateral

Repossessed properties are sold as soon as practicable with the proceeds used to reduce the outstanding balance of the debt. Repossessed assets are classified as other assets in the statement of financial position. The value of assets obtained by the Bank by taking possession held as collateral as security at 31 December 2013 is RO 310 thousand (2012 - RO 310 thousand).

5.2 Market risk

The Bank takes on exposures to market risk which is the risk that the fair value or the future cash flows of the financial assets carried at fair value will fluctuate because of changes in market prices. Market risks arise from the open positions in interest rate, currency and equity products, all of which are exposed to changes in interest rates, credit spreads, equity prices and foreign exchange rates. The market risks are monitored by the Treasury Division and the Risk Management Department. Management is confident that the Bank has proper risk management policies in place to ensure that interest risk, liquidity risk and foreign exchange risk are mitigated considering the macro economic indicators affecting the banking business.

Notes to the financial statements
for the year ended 31 December 2013 (continued)

5. Financial risk management (continued)

5.2 Market risk (continued)

5.2.1 Price risk

The Bank holds listed securities classified as held-for-trading to take advantage of short-term and capital market movements. All investment securities present a risk of loss of capital. The Bank controls this risk through a careful selection of securities in accordance with Investment Management Policy approved by the Board. The maximum risk resulting from financial instruments is determined by the carrying amount of the financial instruments. The Bank's market positions are managed on a daily basis by the Head of Investment Management Department and are reviewed periodically by the Investment Committee.

A significant portion of Bank's investments include equity securities which are publicly traded on the Muscat Securities Market (MSM). The Bank's profits at 31 December 2013 may change by 0.29% (2012 – 0.28%) due to increase/decrease by 10% in the MSM - 30 Index and the GCC market indices, with all the other variables held constant. The Bank's investments have historically performed in line with the MSM - 30 Index.

5.2.2 Interest rate risk

Interest rate risk is the risk that the value of a financial instrument carried at fair value will fluctuate due to changes in the market interest rates. The Bank is exposed to interest rate risk as a result of mismatches or gaps in the amount of interest based assets and liabilities that mature or re-price in a given period. The Bank manages this risk by matching/re-pricing of assets and liabilities. The Bank is not excessively exposed to interest rate risk as its assets and liabilities are re-priced frequently. The Bank's Assets and Liabilities Committee (ALCO) monitors and manages the interest rate with the objective of limiting the potential adverse effects on the Bank's profitability. The table in Note 36 summarises the Bank's exposure to the interest rate risks. It includes the Bank's financial instruments at the carrying amount, categorised by the earlier of the contractual re-pricing and maturity dates.

For managing its interest rate risk in the banking book the Bank stipulates limits on open interest rate sensitive gaps for maturities up to 1 year and also periodically calculates Earnings at Risk (EaR) impact on its Net Interest Income (NII) from 100bps change in interest rates on open interest rate gaps for maturities up to 1 year. The EaR limit is stipulated as a certain percentage of the NII of the Bank for the previous year. The EaR at 31 December 2013 is 1.57% (2012 – 1.41%).

5.2.3 Currency risk

Currency risk arises when the value of a financial instrument changes due to changes in foreign exchange rates. In order to manage currency risk exposure the Bank enters into ready, spot and forward transactions in the inter-bank market as per documented policies approved by the Board of Directors.

Notes to the financial statements
for the year ended 31 December 2013 (continued)

5. Financial risk management (continued)

5.2 Market risk (continued)

5.2.3 Currency risk (continued)

The Bank’s foreign exchange exposure comprises of forward contracts, foreign currencies cash in hand, balances with banks abroad, foreign placements and other assets and liabilities denominated in foreign currency. The management manages the risk by monitoring net open position in line with limits set by the management and approved by the Executive Committee of the Board and entering into forward contracts based on the underlying commercial transactions with the customers.

Additionally, appropriate segregation of duties exist between the front and back office functions while compliance with the net open position is independently monitored on an ongoing basis by the management and the Assets and Liabilities Committee (ALCO). The net open position of the Bank in foreign currency exposures at the year end is set out below:

Foreign currency exposures

	2013	2012
	RO'000	RO'000
Net assets denominated in US Dollars	**1,286**	4,297
Net assets denominated in other foreign currencies	**775**	965
	2,061	5,262

Oman operates with a fixed exchange rate, and the Omani Rial is pegged to the US Dollar at $2.6008 per Omani Rial.

5.2.4 Liquidity risk

Liquidity risk is the risk that the Bank 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 close to its fair value. It includes the risk of being unable to fund assets at appropriate maturities and rates and the risk of being unable to liquidate an asset at a reasonable price and in an appropriate time frame.

The Bank’s funding activities are based on a range of instruments including deposits, other liabilities and assigned capital. Consequently, funding flexibility is increased and dependence on any one source of funds is reduced. The Bank maintains liquidity by continually assessing, identifying and monitoring changes in funding needs required to meet strategic goals set in terms of the overall strategy. In addition the Bank holds certain liquid assets as part of its liquidity risk management strategy.

The Bank manages the liquidity risk based on estimated maturities using the guidelines provided by the Central Bank of Oman for the estimates. The table in Note 35 represents cash flows receivable to and payable by the Bank under derivative and non-derivative assets and liabilities by estimated remaining maturities at the reporting date.

Notes to the financial statements
for the year ended 31 December 2013 (continued)

5. Financial risk management (continued)

5.3 Operational risk

Operational risk is the risk of direct or indirect loss resulting from inadequate or failed internal processes, people, and systems or from external events.

Losses from external events such as a natural disaster that has a potential to damage the Bank's physical assets or electrical or telecommunication failures that disrupt business are relatively easier to define than losses from internal problems such as employee fraud and product flaws. The risks from internal problems are more closely tied to the Bank's specific products and business lines; they are more specific to the Bank's operations than the risks due to external events. Operational risks faced by the Bank include IT Security, telecom failure, frauds, and operational errors.

Operational risk is controlled through a series of strong internal controls and audits, well-defined segregation of duties and reporting lines, operational manuals and standards. Internal audit independently reviews the effectiveness of the Bank's internal controls and its ability to minimize the impact of operational risks.

5.4 Fair value estimation

The estimate of fair values of the financial instruments is based on information available to management as at 31 December 2013. Whilst management has used its best judgment in estimating the fair value of the financial instruments, there are inherent weaknesses in any estimation technique. The estimates involve matters of judgment and cannot be determined with precision. The bases adopted in deriving the fair values are as follows:

5.4.1 Current account balances due to and from banks

The carrying amount of current account balances due to and from banks was considered to be a reasonable estimate of fair value due to their short-term nature.

5.4.2 Loans and advances

The fair value of non-performing loans approximates to the book value adjusted for allowance for loan impairment. For the performing loans, the fair value is taken as being equivalent to its carrying amount as the prevailing interest rates offered on similar loans are not materially different from the actual loan rates.

5.4.3 Investments at fair value through profit or loss and available-for-sale

Quoted market prices, when available, are used as the measure for fair value. However, when the quoted market prices do not exist, fair value presented is estimated using discounted cash flow models or other valuation techniques. Changes in fair value resulting from these calculations are not material to the financial statements.

Notes to the financial statements
for the year ended 31 December 2013 (continued)

5. Financial risk management (continued)

5.4 Fair value estimation (continued)

5.4.4 Customers' deposits

The fair value of demand, call, and savings deposits is the amount payable on demand at the reporting date, which equal to the carrying value of those liabilities. The estimated fair value of fixed rate deposits whose interest rates are materially different from the prevailing market interest rates are determined by discounting the contractual cash flows using the market interest rates currently offered for similar deposits.

5.4.5 Derivatives

The Bank usually enters into short term forward foreign exchange contracts, on behalf of its customers for the sale and purchase of foreign currencies. For forward foreign exchange contracts, it uses a valuation model with readily available market observable inputs. The model incorporates various inputs including the credit quality of counterparties, foreign exchange spot and forward rates and interest rate curves.

5.5 Financial instruments by category

The accounting policies for financial instruments have been applied to the line items below:
Assets as per statement of financial position:

2013

Assets as per statement of financial position	Fair value through profit or loss RO'000	Held-to-maturity RO'000	Available-for-sale investments RO'000	Loans and receivables RO'000	Total RO'000
31 December 2013					
Bank balances and cash	**-**	**116,939**	**-**	**-**	**116,939**
Certificates of deposit	**-**	**100,000**	**-**	**-**	**100,000**
Due from banks	**-**	**50,893**	**-**	**-**	**50,893**
Loans and advances	**-**	**-**	**-**	**1,076,291**	**1,076,291**
Investment securities	**2,044**	**32,073**	**19,320**	**-**	**53,437**
Other assets	**-**	**-**	**-**	**31,985**	**31,985**
	2,044	**299,905**	**19,320**	**1,108,276**	**1,429,545**
2012					
Bank balances and cash	-	149,893	-	-	149,893
Certificates of deposit	-	90,000	-	-	90,000
Due from banks	-	102,829	-	-	102,829
Loans and advances	-	-	-	934,814	934,814
Investment securities	2,301	27,860	10,706	-	40,867
Other assets	-	-	-	30,227	30,227
	2,301	370,582	10,706	965,041	1,348,630

Notes to the financial statements
for the year ended 31 December 2013 (continued)

5. Financial risk management (continued)

5.5 Financial instruments by category (continued)

	Other liabilities	
	2013	2012
Liabilities as per statement of position	**RO'000**	RO'000
Due to banks	**3,862**	59,709
Deposits from customers	**1,149,153**	1,031,144
Other liabilities	**50,896**	41,595
Subordinated bonds	**50,000**	50,000
Taxation	**3,692**	3,850
	1,257,603	1,186,298

6. Capital management

The Bank's objectives of capital management are:

- to comply with the capital requirements set by the regulator i.e. the Central Bank of Oman;
- to safeguard the Bank's ability to continue as a going concern while providing adequate returns to the shareholders; and
- to maintain a strong capital base to support the development of its business.

The principal objective of the Central Bank of Oman's (CBO) capital adequacy requirements is to ensure that an adequate level of capital is maintained to withstand any losses which may result from the risks in a Bank's statement of financial position, in particular credit risk. The CBO's risk-based capital adequacy framework is consistent with the international standards of the Bank for International Settlements (BIS).

Notes to the financial statements
for the year ended 31 December 2013 (continued)

6. Capital management (continued)

The CBO requires the banks registered in the Sultanate of Oman to maintain a minimum capital adequacy ratio of 12% based on guidelines of the Basel II Accord. The ratio calculated in accordance with the CBO and BIS capital adequacy guidelines as per the Basel II Accord is as follows:

	2013	2012
	RO'000	RO'000
Capital		
Tier 1	**185,788**	172,365
Tier 2	**45,255**	53,435
Total capital base	**231,043**	225,800
Risk weighted assets		
Credit risk	**1,279,113**	1,222,375
Market risk	**7,713**	7,950
Operational risk	**112,025**	104,838
Total risk weighted assets	**1,398,851**	1,335,163
Capital adequacy ratio %	**16.52%**	16.91%

The Tier 1 capital consists of paid-up capital and reserves. The Tier 2 capital consists of the subordinated bonds and collective provision made for the loan impairment on the performing portion of the loans and advances against the losses incurred but not identified.

7. Cash and balances with the Central Bank of Oman

	2013	2012
	RO' 000	RO' 000
Cash in hand	**24,279**	23,194
Balances with the Central Bank of Oman:		
- Clearing account	**92,160**	126,199
- Capital deposit	**500**	500
	116,939	149,893

The capital deposit cannot be withdrawn without the approval of the Central Bank of Oman. The capital deposit earns interest at 1.5% per annum (2012 – 1.5% p.a.).

Notes to the financial statements
for the year ended 31 December 2013 (continued)

8. Certificates of deposit

Certificates of deposit are issued by the Central Bank of Oman for periods ranging from 28 days and carry interest at the rate of 0.13% (2012 – 0.09%) per annum.

9. Due from banks

	2013 RO'000	2012 RO'000
Foreign currency:		
Money market placements	**34,650**	82,775
Current accounts	**16,243**	20,054
	50,893	102,829

At 31 December 2013, 100% of the Bank's placements were with three banks rated between A3 to Baa1 by Moody's (2012 – 75% of the Bank's placements were with five banks rated Aa3 to Ba3)

10. Loans and advances

	2013 RO' 000	2012 RO' 000
Corporate loans		
Term loans	**546,682**	448,510
Overdrafts	**111,290**	96,497
Bills discounted	**21,319**	18,883
Islamic finance	**2,888**	-
	682,179	563,890
Personal loans		
Consumer loans	**328,076**	310,571
Mortgage loans	**66,520**	55,317
Overdrafts	**27,237**	30,232
Credit cards	**5,759**	6,325
Islamic finance	**835**	-
	428,427	402,445
Gross loans and advances	**1,110,606**	966,335
Less: allowance for loan impairment and contractual interest not recognised (refer to note (a) below)	**(34,315)**	(31,521)
Net loans and advances	**1,076,291**	934,814

Notes to the financial statements
for the year ended 31 December 2013 (continued)

10. Loans and advances (continued)

(a) Allowance for loan impairment

The movements in the allowance for loan impairment are as follows:

2013

	Allowance for loan impairment RO' 000	Contractual interest not recognised RO' 000	Total RO' 000
At 1 January	**24,777**	**6,744**	**31,521**
Provided during the year	**6,305**	**2,103**	**8,408**
Provided during the year for Islamic financing	**46**	**-**	**46**
Amounts written off during the year	**(276)**	**(385)**	**(661)**
Amounts released / recovered during the year	**(3,534)**	**(1,465)**	**(4,999)**
At 31 December	**27,318**	**6,997**	**34,315**

2012

	Allowance for loan impairment RO' 000	Contractual interest not recognised RO' 000	Total RO' 000
At 1 January	21,328	5,827	27,155
Provided during the year	5,727	1,802	7,529
Amounts written off during the year	(565)	(314)	(879)
Amounts released / recovered during the year	(1,713)	(571)	(2,284)
At 31 December	24,777	6,744	31,521

At 31 December 2013, RO 14,641 thousand (2012 - RO 13,369 thousand) out of the total loan impairment provisions has been made on a portfolio basis against the losses incurred but not identified on the performing portion of the loans and advances.

At 31 December 2013, loans and advances on which contractual interest was not recognised or has not been accrued amounted to RO 36,613 thousand (31 December 2012 – RO 26,087 thousand).

Notes to the financial statements
for the year ended 31 December 2013 (continued)

10. Loans and advances (continued)

Islamic financing

Included in the above loans and advances are the following Islamic financing contracts:

2013

	Personal RO' 000	Corporate RO' 000	Total RO' 000
Musharaka	**570**	**2,888**	**3,458**
Murabaha	**202**	**-**	**202**
Ijarah Muntahia Bittamleek	**63**	**-**	**63**
At 31 December	**835**	**2,888**	**3,723**

	Gross investment in lease RO' 000	Present value of minimum lease payment RO' 000
Within one year	**10**	**7**
Two to five years	**29**	**21**
More than five years	**49**	**35**
	88	**63**
Deferred profit	**(25)**	**-**
Net investment in lease finance	**63**	**63**

(a) Concentration of loans and advances

All loans and advances were granted to customers within the Sultanate of Oman. The concentration of gross loans and advances by economic sector is as follows:

	2013 RO' 000	2012 RO' 000
Personal loans	**428,427**	402,445
Manufacturing	**110,532**	106,897
Transportation	**139,672**	121,693
Construction	**105,490**	76,865
Services	**34,007**	45,034
Wholesale and retail trade	**34,252**	21,236
Mining and quarrying	**15,064**	17,281
Import trade	**32,157**	33,549
Financial institutions	**28,952**	21,888
Electricity , Water and Gas	**44,249**	39,191
Agriculture and allied activities	**4,771**	8,916
Others	**133,033**	71,340
	1,110,606	966,335

Of the above, loans with variable interest rates amount to RO 507,090 thousand (2012 – RO 380,607 thousand), loans carrying fixed interest rates amount to RO 598,232 thousand (2012 - RO 585,728 thousand) and Islamic finance contracts RO 5,284 thousand (2012: nil).

Notes to the financial statements
for the year ended 31 December 2013 (continued)

11. Investment securities

	2013 Carrying value RO'000	**2013 Cost RO'000**	2012 Carrying value RO'000	2012 Cost RO'000
Available-for-sale				
- quoted	**18,949**	**17,561**	10,357	10,165
- unquoted	**371**	**395**	349	396
	19,320	**17,956**	10,706	10,561
Designated as at fair value through profit or loss				
- quoted	**716**	**517**	586	517
- unquoted	**286**	**1,287**	272	1,271
	1,002	**1,804**	858	1,788
Held-for-trading				
- quoted	**1,042**	**1,119**	1,443	1,996
Held-to-maturity				
Oman Government Development Bonds	**32,073**	**32,073**	27,860	27,860
Total investment securities	**53,437**	**52,952**	40,867	42,205

Unquoted financial assets at fair value through profit or loss include investment in the Financial Settlement and Guaranteed Fund of RO 189,783 (2012 – RO 175,062) which is not recoverable until the date the Bank ceases its brokerage activities or the fund is liquidated, whichever is earlier.

Refer note 35 for the maturity profile of the investment securities.

Fair value hierarchy

The Bank uses the following hierarchy for determining and disclosing the fair value of financial investments by valuation technique:

Level 1: quoted (unadjusted) prices in active markets for identical assets or liabilities

Level 2: other techniques for which all inputs which have a significant effect on the recorded fair value are observable, either directly or indirectly.

Notes to the financial statements
for the year ended 31 December 2013 (continued)

11. Investment securities (continued)

Fair value hierarchy (continued)

Level 3: techniques which use inputs which have a significant effect on the recorded fair value that are not based on observable market data.

Transfers between levels
During the reporting year ended 31 December 2013, there were no transfers between Level 1 and Level 2 fair value measurements, and no transfers into and out of Level 3 fair value measurements.

The movements in investment securities may be summarised as follows:

2013	At 1 January 2013 RO'000	Additions RO'000	Disposals (sale and redemption) RO'000	Changes in fair value recorded in statement of comprehensive income RO'000	Changes in fair value recorded in equity RO'000	At 31 December 2013 RO'000
Available-for- sale						
Quoted – level 1	**10,357**	**20,727**	**(13,331)**	**-**	**1,196**	**18,949**
Unquoted – level 3	**349**	**-**	**-**	**-**	**22**	**371**
Designated as at fair value through profit or loss						
Quoted – level 1	**586**	**-**	**-**	**130**	**-**	**716**
Unquoted – level 3	**272**	**14**	**-**	**-**	**-**	**286**
Held for trading						
Quoted – level 1	**1,443**	**8,338**	**(9,216)**	**477**	**-**	**1,042**
Investments held-to-maturity	**27,860**	**4,213**	**-**	**-**	**-**	**32,073**
	40,867	**33,292**	**(22,547)**	**607**	**1,218**	**53,437**
2012						
Available-for- sale						
Quoted – level 1	7,980	4,293	(1,788)	-	(128)	10,357
Unquoted – level 3	336	-	-	-	13	349
Designated as at fair value through profit or loss						
Quoted – level 1	573	13	-	-	-	586
Unquoted – level 3	506	-	(4)	(230)	-	272
Held for trading						
Quoted – level 1	4,582	3,373	(6,892)	380	-	1,443
Investments held-to-maturity	22,412	18,835	(13,387)	-	-	27,860
	36,389	26,514	(22,071)	150	(115)	40,867

Notes to the financial statements
for the year ended 31 December 2013 (continued)

11. Investment securities (continued)

Fair value hierarchy (continued)

Included under investments held to maturity are bonds issued by the Government of Oman amounting to RO 32,073 thousand (2012: RO 27,860 thousand). The bonds are denominated in Rial Omani and carry interest rates varying between 2.75% and 5.5% (2012 – 3.25% to 5.5%) per annum. The maturity profile of these bonds, based on the remaining maturity from the reporting date, is as follows:

	2013 RO'000	2012 RO'000
4 to 12 months	**2,400**	4,000
1 to 5 years	**29,673**	23,860
	32,073	27,860

12. Other assets

Customers' indebtedness against acceptances	**16,748**	19,953
Interest receivable	**4,199**	3,615
Prepayments	**1,489**	1,478
Receivable from investment customers	**1,095**	565
Positive fair value of derivatives (note 33)	**251**	249
Others	**8,203**	4,367
	31,985	30,227

Notes to the financial statements
for the year ended 31 December 2013 (continued)

13. Property and equipment

	Land and buildings RO'000	Computer equipment RO'000	Equipment furniture and fixtures RO'000	Motor vehicles RO'000	Capital work-in-progress RO '000	Total RO'000
At 1 January 2012	6,521	11,326	6,248	575	5,933	30,639
Additions	1,236	1,077	196	57	6,115	8,681
Transfers	-	156	161	-	(317)	-
Disposals	-	(1)	(1)	(49)	-	(51)
At 1 January 2013	**7,757**	**12,558**	**6,640**	**583**	**11,730**	**39,268**
Additions	**-**	**1,473**	**623**	**20**	**5,525**	**7,641**
Transfers	**13,931**	**716**	**1,620**	**-**	**(16,267)**	**-**
Disposals	**(270)**	**-**	**(132)**	**(34)**	**-**	**(436)**
At 31 December 2013	**21,418**	**14,747**	**8,751**	**569**	**988**	**46,473**
Depreciation						
At 1 January 2012	2,569	8,276	4,387	390	-	15,622
Charge for the year	-	1,166	667	83	-	1,916
Relating to disposals	-	(1)	(1)	(47)	-	(49)
At 1 January 2013	**2,569**	**9,441**	**5,053**	**426**	**-**	**17,489**
Charge for the year	**371**	**1,050**	**850**	**66**	**-**	**2,337**
Relating to disposals	**-**	**-**	**(129)**	**(34)**	**-**	**(163)**
At 31 December 2013	**2,940**	**10,491**	**5,774**	**458**	**-**	**19,663**
Carrying value						
At 31 December 2013	**18,478**	**4,256**	**2,977**	**111**	**988**	**26,810**
At 31 December 2012	5,188	3,117	1,587	157	11,730	21,779

Depreciation charge for the year is allocated as follows:

	2013 RO'000	2012 RO'000
Operating expenses (note 29)	**2,294**	1,916
Operating expenses of Islamic window	**43**	-
	2,337	1,916

14. Due to banks

	2013	2012
	RO'000	RO'000
Current accounts	**3,862**	59,709

15. Deposits from customers

	2013	2012
Term deposits	**464,283**	430,361
Demand and call accounts	**508,896**	444,188
Saving accounts	**175,974**	156,595
	1,149,153	1,031,144

The concentration of customers' deposits by Private and Government sector is as follows:

	2013	2012
	RO'000	RO'000
Private	**825,718**	700,710
Government	**323,435**	330,434
	1,149,153	1,031,144

Islamic customer's deposits

Included in the above customers' deposits are the following Islamic customer deposits:

	2013	2012
	RO'000	RO'000
Current accounts- Qard	**13**	-
Mudarabah accounts	**42**	-
	55	-

Notes to the financial statements
for the year ended 31 December 2013 (continued)

16. Other liabilities

	2013 RO'000	2012 RO'000
Liabilities against acceptances	**16,748**	19,953
Payable to investment customers	**12,206**	6,668
Accrued expenses and other payables	**9,436**	4,381
Interest payable	**4,721**	3,514
Cheques and trade settlement payable	**3,877**	2,918
Staff terminal benefits (note 16 a)	**2,283**	2,666
Interest and commission received in advance	**1,385**	1,259
Negative fair value of derivatives (note 33)	**240**	236
	50,896	41,595

16. a Staff terminal benefits

At 1 January	**2,666**	2,352
Charge for the year	**362**	469
Payment to employees during the year	**(745)**	(155)
At 31 December	**2,283**	2,666

17. Subordinated bonds

In order to enhance the capital adequacy and to meet the funding requirements, the Bank issued non-convertible unsecured subordinated bonds of RO 50 Million (50,000,000 units of RO 1 each) for a tenor of five years and one month in April 2012 through private placement. The bonds are listed in the Muscat Securities Market and are transferable through trading. The bonds carry a fixed coupon rate of 5.5% per annum (2012: 5.5% per annum), payable semi-annually with the principal payable on maturity.

18. Taxation

	2013 RO' 000	2012 RO' 000
Statement of profit or loss		
Current year	**3,659**	3,579
Deferred tax	**(4)**	(6)
	3,655	3,573
Statement of financial position		
Current year	**3,419**	3,573
Deferred tax liability	**273**	277
	3,692	3,850
Deferred tax liability		
At 1 January	**277**	283
Movement for the year	**(4)**	(6)
At 31 December	**273**	277

Notes to the financial statements
for the year ended 31 December 2013 (continued)

18. Taxation (continued)

The Bank is liable for income tax in accordance with the income tax laws of the Sultanate of Oman. The tax rate applicable to the Bank is 12%. For determining the tax expense for the year, the accounting profit for the year has been adjusted for tax purposes. Adjustments for tax purposes include items relating to both income and expense. After giving effect to these adjustments, the average effective tax rate is estimated to be 11.89 % (2012 – 12.39%).

The deferred tax liability has been recognised at the effective rate of 12% (2012 – 12%).

The reconciliation between the profit before taxation and the tax expense is as follows:

	2013	2012
	RO' 000	RO' 000
Profit before tax	**28,678**	28,843
Tax at the applicable rate of 12% after statutory deduction of RO 30,000 (2012 - 12%)	**3,438**	3,458
Tax effect of temporary differences	**(4)**	(6)
Tax effect of income that is not taxable and expenses that are not deductible in determining taxable profit	**225**	127
Tax expense for the current year	**3,659**	3,579
Add : Deferred tax liability reversed created during the year	**(4)**	(6)
Tax expense for the year	**3,655**	3,573

Status of tax assessments

The assessments for the years up to 2008 are complete. The assessments for 2009 to 2012 are not yet finalised by the Tax Authorities. Management believes that no significant further liabilities will be incurred by the Bank on completion of the pending tax assessments as compared to the existing provision established.

19. Share capital

The authorized capital is RO 200,000,000 and the issued share capital comprises 1,160,000,000 fully paid shares of RO 0.100 each.

In the Annual General Meeting held on 28 March 2012 the shareholders approved the stock dividend of RO 6 million (6 million shares @ RO 1 each) and rights issue of RO 10 million (10 million shares @ RO 1 each).

Notes to the financial statements
for the year ended 31 December 2013 (continued)

19. Share capital (continued)

The shareholders of the Bank at the reporting date were as follows:

	Country of incorporation	Share-holding %	2013 RO'000	2012 RO'000
Oman International Development & Investment Co. SAOG	Oman	**50.99**	**59,148**	59,148
Arab Bank Plc	Jordan	**49.00**	**56,840**	56,840
Oman Investment Services SAOC	Oman	**0.01**	**12**	12
			116,000	116,000

20. Legal reserve

In accordance with Article 106 of the Omani Commercial Companies Law of 1974, the Bank is required to transfer 10% of its profit after tax for the year to legal reserve until the accumulated balance of the reserve equals at least one third of the Bank's paid up share capital. This reserve is not available for distribution.

21. General reserve

The Bank has established a policy to set aside a portion of the profit each year to a 'General reserve' in order to meet any unforeseen contingencies.

22. Subordinated debt reserve

The subordinated debt reserve has been created by a transfer of 20% of the subordinated bonds out of the profit after tax for the year. The Central Bank of Oman requires that a reserve be set aside annually for the subordinated bonds which are due to mature within five years (refer note 17). The reserve is available for transfer back to retained earnings upon maturity of the subordinated bonds.

23. Dividend proposed and paid

The Board of Directors proposed a cash dividend of RO 0.010 per share totalling to RO 11.6 million for the year ended 31 December 2013 (2012 - RO 0.010 per share totalling to RO 11.6 million). A resolution to approve the dividend will be presented to the shareholders at the Annual General Meeting.

Notes to the financial statements
for the year ended 31 December 2013 (continued)

24. Interest income

	2013 RO'000	2012 RO'000
Loans and advances	**52,694**	49,719
Oman Government Development Bonds	**745**	567
Placements with banks and other money market placements	**57**	145
Certificates of deposits	**114**	85
	53,610	50,516

25. Interest expense

Time deposits	**6,699**	6,077
Subordinated bonds	**2,742**	1,829
Call accounts	**736**	545
Borrowings	**599**	725
Savings accounts	**382**	373
	11,158	9,549

26. Fee and commission income – net

Fee and commission income	**16,222**	16,101
Fee and commission expense	**(1,805)**	(1,856)
	14,417	14,245

27. Investment income

From financial assets at fair value through profit or loss

Fair value changes	**607**	150
Profit on sale of investments	**1,057**	832
Dividend income	**644**	459
	2,308	1,441

28. Other operating income

Exchange income	**4,453**	4,100
Income from Islamic window	**23**	-
Other income	**175**	75

Notes to the financial statements
for the year ended 31 December 2013 (continued)

	4,651	4,175

29. Operating expenses

	2013	2012
	RO'000	RO'000
Staff costs (refer below)	**20,426**	18,089
Other operating expenses	**10,259**	8,435
Depreciation	**2,294**	1,916
Operating expenses of the Islamic window	**723**	-
Directors' remuneration	**96**	102
	33,798	28,542
Details of staff costs are as follows:		
Salaries	**14,092**	12,518
Allowances	**3,043**	2,578
Social security costs	**945**	822
End of service benefits	**362**	469
Other costs	**1,984**	1,702
	20,426	18,089

30. Earnings per share

The calculation of basic earnings per share is based on the profit for the year attributable to the ordinary shareholders as follows:

	2013	2012
Profit for the year (RO'000)	**25,023**	25,270
Weighted average number of shares outstanding during the year	**1,160,000**	1,130,959
Basic earnings per share (RO)	**0.022**	0.022

The weighted average number of shares outstanding during the year 2012 had been adjusted for rights issue and increase in number of shares due to change in the nominal value of shares. The basic earnings per share is the profit for the period divided by the weighted average number of shares outstanding.

No figure for diluted earnings per share has been presented, as the Bank has not issued any instruments, which would have an impact on earnings per share when exercised.

Notes to the financial statements
for the year ended 31 December 2013 (continued)

31. Related party transactions

Management service agreement with a shareholder

The Bank has a management agreement with Arab Bank Plc Jordan, a shareholder. During the year ended 31 December 2013, the management fees as per the agreement amounted to RO 75 thousand (2012: RO 29 thousand).

Other related parties transactions

In the ordinary course of business, the Bank conducts transactions with certain of its Directors and/or shareholders and companies over which they are able to exert significant influence. The aggregate amounts of balances with such related parties are as follows:

2013

	Major shareholders RO'000	Others RO'000	Total RO'000
Loans and advances	**5,000**	**30,817**	**35,817**
Customers' deposits	**472**	**7,099**	**7,571**
Payable to investment customers	**963**	**-**	**963**
Receivables from investment customers	**-**	**176**	**176**
Investments	**782**	**539**	**1,321**
Due from banks	**5,524**	**-**	**5,524**
Due to banks	**1,771**	**-**	**1,771**
Stand by line of credit	**48,125**	**-**	**48,125**
Letters of credit guarantees and acceptances	**158,233**	**3,285**	**161,518**

2012

Loans and advances	4,907	39,508	44,415
Customers' deposits	152	7,532	7,684
Investments	626	443	1,069
Payable to investment customers	1,443	218	1,661
Due from banks	56,794	-	56,794
Due to banks	1,401	-	1,401
Stand by line of credit	48,125	-	48,125
Letters of credit guarantees and acceptances	183,150	2,600	185,750

Notes to the financial statements
for the year ended 31 December 2013 (continued)

31. Related party transactions (continued)

Movement of loans and advances given to related parties:

	2013	2012
	RO'000	RO'000
At 1 January 2013	**44,415**	42,920
Disbursed during the year	**56,399**	19,537
Paid during the year	**(64,997)**	(18,042)
At 31 December 2013	**35,817**	44,415

None of the loans and advances given to related parties were identified as impaired and no provision for any impairment has been recognised (2012: none identified or recognised)

The statement of comprehensive income includes the following amounts in relation to the transactions with related parties:

31 December 2013

	Major shareholders RO'000	**Others RO'000**	**Total RO'000**
Interest and commission income	**288**	**1,055**	**1,343**
Interest expense	**401**	**1**	**402**
31 December 2012			
Interest and commission income	402	1,220	1,622
Interest expense	346	34	380

Key management compensation

The Directors' remuneration is set out in Note 29. The remuneration of other members of key management during the year was as follows:

	2013	2012
	RO'000	RO'000
Salaries and other short-term benefits	**1,390**	1,281
End of service benefits	**93**	185
	1,483	1,466

Notes to the financial statements
for the year ended 31 December 2013 (continued)

32. Cash and cash equivalents

	2013 RO'000	2012 RO'000
Cash and balances with the CBO	**116,939**	149,893
Certificates of deposit	**100,000**	90,000
Due from banks	**50,893**	102,829
Less: due to banks	**(3,862)**	(59,709)
Restricted deposits included under balances with the CBO	**(500)**	(500)
	263,470	282,513

33. Derivative financial instruments

At the reporting date, there were outstanding forward foreign exchange contracts, all maturing within one year, entered into on behalf of customers for the sale and purchase of foreign currencies. These financial instruments have been recognised at prices in active markets for identical assets or liabilities. These fair values and the notional contracted amounts are summarised below:

			Notional amounts by term of maturity			
	Positive fair value RO'000 (note 12)	Negative fair value RO'000 (note 16)	Notional amount RO'000	Within 3 months RO'000	3 - 12 months RO'000	1 - 5 years RO'000
31 December 2013						
Purchase contracts	**251**	**-**	**60,041**	**54,421**	**5,620**	**-**
Sale contracts	**-**	**(240)**	**(60,030)**	**(54,412)**	**(5,618)**	**-**
	251	**(240)**	**11**	**9**	**2**	**-**
31December 2012						
Purchase contracts	249	-	20,895	12,642	8,253	-
Sale contracts	-	(236)	(20,882)	(12,633)	(8,249)	-
	249	(236)	13	9	4	-

Notes to the financial statements
for the year ended 31 December 2013 (continued)

34. Contingent liabilities and commitments

(a) Letters of credit and guarantees

The Bank is a party to financial instruments with off-balance sheet credit risk in the normal course of business to meet the financing needs of its customers. These financial instruments include standby letters of credit, financial guarantees to third parties, commitments to extend credit and acceptances.

The Bank's exposure to credit loss in the event of non-performance by the other party to such financial instruments is represented by the contract value or the notional amount of the instrument. However, generally the credit risk on these transactions is lower than the contract value or the notional amount. In addition, some commitments to extend credit can be cancelled or revoked at any time at the Bank's option.

The risk involved is essentially the same as the credit risk involved in extending loan facilities and therefore these transactions are subject to the same credit organisation, portfolio maintenance and collateral requirements as for customers applying for loans and advances.

The outstanding contract value or the notional amounts of these instruments at 31 December were as follows:

	2013	2012
	RO'000	RO'000
Letters of credit	**461,952**	553,403
Guarantees	**394,281**	415,986
Financial Guarantees	**89,681**	85,183
	945,914	1,054,572

Letters of credit and guarantees amounting to RO 696,813 thousand (2012 - RO 849,010 thousand) were counter guaranteed by other banks.

Letters of credit and guarantees include RO 392 thousand (2012: RO 411 thousand) relating to non-performing loans.

34. Contingent liabilities and commitments

(a) Letters of credit and guarantees (continued)

The concentration of letters of credit and guarantees by industry sector is as follows:

	2013 RO'000	2012 RO'000
Export trade	**399,213**	505,131
Construction	**264,317**	264,433
Government	**94,033**	108,848
Transportation	**49,323**	72,292
Import trade	**62,740**	48,270
Utilities	**46,941**	24,452
Services	**11,406**	12,422
Wholesale and retail trade	**10,764**	11,277
Manufacturing	**7,177**	7,447
	945,914	1,054,572

(b) Capital commitments

At the reporting date, outstanding capital commitments in respect of premises and equipment purchases were RO 1,384 thousand (2012 - RO 5,629 thousand).

(c) Undrawn loan commitments

At the reporting date, outstanding undrawn loan commitments amounted to RO 770 thousand (2012- RO 8,088 thousand). Each undrawn loan commitment is included in the time band containing the earliest date it can be drawn down.

The commitments set out in (b) to (c) above are expected to crystallise in the following periods:

	Up to 1 year RO'000	**1 to 5 years RO'000**	**Over 5 years RO'000**	**Total RO'000**
2013				
Capital commitments	**1,384**	**-**	**-**	**1,384**
Undrawn loan commitments	**-**	**770**	**-**	**770**
2012				
Capital commitments	5,629	-	-	5,629
Undrawn loan commitments	388	7,700	-	8,088

Notes to the financial statements
for the year ended 31 December 2013 (continued)

34. Contingent liabilities and commitments (continued)

(c) Legal claims

Litigation is a common occurrence in the banking industry due to the nature of the business. The Bank has an established protocol for dealing with such legal claims. Once professional advice has been obtained and the amount of damages reasonably estimated, the Bank makes adjustments to account for any adverse effects which the claims may have on its financial standing. At year end, the Bank had certain unresolved legal claims which are not expected to have any significant implication on the Bank financial statements.

35. Assets and liabilities maturity profile

The Bank has established policies to manage the liquidity risk arising from the mismatch in the final maturity of the assets and liabilities on the statement of financial position as explained in note 5.2.4. The table below represents cash flows receivable to and payable by the Bank under derivative and non-derivative assets and liabilities by estimated remaining maturities at the reporting date.

2013	On demand or within 3 months RO'000	3 to 12 months RO'000	1 to 5 Years RO'000	Over 5 years RO'000	Total RO'000
Assets					
Cash and balances with the Central Bank of Oman	58,170	26,682	15,542	16,545	116,939
Certificates of deposit	100,000	-	-	-	100,000
Due from banks	50,893	-	-	-	50,893
Loans and advances	191,251	175,348	273,231	436,461	1,076,291
Investment securities	21,356	2,400	27,681	2,000	53,437
Other assets	27,347	4,061	577	-	31,985
Property and equipment	-	-	-	26,810	26,810
Total assets	449,017	208,491	317,031	481,816	1,456,355
Liabilities					
Due to banks	3,862	-	-	-	3,862
Deposits from customers	420,398	250,980	272,703	205,072	1,149,153
Other liabilities	42,847	1,358	6,691	-	50,896
Subordinated bond	-	-	50,000	-	50,000
Taxation	3,419	273	-	-	3,692
Total liabilities	470,526	252,611	329,394	205,072	1,257,603
Net assets	(21,509)	(44,120)	(12,363)	276,744	198,752

Notes to the financial statements
for the year ended 31 December 2013 (continued)

35. Assets and liabilities maturity profile (continued)

2013	**On demand or within 3 months RO'000**	**3 - 12 months RO'000**	**1 to 5 years RO'000**	**Over 5 years RO'000**	**Total RO'000**
Forward exchange contracts at notional amounts (note 33)	-	-	-	-	-
Purchase contracts	**54,421**	**5,620**	**-**	**-**	**60,041**
Sale contracts	**(54,412)**	**(5,618)**	**-**	**-**	**(60,030)**
	9	**2**	**-**	**-**	**11**
2012					
Assets					
Cash and balances with the Central Bank of Oman	76,297	33,260	17,551	22,785	149,893
Certificates of deposit	90,000	-	-	-	90,000
Due from banks	102,829	-	-	-	102,829
Loans and advances	193,424	103,815	238,590	398,985	934,814
Investment securities	13,007	4,000	21,860	2,000	40,867
Other assets	21,881	8,011	335	-	30,227
Property and equipment	-	-	-	21,779	21,779
	497,438	149,086	278,336	445,549	1,370,409
Liabilities					
Due to banks	59,709	-	-	-	59,709
Deposits from customers	433,887	271,760	143,405	182,092	1,031,144
Other liabilities	32,728	5,865	3,002	-	41,595
Subordinated bonds	-	-	50,000	-	50,000
Taxation	3,567	283	-	-	3,850
Total liabilities	529,891	277,908	196,407	182,092	1,186,298
Net assets	(32,453)	(128,822)	81,929	263,457	184,111
Forward exchange contracts at notional amounts (note 33)	-	-	-	-	-
Purchase contracts	12,642	8,253	-	-	20,895
Sale contracts	(12,633)	(8,249)	-	-	(20,882)
	9	4	-	-	13

Notes to the financial statements
for the year ended 31 December 2013 (continued)

35. Assets and liabilities maturity profile (continued)

The following table below shows the contractual expiry by maturity of the Bank's contingent liabilities and commitments. For issued guarantee contracts, the maximum amount of the guarantee is allocated to the earliest period in which the guarantee could be called.

2013	**On demand or within 3 months RO'000**	**3 to 12 months RO'000**	**1 to 5 years RO'000**	**Over 5 years RO'000**	**Total RO'000**
Letters of guarantee	**138,253**	**141,119**	**204,531**	**59**	**483,962**
Letters of credit	**461,457**	**495**	**-**	**-**	**461,952**
Total commitments and contingencies	**599,710**	**141,614**	**204,531**	**59**	**945,914**
2012					
Letters of guarantee	170,999	97,336	232,633	201	501,169
Letters of credit	152,859	398,239	2,305	-	553,403
Total commitments and contingencies	323,858	495,575	234,938	201	1,054,572

The Bank expects that not all of the contingent liabilities or commitments will be drawn before expiry of the commitments.

The details of Bank's capital commitments, operating lease commitments and undrawn loan commitments are disclosed in note 34.

Notes to the financial statements
for the year ended 31 December 2013 (continued)

36. Assets and liabilities re-pricing profile

The re-pricing profile is based on contractual re-pricing or maturity dates, whichever dates are earlier. The Bank's assets and liabilities are included at carrying amounts.

2013	Average effective interest rate %	Within 3 months RO'000	4 to 12 months RO'000	1 to 5 years RO'000	Over 5 years RO'000	Non-interest bearing RO'000	Total RO'000
Assets							
Cash and balances with the Central Bank of Oman	1.50	-	-	-	500	116,439	116,939
Certificates of deposit	0.13	100,000	-	-	-	-	100,000
Due from banks	0.11	34,650	-	-	-	16,243	50,893
Loans and advances	5.06	201,107	225,778	631,161	14,558	3,687	1,076,291
Investment securities at fair value		-	-	-	-	21,364	21,364
Investment–held to maturity	2.76	-	2,400	27,673	2,000	-	32,073
Other assets		4,199	-	-	-	27,786	31,985
Property and equipment		-	-	-	-	26,810	26,810
Total assets		339,956	228,178	658,834	17,058	212,329	1,456,355
Liabilities							
Due to banks	-	-	-	-	-	3,862	3,862
Deposits from customers	0.94	397,372	180,175	57,694	-	513,912	1,149,153
Other liabilities		4,721	-	-	-	46,175	50,896
Subordinated bonds	5.50	-	-	50,000	-	-	50,000
Taxation		-	-	-	-	3,692	3,692
Total liabilities		402,106	180,175	107,694	-	567,628	1,257,603
Total interest sensitivity gap		(62,150)	48,003	551,140	17,058	(355,299)	198,752

Notes to the financial statements
for the year ended 31 December 2013 (continued)

36. Assets and liabilities re-pricing profile (continued)

2012	Average effective interest rate	Within 3 months RO'000	4 - 12 months RO'000	1 to 5 years RO'000	Over 5 years RO'000	Non-interest bearing RO'000	Total RO'000
Assets							
Cash and balances with the Central Bank of Oman	1.5	-	-	-	500	149,393	149,893
Certificates of deposit	0.08	90,000	-	-	-	-	90,000
Due from banks	0.23	82,775	-	-	-	20,054	102,829
Loans and advances	5.32	222,064	180,159	525,512	7,079	-	934,814
Investment securities at fair value	-	-	-	-	-	13,007	13,007
Investment–held to maturity	2.83	-	4,000	21,860	2,000	-	27,860
Other assets	-	3,615	-	-	-	26,612	30,227
Property and equipment	-	-	-	-	-	21,779	21,779
Total assets		398,454	184,159	547,372	9,579	230,845	1,370,409
Liabilities							
Due to banks		-	-	-	-	59,709	59,709
Deposits from customers	0.94	429,095	116,150	44,033	-	441,866	1,031,144
Other liabilities		3,514	-	-	-	38,081	41,595
Subordinated bonds	5.50	-	-	50,000	-	-	50,000
Taxation		-	-	-	-	3,850	3,850
Total liabilities		432,609	116,150	94,033	-	543,506	1,186,298
Total interest sensitivity gap		(33,081)	68,009	453,339	9,579	(313,735)	184,111

Notes to the financial statements
for the year ended 31 December 2013 (continued)

37. Geographical distribution of assets and liabilities

2013	Sultanate of Oman	GCC countries	Europe	USA	Others	Total
	RO'000	RO'000	RO'000	RO'000	RO'000	RO'000
Assets						
Cash and balances with the Central Bank of Oman	**116,939**	**-**	**-**	**-**	**-**	**116,939**
Certificates of deposit	**100,000**	**-**	**-**	**-**	**-**	**100,000**
Due from banks	**34,658**	**4,923**	**6,427**	**4,346**	**539**	**50,893**
Loans and advances	**1,076,291**	**-**	**-**	**-**	**-**	**1,076,291**
Investment securities	**50,985**	**2,055**	**397**	**-**	**-**	**53,437**
Other assets	**31,985**	**-**	**-**	**-**	**-**	**31,985**
Property and equipment	**26,810**	**-**	**-**	**-**	**-**	**26,810**
Total assets	**1,437,668**	**6,978**	**6,824**	**4,346**	**539**	**1,456,355**
Liabilities						
Due to banks	**249**	**2,321**	**481**	**33**	**778**	**3,862**
Deposits from customers	**1,149,153**	**-**	**-**	**-**	**-**	**1,149,153**
Other liabilities	**50,896**	**-**	**-**	**-**	**-**	**50,896**
Subordinated Bonds	**50,000**	**-**	**-**	**-**	**-**	**50,000**
Taxation	**3,692**	**-**	**-**	**-**	**-**	**3,692**
Total liabilities	**1,253,990**	**2,321**	**481**	**33**	**778**	**1,257,603**
31 December 2012						
Cash and balances with the Central Bank of Oman	149,893	-	-	-	-	149,893
Certificates of deposit	90,000	-	-	-	-	90,000
Due from banks	9,640	76,254	7,450	8,466	1,019	102,829
Loans and advances	934,814	-	-	-	-	934,814
Investment securities	40,228	639	-	-	-	40,867
Other assets	30,227	-	-	-	-	30,227
Property and equipment	21,779	-	-	-	-	21,779
	1,276,581	76,893	7,450	8,466	1,019	1,370,409
Liabilities						
Due to banks	53,462	3,733	425	1,063	1,026	59,709
Deposits from customers	1,031,144	-	-	-	-	1,031,144
Other liabilities	41,595	-	-	-	-	41,595
Subordinated bonds	50,000	-	-	-	-	50,000
Taxation	3,850	-	-	-	-	3,850
	1,180,051	3,733	425	1,063	1,026	1,186,298

Notes to the financial statements
for the year ended 31 December 2013 (continued)

38. Customer concentrations

	Due from banks RO'000	Assets gross loans and advances RO'000	Investment securities RO'000	Deposits from customers RO'000	Liabilities due to banks RO'000	Contingent liabilities RO'000
2013						
Personal	**-**	**428,427**	**-**	**356,769**	**-**	**72**
Corporate	**50,893**	**571,166**	**21,364**	**468,949**	**3,862**	**543,989**
Government	**-**	**111,013**	**32,073**	**323,435**	**-**	**401,853**
	50,893	**1,110,606**	**53,437**	**1,149,153**	**3,862**	**945,914**
2012						
Personal	-	402,445	-	309,202	-	641
Corporate	102,829	452,877	13,007	391,508	59,709	548,800
Government	-	111,013	27,860	330,434	-	505,131
	102,829	966,335	40,867	1,031,144	59,709	1,054,572

39. Segment information

The Bank mainly operates in only one geographical location, the Sultanate of Oman. The Bank has however earned interest income and incurred interest expenses on account of money market placements and borrowings with banks outside the Sultanate of Oman as of 31 December 2013. The information regarding the bank's due from banks and due to banks based on the geographical locations for the years ended 31 December 2013 and 2012 is set out in note 37.

For management purposes, the conventional operations of the Bank is organised into four operating segments based on products and services. The Islamic banking services is offered under the brand name – "Al Yusr". The operating segments are as follows:

Retail banking	Individual personal loan, overdraft, credit card and funds transfer facilities.
Corporate banking	Loans and other credit facilities for corporate and institutional customers.
Investment banking	Asset management services involving investment products and services to institutional investors and intermediaries and other investment banking services including corporate finance, merger and acquisitions advice, specialised financial advice and trading.
Support and unallocated functions	Treasury and other central functions.
Islamic Banking	Sharia' compliant Islamic banking products and services including Ijarah, Murabaha, Mudarbah and Diminishing Musharakah.

Management monitors the operating results of its business units separately for the purpose of making decisions about resource allocation and performance assessment. Segment performance is evaluated based on operating profit or loss which in certain respects is measured differently from operating profit or loss in the financial statements. The costs incurred by the central functions are managed on a group basis and are not allocated to operating segments.

Notes to the financial statements
for the year ended 31 December 2013 (continued)

39. Segment information (continued)

Cash and balances with Central Bank of Oman, Certificate of deposits, due from banks, property and equipment and other assets are unallocated assets. No revenue from transactions with a single external customer or counterparty amounted to 10% or more of the Bank's total revenue in 2013 or 2012.

	Conventional banking					
2013	**Retail banking RO'000**	**Corporate banking RO'000**	**Investment banking RO'000**	**Support and unallocated functions RO'000**	**Al-Yusr RO'000**	**Total RO'000**
Interest income	**28,146**	**24,548**	**-**	**916**	**-**	**53,610**
Interest expense	**(1,494)**	**(6,323)**	**-**	**(3,341)**	**-**	**(11,158)**
Other operating income	**7,716**	**4,443**	**4,607**	**4,587**	**23**	**21,376**
Total operating income	**34,368**	**22,669**	**4,607**	**2,162**	**23**	**63,828**
Assets	**413,243**	**659,388**	**35,273**	**338,992**	**9,459**	**1,456,355**
Liabilities	**356,713**	**792,384**	**35,273**	**71,466**	**1,767**	**1,257,603**
Allowance for impairment	**14,350**	**19,902**	**-**	**-**	**46**	**34,315**
2012						
Interest income	28,434	21,284	-	798	-	50,516
Interest expense	(1,430)	(5,607)	-	(2,512)	-	(9,549)
Other operating income	8,812	4,031	2,714	4,304	-	19,861
Total operating income	35,816	19,708	2,714	2,590	-	60,828
Assets	389,075	545,739	20,994	414,601	-	1,370,409
Liabilities	309,202	721,942	20,994	134,160	-	1,186,298
Allowance for impairment	13,370	18,151	-	-	-	31,521

40. Fiduciary activities

The Bank's fiduciary activities consist of investment management activities conducted as trustee and manager for investment funds and individuals. The aggregate amount of funds managed, which are not included in the Bank's statement of financial position, are as follows:

	2013 RO'000	2012 RO'000
Funds under management	**324,163**	236,848

BASEL II PILLAR 3
AND
BASEL III DISCLOSURE REPORT

Deloitte.

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Report of factual findings to the Board of Directors of Oman Arab Bank SAOC in respect of Basel II – Pillar III Disclosures

We have performed the procedures agreed with you and as prescribed in the Central Bank of Oman ("CBO") Circular No BM 1027 dated December 4, 2007 with respect to the Bases II – Pillar III disclosures ("the disclosures") of the **Oman Arab Bank SAOC** ("the Bank") set out on pages 1 to 12 as at and for the year ended December 31, 2013. The disclosures were prepared by the management in accordance with the CBO's Circular No. BM 1009 dated September 13, 2006 and Circular No. BM 1027 dated December 4, 2007. Our engagement was undertaken in accordance with the International Standard on Related Services applicable to agreed-upon procedures engagements. The procedures, as set out in Circular No. BM 1027 dated December 4, 2007, were performed solely to assist you in evaluating the bank's compliance with the disclosure requirements set out in CBO's Circular number BM 1009 dated September 13, 2006.

We report our findings as follows:

Based on performance of the procedures detailed above, we found the disclosures free from any material misrepresentation.

Because the above procedures do not constitute either an audit or a review made in accordance with International Standards on Auditing or International Standards of Review Engagements, we do not express any assurance on the disclosers.

Had we performed additional procedures or had we performed an audit or review of the financial statements in accordance with International Standards on Auditing or International Standards on Review Engagements, other matters might have come to our attention that would have been reported to you.

Our report is solely for the purpose set forth in the first paragraph of this report and for your information and is not to be used for any other purpose or to be distributed to any other parties other than Central Bank of Oman. This report relates only to the bank's disclosures and does not extend to any financial statements of the Bank taken as a whole or to any other reports of the Bank.

Deloitte & Touche

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Sultanate of Oman
Deloitte & Touche (M.E.) & Co. LLC

Deloitte & Touche (M.E.) & Co. LLC
Muscat, Sultanate of Oman
30 January 2014

BASEL II PILLAR 3 DISCLOSURE
SCOPE OF APPLICATION

Oman Arab Bank SAOC (the Bank) was incorporated in the Sultanate of Oman on 1 October 1984 as a closed joint stock company. The Bank is a subsidiary of Oman International Investment and Development Company SAOG (OMINVEST) which owns 51% of the shares and the remaining 49% is owned by Arab Bank Plc, Jordan.

The Bank's objectives of capital management are:

- to comply with the capital requirements set by the regulator i.e. the Central Bank of Oman(CBO) ;
- to safeguard the Bank's ability to continue as a going concern while providing adequate returns to the shareholders; and
- to maintain a strong capital base to support the development of its business.

The Bank complies with CBO's requirements for the capital adequacy as specified in the Circular provided for the implementation of the Basel II accord. Basel II (the New Accord) consists of three mutually reinforcing Pillars - Minimum Capital Requirements (First Pillar), Supervisory Review Process (Second Pillar) and Market Discipline (Third Pillar). Under the First Pillar, the new framework offers three distinct options, for computing capital requirements for credit and operational risks, respectively. The approaches for credit risk (Standardized, Internal Ratings-Based –Foundation and Advanced) and operational risk (Basic Indicator, Standardized and Advanced measurement) are based on increasing risk sensitivity and allow banks to choose any of the approaches that are most appropriate to their risk management practices.

B. CAPITAL STRUCTURE

The Bank's Tier 1 and Tier 2 capital are as follows:

	RO '000
Paid up share capital	116,000
Legal reserves	27,627
General reserves	20,819
Subordinated Debt reserve	20,000
Retained earnings/(losses) of previous years	1,342
Tier 1 Capital	**185,788**
Collective impairment provisions for loan losses on portfolio basis	14,641
Cumulative fair value gains on investments available-for-sale	614
Subordinated term debt	30,000
Tier 2 Capital	**45,255**
Total Capital	**231,043**

Tier 1 Capital

The Bank's authorised and issued share capital comprises 200,000,000 fully paid shares of RO 0.100 each. In accordance with Article 106 of the Omani Commercial Companies Law of 1974, the Bank is required to transfer 10% of its profit after tax for the year to the legal reserve until the accumulated balance of the reserve equals at least one third of the Bank’s paid up share capital. General reserves have been created out of the Bank's retained earnings to meet any unforeseen contingency.

The subordinated debt reserve has been created by a transfer of 20% of the subordinated bonds out of the profit after tax for the year. The Central Bank of Oman requires that a reserve be set aside annually for the subordinated bonds which are due to mature within five years. The reserve is available for transfer back to retained earnings upon maturity of the subordinated bonds.

BASEL II PILLAR 3 DISCLOSURE (CONTINUED)

B. CAPITAL STRUCTURE (continued)

Tier 2 Capital

Tier 2 Capital consists of the Subordinated Bonds, provision for loan impairment on collective portfolio basis as required by the CBO and cumulative fair value gains on investments available for sale as allowed under the guidelines for Basel II by CBO.

In April 2012 the Bank issued non-convertible unsecured subordinated bonds ("the bonds") of RO 50 Million (50,000,000 units of RO 1 each) for a tenor of five years and one month in April 2012 through private placement in order to enhance the capital adequacy and to meet the funding requirements, The bonds are listed in the Muscat Securities Market and are transferable through trading. The bonds carry a fixed coupon rate payable semi-annually with the principal payable on maturity.

The provisions are made for the loan impairment on the performing portion of the loans and advances against the losses incurred but not identified.

C. CAPITAL ADEQUACY

Qualitative disclosures

Basel II provides a range of options for determining the regulatory capital requirements for credit and operational risks. It allows the banks and the supervisors to select approaches that seem most appropriate for the level of sophistication of the banks' activities, financial market infrastructure and risk management practices.

The Bank has chosen the following approaches for determining the regulatory capital with the approval of Central Bank of Oman:

i. Standardized Approach for the credit risk with a simplified approach for the risk weighting of collaterals under the credit risk mitigation and
ii. Basic Indicator approach for the operational risk.

The Bank's Board of Directors reviews the capital requirements based on the strategic plan of the Bank. This is reviewed periodically based on the current market and economic conditions. While formulating the Bank's strategic plans, the Bank's management takes into account forward-looking factors such as changes in the economic conditions, market and liquidity conditions. The Bank's current and future capital requirements are calculated in relation to its strategic business objectives. The strategic plan delineates the Bank's short-term and long-term capital needs, capital expenditures required for the foreseeable future, target capital levels, and capital sources. The Bank prepares its capital planning and operational budgeting on an annual basis.

Management considers that the Bank has adequate systems for monitoring and reporting risk exposures. The capital needs are assessed based on changes in the Bank's risk profile. The Board of Directors and the senior management receive regular reports or updates on the Bank's risk profile and capital needs through the Assets and Liabilities Committee (ALCO), Management Credit Committee (MCC) and directly from the Risk Management Department. This information is used to:

a. evaluate the level and trend of material risks and their effect on capital requirements;
b. evaluate the sensitivity and reasonableness of the main assumptions used in the capital measurement system;
c. determine that the Bank holds sufficient capital against various risks;
d. determine that the Bank meets its internal capital adequacy goals; and
e. assess its future capital requirements based on the Bank's reported risk profile and in turn make necessary adjustments to the Bank's strategic plan.

The Management is in the process of setting the policies and procedures to progressively move to the advanced approaches set out in Basel II for the capital measurement.

BASEL II PILLAR 3 DISCLOSURE (CONTINUED)

Quantitative disclosure

Table-1
2013

Sl. No	Details	Gross Balance	Net Balance	Risk Weighted Assets
		(Book Value)	(Book Value)	
		RO'000	RO'000	RO'000
1	On -Balance sheet Item	1,491,670	1,468,211	1,028,486
2	Off -Balance sheet Item	946,684	355,939	242,569
3	Assets for Operations risk	112,025	112,025	112,025
4	Assets in Trading book	7,713	7,713	7,713
5	Derivatives	21,459	21,459	8,058
6	**Total**	**2,579,551**	**1,965,347**	**1,398,851**
7	Tier 1 Capital			185,789
8	Tier 2 Capital			45,255
9	Tier 3 Capital			-
10	**Total Regulatory Capital**			**231,044**
10.1	Capital requirement for credit risk			153,494
10.2	Capital requirement for market risk			926
10.3	Capital requirement for operational risk			13,443
11	**Total required capital**			**167,863**
12	**Tier 1 Ratio**			**13.28%**
13	**Total Capital Ratio**			**16.52%**

2012

Sl. No	Details	Gross Balance	Net Balance	Risk Weighted Assets
		(Book Value)	(Book Value)	
		RO'000	RO'000	RO'000
1	On -Balance sheet Item	1,401,929	1,381,141	955,157
2	Off -Balance sheet Item	1,062,660	397,275	260,344
3	Assets for Operational risk	104,838	104,838	104,838
4	Assets in Trading book	7,950	7,950	7,950
5	Derivatives	11,400	11,400	6,874
6	**Total**	**2,588,777**	**1,902,604**	**1,335,163**
7	Tier 1 Capital			172,365
8	Tier 2 Capital			53,435
9	Tier 3 Capital			-
10	**Total Regulatory Capital**			**225,800**
10.1	Capital requirement for credit risk			146,685
10.2	Capital requirement for market risk			954
10.3	Capital requirement for operational risk			12,581
11	**Total required capital**			**160,220**
12	**Tier 1 Ratio**			**12.91%**
13	**Total Capital Ratio**			**16.91%**

BASEL II PILLAR 3 DISCLOSURE (CONTINUED)

D. CREDIT RISK EXPOSURE AND ASSESSMENT

i. General disclosure

Qualitative disclosures

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. Credit exposures arise principally from lending activities, investment activities and other assets in the Bank's asset portfolio. There is also credit risk in off-balance sheet financial instruments, such as loan commitments and financial guarantees.

The Bank attempts to control credit risk by monitoring credit exposures, limiting transactions with specific counterparties, and continually assessing the creditworthiness of counterparties. Concentrations of credit risk arise when a number of counterparties are engaged in similar business activities, or have similar economic features that would cause their ability to meet contractual obligations to be similarly affected by changes in economic, political or other conditions. Concentrations of credit risk indicate the relative sensitivity of the Bank's performance to developments affecting a particular industry or geographic location.

Credit Risk Management and Control

The credit risk management and control are centralised in the credit risk management team which is divided into corporate, financial institutions and retail groups. The credit risk in corporate and financial institutions portfolio is primarily managed by the Credit Department while the Retail Banking Department manages the credit risk in the retail portfolio. The Risk Management Department reviews the credit risk independently and directly reports to the Audit and Risk Management Committee of the Board of Directors. The Bank's assessment of probability of default of individual counterparties is mainly linked with the number of days the borrower was in default as defined by the CBO circular number BM 977 dated 25 September 2004. In addition, the Bank assesses the adequacy of the security and financial performance of the borrowers in further downgrading the classification. The Bank's clients are segmented into the following five rating classes:

Bank's Rating	Past due days Retail loans	 Commercial loans
Standard loans	0-60 days	0-60 days
Special mention loan	60-90 days	60-90 days
Substandard loan	90-180 days	90-270 days
Doubtful loans	180-365 days	270-630 days
Loss	365 days and over	630 days and over

The Bank manages, limits and controls concentrations of credit risk − in particular, to individual counterparties and groups, and to industries and countries. The Bank structures the levels of credit risk it undertakes by placing limits on the amount of risk accepted in relation to one borrower, or groups of borrowers, and to geographical and industry segments. Such risks are monitored and reviewed periodically by the Management Credit Committee, Audit and Risk Management committee of the Board of Directors and the Executive Committee of the Board of Directors.

The exposure to any one borrower including banks and brokers is further restricted by sub-limits covering on- and off-balance sheet exposures. Exposure to credit risk is also managed through regular analysis of the ability of borrowers and potential borrowers to meet interest and capital repayment obligations and by changing these lending limits where appropriate.

Commitments to extend credit represent unused portions of authorisations to extend credit in the form of loans, guarantees or letters of credit. With respect to credit risk on commitments to extend credit, the Bank is potentially exposed to loss in an amount equal to the total unused commitments. However, the likely amount of loss is less than the total unused commitments, as most commitments to extend credit are contingent upon customers maintaining specific credit standards. The Bank monitors the term to maturity of credit commitments because longer-term commitments generally have a greater degree of credit risk than shorter-term commitments.

BASEL II PILLAR 3 DISCLOSURE (CONTINUED)

Credit Risk Management and Control (continued)

Impairment provisioning

Impairment provisions are recognised for financial reporting purposes only for losses that have been incurred at the reporting date based on objective evidence of impairment. Objective evidence that a financial asset or group of assets is impaired includes observable data that comes to the attention of the Bank about the loss events such as delays in repayment of contracted amounts by counterparties as well as considering the guidelines issued by the CBO.

The Bank's credit policy requires the review of individual financial assets on a quarterly basis or earlier when individual circumstances require. Impairment allowances on individually assessed accounts are determined by an evaluation of the incurred loss at the reporting date on a case-by-case basis, and are applied to all individually significant accounts. The assessment normally encompasses collateral held (including re-confirmation of its enforceability) and the anticipated receipts for that individual account.

Collectively assessed impairment allowances are provided for: (i) portfolios of homogenous assets that are individually not significant; and (ii) losses that have been incurred but have not yet been identified, by using the available historical experience, experienced judgment and peer statistics.

Quantitative disclosure

ii. Gross credit risk exposures

Table-2

Sl. No	Type of credit exposure	Average Gross Exposure		Total Gross Exposure as at	
		2013	2012	31-Dec-13	31-Dec-12
		RO'000	RO'000	RO'000	RO'000
1	Overdrafts	115,981	98,282	111,291	96,497
2	Personal Loans	416,967	388,848	428,427	402,445
3	Loans against Trust Receipts	28,057	27,082	28,252	29,226
4	Other Loans	499,683	403,224	521,317	419,284
5	Bills Purchased Discounted	4,130	16,342	21,319	18,883
	Total	**1,064,818**	**933,778**	**1,110,606**	**966,335**

BASEL II PILLAR 3 DISCLOSURE (CONTINUED)

iii. Geographic distribution of exposures

Table-3

2013

Sl. No	Type of credit exposure	Oman RO'000	Other GCC countries RO'000	OECD countries RO'000	India RO'000	Pakistan RO'000	Others RO'000	Total RO'000
1	Overdrafts	111,291	-	-	-	-	-	111,291
2	Personal Loans	428,427	-	-	-	-	-	428,427
3	Loans against Trust Receipts	28,252	-	-	-	-	-	28,252
4	Other Loans	521,317	-	-	-	-	-	521,317
5	Bills Purchased/Discounted	21,319	-	-	-	-	-	21,319
	Total	**1,110,606**	-	-	-	-	-	**1,110,606**

2012

Sl. No	Type of credit exposure	Oman RO'000	Other GCC countries RO'000	OECD countries RO'000	India RO'000	Pakistan RO'000	Others RO'000	Total RO'000
1	Overdrafts	96,497	-	-	-	-	-	96,497
2	Personal loans	402,445	-	-	-	-	-	402,445
3	Loans against trust receipts	29,226	-	-	-	-	-	29,226
4	Other loans	419,284	-	-	-	-	-	419,284
5	Bills purchased discounted	18,883	-	-	-	-	-	18,883
	Total	**966,335**	-	-	-	-	-	**966,335**

BASEL II PILLAR 3 DISCLOSURE (CONTINUED)

iv. Industry or counterparty type distribution of exposures

Table-4

2013

Sl. No	Economic Sector	Overdraft RO'000	Loans RO'000	Bills Purchased/discounted RO'000	Others RO'000	Total RO'000	Off-balance sheet exposure RO'000
1	Import trade	13,343	17,220	1,594	-	32,157	62,740
2	Export trade	189	272	23	-	484	399,213
3	Wholesale & retail trade	9,648	23,158	1,446	-	34,252	10,764
4	Mining & quarrying	707	14,328	29	-	15,064	-
5	Construction	50,653	46,312	8,525	-	105,490	264,317
6	Manufacturing	11,536	96,137	2,859	-	110,532	7,177
7	Electricity, gas and water	154	43,436	659	-	44,249	46,941
8	Transport and communication	656	138,948	68	-	139,672	49,323
9	Financial institutions	1,986	26,900	66	-	28,952	-
10	Services	8,759	22,630	2,618	-	34,007	11,406
11	Personal loans	-	428,427	-	-	428,427	-
12	Agriculture and allied activities	287	4,073	411	-	4,771	-
13	Government	-	-	-	-	-	94,033
14	Non-resident lending	-	47	-	-	47	-
15	All others	13,373	116,108	3,021	-	132,502	-
16	**Total (1 to 15)**	**111,291**	**977,996**	**21,319**	**-**	**1,110,606**	**945,914**

2012

Sl. No	Economic Sector	Overdraft RO'000	Loans RO'000	Bills Purchased/ discounted RO'000	Others RO'000	Total RO'000	Off-balance sheet exposure RO'000
1	Import trade	12,434	20,048	1,067	-	33,549	48,270
2	Export trade	108	583	118	-	809	505,131
3	Wholesale & retail trade	7,281	13,388	567	-	21,236	11,277
4	Mining & quarrying	1,632	15,589	60	-	17,281	-
5	Construction	32,069	38,484	6,312	-	76,865	264,433
6	Manufacturing	18,216	84,959	3,722	-	106,897	7,447
7	Electricity, gas and water	322	38,369	500	-	39,191	24,452
8	Transport and communication	2,744	118,744	205	-	121,693	72,292
9	Financial institutions	844	20,737	307	-	21,888	-
10	Services	13,582	28,752	2,700	-	45,034	12,422
11	Personal loans	-	402,396	-	-	402,396	-
12	Agriculture and allied activities	4,806	3,677	433	-	8,916	-
13	Government	-	-	-	-	-	108,848
14	Non-resident lending	-	93	-	-	93	-
15	All others	2,459	65,136	2,892	-	70,487	-
16	**Total (1 to 15)**	**96,497**	**850,955**	**18,883**	**-**	**966,335**	**1,054,572**

BASEL II PILLAR 3 DISCLOSURE (CONTINUED)

v. Residual contractual maturity of credit exposure

Table-5

2013

Sl. No	Time Band	Overdraft RO'000	Loans RO'000	Bills Purchased/ discounted RO'000	Others RO'000	Total RO'000	Off-balance sheet exposure RO'000
1	Up to 1 month	5,565	62,765	8,188	-	76,518	122,436
2	1-3 months	5,565	97,538	11,629	-	114,732	477,274
3	3-6 months	5,565	43,407	838	-	49,810	79,040
4	6-9 months	5,565	40,426	272	-	46,263	35,696
5	9-12 months	5,565	78,575	53	-	84,193	26,879
6	1-3 years	27,822	147,358	339	-	175,519	203,613
7	3-5 years	27,822	69,889	-	-	97,711	918
8	Over 5 years	27,822	438,038	-	-	465,860	59
9	**Total**	**111,291**	**977,996**	**21,319**	**-**	**1,110,606**	**945,915**

2012

Sl. No	Time Band	Overdraft RO'000	Loans RO'000	Bills Purchased/ discounted RO'000	Others RO'000	Total RO'000	Off-balance sheet exposure RO'000
1	Up to 1 month	4,825	21,088	4,382	-	30,295	139,450
2	1-3 months	4,825	144,556	13,749	-	163,130	551,746
3	3-6 months	4,825	39,579	308	-	44,712	62,664
4	6-9 months	4,825	16,749	189	-	21,763	29,319
5	9-12 months	4,825	36,826	231	-	41,879	40,053
6	1-3 years	24,124	121,046	22	-	145,192	187,237
7	3-5 years	24,124	69,272	2	-	93,398	44,103
8	Over 5 years	24,124	401,842	-	-	425,966	-
9	Total	**96,497**	**850,955**	**18,883**	**-**	**966,335**	**1,054,572**

BASEL II PILLAR 3 DISCLOSURE (CONTINUED)

vi. Loans and provisions by major industry or counterparty type

Table-6

2013

SI. No.	Economic Sector	Gross loans RO'000	Of which NPLs RO'000	Collective impairment provision held RO'000	Specific provision held RO'000	Unrecognized contractual interest RO'000	Provisions made during the year(*) RO'000	Advances written off during the year RO'000
1	Import trade	32,157	3,361	288	955	1,528	312	2
2	Export trade	484	61	4	12	12	6	-
3	Wholesale & retail trade	34,252	670	336	212	422	90	-
4	Mining & quarrying	15,064	-	151	-	-	28	-
5	Construction	105,490	3,455	1,020	1,423	562	315	445
6	Manufacturing	110,532	13,289	686	4,472	1,524	524	-
7	Electricity, gas and water	44,249	-	443	-	-	83	-
8	Transport and communication	139,672	200	1,395	70	33	296	-
9	Financial institutions	28,952	302	287	110	63	69	-
10	Services	34,007	3,980	300	674	781	277	34
11	Personal loans	428,427	9,820	8,372	4,089	1,825	2,598	133
12	Agriculture and allied activities	4,771	252	45	46	43	22	-
13	Government	-	-	-	-	-	-	-
14	Non-resident lending	47	-	1	-	-	-	-
15	All others	132,502	1,223	1,314	614	204	1,731	48
16	**Total**	**1,110,606**	**36,613**	**14,641**	**12,677**	**6,997**	**6,351**	**662**

*** -** The provision shown under this column represents the specific provision made during the year. The collective provisions are made on a portfolio basis.

BASEL II PILLAR 3 DISCLOSURE (CONTINUED)

vi. Loans and provisions by major industry or counterparty type

Table-6 (continued)

2012

SI. No.	Economic Sector	Gross loans RO'000	Of which NPLs RO'000	Collective impairment provision held RO'000	Specific provision held RO'000	Unrecognized contractual interest RO'000	Provisions made during the year(*) RO'000	Advances written off during the year RO'000
1	Import trade	33,549	2,357	312	899	1,286	56	-
2	Export trade	809	90	7	19	16	-	-
3	Wholesale & retail trade	21,236	652	206	211	406	62	11
4	Mining & quarrying	17,281	-	173	-	-	-	-
5	Construction	76,865	4,287	726	1,582	1,139	233	55
6	Manufacturing	106,897	5,026	1,054	3,684	1,193	1,650	11
7	Electricity, gas and water	39,191	-	393	-	-	-	-
8	Transport and communication	121,693	65	1,216	39	25	106	-
9	Financial institutions	21,888	287	216	110	47	2	-
10	Services	45,034	3,380	417	935	610	473	-
11	Personal loans	402,396	9,459	7,859	3,642	1,832	1,411	20
12	Agriculture and allied activities	8,916	67	88	30	37	-	-
13	Government	-	-	-	-	-	-	-
14	Non-resident lending	93	-	1	-	-	-	-
15	All others	70,487	417	701	257	153	51	466
16	**Total**	**966,335**	**26,087**	**13,369**	**11,408**	**6,744**	**4,044**	**563**

*** -** The provision shown under this column represents the specific provision made during the year. The collective provisions are made on a portfolio basis.

BASEL II PILLAR 3 DISCLOSURE (CONTINUED)

vii. Geographic distribution of impaired loans

Table-7

2013

SI. No	Countries	Gross Loans RO'000	Of which NPLs RO'000	Collective impairment provision held RO'000	Specific Provision Held RO'000	Unrecognized contractual interest RO'000	Provisions made during the year (*) RO'000	Advances written off during the year RO'000
1	Oman	1,110,606	36,613	14,641	12,677	6,997	6,351	276
2	Other GCC countries	-	-	-	-	-	-	-
3	OECD countries	-	-	-	-	-	-	-
4	India	-	-	-	-	-	-	-
5	Pakistan	-	-	-	-	-	-	-
6	Others	-	-	-	-	-	-	-
7	**Total**	1,110,606	36,613	14,641	12,677	6,997	6,351	276

2012

SI. No	Countries	Gross Loans RO'000	Of which NPLs RO'000	Collective impairment provision held RO'000	Specific Provision Held RO'000	Unrecognized contractual interest RO'000	Provisions made during the year (*) RO'000	Advances written off during the year RO'000
1	Oman	966,335	26,087	13,369	11,408	6,744	5,727	565
2	Other GCC countries	-	-	-	-	-	-	-
3	OECD countries	-	-	-	-	-	-	-
4	India	-	-	-	-	-	-	-
5	Pakistan	-	-	-	-	-	-	-
6	Others	-	-	-	-	-	-	-
7	**Total**	966,335	26,087	13,369	11,408	6,744	5,727	565

* - includes the specific provisions and general provisions net of recoveries

BASEL II PILLAR 3 DISCLOSURE (CONTINUED)

viii. Movement in gross loans

Table-8

Movement of Gross Loans during the year - 2013

Sl. No	Details	Performing loans		Non-performing loans			
		Standard RO'000	Specially Mentioned RO'000	Sub-Standard RO'000	Doubtful RO'000	Loss RO'000	Total RO'000
1	Opening balance	**929,810**	**10,438**	**967**	**2,689**	**22,431**	**966,335**
2	Migration /changes (+/-)	**(20,050)**	**3,135**	**8,157**	**2,149**	**6,609**	**-**
3	New loans	**806,702**	**245**	**11**	**391**	**3,073**	**810,422**
4	Recovery of loans	**(649,823)**	**(6,461)**	**(2,869)**	**(2,201)**	**(4,089)**	**(665,443)**
5	Loans written off	**(1)**	**-**	**(1)**	**(11)**	**(693)**	**(708)**
6	Closing balance	**1,066,636**	**7,357**	**6,265**	**3,017**	**27,331**	**1,110,606**
7	Provisions held	**14,641**	**-**	**1,000**	**1,133**	**10,544**	**27,318**
8	Unrecognised contractual interest	**-**	**-**	**39**	**202**	**6,756**	**6,997**

Movement of Gross Loans during the year - 2012

Sl. No	Details	Performing loans		Non-performing loans			
		Standard RO'000	Specially Mentioned RO'000	Sub-Standard RO'000	Doubtful RO'000	Loss RO'000	Total RO'000
1	Opening balance	**823,079**	**9,475**	**1,388**	**4,469**	**18,589**	**857,000**
2	Migration /changes (+/-)	(10,325)	6,876	(205)	(1,424)	5,078	-
3	New loans	899,759	160	-	16	389	900,324
4	Recovery of loans	(782,699)	(6,073)	(213)	(361)	(765)	(790,111)
5	Loans written off	(4)	-	(3)	(11)	(860)	(878)
6	Closing balance	929,810	10,438	967	2,689	22,431	966,335
7	Provisions held	13,369	-	250	817	10,341	24,777
8	Unrecognised contractual interest	-	-	28	140	6,576	6,744

E. DISCLOSURE FOR PORTFOLIO SUBJECT TO STANDARDISED APPROACH

Qualitative disclosures

The Bank uses the ratings by Moody's Investor Services for the credit ratings for the purpose of determining the risk weight to be assigned to the exposure for on-balance sheet assets such as loans and advances and inter-bank exposure as well as off-balance sheet items such as Letters of Credit, Guarantees and forward contracts. In the absence of a rating by the Moodys' Investor Service, the Bank uses the ratings, if any, by Standard & Poors, Fitch Ratings or Capital Intelligence which are recognized by the Central Bank of Oman.

The claims on corporate are assigned 100% risk weight except for the claims with eligible financial collaterals and the Bank uses the simple approach for recognizing the collaterals in banking book with the approval of Central Bank of Oman. The Bank's retail loan portfolio is assigned a 100% risk weight except the loans secured by residential mortgage, which meet the conditions of CBO, for which risk weight assigned is 35%.

BASEL II PILLAR 3 DISCLOSURE (CONTINUED)

Quantitative Disclosure
The net exposure after risk mitigation subject to Standardized Approach is as follows:

Table-9

2013

Sl. No	Risk bucket	0% RO '000	20% RO' 000	35% RO' 000	50% RO' 000	100% RO' 000	Total RO' 000
1	Sovereigns(Rated)	242,210	-	-	-	-	242,210
2	Banks(Rated)	-	179,386	-	167,284	117,502	464,172
3	Corporate (Unrated)	-	41,212	-	-	527,508	568,720
4	Retail	-	-	-	-	351,279	351,279
5	Claims secured by residential property	-	-	37,537	-	29,595	67,132
6	Claims secured by commercial property	-	-	-	-	30,993	30,993
7	Past due loans	-	-	-	-	16,938	16,938
8	Other assets	24,279	-	-	-	79,116	103,395
9	Un drawn exposure	-	-	-	-	770	770
	Total	**266,489**	**220,598**	**37,537**	**167,284**	**1,153,701**	**1,845,609**

2012

Sl. No	Risk bucket	0% RO '000	20% RO' 000	35% RO' 000	50% RO' 000	100% RO' 000	Total RO' 000
1	Sovereigns(Rated)	294,196	-	-	0	-	294,196
2	Banks(Rated)	-	166,802	-	190,144	85,803	442,749
3	Corporate (Unrated)	-	25,483	-	0	509,203	534,686
4	Retail	-	-	-	-	337,669	337,669
5	Claims secured by residential property	-	-	-	-	55,317	55,317
6	Claims secured by commercial property	-	-	-	-	23,269	23,269
7	Past due loans	-	-	-	-	7,934	7,934
8	Other assets	23,194	0	-	-	62,713	85,907
9	Un drawn exposure	-	-	-	-	8,088	8,088
	Total	**317,390**	**192,285**	**-**	**190,144**	**1,089,996**	**1,789,815**

BASEL II PILLAR 3 DISCLOSURE (CONTINUED)

F. CREDIT RISK MITIGATION UNDER STANDARDISED APPROACH

Qualitative disclosures

Following are some of the specific credit risk mitigation measures employed by the Bank:

(a) Collateral

The Bank employs a range of policies and practices to mitigate credit risk. The most traditional of these is the taking of security for funds advanced, which is common practice. The Bank implements guidelines on the acceptability of specific classes of collateral or credit risk mitigation. The principal collateral types for loans and advances are:

- charges over business assets such as premises, inventory and accounts receivable;
- lien on fixed deposits;
- cash margins;
- mortgages over residential and commercial properties and
- pledge of marketable shares and securities;

Longer-term finance and lending to corporate entities are generally secured. The housing loans are secured by mortgage over the residential property. Credit cards and similar revolving credit facilities are unsecured. Additionally, in order to minimise the credit loss the Bank seeks additional collateral from the counterparty as soon as impairment indicators are noticed for the relevant individual loans and advances.

(b) Assessment of the financial capabilities of the borrowers

The borrowers with balances above the limit specified are subject to the review of their audited financial statements. The Bank assesses the financial performance of the borrowers by reviewing key performance ratios, including solvency and liquidity ratios. The annual reviews are performed by the relationship managers and are also reviewed by the Risk Management Department.

(c) Credit-related commitments

The primary purpose of these instruments is to ensure that funds are available to a customer as required. Guarantees and standby letters of credit carry the same credit risk as loans. Documentary and commercial letters of credit – which are written undertakings by the Bank on behalf of a customer authorising a third party to draw drafts on the Bank up to a stipulated amount under specific terms and conditions - are collateralised by the underlying shipments of goods to which they relate and therefore carry less risk than a direct loan.

Quantitative disclosure

	2013 RO '000	2012 RO '000
Total exposure covered by eligible financial collateral	**44,810**	**27,753**
Value of the eligible collateral	**42,568**	**27,491**

BASEL II PILLAR 3 DISCLOSURE (CONTINUED)

G. MARKET RISK IN TRADING BOOK

Qualitative disclosures

The Bank takes on exposures to market risk which is the risk that the fair value or the future cash flows of the financial assets carried at fair value will fluctuate because of changes in market prices. Market risks arise from the open positions in interest rate, currency and equity products, all of which are exposed to changes in interest rates, credit spreads, equity prices and foreign exchange rates. The market risks are monitored by the Treasury Division and the Risk Management Department. Management is confident that the Bank has proper risk management policies in place to ensure that interest risk, liquidity risk and foreign exchange risk are mitigated considering the macroeconomic indicators affecting the banking business.

The Bank manages its market risk in the trading book using tools such as position limits and stop loss limits.

Currency risk arises where the value of a financial instrument changes due to changes in foreign exchange rates. In order to manage currency risk exposure the Bank enters into ready, spot and forward transactions in the inter-bank market as per documented policies approved by the Board of Directors.

The Bank's foreign exchange exposure comprises of forward contracts, foreign currencies cash in hand, balances with banks abroad, foreign placements and other assets and liabilities denominated in foreign currency. The management manages the risk by monitoring net open position in line with limits set by the management and entering into forward contracts based on the underlying commercial transactions with the customers. Additionally, appropriate segregation of duties exist between the front and back office functions while compliance with the net open position is independently monitored on an ongoing basis by the management and the Assets and Liabilities Committee (ALCO).

Quantitative disclosure

The impact of 10% change in the market price of the quoted equities which are part of the investments held for trading at 31 December 2013 is ±0.29% of the total income (2012 – ± 0.28%).

H. INTEREST RATE RISK IN BANKING BOOK

Qualitative disclosures

Interest rate risk is the risk that the value of a financial instrument carried at fair value will fluctuate due to changes in the market interest rates. The Bank is exposed to interest rate risk as a result of mismatches or gaps in the amount of interest based assets and liabilities that mature or re-price in a given period. The Bank manages this risk by matching/re-pricing of assets and liabilities. The Bank is not excessively exposed to interest rate risk as substantial portion of its assets and liabilities are re-priced frequently. The Bank's Assets and Liabilities Committee (ALCO) monitors and manages the interest rate risk with the objective of limiting the potential adverse effects on the Bank's profitability.

For managing its interest rate risk in the banking book the Bank stipulates limits on open interest rate sensitive gaps for maturities up to 1 year and also periodically calculates Earnings at Risk (EaR) impact on its Net Interest Income (NII) from 100bps change in interest rates on open interest rate gaps for maturities up to 1 year. The EaR limit is stipulated as a certain percentage of the NII of the Bank for the previous year.

Quantitative disclosure

The EaR at 31 December 2013 is 1.57% (2012 – 1.41%).

BASEL II PILLAR 3 DISCLOSURE (CONTINUED)

H. INTEREST RATE RISK IN BANKING BOOK (continued)

The table below summarises the Bank's exposure to the interest rate risks. It includes the Bank's financial instruments at the carrying amount, categorised by the earlier of the contractual re-pricing and maturity dates.

2013	*Average effective interest rate %*	*Within 3 months RO'000*	*4 to 12 months RO'000*	*1 to 5 years RO'000*	*Over 5 years RO'000*	*Non-interest bearing RO'000*	*Total RO'000*
Assets							
Cash and balances with the Central Bank of Oman	1.50	-	-	-	500	116,439	116,939
Certificates of deposit	0.13	100,000	-	-	-	-	100,000
Due from banks	0.11	34,650	-	-	-	16,243	50,893
Loans and advances	5.06	201,107	225,778	631,161	4,558	3,687	1,076,291
Investment securities at fair value		-	-	-	-	21,364	21,364
Investment – held to maturity	2.76	-	2,400	27,673	2,000	-	32,073
Other assets		4,199	-	-	-	27,786	31,985
Property and equipment		-	-	-	-	26,810	26,810
Total assets		**339,956**	**228,178**	**658,834**	**17,058**	**212,329**	**1,456,355**
Liabilities							
Due to banks	-	-	-	-	-	3,862	3,862
Deposits from customers	0.94	397,372	180,175	57,694	-	513,912	1,149,153
Other liabilities		25,870	379	81	-	24,566	50,896
Subordinated bond	5.50		-	50,000	-	-	50,000
Taxation		-	-	-	-	3,692	3,692
Total liabilities		**423,242**	**180,554**	**107,775**	**-**	**546,032**	**1,257,603**
Total interest sensitivity gap		**(83,286)**	**47,624**	**551,059**	**17,058**	**(333,703)**	**198,752**
Cumulative interest sensitivity gap		**(83,286)**	**(35,662)**	**515,397**	**532,455**	**198,752**	

2012	*Average effective interest rate %*	*Within 3 months RO'000*	*4 to 12 months RO'000*	*1 to 5 years RO'000*	*Over 5 years RO'000*	*Non-interest bearing RO'000*	*Total RO'000*
Assets							
Cash and balances with the Central Bank of Oman	2.00	-	-	-	500	149,393	149,893
Certificates of deposit	0.08	90,000	-	-	-	-	90,000
Due from banks	0.23	82,775	-	-	-	20,054	102,829
Loans and advances	5.32	222,064	180,159	525,512	7,079	-	934,814
Investment securities at fair value		-	-	-	-	13,007	13,007
Investment – held to maturity	2.83	-	4,000	21,860	2,000	-	27,860
Other assets		4,689	-	-	-	25,538	30,227
Property and equipment		-	-	-	-	21,779	21,779
Total assets		**399,528**	**184,159**	**547,372**	**9,579**	**229,771**	**1,370,409**
Liabilities							
Due to banks	-	-	-	-	-	59,709	59,709
Deposits from customers	0.94	429,095	116,150	44,033	-	441,866	1,031,144
Other liabilities		24,938	531	182	-	15,944	41,595
Subordinated bond	5.50		-	50,000	-	-	50,000
Taxation		-	-	-	-	3,850	3,850
Total liabilities		**454,033**	**116,681**	**94,215**	**-**	**521,369**	**1,186,298**
Total interest sensitivity gap		**(54,505)**	**67,478**	**453,157**	**9,579**	**(291,589)**	**184,111**
Cumulative interest sensitivity gap		**(54,505)**	**12,973**	**466,130**	**475,709**	**184,111**	

BASEL II PILLAR 3 DISCLOSURE (CONTINUED)

I. LIQUIDITY RISK

Qualitative Disclosures

Liquidity risk is the risk that the Bank 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 close to its fair value. It includes the risk of being unable to fund assets at appropriate maturities and rates and the risk of being unable to liquidate an asset at a reasonable price and in an appropriate time frame.

The Bank's funding activities are based on a range of instruments including deposits, other liabilities and assigned capital. Consequently, funding flexibility is increased and dependence on any one source of funds is reduced. The Bank maintains liquidity by continually assessing, identifying and monitoring changes in funding needs required to meet strategic goals set in terms of the overall strategy. In addition the Bank holds certain liquid assets as part of its liquidity risk management strategy.

The Bank manages the liquidity risk based on estimated maturities using the guidelines provided by the Central Bank of Oman for the estimates. The table below represents cash flows receivable to and payable by the Bank under derivative and non-derivative assets and liabilities by estimated remaining maturities at the balance sheet date.

2013	*On demand or within 3 months RO'000*	*3 to 12 months RO'000*	*1 to 5 Years RO'000*	*Over 5 years RO'000*	*Total RO'000*
Assets					
Cash and balances with the Central Bank of Oman	58,170	26,682	15,542	16,545	116,939
Certificates of deposit	100,000	-	-	-	100,000
Due from banks	50,893	-	-	-	50,893
Loans and advances	191,251	175,348	273,231	436,461	1,076,291
Investment securities	21,356	2,400	27,681	2,000	53,437
Other assets	27,347	4,061	577	-	31,985
Property and equipment	-	-	-	26,810	26,810
Total assets	**449,017**	**208,491**	**317,031**	**481,816**	**1,456,355**
Liabilities					
Due to banks	3,862	-	-	-	3,862
Deposits from customers	420,398	250,980	272,703	205,072	1,149,153
Other liabilities	42,847	1,358	6,691	-	50,896
Subordinated bond	-	-	50,000	-	50,000
Taxation	3,419	273	-	-	3,692
Total liabilities	**470,526**	**252,611**	**329,394**	**205,072**	**1,257,603**
Net assets	**(21,509)**	**(44,120)**	**(12,363)**	**276,744**	**198,752**
Forward exchange contracts at notional amounts (note 32)	-	-	-	-	-
Purchase contracts	54,421	5,620	-	-	60,041
Sale contracts	(54,412)	(5,618)	-	-	(60,030)
	9	**2**	**-**	**-**	**11**

BASEL II PILLAR 3 DISCLOSURE (CONTINUED)
I. LIQUIDITY RISK (continued)

The Bank manages the liquidity risk based on estimated maturities using the guidelines provided by the Central Bank of Oman for the estimates. The table below represents cash flows receivable to and payable by the Bank under derivative and non derivative assets and liabilities by estimated remaining maturities at the balance sheet date.

2012	*On demand or within 3 months RO'000*	*3 to 12 months RO'000*	*1 to 5 Years RO'000*	*Over 5 years RO'000*	*Total RO'000*
Assets					
Cash and balances with the Central Bank of Oman	76,297	33,260	17,551	22,785	149,893
Certificates of deposit	90,000	-	-	-	90,000
Due from banks	102,829	-	-	-	102,829
Loans and advances	193,424	103,815	238,590	398,985	934,814
Investment securities	13,007	4,000	21,860	2,000	40,867
Other assets	21,881	8,011	335	-	30,227
Property and equipment	-	-	-	21,779	21,779
Total assets	**497,438**	**149,086**	**278,336**	**445,549**	**1,370,409**
Liabilities					
Due to banks	59,709	-	-	-	59,709
Deposits from customers	433,887	271,760	143,405	182,092	1,031,144
Other liabilities	32,728	5,865	3,002	-	41,595
Subordinated bond	-	-	50,000	-	50,000
Taxation	3,567	283	-	-	3,850
Total liabilities	**529,891**	**277,908**	**196,407**	**182,092**	**1,186,298**
Net assets	**(32,453)**	**(128,822)**	**81,929**	**263,457**	**184,111**
Forward exchange contracts at notional amounts (note 32)					
Purchase contracts	12,642	8,253			20,895
Sale contracts	(12,633)	(8,249)			(20,882)
	9	**4**	**-**	**-**	**13**

J. OPERATIONAL RISK

Qualitative Disclosures

The Bank is in the process of setting up the systems for collecting the data relating to operational risk. The measurement of the operational risk requires historical data for at least 3 years in order to perform the calculations.

Quantitative Disclosures

The Risk Weighted Assets for the operational risk using the Basic Indicator Approach is RO 112.025 million at December 31 2013 (2012: RO 104.84 million).

BASEL III DISCLOSURE

K. COMPOSITION OF CAPITAL DISCLOSURE

The Basel III regulations adopted by the CBO aims at strengthening the capital and liquidity standards of the banks in Oman. The elements of the Basel III regulations consist of

- Enhancing the definition of capital and strengthening the eligibility criteria for inclusion of capital instruments
- Raising the minimum capital requirements and introducing capital buffers for conservation and dealing with systemic risks in the form of Capital Conservation Buffer and Countercyclical Buffer
- Enhancing coverage of risk arising from derivatives, repos and securities financing
- Implementing the leverage ratio to control the build-up of leverage and mitigating the impact of excessive deleveraging
- Higher capital requirements for large and systemically important banks
- Implementing the Liquidity Coverage Ratio to ensure that the banks hold higher quality of liquid assets
- Implementing Net Stable Funding Ratio to ensure financing of activities with more stable source of funding

The requirements of Basel III will be gradually implemented starting from 2013 and the higher capital requirements would be implemented by 2015. The banks in Oman have to comply with the related disclosure requirements issued by CBO in the circular BM-1114 dated 16 November 2013.The transition period of phasing-in of regulatory adjustments of capital under Basel III in Oman would be from December 31, 2013 to December 31, 2017. During the transition period of phasing-in of regulatory deductions under Basel III the banks in Oman will use a modified version of disclosure of the components of capital.

A reconciliation of the Bank's Statement of Financial Position with the regulatory capital elements is provided as follows using the three step approach outlined by the Basel Committee:

Step 1: Disclosure of the reported statement of financial position under the regulatory scope of consolidation

This step involves disclosing how the balance sheet in the published financial statements changes when the regulatory scope of consolidation is applied. This disclosure is not made since there is no difference between the scope of regulatory and accounting consolidation.

Step 2: Expanding the lines of the regulatory statement of financial position to display all of the components used in the definition of capital disclosure template

The rows of the regulatory-scope statement of financial position have been expanded such that all of the components used in the composition of capital disclosure are displayed separately.

BASEL III DISCLOSURE (CONTINUED)

RECONCILIATION	Financial Position as in published financial statements As at Dec-31-2013 RO '000	Under regulatory scope of consolidation As at Dec-31-2013 RO '000	Reference
Assets			
Cash and balances with CBO	**116,939**	**116,939**	
Certificates of deposit	**100,000**	**100,000**	
Balance with banks and money at call and short notice	**50,893**	**50,893**	
Investments :	**53,437**	**53,437**	
Of which :			
Held to Maturity	32,073	32,073	
Available for Sale	19,320	19,320	
Held for Trading	2,044	2,044	
Loans and advances	**1,076,291**	**1,076,291**	
Of which :			
Loans and advances to domestic banks	-	-	
Loans and advances to non-resident banks	-	-	
Loans and advances to domestic customers	1,106,883	1,048,464	
Loans and advances to non-resident Customers for domestic operations	-	-	
Loans and advances to non-resident Customers for operations abroad	-	-	
Loans and advances to SMEs	-	58,419	
Financing from Islamic banking window	3,723	3,723	
Provision for loan impairment	(34,315)	(34,315)	
Of which :			
Specific provision	(19,674)	(19,674)	
Collective provision	(14,641)	(14,641)	a
Fixed assets	**26,810**	**26,810**	
Other assets	**31,985**	**31,985**	
Total Assets	**1,456,355**	**1,456,355**	

BASEL III DISCLOSURE (CONTINUED)

RECONCILIATION	Financial Position as in published financial statements As at Dec-31-2013 RO '000	Under regulatory scope of consolidation As at Dec-31-2013 RO '000	Reference
Capital & Liabilities			
Paid-up Capital	**116,000**	**116,000**	
Of which:			
Amount eligible for CET1	116,000	116,000	b
Amount eligible for AT1	-	-	
Reserves & Surplus	**82,752**	**82,752**	
Of which:			
Legal reserve	27,627	27,627	c
General reserve	20,819	20,819	d
Retained earnings	1,342	1,342	e
Proposed dividends	11,600	11,600	
Cumulative changes in fair value of investments	1,364	1,364	
Of which:			
Amount eligible for Tier 2 capital	1,364	614	f
Amount ineligible due to regulatory adjustment	-	750	
Subordinated debt reserve	20,000	20,000	g
Total Capital	**198,752**	**198,752**	

BASEL III DISCLOSURE (CONTINUED)

RECONCILIATION	Financial Position as in published financial statements As at Dec-31-2013 RO '000	Under regulatory scope of consolidation As at Dec-31-2013 RO '000	Reference
Deposits	**1,149,153**	**1,149,153**	
Of which:			
Deposits from banks	-	-	
Customer deposits	1,149,098	1,149,098	
Deposits of Islamic Banking window	55	55	
Borrowings	**53,862**	**53,862**	
Of which:			
From CBO	-	-	
From banks	3,862	3,862	
From other institutions & agencies	-	-	
Borrowings in the form of bonds,Debentures and sukuks	50,000	50,000	
Of which:			
Directly issued qualifying Tier 2 instruments	50,000	30,000	h
Amount de-recognised from Tier 2 capital	-	20,000	
Other liabilities & provisions	**54,588**	**54,588**	
Total Capital, Other liabilities & provisions	**1,456,355**	**1,456,355**	

BASEL III DISCLOSURE (CONTINUED)

Step 3: Mapping each of the components that are disclosed in Step 2 to the composition of capital disclosure

	Common Equity Tier 1 capital: instruments and reserves As at December 31 2013	**Under regulatory scope of consolidation RO '000**	**Reference**
1	Directly issued qualifying common share capital	116,000	b
2	Retained earnings	1,342	e
3	Accumulated other comprehensive income (and other reserves)	68,446	c + d + g
4	Directly issued capital subject to phase out from CET1 (only applicable to non-joint stock companies)		
5	Common share capital issued by subsidiaries and held by third parties (amount allowed in group CET1)		
6	**Common Equity Tier 1 capital (CET1)**	**185,788**	
7	**Additional Tier 1 capital (AT1)**	-	
8	**Tier 1 capital (T1 = CET1 + AT1)**	**185,788**	
	Tier 2 capital: instruments and provisions		
9	Directly issued qualifying Tier 2 instruments	30,000	h
10	Provisions	14,641	a
11	Amount of Cumulative changes in fair value of investments eligible for Tier 2 capital	614	f
12	**Tier 2 capital (T2)**	**45,255**	
	Total capital (TC = T1 + T2)	**231,043**	

BASEL III DISCLOSURE (CONTINUED)

The Bank issued unsecured subordinated bonds for OMR 50 Million through private placement on 10 April 2012. . The bonds are eligible for inclusion in Tier 2 capital under the Basel III regulations. The full terms and conditions of the bonds are available in the bank's website. The main features of the bonds are as follows:

1	Issuer	OMAN ARAB BANK
2	Unique identifier (eg CUSIP, ISIN or Bloomberg identifier for private placement)	-
3	Governing law(s) of the instrument *Regulatory treatment*	Oman Banking law
4	Transitional Basel III rules	Not eligible for inclusion in Tier -2 Capital
5	Post-transitional Basel III rules	Not eligible for inclusion in Tier -2 Capital
6	Eligible at solo/group/group & solo	Solo
7	Instrument type (types to be specified by each jurisdiction)	Bonds
8	Amount recognised in regulatory capital (Currency in mil, as of most recent reporting date)	OMR 30 Million
9	Par value of instrument	OMR 50 Million
10	Accounting classification	Subordinated Debt
11	Original date of issuance	10/04/2012
12	Perpetual or dated	Dated
13	Original maturity date	10/05/2017
14	Issuer call subject to prior supervisory approval	-
15	Optional call date, contingent call dates and redemption amount	-
16	Subsequent call dates, if applicable	-
	Coupons / dividends	
17	Fixed or floating dividend/coupon	Fixed coupon
18	Coupon rate and any related index	5.50%
19	Existence of a dividend stopper	-
20	Fully discretionary, partially discretionary or mandatory	-
21	Existence of step up or other incentive to redeem	-
22	Noncumulative or cumulative	Non-cumulative
23	Convertible or non-convertible	Non-convertible
24	If convertible, conversion trigger (s)	-
25	If convertible, fully or partially	-
26	If convertible, conversion rate	-
27	If convertible, mandatory or optional conversion	-
28	If convertible, specify instrument type convertible into	-
29	If convertible, specify issuer of instrument it converts into	-
30	Write-down feature	-
31	If write-down, write-down trigger(s)	-
32	If write-down, full or partial	-
33	If write-down, permanent or temporary	-
34	If temporary write-down, description of write-up mechanism	-
35	Position in subordination hierarchy in liquidation (specify instrument type immediately senior to instrument)	Subordinate to depositors and general creditors
36	Non-compliant transitioned features	-

BASEL III DISCLOSURE (CONTINUED)

The following table shows the composition of capital under Basel III :

		AMOUNTS SUBJECT TO PRE-BASEL III TREATMENT RO '000
Common Equity Tier 1 capital: instruments and reserves		
1	Directly issued qualifying common share capital (and equivalent for non-joint stock companies) plus related stock surplus	116,000
2	Retained earnings	1,342
3	Accumulated other comprehensive income (and other reserves)	68,446
4	Directly issued capital subject to phase out from CET1 (only applicable to non-joint stock companies)	-
	Public sector capital injections grandfathered until 1 January 2018	-
5	Common share capital issued by subsidiaries and held by third parties (amount allowed in group CET1)	-
6	**Common Equity Tier 1 capital before regulatory adjustments**	**185,788**
Common Equity Tier 1 capital: regulatory adjustments		
7	Prudential valuation adjustments	-
8	Goodwill (net of related tax liability)	-
9	Other intangibles other than mortgage-servicing rights (net of related tax liability)	-
10	Deferred tax assets that rely on future profitability excluding those arising from temporary differences (net of related tax liability)	-
11	Cash-flow hedge reserve	-
12	Shortfall of provisions to expected losses	-
13	Securitisation gain on sale (as set out in paragraph 14.9 of CP-1)	-
14	Gains and losses due to changes in own credit risk on fair valued liabilities.	-
15	Defined-benefit pension fund net assets	-
16	Investments in own shares (if not already netted off paid-in capital on reported balance sheet)	-
17	Reciprocal cross-holdings in common equity	-
18	Investments in the capital of banking, financial, insurance and takaful entities that are outside the scope of regulatory consolidation, net of eligible short positions, where the bank does not own more than 10% of the issued share capital (amount above 10% threshold)	-
19	Significant investments in the common stock of banking, financial, insurance and takaful entities that are outside the scope of regulatory consolidation, net of eligible short positions (amount above 10% threshold)	-

BASEL III DISCLOSURE (CONTINUED)

		AMOUNTS SUBJECT TO PRE-BASEL III TREATMENT RO '000
	Common Equity Tier 1 capital: instruments and reserves	
20	Mortgage Servicing rights (amount above 10% threshold)	-
21	Deferred tax assets arising from temporary differences (amount above 10% threshold, net of related tax liability)	-
22	Amount exceeding the 15% threshold	-
23	of which: significant investments in the common stock of financials	-
24	of which: mortgage servicing rights	-
25	of which: deferred tax assets arising from temporary differences	-
26	National specific regulatory adjustments	-
27	Regulatory adjustments applied to Common Equity Tier 1 in respect of amounts subject to Pre-Basel III Treatment	-
28	**Total regulatory adjustments to Common equity Tier 1**	**-**
29	**Common Equity Tier 1 capital (CET1)**	**185,788**
	Additional Tier 1 capital: instruments	
30	Directly issued qualifying Additional Tier 1 instruments plus related stock surplus	-
31	of which: classified as equity under applicable accounting standards	-
32	of which: classified as liabilities under applicable accounting standards	-
33	Directly issued capital instruments subject to phase out from Additional Tier 1	-
34	Additional Tier 1 instruments (and CET1 instruments not included in row 5) issued by subsidiaries and held by third parties (amount allowed in group AT1)	-
35	*of which: instruments issued by subsidiaries subject to phase out*	-
36	**Additional Tier 1 capital before regulatory adjustments**	**-**

BASEL III DISCLOSURE (CONTINUED)

		AMOUNTS SUBJECT TO PRE-BASEL III TREATMENT RO '000
Additional Tier 1 capital: regulatory adjustments		
37	Investments in own Additional Tier 1 instruments	-
38	Reciprocal cross-holdings in Additional Tier 1 instruments	-
39	Investments in the capital of banking, financial, insurance and takaful entities that are outside the scope of regulatory consolidation, net of eligible short positions, where the bank does not own more than 10% of the issued common share capital of the entity (amount above 10% threshold)	-
40	Significant investments in the capital of banking, financial, insurance and takaful entities that are outside the scope of regulatory consolidation (net of eligible short positions)	-
41	National specific regulatory adjustments	-
	REGULATORY ADJUSTMENTS APPLIED TO ADDITIONAL TIER 1 IN RESPECT OF AMOUNTS SUBJECT TO PRE-BASEL III TREATMENT	-
42	Regulatory adjustments applied to Additional Tier 1 due to insufficient Tier 2 to cover deductions	-
43	**Total regulatory adjustments to Additional Tier 1 capital**	-
44	**Additional Tier 1 capital (AT1)**	-
45	**Tier 1 capital (T1 = CET1 + AT1)**	**185,788**
Tier 2 capital: instruments and provisions		
46	Directly issued qualifying Tier 2 instruments plus related stock surplus	30,000
47	*Directly issued capital instruments subject to phase out from Tier 2*	-
48	Tier 2 instruments (and CET1 and AT1 instruments not included in rows 5 or 34) issued by subsidiaries and held by third parties (amount allowed in group Tier 2)	-
49	*of which: instruments issued by subsidiaries subject to phase out*	-
50	Provisions	14,641
51	**Tier 2 capital before regulatory adjustments**	**44,641**

BASEL III DISCLOSURE (CONTINUED)

		AMOUNTS SUBJECT TO PRE-BASEL III TREATMENT RO '000
	Tier 2 capital: regulatory adjustments	
52	Investments in own Tier 2 instruments	-
53	Reciprocal cross-holdings in Tier 2 instruments	-
54	Investments in the capital of banking, financial, insurance and takaful entities that are outside the scope of regulatory consolidation, net of eligible short positions, where the bank does not own more than 10% of the issued common share capital of the entity (amount above the 10% threshold)	-
55	Significant investments in the capital banking, financial, insurance and takaful entities that are outside the scope of regulatory consolidation (net of eligible short positions)	-
56	National specific regulatory adjustments	-
	REGULATORY ADJUSTMENTS APPLIED TO TIER 2 IN RESPECT OF AMOUNTS SUBJECT TO PRE-BASEL III TREATMENT.	614
	OF WHICH: Cumulative unrealised gains on available-for-sale financial instruments	614
57	**Total regulatory adjustments to Tier 2 capital**	**614**
58	**Tier 2 capital (T2)**	**45,255**
59	**Total capital (TC = T1 + T2)**	**231,043**

BASEL III DISCLOSURE (CONTINUED)

		AMOUNTS SUBJECT TO PRE-BASEL III TREATMENT RO '000
	RISK WEIGHTED ASSETS IN RESPECT OF AMOUNTS SUBJECT TO PRE-BASEL III TREATMENT	**1,398,851**
60	**Total risk weighted assets (60a+60b+60c)**	**1,398,851**
60a	*Of which: Credit risk weighted assets*	1,279,113
60b	*Of which: Market risk weighted assets*	7,713
60c	*Of which: Operational risk weighted assets*	112,025
	Capital Ratios	
61	Common Equity Tier 1 (as a percentage of risk weighted assets)	13.28%
62	Tier 1 (as a percentage of risk weighted assets)	13.28%
63	Total capital (as a percentage of risk weighted assets)	16.52%
64	Institution specific buffer requirement (minimum CET1 requirement plus capital conservation buffer plus countercyclical buffer requirements plus G-SIB/D-SIB buffer requirement expressed as a percentage of risk weighted assets)	0.00%
65	*of which: capital conservation buffer requirement*	-
66	*of which: bank specific countercyclical buffer requirement*	-
67	*of which: D-SIB/G-SIB buffer requirement*	-
68	Common Equity Tier 1 available to meet buffers (as a percentage of risk weighted assets)	-
National minima (if different from Basel III)		
69	National Common Equity Tier 1 minimum ratio (if different from Basel 3 minimum)	7.00%
70	National Tier 1 minimum ratio (if different from Basel 3 minimum)	9.00%
71	National total capital minimum ratio (if different from Basel 3 minimum)	12.00%
Amounts below the thresholds for deduction (before risk weighting)		
72	Non-significant investments in the capital of other financials	-
73	Significant investments in the common stock of financials	-
74	Mortgage servicing rights (net of related tax liability)	-
75	Deferred tax assets arising from temporary differences (net of related tax liability)	-
Applicable caps on the inclusion of provisions in Tier 2		
76	Provisions eligible for inclusion in Tier 2 in respect of exposures subject to standardised approach (prior to application of cap)	14,641
77	Cap on inclusion of provisions in Tier 2 under standardised approach	1.25%
78	Provisions eligible for inclusion in Tier 2 in respect of exposures subject to internal ratings-based approach (prior to application of cap)	-
79	Cap for inclusion of provisions in Tier 2 under internal ratings-based approach	-

BASEL III DISCLOSURE (CONTINUED)

		AMOUNTS SUBJECT TO PRE-BASEL III TREATMENT
	Capital instruments subject to phase-out arrangements (only applicable between 1 Jan 2018 and 1 Jan 2022)	
80	*Current cap on CET1* instruments *subject to phase out arrangements*	-
81	*Amount excluded from CET1 due to cap (excess over cap after redemptions and maturities)*	-
82	*Current cap on AT1 instruments subject to phase out arrangements*	-
83	*Amount excluded from AT1 due to cap (excess over cap after redemptions and maturities)*	-
84	*Current cap on T2 instruments subject to phase out arrangements*	-
85	*Amount excluded from T2 due to cap (excess over cap after redemptions and maturities)*	-