BANK SOHAR SAOG

FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2011

Registered office and principal place of business:

Bank Sohar Building
P.O. Box 44, Hai Al-Mina,
PC 114, Muscat
Sultanate of Oman

Bank Sohar SAOG

BOARD OF DIRECTORS' REPORT -2011

It is my privilege to present to you the report of Bank Sohar's financial performance for the year ended 31st December 2011.

2011 has been a significant year indeed for a number of reasons. On the macroeconomic front, Oman embarked on the 8th Five Year Plan, which has long served as an effective blueprint for the nation's continued modernisation and economic development.

The economy continued to hold up remarkably well despite the challenging global economic environment. The Sultanate also celebrated the 41st National Day anniversary, marking yet another milestone in the reign of His Majesty Sultan Qaboos bin Said, under whose enlightened leadership the Sultanate continues to march towards progress and prosperity.

The year has been equally notable for Bank Sohar as well. For one, the Sultanate's youngest bank will be completing five years of successful operations by April 2012 and remains well poised for robust growth in the future. Maintaining a trend in profitable operations spanning all four quarters of the financial year, Bank Sohar achieved a Net Profit of OMR 14.497 million, compared with a Net Profit of OMR 10.220 million during 2010.

The Board of Directors has recommended a cash dividend of 8 per cent for the year, which corresponds to Eight baizas per share. The Board of Directors has also recommended a rights issue to the tune of 10 million

Omani rial to its existing shareholders to be used as capital for the Islamic window to be created.

ECONOMY

A combination of prudent macroeconomic policies and stimulatory spending mechanisms continues to underpin Oman's economic growth, infrastructure development, and employment generation objectives. This commitment to growth is even more so evident in the 2012 budget with total expenditure rising 23% to about OMR 10 billion, against the original 2011 budget figures (or an increase of 8.7% against the amended budgeted level of OMR 9.2 billion in 2011).

Revenue receipts for the financial year are projected at OMR 8.8 billion, which represent a 20.8% increase in comparison with the original 2011 budget revenue of RO 7.28 billion. The lion's share will come from crude oil exports based on an assumed budgeted price of $75 per barrel (as opposed to $58 per barrel in the 2011 budget). The projected deficit of OMR 1.2 billion is expected to be met from surpluses of the previous years, as well as higher oil earnings.

Importantly, the 2012 budget aims to build on the government's successes in providing employment for citizens, Around 36,000 new jobs will be created in 2012, on top of the estimated 94,000 new openings already created in 2011.

Government spending during the Eighth Five Year Plan (2011 – 2015) is set to exceed OMR 54 billion, which represents a 26.4 per cent increase over the original projection of OMR 42.7 billion. Of this total, roughly

OMR 11 billion will go towards meeting the government's commitments with regard to job creation, improving living standards, and a host of other schemes such as pension, scholarship and social welfare schemes. Allocations towards key economic sectors, notably tourism, industry, agriculture and fisheries, are projected to grow in line with the government's economic diversification

strategies. Gross Domestic Product (GDP) growth is forecast at around 6 per cent annually at current prices, and 5 per cent at constant prices.

A key goal of the Eighth Plan is to ensure that inflation – a subject of keen focus for the Omani government – is brought within control and remains within acceptable limits. Inflation is currently within the 4% range, in trend with 2011 levels – the result of successful efforts by the government in reining in inflationary forces.

Commercial banks in the Sultanate continued to perform remarkably well during 2011 notching notable gains in all key areas of banking operations. The total assets of commercial banks rose 14.4 per cent to OMR 17.934 billion as of 30th November 2011, versus OMR 15.679 billion same period of 2010.

Underscoring the inherent strengths of the Omani banking sector, international ratings agency Moody's affirmed the outlook on the Sultanate's banks as "stable" in its review of the sector last November. Highlighting the banks' solid capitalization, stable funding bases, high liquidity buffers, low levels of non-performing loans. Moody's expectation of adequate earnings, despite higher operating costs.

FINANCIAL OVERVIEW 2011

We are glad to report that Bank Sohar has made a net profit of OMR 14.497 million for the year, which is 41.8 per cent higher than the previous year's net profit of OMR 10.220 million. The operating profit for the year was OMR 20.007 million as compared to OMR 15.645 million in 2010, an increase of 27.9 per cent. Net interest income during the year climbed 13.6 per cent to OMR 34.757 million, as compared to OMR 30.595 million in 2010. The operating income for the year 2011 increased to OMR 43.186 million, as compared to OMR 35.231 million in 2010, an increase of 22.60 per cent. The cost to income ratio stood at 53.67 per cent in 2011, down from 55.6 per cent in 2010.

Impressive gains were achieved in other areas of the Bank's business as well. Net loans and advances jumped 12.9 per cent during the year to touch OMR 1,020 million, against the previous year's level of OMR 903 million. Customer deposits grew 17.2 per cent to OMR 1,171 million during the year, as compared to OMR 999 million in 2010. The Bank's share of Private Sector Credit stood at 8.41 per cent till November 2011 as compared to 8.83 in December 2010 while the Bank's share of Private Sector Deposit was 6.73 per cent in November 2011, marginally up from 6.62 per cent at the end of 2010.

Bank Sohar's admirable financial performance during 2011 was the result of energetic and sustained efforts by the management and staff to build on the successes of the previous year, as well as to focus on all aspects of the Bank's business. These efforts were supplemented by a concerted drive to improve the overall quality of its assets, enhance yield growth, and reduce operating expenses.

Affirming its confidence in Bank Sohar's policies and growth strategy, leading international ratings agency Fitch assigned a Long Term Issuer Default Rating of BBB+ to the Bank in 2011. The positive rating recognizes the strength of the Bank's commercial franchise and its growing market presence in the Sultanate. It also acknowledges the Bank's very low non-performing loan ratio and its good provisioning coverage ratio. In essence, the BBB+ Rating attests to the excellent asset quality of the Bank and its prudent functioning. Most importantly, the rating underscores the robust confidence enjoyed by its retail and wholesale customers – a praiseworthy achievement indeed for a mere five-year old institution.

FUTURE PLANS

Bank Sohar is committed to pursuing vigorous growth in 2012, not only in terms of its market size but also in the diversity of financial products and services available to its growing customer base.

A key objective for this year is the introduction of Islamic Banking. Towards this goal, the Bank is putting in place frameworks, systems and procedures to facilitate the roll-out of shariah-compliant products and services. Competition in this emerging financial sector is expected to be fierce, given the widespread interest in Islamic Banking evinced by local commercial banks, but Bank Sohar is determined to be a key player in this business.

Further, in line with its efforts to expand its network and the reach of its services, Bank Sohar plans to open new branches and broaden its ATM infrastructure during the course of 2012. This investment is central to the Bank's strategy of being close to its customers.

In fact, several significant additions were made to Bank Sohar's network during 2011. A new branch was opened in Al Buraimi last June, marking Bank Sohar's debut in Buraimi Governorate. This was followed by the launch of three new branches in Ruwi, Al Amerat and Al Khabourah during the third quarter, thereby enhancing the Bank's ability to serve both retail and corporate clients. In tandem with this expansion, the Bank's Automated Teller Machine (ATM) was also upgraded to also offer Cash Deposit facilities, or through the installation of dedicated Cash Deposit machines at key locations. As of end-December 2011, Bank Sohar's network comprised of 25 branches and 44 ATMs.

As a responsible corporate citizen, and mindful of developments witnessed around the Sultanate in 2011, Bank Sohar made common cause with the government, as well as the private sector, in taking on more Omani nationals on its rolls. As a result of various recruitment and training initiatives, Bank Sohar has 549 staff on its rolls (as of 31st December 2011), with Omanisation pegged at an impressive 90.71 per cent.

Besides, the Bank responded positively to a number of changes and enhancements enacted by the concerned authorities with regard to various administrative, pension-related, and other systems. No doubt, these changes will contribute to the nation's socio-economic development and continued modernization. Bank Sohar gratefully appreciates and acknowledges His Majesty the Sultan’s guidance and wise directives in this regard.

CORPORATE GOVERNANCE

The Bank has included a comprehensive report on Corporate Governance duly certified by the statutory auditors within the Annual Report for the year 2011. This Report has been made in line with the directives provided for the same under the Code of Corporate Governance promulgated by the Capital Market Authority. In the Bank’s first Annual Report, we confirmed that the Bank will adhere to the best traditions of corporate governance and provide both disclosure and accountability. We have honored that assurance during the current year and will continue to do so. The Bank has also conducted an annual review on the effectiveness of the Bank’s system of internal control.

CORPORATE SOCIAL RESPONSIBILITY

Bank Sohar is distinguished by its active and innovative Corporate Social Responsibility Program. Through its steadfast support for various community welfare, health, education and employment initiatives, the Bank continues to make a difference to society.

Among the major events supported by the Bank in 2011 were the 13th Muscat Festival, 1st Regional Youth Ambassador Assembly for Road Safety, and Salalah Tourism Festival. Several educational institutions, sports clubs, and charitable organizations, amongst other entities, have also benefited from the Bank’s funding support during the year.

FOR THE RECORD

In concluding, I extend my heartfelt thanks to the Board of Directors, management, staff and stakeholders for their concerted and collective efforts in making our young institution a 'Bank with a difference' in the face of fairly formidable competition and other challenges. We owe our success in large measure to our growing family of customers whose confidence in our products and services serves as a beacon of inspiration for our continued growth.

We also commend the Central Bank of Oman and the Capital Market Authority for their excellent stewardship of the banking sector in Oman. Recognition is also due to the Government of His Majesty the Sultan for its farsighted, citizen-centric and business-friendly policies that have enabled Bank Sohar in particular, and the financial sector in general, to grow and expand. And finally, the Board of Directors expresses its unstinting gratitude to His Majesty the Sultan, Architect of Oman's Modern Renaissance, for his wise and benevolent leadership.

Salim Said Al Fannah Al Araimi
Chairman

STATEMENT OF FINANCIAL POSITION
AS AT 31 DECEMBER 2011

Restated Note A3.1 2009 USD'000	Restated Note A3.1 2010 USD'000	2011 USD'000		Notes	2011 RO'000	Restated Note A3.1 2010 RO'000	Restated Note A3.1 2009 USD'000
			ASSETS				
343,558	272,784	**159,774**	Cash and balances with Central Bank	B1	**61,513**	105,022	132,270
52,675	310,291	**601,455**	Due from banks and other money market lendings	B2	**231,560**	119,462	20,280
2,043,595	2,345,544	**2,648,192**	Loans and advances-net	B3	**1,019,554**	903,034	786,784
160,234	278,309	**222,491**	Investment securities	B4	**85,659**	107,149	61,690
37,247	35,753	**36,771**	Property, equipment and fixtures	B5	**14,157**	13,765	14,340
24,014	26,449	**50,738**	Other assets	B6	**19,534**	10,183	9,246
2,661,323	3,269,130	**3,719,421**			**1,431,977**	1,258,615	1,024,610
			LIABILITIES				
55,584	133,188	**112,042**	Due to banks and other money market borrowings	B7	**43,136**	51,277	21,400
101,397	18,280	**-**	Certificates of deposit	B8	**-**	7,038	39,038
2,162,205	2,595,156	**3,042,694**	Customers' deposits	B9	**1,171,437**	999,135	832,449
50,114	71,777	**100,566**	Other liabilities	B11	**38,718**	27,634	19,294
-	129,870	**129,870**	Subordinated loans	B12	**50,000**	50,000	-
2,369,300	2,948,271	**3,385,172**			**1,303,291**	1,135,084	912,181
			SHAREHOLDERS' EQUITY				
259,740	259,740	**259,740**	Share capital	B13	**100,000**	100,000	100,000
8,397	11,052	**14,818**	Legal reserve	B14	**5,705**	4,255	3,233
-	1,073	**1,073**	General reserve	B14	**413**	413	-
1,106	3,397	**(5,283)**	Fair value reserve	B15	**(2,034)**	1,308	426
22,780	45,597	**63,901**	Retained earnings		**24,602**	17,555	8,770
292,023	320,859	**334,249**			**128,686**	123,531	112,429
2,661,323	3,269,130	**3,719,421**			**1,431,977**	1,258,615	1,024,610
			Net assets per share (in baizas)	B16	**128.69**	123.53	112.43
29.20	32.09	**33.43**	**Net assets per share (in cents)**	B16			
277,732	467,244	**477,039**	**CONTINGENT LIABILITIES**	B17	**183,660**	179,889	106,927
69,366	544,875	**721,242**	**COMMITMENTS**	B17	**277,678**	209,777	26,706

The financial statements on pages 2 to 56 were approved and authorized for issue by the Board of Directors on 24 January 2012 and signed on their behalf by:

Chairman

Deputy Chairman

Report of the Auditors - page 1.

STATEMENT OF COMPREHENSIVE INCOME
FOR THE YEAR ENDED 31 DECEMBER 2011

2010 USD'000	2011 USD'000		Notes	2011 RO'000	2010 RO'000
151,680	**157,961**	Interest income	C1	**60,815**	58,397
(72,213)	**(67,683)**	Interest expense	C2	**(26,058)**	(27,802)
79,467	**90,278**	**Net interest income**		**34,757**	30,595
12,042	**21,894**	Other operating income	C3	**8,429**	4,636
91,509	**112,172**	**OPERATING INCOME**		**43,186**	35,231
		OPERATING EXPENSES			
(30,400)	**(36,592)**	Staff costs		**(14,088)**	(11,704)
(15,639)	**(18,888)**	Other operating expenses	C4	**(7,272)**	(6,021)
(4,834)	**(4,725)**	Depreciation	B5	**(1,819)**	(1,861)
(50,873)	**(60,205)**			**(23,179)**	(19,586)
40,636	**51,967**	**OPERATING PROFIT**		**20,007**	15,645
(55)	**(44)**	Impairment on investments		**(17)**	(21)
(2,753)	**(2,288)**	Impairment allowance on portfolio basis	B3	**(881)**	(1,060)
(7,595)	**(6,717)**	Impairment allowance on specific basis	B3	**(2,586)**	(2,924)
30,233	**42,918**	**PROFIT BEFORE TAX**		**16,523**	11,640
(3,688)	**(5,262)**	**Income tax expense**	C5	**(2,026)**	(1,420)
26,545	**37,656**	**PROFIT FOR THE YEAR**		**14,497**	10,220
		Other comprehensive income			
2,291	**(8,231)**	Net changes in fair value of available for sale financial assets net of income tax		**(3,169)**	882
2,291	**(8,231)**	**Other comprehensive income for the year, net of income tax**		**(3,169)**	882
28,836	**29,424**	**TOTAL COMPREHENSIVE INCOME FOR THE YEAR**		**11,328**	11,102
		Basic earnings per share - in baizas		**14.50**	10.22
2.66	**3.77**	Basic earnings per share - in cents			

The notes and other explanatory information on pages 7 to 56 form an integral part of these financial statements.

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STATEMENT OF CHANGES IN EQUITY
FORTHE YEAR ENDED 31 DECEMBER 2011

	Share capital RO'000	Legal reserve RO'000	General reserve RO'000	Fair value reserve RO'000	Retained earnings RO'000	Total RO'000
Balance as at 1 January 2010 as previously reported	100,000	2,533	-	426	2,470	105,429
Effect of correction of prior period error [Note A3.1]	-	-	-	-	7,000	7,000
Transfers	-	700	-	-	(700)	-
Balance as at 1 January 2010 - restated	100,000	3,233	-	426	8,770	112,429
Total comprehensive income						
Profit for the year	-	-	-	-	10,220	10,220
Other comprehensive income						
Net change in fair value of available for sale investments (note B4)	-	-	-	882	-	882
Total comprehensive income	-	-	-	882	10,220	11,102
Transfers	-	1,022	413	-	(1,435)	-
Balance as at 31 December 2010	100,000	4,255	413	1,308	17,555	123,531

	Share capital RO'000	**Legal reserve RO'000**	**General reserve RO'000**	**Fair value reserve RO'000**	**Retained earnings RO'000**	**Total RO'000**
Balance as at 1 January 2011	**100,000**	**4,255**	**413**	**1,308**	**17,555**	**123,531**
Total comprehensive income						
Profit for the year	**-**	**-**	**-**	**-**	**14,497**	**14,497**
Other comprehensive income						
Net change in fair value of available for sale investments - net of tax (note B4)	**-**	**-**	**-**	**(3,169)**	**-**	**(3,169)**
Release on sale of available for sale financial assets	**-**	**-**	**-**	**(173)**	**-**	**(173)**
Total comprehensive income	**-**	**-**	**-**	**(3,342)**	**14,497**	**11,155**
Dividends paid for the year 2010	**-**	**-**	**-**	**-**	**(6,000)**	**(6,000)**
Transfers	**-**	**1,450**	**-**	**-**	**(1,450)**	**-**
Balance as at 31 December 2011	**100,000**	**5,705**	**413**	**(2,034)**	**24,602**	**128,686**

The notes and other explanatory information on pages 7 to 56 form an integral part of these financial statements.

Report of the Auditors - page 1.

STATEMENT OF CHANGES IN EQUITY (Continued)
FORTHE YEAR ENDED 31 DECEMBER 2011

	Share capital USD'000	Legal reserve USD'000	General reserve USD'000	Fair value reserve USD'000	Retained earnings USD'000	Total USD'000
Balance as at 1 January 2010 as previously reported	259,740	6,579	-	1,106	6,416	273,841
Effect of correction of prior period error [Note A3.1]	-	-	-	-	18,182	18,182
Transfers	-	1,818	-	-	(1,818)	-
Balance as at 1 January 2010 - restated	259,740	8,397	-	1,106	22,780	292,023
Total comprehensive income						
Profit for the year	-	-	-	-	26,545	26,545
Other comprehensive income						
Net change in fair value of available for sale investments (note B4)	-	-	-	2,291	-	2,291
Total comprehensive income	-	-	-	2,291	26,545	28,836
Transfers	-	2,655	1,073	-	(3,728)	-
Balance as at 31 December 2010	259,740	11,052	1,073	3,397	45,597	320,859

	Share capital USD'000	**Legal reserve USD'000**	**General reserve USD'000**	**Fair value reserve USD'000**	**Retained earnings USD'000**	**Total USD'000**
Balance as at 1 January 2011	**259,740**	**11,052**	**1,073**	**3,397**	**45,597**	**320,859**
Total comprehensive income						
Profit for the year	**-**	**-**	**-**	**-**	**37,656**	**37,656**
Other comprehensive income						
Net change in fair value of available for investments - net of tax (note B4)	**-**	**-**	**-**	**(8,231)**	**-**	**(8,231)**
Release on sale of available for sale financial assets	**-**	**-**	**-**	**(449)**	**-**	**(449)**
Total comprehensive income	**-**	**-**	**-**	**(8,680)**	**37,656**	**28,976**
Dividends paid for the year 2010	**-**	**-**	**-**	**-**	**(15,586)**	**(15,586)**
Transfers	**-**	**3,766**	**-**	**-**	**(3,766)**	**-**
Balance as at 31 December 2011	**259,740**	**14,818**	**1,073**	**(5,283)**	**63,901**	**334,249**

The notes and other explanatory information on pages 7 to 56 form an integral part of these financial statements.

Report of the Auditors - page 1.

STATEMENT OF CASH FLOWS
FORTHE YEAR ENDED 31 DECEMBER 2011

2010 USD'000	2011 USD'000		2011 RO'000	2010 RO'000
		Operating activities		
30,233	**42,918**	Profit before tax	**16,523**	11,640
		Adjustments for:		
4,834	**4,725**	Depreciation	**1,819**	1,861
10,348	**9,049**	Impairment for credit losses and investment	**3,484**	3,984
1,179	**-**	Reserve interest on loans	**-**	454
(5)	**(488)**	Gain on sale of investment securities	**(188)**	(2)
(1,303)	**(2,205)**	Interest on investment	**(849)**	(502)
45,286	**53,997**	**Operating profit before changes in working capital**	**20,789**	17,435
(298,476)	**(311,657)**	Loans and advances	**(119,988)**	(120,688)
(2,488)	**(24,083)**	Other assets	**(9,272)**	(958)
(83,117)	**(18,281)**	Certificates of deposit	**(7,038)**	(32,000)
432,951	**447,535**	Customers' deposits	**172,301**	166,686
33,065	**(7,094)**	Due to banks and other money market borrowings	**(2,731)**	12,730
(296,299)	**(159,675)**	Due from banks and other money market lendings	**(61,475)**	(108,300)
20,327	**29,223**	Other liabilities	**11,251**	8,570
(148,751)	**9,966**	**Cash from/(used in) operating activities**	**3,837**	(56,225)
(1,927)	**(3,423)**	**Income tax paid**	**(1,318)**	(742)
(150,678)	**6,543**	**Net cash from/(used in) operating activities**	**2,519**	(57,267)
		Investing activities		
(17,612)	**(38,304)**	Purchase of investments	**(14,747)**	(6,781)
31,996	**4,057**	Proceeds from sale/redemption of investments	**1,562**	12,319
(5,643)	**(5,748)**	Purchase of property, equipment and fixtures	**(2,213)**	(2,173)
1,304	**2,205**	Interest received on investments	**849**	502
-	**8**	Proceeds from sale of property, equipment and fixtures	**3**	-
10,045	**(37,782)**	**Net cash (used in)/from investing activities**	**(14,546)**	3,867
		Financing activities		
-	**(15,584)**	Dividend paid	**(6,000)**	-
129,870	**-**	Subordinate loans received during the year	**-**	50,000
129,870	**(15,584)**	**Net cash (used in)/from financing activities**	**(6,000)**	50,000
(10,763)	**(46,823)**	**Net change in cash and cash equivalents**	**(18,027)**	(3,400)
455,732	**444,969**	**Cash and cash equivalents at beginning of the year**	**171,313**	175,457
444,969	**398,145**	**Cash and cash equivalents at the end of the year**	**153,286**	172,057
		Representing:		
270,852	**159,774**	Cash and balances with Central Banks	**61,513**	105,022
28,992	**160,481**	Due from banks and other money market lendings	**61,785**	11,162
245,247	**163,961**	Investment securities	**63,125**	94,420
(100,122)	**(86,070)**	Due to banks and other money market borrowings	**(33,137)**	(38,547)
444,969	**398,145**		**153,286**	172,057

The notes and other explanatory information on pages 7 to 56 form an integral part of these financial statements.

Report of the Auditors - page 1.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2011

A1 Legal status and principal activities

Bank Sohar SAOG ("the Bank") was established in the Sultanate of Oman on 4 March 2007 as a joint stock company and is primarily engaged in corporate and retail banking activities through a network of twenty five branches within the Sultanate of Oman. The Bank operates under a banking licence issued by the Central Bank of Oman and is covered by its deposit insurance scheme. The Bank started commercial operations from 9 April 2007. The registered address of the Bank is PO Box 44, Hai Al Mina, Postal Code 114, Muscat, Sultanate of Oman. The Bank has its primary listing on the Muscat Securities Market.

The Bank employed 549 employees as of 31 December 2011 (31 December 2010: 513).

A2 Basis of preparation

A2.1 Statement of compliance

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

A2.2 Basis of measurement

The financial statements have been prepared under the historical cost convention except for derivative financial instruments and available for sale financial assets which have been measured at fair value.

A2.3 Functional and presentation currency

These financial statements are presented in Rial Omani, which is the Bank's functional currency and also in US Dollars, for the convenience of the readers. The US Dollar amounts, which are presented in these financial statements have been translated from the Rial Omani amounts at an exchange rate of US Dollar 1 = RO 0.385. All financial information presented in Rial Omani and US Dollars has been rounded to the nearest thousands.

A2.4 Use of estimates and judgements

The preparation of financial statements in conformity with IFRS requires management to make judgements, estimates and assumptions that effect the application of accounting policies and reported amounts of assets and liabilities, income and expenses. Actual results may differ from these estimates.

The estimates and associated assumptions are based on industry data and various other factors that are believed by the Bank to be reasonable under the circumstances, the results of which form the basis of making the judgments about carrying values of assets and liabilities that are not readily apparent from other sources.

The estimates and underlying assumptions are reviewed on a regular basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised if the revision affects only that period or in the period of the revision and future periods if the revision affects both current and future periods. Estimates considered by the Bank to have a significant risk of material adjustment in subsequent periods are discussed in note A4.

A2.5 Standards, amendments and interpretations effective in 2011 and relevant for the Bank's operations

For the year ended 31 December 2011, the Bank has adopted all of 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 periods beginning on 1 January 2011.

The adoption of those standards and interpretations has not resulted in changes to the Bank's accounting policies and has not affected the amounts reported for the current period.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2011 (continued)

A2 Basis of preparation (continued)

A2.6 Standards, amendments and interpretations to existing standards that are not yet effective and have not been early adopted by the Bank:

The following standards, amendments and interpretations to existing standards have been published and are mandatory for the Bank's accounting periods beginning on or after 1 January 2012 or later periods, but the Bank has not early adopted them and the impact of these standards and interpretations is not reasonably estimable as at 31 December 2011:

IFRS 9, 'Financial instruments part 1: Classification and measurement', (effective on or after 1 January 2013);
IFRS 10, 'Consolidated financial statements' (effective on or after 1 January 2013);
IFRS 12, 'Disclosures of interests in other entities' (effective on or after 1 January 2013); and
IFRS 13, 'Fair value measurement' (effective on or after 1 January 2012).

A3 Significant accounting policies

The accounting policies set out below have been applied consistently by the Bank to all periods presented in these financial statements, unless otherwise stated.

A3.1 Correction of prior period error

Effective from 1 January 2011, the Bank has corrected a prior period error in relation to the recognition of 'assets without consideration and condition'. Based on the guidance provided by IFRS 'Framework for the preparation and presentation of consolidated financial statements', management restated the prior years' financial statements in accordance with IAS 8 - Accounting Policies, Changes in Accounting Estimates and Errors. The effect of this correction is applied retrospectively.

Previously, 'assets without consideration' were accounted at fair value in the statement of financial position under the appropriate classification and simultaneously 'deferred income' was created and classified as 'other liabilities'. After the correction the 'assets without consideration' are accounted at fair value in the statement of financial position under the appropriate classification and, corresponding credit is recognised as income directly in the statement of comprehensive income in the period when it is received.

Consistent with the correction of the error, the fair value of land amounting to RO 7,000,000 which should have been recognised as income in the year 2008 at the time of receipt of land, is recognised in the retained earnings of the Bank. The retained earnings balance has been restated in the statement of changes in equity.

A3.2 Foreign currency translation

Transactions in foreign currencies are translated into functional currency at the spot exchange rate at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies at the reporting date are retranslated into the functional currency at the spot exchange rate at that date. The foreign currency gain or loss on monetary items is the difference between amortised cost in the functional currency at the beginning of the period, adjusted for the effective interest and payments during the period, and the amortised cost in the foreign currency translated at the spot exchange rate at the end of the period. The non-monetary assets and liabilities denominated in foreign currencies that are measured at fair value are retranslated into the functional currency at the spot exchange rate at the date the fair value was determined. Foreign currency differences arising on retranslation are recognized in the statement of comprehensive income, except for non-monetary financial assets, such as equities classified as available-for-sale, which are included in other comprehensive income. Non-monetary assets and liabilities that are measured in terms of historical cost in a foreign currency are translated using the exchange rate at the date of the transaction.

A3.3 Revenue and expense recognition

A3.3.a Interest income and expense

Interest income and expense is recognised in the statement of comprehensive income using the effective interest method. The effective interest rate is the rate that exactly discounts the estimated future cash payments and receipts through the expected life of the financial asset or liability (or, where appropriate, a shorter period) to the carrying amount of the financial asset or liability. The effective interest rate is established on initial recognition of the financial asset/liability and is not revised subsequently. Interest income and expense presented in the statement of comprehensive income include:

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2011 (continued)

A3 Significant accounting policies (continued)

A3.3 Revenue and expense recognition (continued)

A3.3.a Interest income and expense (continued)

- Interest on financial assets and liabilities at amortised cost on an effective interest rate basis;
- Interest on available for sale investment securities on an effective interest rate basis; and
- Fair value changes in qualifying derivatives (including hedge ineffectiveness) and related hedged items when interest rate risk is the hedged risk.

Interest income which is doubtful of recovery is included in impairment allowance and excluded from income until it is received in cash.

A3.3.b Fair value gains and losses

Fair value changes on derivatives held for risk management purposes and available for sale financial assets are presented in the statement of comprehensive income.

Net income from financial instruments at fair value relates to non-qualifying derivatives held for risk management purposes and available for sale financial assets, including all realised and unrealised fair value changes interest, dividend and foreign exchange differences.

A3.3.c Dividend income

Dividend income is recognized when the right to receive dividend is established.

A3.3.d Fees and commission

Fees and commission income and expenses that are integral to the effective interest rate on a financial asset or liability are included in the measurement of the effective interest rate.

Other fees and commission income include account servicing fees, credit related fees, advisory fees, administration fees and other management fees, sales commission, placement fees and syndication fees. These are recognised as the related services are performed.

A3.3.e Provisions

A provision is recognised if, as a result of a past event, the Bank has a present legal or constructive obligation that can be estimated reliably, and it is probable that an outflow of economic benefits will be required to settle the obligation. Provisions are equivalent to the amortised value of the future liabilities which is determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and the risk specific to the liability.

A3.3.f Offsetting of income and expense

Income and expenses are presented on a net basis only when permitted by the IFRS, or for gains and losses arising from a group of similar transactions such as in the Bank's trading activity.

A3.4 Financial assets and liabilities

A3.4.a Classification

The Bank classifies its financial assets in the following categories: at fair value through profit or loss, loans and receivables, held to maturity and available-for-sale. The classification depends on the purpose for which the financial assets were acquired. Management determines the classification of its financial assets at initial recognition.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2011 (continued)

A3 Significant accounting policies (continued)

A3.4 Financial assets and liabilities (continued)

A3.4.a Classification (continued)

Financial assets at fair value through profit or loss

Financial assets at fair value through profit or loss are financial assets held for trading. A financial asset is classified in this category if acquired principally for the purpose of selling in the short-term. Derivatives are also categorised as held for trading unless they are designated as hedging instruments.

Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market and the Bank does not intend to sell immediately or in the near term.

Loans and receivables are initially recognised at fair value which is the cash consideration to originate or purchase the loan including any transaction costs - and measured subsequently at amortised cost using the effective interest method less specifically identified and collective allowance for impairment and recognised in the statement of comprehensive income as ‘impairment allowance’. Specific provisions are made against the carrying amount of loans and receivables that are identified as being impaired based on regular reviews of outstanding balances to reduce the impaired loans and receivables to their recoverable amounts. Loans and receivables are reported in the statement of financial position as loans and advances to banks or customers. Interest on loans is included in the statement of comprehensive income and is reported as ‘interest income’.

Held to maturity financial assets

Held to maturity financial assets are non-derivative assets with fixed or determinable payments and fixed maturity that the Bank has the positive intent and ability to hold to maturity and which are not designated at fair value through profit or loss or available-for-sale.

These are initially recognised at fair value including direct and incremental transaction costs and measured subsequently at amortised cost, using the effective interest method.

Interest on held to maturity investments is included in the statement of comprehensive income and reported as ‘interest income’. In the case of impairment, the impairment loss is been reported as a deduction from the carrying value of the investment and recognised in the statement of comprehensive income as ‘impairment on investments’. Held to maturity investments include corporate bonds and other debt securities.

Available-for-sale financial assets

Available-for-sale financial assets are non-derivatives that are either designated in this category or not classified in any of the other categories.

Available-for-sale investments are financial assets that are intended to be held for an indefinite period of time, which may be sold in response to needs for liquidity or changes in interest rates, exchange rates or equity prices or that are not classified as loans and receivables, held to maturity investments or financial assets at fair value through profit or loss.

Available-for-sale financial assets are initially recognised at fair value, which is the cash consideration including any transaction costs, and measured subsequently at fair value with gains and losses being recognised in the statement of other comprehensive income, except for impairment losses and foreign exchange gains and losses, until the financial asset is derecognised. If an available-for-sale financial asset is determined to be impaired, the cumulative gain or loss previously recognised in the statement of other comprehensive income is recognised in the statement of comprehensive income. However, interest is calculated using the effective interest method, and foreign currency gains and losses on monetary assets classified as available for sale are recognised in the statement of comprehensive income. Dividends on available-for-sale equity instruments are recognised in the statement of comprehensive income in ‘other operating income’ when the Bank’s right to receive payment is established.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2011 (continued)

A3 Significant accounting policies (continued)

A3.4 Financial assets and liabilities (continued)

A3.4.b Recognition

The Bank initially recognises loans and advances, deposits, debt securities issued and subordinated liabilities on the date that they are originated. All other financial assets and liabilities are initially recognised on the trade date at which the Bank becomes a party to the contractual provisions of the instrument.

A3.4.c Derecognition

The Bank derecognises a financial asset when the contractual rights to receive the cash flows from the asset expire, or it transfers the rights to receive the contractual cash flows on the financial asset in a transaction in which substantially all the risks and rewards of ownership of the financial asset are transferred. The Bank derecognises a financial liability when its contractual obligations are discharged or cancelled or expired.

A3.4.d Offsetting of financial assets and financial liabilities

Financial assets and liabilities are offset and the net amount presented in the statement of financial position when, and only when, the Bank has a legal right to set off the amounts and intends either to settle on a net basis or to realise the asset and settle the liability simultaneously.

A3.4.e Amortised cost measurement

The amortised cost of a financial asset or liability is the amount at which the financial asset or liability is measured at initial recognition, minus principal repayments, plus or minus the cumulative amortisation using effective interest method of any difference between the initial amount recognised and the maturity amount, minus any reduction for impairment.

A3.4.f Fair value measurement

A number of the Bank's accounting policies and disclosures require the determination of fair value, for both financial and non-financial assets and liabilities. Fair values have been determined for measurement and/or disclosure purposes based on a number of accounting policies and methods. Where applicable, information about the assumptions made in determining fair values is disclosed in the notes specific to that asset or liability.

For investments where there is no quoted market price, a reasonable estimate of the fair value is determined by reference to the current market value of a similar investment, or is based on the expected discounted cash flows. Investments having short term maturities are not discounted.

The fair value of loans and advances is estimated at the present value of future cash flows, discounted at the market rate of interest at the reporting date.

The fair value of forward exchange contracts is based on their quoted price, if available. If a quoted price is not available, then fair value is estimated by discounting the difference between the contractual forward price and the current forward price for the residual maturity of the contract using a risk-free interest rate (based on government bonds). The fair value of interest rate swaps is based on broker quotes. Those quotes are tested for reasonableness by discounting estimated future cash flows based on the terms and maturity of each contract and using market interest rates for a similar instrument at the measurement date. Fair values reflect the credit risk of the instrument and include adjustments to take account of the credit risk of the Bank and counterparty when appropriate.

Fair value, which is determined for disclosure purposes, is calculated based on the present value of future principal and interest cash flows, discounted at the market rate of interest at the reporting date.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2011 (continued)

A3 Significant accounting policies (continued)

A3.4 Financial assets and liabilities (continued)

A3.4.g Identification and measurement of impairment of financial assets

(i) Assets carried at amortised cost

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 Bank, including adverse changes in the payment status of borrowers in the group, 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.

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.

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 group and historical loss experience for assets with credit risk characteristics similar to those in the group.

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.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2011 (continued)

A3 Significant accounting policies (continued)

A3.4 Financial assets and liabilities (continued)

A3.4.g Identification and measurement of impairment of financial assets (continued)

(ii) Assets classified as available-for-sale

The Bank assesses at the end of each reporting period whether there is objective evidence that a financial asset or a group of financial assets is impaired. For debt securities, the Bank uses the criteria referred to in (i) above. In the case of equity investments classified as available-for-sale, a significant or prolonged decline in the fair value of the security below its cost is also evidence that the assets are impaired. If any such evidence exists for available-for-sale financial assets, the cumulative loss - measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that financial asset previously recognised in profit or loss - is removed from equity and recognised in the statement of comprehensive income. Impairment losses recognised in the statement of comprehensive income on equity instruments are not reversed through the statement of comprehensive income.

A3.4.h Cash and cash equivalents

Cash and cash equivalents consist of cash in hand, unrestricted balances held with central banks and highly liquid financial assets with original maturities of upto three months, which are subject to insignificant risk of changes in their fair value, and are used by the Bank in management of its short term commitments. Cash and cash equivalents are carried at amortised cost in the statement of financial position.

A3.4.i Repurchase and resale agreements

Securities sold with a commitment to repurchase (repos) at a specified future date are recognised in the statement of financial position and are measured in accordance with accounting policies for trading securities or investment securities. The counterparty liability for amounts received under these agreements is included in 'due to banks and other money market borrowings'. The difference between sale and repurchase price is treated as interest expense and accrued over the life of the repo agreement.

Securities purchased with a corresponding commitment to resell at a specified future date (reverse repos) are not recognised in the statement of financial position and the amounts paid under these agreements are included in 'due from banks and other money market lendings'. The difference between purchase and resale price is treated as interest income and accrued over the life of the reverse repo agreement.

A3.4.j Acceptances

Acceptances are disclosed on the statement of financial position under other assets with corresponding liability disclosed under other liabilities. Therefore, there is no off-balance sheet commitment for acceptances.

A3.4.k Derivatives held for risk management purposes

Derivatives held for risk management purposes include all derivative assets and liabilities that are not classified as trading assets and liabilities. Derivatives held for risk management purposes are measured at fair value in the statement of financial position. The treatment of changes in their fair value depends on their classification into the following categories:

Fair value hedge

When a derivative is designated as a hedge of the change in fair value of a recognised asset or liability or a firm commitment, changes in the fair value of the derivative are recognised immediately in statement of comprehensive income together with changes in the fair value of the hedged item that are attributable to the hedged risk.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2011 (continued)

A3 Significant accounting policies (continued)

A3.4 Financial assets and liabilities (continued)

A3.4.k Derivatives held for risk management purposes (continued)

If the derivative expires or is sold, terminated, or exercised, no longer meets the criteria for fair value hedge accounting, or the designation is revoked, hedge accounting is discontinued. Any adjustment up to that point, to a hedged item for which the effective interest method is used, is amortised to profit or loss as part of the recalculated effective interest rate of the item over its remaining life.

Cash flow hedge

When a derivative is designated as the hedging instrument in a hedge of the variability in cash flows attributable to a particular risk associated with a recognised asset or a liability or a highly probable forecast transaction that could affect profit or loss, the effective portion of changes in the fair value of the derivative is recognised in other comprehensive income in hedging reserve. The amount recognised in other comprehensive income is reclassified to comprehensive income as a reclassification adjustment in the same period as the hedged cash flows affect profit or loss, and in the same line item in the statement of comprehensive income. Any ineffective portion of changes in the fair value of the derivative is recognised immediately in statement of comprehensive income.

If the hedging derivative expires or is sold, terminated, or exercised, or the hedge no longer meets the criteria for cash flow hedge accounting, or the hedge designation is revoked, then the hedge accounting is discontinued prospectively. In a discontinued hedge of a forecast transaction the cumulative amount recognized in other comprehensive income from the period when the hedge was effective is reclassified from the equity to statement of comprehensive income as a reclassification adjustment when the forecast transaction occurs and affects profit or loss. If the forecast transaction is no longer expected to occur, then the balance in other comprehensive income is reclassified immediately to statement of comprehensive income as a reclassification adjustment.

Other non-trading derivative

When a derivative is not held for trading, and is not designated in a qualifying hedge relationship, all changes in its fair value are recognised immediately in statement of comprehensive income.

A3.5 Property, equipment and fixtures

Items of property, equipment and fixtures are measured at cost less accumulated depreciation and impairment losses. Cost includes expenditure that is directly attributable to the acquisition of the asset. Depreciation is provided on a straight-line basis over the estimated useful lives of property, equipment and fixtures, except freehold land. The estimated useful lives for the current period are as follows:

	Years
Motor vehicles	5
Furniture & fixtures	5
Office equipment	6-7
Production software	6-7

The assets' residual values, useful lives and depreciation methods are reviewed and adjusted if appropriate at each reporting date. Based on the recent estimation, the Bank has changed the useful life of motor vehicles and furniture & fixtures from 3 to 5 years. The change of estimated useful live is accounted for as a change in estimate by adjusting the depreciation charge for the current year as the change affects the current year and by adjusting the charge for future years to the extent that it affects the future years.

An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount.

Gains and losses on disposals are determined by comparing the proceeds with the carrying amount and are recognised within 'other operating income' in the statement of comprehensive income.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2011 (continued)

A3 Significant accounting policies (continued)

A3.5 Property, equipment and fixtures (continued)

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, equipment and fixtures. All other expenditure is recognised in the statement of comprehensive income as an expense as incurred.

A3.6 Deposits, debt securities issued and subordinated liabilities

All money market and customer deposits are initially measured at fair value plus transaction cost and subsequently carried at amortised cost. Deposits, debt securities issued and subordinated liabilities are measured at their amortized cost using the effective interest method. The Bank classifies capital instruments as financial liabilities or equity instruments in accordance with the substance of the contractual terms of the instrument.

A3.7 Taxation

Taxation is provided in accordance with Omani fiscal regulations. Income tax comprises current and deferred tax. Income tax expense is recognised in the statement of comprehensive income except to the extent that it relates to items recognised directly in equity or other comprehensive income.

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

Deferred tax assetss/liabilities are 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. Deferred tax is measured at the tax rates that are expected to be applied to the temporary difference when they reverse, based on the laws that have been enacted or substantively enacted by 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 utilized. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

A3.8 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.

A3.9 Trade and settlement date accounting

All “regular way” purchases and sales of financial assets are recognised on the trade date, i.e. the date that the entity commits to purchase or sell the asset. Regular way purchase or sales are 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.

A3.10 Leases

Operating lease payments are recognised as an expense in the statement of comprehensive income on a straight-line basis over the lease term.

A3.11 Financial guarantees

Financial guarantees are contracts that require the Bank to make specified payments to reimburse the holder for a loss it incurs because a specified debtor fails to make payment, when due in accordance with the terms of a debt instrument.

A3 Significant accounting policies (continued)

A3.11 Financial guarantees (continued)

Financial guarantee liabilities are initially recognised at their fair value, and the initial fair value is amortised over the life of the financial guarantee. The guarantee liability is subsequently carried at the higher of this amortised amount and the present value of any expected payment (when a payment under the guarantee has become probable). The unamortized value or present value of the expected payment arising from the financial guarantee as the case may be is included in the other liabilities.

A3.12 Employee benefits

A3.12.a Terminal benefits

End of service benefits are accrued in accordance with the terms of employment of the company's employees at the reporting date, having regard to the requirements of the Oman Labour Law 2003, as amended.

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

A3.12.b Short term benefits

Short term benefit obligations are measured on an undiscounted basis and are expensed as the related service is provided.

A provision is recognised for the amount expected to be paid if the Bank has a present legal or constructive obligation to pay this amount as a result of past service provided by the employee and the obligation can be estimated reliably.

A3.13 Earnings per share

The Bank presents basic and diluted earnings per share (EPS) data for its ordinary shares. Basic EPS is calculated by dividing the profit or loss attributable to ordinary shareholders of the Bank by the weighted average number of ordinary shares outstanding during the year. Annualised EPS is calculated by annualizing the basic EPS for the whole year. Diluted EPS is determined by adjusting the profit or loss attributable to ordinary shareholders and weighted average number of ordinary shares outstanding for the effects of all dilutive potential ordinary shares, which comprise convertible notes or similar instruments.

A3.14 Corresponding figures

The corresponding figures included for comparative purposes have been reclassified to conform to the presentation in the current year.

A3.15 Segment reporting

An operating segment is the component of the Bank that engages in business activities from which it may earn revenues and incur expenses, including revenue and expenses that relate to transaction with any of the Bank’s other components, whose operating results are reviewed regularly by the Bank’s CEO (being the chief operating decision maker) to make decisions about resources allocated to each segment and assess its performance, and for which discrete financial information is available.

A4 Critical accounting estimates and judgements

The preparation of financial statements requires management to make judgements, estimates and assumptions that affect the application of accounting policies and reported amounts of assets, liabilities, income and expenses. The estimates and associated assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances, the results of which form the basis of making the judgements about carrying values of assets and liabilities that are not readily apparent from other sources. The resulting accounting estimates will, by definition, seldom equal the related actual results.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2011 (continued)

A4 Critical accounting estimates and judgements (continued)

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised if the revision affects only that period or in the period of the revision and future periods if the revision affects both current and future periods. The Bank's significant accounting estimates are on:

A4.1 Impairment losses on loans and advances

The Bank reviews its loan portfolios to assess impairment on a monthly basis. In determining whether an impairment loss should be recorded in the statement of comprehensive income, the Bank makes judgements as to whether there is any observable data indicating an impairment followed by measurable decrease in the estimated future cash flows from a portfolio of loans before the decrease can be identified within that portfolio. This evidence may include observable data indicating that there has been an adverse change in the payment status of borrowers and or national or local economic conditions that correlate with defaults on assets. 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. The methodology and assumptions used for estimating both the amount and timing of future cash flows are reviewed periodically to reduce any difference between loss estimates and actual loss experience. For individually significant loans and advances which are impaired, the necessary impairment loss is considered based on the future cash flow estimates. Individually significant loans and advances which are not impaired and all individually insignificant loans and advances are then assessed collectively considering historical experience and observable data on a portfolio basis, in group of assets with similar risk characteristics to determine whether collective impairment loss to be made. In determining collective impairment loss, the Bank takes into account several factors including credit quality, concentration risk, levels of past due, sector performance, available collateral and macro economic conditions.

A4.2 Fair value of derivatives and other financial instruments

The fair value of financial instruments that are not traded in an active market (for example, over-the-counter derivatives) is determined by using valuation techniques. The Bank uses its judgement to select a variety of methods and make assumptions that are mainly based on market conditions existing at the end of each reporting period. The Bank uses expected cash flow analysis for various available-for-sale financial assets that are not traded in active markets.

A4.3 Impairment of available-for-sale equity investments

The Bank determines that available-for-sale equity investments are impaired when there has been a significant or prolonged decline in the fair value below its cost or objective evidence of impairment exists. This determination of what is considered to be significant or prolonged requires judgement. In applying judgement, the Bank evaluates among other factors, the volatility in share price. Objective evidence of impairment may be due to deterioration in the financial health of the investee, industry and sector performance.

B1 Cash and balances with central bank

2010 USD'000	**2011 USD'000**		**2011 RO'000**	2010 RO'000
16,961	**20,691**	Cash	**7,966**	6,530
1,299	**1,299**	Capital deposit with Central Bank of Oman	**500**	500
254,524	**137,784**	Unrestricted balances with Central Bank	**53,047**	97,992
272,784	**159,774**		**61,513**	105,022

The capital deposit with the Central Bank of Oman cannot be withdrawn without its approval.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2011 (continued)

B2 Due from banks and other money market lendings

2010 USD'000	2011 USD'000		2011 RO'000	2010 RO'000
		Local currency:		
2,597	**38,961**	Money market lendings	**15,000**	1,000
2,597	**38,961**		**15,000**	1,000
		Foreign currency:		
280,000	**535,974**	Money market lendings	**206,350**	107,800
27,694	**26,520**	Nostro balances abroad	**10,210**	10,662
307,694	**562,494**		**216,560**	118,462
310,291	**601,455**		**231,560**	119,462

B3 Loans and advances - net

2010 USD'000	2011 USD'000		2011 RO'000	2010 RO'000
15,000	**78,190**	Loans to banks	**30,103**	5,775
1,428,070	**1,669,805**	Corporate loans	**642,875**	549,807
946,905	**955,711**	Personal loans	**367,949**	364,558
2,389,975	**2,703,706**	Gross loans and advances	**1,040,927**	920,140
(32,930)	**(35,218)**	Impairment allowance on portfolio basis	**(13,559)**	(12,678)
(11,501)	**(20,296)**	Impairment allowance on specific basis (including reserve interest)	**(7,814)**	(4,428)
2,345,544	**2,648,192**	Net loans and advances	**1,019,554**	903,034

Personal loans include RO 16,190,703 provided to staff on concessional terms (2010: RO 15,124,351).

Loans and advances comprise:

2010 USD'000	2011 USD'000		2011 RO'000	2010 RO'000
2,189,099	**2,456,537**	Loans	**945,767**	842,803
143,764	**164,216**	Overdrafts	**63,223**	55,349
39,042	**55,434**	Loan against trust receipts	**21,342**	15,031
18,070	**27,519**	Bills discounted	**10,595**	6,957
2,389,975	**2,703,706**	Gross loans and advances	**1,040,927**	920,140
(32,930)	**(35,218)**	Impairment allowance on portfolio basis	**(13,559)**	(12,678)
(11,501)	**(20,296)**	Impairment allowance on specific basis (including reserve interest)	**(7,814)**	(4,428)
2,345,544	**2,648,192**	Net loans and advances	**1,019,554**	903,034

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2011 (continued)

B3 Loans and advances-net (continued)

As per the CBO requirements, the movement in the impairment allowance is analysed as below:

2010 USD'000	2011 USD'000		2011 RO'000	2010 RO'000
		Impairment allowance on portfolio basis		
30,177	**32,930**	Balance at beginning of year	**12,678**	11,618
2,753	**2,288**	Provided during the year	**881**	1,060
32,930	**35,218**	Balance at the end of the year	**13,559**	12,678
		Impairment allowance on specific basis		
		Loan loss provision		
2,348	**9,943**	Balance at beginning of year	**3,828**	904
9,984	**11,109**	Provided during the year	**4,277**	3,844
(2,389)	**(4,392)**	Write back during the year	**(1,691)**	(920)
9,943	**16,660**	Balance at the end of the year	**6,414**	3,828
		Reserved interest		
377	**1,558**	Balance at beginning of year	**600**	145
1,496	**2,481**	Reserved during the year	**955**	576
(315)	**(403)**	Interest released during the year	**(155)**	(121)
1,558	**3,636**	Balance at end of the year	**1,400**	600
11,501	**20,296**		**7,814**	4,428

Impairment allowance on portfolio basis is established to meet the credit risks inherent within the loans and advances on a portfolio basis.

All loans and advances require payment of interest, some at fixed rates and others at rates that reprice prior to maturity. Interest reserve account is maintained by the Bank to comply with rules, regulations and guidelines issued by CBO against loans and advances which are impaired. As of 31 December 2011, loans and advances on which interest is not being accrued or where interest has been reserved amounted to RO 15,998,677 (2010: RO 8,051,521).

The table below analyses the concentration of gross loans and advances by economic sector:

2010 USD'000	2011 USD'000		2011 RO'000	2010 RO'000
946,904	**955,187**	Personal	**367,949**	364,558
327,369	**486,618**	Construction	**187,244**	126,037
229,088	**299,579**	Services	**115,240**	88,199
130,470	**140,782**	Financial institutions	**54,201**	50,231
128,395	**86,740**	Manufacturing	**33,395**	49,432
331,743	**85,751**	International trade	**33,014**	127,721
17,169	**53,725**	Mining and quarrying	**20,684**	6,610
49,740	**34,608**	Non-resident	**13,324**	19,150
1,255	**1,153**	Government	**444**	483
227,842	**559,563**	Other	**215,432**	87,719
2,389,975	**2,703,706**		**1,040,927**	920,140

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FOR THE YEAR ENDED 31 DECEMBER 2011 (continued)

B4 Investment securities

2010 USD'000	2011 USD'000		2011 RO'000	2010 RO'000
267,816	**205,504**	Available for sale investments	**79,119**	103,109
10,493	**16,987**	Held to maturity investments	**6,540**	4,040
278,309	**222,491**		**85,659**	107,149

Available for sale investments comprise:

	Carrying/ fair value 2011 RO'000	Cost 2011 RO'000	Carrying/ fair value 2010 RO'000	Cost 2010 RO'000
Unquoted securities	**6,040**	**7,774**	427	515
Quoted securities	**9,954**	**10,460**	8,262	7,379
Treasury bills	**63,125**	**63,113**	94,420	94,385
	79,119	**81,347**	103,109	102,279

	Carrying/ fair value 2011 USD'000	Cost 2011 USD'000	Carrying/ fair value 2010 USD'000	Cost 2010 USD'000
Unquoted securities	**15,688**	**20,192**	1,109	1,338
Quoted securities	**25,855**	**27,169**	21,460	19,166
Treasury bills	**163,961**	**163,930**	245,247	245,156
	205,504	**211,291**	267,816	265,660

Held to maturity investments comprise:

2010 USD'000	2011 USD'000		2011 RO'000	2010 RO'000
4,000	**4,000**	Corporate bonds	**1,540**	1,540
6,493	**12,987**	Debt securities	**5,000**	2,500
10,493	**16,987**		**6,540**	4,040

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2011 (continued)

B5 Property, equipment and fixtures

	Freehold land* RO'000	Production software RO'000	Furniture & fixtures RO'000	Office equipments RO'000	Motor vehicles RO'000	Capital work in progress RO'000	Total RO'000
Cost:							
At 1 January 2011	**7,000**	**5,684**	**2,229**	**3,109**	**525**	**25**	**18,572**
Additions	**-**	**488**	**891**	**586**	**71**	**178**	**2,214**
Disposals	**-**	**-**	**(1)**	**(3)**	**-**	**-**	**(4)**
At 31 December 2011	**7,000**	**6,172**	**3,119**	**3,692**	**596**	**203**	**20,782**
Accumulated depreciation:							
At 1 January 2011	**-**	**(2,003)**	**(1,321)**	**(1,173)**	**(310)**	**-**	**(4,807)**
Depreciation	**-**	**(905)**	**(335)**	**(522)**	**(57)**	**-**	**(1,819)**
Disposals	**-**	**-**	**-**	**1**	**-**	**-**	**1**
At 31 December 2011	**-**	**(2,908)**	**(1,656)**	**(1,694)**	**(367)**	**-**	**(6,625)**
Net book value:							
At 31 December 2011	**7,000**	**3,264**	**1,463**	**1,998**	**229**	**203**	**14,157**
At 31 December 2011 USD '000	**18,182**	**8,478**	**3,800**	**5,190**	**595**	**527**	**36,771**

	Freehold land* RO'000	Production software RO'000	Furniture & fixtures RO'000	Office equipments RO'000	Motor vehicles RO'000	Capital work in progress RO'000	Total RO'000
Cost:							
At 1 January 2010	7,000	4,540	1,741	2,767	351	887	17,286
Additions	-	1,144	488	342	174	25	2,173
Disposals	-	-	-	-	-	(887)	(887)
At 31 December 2010	7,000	5,684	2,229	3,109	525	25	18,572
Accumulated depreciation:							
At 1 January 2010	-	(1,247)	(766)	(735)	(198)	-	(2,946)
Depreciation	-	(756)	(555)	(438)	(112)	-	(1,861)
At 31 December 2010	-	(2,003)	(1,321)	(1,173)	(310)	-	(4,807)
Net book value:							
At 31 December 2010	7,000	3,681	908	1,936	215	25	13,765
At 31 December 2010 USD '000	18,182	9,561	2,358	5,029	558	65	35,753

Freehold land represents three plots of land received by the Bank as grant from the Government of Sultanate of Oman during the year 2008. The Bank has recorded the land based on the average valuation of the two professional valuators carried out during 2008.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2011 (continued)

B6 Other assets

2010 USD'000	2011 USD'000		2011 RO'000	2010 RO'000
13,855	**34,553**	Acceptances	**13,303**	5,334
6,571	**6,868**	Interest receivable	**2,644**	2,530
2,901	**3,644**	Prepayments and deposits	**1,403**	1,117
29	**232**	Deferred tax asset (note C5)	**89**	11
3,093	**5,441**	Other	**2,095**	1,191
26,449	**50,738**		**19,534**	10,183

B7 Due to banks and other money market borrowings

2010 USD'000	2011 USD'000		2011 RO'000	2010 RO'000
		Local currency:		
10,000	**-**	Money market borrowings	**-**	3,850
120	**725**	Vostro balances	**279**	46
10,120	**725**		**279**	3,896
		Foreign currency:		
123,068	**111,317**	Money market borrowings	**42,857**	47,381
123,068	**111,317**		**42,857**	47,381
133,188	**112,042**		**43,136**	51,277

B8 Certificates of deposit

2010 USD'000	2011 USD'000		2011 RO'000	2010 RO'000
101,397	**18,280**	Balance at beginning of year	**7,038**	39,038
(83,117)	**(18,280)**	Redeemed during the year	**(7,038)**	(32,000)
18,280	**-**	Balance at end of year	**-**	7,038

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2011 (continued)

B9 Customers' deposits

2010 USD'000	2011 USD'000		2011 RO'000	2010 RO'000
1,842,613	**2,014,514**	Term deposits	**775,588**	709,406
446,164	**611,904**	Demand deposits	**235,583**	171,773
302,951	**411,517**	Saving deposits	**158,434**	116,636
3,428	**4,759**	Margin accounts	**1,832**	1,320
2,595,156	**3,042,694**		**1,171,437**	999,135
		Retail customers:		
302,951	**411,517**	Saving deposits	**158,434**	116,636
78,379	**57,681**	Term deposits	**22,207**	30,176
22,114	**23,395**	Demand deposits	**9,007**	8,514
		Corporate customers:		
1,764,234	**1,956,834**	Term deposits	**753,381**	679,230
424,049	**588,509**	Demand deposits	**226,576**	163,259
3,428	**4,758**	Other	**1,832**	1,320
2,595,156	**3,042,694**		**1,171,437**	999,135

B10 Deferred income

Effective 1 January 2011, the Bank has corrected the prior period error for the recognition of 'assets without consideration and condition'. Based on the guidance provided by IFRS 'Framework for the preparation and presentation of consolidated financial statements', management restated the prior years' financial statements in accordance with IAS 8 - Accounting Policies, Changes in Accounting Estimates and Errors.

Consequently, the fair value of land amounting to RO 7,000,000 which should have been recognised as income in the year 2008 at the time of receipt of land, is recognised in the retained earnings of the Bank.

B11 Other liabilities

2010 USD'000	2011 USD'000		2011 RO'000	2010 RO'000
40,878	**35,681**	Interest payable	**13,737**	15,738
13,855	**34,553**	Acceptances	**13,303**	5,334
4,883	**6,963**	Staff entitlements	**2,681**	1,880
3,636	**5,140**	Income tax payable	**1,979**	1,400
8,525	**18,229**	Other accruals and provisions	**7,018**	3,282
71,777	**100,566**		**38,718**	27,634
		Staff entitlements:		
579	**766**	End of service benefits	**295**	223
4,304	**6,197**	Other liabilities	**2,386**	1,657
4,883	**6,963**		**2,681**	1,880
		Movement in the end of service benefits liability:		
322	**579**	At 1 January	**223**	124
288	**390**	Expenses recognized in the profit or loss	**150**	111
(31)	**(203)**	End of service benefits paid	**(78)**	(12)
579	**766**	At 31 December	**295**	223

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2011 (continued)

B12 Subordinated loans

The Bank raised an unsecured subordinated loan of RO 50 million in 2010 with a maturity of 7 years. The instrument is unlisted, non-transferable, non-negotiable and non-convertible with no early call option. The instrument carries a fixed rate of interest of 6.5%. According to the Regulations of Central Bank of Oman, the subordinated loan is considered as Tier II capital for Capital Adequacy purposes. Principal amount of the subordinated loan is repayable on maturity while interest is payable semi-annually. The Bank is required to create a subordinated loan reserve equal to 20% of the issue value annually from August 2012 up till the maturity of the subordinated loans. This reserve will be created from retained earnings.

B13 Share capital

The authorised, issued and paid up share capital of the Bank is 1,000,000,000 shares of RO 0.100 each (2010 - 1,000,000,000 shares of RO 0.100 each).

As of 31 December 2011, the following shareholders held 10% or more of the Bank's capital, either individually or together with family members:

	Number of shares	*% Holding*
The Royal Court of Affairs	**145,690,340**	**14.57**

B14 Reserves

B14.1 Legal reserve

In accordance with the Commercial Companies Law of Oman of 1974, an annual appropriation of 10% of the net profit for the year is required to be made to legal reserve until such time that the accumulated reserve is equal to at least one third of the Bank's issued share capital.

B14.2 General reserve

The Board of Directors has decided to create a non distributable general reserve with the amount of RO ------- (2010 - RO 412,500) during the year.

B15 Fair value reserve

The fair value reserve includes the cumulative net change in the fair value of the available-for-sale investments net of applicable income tax until the investment is derecognised or impaired.

B16 Net assets per share

The calculation of net assets per share is based on net assets of RO 128,686,000 as at 31 December 2011 (2010 (restated) - RO 123,531,000) attributable to ordinary shareholders on 1,000,000,000 ordinary shares, being the number of shares outstanding as at 31 December 2011.

B17 Contingent liabilities and commitments

B17.1 Contingent liabilities

Standby letters of credit and guarantees commit the Bank to make payments on behalf of customers contingent upon the failure of the customer to perform under the terms of the contract.

2010 USD'000	**2011 USD'000**		**2011 RO'000**	2010 RO'000
307,283	**321,218**	Guarantees	**123,669**	118,304
159,961	**155,821**	Documentary letters of credit	**59,991**	61,585
467,244	**477,039**		**183,660**	179,889

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2011 (continued)

B17 Contingent liabilities and commitments (continued)

B17.1 Contingent liabilities (continued)

The table below analyses the concentration of contingent liabilities by economic sector:

2010 USD'000	**2011 USD'000**		**2011 RO'000**	2010 RO'000
175,158	**121,351**	Construction	**46,720**	67,436
66,286	**98,584**	Financial institution	**37,955**	25,520
118,649	**81,478**	Government	**31,369**	45,680
53,473	**74,566**	Services	**28,708**	20,587
23,242	**59,122**	International trade	**22,762**	8,948
20,517	**23,530**	Manufacturing	**9,059**	7,899
18	**4,870**	Transport and communication	**1,875**	7
9,901	**13,538**	Others	**5,212**	3,812
467,244	**477,039**		**183,660**	179,889

B17.2 Commitments

Contractual obligations including contracts for purchase and sale of foreign exchange are stated at fair value as commitments. Credit related commitments include commitments to extend credit, standby letters of credit and guarantees, which are designed to meet the requirements of the Bank's customers. Commitments to extend credit represent contractual commitments to make loans and revolving credits. Commitments generally have fixed expiry dates or other termination clauses and require the payment of a fee. Since commitments may expire without being drawn upon, the total contract amounts do not necessarily represent future cash obligations.

2010 USD'000	**2011 USD'000**		**2011 RO'000**	2010 RO'000
3,440	**2,744**	Capital commitments	**1,056**	1,324
541,435	**718,498**	Credit related commitments	**276,622**	208,453
544,875	**721,242**		**277,678**	209,777

B18 Related party transactions

In the ordinary course of business the Bank conducts transactions with certain of its directors, shareholders, senior management and companies in which they have a significant interest. These transactions are conducted on an arms length basis and are approved by the Bank's management and Board of Directors.

No specific provision has been established in respect of the loans given to related parties.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2011 (continued)

B18 Related party transactions (continued)

The aggregate amount of balances and the income and expenses generated with such related parties are as follows:

2010 USD'000	**2011 USD'000**		**2011 RO'000**	2010 RO'000
67,384	**219,127**	Loans and advances	**84,364**	25,943
61,371	**171,104**	Loans disbursed during the year	**65,875**	23,628
(30,891)	**(125,494)**	Loans repaid during the year	**(48,315)**	(11,893)
49,010	**222,696**	Deposits	**85,738**	18,869
107,569	**879,494**	Deposits received during the year	**338,605**	41,414
(108,919)	**(763,753)**	Deposits paid during the year	**(294,045)**	(41,934)
543	**5,608**	Interest income	**2,159**	209
(1,345)	**(5,561)**	Interest expense	**(2,141)**	(518)
		Senior Management compensation		
5,753	**8,065**	Salaries and other short term benefits	**3,105**	2,215
151	**506**	**Directors' sitting fees and remuneration**	**195**	58

B19 Fair value of financial instruments

The Bank considers that the fair value of financial instruments is not significantly different to their carrying value at each of those dates. The table below sets out the classification of each class of financial assets and liabilities, and their fair values as at 31 December 2011:

At 31 December 2011	Loans and receivables RO 000	Held to maturity RO 000	Available for sale RO 000	Total carrying amount RO 000	Fair value RO 000
Assets as per statement of financial position					
Cash and balances with Central Bank	**61,513**	**-**	**-**	**61,513**	**61,513**
Due from banks and other money market lendings	**231,560**	**-**	**-**	**231,560**	**231,560**
Loans and advances	**1,019,554**	**-**	**-**	**1,019,554**	**1,019,554**
Investment securities	**-**	**6,540**	**79,119**	**85,659**	**85,659**
Other assets (excluding prepayments)	**18,042**	**-**	**-**	**18,042**	**18,042**
Total	**1,330,669**	**6,540**	**79,119**	**1,416,328**	**1,416,328**

	Financial Liabilities	
	Total carrying amount RO 000	**Fair value RO 000**
Liabilities as per statement of financial position		
Due to banks and other money market borrowings	**43,136**	**43,136**
Customers' deposits	**1,171,437**	**1,171,437**
Other liabilities (excluding accruals)	**36,012**	**36,012**
Subordinated loans	**50,000**	**50,000**
Total	**1,300,585**	**1,300,585**

At 31 December 2010	Loans and receivables RO 000	Held to maturity RO 000	Available for sale RO 000	Total carrying amount RO 000	Fair value RO 000
Assets as per statement of financial position					
Cash and balances with Central Bank	105,022	-	-	105,022	105,022
Due from banks and other money market lendings	119,462	-	-	119,462	119,462
Loans and advances	903,034	-	-	903,034	903,034
Investment securities	-	4,040	103,109	107,149	107,149
Other assets (excluding prepayments)	9,055	-	-	9,055	9,055
Total	1,136,573	4,040	103,109	1,243,722	1,243,722

	Financial Liabilities	
	Total carrying amount RO 000	Total carrying amount RO 000
Liabilities as per statement of financial position		
Due to banks and other money market deposits	51,277	51,277
Certificates of deposit	7,038	7,038
Customers' deposits	999,135	999,135
Other liabilities (excluding accruals)	26,234	26,234
Subordinated loans	50,000	50,000
Total	1,133,684	1,133,684

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2011 (continued)

B19 Fair value of financial instruments (continued)

At 31 December 2011	Loans and receivables USD 000	Held to maturity USD 000	Available for sale USD 000	Total carrying amount USD 000	Fair value USD 000
Assets as per statement of financial position					
Cash and balances with Central Bank	**159,774**	**-**	**-**	**159,774**	**159,774**
Due from banks and other money market lendings	**601,455**	**-**	**-**	**601,455**	**601,455**
Loans and advances	**2,648,192**	**-**	**-**	**2,648,192**	**2,648,192**
Investment securities	**-**	**16,987**	**205,504**	**222,491**	**222,491**
Other assets (excluding prepayments)	**46,862**	**-**	**-**	**46,862**	**46,862**
Total	**3,456,283**	**16,987**	**205,504**	**3,678,774**	**3,678,774**

	Financial Liabilities	
	Total carrying amount USD 000	**Fair value USD 000**
Liabilities as per statement of financial position		
Due to banks and other money market borrowings	**112,042**	**112,042**
Customers' deposits	**3,042,694**	**3,042,694**
Other liabilities (excluding accruals)	**93,538**	**93,538**
Subordinated loans	**129,870**	**129,870**
Total	**3,378,144**	**3,378,144**

At 31 December 2010	Loans and receivables USD 000	Held to maturity USD 000	Available for sale USD 000	Total carrying amount USD 000	Fair value USD 000
Assets as per statement of financial position					
Cash and balances with Central Bank	272,784	-	-	272,784	272,784
Due from banks and other money market lendings	310,291	-	-	310,291	310,291
Loans and advances	2,345,544	-	-	2,345,544	2,345,544
Investment securities	-	10,493	267,816	278,309	278,309
Other assets (excluding prepayments)	23,519	-	-	23,519	23,519
Total	2,952,138	10,493	267,816	3,230,447	3,230,447

	Financial Liabilities	
	Total carrying amount USD 000	Total carrying amount USD 000
Liabilities as per statement of financial position		
Due to banks and other money market deposits	133,188	133,188
Certificates of deposit	18,280	18,280
Customers' deposits	2,595,156	2,595,156
Other liabilities (excluding accruals)	68,140	68,140
Subordinated loans	129,870	129,870
Total	2,944,634	2,944,634

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2011 (continued)

B19 Fair value of financial instruments (continued)

Estimation of fair values:

The following summarises the major methods and assumptions used in estimating the fair values of assets and liabilities.

Loans and advances

Fair value is calculated based on discounted expected future principal and interest cash flows. Loan repayments are assumed to occur at contractual repayment dates, where applicable. For loans that do not have fixed repayment dates or that are subject to prepayment risk, repayments are estimated based on experience in previous periods when interest rates were at levels similar to current levels, adjusted for any differences in interest rate outlook. Expected future cash flows are estimated considering credit risk and any indication of impairment. Expected future cash flows for homogeneous categories of loans are estimated on a portfolio basis and discounted at current rates offered for similar loans to new borrowers with similar credit profiles. The estimated fair values of loans reflect changes in credit status since the loans were made and changes in interest rates in the case of fixed rate loans.

Investments carried at amortised cost and derivatives

Fair value is based on quoted market prices at the reporting date without any deduction for transaction costs. If a quoted market price is not available, fair value is estimated based on discounted cash flow and other valuation techniques.

Where discounted cash flow techniques are used, estimated future cash flows are based on management's best estimates and the discount rate is a market related rate for a similar instrument at the reporting date.

Bank and customer deposits

For demand deposits and deposits with no defined maturities, fair value is taken to be the amount payable on demand at the reporting date. The estimated fair value of fixed-maturity deposits, including certificates of deposit, is based on discounted cash flows using rates currently offered for deposits of similar remaining maturities. The value of long-term relationships with depositors is not taken into account in estimating fair values.

Other on-balance sheet financial instruments

The fair values of all on-balance sheet financial instruments are considered to approximate their book values.

Off-balance sheet financial instruments

No fair value adjustment is made with respect to credit-related off-balance sheet financial instruments, which include commitments to extend credit, standby letters of credit and guarantees, as the related future income streams materially reflect contractual fees and commissions actually charged at the reporting date for agreements of similar credit standing and maturity.

Foreign exchange contracts are valued based on market prices. The market value adjustments in respect of foreign exchange contracts are included in the book values of other assets and other liabilities.

Valuation of financial instruments:

The Bank measures fair values using the following fair value hierarchy that reflects the significance of the inputs used in making the measurements:

Level 1 - Quoted prices (unadjusted) in active markets for identical assets or liabilities.

Level 2- Inputs other than quoted prices included within level 1 that are observable for the asset or liability, either directly (that is, as prices) or indirectly (that is, derived from prices).

Level 3 - Inputs for the asset or liability that are not based on observable market data (that is, unobservable inputs).

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2011 (continued)

B19 Fair value of financial instruments (continued)

The table below analyses financial instruments measured at fair value at the end of the reporting period:

	31 December 2011			31 December 2010		
	Investment securities RO '000	Derivatives RO '000	Total RO '000	Investment securities RO '000	Derivatives RO '000	Total RO '000
Level 1	5,525	-	5,525	8,262	-	8,262
Level 2	73,594	59	73,653	94,847	47	94,893
Level 3	6,540	-	6,540	4,040	-	4,040
	85,659	59	85,718	107,149	47	107,195

	31 December 2011			31 December 2010		
	Investment securities USD '000	Derivatives USD '000	Total USD '000	Investment securities USD '000	Derivatives USD '000	Total USD '000
Level 1	14,351	-	14,351	21,460	-	21,460
Level 2	191,153	153	191,306	246,356	119	246,475
Level 3	16,987	-	16,987	10,493	-	10,493
	222,491	153	222,644	278,309	119	278,428

B20 Derivatives

In the ordinary course of business the Bank enters into various types of transactions that involve derivative financial instruments. A derivative financial instrument is a financial contract between two parties where payments are dependent upon movements in price in one or more underlying financial instrument, reference rate or index. These derivatives are stated at fair value. The fair value of a derivative is the equivalent of the unrealised gain or loss from marking to market the derivative using prevailing market rates or internal pricing models. Unrealised gains or losses are included in the statement of comprehensive income. The derivative financial instruments used by the Bank are described below:

B20.1 Derivative product types

Forwards and futures are contractual agreements to either buy or sell a specified currency, commodity or financial instrument at a specific price and date in the future.

Swaps are contractual agreements between two parties to exchange interest or foreign currency differentials based on a specific notional amount. For interest rate swaps, counter parties generally exchange fixed and floating rate interest payments based on a notional value in a single currency.

Options are contractual agreements that convey the right, but not the obligation, to either buy or sell a specific amount of a commodity, foreign currency or financial instrument at a fixed price, either at a fixed future date or at any time within a specified period.

B20.2 Derivatives held or issued for hedging purposes

As part of its asset and liability management the Bank uses derivatives for hedging purposes in order to reduce its exposure to currency and interest rate risks. This is achieved by hedging specific financial instruments and forecasted transactions as well as strategic hedging against overall statement of financial position exposures.

The Bank uses forward foreign exchange contracts, to hedge against specifically identified currency risks. The Bank uses forward foreign exchange contracts to hedge against exposures in various currencies to meet the net open position limit as specified by Central Bank of Oman.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2011 (continued)

B20 Derivatives (continued)

B20.2 Derivatives held or issued for hedging purposes (continued)

For interest rate risk strategic hedging is carried out by monitoring the re-pricing of financial assets and liabilities and entering into interest rate swaps to hedge a proportion of the interest rate exposure. As strategic hedging does not qualify for special hedge accounting, the related derivatives are accounted for as trading instruments.

The table below shows the notional amounts of derivative financial instruments as on the reporting date, which are the amount of a derivative's underlying asset, reference rate or index and is the basis upon which changes in the value of derivatives are measured.

At 31 December 2011

		Notional amounts by term to maturity		
	Notional amount	Within 3 months	3 - 12 months	1 - 5 years
	RO'000	RO'000	RO'000	RO'000
Forward foreign exchange purchase contracts	381,474	330,125	51,349	-
Forward foreign exchange sales contracts	381,647	330,238	51,409	-
	USD'000	USD'000	USD'000	USD'000
Forward foreign exchange purchase contracts	990,842	857,468	133,374	-
Forward foreign exchange sales contracts	991,291	857,761	133,530	-

At 31 December 2010

		Notional amounts by term to maturity		
	Notional amount	Within 3 months	3 - 12 months	1 - 5 years
	RO'000	RO'000	RO'000	RO'000
Forward foreign exchange purchase contracts	329,299	253,767	75,532	-
Forward foreign exchange sales contracts	329,883	254,302	75,581	-
	USD'000	USD'000	USD'000	USD'000
Forward foreign exchange purchase contracts	855,322	659,135	196,187	-
Forward foreign exchange sales contracts	856,839	660,525	196,314	-

B21 Proposed dividend

For the year 2011, the Board of Directors have proposed a cash dividend of RO 8 million, i.e.8% of the share capital and 8 baizas per share (2010 - RO RO 6 million, i.e. 6% of the share capital and 6 baizas per share). The proposed cash dividend is subject to formal approval of the shareholders at the Annual General Meeting.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2011 (continued)

C1 Interest income

2010 USD'000	2011 USD'000		2011 RO'000	2010 RO'000
146,917	**149,995**	Loans and advances to customers	**57,748**	56,563
3,460	**5,761**	Due to banks and other money market lendings	**2,218**	1,332
1,303	**2,205**	Investment securities	**849**	502
151,680	**157,961**		**60,815**	58,397

C2 Interest expense

2010 USD'000	2011 USD'000		2011 RO'000	2010 RO'000
60,145	**54,673**	Customers' deposits	**21,049**	23,156
3,211	**8,441**	Subordinated loans	**3,250**	1,236
4,117	**4,496**	Due to banks and other money market borrowings	**1,731**	1,585
4,740	**73**	Certificates of deposits	**28**	1,825
72,213	**67,683**		**26,058**	27,802

C3 Other operating income

2010 USD'000	2011 USD'000		2011 RO'000	2010 RO'000
10,010	**17,283**	Fees and commission	**6,654**	3,854
1,797	**2,255**	Net gains from foreign exchange dealings	**868**	692
230	**1,868**	Dividend income	**719**	88
5	**488**	Realised gains on investments	**188**	2
12,042	**21,894**		**8,429**	4,636

C4 Other operating expenses

2010 USD'000	2011 USD'000		2011 RO'000	2010 RO'000
11,976	**14,247**	Operating and administration costs	**5,485**	4,611
3,512	**4,135**	Establishment costs	**1,592**	1,352
151	**506**	Directors' sitting fees	**195**	58
15,639	**18,888**		**7,272**	6,021

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2011 (continued)

C5 Income tax

a) Recognised in the statement of comprehensive income

2010 USD'000	2011 USD'000		2011 RO'000	2010 RO'000
3,634	**4,927**	Current tax	**1,897**	1,399
54	**335**	Deferred tax expense	**129**	21
3,688	**5,262**	Total tax expenses	**2,026**	1,420

The Bank is liable to income tax for the year 2011 in accordance with the income tax laws of the Sultanate of Oman at the rate of 12% on taxable profits in excess of RO 30,000.

b) Reconciliation

2010 USD'000	2011 USD'000		2011 RO'000	2010 RO'000
30,233	**42,918**	Accounting profit for the year	**16,523**	11,640
3,618	**5,151**	Income tax	**1,983**	1,393
38	**5**	Non deductible expenses	**2**	15
(23)	**(229)**	Tax exempt income	**(88)**	(9)
55	**335**	Current year deferred tax	**129**	21
3,688	**5,262**	Income tax expense	**2,026**	1,420

c) Deferred tax asset

2010 USD'000	2011 USD'000		2011 RO'000	2010 RO'000
29	**231**	Fair value adjustment on investments	**89**	11
29	**231**		**89**	11

d) Tax assessment

The assessments of the Bank for the years 2007 to 2010 have not yet been agreed with the Secretariat General for Taxation at the Ministry of Finance. The Bank is of the opinion that additional taxes, if any, related to the open tax years would not be significant to the financial position of the Bank as at 31 December 2011.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2011 (continued)

C6 Basic earnings per share

Earnings per share is calculated by dividing the net profit for the year by the weighted average number of shares outstanding during the year.

2010 USD'000	2011 USD'000		2011 RO'000	2010 RO'000
26,545	**37,656**	Net profit for the year	**14,497**	10,220
1,000,000	**1,000,000**	Weighted average number of shares of RO 0.100 each outstanding during the year (in thousands)	**1,000,000**	1,000,000
		Net earnings per share for the year (in baizas)	**14.50**	10.22
2.66	**3.77**	Net earnings per share for the year (in cents)		

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

D Financial risk management

The primary objective of the risk management system is to safeguard the Bank's capital, its financial resources and from various risks. The Bank has exposure to the following risk from its use of financial instruments:

- Credit risk
- Liquidity risk
- Market risk
- Operational risk

The Board of Directors has overall responsibility for the establishment and oversight of the Bank's risk management framework. The Board has established the Asset and Liability Committee (ALCO) and Risk Management Committee, which are responsible for developing and monitoring the Bank's risk management policies in their specified areas. All board committees report regularly to the Board of Directors on their activities.

The Bank's risk management policies are established to identify and analyse the risks faced by the Bank, to set appropriate risk limits and controls, and to monitor risks and adherence to the limits. Risk management polices and systems are reviewed regularly to reflect changes in market conditions, products and services offered. The Bank through its training and management procedures, aims to develop a constructive control environment, in which all employees understand their roles and obligations.

The Bank's Audit Committee is responsible for monitoring compliance with the Bank's risk management policies and procedures, and for reviewing the adequacy of the risk management framework in relation to the risks faced by the Bank. The Bank's Audit Committee is assisted in these functions by Internal Audit department. Internal Audit department undertakes both regular and ad-hoc reviews of risk management controls and procedures, the results of which are reported to the Audit Committee.

D1 Credit risk

Credit risk is the risk of financial loss to the Bank if a customer or counterparty to a financial instrument fails to meet its contractual obligations, and arises principally from the Bank's loans and advances to customers, other banks and investment securities. For risk management reporting purposes the Bank considers and consolidates all elements of credit risk exposure (such as individual obligor default risk, country and sector risk)

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2011 (continued)

D Financial risk management (continued)

D1 Credit risk (continued)

D1.1 Management of credit risk (continued)

The Board of Directors has delegated responsibility for the monitoring of credit risk to its Risk Management Committee. A separate Risk Management Department, reporting to the chairman of the Risk Management Committee, is responsible for the following:

- formulating credit risk policies in consultation with business units, covering collateral requirements, credit assessment, risk grading and reporting, documentary and legal procedures, and compliance with regulatory and statutory requirements.
- establishing the authorization structure for the approval and renewal of credit facilities.
- reviewing and assessing credit risk. The Board's Risk Management Committee assesses all credit exposures in excess of designated limits, prior to facilities being committed to customers by the business unit concerned. Renewals and reviews of facilities are subject to the same review process. The process also includes approval by Risk of borrower ratings arrived at by the business units.
- limiting concentrations of exposure to counterparties, geographies and industries (for loans and advances), and by issuer, market liquidity and country (for investment securities).
- developing and maintaining the Bank's risk grading in order to categorise exposures according to the degree of risk of financial loss faced and to focus management on the attendant risks.
- reviewing compliance of business units with agreed exposure limits, including those for selected industries, country risk and product types. Ensuring always to be with in the single obligor limit and also within the concentration risk limit, for various sectors, which are continuously monitored.
- providing advice, guidance and specialist skills to business units to promote best practice throughout the Bank in the management of credit risk.

Each business unit is required to implement Bank's credit risk policies and procedures, with credit approval authorities delegated from the Risk Management Committee. Business units have their counter parts in risk management, having specialised expertise in managing risks typical to these business units. Regular audits of business units and the Bank's credit processes are undertaken by Internal Audit Department.

The Bank employs a range of policies and practices to mitigate credit risk. The Bank follows a risk mitigation practice of identifying business cash flows as the primary take out for the advances extended. These cash flows are then tested for sustainability over the tenor of the credit facility and a suitable mechanism is put in place to capture the same into the client account with the Bank. To cover unforeseen risk, which dry up the cash flows, additional tangible securities are taken such as real estate or equity shares. The Bank implements guidelines on the acceptability of specific classes of collateral credit risk mitigation. The principal types of collaterals for loans and advances are:

- mortgages over properties;
- charges over business assets such as premises inventory and accounts receivable;
- charges over financial instruments such as debt securities and equities.

Longer-term finance and lending to corporate entities are generally secured; revolving individual credit facilities are generally unsecured from a collateral perspective, whereas credit risk is primarily mitigated through capture of business cash flows. In addition, in order to minimise the credit loss, the Bank will seek additional collateral from the counterparty as soon as impairment indicators are noticed for the relevant individual loans and advances. Collateral held as security for financial assets other than loans and advances, is determined by the nature of the instrument. Debt securities, treasury and other eligible bills are generally unsecured.

All loans and advances of the Bank are regularly monitored to ensure compliance with the stipulated repayment terms. Those loans and advances are classified into one of the 5 risk classification categories: Standard, Special Mention, Substandard, Doubtful, and Loss – as stipulated by Central Bank of Oman regulations and guidelines. The responsibility for identifying problem accounts and classifying them rests with business line function.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2011 (continued)

D Financial risk management (continued)

D1 Credit risk (continued)

D1.2 Exposure to credit risk

The credit exposure of the Bank as on the reporting date is as follows:

	2011 Loans and advances-Gross RO'000	2011 Due from banks and other money market lendings RO'000	2011 Investment securities RO'000	2010 Loans and advances-Gross RO'000	2010 Due from banks and other money market borrowings RO'000	2010 Investment securities RO'000
Carrying amount	1,040,927	231,560	71,369	920,140	119,462	98,460
Past due but not impaired						
1-30 days	15,783	-	-	3,305	-	-
31-60 days	2,995	-	-	5,762	-	-
61-89 days	1,360	-	-	4,114	-	-
	20,138	-	-	13,181	-	-
Past due and impaired	15,999	-	-	8,051	-	-
Neither past due nor impaired	1,004,790	231,560	71,369	898,908	119,462	98,460

	2011 Loans and advances-Gross USD'000	2011 Due from banks and other money market lendings USD'000	2011 Investment securities USD'000	2010 Loans and advances-Gross USD'000	2010 Due from banks and other money market borrowings USD'000	2010 Investment securities USD'000
Carrying amount	2,703,706	601,455	185,374	2,389,975	310,291	255,740
Past due but not impaired						
1-30 days	40,995	-	-	8,584	-	-
31-60 days	7,779	-	-	14,966	-	-
61-89 days	3,532	-	-	10,686	-	-
	52,306	-	-	34,236	-	-
Past due and impaired	41,556	-	-	20,912	-	-
Neither past due nor impaired	2,609,844	601,455	185,374	2,334,827	310,291	255,740

Total impairment above includes impairment for off-balance sheet exposures as well.

Restructured and rescheduled loans during the year on standard portfolio amounted to RO 638,066 and on classified portfolio amounted to RO 19,704,027.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2011 (continued)

D Financial risk management (continued)

D1 Credit risk (continued)

D1.2 Exposure to credit risk

Maximum exposure to credit risk before collateral held or other credit enhancements for all on-balance sheet assets are based on net carrying amounts as reported in the statement of financial position.

The maximum credit risk exposures relating to off-balance sheet items calculated as per Basel II guidelines are provided in note D5
. The amounts represented in the note D5 represent a worst case scenario of credit risk exposure as of 31 December 2011 and 2010, without taking into account of any collateral held or other credit enhancements attached.

D1.3 Credit rating analysis

The table below presents an analysis of debt securities, treasury bills and other eligible bills by rating agency designation at 31 December 2011, based on Moody's ratings or equivalent.

2010 USD'000	**2011 USD'000**		**2011 RO'000**	2010 RO'000
4,000	**4,000**	Baa1 to Baa3	**1,540**	1,540
6,494	**17,413**	Unrated bonds	**6,704**	2,500
245,247	**163,961**	Sovereign treasury bills	**63,125**	94,420

The following table shows the gross placements held with counterparties at the reporting date:

2010 USD'000	**2011 USD'000**		**2011 RO'000**	2010 RO'000
16,390	**163,244**	Aaa to Aa3	**62,849**	6,310
87,514	**186,600**	A1 to A3	**71,841**	33,693
203,790	**251,525**	Baa1 to Baa3	**96,837**	78,459
87,514	**186,600**	Unrated	**33**	1,000

The Bank performs an independent assessment based on quantitative and qualitative factors in cases where a bank is unrated.

D1.4 Impaired loans and securities

These are loans and securities for which the Bank determines that it is probable that it will be unable to collect all the principal and interest due according to the contractual terms of the loan /securities agreement.

D1.4.a Past due but not impaired

These are loans and securities where contractual interest or principal payments are past due but the Bank believes that impairment is not appropriate on the basis of the level of security /collateral available and /or the stage of collection of amounts owed by the Bank.

D1.4.b Loans with renegotiated terms

Loans with renegotiated terms are loans that have been restructured due to deterioration in the borrower's financial position and where the Bank has made concessions that it would not otherwise consider. Once the loan is restructured it remains in this category independent of satisfactory performance after restructuring.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2011 (continued)

D Financial risk management (continued)

D1 Credit risk (continued)

D1.4 Impaired loans and securities (continued)

D1.4.c Allowances for impairment

The Bank establishes an allowance for impairment losses account that represents its estimate of incurred losses in its loan portfolio. The main components of this allowance are specific loss components that relate to individually significant exposures, and a collective loan loss allowance established for group of homogenous assets in respect of losses that have been incurred but have not been identified on loans subject to individual assessment for impairment.

D1.4.d Write off policy

The Bank writes off a loan/security balance (and any related allowances for impairment losses) when the Bank determines that the loan/security is uncollectible. This determination is reached after considering information such as the occurrence of significant changes in the borrower/issuer's financial position such that the borrower/issuer can no longer repay the obligation, or that proceeds from the collateral will not be sufficient to pay back the entire exposure. For smaller balance standardised loans, charge off decisions generally are based on a product specific past due status.

Set out below is an analysis of gross and net (of allowances for impairment) amounts of individually impaired assets by risk classification.

	2011		2010	
	Loans and advances		Loans and advances	
Particulars	**Gross**	**Net**	Gross	Net
	RO'000	**RO'000**	RO'000	RO'000
Sub-standard	**7,178**	**5,186**	1,669	1,223
Doubtful	**2,279**	**1,099**	1,213	577
Loss	**6,542**	**1,900**	5,169	1,824
	15,999	**8,185**	8,051	3,624
Particulars	**Gross**	**Net**	Gross	Net
	USD'000	**USD'000**	USD'000	USD'000
Sub-standard	**18,644**	**13,470**	4,335	3,177
Doubtful	**5,919**	**2,855**	3,151	1,499
Loss	**16,993**	**4,935**	13,426	4,738
	41,556	**21,260**	20,912	9,414

D 1.5 Collateral securities

The Bank holds collateral against the loans and advances to customers in the form of mortgage interests over property, other registered securities, assets and guarantees. Estimates of fair value are based on the value of the collateral assessed at the time of borrowing and updated once in three years, except when a loan is individually assessed as impaired. The shares of MSM listed companies which are taken as securities are valued on fortnightly basis, unless there is significant fluctuations whereby the valuation is done on daily basis to manage the risks of extreme volatility.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2011 (continued)

D Financial risk management (continued)

D1 Credit risk (continued)

D 1.5 Collateral securities (continued)

An estimate of the fair value of collateral and other security enhancements held against loans and advances is shown below:

2010 USD'000	2011 USD'000		2011 RO'000	2010 RO'000
		Against past due but not impaired		
13,322	**80,771**	Property	**31,097**	5,129
1,338	**1,177**	Fixed deposits	**453**	515
-	**2,304**	Equity	**887**	-
14,660	**84,252**		**32,437**	5,644
		Against past due and impaired		
5,943	**7,571**	Property	**2,915**	2,288
		Against neither past due nor impaired		
330,494	**333,039**	Property	**128,220**	127,240
187,779	**209,312**	Commercial mortgage	**80,585**	72,295
74,426	**63,099**	Fixed deposits	**24,293**	28,654
53,678	**52,649**	Equity	**20,270**	20,666
48,449	**37,094**	Guarantees	**14,281**	18,653
694,826	**695,193**		**267,649**	267,508
715,429	**787,016**		**303,001**	275,440

D1.6 Settlement Risk

Settlement risk is the risk of loss due to the failure of a party to honour its obligations to deliver cash, securities or other assets as contractually agreed on the day of settlement.

In foreign exchange trades, though there is fulfilment of both the legs of the transaction on the settlement date as is common practice between trading partners (free settlement), there will be risk on account of different time zones. In these cases, the settlement risk is mitigated through the execution of bilateral payment netting agreements.

D1.7 Concentrations

Concentrations of credit risk arise when a number of counter parties are engaged in similar business activities or activities in the same geographic region or have similar economic features that would cause their ability to meet contractual obligations to be affected similarly 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 Bank seeks to manage its credit risk exposure through diversification of lending activities to avoid undue concentrations of risks with individuals or group of customers in specific locations or businesses. It also obtains appropriate security.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2011 (continued)

D Financial risk management (continued)

D1 Credit risk (continued)

D1.7 Concentrations (continued)

	2011 Loans and advances-Gross	2011 Due from banks and other money market lendings	2011 Investment securities	2010 Loans and advances-Gross	2010 Due from banks and other money market lendings	2010 Investment securities
	RO'000	RO'000	RO'000	RO'000	RO'000	RO'000
Concentration by sector						
Corporate	672,978	-	22,534	555,582	-	12,729
Personal	367,949	-	-	364,558	-	-
Sovereign	-	-	63,125	-	-	94,420
Banks	-	231,560	-	-	119,462	-
	1,040,927	231,560	85,659	920,140	119,462	107,149
Concentration by location						
Middle east	1,014,362	104,361	80,041	920,140	45,207	106,755
Europe	-	55,670	4,150	-	37,328	-
North America	-	4,075	1,468	-	4,090	394
Asia	26,565	67,449	-	-	32,822	-
Australia	-	5	-	-	15	-
	1,040,927	231,560	85,659	920,140	119,462	107,149
	USD'000	USD'000	USD'000	USD'000	USD'000	USD'000
Concentration by sector						
Corporate	1,747,995	-	58,530	1,443,070	-	33,063
Personal	955,711	-	-	946,905	-	-
Sovereign	-	-	163,961	-	-	245,246
Banks	-	601,455	-	-	310,291	-
	2,703,706	601,455	222,491	2,389,975	310,291	278,309
Concentration by location						
Middle east	2,634,711	271,069	207,899	2,389,975	117,421	277,286
Europe	-	144,597	10,779	-	96,956	-
North America	-	10,584	3,813	-	10,623	1,023
Asia	69,000	175,192	-	-	85,252	-
Australia	-	13	-	-	39	-
	2,703,706	601,455	222,491	2,389,975	310,291	278,309

Concentration by location for loans and advances is measured based on the location of the entity holding the asset, which has a high correlation with the location of the borrower. Concentration by location for investment securities is measured based on the location of the issuer of the security. The Bank seeks to manage its credit risk exposure through diversification of lending activities to avoid undue concentrations of risk with banks or customers in a specific currency. It also obtains security when appropriate. An analysis of the Bank's gross exposure to relevant segments is provided in note D6.

D Financial risk management (continued)

D2 Liquidity risk

Liquidity risk is the risk that the Bank will encounter difficulty in meeting its obligations associated with its financial liabilities that are settled by delivering cash or another financial asset.

D2.1 Management of liquidity risk

The Bank's approach to managing liquidity is to ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions without incurring unacceptable losses or risking damage to the Bank's reputation. The Bank has put in place an approved Contingency Liquidity Plan to facilitate management of liquidity

Liquidity risk is managed by the Bank through closely monitoring the liquidity gap against the limit fixed.

Adequate liquidity is ensured by Treasury, which receives information from other business units regarding the liquidity profile of their financial assets and liabilities and details of other projected cash flows arising from projected future business. Central Treasury then maintains a portfolio of short-term liquid assets, largely made up of short-term liquid investment securities, loans and advances to banks and other inter-bank facilities, to ensure that sufficient liquidity is maintained within the Bank as a whole. In this process due care is taken to ensure that the Bank complies with all the Central Bank regulations.

All liquidity policies and procedures are subject to review and approved by ALCO.

D2.2 Exposure to liquidity risk

The lending ratio, which is the ratio of the total loans and advances to customer deposits and capital, is monitored on a daily basis in line with the regulatory guidelines. Internally the lending ratio is set at a more conservative basis than required by regulation. The Bank also manages its liquidity risk on a monthly basis monitoring the liquid ratio which is a ratio of net liquid assets to total assets. For this purpose net liquid assets are considered as including cash and cash equivalents and investment grade debt securities for which there is an active and liquid market.

Details of the reported lending and liquid ratio as at 31 December 2011 were as follows:

	2011		2010	
	Lending ratio	**Liquid ratio**	Lending ratio	Liquid ratio
Average for the year	**84.28%**	**21.46%**	84.40%	21.64%
Maximum for the year	**85.33%**	**26.43%**	87.04%	22.45%
Minimum for the year	**83.42%**	**17.43%**	80.91%	24.80%

The table below summarises the maturity profile of the Bank's liabilities as on the reporting date based on contractual repayment arrangements. The contractual maturities of assets and liabilities have been determined on the basis of the remaining period at the statement of financial position date to the contractual maturity date and do not take account of the effective maturities as indicated by the Bank's deposit retention history and the availability of liquid funds.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2011 (continued)

D Financial risk management (continued)

D2 Liquidity risk (continued)

D2.2 Exposure to liquidity risk (continued)

	Within three months RO'000	Four months to 12 months RO'000	One to three years RO'000	More than three years RO'000	Total RO'000
31 December 2011					
Assets					
Cash and balances with Central Banks	23,423	20,566	6,883	10,641	61,513
Due from banks and other money market lendings	158,025	73,535	-	-	231,560
Loans and advances	254,441	109,096	142,167	513,850	1,019,554
Investment securities	63,126	-	14,289	8,244	85,659
Property and equipment and other assets	16,454	2,740	100	14,397	33,691
Total assets	515,469	205,937	163,439	547,132	1,431,977
Liabilities and equity					
Due to banks and other money market borrowings	43,136	-	-	-	43,136
Customers' deposits	342,622	453,452	151,761	223,602	1,171,437
Other liabilities	27,243	8,814	1,187	1,474	38,718
Subordinated loans	-	-	-	50,000	50,000
Shareholders' funds	-	-	-	128,686	128,686
Total liabilities and equity	413,003	462,266	152,948	403,762	1,431,977

	Within three months USD'000	Four months to 12 months USD'000	One to three years USD'000	More than three years USD'000	Total USD'000
31 December 2011					
Assets					
Cash and balances with Central Banks	60,839	53,418	17,878	27,639	159,774
Due from banks and other money market lendings	410,455	191,000	-	-	601,455
Loans and advances	660,886	283,366	369,265	1,334,675	2,648,192
Investment securities	163,964	-	37,114	21,413	222,491
Property and equipment and other assets	42,737	7,117	260	37,394	87,509
Total assets	1,338,881	534,901	424,517	1,421,122	3,719,421
Liabilities and equity					
Due to banks and other money market borrowings	112,042	-	-	-	112,042
Customers' deposits	889,927	1,177,797	394,184	580,786	3,042,694
Other liabilities	70,761	22,894	3,083	3,828	100,566
Subordinated loans	-	-	-	129,870	129,870
Shareholders' funds	-	-	-	334,249	334,249
Total liabilities and equity	1,072,730	1,200,691	397,267	1,048,733	3,719,421

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2011 (continued)

D Financial risk management (continued)

D2 Liquidity risk (continued)

D2.2 Exposure to liquidity risk (continued)

31 December 2010	Within three months RO'000	Four months to 12 months RO'000	One to three years RO'000	More than three years RO'000	Total RO'000
Assets					
Cash and balances with Central Banks	67,686	14,345	13,335	9,656	105,022
Due from banks and other money market lendings	102,137	15,400	1,925	-	119,462
Loans and advances	180,724	102,019	131,226	489,065	903,034
Investment securities	94,420	-	8,689	4,040	107,149
Property and equipment and other assets	9,788	148	73	13,939	23,948
Total assets	454,755	131,912	155,248	516,700	1,258,615
Liabilities and equity					
Due to banks and other money market borrowings	51,277	-	-	-	51,277
Customers' deposits and certificates of deposit	283,402	285,762	259,092	177,917	1,006,173
Other liabilities	9,310	5,646	4,395	8,283	27,634
Subordinated loans	-	-	-	50,000	50,000
Shareholders' funds	-	-	-	123,531	123,531
Total liabilities and equity	343,989	291,408	263,487	359,731	1,258,615

31 December 2010	Within three months USD'000	Four months to 12 months USD'000	One to three years USD'000	More than three years USD'000	Total USD'000
Assets					
Cash and balances with Central Banks	175,808	37,260	34,636	25,080	272,784
Due from banks and other money market lendings	265,291	40,000	5,000	-	310,291
Loans and advances	469,413	264,984	340,847	1,270,300	2,345,544
Investment securities	245,247	-	22,569	10,493	278,309
Property and equipment and other assets	25,423	384	190	36,205	62,202
Total assets	1,181,182	342,628	403,242	1,342,078	3,269,130
Liabilities and equity					
Due to banks and other money market borrowings	133,188	-	-	-	133,188
Customers' deposits and certificates of deposit	736,109	742,239	672,966	462,122	2,613,436
Other liabilities	24,182	14,665	11,416	21,514	71,777
Subordinated loans	-	-	-	129,870	129,870
Shareholders' funds	-	-	-	320,859	320,859
Total liabilities and equity	893,479	756,904	684,382	934,365	3,269,130

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2011 (continued)

D Financial risk management (continued)

D2 Liquidity risk (continued)

D2.2 Exposure to liquidity risk (continued)

The Bank prepares a liquidity gap report to monitor the Bank's short term liquidity position on the Rial denominated assets and liabilities in a time horizon spanning one month. The gap is adjusted for availability of instruments for repo or refinance and also for unavailed committed lines of credit, if any. This statement of short term liquidity is to be reported to the ALCO every month and onward reported to Risk Management Committee.

D3 Market risk

Market risk is the exposure to loss resulting from the changes in the interest rates, foreign currency exchange rates, equity prices and commodity prices. The objective of market risk management is to manage and control market risk exposures within acceptable parameters, while optimising the return to risk.

D3.1 Measurement of market risk

The Bank is mainly engaged in Spots, Forwards and Currency swaps. Since the positions are taken mainly for customer transactions, the complexity is further reduced. In view of above, the Bank measures and controls the risk by using a limit framework. As and when the Bank enters into more complex derivatives, it will have more sophisticated models and techniques to measure market risk, supported by suitable mechanism.

D3.2 Management of market risks

The Bank separates its exposure to market risk between trading and non trading portfolios. Trading portfolios include all positions arising from market making and proprietary position taking, together with financial assets and liabilities that are managed on a fair value basis.

All foreign exchange risk within the Bank is transferred by Central Treasury to the trading book. Accordingly, the foreign exchange position is treated as a part of the Bank's trading portfolio for risk management purposes. Foreign currency risk is monitored and managed by the Bank by establishment of Mid Office to monitor the market risk, and the risk is managed by putting in place Market Risk Management Policy, and implementing limit framework, reporting tools like Currency Position Report, Risk Analysis of Currency Position, Breach Analysis Report, and Dealer Limit Breach report.

Overall authority for market risk is vested in ALCO. The risk management function is responsible for development of detailed risk management policies (subject to approval by ALCO and Risk Management Committee of the Board). The Market Risk Policy is periodically reviewed to keep it up to date with the market developments.

D3.3 Exposure to interest rate risk – non trading portfolios

Interest rate risk arises from the possibility that changes in interest rates will affect future profitability or the fair values of financial instruments. The Bank is exposed to interest rate risk as a result of mismatches of interest rate and re-pricing tenure of rate sensitive assets and liabilities.

The effective interest rate (effective yield) of a monetary financial instrument is the rate used in a present value calculation which results in the carrying amount of the instrument. The rate is a historical rate for a fixed rate instrument carried at amortised cost and a current rate for a floating rate instrument or an instrument carried at fair value.

The principal risk to which non-trading portfolios are exposed is the risk of loss from fluctuations in the future cash flows or fair values of financial instrument because of a change in market interest rates. Interest rate risk is managed principally through monitoring interest rate gaps. The ALCO is the monitoring body for compliance with these limits and is assisted by Risk Management in its day-to-day monitoring activities. A summary of the Bank's interest rate gap position on non-trading portfolios is provided in this note. The Bank also assesses interest rate risk by assessing the interest rate impact (both earnings perspective and economic value perspective) as per Basel-II guidelines communicated by Central Bank of Oman by applying interest rate shock of 200 bps and takes measures to reduce the impact. The Bank also assesses impact on earnings of interest rate shock of 50,100 and 200 bps.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2011 (continued)

D Financial risk management (continued)

D3 Market risk (continued)

D3.3 Exposure to interest rate risk – non trading portfolios (continued)

The Bank's interest sensitivity position based on contractual re-pricing arrangements at 31 December 2011 was as follows:

	Effective annual interest rate %	Within three months RO'000	Four months to 12 months RO'000	Over one year RO'000	Non-sensitive to interest rate RO'000	Total RO'000
31 December 2011						
Assets						
Cash and balances with Central Banks	2.00	-	-	-	61,513	61,513
Due from banks and other money market lendings	1.68	158,025	73,535	-	-	231,560
Loans and advances	5.92	435,059	169,453	428,601	(13,559)	1,019,554
Investment securities	1.27	68,126	3,244	4,197	10,092	85,659
Property, equipment and fixtures		-	-	-	14,157	14,157
Other assets		-	-	-	19,534	19,534
Total assets		661,210	246,232	432,798	91,737	1,431,977
Liabilities and equity						
Due to banks and other money market borrowings	0.91	43,136	-	-	-	43,136
Customers' deposits	2.14	240,968	390,275	147,375	392,819	1,171,437
Other liabilities	-	-	-	-	38,718	38,718
Subordinated loans	6.50	-	-	50,000	-	50,000
Shareholders' funds		-	-	-	128,686	128,686
Total liabilities and equity		284,104	390,275	197,375	560,223	1,431,977
Total interest rate sensitivity gap		377,106	(144,043)	235,423	(468,486)	-
Cumulative interest rate sensitivity gap		377,106	232,063	468,486	-	-

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2011 (continued)

D Financial risk management (continued)

D3 Market risk (continued)

D3.3 Exposure to interest rate risk – non trading portfolios (continued)

	Effective annual interest rate %	Within three months USD'000	Four months to 12 months USD'000	Over one year USD'000	Non-sensitive to interest rate USD'000	Total USD'000
31 December 2011						
Assets						
Cash and balances with Central Banks	2.00	-	-	-	159,774	159,774
Due from banks and other money market lendings	1.68	410,455	191,000	-	-	601,455
Loans and advances	5.92	1,130,023	440,138	1,113,249	(35,218)	2,648,192
Investment securities	1.27	176,951	8,426	10,901	26,213	222,491
Property, equipment and fixtures		-	-	-	36,771	36,771
Other assets		-	-	-	50,738	50,738
Total assets		1,717,429	639,564	1,124,150	238,278	3,719,421
Liabilities and equity						
Due to banks and other money market borrowings	0.91	112,042	-	-	-	112,042
Customers' deposits	2.14	625,891	1,013,701	382,792	1,020,310	3,042,694
Other liabilities	-	-	-	-	100,566	100,566
Subordinated loans	6.50	-	-	129,870	-	129,870
Shareholders' funds		-	-	-	334,249	334,249
Total liabilities and equity		737,933	1,013,701	512,662	1,455,125	3,719,421
Total interest rate sensitivity gap		979,946	(374,137)	611,488	(1,216,847)	-
Cumulative interest rate sensitivity gap		979,946	605,359	1,216,847	-	-

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2011 (continued)

D Financial risk management (continued)

D3 Market risk (continued)

D3.3 Exposure to interest rate risk – non trading portfolios (continued)

	Effective annual interest rate %	Within three months RO'000	Four months to 12 months RO'000	Over one year RO'000	Non-sensitive to interest rate RO'000	Total RO'000
31 December 2010						
Assets						
Cash and balances with Central Banks	2.00	-	-	-	105,022	105,022
Due from banks and other money market lendings	0.79	101,636	17,826	-	-	119,462
Loans and advances	6.61	327,680	115,413	472,619	(12,678)	903,034
Investment securities	0.94	94,420	-	-	12,729	107,149
Property, equipment and fixture		-	-	-	13,765	13,765
Other assets		-	-	-	10,183	10,183
Total assets		523,736	133,239	472,619	129,029	1,258,615
Liabilities and equity						
Due to banks and other money market borrowings	2.08	51,277	-	-	-	51,277
Customers' deposits	5.52	209,873	239,789	556,511	-	1,006,173
Other liabilities	2.76	-	-	-	27,634	27,634
Subordinated loans	6.53	-	-	50,000	-	50,000
Shareholders' funds		-	-	-	123,531	123,531
Total liabilities and equity		261,150	239,789	606,511	151,165	1,258,615
Total interest rate sensitivity gap		262,586	(106,550)	(133,892)	(22,144)	-
Cumulative interest rate sensitivity gap		262,586	156,036	22,144	-	-

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2011 (continued)

D Financial risk management (continued)

D3 Market risk (continued)

D3.3 Exposure to interest rate risk – non trading portfolios (continued)

	Effective annual interest rate %	Within three months USD'000	Four months to 12 months USD'000	Over one year USD'000	Non-sensitive to interest rate USD'000	Total USD'000
31 December 2010						
Assets						
Cash and balances with Central Banks	2.00	-	-	-	272,284	272,284
Due from banks and other money market lendings	0.79	263,990	46,301	-	-	310,291
Loans and advances	6.61	851,117	299,774	1,227,583	(32,930)	2,345,544
Investment securities	0.94	245,247	-	-	33,062	278,309
Property, equipment and fixtures		-	-	-	35,753	35,753
Other assets		-	-	-	26,449	26,449
Total assets		1,360,354	346,075	1,227,583	335,118	3,269,130
Liabilities and equity						
Due to banks and other money market borrowings	2.08	133,188	-	-	-	133,188
Customers' deposits	5.52	545,125	622,829	1,445,482	-	2,613,436
Other liabilities	2.76	-	-	-	71,777	71,777
Subordinated loans	6.53	-	-	129,870	-	129,870
Shareholders' funds		-	-	-	320,859	320,859
Total liabilities and equity		678,313	622,829	1,575,352	392,636	3,269,130
Total interest rate sensitivity gap		682,041	(276,754)	(347,769)	57,518	-
Cumulative interest rate sensitivity gap		682,041	405,287	57,518	-	-

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2011 (continued)

D Financial risk management (continued)

D3 Market risk (continued)

D3.3 Exposure to interest rate risk – non trading portfolios (continued)

The Bank's present business is being done with basic products. The risk is managed by taking views on interest rate movements for the year and realigning the portfolios and covenants of lending, so as to be proactive and minimize any adverse effects. The benchmark presently available in Oman is the 28-day Central Bank of Oman CD rate. The statistics on movement of the rate in CDs and weighted average cost of deposits and the interest on loans are provided below:

2011	**Jan**	**Feb**	**Mar**	**Apr**	**May**	**Jun**	**Jul**	**Aug**	**Sep**	**Oct**
CD Rate	**0.06%**	**0.06%**	**0.06%**	**0.06%**	**0.04%**	**0.03%**	**0.02%**	**0.03%**	**0.03%**	**0.07%**
Deposit Rate	**1.52%**	**1.44%**	**1.41%**	**1.37%**	**1.35%**	**1.36%**	**1.33%**	**1.35%**	**1.36%**	**1.35%**
Lending Rate	**5.91%**	**5.87%**	**5.81%**	**5.79%**	**5.76%**	**5.69%**	**5.69%**	**5.68%**	**5.64%**	**5.57%**

2010	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct
CD Rate	0.05%	0.04%	0.04%	0.04%	0.05%	0.08%	0.11%	0.08%	0.07%	0.07%
Deposit Rate	2.01%	1.98%	1.94%	1.90%	1.89%	1.83%	1.82%	1.76%	1.70%	1.67%
Lending Rate	6.50%	6.46%	6.39%	6.38%	6.38%	6.21%	6.19%	6.15%	6.11%	6.07%

The management of interest rate risk is one of the critical components of market risk management in banks. Interest rate risk primarily arises on account of mismatch of the Bank's assets with its liabilities that fund the assets. There are basically two approaches to management of interest rate risk in banks, namely "Earnings Approach" and "Economic Value Approach". The interest rate risk is assessed based on the impact of interest rate shock on the Bank's earnings and capital.

The focus of earnings approach is understanding the impact of interest rate changes (shock) of assets and liabilities on the Net Interest Income of the Bank. It measures the extent of capability of the Bank to absorb decline in net interest income caused by interest rate changes.

Interest rate risk also influences the present value of bank's asset and liabilities. Economic value perspective considers the present value of banks assets and liabilities and assesses the potential longer term impact of interest rates on the Bank. This perspective focuses on how the economic value of bank's assets, liabilities, change with movements in interest rates and it reflects the impact of fluctuation in the interest rates on the economic value of the institution.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2011 (continued)

D Financial risk management (continued)

D3 Market risk (continued)

D3.3 Exposure to interest rate risk – non trading portfolios (continued)

Basel-II Accord has recommended for assessing the impact of interest rate risk by applying 200 bps interest rate sensitivity and accordingly the impact of 200 bps interest rate shock on Bank's earnings and capital is provided below:

2010 USD'000	**2011 USD'000**		**2011 RO'000**	2010 RO'000
79,467	**90,278**	**Net interest income**	**34,757**	30,595
79,467	**90,278**	**Annualized net interest income**	**34,757**	30,595
465,241	**477,808**	**Capital**	**183,956**	179,118
		Based on 50 bps interest rate shock		
2,813	**4,135**	Impact of 50 bps interest rate shock	**1,592**	1,083
3.54%	**4.58%**	Impact as % to net interest income	**4.58%**	3.54%
0.61%	**0.83%**	Impact as % to capital	**0.83%**	0.61%
		Based on 100 bps interest rate shock		
5,626	**8,268**	Impact of 100 bps interest rate shock	**3,183**	2,166
7.08%	**9.16%**	Impact as % to net interest income	**9.16%**	7.08%
1.21%	**1.66%**	Impact as % to capital	**1.66%**	1.21%
		Based on 200 bps interest rate shock		
11,252	**16,538**	Impact of 200 bps interest rate shock	**6,367**	4,332
14.16%	**18.32%**	Impact as % to net interest income	**18.32%**	14.16%
2.43%	**3.32%**	Impact as % to capital	**3.32%**	2.43%

D3.4 Exposure to other market risks

Investment value risk is the risk of reduction in the market value of the Bank's portfolio as a result of diminishment in the market value of individual investments. The responsibility for management of investment value risk rests with the Investment division under the supervision and guidance of the Management Investment Committee and Board Executive Committee of the Bank. The Bank's investments are governed by an investment policy approved by the Board of Directors.The rating and price of the instruments are monitored on a regular basis and necessary actions are taken to reduce exposure if needed. The portfolio is revalued at market price to ensure that unrealised losses, if any, on account of reduction in the market value of the investments remains within the acceptable parameters.

Exposure and sensitivity analysis

The Bank analyses price sensitivity of the equity portfolio as follows:

a) For the local quoted equity portfolio, based on the beta factor of the portfolio performance to the MSM30 Index performance.

b) For the international quoted equity portfolio, based on the individual security market price movement.

The Bank's market risk is affected mainly by changes to the actual market price of financial assets. Actual performance of the Bank's local equity portfolio has a correlation to the performance of MSM30 Index.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2011 (continued)

D Financial risk management (continued)

D3 Market risk (continued)

D3.4 Exposure to other market risks (continued)

Security as per country	Changes in fair value +/- 5% 2011 RO'000	2010 RO'000
Oman	498	413
GCC	6	-
UAE	14	-
UK	208	-
Bermuda	71	-

Security as per country	Changes in fair value +/- 5% 2011 USD'000	2010 USD'000
Oman	1,294	1,073
GCC	16	-
UAE	36	-
UK	540	-
Bermuda	184	-

Currency risk

Currency risk is the risk that the value of a financial instrument will fluctuate due to changes in foreign exchange rates. The Board has set limits on the overall open position and for open position for each currency. The open position limits include overnight open position and intraday open position. Open positions are monitored on a daily basis and hedging strategies used to ensure positions are maintained within established limits. The Bank had the following net exposures denominated in foreign currencies:

	2011			2010		
	Assets RO'000	Liabilities RO'000	Net assets RO'000	Assets RO'000	Liabilities RO'000	Net assets RO'000
US Dollar	399,918	435,884	(35,966)	360,222	373,120	(12,897)
Saudi Rial	64,162	64,170	(8)	94,746	1,08,056	(13,310)
Euro	15,807	15,815	(8)	18,185	18,184	1
UAE Dirhams	3,872	793	3,080	11,019	4,350	6,668
Qatari Rial	22	19	3	114	8	106
Kuwaiti Dinar	68	15	53	65	-	65
Japanese Yen	4	1	3	3	-	3
Pound Sterling	2,402	2,402	-	783	785	(2)
Indian Rupee	283	223	59	8	-	8
Others	461	270	191	897	788	109

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2011 (continued)

D Financial risk management (continued)

D3 Market risk (continued)

D3.4 Exposure to other market risks (continued)

	2011			2010		
	Assets USD'000	**Liabilities USD'000**	**Net Assets USD'000**	Assets USD'000	Liabilities USD'000	Net Assets USD'000
US Dollar	**1,038,748**	**1,132,166**	**(93,418)**	935,642	969,143	(33,499)
Saudi Rial	**166,655**	**166,675**	**(21)**	246,094	280,665	(34,571)
Euro	**41,057**	**41,078**	**(21)**	47,234	47,231	3
UAE Dirhams	**10,057**	**2,060**	**8,000**	28,621	11,299	17,319
Qatari Rial	**57**	**49**	**8**	296	21	275
Kuwaiti Dinar	**177**	**39**	**138**	169	-	169
Japanese Yen	**10**	**3**	**8**	8	-	8
Pound Sterling	**6,239**	**6,239**	**-**	2,034	2,039	(5)
Indian Rupee	**735**	**579**	**153**	21	-	21
Others	**1,201**	**703**	**498**	2,330	2,047	283

The Bank takes on exposure to the effects of fluctuations in the prevailing foreign currency exchange rates on its financial position and cash flows. The Board sets limits on the level of exposure by currency and in aggregate for both overnight and intra-day positions, which are monitored daily.

Changes in the non parity foreign currency prices as at 31 December 2011 on net assets is considered negligible

D4 Operational risk

Operational risk is defined as the risk of direct or indirect loss resulting from inadequate or failed internal processes, people and systems or from external events. Operational risk arises due to variety of causes associated with the Bank's processes, personnel, technology and infrastructure and from external events and to include risks other than credit, market and liquidity risks.

The Bank's objective is to manage operational risk to avoid/reduce financial losses to the Bank by establishment of necessary controls, systems and procedures. The Bank recognises that over controlled environment will affect the Bank's business and earnings, besides adding to costs. Therefore, the Bank aims at effective management of operational risk through control optimisation and well established systems, methods and governance framework.

The primary responsibility for development and implementation of controls to address operational risk is assigned to senior management within each business unit. This responsibility is supported by the development of overall bank standards in the following areas for management of operational risk:

- Clear reporting lines
- Proper delegation of powers
- Appropriate segregation of duties and authorisation of transactions through a maker checker system and authorisation matrix
- Ownership reconciliation and monitoring of accounts
- Documentation of controls and processes
- Compliance with regulatory and other legal requirements
- Periodic assessment of the operational risks faced and evaluating the adequacy of controls and procedures to address the risks identified
- Reporting of operational losses and incidents triggering operational losses and remedial action
- Development of contingency plans
- Training, skill up gradation and professional development
- Ethical and business standards
- Risk mitigation through insurance, wherever desirable

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2011 (continued)

D Financial risk management (continued)

D4 Operational risk (continued)

Compliance with Bank standards is supported by a programme of periodic reviews undertaken by Internal Audit. The results of Internal Audit reviews are discussed with the management of the business unit to which they relate, with summaries submitted to the Audit Committee and senior management of the Bank. The Bank is also in the process of implementing a comprehensive Operational Risk Management Framework by which bank has put in place Operational Risk Management Policy, Risk and Control Self Assessment (RCSA) Policy , Operational Risk Loss Event Reporting Framework, Maintenance of Operational Risk Loss Data Base and RCSA Framework. The Bank has developed an in-house RCSA model and has conducted Risk and Control Self Assessment for all major business activities like Corporate Banking, Retail Banking, Treasury, Card operations and Deposits.

D5 Capital management

D5.1 Regulatory capital

The Bank's lead regulator, Central Bank of Oman, sets and monitors capital requirements for the Bank as a whole. In implementing current capital requirements Central Bank of Oman requires the Bank to maintain a prescribed ratio of total capital to total risk-weighted assets. The Bank calculates capital requirements for market risk and operational risk based upon the model prescribed by Central Bank of Oman as follows:

- Sovereign entities – Nil
- Banks – Risk weightage based upon ratings by Moody's.
- Retail and Corporate loans – In the absence of credit rating model 100% risk weightage is taken.
- Off balance sheet items – As per credit conversion factors and risk weightage prescribed by Central Bank of Oman.

The Bank's regulatory capital is analysed into three tiers:

- Tier 1 capital, which includes ordinary share capital, share premium, perpetual bonds (which are classified as innovative Tier 1 securities), retained earnings, translation reserve and minority interests after deductions for goodwill and intangible assets, and other regulatory adjustments relating to items that are included in equity but are treated differently for capital adequacy purposes.

- Tier 2 capital, which includes qualifying subordinated liabilities, collective impairment allowances and the element of the fair value reserve relating to unrealised gains on equity instruments classified as available-for-sale.

- Tier 3 capital, which includes short term subordinated debts which if circumstances demand would be capable of becoming the Bank's permanent capital.

Various limits are applied to elements of the capital base. The amount of innovative tier 1 securities cannot exceed 15 percent of total tier 1 capital; qualifying tier 2 capital cannot exceed tier 1 capital; and qualifying term subordinated loan capital may not exceed 50 percent of tier 1 capital. There are also restrictions on the amount of collective impairment allowances that may be included as part of tier 2 capital. Other deductions from capital include the carrying amounts of investments in subsidiaries that are not included in the regulatory consolidation, investments in the capital of Banks and certain other regulatory items.

Banking operations are categorized as either trading book or banking book, and risk-weighted assets are determined according to specified requirements that seek to reflect the varying levels of risk attached to assets and off-balance sheet exposures. To compute the capital charge for operational risk the Bank has considered the gross income for seven quarters, being the period since the commencement of operations, due to non-availability of data for previous three years as required under basic indicator approach for computation of capital for operational risk. The Bank's policy is to maintain a strong capital base as to maintain investor, creditor and market confidence and to sustain future development of the business. The impact of the level of capital on shareholders' return is also recognized and the Bank recognizes the need to maintain a balance between the higher returns that might be possible with greater gearing and the advantages and security afforded by a sound capital position. The Bank and its individually regulated operations have complied with all externally imposed capital requirements throughout the year. There have been no material changes in the Bank's management of capital during the year.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2011 (continued)

D Financial risk management (continued)

D5 Capital management (continued)

D5.1 Regulatory capital (continued)

The international standard for measuring capital adequacy is the risk asset ratio, which relates capital to balance sheet assets and off balance sheet exposures weighted according to broad categories of risk.

The risk asset ratio calculated in accordance with the capital adequacy guidelines of the Bank for International Settlement is as follows:

2010 USD'000	2011 USD'000		2011 RO'000	2010 RO'000
		Tier I capital		
259,740	**259,740**	Ordinary share capital	**100,000**	100,000
11,052	**14,818**	Legal reserve	**5,705**	4,255
1,073	**1,073**	General reserve	**413**	413
29,234	**43,122**	Retained earnings	**16,602**	11,255
(291)	**(5,660)**	Fair value losses	**(2,179)**	(112)
(29)	**(545)**	Deferred tax asset	**(210)**	(11)
300,779	**312,548**	**Total**	**120,331**	115,800
		Tier 2 capital		
32,930	**35,218**	Impairment allowance on portfolio basis	**13,559**	12,678
1,662	**171**	Fair value gains	**66**	640
129,870	**129,870**	Subordinated loan	**50,000**	50,000
164,462	**165,259**	**Total**	**63,625**	63,318
465,241	**477,808**	**Total regulatory capital**	**183,956**	179,118
		Risk-weighted assets		
2,755,958	**3,193,465**	Retail Bank, corporate Bank and market risk	**1,229,484**	1,061,044
167,086	**167,377**	Operational risk	**64,440**	64,328
2,923,044	**3,360,842**	**Total risk-weighted assets**	**1,293,924**	1,125,372
		Capital adequacy ratio		
15.92%	**14.22%**	Total regulatory capital expressed as a percentage of total risk-weighted assets	**14.22%**	15.92%
10.29%	**9.30%**	Total tier I capital expressed as a percentage of total risk-weighted assets	**9.30%**	10.29%

The capital adequacy ratio is calculated in accordance with the Basel II norms as adopted by Central Bank of Oman.

D5.2 Capital allocation

The allocation of capital between specific operations and activities is, to a large extent, driven by optimization of the return achieved on the capital allocated. The amount of capital allocated to each operation or activity is based primarily upon the regulatory capital, but in some cases the regulatory requirements do not reflect fully the varying degree of risk associated with different activities. In such cases the capital requirements may be flexed to reflect differing risk profiles, subject to the overall level of capital to support a particular operation or activity not falling below the minimum required for regulatory purposes.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2011 (continued)

D Financial risk management (continued)

D5 Capital management (continued)

D5.2 Capital allocation

Although maximization of the return on risk-adjusted capital is the principal basis used in determining how capital is allocated within the Bank to particular operations or activities, it is not the sole basis used for decision making. Account also is taken of synergies with other operations and activities, the availability of management and other resources, and the fit of the activity with the Bank’s longer term strategic objectives.

D6 Segmental information

Segment information is presented in respect of the Bank’s operating segments. For management purposes, the Bank is organised into three operating segments based on products and services as follows:

- Wholesale banking includes deposits including current accounts, term deposit etc. for corporate and institutional customers, Treasury and Trade finance.
- Retail banking includes customers’ deposits, consumer loans, overdrafts, credit card and fund transfer facilities.
- Corporate banking includes the pool of resources considered for transfer pricing and absorbs the cost of impairment loss on portfolio basis and income tax expense.

The CEO 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. Income taxes are managed on Bank basis and are not allocated to operating segments.

Interest income is reported net as CEO primarily relies on net interest income as a performance measure, not the gross income and expense.

Transfer prices between operating segments are on an arm’s length basis in a manner similar to transactions with third parties.

No revenue from transactions with a single external customer or counterparty amounted to 10% or more of the Bank’s total revenue in 2011 or 2010.

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2011 (continued)

D6 Segmental information (continued)

Segment information is as follows:

	2011				2010			
	Retail banking RO'000	**Wholesale banking RO'000**	**Corporate RO'000**	**Total RO'000**	Retail banking RO'000	Wholesale banking RO'000	Corporate RO'000	Total RO'000
Net interest income	**16,821**	**21,813**	**(3,877)**	**34,757**	12,211	14,333	4,051	30,595
Other operating income	**3,580**	**3,975**	**874**	**8,429**	1,548	2,996	92	4,636
Operating expenses	**(17,143)**	**(6,036)**	**-**	**(23,179)**	(14,355)	(5,231)	-	(19,586)
Staff cost	**(10,061)**	**(4,027)**	**-**	**(14,088)**	(8,252)	(3,452)	-	(11,704)
Other operating expenses	**(5,683)**	**(1,589)**	**-**	**(7,272)**	(4,665)	(1,356)	-	(6,021)
Depreciation	**(1,399)**	**(420)**	**-**	**(1,819)**	(1,438)	(423)	-	(1,861)
Operating profit/(loss)	**3,258**	**19,752**	**(3,003)**	**20,007**	(596)	12,098	4,143	15,645
Impairment on investments	**-**	**-**	**(17)**	**(17)**	-	-	(21)	(21)
Portfolio provision	**-**	**-**	**(881)**	**(881)**	-	-	(1,060)	(1,060)
Specific provisions	**(1,199)**	**(1,387)**	**-**	**(2,586)**	(2,176)	(748)	-	(2,924)
	2,059	**18,365**	**(3,901)**	**16,523**	(2,772)	11,350	3,062	11,640
Income tax expense	**-**	**-**	**(2,026)**	**(2,026)**	-	-	(1,420)	(1,420)
Segment profit/(loss) for the year	**2,059**	**18,365**	**(5,927)**	**14,497**	(2,772)	11,350	1,642	10,220
Segment assets	**363,263**	**964,536**	**104,178**	**1,431,977**	361,087	762,732	134,796	1,258,615
Segment liabilities	**189,648**	**1,024,925**	**217,404**	**1,431,977**	155,326	895,086	208,203	1,258,615

	2011				2010			
	Retail banking USD'000	**Wholesale banking USD'000**	**Corporate USD'000**	**Total USD'000**	Retail banking USD'000	Wholesale banking USD'000	Corporate USD'000	Total USD'000
Net interest income	**43,691**	**56,657**	**(10,070)**	**90,278**	31,717	37,229	10,521	79,467
Other operating income	**9,299**	**10,325**	**2,270**	**21,888**	4,021	7,782	239	12,042
Operating expenses	**(44,527)**	**(15,678)**	**-**	**(60,205)**	(37,286)	(13,587)		(50,873)
Staff cost	**(26,132)**	**(10,460)**	**-**	**(36,592)**	(21,434)	(8,966)	-	(30,400)
Other operating expenses	**(14,761)**	**(4,127)**	**-**	**(18,888)**	(12,117)	(3,522)	-	(15,639)
Depreciation	**(3,634)**	**(1,091)**	**-**	**(4,725)**	(3,735)	(1,099)	-	(4,834)
Operating profit/(loss)	**8,463**	**51,304**	**(7,800)**	**51,967**	(1,548)	31,424	10,760	40,636
Impairment on investments	**-**	**-**	**(44)**	**(44)**	-	-	(55)	(55)
Portfolio provision	**-**	**-**	**(2,288)**	**(2,288)**	-	-	(2,753)	(2,753)
Specific provisions	**(3,114)**	**(3,603)**	**-**	**(6,717)**	(5,652)	(1,943)	-	(7,595)
	5,349	**47,701**	**(10,132)**	**42,918**	(7,200)	29,481	7,952	30,233
Income tax expense	**-**	**-**	**(5,262)**	**(5,262)**	-	-	(3,688)	(3,688)
Segment profit/(loss) for the year	**5,349**	**47,701**	**(15,394)**	**37,656**	(7,200)	29,481	4,264	26,545
Segment assets	**943,540**	**2,505,288**	**270,593**	**3,719,421**	937,888	1,981,122	350,120	3,269,130
Segment liabilities	**492,592**	**2,662,143**	**564,686**	**3,719,421**	403,444	2,324,899	540,787	3,269,130

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