البنك الوطني العماني

National Bank of Oman

Annual Report 2012

For You. For Our Nation.

His Majesty Sultan Qaboos bin Said

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Omar Hussain Al Fardan
Chairman

Chairman's Report 2012

To Our Esteemed Shareholders

On behalf of your Board of Directors, I am pleased to share with you the results of the Bank for the year ended 31 December 2012. The Bank recorded a strong performance during the year despite regulatory changes and ongoing global concerns.

Oman Economy

Oman experienced a strong economic growth with GDP growth estimated to be around 8.3% for 2012. This was driven primarily by increased government spending on the back of high oil prices. The inflation rate during 2012 remained at approximately 3%.

Oman's economy is budgeted to grow by 7% in 2013. The government is looking to maintain growth and increase employment with higher allocations for capital projects in the 2013 budget. Public expenditure, approved in the budget 2013, amounts to RO 12.9 billion, an increase of 29% compared with 2012. The budget for the development expenditure programs of the Ministries and Government units has been enhanced by 30% to assist in the completion of infrastructure projects.

The new budget includes a 40% increase in spending on education, job creation programs and social support schemes, many of which are aimed at providing young Omanis with the skills to enter the private sector.

Financial Performance

The Bank achieved a net profit after tax of RO 40.7 million for the twelve months ended 31 December 2012 compared with RO 34.2 million for 2011, an increase of 19%.

The operating profit of the Bank grew from RO 48.8 million in 2011 to RO 52.0 million for the year ended December 2012. The operating income increased to RO 98.6 million from RO 92.2 in the previous year, an increase of 6.9%, due, mainly, to an increase in the net interest income arising from higher loan disbursals and lower cost of funds.

An increase of RO 180 million in the Bank's low cost deposits during the year has led to an overall decrease in the cost of funds from 2.13% in 2011 to 1.98% for 2012. Net interest spread was 3.09% for the year ended 31 December 2012.

Operating expenses were RO 46.7 million and have increased by RO 3.2 million or 7% over the previous year. The increase can be mainly attributed to higher staff costs and marketing expenses.

Net cost of credit was RO 5.3 million for the year ended 31 December 2012, 48% lower than the previous year, predominantly due to a reduction in the credit loss expense and impairment of investments.

Chairman's Report 2012

The Bank grew its net advances by RO 241 million to RO 1.9 billion at the end of December 2012, an increase of 14.4% over 2011. Customer deposits increased by 17.9% to RO 1.9 billion at 31 December 2012 compared with RO 1.6 billion at the end of 2011.

The Bank is in the process of exiting from Egypt; bringing down the number of branches from five in 2010, to one in 2012.

The Board has recommended a cash dividend of RO 0.0175 per share based on the dividend policy approved by the Board of Directors.

Capital

In the last quarter of 2012, the Bank raised subordinated debt of RO 7 million through a private placement to further strengthen its tier II capital. The regulatory capital of the Bank now stands at RO 345 million. The Capital Adequacy Ratio was 14.4%, as at 31 December 2012, well above the Central Bank's minimum requirement of 12%.

Bank of the Year – Oman

In 2012, the Bank was awarded the highly coveted 'Bank of The Year – Oman' award by the Banker Magazine, U.K. This award, which aims to promote industry excellence in global banking has been conferred on the Bank, in recognition of its consistent performance over the past few years.

Islamic Banking

The Bank has launched its Sharia compliant brand named 'Muzn'. Muzn offers a rich bouquet of products and services which cater to institutional, corporate, SME and retail clientele. The Bank intends to expand its Muzn branch network to cover all major regions in the Sultanate.

Corporate Governance

In accordance with the directives of the Code of Corporate Governance promulgated by the Capital Market Authority, the Bank includes a report on the implementation and effectiveness of Corporate Governance guidelines, directives and recommendations duly certified by the statutory auditors, within the Annual Report.

The Bank was awarded the Hawkamah Bank Corporate Governance Award 2012, thus validating the Bank's continued efforts and commitment to good corporate governance practice. This is the fourth year in succession that the Bank has received this award.

Corporate Social Responsibility (CSR)

CSR in its essence is how the Bank manages the business processes to produce an overall positive impact on society. The four key segments focused on by the Bank for CSR are: Health & Human Services, Civic, Education & Youth, and Environment.

In 2012, the Bank's community investment was RO 200,000. The Bank's CSR initiatives included training programmes for young Omani high school graduates, renovation of existing homes for truly needy families in co-ordination with the Ministry of Social Development and many others. In addition, the Bank's employees participated in its CSR initiatives, through the NBO Employee Volunteers programme.

The Year Ahead

The outlook for Oman's economy in 2013 is positive with an increase in government spending and the focus on infrastructure projects, is expected to boost economic growth. The launch of Islamic banking operations also opens up new opportunities for banks in the coming years.

The Wholesale and Investment Banking franchise will continue to support domestic project financing and related activity while mortgage, small business units, cards business and low cost deposits will remain the key focus of Retail Banking.

Participation in major domestic transactions and cross border activity in conjunction with the strategic alliance partner, Commercial Bank of Qatar, continues to be key in driving efficiencies by sharing global best practices.

Appreciation

The members of the Board of Directors join me in acknowledging and thanking our valued customers, correspondent banks and shareholders for the confidence they continue to have in the Bank.

We also thank and express our appreciation to the Central Bank of Oman and the Capital Market Authority for their prudent supervision and guidance.

We thank the Bank's management and staff for their dedication and commitment.

Above all, we pay tribute to His Majesty, Sultan Qaboos Bin Said, for his inspiring leadership and vision under whose wise guidance all of us in Oman, will assuredly remain on the path towards continued successful development.

Omar Hussain Al Fardan
Chairman

Board of Directors

Board of Directors

Omar Hussain Al Fardan
Chairman

Chairman of the Board of Directors, National Bank of Oman and Chairman of the Executive Committee of the Board.

Board Member of The Commercial Bank of Qatar (Q.S.C.) and Vice Chairman of United Arab Bank, Sharjah. He is also the Chairman of Qatar District Cooling Co. Q.C.S.C., Qatar; Vice Chairman of Middle East Dredging Co. Q.S.C., Qatar; President of Resorts Development Company, Qatar; President of Al Fardan Group Holding Co. S.O.C., Qatar and Director of its subsidiaries; Director of United Development Company P.S.C., Qatar; Director of Marsarabia, Director of Qatar Red Crescent Society and Trustee of the American University Beirut. Omar Al Fardan holds a B.A. in Business Administration and a Masters in Finance from Webster University, Geneva.

Mohammed Mahfoodh Al Ardhi
Deputy Chairman

Director since March 2011. Chairman of Credit Committee of the Board.

He is Director of The Board of Investcorp Bank, NYC, USA, The International Advisory Board of The Brookings Institute, Washington DC, USA and Member Board of Trustees of Eisenhower Fellowships Philadelphia, USA. A retired Air Vice Marshal by profession, Mr. Mohammed Mahfoodh Al Ardhi joined the Royal Air Force of Oman (R.A.F.O.) in 1978, and was subsequently appointed as Chief of Omani Air Force. In 2000, he was awarded the "Order of Oman" by His Majesty Sultan Qaboos bin Said Mr. Al Ardhi holds a Bachelor of Science Degree in Military Science from Royal Air Force Staff College in Bracknell, England and a Masters in Public Policy from John F. Kennedy School of Government, Harvard University USA.

Sayyidah Rawan Ahmed Al Said
Director

Director since April 2005. Chairperson of the Audit Committee and Member of the Executive Committee of the Board . She has 25 years of experience in the investment field both in public and private sectors. Prior to joining ONIC Holding Group as Managing Director & Group CE, she held the position of Deputy CEO at State General Reserve Fund of Oman. She is on the Board of a number of reputed Companies and Financial Institutions in Oman and across GCC. Sayyidah Rawan holds a M.Sc. in Economics & Finance from Loughborough University UK. She also holds a Post Graduate Diploma in Investment Analysis from Stirling University, UK and B.A. in Economics & Political Science from the American University, (AUC), Cairo.

Sheikh Abdullah bin Ali bin Jabor Al Thani
Director

Director since July 2005. Member of the Credit Committee of the Board. Deputy Chairman of The Commercial Bank of Qatar (Q.S.C.) and Director of United Arab Bank, Sharjah. Sheikh Abdullah Bin Ali Bin Jabor Al Thani holds a B.A. in Social Science from Qatar University.

Anil Kumar Nahar
Director

Director since November 2003. Member of the Audit Committee of the Board and Risk Committee of the Board. Chief Financial Officer, Bahwan Engineering Company, which is part of the Suhail Bahwan Group (Holding) LLC. Director of Oman Dental College (S.A.O.C.), Al Suwadi Power Co. S.A.O.C., Al Batinah Power Co. S.A.O.C. and Sharqiyah Desalination Co. S.A.O.C. Mr. Anil is a Chartered Accountant – Institute of Chartered Accounts, India. He also holds a Bachelor of Commerce from Vikram University, India.

Andrew Charles Stevens
Director

Director since July 2005. Member of the Executive and Credit Committees of the Board. Director of United Arab Bank, Sharjah, President /Chairman of Orient 1 Limited, Director of Qatar Insurance Company International and Group Chief Executive Officer, The Commercial Bank of Qatar (Q.S.C.); Andrew Stevens graduated from Birmingham University, England with a B.Com (Hons) in Banking and Finance

Saleh Nasser Abood Al Habsi
Director

Director since March 2008. Member of the Credit Committee of the Board. He previously held the position of Chairman of the Board Risk Committee of the Bank. Having 20 years' experience in the financial sector, Mr. Al Habsi is currently General Manager of MOD Pension Fund. He is Deputy Chairman of Gulf Custody Co Oman and Member of the Board GrowthGate Capital , a regional Private Equity Co. He is also a member of Investors Committee of Investment Stabilization Fund. Previously, he served as Chairman of Muscat Fund, was a Board Member of Bank Dhofar S.A.O.G., as well as Al Omaniya Financial Services S.A.O.G. Mr. Saleh holds an MBA and M.Sc. in Finance both from University of Maryland at College Park (USA), and B.S.B.A. B.A. from Boston University (USA).

Saif Said Salim Al Yazidi
Director

Director since March 2008. Member of Credit Committee of the Board. Member of the Board of Oman International Development and Investment Company & Muscat Gases Company. Mr. Al Yazidi holds a Bachelors Degree in Management Sciences, Accounting and a Masters in Business Administration (M.B.A.). He is the Director of Investment at the Civil Service Employees Pension Fund.

Suresh M. Shivdasani
Director

Director since June 2010. Member of the Risk Committee and EXCOB Committee of the Board. Mr. Shivdasani is the Managing Director, Sohar International Urea and Chemical Industries S.A.O.C and Advisor to the Chairman, Suhail Bahwan Group. Mr. Suresh Shivdasani holds a B.Tech Degree in Electrical Engineering from the Indian Institute of Technology (IIT) Delhi- India, and an M.B.A. Degree from McMaster University Canada.

Robert Sharpe
Director

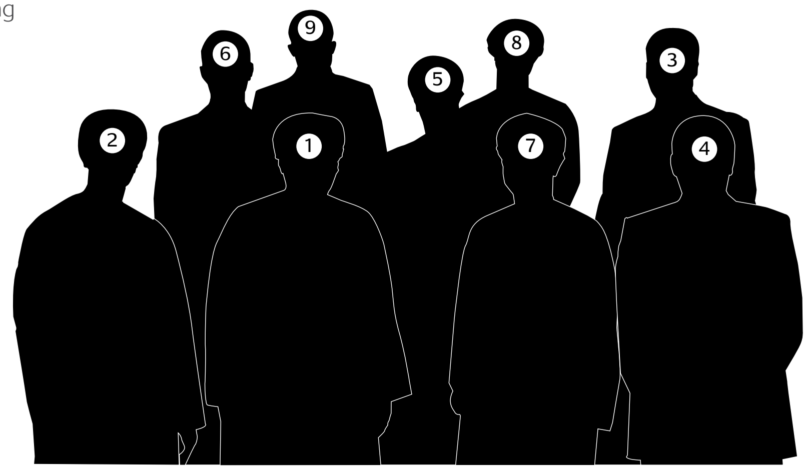
Director since March 2011. Chairman of the Risk Committee and Member of the Audit Committee of the Board. Mr. Sharpe is the Vice Chairman of Orient 1 and a Board Director of United Arab Bank in the UAE. He has over 35 years' experience in Banking . He also has considerable experience as an Independent Board Director having served on the Boards of several listed and private companies in the UK including subsidiaries of Barclays Bank and HSBC.

Faisal Abdullah Al Farsi
Director

Director since September 2011. Member of Board Audit Committee and Risk Committee of the Board. In 1995 he joined the Public Authority for Social Insurance where he occupied various positions which include Manager of Insurance Benefits, and acting Manager of Insurance Services . He was a Board Member of several General Joint Stock Companies including banks. Mr. Faisal holds a Bachelors Degree in General Administration and a Masters Degree in International Business Law. Currently he is the Manager of Planning Department at Public Authority for Social Insurance.

Executive Management

1. **Salaam Said Al Shaksy**
   Chief Executive Officer
2. **Ahmed Jaffer Al Musalmi**
   Deputy Chief Executive Officer
3. **Humayun Kabir**
   General Manager - Wholesale Banking
4. **Harshdeep Singh Munjal**
   General Manager - Retail and Private Banking
5. **Nasser Mohammed Al Hajri**
   Chief Human Resources Officer
6. **Stephen Clayton**
   Chief Risk Officer
7. **Nasser Salim Rashdi**
   Chief Internal Auditor
8. **Mansoor Darwish Al Raisi**
   Deputy General Manager - Compliance
9. **V. Balasubramanian**
   Chief Financial Officer



Corporate Governance Report – 2012

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Sultanate of Oman

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Report to the shareholders of National Bank of Oman SAOG ("the Bank") of factual findings in connection with the Corporate Governance report of the Bank and application of the Corporate Governance practices in accordance with Capital Market Authority Code of Corporate Governance

We have performed the procedures prescribed in the Capital Market Authority ("CMA") Circular No. 16/2003 dated 29 December 2003 ("the Procedures") with respect to the Corporate Governance Report of the Bank ("the Report") and its application of the Corporate Governance practices in accordance with the CMA Code of Corporate Governance ("the Code") issued under Circular No. 11/2002 dated 3 June 2002 and the CMA Rules and Guidelines on disclosure, issued under CMA Administrative Decision 5/2007, dated 27 June 2007. The Report is set out on pages 13 to 23.

Our engagement was undertaken in accordance with the International Standards on Related Services applicable to agreed-upon procedures engagements. The Procedures were performed solely to assist you in evaluating the Report.

We found the Report reflects, in all material respects, the Bank's application of the provisions of the Code and is free from any material misrepresentation.

Because the Procedures do not constitute either an audit or a review made in accordance with International Standards on Auditing or International Standards on Review Engagements, we do not express any assurance on the Bank's Corporate Governance Report. Had we performed additional procedures or had we performed an audit or review of this Report in accordance with International Standards on Auditing or International Standards on Review Engagements, other matters might have come to our attention that would have been reported to you.

This report is solely for the purpose set forth in the second paragraph above, and for inclusion, with the Report, in the Bank's annual report, and is not to be used for any other purpose; and we accept no responsibility to any third party. This report relates only to the Report included in the Bank's annual report for the year ended 31 December 2012 and does not extend to the financial statements or any other reports of the Bank, taken as a whole.

KPMG

24 January 2013

Paul Callaghan

Corporate Governance Report – 2012

Corporate governance deals with the way companies are managed and led, defines the roles of the Directors and formalizes the internal control process within the institution.

The Board of Directors of National Bank of Oman the Bank) supports the fostering of a healthy governance culture at the Bank. Accordingly, the Board and its Committees continuously evaluate and improve their governance practices, policies and procedures and confirm that the Bank applies the principles set out in the Capital Market Authority (the CMA) Code of Corporate Governance (the Code) as amended for MSM Listed Companies and the regulations for Corporate Governance of Banking and Financial Institutions issued by the Central Bank of Oman.

In recognition of the best practices and corporate governance measures applied by it, the National Bank of Oman has crowned its achievements in 2012 by winning the Bank of the Year – Oman' Award for 2012, by The Banker Magazine, U.K, Best Institution in the Field of Social Responsibility in Oman", 2012 , Developing Sustainable Strategies Award' at the Asian CSR Leadership Awards 2012 & Hawkamah Bank Corporate Governance – 'Honorable Mention' Award 2012.

In accordance with the directives of the Code of Corporate Governance promulgated by the Capital Market Authority, we continue to include a separate report on the bank's Corporate Governance duly certified by the statutory auditors within the Annual Report.

01. Board of Directors

The Board of Directors is responsible for the overall direction, supervision and control of the Bank. Specific responsibilities of the Board include laying down and approving the business objectives of the Bank, approving strategies and policies which need to be pursued in order to achieve these objectives, and reviewing on an on-going basis the performance of the Bank in relation to its stated objectives as well as adherence to policies.

02. Appointment of Directors

The Board is comprised of 11 members who have been elected by the shareholder in March 2011 for a period of three years. The current term of all the Directors expires in March 2014.

03. Process of nomination of the Directors

The nomination of the Directors is as per Articles 29 to 34 of the Bank's Article of Association.

The Board reviews the appropriate skills and characters required of the Board Members and recommends suitable names for the shareholders for election. Shareholders retain the power to elect any candidate to the Board irrespective of whether this candidate is recommended by the Board or otherwise.

04. Characteristics and core competency of the Board

Members of the Board and its committees bring appropriate knowledge and experience as well as independent judgment to Board meetings and resolutions. The Board collectively possesses professional knowledge, business expertise, industry knowledge and financial awareness to carry out its oversight responsibilities over the executive and senior management of the Bank.

05. Information given to the Board

The Directors are given appropriate and timely information so that they can maintain full and effective control over strategic, financial, operation, compliance and governance issues. The information provided to the Board is as per the guidelines provided in the Code.

On appointment, each Director receives information about the Bank and is advised of the legal, regulatory and other obligations devolving upon a Director of listed companies.

06. Composition of the Board

No Director is a member of the Board of more than four public joint stock companies or banks whose principal place of business is in the Sultanate of Oman, or is a Chairman of more than two such companies.

The following tables show the position of each of the current Board members in line with the Code's requirements:

Table 1

Name of the Directors	Representing	Category of the Director*
Mr. Omar Hussain Al Fardan – Chairman	Himself	NEX-NIND
Mr. Mohammed Mahfoodh Al Ardhi – Deputy Chairman	Rimal Investment Projects LLC	NEX-IND
Sayyidah Rawan Ahmed Al Said	Herself	NEX-IND
Mr. Anil Kumar Nahar	Himself	NEX-NIND
Sheikh Abdullah bin Ali bin Jabor Al Thani	The Commercial Bank of Qatar- Equity Investor	NEX-NIND
Mr. Andrew Charles Stevens	Himself	NEX-NIND
Mr. Robert Sharpe	Himself	NEX-NIND
Mr. Faisal Abdullah Al Farsi	Public Authority for Social Insurance- Equity Investor	NEX – IND
Mr. Saleh Nasser Al Habsi	Ministry of Defense Pension Fund- Equity Investor	NEX-IND
Mr. Saif Said Al Yazidi	Himself	NEX-IND
Mr. Suresh M Shivdasani	Suhail Bahwan Group (Holding)	NEX- NIND

*NEX: Non-Executive Director, IND: Independent, NIND: Non Independent

Table 2

Name of the Directors	Other Board Committees Membership*	No. of other S.A.O.G Boards	No. of Board Meetings attended	Attended last AGM on 25th MARCH 2012 (Yes/No/NA)
Mr. Omar Hussain Al Fardan – Chairman	EXCOB	Nil	5	No
Mr. Mohammed Mahfoodh Al Ardhi – Deputy Chairman	CCB	Nil	5	Yes
Sayyidah Rawan Ahmed Al Said	EXCOB, BAC	3	5	Yes
Mr. Anil Kumar Nahar	BAC, BRC	Nil	6	Yes
Sheikh Abdullah bin Ali bin Jabor Al Thani	CCB	Nil	3	Yes
Mr. Andrew Charles Stevens	EXCOB, CCB	Nil	6	Yes
Mr. Saleh Nasser Al Habsi	CCB	Nil	6	Yes
Mr. Saif Said Al Yazidi	CCB	2	5	Yes
Mr. Robert Sharpe	BAC, BRC	Nil	5	Yes
Mr. Suresh M Shivdasani	BRC, EXCOB	Nil	3	Yes
Mr. Faisal Abdullah Al Farsi	BAC, BRC	Nil	5	Yes

*BAC: Board Audit Committee, CCB: Credit Committee of the Board, BRC: Board Risk Committee, EXCOB: Executive Committee of the Board.

07. Number and dates of Board meetings

National Bank of Oman held 6 Board meetings during 2012. They were on 23rd January, 25th March, 29th April, 10th June , 07th August and 05th December 2012. The maximum interval between two meetings was 117 days. This is in compliance with Article 4 of the Code, which requires meetings to be held within a maximum time of four months.

08. Remuneration to Board and Top Management

The sum of the benefits (e.g. salaries, perquisites, bonuses, gratuity, pension, etc.) paid to the top senior managers of the Bank in 2012 is RO 1,231,980

Staff service contracts are 2 years for expatriate officers and determined by the prevailing labour laws for Omanis. The notice period is between 2 and 4 months.

As all members of the Board are Non-executive Directors, accordingly no fixed remuneration or performance linked incentive are applicable. The Non-executive Directors are paid sitting fees and reimbursement of expense for attending the Board and committee meetings. In addition to the sitting fees paid, the total remuneration for 2013 of the Directors is RO 121,200.000 subject to the Annual General Meeting approval proposed to be held on 26th March 2013.

The details of the sitting fees paid or accrued for payment during 2012 are as follows:

Table 3

Name of the Directors	Total Fees RO	Remarks
Mr. Omar Hussain Al Fardan - Chairman	5,100.000	
Mr. Mohammed Mahfoodh Al Ardhi – Deputy Chairman	7,900.000	
Sayyidah Rawan Ahmed Al Said	7,300.000	
Mr. Anil Kumar Nahar	7,200.000	
Sheikh Abdullah bin Ali bin Jabor Al Thani	6,500.000	
Mr. Andrew Charles Stevens	10,000.000	
Mr. Saleh Nasser Al Habsi	8,600.000	
Mr. Saif Said Al Yazidi	8,500.000	
Mr. Robert Sharpe	7,100.000	
Mr. Suresh M Shivdasani	4,900.000	
Mr. Faisal Abdullah Al Farsi	5,700.000	
Total	**78,800.000**	

The total hotel and travel expense related to the Board Members during 2012 is RO 28,505

09. Board Committees

As at December 2012, The Board of Directors has four standing committees, the Credit Committee, the Audit Committee, the Risk Committee and the Executive Committee.

10. Audit Committee of the Board:

The Audit Committee comprises four members. The committee has met seven times in 2012.

The composition of the Audit Committee and particulars of meetings attended by the members of the Audit Committee are given in the table below:

Table 4

Name	Position	Meetings attended	Remarks
Sayyidah Rawan Ahmed Al Said	Chairperson	6	
Mr. Anil Kumar Nahar	Member	7	
Mr. Saif Said Al Yazidi	Member	3	Resigned in June 2012
Mr. Robert Sharpe	Member	7	
Mr. Faisal Abdullah Al Farsi	Member	6	

The Audit Committee Charter which specifies the responsibility and authority of the Board Audit Committee is approved by the Board, annually.

The responsibilities of the Committee as specified in this Audit Committee Charter include:

- Assisting the Board in discharging its statutory/oversight responsibilities on financial and accounting matters.
- Overseeing the financial reporting process on behalf of the Board including review of the annual and quarterly financial statements and to recommend such statements for approval of the Board. To review qualifications if any, in the draft financial statements and discussion of the accounting principles;
- Reviewing the audit plans and reports of the external auditors and internal auditors and considering the effectiveness of the actions taken by management on the auditors' recommendations;
- Appraising and reporting to the Board on the audits undertaken by the external auditors and internal auditors, the adequacy of disclosure of information, and the appropriateness and quality of the system of management and internal controls;
- Reviewing the independence (particularly with reference to any other non-audit services), fee and terms of engagement of the bank's external auditor and recommend their selection to the Board for putting before Annual General Meeting for appointment.
- Reviewing and approving the Audit Division Charter annually, which describes the independence, authority, scope, responsibility and standards of the Internal Audit function. Directing and supervising the activities of the Internal Audit function.

11. Credit Committee of the Board (CCB):

The Credit Committee comprises of 5 members and met 10 times during 2012. The names of the members, their positions and their meetings and attendance appear in the table below:

Table 5

Name	Position	Meetings attended	Remarks
Mr. Mohammed Mahfoodh Al Ardhi	Chairman	9	
Mr. Andrew Charles Stevens	Member	8	
Mr. Saleh Nasser Al Habsi	Member	8	
Sh. Abdullah bin Ali bin Jabor Al Thani	Member	7	
Mr. Saif Said Al Yazidi	Member	8	

The CCB's main responsibilities are:

To approve transactions up to the maximum legal limits of the Bank including underwriting exposures and sell down targets.

Review reports of risk assets covering bank wide portfolio trends including higher risk assets, exposures as well as the other reports at least every quarter.

Review management of recovery strategies of problem loans and adequacy of provisioning.

12. Board Risk Committee (BRC):

The Risk Committee of the Board comprises of four members and met six times during the year2012. The major responsibilities of the committee include risk identification and review, risk policy, risk limits and risk management and monitoring. The names of the members appear in the table below:

Table 6

Name	Position	Meetings attended*	Remarks
Mr. Robert Sharpe	Chairman	6	Appointed as Chairman on **10.06.2012**
Mr. Faisal Al Farsi	Member	3	Appointed on **10.06.2012**
Mr. Suresh M Shivdasani	Member	4	
Mr. Anil Nahar	Member	5	
Mr. Mohammed Al Ardhi	Member	1	Resigned on **10.06.2012**
Mr. Saleh Nasser Al Habsi	Ex-Chairman	2	Resigned on **10.06.2012**

13. Executive Committee of the Board (EXCOB)

The Executive Committee of the Board comprises of four members and met seven times during the year 2012. The names of the members and their positions are as set out in the table below:

Table 7

Name	Position	Meetings attended	Remarks
Mr. Omar Hussain Al Fardan	Chairman	7	
Sayyidah Rawan Ahmed Al Said	Member	7	
Mr. Andrew Charles Stevens	Member	7	
Mr. Suresh Shivdasani	Member	5	

The main responsibilities of the EXCOB are stated below:

- To develop the long term strategy of the Bank based on economic and market conditions and the Board's vision and recommend for Board approval.
- To review the performance of the Bank against agreed strategy and budgets.
- To review and recommend for Board approval the Bank's annual Budgets and Business Plans including all Operating and Capital Expenditure budgets of the Bank in line with the long term strategy and changes in economical, market and regulatory environments.
- To review the performance of the investment banking function including all investments reports.
- To review and approve the Banks Dividend Policy and recommend to the Board the proposed dividend payout.
- To be responsible for setting the Bank's remuneration framework for management and staff.
- To review prevailing compensation and benefits and ensure consistency with market trends.
- To review, approve and amend policies related to employee reward and performance related incentive plans.
- To review the Bank's Omanisation policies and the development of the Omani Middle and Senior Management executives of the Bank.

14. Board Members Profile

Mr. Omar Hussain Al Fardan, Chairman

Chairman of the Board of Directors, National Bank of Oman and Chairman of the Executive Committee of the Board.

Board Member of The Commercial Bank of Qatar (Q.S.C.) and Vice Chairman of United Arab Bank, Sharjah.

He is also the Chairman of Qatar District Cooling Co. Q.C.S.C., Qatar; Vice Chairman of Middle East Dredging Co. Q.S.C., Qatar; President of Resorts Development Company, Qatar; President of Alfardan Group Holding Co. S.O.C., Qatar and Director of its subsidiaries; Director of United Development Company P.S.C., Qatar; Director of Marsarabia, Director of Qatar Red Crescent Society and Trustee of the American University Beirut.

Omar Alfardan holds a B.A. in Business Administration and a Masters in Finance from Webster University, Geneva.

Mr. Mohammed Mahfoodh Al Ardhi, Deputy Chairman

Director since March 2011. Chairman of Credit Committee of the Board.

He is Director of The Board of Investcorp Bank, NYC, USA, The International Advisory Board of The Brookings Institute, Washington DC, USA and Member Board of Trustees of Eisenhower Fellowships Philadelphia, USA.

A retired Air Vice Marshal by profession, Mr. Mohammed Mahfoodh Al Ardhi joined the Royal Air Force of Oman (R.A.F.O.) in 1978, and was subsequently appointed as Chief of Omani Air Force. In 2000, he was awarded the "Order of Oman" by His Majesty Sultan Qaboos bin Said Al-Said.

Mr. Al Ardhi holds a Bachelor of Science degree in Military Science from Royal Air Force Staff College in Bracknell, England and a Masters in Public Policy from John F. Kennedy School of Government, Harvard University USA.

Sayyidah Rawan Al Said, Director

Director since April 2005. Chairperson of the Audit Committee and member of the Executive Committee of the Board .

She has 25 years of experience in the investment field both in public and private sectors. Prior to joining ONIC Holding Group as Managing Director & Group CE, she held the position of Deputy CEO at State General Reserve Fund of Oman.

She is on the Board of a number of reputed Companies and Financial Institutions in Oman and across GCC.

Sayyidah Rawan holds a M.Sc. in Economics & Finance from Loughborough University UK. She also holds a Post Graduate Diploma in Investment Analysis from Stirling University, UK and B.A. in Economics & Political Science from the American University, (AUC), Cairo.

Mr. Anil Kumar Nahar, Director

Director since November 2003. Member of the Audit Committee of the Board and Risk Committee of the Board.

Chief Financial Officer, Bahwan Engineering Company, which is part of the Suhail Bahwan Group (Holding) LLC. Director of Oman Dental College (S.A.O.C.), Al Suwadi Power Co. S.A.O.C., Al Batinah Power Co. S.A.O.C. and Sharqiyah Desalination Co. S.A.O.C.

Mr. Anil is a Chartered Accountant – Institute of Chartered Accounts, India. He also holds a Bachelor of Commerce from Vikram University, India.

Sheikh Abdullah bin Ali bin Jabor Al Thani, Director

Director since July 2005. Member of the Credit Committee of the Board.

Deputy Chairman of The Commercial Bank of Qatar (Q.S.C.) and Director of United Arab Bank, Sharjah.

Sheikh Abdullah Bin Ali Bin Jabor Al Thani holds a B.A. in Social Science from Qatar University.

Mr. Andrew Charles Stevens, Director

Director since July 2005. Member of the Executive and Credit Committees of the Board.

Director of United Arab Bank, Sharjah, President / Chairman of Orient 1 Limited, Director of Qatar Insurance Company International and Group Chief Executive Officer, The Commercial Bank of Qatar (Q.S.C.);

Andrew Stevens graduated from Birmingham University, England with a B.Com. (Hons) in Banking and Finance

Mr. Saleh Nasser Abood Al Habsi, Director

Director since March 2008. and Member of the Credit Committee of the Board. He previously held the position of Chairman of the Board Risk Committee of the bank.

Having 20 years' experience in the financial sector, Mr, Al Habsi is currently General Manager of MOD Pension Fund,.

He is Deputy Chairman of Gulf Custody Co. Oman and member of the Board GrowthGate Capital, a regional private equity Co. He is also a member of Investors committee of Investment Stabilization Fund.

Previously, he served as Chairman of Muscat Fund, was a board member of Bank Dhofar S.A.O.G., as well as Al Omaniya Financial Services S.A.O.G.

Mr. Saleh holds M.B.A. and M.Sc. in Finance both from University of Maryland at College Park (USA),and BSBA and BA from Boston University (USA).

Mr. Saif Said Salim Al Yazidi, Director

Director since March 2008. Member of Credit Committee of the Board.

Member of the Board of Oman International Development and Investment Company & Muscat Gases Company.

Mr. Al Yazidi holds a Bachelors Degree in Management Sciences, Accounting and a Masters in Business Administration (MBA). He is the Director of Investment at The Civil Service Employees Pension Fund.

Mr. Suresh M. Shivdasani, Director

Director since June 2010. Member of the Risk Committee and EXCOB Committee of the Board.

Mr. Shivdasani is the Managing Director, Sohar International Urea and Chemical Industries S.A.O.C. and Advisor to the Chairman, Suhail Bahwan Group.

Mr. Suresh Shivdasani holds a B.Tech. degree in Electrical Engineering from the Indian Institute of Technology (IIT) Delhi- India, and an M.B.A. degree from McMaster University Canada.

Mr. Robert Sharpe, Director

Director since March 2011. Chairman of Risk Committee and Member of Audit Committee of the Board. Mr. Sharpe is the Vice Chairman of Orient 1 and a Board Director of United Arab Bank in the UAE. He has over 35 years experience in Banking .He also has considerable experience as an Independent Board Director having served on the Boards of several listed and private companies in the UK including subsidiaries of Barclays Bank and HSBC.

Mr. Faisal Abdullah Al Farsi, Director

Director since September 2011. Member of Board Audit Committee and Risk Committee of the Board. In 1995 he joined the Public Authority for Social Insurance where He occupied various positions which include Manager of Insurance Benefits, and acting Manager of Insurance Services .

He was a Board member of several General Joint Stock Companies including banks.

Mr. Faisal holds a Bachelor Degree in General Administration and a Master Degree in International Business Law.

Currently he is the Manager of Planning Department at Public Authority for Social Insurance.

15. Composition of the Management:

The organization chart of the Bank's management includes a Chief Executive Officer as the leader of the organization whose appointment, functions and package are determined by the Board. The Deputy CEO and General Managers are appointed to assist the CEO and to lead functional groups in the Bank. The organization chart also includes Deputy General Managers and Assistant General Managers besides the Divisional Heads. The following table gives details of the top management officers along with their positions:

Table (10)

Name	Position
Salaam Said Al Shaksy	Chief Executive Officer
Ahmed Jaffer Al Musalmi	Deputy CEO
Humayun Kabir	GM- Wholesale Banking
Stephen Clayton	GM- Chief Risk Officer
Harshdeep Munjal	GM- Retail & Private Banking
Faizal Mohamed Eledath	GM- Chief Information Officer

16. Market Price Data:

The following table shows the high, low, and average prices of the Bank's shares and compares the Bank's performance against the broad index of banks and investment companies during 2012

NBO AND MSM BANK & INVESTMENT INDEX - FY 2012

Table (11)

Banks & Investment index				NBO price			
Month	High	Low	Closing	Month	High	Low	Closing
Jan-12	6555.2	6317.59	6317.59	Jan-12	0.327	0.312	0.319
Feb-12	6516.28	6270.78	6504.93	Feb-12	0.320	0.313	0.320
Mar-12	6974.74	6504.82	6642.69	Mar-12	0.320	0.276	0.292
Apr-12	7256.2	6646.97	6927.76	Apr-12	0.307	0.290	0.292
May-12	6928.46	6460.35	6671.95	May-12	0.300	0.275	0.287
Jun-12	6687.41	6355.86	6384.43	Jun-12	0.293	0.277	0.291
Jul-12	6428.39	5843.11	5894.03	Jul-12	0.290	0.260	0.262
Aug-12	6436.82	5892.74	6268.71	Aug-12	0.268	0.261	0.264
Sep-12	6383.17	6164.76	6176.8	Sep-12	0.272	0.265	0.270
Oct-12	6366.37	6176.38	6215.91	Oct-12	0.284	0.272	0.274
Nov-12	6335.4	6114.83	6123.3	Nov-12	0.280	0.271	0.275
Dec-12	6667.82	6123.3	6624.06	Dec-12	0.287	0.273	0.285

17. Related party transactions

Details of all transactions where a Director and/or other related parties might have a potential interest are provided to the Board for their review and approval, and the interested Director neither participates in the discussions, nor do they vote on such matters.

Every quarter the details of the related party transactions are produced and submitted to the Board for review and approval as part of approving the bank's quarterly financial statements.

Details of all the related party transactions are provided to the shareholders as part of the financial statements submitted for approval at the Annual General Meeting along with the statement that transactions are on an arms length and independent basis and reasonable.

18. Internal Control Review

The Board attaches great importance to maintaining a strong control environment and their review has covered all controls, including financial, operational, compliance and risk management.

The Board has a collective responsibility for the establishment, maintenance and review of a system of internal controls that provides reasonable assurance of effective and efficient operations, internal financial control, and compliance with the relevant laws and regulations.

The Board has established a management structure that clearly defines roles and responsibility and reporting lines and has approved the updated policies including credit, expenditure, disclosure, corporate governance etc.

The Bank's financial position, results of operations and business performance is regularly reported to the Board. The actual performance achieved against budgets and prior period is reported and closely monitored.

Financial information is prepared using appropriate accounting policies that are consistently applied. Operational procedures and controls have been established to facilitate complete, accurate and timely processing of transactions and the safeguarding of assets through policies and procedures manuals, desk performance instructions and other circulars.

The Bank's internal disclosure policy includes the close season period definition. This is notified to all the insiders on quarterly basis or when required.

19. Shareholders

Communication with shareholders and investors

The Board is committed to ensure that all material information relating to the Bank's business operations is regularly communicated to its stakeholders and members of the investment community.

The Bank has its own web site, where relevant information relating to the Bank, its products, its operations and annual and quarterly financial statements are posted. The Bank's web-site address is www.nbo.co.om.

The quarterly, half-yearly, and annual results of operations of the Bank are published in leading Arabic and English newspapers in the Sultanate of Oman. After completion of the statutory audit, the annual report and summary financial statements are sent by post to all shareholders along with the notice of the forthcoming Annual General Meeting of the Bank. Further, the shareholders are advised to contact the Bank whenever they require any updated information regarding the Bank or its operations.

The distribution of dividend to the shareholders by the Bank during the last five years appears in the table below:

Table (12)

Year	Cash dividend	Bonus shares
2008	17.5%	Nil
2009	12 %	Nil
2010	15 %	Nil
2011	17.5%	2.5%
2012 (subject to Shareholders' approval)	17.5	Nil

20. Corporate Social Responsibility (CSR):

During the year 2012, the Bank distributed donations to the charitable organizations and other non-profitable organizations and participated in CSR initiatives totaling RO. 197,080.00 as approved by the Annual General Meeting held on 25th March 2012.

Details of NBO main donations and CSR initiatives during the year 2012:

Amount OMR	Details
18,000	Oman Association for the Disabled - Funds towards 180 wheelchairs , 4 beds & hearing aids
6,791	National Assoc. for Cancer Awareness – Funding going towards NACA walkathon & mobile mammography unit
3,500	Environment Society of Oman – Funding towards community outreach project colleges & school etc.
6,000	Awladina Road Safety Association – Funding going towards 300 children car seats & awareness program
2,500	AIESEC – 3 Omani students work experience in Lebanon – media companies
6,000	Assoc. of Early Intervention – awareness programs
1,000	Dar Al Atta – College students fundraising project
8,000	"Hayatakum" Programme – covering all social issues in Oman including drugs, road safety
42,750	Bahwan Cybertek – Training 15 Young Omanis in money exchange – 7 months program
8,000	Iftar Sa'im Road Trips – Reaching out to poor families throughout the Sultanate
5,000	inJAz Oman – Training Omani College students to set up their businesses
20,000	Financial Education Summit
2,000	Al Roya Sinbad - Mobile Library Unit (reaching out to children through out the Sultanate)
1,000	College of Banking and Financial Studies – 3 Students cultural exchange program to Bradford University
5,000	Oman Water Society – awareness program
2,500	SQU - College of Medicine - participation in the WHO patient safety project
5,000	Oman Paralympic Committee – sent two qualified Omani Paralympics in London 2012
4,300	Miscellaneous
2,000	OCC - Keep Oman Clean Khareef Festival
16,000	Outward Bound Oman – Training 72 Young Omani high school students from government schools
1,000	Road Safety Campaign Amerat
1,000	Eid Gathering for Children -
2,000	Dar Al Hanan – Support towards administrative cost of children cancer patients from the region
6,200	United Nations Conference - focusing on Sustainability
5,000	SQU - Genetics Conference – awareness program
5,000	Art of Living – Youth Leadership Development Program
10,000	Chairman's Awards 2012 (date 1st week of 2013) recognising NBO employee volunteers and civic partners
500	Royal Hospital Conference - International Conference in Obstertics & Gynaecology 5th - 7th December
500	Ibda Al Tufoly
538.8	Supply of AC's to Social Security Homes
Total OMR	197,080.000

21. Distribution of Shareholding:

Major shareholders (5% and above)

Shareholder name	No. of shares as on 31st December 2012	% of Capital
COMMERCIAL BANK OF QATAR	386,699,095	34.90
SUHAIL BAHWAN GROUP HOLDING LLC	163,370,045	14.74
CIVIL SERVICE EMPLOYEES PENSION FUND	86,347,794	7.79
HSBC A/C MINISTRY OF DEFENCE PENSION FUND	84,847,347	7.66
PUBLIC AUTHORITY FOR SOCIAL INSURANCE	66,425,447	5.99

The shareholding pattern as on 31 December 2012 was:

Number of Shares	Number of Shareholders	Total Shares	% of Capital
7,000,000 and above	17	985,951,035	90
3,000,000 to 6,999,999	7	31,371,211	3
1,500,000 to 2,999,999	12	23,373,534	2
500,000 to 1,499,999	32	27,566,630	2
100,000 to 499,999	114	25,824,732	2
Below 100,000	6565	13,937,858	1
Total		**1,108,025,000**	**100%**

A copy of the Management Discussion and Analysis is circulated as part of the Annual report.

There are no Global Depository Receipts/Warrants or any Convertible instruments outstanding.

22. Auditors:

Having strong internal and external auditors is recognized by the Board as part of sound corporate governance, and as important agents providing an independent and continuous assessment of the adequacy of, and compliance with, the Bank's established policies and procedures.

23. KPMG

"The shareholders of the Company appointed KPMG as the Company's auditors for the year 2012. KPMG is a leading accounting firm in Oman and is a part of KPMG Lower Gulf that was established in 1974. KPMG in Oman employs more than 130 people, amongst whom are 4 Partners, 5 Directors and 20 Managers, including Omani nationals and is a member of the KPMG network of independent firms affiliated with KPMG International Co-operative. KPMG is a global network of independent firms providing Audit, Tax and Advisory services and has more than 152,000 outstanding professionals working together in 156 countries worldwide.

KPMG in Oman is accredited by the Capital Market Authority (CMA) to audit joint stock companies (SAOG's). During the year 2012, KPMG billed an amount of RO 63,600 towards professional services rendered to the Company.

24. Declaration

The Board of Directors declares its liability for preparation of the financial statements in accordance with the applicable standards and rules.

For the year under review the Board has conducted a review of the effectiveness of the Bank's internal control policies and procedures and is satisfied that the Bank's internal control are effective and that appropriate procedures are in place to implement the code's requirements.

The Board of Directors confirms that there are no material issues that affect the continuation of the company and its ability to continue its operations during the next financial year.

Omar Hussain Al Fardan
Chairman

Basel II - Pillar III Report 2012

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Sultanate of Oman

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Report to the Board of Directors of National Bank of Oman SAOG in respect of the Basel II – Pillar III Disclosures

We have performed the procedures agreed with you and as prescribed in the Central Bank of Oman ("CBO") Circular No. BM 1027 dated 4 December 2007 ("the Procedures") with respect to the Basel II – Pillar III disclosures ("the Disclosures"), set out on pages 26 to 42, of National Bank of Oman SAOG (the "Bank") as at and for the year ended 31 December 2012. The Disclosures were prepared by the Management in accordance with CBO Circular No. BM 1009 dated 13 September 2006 and Circular No. BM 1027 dated 4 December 2007. Our engagement was undertaken in accordance with the International Standard on Related Services applicable to agreed-upon procedures engagements. The Procedures were performed solely to assist you in evaluating the Bank's compliance with the disclosure requirements set out in CBO Circular No. BM 1009 dated 13 September 2006.

We report our findings as follows:

Based solely on performance of the Procedures, we found no exceptions which require to be reported herein.

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

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

Our report is solely for the purpose set forth in the first paragraph of this report and for your information and is not to be used for any other purpose or to be distributed to any other parties other than Central Bank of Oman; and we accept no liability to any third party. This report relates only to the Bank's Disclosures and does not extend to the financial statements of the Bank taken as a whole or to any other reports of the Bank.

24 January 2013

Paul Callaghan

Name: - NATIONAL BANK OF OMAN S.A.O.G

This is a standalone entity.

CAPITAL STRUCTURE

The authorised share capital of the bank as at 31 December 2012 is 2,000,000,000 shares of RO 0.100 each. The issued and paid up capital of the bank as at 31 December 2012 is 1,108,025,000 shares of RO 0.100 each

The bank in the prior years has deposited in UAE and Egypt, an amount of RO 5.5 million and RO 19.25 million respectively, of capital as support for its overseas branches. These amounts cannot be withdrawn without the approval of the Central Banks of the countries concerned.

The bank's capital structure as at close of 31 December 2012, based on Central Bank of Oman's (CBO) guidelines issued on the matter is as follows:

Sl. No.	Elements of Capital	Amount in RO 000's
	Tier I Capital	
	Local Banks	
1	Paid-up capital	110,803
2	Share premium	34,465
3	Legal reserve	39,586
4	General reserve	4,419
5	Subordinated debt reserve	25,800
6	Stock dividend	-
7	Retained earnings	65,069
8	Non-cumulative perpetual preferred stock	-
9	Other non-distributable reserve	-
	Foreign Banks	
10	Assigned capital	-
11	Capital deposits	-
12	Retained earnings	-
13	Interest free funds from HO	-
	Total Gross Tier I Capital	**280,142**
	Deductions	
14	Goodwill	-
15	Deferred tax asset	(409)
16	Intangible Assets, including cumulative unrealised losses recognised directly in equity	(54)
17	Reciprocal crossholding of bank capital, artificially designed to inflate the capital position of banks	-
	Sub-total	(463)
18	**Tier I capital after the above deductions**	**279,679**
19	50% of investments in the capital of banks and other financial entities, other than reciprocal cross holdings of bank capital	-
20	50% of Significant minority and majority investments in commercial entities, which exceed 5% of the bank's net worth for individual significant investments and 20% of the bank's net worth for aggregate of such investments	-
21	50% of shortfall in the regulatory capital requirements in the un-consolidated entities	-

CAPITAL STRUCTURE (continued)

Sl. No.	Elements of Capital	Amount in RO 000's
22	50% of investments in unconsolidated banking and financial subsidiary companies, associates or affiliates, etc	-
	Sub-total	-
23	**Tier I capital after all deductions**	**279,679**
	Tier II Capital	
24	Undisclosed reserves	-
25	Revaluation reserves / Cumulative fair value gains or losses on available for sale instruments	531
26	General loan loss provision/General loan loss reserve	29,222
27	Subordinated debt	35,900
28	Hybrid debt capital instruments	-
29	**Total Tier II Capital**	**65,653**
	Deductions	
30	50% of investments in the capital of banks and other financial entities, other than reciprocal cross holdings of bank capital	-
31	50% of Significant minority and majority investments in commercial entities, which exceed 5% of the bank's net worth for individual significant investments and 20% of the bank's net worth for aggregate of such investments	-
32	50% of shortfall in the regulatory capital requirements in the un-consolidated entities	-
33	50% of investments in un-consolidated banking and financial subsidiary company's associates or affiliates, etc	-
	Total deductions from Tier II	**-**
	Tier II Capital (Net)	**65,653**
34	**Tier III Capital (eligible)**	-
35	**Total Regulatory Capital**	**345,332**

Note: Retained earnings are after deduction of RO 19.4 million towards proposed cash dividend.

CAPITAL ADEQUACY

Qualitative Disclosures:

The ultimate objectives of capital management are three fold:

- Ensure stability of the bank by holding enough capital to cover unexpected loss.
- Enhance the efficiency of the bank, by increasing the risk adjusted return at various levels of aggregation (and there by insuring that too much "excess" capital is not held unnecessarily).
- Incentivize informed decision making and pro active risk management through an efficient and effective allocation of capital across the business.

The capital management plan envisaged for the bank is based on the regulatory risk capital framework of Basel II and using standardised approach for calculating the credit as well market risk and the basic indicator approach for operational risk as prescribed by CBO.

The capital management policy of the bank aims to ensure that on a risk adjusted return on capital basis (RAROC), individual lines of business are allocated an appropriate amount of capital. The RAROC model has been implemented for the entire portfolio except for Retail banking where the Central Bank of Oman has defined caps on interest rates, which are followed. In most cases capital is allocated to achieve the most efficient use of capital. However, instances exist for which the bank will allocate capital to a business line for strategic reasons.

CAPITAL ADEQUACY (continued)

The Asset Liability Committee (ALCO) currently reviews and monitors capital adequacy and requirement on an ongoing basis. Capital adequacy calculation is prepared and submitted for ALCO's review every month. Various stress scenarios, taking into account the earning volatility, credit and market risk impact along with capital allocation by line of business is reviewed in this forum.

Qualitative Disclosures:

A set of triggers is proposed as part of the capital management so as to provide the bank with an early warning system in terms of its level of capital, to enable it to take suitable measures at an early stage to prevent capital falling below acceptable limits.

The Bank has prepared an ICAAP (Internal Capital Adequacy Assessment Process) document in line with Basel II guidelines to evaluate all Enterprise-wide Risks that are not fully captured in the Pillar I Risks. The document addresses through objective and subjective evaluation, the adequacy of capital after considering the impact of the additional risks, such as, Residual Credit Risk, Residual Credit Risk Mitigation (CRM) Risk, Residual Credit Risk - Equity, Residual Market Risk - Currency, Credit Concentration Risk, Liquidity Risk, Interest Rate Risk in Banking Book, Settlement Risk, Reputation Risk, Strategic Risk and Compliance Risk as well as various levels of stress tests. Following the guidelines issued by the Central Bank of Oman in December 2011, assessment under ICAAP will be carried out and submitted to the Central Bank of Oman within the prescribed guidelines.

Quantitative Disclosures:

Position as at 31.12.12

(RO'000)

Sl. No.	Details	Amount
1	**Tier I capital (after supervisory deductions)**	**279,679**
2	**Tier II capital (after supervisory deductions & upto eligible limits)**	**65,653**
3	Tier III capital (upto a limit where Tier II & Tier III does not exceed Tier I)	-
4	Of which, total Eligible Tier III Capital	-
5	**Risk Weighted Assets (RWAs) – Banking Book**	**2,220,927**
6	**Risk Weighted Assets (RWAs) – Operational Risk**	**166,651**
7	**Total Risk Weighted Assets (RWAs) – Banking Book + Operational Risk**	**2,387,578**
8	Minimum required capital to support RWAs of banking book and operational risk	286,509
	i) Minimum required Tier I capital for banking book and operational risk	220,856
	ii) Tier II capital required for banking book and operational risk	65,653
9	Tier I capital available for supporting Trading Book	58,823
10	Tier II capital available for supporting Trading book	-
11	**Risk Weighted Assets (RWAs) – Trading Book**	**10,041**
12	Total capital required to support Trading Book	1,205
13	Minimum Tier I capital required for supporting Trading Book	343
14	Used Eligible Tier III Capital	-
15	**Total Regulatory Capital**	**345,332**
16	**Total Risk Weighted Assets – Whole bank**	**2,397,619**
17	**BIS Capital Adequacy Ratio**	**14.4**
18	Unused but eligible Tier III Capital	-

CAPITAL ADEQUACY (continued)

Certain additional capital adequacy disclosures are as follows:

Position as at 31.12.12

(RO'000)

Sl. No.	Details	Gross balance (Book value)	Net balance (Book value)	Risk Weighted Assets
1	On balance sheet item	2,580,323	2,488,123	1,867,296
2	Off balance sheet item	390,106	390,106	334,341
3	Derivatives	19,290	19,290	19,290
4	Operational Risk	-	-	166,651
5	Market Risk	-	-	10,041
6	**Total**	**2,989,719**	**2,897,519**	**2,397,619**
7	Tier I Capital	279,679	-	-
8	Tier 2 Capital	65,653	-	-
9	Tier 3 Capital	-	-	-
10	**Total Regulatory Capital**	**345,332**	**-**	**-**
10.1	Capital requirement for credit risk	266,511	-	-
10.2	Capital requirement for market risk	1,205	-	-
10.3	Capital requirement for operational risk.	19,998	-	-
11	**Total required Capital**	**287,714**	**-**	**-**
12	Tier I Ratio	11.7	-	-
13	**Total Capital ratio**	**14.4**	**-**	**-**

RISK EXPOSURE AND ASSESSMENT:

Risk Management

The primary objective of risk management is to safeguard the Bank's resources from the various risks which the Bank faces. The Risk Group comprises of Corporate Credit Risk, Retail Credit Risk, Market Risk, Operational Risk, Information Security and Business Continuity Risk, Legal Risk, Loan Review Mechanism and Remedial Management. All risk management functions report to Chief Risk Officer and are independent from Business Units.

The Bank's Credit Risk Strategy is aimed at adopting a structured approach to credit growth and de-emphasizing areas that are considered relatively high risk based on the prevailing and expected market conditions.

The administrative framework and the policies and procedures in place for the management of risks are based on international best practices, the recommendations of the Basel Committee and the guidelines of the Central Bank of Oman.

The Bank has exposure to the following risks:-

Credit Risk

Qualitative Disclosures:

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 and 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).

Credit Risk (continued)

The Bank manages and controls credit risk by setting internal limits on the amount of risk it is willing to accept for individual counterparties and groups (single obligors) and industry sectors in line with the guidelines of Central Bank of Oman. The Bank computes expected losses on credit exposure on the basis of risk classification of both corporate and retail loans in the delinquent category based on the guidelines of Central Bank of Oman. The objective of the Bank in management of credit risk is to protect the credit quality of its credit exposures. Credit Risk is managed within the regulatory requirement of Central Bank of Oman, risk framework provided in the Risk Charter and Credit Policies and Procedures.

The policies and procedures are periodically reviewed by the Management and the Board Risk Committee to ensure alignment to the current best practices. Credit exposures are approved by delegated authorities based on delegation by the Board and Board Risk Committee. The delegation of authorities is based on the size of the single obligor exposure, the credit quality (internal, external rating) as well as level of credit risk mitigation (collateral, guarantees, etc.) for the proposed exposures. For retail exposures, there is delegation of authority for handling exceptions to approved program lending. Control, monitoring and management of credit exposures are done in coordination with respective Business Units as per established procedures.

The Bank has in place a robust credit risk management structure comprising of Corporate Credit Risk, Retail Credit Risk, Loan Review Mechanism, Remedial Management and Credit Administration and Control Divisions.

Corporate Credit Risk:

Corporate Credit Risk Division is responsible for managing all Corporate, Business Banking and Financial Institutions exposures. The Division reviews and assesses credit risk for proposed exposures prior to facilities being committed to customers by the concerned business units. Renewals and reviews of facilities are subject to the same process. Each proposal is also assessed with respect to established concentration limits for various economic sectors, countries, risk grades, etc. and deviations, if any are highlighted. All Corporate and middle market customers are internally risk rated as per Moody's Risk Analyst and approved credit policy and procedures. Moody's long term foreign currency deposit ratings are used for risk rating financial institutions and country exposures. The Bank uses a RAROC model for risk based pricing and each credit proposal is assessed based on internal benchmarks of required risk adjusted returns. Each proposal is also assessed with respect to established concentrations limits for various economic sectors, countries, etc., in line with regulatory guidelines.

Proposals are approved by the delegated authorities based on total amount of facilities to a Single Obligor or Group (with common shareholding or management control as per internal and regulatory guidelines), obligor risk rating and collateral.

Credit risk at the Bank is managed in two dimensions, portfolio level and obligor level. In order to manage concentration risks, sector wise limits have been prescribed in the Credit Risk Policy. Limits have been put in place for Cross-border Risk and Sovereign Risk.

Retail Credit Risk:

Retail Credit Division manages the credit risk in the retail portfolio. Credit facilities are offered to retail customers primarily based on Product Programs. A programmed lending approach contains standard risk acceptance criteria and loan processing practices in order to optimize the efficiency and risk/ reward of those portfolios. Product programs are approved by Board Risk Committee and their performance is monitored on a regular basis and reviewed.

Based on the prevailing market conditions, the Bank sustained its continuous monitoring of the portfolio with a thorough review of the Credit Policy / Product Program. Credit facilities outside the Product Programs / Policy Parameters are individually reviewed and assessed by the Retail Banking division & the Retail Credit Risk Division.

Several system enhancements and new processes have been introduced across critical activities to improve processing quality and efficiency and to enhance the recovery methodologies of the retail portfolio. The Bank has implemented an automated Loan Collection System in order to enhance its collections and recovery processes. It also implemented an automated Loan Origination System to further enhance its Retail Credit Risk framework.

Loan Review Mechanism

An independent Loan Review Mechanism Division evaluates the quality of loan book, balance between risk and reward and brings about qualitative improvements in credit administration. The division evaluates effectiveness of loan administration, integrity of credit grading process, assessment of general and specific loan loss provisions, portfolio quality, etc.

Credit Risk (continued)

Remedial Management:

Remedial Management is responsible for relentlessly pursuing each delinquent account, by using all available measures, to reduce exposure to high risk groups, to maximize recoveries, rehabilitating these relationships so that they can be returned to the business lines as fully performing accounts and progressively improve the status of the portfolio.

Credit Administration and Control:

The Credit Administration and Control section ensures:

- Documentation for all loans is properly completed, executed and maintained.
- The correct approving authority approves credit lines and details are accurately recorded.
- Production of adequate and accurate reports covering various credit risk exposures.
- Irregularities are reported and corrective action is taken.
- Review of and participation in any new/existing product offerings of the Bank.
- Various internal reporting and external reporting is prepared on a periodical basis.
- That all approved limits are input into the system under a “maker and checker” concept.
- Disbursement of funds for all approved credit exposures is appropriately authorized.

Risk Reporting and Measurement Systems

The scope and nature of the risk reporting and/or measurement system are as follows:

Risk Reporting

A comprehensive review of the Corporate Credit Portfolio is conducted on a quarterly basis and provided to the Senior Management and the Risk Committee of the Board. Salient areas covered in the review include:

- Exposures downgraded/negatively migrated
- Weighted average credit grade profile
- Portfolio concentration/ performance
- Position of restructured exposures
- Position of past due exposures
- Exposures secured by equity
- Exposures to real estate and leasing sectors
- Syndicated exposures
- New relationships
- Exposures to senior members and non-resident borrowers
- Exposures to countries / financial institutions

In addition, the bank conducts industry studies in various sectors considered to have a bearing on the portfolio credit quality, such as, real estate, leasing, and sectors impacted by volatility in commodity prices. For FIG exposures the bank conducts stress tests and quarterly reviews of adverse rating migrations and outlooks in line with best practices and regulatory guidelines. These reports are reviewed periodically by the Management and Board Risk Committees.

A review of the Retail Credit Portfolio is conducted on a monthly basis and provided to the Management Risk Committee, and every quarter the latest report is presented to the Board Risk Committee. Salient areas covered in the review include:

Credit Risk (continued)

- Portfolio review
- Management summary, delinquency and NPA trends (including product-wise delinquency analysis, vintage analysis, delinquencies across various credit criteria, etc.)
- Projects undertaken / fulfilled during the month
- Recoveries

Measurement:

Currently the Bank computes the expected losses on its credit exposure on the basis of risk classification of both corporate and retail loans to delinquent category based on extant guidelines of the Central Bank.

Policies for hedging and/or mitigating risk and strategies are in place for monitoring the continuing effectiveness of hedges/ mitigants. The Bank obtains collateral/ credit mitigants against loans and advances in the form of mortgage over property, pledges over cash/ securities, guarantees, etc. Estimates of fair value are based on the value of the collateral assessed at the time of borrowing and at regular intervals as per internally approved procedures - every three years for properties, daily for equities, etc. Collateral generally is not held against credit exposures to banks.

Definition of past due and impaired (for accounting purpose):

A loan, where repayments of principal and interest are pre-determined, shall be considered as past due, when it has not been paid on the due date fixed by the Bank, as per terms of sanction.

- Credit facilities like overdrafts, lines of credit, etc. where no definite repayments are pre-determined shall be treated past due, if:
- The outstanding balance remains continuously in excess of 10% of the sanctioned/authorized limit, or
- In cases where the outstanding balance in the principal operating account is less than the sanctioned/authorized limit, but there are not enough credits in the account to cover the interest charged, or
- In cases where unauthorized drawings have frequently been allowed.
- Bills, which remain unpaid on due dates, shall be considered as past due.

All loans and advances, which are classified as substandard, doubtful and loss, are categorized as Non-Performing Loans (“NPL”) i.e. impaired assets.

An evaluation in made on an ongoing basis, at least quarterly, to determine whether there is objective evidence that a specific financial asset may be impaired. If such evidence exists, the estimated recoverable amount of that asset is determined and any impairment loss, based on the net present value of future anticipated cash flows, recognized in the income statement.

Credit Risk Management Policy:

A comprehensive set of Corporate Credit Risk Policy and Procedures Manuals, provides detailed policy guidelines and embedded in which are the regulatory/ in-house limits. Further, procedures manuals provide detailed process guidelines about the credit process and the templates to be used to process the individual credit applications. Financial Institutions Group (FIG) exposures are managed as per the Financial Institutions Policy guidelines. Retail Credit Policy outlines the policy guidelines related to retail banking and covers product programs and parameters relating to Salary Related Loans, Mortgages, Credit Cards and other retail product offerings. Credit Policies and Procedures are periodically reviewed to ensure that they are aligned to the market and regulatory guidelines.

Credit Risk (continued)

Quantitative Disclosure:

i Total gross credit exposures, plus daily average of gross exposure over the period broken down by major types of credit exposure as at 31 December 2012:

(RO'000)

Sl. No.	Type of Credit Exposure	Average Gross Exposure		Total Gross Exposure as at	
		Current Year	Previous Year	31 December 12	31 December 11
1	Overdrafts	45,606	47,259	39,630	43,051
2	Personal loans	883,158	696,029	963,568	780,272
3	Loans against trust receipts	49,487	40,082	57,286	38,723
4	Other loans	896,679	802,981	906,332	852,025
5	Bills purchased / discounted	25,145	15,471	19,576	19,617
6	Any other	-	-	-	-
	Total	**1,900,075**	**1,601,822**	**1,986,392**	**1,733,688**

ii Geographic distribution of exposures, broken down to in significant area by major types of credit exposure as at 31 December 2012:

(RO'000)

Sl. No.	Type of Credit Exposure	Oman	Other GCC countries	OECD countries	India	Pakistan	Others	Total
1	Overdrafts	32,544	6,852	-	-	-	234	39,630
2	Personal loans	960,965	2,011	-	-	-	592	963,568
3	Loans against trust receipts	52,504	4,782	-	-	-	-	57,286
4	Other loans	847,258	57,412	-	-	-	1,662	906,332
5	Bills purchased / discounted	19,576	-	-	-	-	-	19,576
6	Any other	-	-	-	-	-	-	-
	Total	**1,912,847**	**71,057**	**-**	**-**	**-**	**2,488**	**1,986,392**

Credit Risk (continued)

iii Industry or counter party type distribution of exposures, broken down by major types of credit exposure as at 31 December 2012:

(RO'000)

Sl. No.	Economic Sector	Overdraft	Loans	Bills Purchased / Discounted	Others	Total	Off Balance Sheet Exposure
1	Import trade	-	-	-	52,504	52,504	31
2	Export trade	-	327	-	-	327	-
3	Wholesale and retail trade	9,150	103,233	503	4,523	117,409	43,050
4	Mining and quarrying	837	34,530	828	-	36,195	736
5	Construction	5,356	138,179	10,182	259	153,976	139,110
6	Manufacturing	3,744	135,212	250	-	139,206	33,936
7	Electricity, gas and water	-	89,929	249	-	90,178	49,356
8	Transport and Communication	389	112,990	-	-	113,379	5,798
9	Financial institutions	9,799	84,651	-	-	94,450	188,126
10	Services	2,114	108,282	3,734	-	114,130	28,688
11	Personal loans	-	963,568	-	-	963,568	195
12	Agriculture and allied activities	931	11,808	41	-	12,780	368
13	Government	32	385	-	-	417	14,092
14	Non-Resident lending	-	32,835	-	-	32,835	-
15	All Others	7,278	53,971	3,789	-	65,038	13,137
	Total	**39,630**	**1,869,900**	**19,576**	**57,286**	**1,986,392**	**516,623**

iv Residual contractual maturity as at 31 December 2012, in line with guidelines issued by CBO, breakdown of the whole portfolio, broken down by major types of credit exposure is as follows:

(RO'000)

Sl. No.	Time Band	Overdraft	Loans	Bills Purchased / Discounted	Others	Total	Off Balance Sheet Exposure
1	Up to 1 month	1,982	147,945	10,332	20,688	180,947	94,719
2	1-3 months	1,982	250,308	8,021	20,287	280,598	138,853
3	3-6 months	1,982	36,234	1,223	16,093	55,532	77,447
4	6-9 months	1,982	24,548	-	218	26,748	91,411
5	9-12 months	1,982	82,247	-	-	84,229	55,564
6	1-3 years	9,907	185,992	-	-	195,899	41,725
7	3-5 years	9,907	148,543	-	-	158,450	3,424
8	Over 5 years	9,906	994,083	-	-	1,003,989	13,480
	Total	**39,630**	**1,869,900**	**19,576**	**57,286**	**1,986,392**	**516,623**

Credit Risk (continued)

v Total loan broken down by major industry or counter party type as at 31 December 2012:

(RO'000)

Sl. No.	Economic Sector	Gross Loans	Of which, NPLs	General Provisions held	Specific Provisions held	Reserve Interest	Provisions made during the year	Advances written off during the year
1	Import Trade	52,504	-	525	-	-	-	-
2	Export Trade	327	327	-	327	-	-	-
3	Wholesale & Retail Trade	117,409	11,727	1,057	3,836	6,165	749	33
4	Mining & Quarrying	36,195	-	362	-	-	-	-
5	Construction	153,976	8,759	1,452	5,655	4,204	255	29
6	Manufacturing	139,206	5,599	1,336	4,346	2,660	2,475	75
7	Electricity, gas and water	90,178	-	902	-	-	-	706
8	Transport and Communication	113,379	1,673	1,117	663	407	301	-
9	Financial Institutions	94,450	-	945	-	-	-	-
10	Services	114,130	1,015	1,131	458	481	23	114
11	Personal Loans	963,568	16,173	18,950	6,632	1,390	9,433	5,760
12	Agriculture and Allied Activities	12,780	5,239	75	476	742	150	-
13	Government	417	-	4	-	-	-	-
14	Non-Resident Lending	32,835	-	328	-	-	-	-
15	All Others	65,038	2,686	1,038	6,386	780	3,555	-
	Total	**1,986,392**	**53,198**	**29,222**	**28,779**	**16,829**	**16,941**	**6,717**

vi Amount of impaired loans as at 31 December 2012, broken down by significant geographical areas including, with the amounts of specific and general allowances related to each geographical area:

(RO'000)

Sl. No.	Country	Gross Loans	Of which NPL's	General Provisions Held	Specific Provisions Held	Reserve Interest	Provisions made during the year	Advances written off during the year
1	Oman	1,912,847	37,961	28,533	19,143	13,319	15,859	6,246
2	Other GCC Countries	71,057	12,779	688	7,252	3,408	1,079	186
3	OECD Countries	-	-	-	-	-	-	-
4	India	-	-	-	-	-	-	-
5	Pakistan	-	-	-	-	-	-	-
6	Others	2,488	2,458	1	2,384	102	3	285
	Total	**1,986,392**	**53,198**	**29,222**	**28,779**	**16,829**	**16,941**	**6,717**

Credit Risk (continued)

vii Movements of gross loans

(RO'000)

Movement of Gross Loans during the year ended 31 December 2012							
Sl. No.	Details	Performing Loans		Non-performing Loans			
		Standard	Special Mention	Sub-Standard	Doubtful	Loss	Total
1	Opening balance	1,590,171	79,480	15,800	20,282	27,955	1,733,688
2	Migration / changes (+/-)	(36,795)	24,739	3,022	(997)	10,031	-
3	New loans	808,320	763	123	1,652	2,963	813,821
4	Recovery of loans	(495,114)	(38,370)	(11,956)	(2,542)	(6,418)	(554,400)
5	Loans written off	-	-	-	-	(6,717)	(6,717)
6	Closing balance	1,866,582	66,612	6,989	18,395	27,814	1,986,392
7	Provisions held	28,429	8,644	1,810	6,409	12,709	58,001
8	Reserve interest	-	2,869	283	1,737	11,940	16,829

Credit Risk – Disclosures for portfolios subject to the standardized approach.

Qualitative Disclosures:

- The bank is following Moody's rating for both sovereign and interbank transaction (exposure) and the balance exposure is treated as unrated at 100% risk.
- With the approval of the CBO, the bank uses the discretion to treat loans and advances as unrated at risk weight of 100%, except housing loans which are risk weighted at 35% based on the requirements as stipulated in the guidelines issued by CBO.
- Similarly, with the approval of CBO, the bank uses the discretion of the simple approach for recognising collaterals.

Credit Risk (continued)

Quantitative Disclosures:

Exposure amount as at 31 December 2012, subject to the standardized approach is as below:

(RO'000)

Sl. No.	Product / Rating	Carrying 0%	Carrying 20%	Carrying 35%	Carrying 50%	Carrying 100%	Carrying 150%	Total
	Rated							
1	Sovereign	332,367	-	-	-	1,268	-	333,635
2	Banks	-	109,438	-	68,455	61,567	6,592	246,052
	Unrated							
3	Corporate	-	48,648	-	-	707,872	-	756,520
4	Retail	-	-	-	-	780,609	-	780,609
5	Claims secured by residential property	-	-	155,298	-	21,444	-	176,742
6	Claims secured by commercial property	-	-	-	-	142,998	-	142,998
7	Past due loans			-	-	48,015	-	48,015
8	Other assets	31,175	2,922	-	-	48,265	9,907	92,269
9	Venture Capital & Private Equity Investments	-	-	-	-	-	3,483	3,483
10	Off-balance Sheet Items	2,818	11,343	-	87,744	307,491	-	409,396
	Total Banking Book	**366,360**	**172,351**	**155,298**	**156,199**	**2,119,529**	**19,982**	**2,989,719**

Credit Risk Mitigation

Qualitative Disclosures:

The bank holds collateral against loans and advances to customers in the form of cash, government development bonds, acceptable financial securities, mortgage interest over property, other registered charge over assets and guarantees. Estimates of fair value are based on the value of the collateral assessed on an on-going basis.

The Bank has adopted the simple approach for collaterals.

Quantitative Disclosures:

(RO'000)

Sl. No.	Details	Amount
1	Corporate 100% Cash	40,001
2	Specific provisions on loans and advances and due from banks	52,199
3	**Total**	**92,200**

The capital requirement on credit risk as at 31 December 2012 is RO ('000) 266,511.

Market Risk

Market Risk arises from fluctuations in interest rates, foreign exchange rates and equity prices. The board has set limits for acceptable levels of Market Risk. The Assets and Liabilities Committee (ALCO) monitors this on a regular basis. Market Risk is managed based on Central Bank of Oman guidelines and the Market Risk Policy, which is approved and periodically reviewed by the Risk Committee of the Board. Separate market risk policies exist for the Bank's operations in Egypt and UAE to make them compatible with the local regulatory and operational environments. Stress tests are also conducted periodically to analyze the impact of bank and market specific crises on the earnings and capital of the Bank. Variables include movements in equity value, foreign exchange, etc. The results are reviewed by ALCO, Management and Board Committees.

Market Risk Division provides risk-weightings for treasury products in line with best practices based on potential future exposure. The middle-office along with Treasury and Investment Banking Operations monitors the Market Risk positions of the Bank.

Market Risk (continued)

Trading Book

The exposure under the trading book of the Bank includes relatively small foreign exchange exposure primarily arising from the holding of day-end positions in currencies overnight, and exposure towards interest rate related instruments. Value-at-risk (VaR) is computed every month for all non-pegged currencies in which the Bank's end-of-the-day position is above a minimum threshold. The VaR is reviewed by ALCO, Management Risk Committee and Board Risk Committee.

Procedure: For the purpose of capital charge, the three month average of the sum of the net short positions or net long positions, whichever is higher, is taken. The average is worked out on the basis of the actual positions as obtained on all the working days during the three month period immediately preceding the reporting date. The capital charge is computed at 12% to reflect the general market risk.

Capital required for trading book as at 31 December 2012:

- Foreign Exchange Risk - RO ('000) 1,205

Banking book

Equity Price Risk

The proprietary equity positions are held in the 'Available for Sale' category and not in the 'Held for Trading' category. As such, no VaR is calculated on the equity investments of the Bank as in the entire equity portfolio is held in the 'Available for Sale' category for medium to long term income and capital appreciation. The market risk is monitored though daily Mark to Market reports which are circulated to the management and required actions, if any, are promptly taken as per the Investment Policy, which inter-alia provides sector concentration limits, trigger levels and other guidelines for prudent management of the portfolio.

Interest Rate Risk

The principal market risk to which non-trading portfolio is exposed is the risk of loss from fluctuation in the future cash flows or fair values of financial instruments because of changes in market interest rates. 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 re-pricing of assets and liabilities.

Interest rate risk is managed by monitoring the sensitivity of the Bank's financial assets and liabilities to various standard interest rate scenarios. Standard scenarios that are considered on a monthly basis include a 200 basis point (bp) parallel fall or rise in yield curves to review the impact on the economic value of the assets and liabilities and the equity of the Bank, a 200 basis points (bp) parallel fall or rise in yield curve for the time period up to one year to review its impact on the earnings of the Bank.

In respect of monitoring the impact of interest rate changes on the earnings of the Bank, the Bank has set internal limits. Positions are monitored on a monthly basis and hedging strategies used to ensure positions are maintained within established limits.

Methods and assumptions used in preparing the sensitivity analysis: The methods for interest rate sensitivity analysis are: traditional Maturity Gap Analysis (to measure the interest rate sensitivity of earnings), and Duration (to measure interest rate sensitivity of capital): methodology provided by BIS in its paper on 'Principles for the Management and Supervision of Interest Rate Risk' issued in July 2004.

Quantitative Disclosures:

The assumptions used to measure the sensitivity is parallel shift in interest rate by 200 basis points (bps) to measure the interest sensitivity of earnings and interest rate sensitivity of capital.

As at December 2012	200 bps increase	200 bps decrease
Earnings impact - RO'000s	9,087	(9,087)
Earnings impact - USD'000s	23,602	(23,602)

The bank has been consistently using the above methods/assumptions to conduct interest rate sensitivity analysis. The analysis is carried out at monthly rests and results thereof monitored against the in-house prescribed limits; the results are also actively deliberated at the ALCO meetings. There have not been any significant changes in interest rate risk management process in the bank during the year.

Interest Rate Risk (continued)

The bank's interest sensitivity position, in line with guidelines issued by Central bank of Oman, based on contractual re-pricing arrangements at 31 December 2012 was as follows:

	Average effective interest rate	On demand within 3 months RO'000	3 to 12 months RO'000	1 to 5 years RO'000	Over 5 years RO'000	Non interest sensitive RO'000	Total RO'000
Cash and balances with Central Banks	0.08%	28,554	-	-	-	187,184	215,738
Due from banks and other money market placements	1.53%	195,373	21,888	-	-	-	217,261
Loans and advances (net)	5.67%	822,246	296,461	361,907	393,077	37,871	1,911,562
Non-trading financial investments	3.00%	6,870	10,000	73,115	-	20,737	110,722
Premises and equipment	N/A	-	-	-	-	20,498	20,498
Deferred tax assets	N/A	-	-	-	-	409	409
Other assets	N/A	-	-	-	-	61,628	61,628
Total assets		**1,053,043**	**328,349**	**435,022**	**393,077**	**328,327**	**2,537,818**
Due to banks and other money market deposits	1.59%	210,447	-	-	-	-	210,447
Customers' deposits	1.89%	212,521	686,977	343,400	-	643,856	1,886,754
Other liabilities	N/A	-	-	-	-	68,778	68,778
Taxation	N/A	-	-	-	-	5,687	5,687
Subordinated funds	6.55%	-	-	54,700	7,000	-	61,700
Shareholders' equity	N/A	-	-	-	-	304,452	304,452
Total liabilities and shareholders' equity		**422,968**	**686,977**	**398,100**	**7,000**	**1,022,773**	**2,537,818**
Total interest rate sensitivity gap		**630,075**	**(358,628)**	**36,922**	**386,077**	**(694,446)**	**-**
Cumulative interest rate sensitivity gap		**630,075**	**271,447**	**308,369**	**694,446**	**-**	**-**

Liquidity Risk

Qualitative Disclosures:

Liquidity may be defined as a bank's ability to ensure the availability of funds to meet all on-balance sheet and off-balance sheet commitments at a reasonable price. Liquidity Risk can in turn be defined as the risk to earnings and capital arising from a bank's potential inability to meet its liabilities when they become due. Conversely, liquidity risk also manifests itself in the form of opportunity losses due to holding excess liquidity relative to liabilities.

The strategy of the Bank in management of liquidity risk is to minimize the resultant impact on the earnings of the Bank. 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 manages the liquidity risk based on Central Bank of Oman guidelines and Liquidity Risk Policy and Liquidity Contingency Policy.

Process: NBO takes a two-tiered approach to Liquidity Risk Management

Going concern Liquidity Management - management of the liquidity position within specified parameters to ensure all liabilities can be met on a timely basis.

Liquidity Risk (continued)

Event Risk Liquidity Management - ensuring that in the event of either a firm-specific or general market event, the Bank is able to generate sufficient liquidity to withstand a short term liquidity crisis. Event Risk Liquidity Management includes the following tools:

- Stress test: a quantitative analysis of liquidity impact of several (market and bank specific) liquidity crises.
- Liquidity buffer: mitigation of an event risk is achieved through the provision of standby liquidity in the form of unencumbered, Central Bank eligible collateral and stand-by lines.
- Contingency Funding Plan: A comprehensive Liquidity Contingency Plan is in place at the Bank.

The overall Liquidity Risk is kept at such a level that NBO is able to resume its business after a specified crisis.

Treasury division of the Bank 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. Treasury division maintains a portfolio of short-term liquid assets, largely made up of short-term liquid investment securities and inter-bank facilities, to ensure that sufficient liquidity is maintained within the Bank as a whole.

The Bank is subject to liquidity limits prescribed by the CBO. Additionally, the bank has also set internal mismatch limits by currency and limits for ensuring that liquidity lines are sufficient to meet short term maturing obligations.

The monthly liquidity position is monitored through the Statement of Maturities of Assets and Liabilities to ensure that the gaps are within the limits prescribed by the regulator and those set in-house. The Bank also periodically conducts stress tests on liquidity based on market and bank specific events.

Management periodically reviews the strategy and policies related to management of liquidity to ensure that necessary actions are implemented for monitoring and controlling liquidity risk.

The Bank has in place a state an effective and efficient liquidity risk management structure comprising an active ALCO which meets at monthly intervals and more frequently, if required. ALCO is kept informed regularly of the liquidity situation of the Bank and immediately if there are any material changes in the Bank's current or prospective liquidity position.

The scope and nature of the risk reporting and/or measurement system:

Scope and Nature of Risk Reporting:

A statement: Maturities of Assets and Liabilities is prepared on a monthly basis and more frequently, as required, by the Financial Control Division which contains the maturity profile of the various assets and liabilities and off-balance sheet items. The statement contains the cumulative gaps vis-à-vis cumulative liabilities for each prescribed time band and the position of these gaps vis-à-vis the Regulatory and in-house limits is also reported therein. This statement is placed before the ALCO at its meetings and in case any of the gap limits is exceeded the same is escalated immediately to the ALCO along with analysis and further action planned to bring the position within the limits.

A Liquidity Lines statement is also prepared based on assumptions set out in the Liquidity Policy to evaluate the Bank's ability to meet its liabilities maturing in one month time band. Further, the liquidity of the Bank is assessed under bank specific and market specific stress scenarios and impact on gap positions and Liquidity Lines is estimated. Daily Financial Risk Report is used for monitoring the daily ratios and gaps and Early Warning Indicators for assessing any potential liquidity impact of leading indicators. These reports are regularly reviewed by the ALCO, Management and Board Risk Committee.

Measurement:

The monitoring and control of Liquidity Risk is done on an ongoing basis. The Bank uses the maturity ladder approach, which calculates the cumulative surplus or deficit of funds at selected time bands. The cash flows are placed in different time bands based on future behavior of assets, liabilities and off-balance sheet positions. In order to ensure uniformity in the treatment of behavioral patterns of assets, liabilities and off-balance sheet positions, the Central Bank has evolved a broad framework, which has been subscribed to by the Bank. In addition, the Bank regularly evaluates its liquidity position with respect to the liquidity ratios prescribed in the Liquidity Risk Policy.

Liquidity Risk (continued)

Policies for hedging and/or mitigating risk and strategies and processes for monitoring the continuing effectiveness of hedges/mitigants:

The Bank has put in place "Liquidity Risk Policy" and "Liquidity Contingency Plan"- duly approved by the Board Risk Committee, which provides detailed guidelines for mitigating the risk. In case of a contingency, the policy provides a blue-print for asset sales, market access and restructuring the maturity and composition of assets and liabilities.

As an on-going mitigant the Bank has in place the availability of liquidity support in the form of committed lines of credit and reciprocal arrangements. The continuing availability of the CBO liquidity window, which was introduced in the wake of the global financial crisis, is also one of the mitigants of the liquidity risk. Besides, the Bank ensures the liquidity of certain assets as per the Liquidity Contingency Plan as a buffer against liquidity events.

The Bank has also put in place Country and Transfer Risk Policies to primarily control and monitor cross border exposures.

Quantitative Disclosures:

The maturity profile of the assets and liabilities in line with guidelines issued by Central bank of Oman, at 31 December 2012 was as follows:

	On demand within 3 months RO'000	3 to 12 months RO'000	Subtotal less than 12 months RO'000	1 to 5 years RO'000	Over 5 years RO'000	Subtotal over 12 months RO'000	Total RO'000
Cash and balances with Central Banks	128,296	34,973	163,269	32,456	20,013	52,469	215,738
Due from banks and other money market placements	168,512	48,749	217,261	-	-	-	217,261
Loans and advances (net)	461,545	110,386	571,931	354,349	985,282	1,339,631	1,911,562
Non-trading financial investments	89,985	-	89,985	20,737	-	20,737	110,722
Premises and equipment	-	-	-	-	20,498	20,498	20,498
Deferred tax assets	409	-	409	-	-	-	409
Other assets	59,737	1,797	61,534	94	-	94	61,628
Total assets	**908,484**	**195,905**	**1,104,389**	**407,636**	**1,025,793**	**1,433,429**	**2,537,818**
Due to banks and other money market deposits	104,572	9,625	114,197	96,250	-	96,250	210,447
Customers' deposits	409,083	597,154	1,006,237	540,303	340,214	880,517	1,886,754
Other liabilities	58,091	7,194	65,285	3,493	-	3,493	68,778
Taxation	5,687	-	5,687	-	-	-	5,687
Subordinated funds	-	-	-	54,700	7,000	61,700	61,700
Shareholders' equity	-	-	-	-	304,452	304,452	304,452
Total liabilities and shareholders' equity	**577,433**	**613,973**	**1,191,406**	**694,746**	**651,666**	**1,346,412**	**2,537,818**

Operational Risk

Operational risk is the risk of loss arising from systems failure, human error, fraud or external events. When controls fail to perform, operational risks can cause damage to reputation, have legal or regulatory implications, or lead to financial loss. The Bank cannot expect to eliminate all operational risks, but through a control framework and by monitoring and responding to potential risks, the Bank is able to manage the risks. Controls include effective segregation of duties, access, authorization and reconciliation procedures, staff training and assessment processes, including the use of internal audit.

The bank follows basic indicator approach for determining operational risk.

The Capital charge for operational risk under Basic Indicator approach is calculated by taking the average of gross income multiplied by 15%, for each of the last three financial years, excluding years of negative or zero gross income. The gross income is Net interest income (+) Non interest income (+) Provisions for unpaid interest (-) realized profit on sale of Held to Maturity (HTM) and Available for Sale (AFS) investments (-) extraordinary / irregular items of income.

Capital requirement for operational risk as per Basel II is RO (000s) 19,998.

Insurance is another tool used by the bank as an operational risk mitigant. Insurance such as Bankers' Blanket Bond, Electronic and Computer Crimes, Professional Indemnity, incomplete transactions, etc as obtained by the Bank aim at protecting the Bank from high severity risks by reducing the financial impact of the same.

In addition to the above and in order to keep control of operational incidences / losses the bank has set in place a special operational risk appetite against which incidents / losses are being monitored regularly for possible breaches and appropriate mitigates are put in place.

This report on Basel II disclosures set out from pages no 26 to 42 was authorized for issue by the Board of Directors on 24 January 2013.

Omar Hussain Al Fardan
Chairman

Management Discussion and Analysis Report 2012

Economic Development

The Oman economy experienced a strong GDP growth estimated to be around 8.3% in year 2012. This growth is driven primarily by expanding government spending and domestic demand, both boosted by high oil prices, which continued to trade at or around $109 per barrel in December. The inflation rate during 2012 remained within the government's targeted limit at approximately 3%. Total credit grew by 14.4%, whilst total deposits increased by 12.7% during 2012.

The government is looking to maintain growth and increase employment this year, with higher allocations for capital works projects in the 2013 budget. Public expenditure, approved in the budget 2013, amounts to RO 12.9 billion, an increase of 29% compared with 2012. The budget for the development expenditure programs of the Ministries and Government units has been enhanced by 30% to assist with the completion of infrastructure projects.

The new budget also includes 40% increase in spending on education, job creation programs and social support schemes, many of which are aimed at providing young Omanis with the skills to enter the private sector. Considering the above factors, Oman economy is budgeted to grow by 7% in 2013.

GDP growth 2012

The Oman economy experienced a strong GDP growth estimated to be around 8.3% in year 2012. This growth is driven primarily by expanding government spending and domestic demand, both boosted by high oil prices, which continued to trade at or around $109 per barrel in December.

Industry Structure and Development

The financial sector in Oman is broadly classified into the following categories:

- Central Bank of Oman
- Commercial and specialized banks
- Non-banking financial institutions
- Brokerage and finance houses
- Money Exchange companies

The Central Bank of Oman provides oversight and regulatory supervision to the banking and non-banking Finance Companies.

Commercial banks in Oman provide a full range of banking services in both domestic and foreign currencies for both corporations and individuals; some of these banks also provide investment services including brokerage for the Muscat Securities Market.

Non-banking financial institutions play a traditional retail role in small ticket consumer financing as well as hire purchase, auto finance and leasing.

Other institutions including government sponsored and pension funds, insurance companies and mutual funds also play a part in the overall provision of capital and liquidity in Oman. Corporate Governance standards are set by the Capital Markets Authority, which together with the Muscat Securities Market, facilitate the smooth running of the local bourse as well as the issue of new securities.

Further to the approval from CBO, currently there are two new Islamic banks established in Oman expected to commence operations in 2013.

Oman Banking sector – Year 2012

The Oman Banking sector reported a strong growth in the year 2012. Total assets increased to RO 20.96 billion as at December 2012 against RO 18.4 billion in December 2011, an increase of 13.9%. Cash on hand and deposits of commercial banks with CBO increased to RO 1.57 billion at the end of December 2012 compared to RO 978 million for the same period the previous year. Total credit grew by 14.4% to RO 14.3 billion as at December 2012 which accounted for 68% of the total assets. While credit to the Government sector declined by 4.9%, credit to public enterprises and the private sector increased by 16.4 % and 14.9 % respectively. Investments in securities by commercial banks declined by 3.2% during the year 2012 as compared to 2011.

Banking sector growth 2012

The Oman Banking sector reported a strong growth in the year 2012. Total assets increased to RO 20.96 billion as at December 2012 against RO 18.4 billion in December 2011, an increase of 13.9%.

On the liabilities side of the balance sheet, total deposits in Rial Omani as well foreign currency witnessed a year on year growth of 12.7% to RO 14.2 billion in December2012 from RO 12.6 billion in December 2011. Private sector deposits increased by 12.3% to close at RO 9 billion at December2012 against RO 8 billion a year ago. Government deposits grew by 17.3% whereas deposit of public enterprises marginally declined by 0.01 billion to close at RO 0.97 billion for the year 2012.

Overall, the banking sector in Oman is set for healthy growth in the year 2013. Heavy government expenditure as indicated earlier is expected to foster credit expansion. New Islamic banks expected to start the operations in the year ahead will also bring with them fresh challenges. Compliance with the regulatory requirement for minimum capital for conventional banking, as well as Islamic banking, will definitely form an agenda with most banks this year.

National Bank of Oman 2012

In Dec 2012, the Fitch rating agency assigned a long term issuer default rating of BBB+ with a stable outlook. The report highlights the Bank's performance in 2012 and the strategic decisions that focus on business expansion and diversification. The report further highlights the fact that the Bank has increased the Retail lending despite recent Central Bank of Oman (CBO) regulations, and also increasing its share of low-cost deposits. Commenting on the Bank's good balance sheet liquidity, the report states that the objective of the Bank to diversify the franchise by moving into new or underrepresented segments has yielded encouraging results till date.

Synergies with Strategic Partner, Commercial Bank of Qatar (CBQ)

National Bank of Oman continues to work closely with its strategic alliance partner, Commercial Bank of Qatar, in many areas including cross-border business and the sharing of global best practice in terms of products, processes and systems.

Islamic Banking

The Bank has launched its Sharia compliant brand named 'Muzn'. Muzn offers a rich bouquet of products and services which cater to institutional, corporate and retail clientele. The Bank will progressively open more Muzn branches in all regions.

Financial Performance

The Bank achieved a net profit after tax of RO 40.7 million for the twelve months ended 31 December 2012 compared with RO 34.2 million for 2011, an increase of 19%. The overseas operations continued to contribute to the overall net profit of the Bank with an addition of RO 0.9 million for the current year. The Bank is in the process of implementing the exit strategy of its operations in Egypt; two branches have accordingly been closed during the course of 2012.

The operating profit of the Bank grew from RO 48.8 million in 2011 to RO 52.0 million for the year ended December 2012. The operating income increased to RO 98.6 million from RO 92.2 in the previous year, an increase of 6.9%, due, mainly, to an increase in the net interest income arising from higher loan disbursals and lower cost of funds.

The increase of RO 180 million in the Bank's low cost deposits during the year 2012 has led to an overall decrease in the cost of funds from 2.13% at close of 2011 to 1.98% at close of 2012. Net spreads stood at 3.09% as at December 2012.

Operating expenses were RO 46.7 million and have increased by RO 3.2 million or 7% over the previous year. The increase can be mainly attributed to higher staff costs and marketing expenses.

Net cost of credit at RO 5.3 million at close of December 2012 is 48% lower than the previous year, predominantly due to, a reduction in the credit loss expense and impairment of investments.

The Bank grew its net advances by RO 241 million to RO 1.9 billion at the end of December 2012, an increase of 14.4% over 2011. Customer deposits increased by 17.9% and stood at RO 1.9 billion as at close of December 2012 compared with RO 1.6 billion at 31 December 2011.

The performance of various segments is covered in detail in the financial statements under segmental information (note 31) of the financial statements for the year ended 31 December 2012.

KEY DEVELOPMENTS - CORE SEGMENTS

Retail and Private Banking

The Retail Banking Division has again improved on the records set for business growth and profitability. It has also introduced new innovative products that have been well received by the market. Quality assets have been booked and market share for Low-Cost Deposits and Housing Loans has been substantially increased.

The Bank, through its Retail Banking Division, has continued to invest in customer facing initiatives, which included a network of 66 branches as at December 2012. Additionally, the Bank has commenced a migration to "Full Function" ATM's that cater to both deposits and withdrawals. As a first in Oman, the Call Centre continues to operate 24 hours to cater to its valued customers. Mobile Banking, the Mobile Branch, Top-Ups and Bill Payments were all launched with great success and well received by customers.

The Bank's Wealth Management Division introduced its new Private Banking services that have successfully launched a new wealth management system. Yet another first in Oman, this division offers the Reliance Portfolio Management service to all Non Resident Indians as well as Omani's. It has also launched the Infinity Card, Direct Debit services and introduced the Afaaq programme that rewards all Sadara customers with exclusive offers from selected merchants. Other initiatives include the launch of Online Insurance Sales as well as the Small Business Unit which focusses on assisting established businesses to grow their businesses to the next level.

New Wealth Management Services

The Bank's Wealth Management Division introduced its new Private Banking services that have successfully launched a new wealth management system. Yet another first in Oman, this Division offers the Reliance Portfolio Management service to all Non Resident Indians as well as Omani's.

Both the Elite and Al Kanz Millionaire savings account scheme continued to set new records with continued growth in market share during 2012. With these leading products, the Retail Banking Division has been able to successfully grow its market share by more than three percent. The Al Manzel product is regarded as the leading Housing Loan Finance product in Oman with the fastest turnaround time and lowest interest rates.

A number of Credit Card promotions were successfully launched in the summer of 2012, while all Credit and Debit Cards were rebranded and the Infinite Credit Card was launched to a few selected customers.

In 2013, the Bank will continue its focus on delivering superior customer service, while on the product front; Al Kanz Millionaire will remain a key focus area, in addition to SBU's, Housing Finance, Credit and Debit Cards, Wealth Management and Bancassurance.

Wholesale Banking

Corporate Banking

2012 was a year of major and quantum changes for Corporate Banking as it crossed an important milestone of RO 1 billion of corporate funded facilities. While crossing the milestone, corporate banking has focused and will continue to focus on three important cornerstones viz. customer-centric approach to corporate loan growth, a strong marketing approach based on targeting the important sectors of the economy for this growth and a backbone within the department to deliver quality services to the corporate customers.

The ongoing 3 year strategy implementation continued in 2012. As part of this, the division recruited a number of young Omanis to drive the growth in business and also is investing time and resources on the Omanis to continue to maintain this momentum. A systematic approach to marketing National Bank of Oman among the large & tier 2 corporates has been put in place, to provide a full range of services.

Also, a dedicated Corporate Loan Administration Unit within the Division has been set up to act as a backbone in delivering quality and timely services to the corporate customers and as an interface between the customer-relationship managers and the Risk and Credit Administration Departments within the Bank. Systems and procedures have been devised to track the flow of work within the bank in dealing with corporate customers and Service Level Agreements have been put in place to ensure that these are adhered to and seamless and quick services are provided to corporate customers. This has proved to be a very successful and useful experiment as it has cut down large amount of procedural delays in delivering quality services and has enhanced corporate customer satisfaction levels.

New Wealth Management Services

The ongoing 3 year strategy implementation continued in 2012. As part of this, the Division recruited a number of young Omanis to drive the growth in business and also is investing time and resources on the Omanis to continue to maintain this momentum.

Another important strategy initiative was to use synergies with the alliance banks to target large customers and projects by partnering with them on specific transactions. This has been a success in servicing large customers with their credit requirements and the combined balance sheet strength of the alliance banks is being used for this purpose.

The Bank comprehends that there is enormous potential in the largely untapped Medium Enterprises segment in the country. A dedicated and strong division within Wholesale Banking has been set up to target this segment more aggressively in the coming years. The exercise to identify businesses among the existing client base fulfilling the parameters of medium enterprises has been completed and these will now be serviced by the new division to make it easier and faster for this important segment of the economy to obtain bank assistance. The benefits of this unit are expected to show more prominently in the coming year.

Growth in the corporate book has been impressive, in the face of heavy competition. Bank has been able to sustain this level of competition and grow its loan book due to our strong marketing team and the quality services that the bank has been able to offer.

The Bank successfully financed projects of national importance which required large funding, while maintaining its focus on the infrastructure, oil and gas and contracting businesses which remain the driving forces of the Omani economy.

The Bank has also closely associated itself with Duqm as the emerging industrial and port town. The Bank is seriously looking at other large projects slated to be launched in Duqm in 2013. The bank has also been working closely with large players in the Oil & Gas sector to provide a number of funded and debt advisory services to these players and looks at these advisory services as value additions to the customers and as an important source of income for the bank.

A dedicated Wholesale Banking distribution unit has been created. This unit will aggressively market NBO throughout the country for providing wholesale banking services to corporates with special emphasis on transaction banking. The Corporate Banking franchise will continue to support domestic project financing and related activity in the coming year armed with the successful implementation of various strategic initiatives to focus, target and acquire new businesses in the large as well as the medium segments and the strong backbone support service units set up within corporate banking to deliver quality services.

Investment Banking

The markets across the world recovered smartly in FY 2012 as investor confidence began to strengthen. Though the Oman stock market continued to face challenges, it managed to end the year on a positive note with a gain of 1.15%.

Oman Stock Market

The markets across the world recovered smartly in FY 2012 as investor confidence began to strengthen. Though the Oman stock market continued to face challenges, it managed to end the year on a positive note with a gain of 1.15%.

Although the local stock market continued to test the skills of the best fund managers, the Investment Banking Division turned in a strong performance and booked significant dividend income and reasonable level of capital gains on the bank's portfolio.

The Asset Management unit continued to turn in strong performances for its clients and is now on the verge of introducing new investment products in the coming year that will provide it a wider footprint in the region.

The Corporate Finance & Advisory unit has won a number of financial advisory and placement mandates. The unit has a number of deals in the pipeline which bode well for the future performance of the division. The division increased its market share and strengthened its leadership position in the Fund Custody and Administration business where it has built a strong franchise in a short span of time. The Brokerage unit continued to turn in strong performance as reflected in its improved ranking in FY 2012, which it expects to take higher in the new year.

Treasury

National Bank of Oman's Treasury Division offers foreign exchange and derivative solutions to customers and continues to be a major player in this segment. These products and services are aimed at managing customers' Foreign Exchange and Risk hedging needs through Forwards, Swaps, Options and other customized structured products. The Bank hedges its market risks related to these products with banking counterparties. Treasury Division continues to grow business through additional contracts with existing clients and creating new relationships with new corporate customers.

International Banking–Financial Institutions Group (FIG)

National Bank of Oman's Financial Institution Group maintains alliance with a large network of Local/ International Banks facilitating state of the art international trade and payment products to National Bank of Oman's Corporate and Institutional Clients. The Group also maintains Correspondent Banking Relationships with a large number of banks facilitating various business activities like:

- Confirmation of L/C's in favor of customers in Oman.
- Risk Participation Funded/Un-funded on LCs/ Trade loans / Syndicated loans
- Buyer Credit/ Post Finance funding to Banks for their importers.
- Secondary market purchase of syndicated loans
- Issuance of guarantees against counter guarantees of Correspondent Banks
- Apart from FIG's current countries under coverage the division looks to extend its business to other countries.

Risk Management

Policies and procedures were reviewed and approved and new initiatives were undertaken for further enhancing the risk management practices in the areas of Credit Risk, Market Risk, Operational Risk, Information Security and Business Continuity Risk and Recoveries. As part of the initiatives undertaken to move to advanced Basel II approaches, the division carried out an enterprise – wide assessment of all risks as part of the preparation for ICAAP (Internal Capital Adequacy Assessment Process) and carried out a trial run during 2012. Further, in line with best practices and regulatory recommendations, the Bank has established an independent Loan Review Mechanism Division with a mandate for constantly evaluating the quality of the loan book and the integrity of our credit processes.

Corporate Credit Risk

The Division was involved in developing a Corporate Credit Risk Strategy to achieve a structured approach to credit growth while de-emphasizing areas that were considered relatively high risk, based on the prevailing and expected market conditions. While continuing with prudent credit practices, the Bank supported deserving entities in the mid-sector corporate segment with adequate credit facilities for their business requirements. The continued stress in the global markets, especially in Europe and USA continues to result in downgrading of countries and banks by the rating agencies. The Bank took measures to proactively rationalize its exposures to counterparty banks and countries. Apart from monitoring credit exposures on a regular basis, the Bank was also regularly tracking portfolio credit quality, concentration risks, exposures to sensitive sectors and conducting stress tests on various aspects of our credit portfolio.

Retail Credit Risk

Credit facilities are offered to retail customers primarily based on Product Program approach which contains standard risk acceptance criteria & loan processing practice. The approach is followed to optimize the efficiency & risk /reward of the portfolio. Product Programs are reviewed by the concerned group including Risk, Compliance, Finance, Credit Administration etc. and approved by the Board Risk Committee. Credit facilities outside the Product Programs were individually assessed by the Retail Risk Division and approved as per the delegated authorities. The lending criteria were continually revised through a review of the Product program performance and market conditions.

Automated Loan Collection System

The Bank has implemented an automated Loan Collection System in order to enhance its collections and recovery processes. Loan Origination System was implemented to further enhance Credit Risk framework.

A review of the Retail Credit Portfolio was conducted at regular intervals. Salient areas covered include delinquency analysis, NPA trends and recoveries. Several system enhancements and new processes have been introduced across critical activities to improve processing quality and efficiency and to enhance the recovery methodologies of delinquent accounts in the retail portfolio.

The Bank has implemented an automated Loan Collection System in order to enhance its collections and recovery processes. Loan Origination System was implemented to further enhance Credit Risk framework.

Liquidity Risk Management

Liquidity conditions in the global markets showed some distinct signs of easing up as the year progressed, which was reflected in improved liquidity as compared to the preceding year. However, the crisis over European Sovereign Debts remains a concern and the market liquidity is yet to reach its normal levels. At the same time, the year saw a continuing surplus of short tenor Omani Rials in the banking system leading to close-to-nil yields on Central Bank of Oman CDs.

Our Liquidity Contingency Plan underwent detailed review and was further strengthened by incorporating measures for such contingencies as intraday funding crisis and operational disruptions.

The regular projections of maturity gaps for both Omani Rials and US Dollars enabled the Bank's ALCO (Asset Liability Committee) to formulate action plans in a timely manner, thus enabling it to effectively manage its liquidity position through a combination of available measures.

Liquidity Risk position continues to be monitored regularly through the analysis of various reports, such as Maturity of Assets and Liabilities, Liquidity Lines, Early Warning Indicators, Stock Ratios, Simulation of Gaps in Omani Rials and US Dollars, Stress Tests and the Daily Financial Risk (DFR)report.

Market Risk Management

The middle-office within the Market Risk division along with Treasury and Investment Banking Operations continued daily monitoring of Market Risk positions in foreign exchange and investments for the Bank.

The bank transacted some derivative option structures for customers desiring to hedge their exposures which were covered back to back in the interbank market. The counterparty credit risk on account of these transactions was monitored as per the approved policy of the bank.

The Interest Rate Risk in the Banking Book was analyzed at regular frequencies, and presented to ALCO based on the impact on the Economic Value, as well as the Earnings at Risk on account of parallel shifts in the interest rates. The analysis was done based on Basel Committee and CBO guidelines. Monthly stress tests were conducted to study the adverse movements in the currency rates, as well as impairment in investment exposures.

The Bank is at an advanced stage of selecting a vendor for a new integrated Treasury Front Office, Mid-Office and Back Office system to enhance the capturing and monitoring of Market Risks on a real time basis in line with best practices and regulatory requirements.

Remedial Management

Remedial Management is responsible for relentlessly pursuing each delinquent account, by using all available measures to reduce exposure to high risk groups, to maximize recoveries, rehabilitating these relationships so that they can be returned to the business lines as fully performing accounts and progressively improve the status of the portfolio. This is reflected in the decline in the non-performing loan ratio.

The divisions efforts also helped the Bank to reduce the net impairment losses from RO 10 million in 2011 to RO 5.2 million in 2012.

Compliance

The Bank has been proactive in managing its compliance risk. The Board and management endeavor to ensure the Bank's operations and business conduct are consistent with the laws and regulations of the Sultanate and other markets it operates. These include, but are not limited to, Laws and Regulations issued by the Central Bank of Oman and Capital Market Authority, as well as internationally accepted best practices. The Bank fosters a culture of compliance which is seen not only as a requirement of law but also as a good business practice. As such the NBO customers are assured of their rights and privileges.

The compliance division is involved in reviewing the Bank's policies and procedures, services and products, to ensure compliance with various laws and regulations and internationally accepted best practices.

The Bank remains committed to combating money laundering and terrorism financing by improving control measures as the regulatory environment becomes more demanding. To this end, the Bank has in place comprehensive policies and procedures, and a state of the art Anti Money Laundering system which has enhanced the Bank's ability to effectively monitor and detect suspicious transactions.

The Bank also ensures that its staff knowledge and skills commensurate with its commitment to combat money laundering and terrorism financing. As such, the bank has, in addition to the in-house and on-the-job training, in place an AML E-Learning program that is mandatory for all employees of the bank.

Operations

2012 has been a successful year for the Operations Division for implementing a positive change in operational services. The division played a key role in supporting the lines of business in their asset expansion endeavor.

During the course of the year, the process centralization were effected in the areas of Credit Administration, Trade Service Operations and improvised straight through processing in Remittance operations. The mortgage operations were streamlined to deliver a record growth during the year. The front line operations were reviewed and modified to improve the Turnaround Time in service delivery.

The Bank entered in to the online exchange of signatures through secured internet servers between correspondent banks. Treasury and Investment banking operations provided support to quality delivery of Treasury Products, Investment fund custody and administration support towards new mandates during the year.

Information Technology

The Bank views IT to be a key enabler to its business strategy. The Information Technology Division (ITD) has drawn out a comprehensive 3-year IT strategy fully aligned with the business strategy and is in the midst of executing number of initiatives covering implementation of innovative and functionally rich banking systems, modernizing its technology infrastructure, enhancing its processes for effectiveness and developing and nurturing its talent pool. ITD works very closely with its business counterparts to ensure it caters to both strategic and operational goals of the business. Some of the 2012 initiatives include:

- Implementation of a full-fledged Islamic Banking ecosystem
- Significantly enhancing the turn-around-time and transparency through the implementation of loan processing system
- Implementing a Wealth Management platform for Sadara affluent segment
- Launch of new innovative retail products (Al Amaal Child, Mustaqbali, etc.)
- Enabling process efficiency for our corporate customers through Straight through processing of number of B2B transactions
- Functional enhancements on corporate and retail internet banking platforms
- Infrastructure upgrades through virtualization and storage consolidation

Human Resources

The year 2012 has been a significant year with several key initiatives undertaken by the Human Resources Group which continues to remain closely aligned with corporate objectives and business functions.

In 2012, the Human Resource strategic transformation process was implemented. The strategic initiatives include:

- Creation of performance based culture through overhauling the current performance management philosophy.
- To align NBO HR to best practices, HR policy was revised and implemented along with a revised grade and salary structure for the bank.
- Creation of a learning organization via establishment of Academy of Excellence in terms of new campus and new/overhauled programs to ensure best in the breed learning environment
- Overhauling job descriptions and creation of competency frame work in order to ensure clarity of jobs and their benchmarking against market. Also, to ensure that people development is based on scientific & proven methodology of skills gap analysis.
- E-HR: Automation of HR services (benefits) in order to ensure in time & quality services to all our staff

Finance

The Division ensures that the financial statements are prepared in compliance with the International Financial Reporting Standards.

Key initiatives in 2012 include effective insurance claim management and settlements. The division continues to play a key role in providing MIS reports and analysis to the executive management, business managers and line managers through a variety of operational, tactical and strategic reports. It also ensures that structured and adequate information is available at all times so that informed business decisions are possible.

During 2012, the division had an active role in raising funds through Syndicated facility and Subordinated debt that enhances the Tier II capital.

Corporate Social Responsibility (CSR) & Corporate Communications

CSR in its essence is how the Bank manages the business processes to produce an overall positive impact on society. The four key segments focused on by the Bank for CSR are Health & Human Services, Civic, Education, Youth and the Environment.

In 2012, the Bank's community investment was RO 200,000. The CSR initiatives of the Bank in 2012 included training programmes for young Omani high school graduates, renovation of existing homes for truly needy families in co-ordination with the Ministry of Social Development and many others. In addition, the Bank's employees also participated in the CSR initiatives of the Bank, through the NBO Employee Volunteers programme.

Internal Audit Function

The Internal Audit Division is an independent function reporting to the Board of Directors through the Board Audit Committee with dotted reporting line to the CEO for administrative purpose.

The Division uses Risk Based Audit Approach to examine and evaluate the effectiveness and adequacy of the systems of management control provided by the Bank to direct its activities towards the accomplishment of its objectives in accordance with the Bank's policies and plans within the regulatory framework.

The internal audit methodology has been re-engineered to align with the COSO Framework. (Committee of

Sponsoring Organizations of the Treadway Commission). Accordingly the evaluation of the internal control system is designed to ensure (1) the effectiveness and efficiency of operations, (2) the reliability of financial reporting and (3) the compliance of applicable laws and regulations." These objectives are assessed under five elements viz: control environment, risk assessment, information and communication, control activities, and monitoring.

The audit plan covers the review of all head-office divisions, local and overseas branches of the Bank as well as the conduct of fraud investigations.

The Division has implemented an internal audit governance portal that enabled the automation of the audit process from risk assessment through reporting; ties risks to key processes and organizations that feed the audit planning process and easily integrate internal auditing into the Governance, Risk Management and Compliance program.

Quality Assurance Reviews on Internal Audit

The division has developed and maintains a quality assurance and improvement program (internal and external) that covers all aspects of the internal audit activity.

Internal Control Systems and their adequacy

The management is aware of its responsibilities to the various stakeholders of the Bank. As part of fulfilling its responsibilities and ensuring that all areas of the Bank's operations are managed effectively and efficiently, progressive enhancements to the internal control systems of the Bank were introduced during the year which included new policies and procedures, quality control reviews, and related enhanced controls.

The management continues to take steps to enhance the internal control systems to support the achievement of the corporate objectives and to ensure that stakeholders' interests are protected. Importantly, the management takes cognizance of the role played by the Internal Audit division and the Compliance division and their recommendations.

Outlook

The outlook for Oman's economy in 2013 is positive with the increase in government spending. The focus on infrastructure projects is expected to boost economic growth. The launch of Islamic banking operations also opens up new opportunities for banks in the coming years.

In this economic environment, the Bank continues its focus on sustainable growth and is poised to take advantage of the growth opportunities so created through the above Government initiatives.

Oman will remain the primary focus in the coming year, with the Bank capitalizing on the UAE franchise as an additional service point for its Omani customers. Strong risk management will remain a key to mitigation of potential risks as the Bank embarks on its strategic journey of diversified revenue growth and cost management

To summarize, we look forward to year 2013 with optimism, as continued Government expenditure expects to maintain growth momentum, creating adequate opportunities for the banking sector.

Salaam Al Shaksy
Chief Executive Officer

Muzn-National Bank of Oman's Islamic Banking Window

Muzn Islamic Banking

Muzn Islamic Banking is the licensed Islamic Banking window of National Bank of Oman operating in the Sultanate of Oman. National Bank of Oman has the unique distinction of being the first local conventional bank to be established in 1973.

Our aim is to create ethical value for our customers through our Shari'a compliant Islamic products and services.

Our Mission is to provide innovative, competitive and quality Islamic Banking products and services; ensuring these are accessible and understood by all.

Our Vision is to be the leading provider of Islamic financial services in the country.

Muzn's independent Shari'a Supervisory Board is an external Shari'a Committee comprising of independent and well renowned Shari'a Scholars who guide and ensure that the operations, services and products offered by Muzn Islamic Banking comply with the principles of Shari'a. Our Shari'a Supervisory Board consists of three prominent Shari'a Scholars namely:

- **Sheikh Dr. Mohamed bin Ali Elgari**, is a Professor of Islamic Economics at King Abdulaziz University, Saudi Arabia. He is an Expert at the Islamic Jurisprudence Academy of the Organisation of Islamic Cooperation (OIC) and the Islamic Jurisprudence Academy of the Islamic World League and a member of the Shari'a Council of Accounting and Auditing Organisation for Islamic Financial Institutions (AAOFI), Chairman Shari'a Supervisory Board of Muzn Islamic Banking Services and Board Member of several reputable Islamic Banks and Takaful Companies.
- **Sheikh Dr. Mohammed Daud Bakar**, is a Malaysian Shari'a Scholar, his area of specialization includes Islamic Legal Theory, Islamic Banking and Finance and Islamic Law of Zakah. Dr. Bakar has published more than 30 articles in academic journals. Sheikh Baker is also Chairman of the Central Shari'a Advisory Council of the Central Bank of Malaysia, Securities Commission of Malaysia and member of several Shari'a Boards for banks and Islamic financial institutions worldwide.
- **Sheikh Khalfan bin Mohammed Al-Esry**, is a leading Omani Shari'a Scholar and recognized public figure in Oman. He is a coach and facilitator on Personal Leadership with extensive knowledge and experience in multicultural management and organizational behavior. Sheikh Al-Esry has sound experience in Shari'a and regularly contributes towards education of Shari'a Principles to the communities in Oman.

Remuneration for Shari'a Supervisory Board Members 2012:

Total Remuneration paid to the three Scholars for the year 2012 was OMR 20,596.970

The breakup is as follows:

Name of the Board Member	Total fees (OMR)	Remarks
Sheikh Dr. Mohamed bin Ali Elgari	7,699.800	Appointed on 10th June 2012
Sheikh Khalfan bin Mohammed Al-Esry	6,641.080	Appointed on 10th June 2012
Dr. Mohammed Daud Bakar	6,256.090	Appointed on 10th June 2012
Total (OMR)	**20,596.970**	

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INDEPENDENT AUDITOR'S REPORT TO THE SHAREHOLDERS OF NATIONAL BANK OF OMAN SAOG

Report on the Financial Statements

We have audited the financial statements of National Bank of Oman SAOG ('the bank'), set out on pages 56 to 106 which comprise the statement of financial position as at 31 December 2012, and the statement of comprehensive income, statement of changes in equity and statement of cash flows for the year then ended, and a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate for the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

Opinion

In our opinion, the financial statements present fairly, in all material respects, the financial position of the bank as at 31 December 2012 and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

Other matters

The financial statements for the year ended 31 December 2011 were audited by another auditor who expressed an unmodified opinion on those financial statements dated 23 January 2012.

Report on Other Legal and Regulatory Requirements

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

24 January 2013

Paul Callaghan

2011 USD'000	2012 USD'000		Notes	2012 RO'000	2011 RO'000
		ASSETS			
573,431	**560,358**	Cash and balances with Central Banks	4	**215,738**	220,771
416,997	**564,314**	Due from banks and other money market placements (net)	5	**217,261**	160,544
4,339,683	**4,965,096**	Loans and advances to customers (net)	6	**1,911,562**	1,670,778
246,810	**287,590**	Non-trading financial investments	7	**110,722**	95,022
53,260	**53,242**	Premises and equipment	8	**20,498**	20,505
1,252	**1,062**	Deferred tax asset	13	**409**	482
158,365	**160,073**	Other assets	9	**61,628**	60,970
5,789,798	**6,591,735**	**TOTAL ASSETS**		**2,537,818**	2,229,072
		LIABILITIES, SUBORDINATED DEBT AND EQUITY			
		LIABILITIES			
579,608	**546,616**	Due to banks and other money market deposits	10	**210,447**	223,149
4,155,387	**4,900,660**	Customers' deposits	11	**1,886,754**	1,599,824
168,655	**178,644**	Other liabilities	12	**68,778**	64,932
13,610	**14,771**	Taxation	13	**5,687**	5,240
4,917,260	**5,640,691**	**TOTAL LIABILITIES**		**2,171,666**	1,893,145
		SUBORDINATED DEBT			
142,078	**160,260**	**Subordinated debt**	14	**61,700**	54,700
		EQUITY			
280,779	**287,799**	Share capital	15	**110,803**	108,100
89,519	**89,519**	Share premium	16	**34,465**	34,465
100,369	**102,821**	Legal reserve	17	**39,586**	38,642
11,478	**11,478**	General reserve	18	**4,419**	4,419
47,527	**79,790**	Other non-distributable reserves	19	**30,719**	18,298
49,138	**50,366**	Proposed cash dividend	20	**19,391**	18,918
7,021	**-**	Proposed stock dividend	20	**-**	2,703
144,629	**169,011**	Retained earnings		**65,069**	55,682
730,460	**790,784**	**TOTAL EQUITY**		**304,452**	281,227
5,789,798	**6,591,735**	**TOTAL LIABILITIES, SUBORDINATED DEBT AND EQUITY**		**2,537,818**	2,229,072

The financial statements were authorised for issue on 24th January 2013 in accordance with a resolution of the Board of Directors.

Chairman

Chief Executive Officer

The attached notes 1 to 34 form part of these financial statements.

Statement of Comprehensive Income

For the year ended 31st December 2012

2011 USD'000	2012 USD'000		Notes	2012 RO'000	2011 RO'000
242,483	**278,184**	Interest income	22	**107,101**	93,356
(91,348)	**(103,693)**	Interest expense	23	**(39,922)**	(35,169)
151,135	**174,491**	Net interest income		**67,179**	58,187
88,436	**81,729**	Other operating income	24	**31,466**	34,048
239,571	**256,220**	**OPERATING INCOME**		**98,645**	92,235
		OPERATING EXPENSES			
(64,624)	**(68,917)**	Staff costs		**(26,533)**	(24,880)
(37,322)	**(42,665)**	Other operating expenses	25	**(16,426)**	(14,369)
(10,927)	**(9,678)**	Depreciation	8	**(3,726)**	(4,207)
(112,873)	**(121,260)**			**(46,685)**	(43,456)
126,698	**134,960**	**PROFIT FROM OPERATIONS BEFORE IMPAIRMENT LOSSES AND TAX**		**51,960**	48,779
(49,174)	**(44,002)**	Credit loss expense – customers' loan	6	**(16,941)**	(18,932)
19,546	**9,039**	Recoveries and releases from provision for credit losses	6	**3,480**	7,525
11,236	**25,252**	Recoveries from loans and advances written off		**9,722**	4,326
(5,943)	**(4,003)**	Impairment losses on available for sale investments	7	**(1,541)**	(2,288)
(1,849)	**-**	Provision – others		**-**	(712)
(26,184)	**(13,714)**	TOTAL IMPAIRMENT LOSSES (NET)		**(5,280)**	(10,081)
100,514	**121,246**	PROFIT BEFORE TAX		**46,680**	38,698
(11,678)	**(15,630)**	Taxation	13	**(6,018)**	(4,496)
88,836	**105,616**	**PROFIT FOR THE YEAR**		**40,662**	34,202
		OTHER COMPREHENSIVE INCOME			
(6,750)	**3,868**	Net movement on available for sale investments		**1,489**	(2,599)
75	**(21)**	Tax effect of net movement on available for sale investments		**(8)**	29
(6,675)	**3,847**	**OTHER COMPREHENSIVE INCOME / (EXPENSE) FOR THE YEAR**		**1,481**	(2,570)
82,161	**109,463**	**TOTAL COMPREHENSIVE INCOME FOR THE YEAR**		**42,143**	31,632
0.08	**0.10**	Earnings per share: Basic and diluted	27	**0.037**	0.031

The attached notes 1 to 34 form part of these financial statements.

(RO'000)	Share capital	Share premium	Legal reserve	General reserve	Other non-distri-butable reserves	Proposed cash dividend	Proposed stock dividend	Retained earnings	Total
Balance at 1 January 2011	108,100	34,465	35,392	4,419	14,748	16,215	-	52,471	265,810
Total comprehensive income for the year									
Profit for the year	-	-	-	-	-	-	-	34,202	34,202
Net movement on available for sale investments	-	-	-	-	(2,570)	-	-	-	(2,570)
Transactions with owners recorded directly in equity									
Dividend paid	-	-	-	-	-	(16,215)	-	-	(16,215)
Proposed cash dividend	-	-	-	-	-	18,918	-	(18,918)	-
Proposed stock dividend	-	-	-	-	-	-	2,703	(2,703)	-
Transfer to subordinated debt reserve	-	-	-	-	6,120	-	-	(6,120)	-
Transfer to legal reserve	-	-	3,250	-	-	-	-	(3,250)	-
Balance at 31 December 2011	108,100	34,465	38,642	4,419	18,298	18,918	2,703	55,682	281,227
Balance at 1 January 2012	**108,100**	**34,465**	**38,642**	**4,419**	**18,298**	**18,918**	**2,703**	**55,682**	**281,227**
Total comprehensive income for the year									
Profit for the year	-	-	-	-	-	-	-	**40,662**	**40,662**
Net movement on available for sale investments	-	-	-	-	**1,481**	-	-	-	**1,481**
Transactions with owners recorded directly in equity									
Issue of shares	**2,703**	-	-	-	-	-	**(2,703)**	-	-
Dividend paid	-	-	-	-	-	**(18,918)**	-	-	**(18,918)**
Proposed cash dividend	-	-	-	-	-	**19,391**	-	**(19,391)**	-
Proposed stock dividend	-	-	-	-	-	-	-	-	-
Transfer to subordinated debt reserve	-	-	-	-	**10,940**	-	-	**(10,940)**	-
Transfer to legal reserve	-	-	**944**	-	-	-	-	**(944)**	-
Balance at 31 December 2012	**110,803**	**34,465**	**39,586**	**4,419**	**30,719**	**19,391**	-	**65,069**	**304,452**
Balance at 1 January 2012 – In USD'000	280,779	89,519	100,369	11,478	47,527	49,138	7,021	144,629	730,460
Balance at 31 December 2012 – In USD'000	**287,799**	**89,519**	**102,821**	**11,478**	**79,790**	**50,366**	-	**169,011**	**790,784**

The attached notes 1 to 34 form part of these financial statements.

Statement of Cash Flows
For the year ended 31st December 2012

2011 USD'000	2012 USD'000		Notes	2012 RO'000	2011 RO'000
		OPERATING ACTIVITIES			
100,514	**121,246**	Profit before taxation		**46,680**	38,698
		Adjustments for:			
10,927	**9,678**	Depreciation	8	**3,726**	4,207
(15,836)	**30,961**	Provision for credit losses (net)		**11,920**	(6,097)
5,943	**4,003**	Impairment losses on available for sale investments	7	**1,541**	2,288
1,177	**-**	Provision against collateral assets		**-**	453
(694)	**(790)**	Profit on sale of equipment (net)		**(304)**	(267)
(2,130)	**(990)**	Profit on sale of investments	24	**(381)**	(820)
(7,488)	**(8,402)**	Investment income		**(3,235)**	(2,883)
92,413	**155,706**	**Operating profit before changes in operating assets and liabilities**		**59,947**	35,579
855	**(88,184)**	Due from banks and other money market placements		**(33,951)**	329
18,000	**(68,000)**	Due to banks and other money market deposits		**(26,180)**	6,930
(782,647)	**(656,374)**	Loans and advances to customers		**(252,704)**	(301,319)
(44,314)	**(1,709)**	Other assets		**(658)**	(17,061)
714,114	**745,273**	Customers' deposits		**286,930**	274,934
46,358	**9,990**	Other liabilities		**3,846**	17,848
44,779	**96,702**	**Cash from operations**		**37,230**	17,240
(9,990)	**(14,247)**	Taxes paid		**(5,485)**	(3,846)
34,789	**82,455**	**Net cash from operating activities**		**31,745**	13,394
		INVESTING ACTIVITIES			
(115,877)	**(55,514)**	Purchase of non-trading investments		**(21,373)**	(44,613)
22,244	**15,158**	Proceeds from sale of non-trading investments		**5,836**	8,564
(6,629)	**(10,171)**	Purchase of premises and equipment	8	**(3,916)**	(2,552)
1,151	**1,265**	Disposal of premises and equipment		**487**	443
3,990	**5,992**	Income from bond and other investments	24	**2,307**	1,536
3,498	**2,410**	Dividend income	24	**928**	1,347
185	**416**	Translation differences on premises and equipment and tax		**160**	71
(91,438)	**(40,444)**	**Net cash used in investing activities**		**(15,571)**	(35,204)
		FINANCING ACTIVITIES			
(42,117)	**(49,138)**	Payment of dividend		**(18,918)**	(16,215)
62,597	**18,182**	Net movement in subordinated debt	14	**7,000**	24,100
20,480	**(30,956)**	**Net cash (used in) / from financing activities**		**(11,918)**	7,885
(36,169)	**11,055**	INCREASE / (DECREASE) IN CASH AND CASH EQUIVALENTS		**4,256**	(13,925)
750,251	**714,083**	Cash and cash equivalents at the beginning of the year		**274,922**	288,847
714,082	**725,138**	**CASH AND CASH EQUIVALENTS AT THE END OF THE YEAR**		**279,178**	274,922
		REPRESENTING:			
572,132	**559,060**	Cash and balances with Central Banks	4	**215,238**	220,271
141,950	**166,078**	Deposits and balances with other banks and financial institutions (net)		**63,940**	54,651
714,082	**725,138**			**279,178**	274,922

The attached notes 1 to 34 form part of these financial statements.

1 LEGAL STATUS AND PRINCIPAL ACTIVITIES

National Bank of Oman SAOG ("NBO", "the bank") was established in the Sultanate of Oman in 1973 as a joint stock company and is engaged in retail banking, wholesale banking, and investment banking services within the Sultanate of Oman with overseas branches in the United Arab Emirates and Egypt. The bank operates in Oman under a banking licence issued by the Central Bank of Oman and is covered by its deposit insurance scheme. The registered address of the bank is PO Box 751, Ruwi, Postal Code 112, Muscat, Sultanate of Oman. The bank has a primary listing on Muscat Stock Exchange.

The bank employed 1,352 employees as at 31 December 2012 (2011: 1,339).

2 BASIS OF PREPARATION

Basis of measurement

The financial statements are prepared under the historical cost convention as modified to include the revaluation of freehold land and buildings and the measurement at fair value of derivatives, investments classified as available for sale and investment carried at fair value through profit and loss.

Functional and presentation currencies

These financial statements are presented in Rial Omani rounded to the nearest thousand Rial Omani, except when otherwise indicated. The functional currencies of the bank's operations are as follows:

- Sultanate of Oman : Rial Omani
- United Arab Emirates : UAE Dirham
- Egypt : US Dollar

The United States Dollar amounts shown in the financial statements have been translated from Rial Omani at an exchange rate of RO 0.385 to each US Dollar, and are shown for the convenience of the reader only.

Statement of compliance

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

The bank presents its statement of financial position broadly in order of liquidity.

Significant accounting judgments and estimates

In the process of applying the bank's accounting policies, management has used its judgments and made estimates in determining the amounts recognised in the financial statements. The most significant use of judgments and estimates are as follows:

Going concern

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

Impairment losses on loans and advances

The bank reviews its individually significant loans and advances at each reporting date to assess whether an impairment loss should be recorded in the statement of comprehensive income. In particular, judgment by management is required in the estimation of the amount and timing of future cash flows when determining the impairment loss. In estimating these cash flows, the bank makes judgments about the borrower's financial situation and the net realisable value of collateral. These estimates are based on assumptions about a number of factors and actual results may differ, resulting in future changes to the allowance.

Loans and advances that have been assessed individually and found not to be impaired and all individually insignificant loans and advances are then assessed collectively, in groups of assets with similar risk characteristics, to determine whether provision should be made due to incurred loss events for which there is objective evidence but whose effects are not yet evident. The collective assessment takes account of data from the loan portfolio (such as credit quality, levels of arrears, credit utilisation, loan to collateral ratios etc.) and concentrations of risks.

Impairment of equity investments

The bank treats available-for-sale equity investments as impaired when there has been a significant or prolonged decline in the fair value below its cost or where other objective evidence of impairment exists. The determination of what is 'significant' or 'prolonged' requires judgment.

Fair value of financial instruments

Where the fair values of financial assets and financial liabilities recorded on the statement of financial position cannot be derived from active markets, they are determined using a variety of valuation techniques that include the use of mathematical models. The inputs to these models are derived from observable market data where possible, but where observable market data are not available, judgment is required to establish fair values.

2 BASIS OF PREPARATION (continued)

Deferred tax assets

Deferred tax assets are recognized for all unused tax losses to the extent that it is probable that taxable

profit will be available against which the losses can be utilized. Significant management judgment is required to determine the amount of deferred tax assets that can be recognized, based upon the likely timing and level of future taxable profits together with future tax planning strategies.

Standards, Amendments and interpretations that are not yet effective and have not been early adopted by the Bank

- IFRS 10 – Consolidated Financial Statements (effective on or after 1 January 2013)
- IFRS 11 – Joint Arrangements - (effective on or after 1 January 2013)
- IFRS 12 – Disclosure of Interests in Other Entities (effective on or after 1 January 2013)
- IFRS 13 – Fair Value Measurement –(effective on or after 1 January 2013)
- IAS 19 – Employee Benefits (2011) - (effective on or after 1 January 2013)

3 SIGNIFICANT ACCOUNTING POLICIES

Date of recognition

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

Initial measurement of financial instruments

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

Cash and cash equivalents

Cash and cash equivalents consist of cash on hand, balances with banks and other financial institutions, treasury bills and money market placements, deposits and certificates of deposit maturing within three months of the date of acquisition. Cash and cash equivalents are carried at amortised cost in the statement of financial position.

Financial assets and financial liabilities designated at fair value through profit or loss

Financial assets and financial liabilities classified in this category are designated by management on initial recognition when the following criteria are met:

- the designation eliminates or significantly reduces the inconsistent treatment that would otherwise arise from measuring the assets or liabilities or recognizing gains or losses on them on a different basis; or
- the assets and liabilities are part of a group of financial assets, financial liabilities or both which are managed and their performance evaluated on a fair value basis, in accordance with a documented risk management or investment strategy; or
- The financial instrument contains an embedded derivative, unless the embedded derivative does not significantly modify the cash flows or it is clear, with little or no analysis, that it would not be separately recorded.

Financial assets and financial liabilities at fair value through profit or loss are recorded in the statement of financial position at fair value. Changes in fair value are recorded in ‘other operating income’. Interest earned or incurred is accrued in ‘Interest income’ or ‘Interest expense’, respectively, using the effective interest rate (EIR), while dividend income is recorded in ‘Other operating income’ when the right to the payment has been established.

Held to maturity

Held-to-maturity financial investments are those which carry fixed or determinable payments and have fixed maturities and which the bank has the intention and ability to hold to maturity. After initial measurement, held-to-maturity financial investments are subsequently measured at amortised cost using the effective interest rate method, less allowance for impairment. Amortised cost is calculated by taking into account any discount or premium on acquisition and fees that are an integral part of the effective interest rate. The amortisation is included in ‘Interest income’ in the statement of comprehensive income. The losses arising from impairment of such investments are recognised in the statement of comprehensive income.

If the bank were to sell or reclassify more than an insignificant amount of held-to-maturity investments before maturity (other than in certain specific circumstances), the entire category would be tainted and would have to be reclassified as available-for-sale. Furthermore, the bank would be prohibited from classifying any financial asset as held to maturity during the following two years.

3 SIGNIFICANT ACCOUNTING POLICIES (continued)

Available for sale

Available-for-sale investments include equity and debt securities. Equity investments classified as available-for - sale are those which are neither

classified as held-for-trading nor designated at fair value through profit or loss. Debt securities in this category are those which are intended to be held for an indefinite period of time and which may be sold in response to needs for liquidity or in response to changes in the market conditions.

The bank has not designated any loans or receivables as available-for-sale.

After initial measurement, available-for-sale financial investments are subsequently measured at fair value, unless fair value cannot be reliably determined in which case they are measured at cost less impairment. Fair value changes are reported as a separate component of equity until the investment is derecognised or the investment is determined to be impaired. On derecognition or impairment, the cumulative gain or loss previously reported as "cumulative changes in fair value" within equity, is included in the profit or loss for the year. Interest earned whilst holding available-for-sale financial investments is reported as interest income using the EIR. Dividends earned whilst holding available-for-sale financial investments are recognised in the statement of comprehensive income as 'Other operating income' when the right of the payment has been established. The losses arising from impairment of such investments are recognised in the profit or loss for the year in 'Impairment losses on financial investments' and removed from the 'Available-for-sale reserve'.

Due from banks and loans and advances to customers

Due from banks and loans and advances to customers are financial assets with fixed or determinable payments and fixed maturities that are not quoted in an active market. They are not entered into with the intention of immediate or short-term resale. After initial measurement, amounts due from banks and loans and advances to customers are subsequently measured at amortised cost using the effective interest rate method, less allowance for impairment. Amortised cost is calculated by taking into account any discount or premium on acquisition and fees and costs that are an integral part of the effective interest rate. The amortisation is included in 'Interest income' in the profit or loss for the year. The losses arising from impairment are recognised in the profit or loss for the year in 'Credit loss expense'.

Determination of fair values

The fair value for financial instruments traded in active markets at the reporting date is based on their quoted market price or dealer price quotations, without any deduction for transaction costs.

For all other financial instruments not traded in an active market, the fair value is determined by using appropriate valuation techniques. Valuation techniques include the discounted cash flow method, comparison to similar instruments for which market observable prices exist, options pricing models, credit models and other relevant valuation models.

Certain financial instruments are recorded at fair value using valuation techniques in which current market transactions or observable market data are not available. Their fair value is determined using a valuation model.

Premises and equipment

Premises and equipment are initially recorded at cost or deemed cost. Revaluations of buildings are carried out every five years on an open market value for existing use basis by an independent valuer. Net surpluses arising on revaluation are credited to a capital reserve, except that a revaluation increase is recognised as income to the extent that it reverses a revaluation decrease of the same asset previously recognised as an expense.

A decrease as a result of a revaluation is recognised as an expense, except that it is charged directly against any related revaluation surplus to the extent that the decrease does not exceed the amount held in the revaluation surplus in respect of that same asset. On disposal the related revaluation surplus is credited to retained earnings.

Depreciation is provided on a straight-line basis over the estimated useful lives of all premises and equipment other than freehold land, which is deemed to have an indefinite life, and capital work in progress. The rates of depreciation are based upon the following estimated useful lives:

Buildings on freehold land	25 years
Buildings on leasehold land	10 years
Leasehold improvements	3 to 5 years
Motor vehicles	4 years
Furniture	10 years
Equipment	5 years

The assets' residual values, useful lives and depreciation methods are reviewed and adjusted if appropriate at each statement of financial position date.

3 SIGNIFICANT ACCOUNTING POLICIES (continued)

Derecognition of financial assets and financial liabilities

Financial assets:

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

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

When the bank has transferred its rights to receive cash flows from an asset or has entered into a pass-through arrangement, and has neither transferred nor retained substantially all the risks and rewards of the asset nor transferred control of the asset, the asset is recognised to the extent of the bank's continuing involvement in the asset. In that case, the bank also recognises an associated liability. The transferred asset and the associated liability are measured on a basis that reflects the rights and obligations that the bank has retained. Continuing involvement that takes the form of a guarantee over the transferred asset is measured at the lower of the original carrying amount of the asset and the maximum amount of consideration that the bank could be required to repay.

Financial liabilities:

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

Collateral pending sale

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

Deposits

All money market and customer deposits are carried at amortised cost using EIR.

Other borrowed funds

Other borrowings including subordinate private placements are recognised initially at their issue proceeds. Borrowings are subsequently stated at amortised cost; any difference between proceeds, net of transaction costs, and the redemption value is recognised in the profit or loss over the period of the borrowings using EIR.

Taxation – current and deferred

Taxation is provided for based on the relevant tax laws of the respective countries, in which the bank operates.

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

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

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

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

Derivatives and hedge accounting

The bank makes use of derivative instruments to manage exposures to interest rate, foreign currency and credit risks, including exposures arising from forecast transactions. In order to manage particular risks, the bank applies hedge accounting for transactions which meet the specified criteria.

3 SIGNIFICANT ACCOUNTING POLICIES (continued)

Derivatives and hedge accounting (continued)

At inception of the hedge relationship, the bank formally documents the relationship between the hedged item and the hedging instrument, including the nature of the risk, the objective and strategy for undertaking the hedge and the method that will be used to assess the effectiveness of the hedging relationship.

Also at the inception of the hedge relationship, a formal assessment is undertaken to ensure the hedging instrument is expected to be highly effective in offsetting the designated risk in the hedged item. A hedge is regarded as highly effective if the changes in fair value or cash flows attributable to the hedged risk during the period for which the hedge is designated are expected to offset in a range of 80% to 125%. For situations where that hedged item is a forecast transaction, the bank assesses whether the transaction is highly probable and presents an exposure to variations in cash flows that could ultimately affect the profit or loss for the year.

Derivative financial instruments including credit default swaps, which are not designated and qualified as hedges are recorded at fair value and unrealised gains or losses are included in the profit or loss for the year.

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.

Financial guarantees

In the ordinary course of business, the bank gives financial guarantees. Financial guarantees are initially recognised in the financial statements at fair value, in "other liabilities". Subsequent to initial recognition, the bank measures such guarantees at the higher of the initial fair value less, when appropriate, cumulative amortisation calculated to recognise the fee in the profit or loss for the year in "Net fees and commission income" over the term of the guarantee, and the best estimate of the expenditure required to settle any financial obligation arising as a result of the guarantee.

Any increase in the liability relating to financial guarantees is taken to the profit or loss for the year. Any financial guarantee liability remaining is recognised in the statement of comprehensive income when the guarantee is discharged, cancelled or expires.

Provisions

Provisions are recognised when the bank has a present obligation (legal or constructive) arising from a past event and the costs to settle the obligation are both probable and able to be reliably measured.

Impairment of financial assets

The bank assesses at each reporting date whether there is any objective evidence that a financial asset or a group of financial assets is impaired. A financial asset or a group of financial assets is deemed to be impaired if, and only if, there is objective evidence of impairment as a result of one or more events that has occurred after the initial recognition of the asset (an incurred 'loss event') and that loss event (or events) has an impact on the estimated future cash flows of the financial asset or the group of financial assets that can be reliably estimated. Evidence of impairment may include indications that the borrower or a group of borrowers is experiencing significant financial difficulty, default or delinquency in interest or principal payments, the probability that they will enter bankruptcy or other financial reorganisation and where observable data indicate that there is a measurable decrease in the estimated future cash flows, such as changes in arrears or economic conditions that correlate with defaults. If such evidence exists, the impairment loss is recognized in the profit or loss for the year.

Due from banks and loans and advances to customers

For amounts due from banks and loans and advances to customers carried at amortised cost, the bank first assesses individually whether objective evidence of impairment exists individually for financial assets that are individually significant, 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 has been incurred, the amount of the loss is measured as the difference between the assets' carrying amount and the present value of estimated future cash flows (excluding future expected credit losses that have not yet been incurred). 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 profit or loss for the year. Interest income continues to be accrued on the reduced

3 SIGNIFICANT ACCOUNTING POLICIES (continued)

Due from banks and loans and advances to customers (continued)

carrying amount based on the original effective interest rate of the asset. Loans together with the associated allowance are written off when there is no realistic prospect of future recovery and all collateral has been realised or has been transferred to the bank. If, in a subsequent year, the amount of the estimated impairment loss increases or decreases because of an event occurring after the impairment was recognised, the previously recognised impairment loss is increased or reduced by adjusting the allowance account. If a future write-off is later recovered, the recovery is credited to the 'Recoveries from loans and advances written off'.

The present value of the estimated future cash flows is discounted at the financial asset's original effective interest rate. If a loan has a variable interest rate, the discount rate for measuring any impairment loss is the current effective interest rate. 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.

For the purpose of a collective evaluation of impairment, financial assets are grouped on the basis of the bank's internal credit grading system that considers credit risk characteristics such as asset type, industry, geographical location, collateral type, past-due status and other relevant factors.

Future cash flows on a group of financial assets that are collectively evaluated for impairment are estimated on the basis of historical loss experience for assets with credit risk characteristics similar to those in the group. Historical loss experience is adjusted on the basis of current observable data to reflect the effects of current conditions that did not affect the years on which the historical loss experience is based and to remove the effects of conditions in the historical period that do not exist currently. Estimates of changes in future cash flows reflect, and are directionally consistent with, changes in related observable data from year to year (such as changes in unemployment rates, property prices, payment status, or other factors that are indicative of incurred losses in the group and their magnitude). The methodology and assumptions used for estimating future cash flows are reviewed regularly to reduce any differences between loss estimates and actual loss experience.

Held-to-maturity financial investments

For held-to-maturity investments the bank assesses individually whether there is objective evidence of impairment. If there is objective evidence that an impairment loss has been incurred, the amount of the loss is measured as the difference between the assets' carrying amount and the present value of estimated future cash flows. The carrying amount of the asset is reduced and the amount of the loss is recognised in the profit or loss for the year.

If, in a subsequent year, the amount of the estimated impairment loss decreases because of an event occurring after the impairment was recognised, any amounts formerly charged are credited to the 'Impairment losses on financial investments'.

Available-for-sale financial investments

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

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

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

Renegotiated loans

Where possible, the bank seeks to restructure loans rather than to take possession of collateral. This may involve extending the payment arrangements and the agreement of new loan conditions. Once the terms have been renegotiated, the loan is no longer considered past due. Management continuously reviews renegotiated loans to ensure

3 SIGNIFICANT ACCOUNTING POLICIES (continued)

Renegotiated loans (continued)

that all criteria are met and that future payments are likely to occur. The loans continue to be subject to an individual or collective impairment assessment, calculated using the loan's original effective interest rate.

Offsetting

Financial assets and financial liabilities are offset and the net amount reported in the statement of financial position if, and only if, there is a currently enforceable legal right to offset the recognised amounts and there is an intention to settle on a net basis, or to realise the asset and settle the liability simultaneously.

Revenue recognition

Revenue is recognised to the extent that it is probable that the economic benefits will flow to the bank and the revenue can be reliably measured. The following specific recognition criteria must also be met before revenue is recognised.

Interest and similar income and expense

For all financial instruments measured at amortised cost, interest bearing financial assets classified as available for-sale and financial instruments designated at fair value through profit or loss, interest income or expense is recorded using the EIR, which is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument or a shorter period, where appropriate, to the net carrying amount of the financial asset or financial liability. The calculation takes into account all contractual terms of the financial instrument and includes any fees or incremental costs that are directly attributable to the instrument and are an integral part of the EIR, but not future credit losses.

The carrying amount of the financial asset or financial liability is adjusted if the bank revises its estimates of payments or receipts. The adjusted carrying amount is calculated based on the original EIR and the change in carrying amount is recorded as 'Other operating income'

Fee and commission income

The bank earns fee and commission income from a diverse range of services it provides to its customers. Fee income can be divided into the following two categories:

- Fee income earned from services that are provided over a certain period of time
- Fees earned for the provision of services over a period of time are accrued over that period. These fees include commission income and asset management, custody and other management and advisory fees.

Loan commitment fees for loans that are likely to be drawn down and other credit related fees are deferred (together with any incremental costs) and recognised as an adjustment to the EIR on the loan. When it is unlikely that a loan will be drawn down, the loan commitment fees are recognised over the commitment period on a straight line basis.

Fee income from providing transaction services

Fees arising from negotiating or participating in the negotiation of a transaction for a third party, such as the arrangement of the acquisition of shares or other securities or the purchase or sale of businesses, sale of insurance products are recognised on completion of the underlying transaction. Fees or components of fees that are linked to a certain performance are recognised after fulfilling the corresponding criteria.

Dividend income

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

Foreign currencies

(i) Transactions denominated in foreign currencies are translated into Rial Omani and recorded at rates of exchange ruling at the value dates of the transactions.

(ii) Monetary assets and liabilities denominated in foreign currencies are translated into Rial Omani at exchange rates ruling at the reporting date. Realised and unrealised gains and losses are dealt with in profit or loss for the year.

(iii) As at the reporting date, the assets and liabilities of overseas branches are translated into the bank's presentation currency at the rate of exchange as at the reporting date, and their statement of comprehensive incomes are translated at the weighted average exchange rates for the year. Exchange differences arising on translation are taken directly to a separate component of equity. On disposal of a foreign entity, the deferred cumulative amount recognised in equity relating to that particular foreign operation is recognised in the profit or loss in 'Other operating expenses' or 'Other operating income'. As the functional currencies of the bank's overseas branches are pegged to Rial Omani, there are no major exchange differences arising on translation.

3 SIGNIFICANT ACCOUNTING POLICIES (continued)

Repurchase and resale agreements

Assets 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 counter party liability for amounts received under these agreements is included in due to banks and other financial institutions. The difference between sale and repurchase price is treated as interest expense and accrued over the life of the repo agreement. Assets 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 deposits with banks and other financial institutions. The difference between purchase and resale price is treated as interest income and accrued over the life of the reverse repo agreement.

Leases

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

Staff terminal benefits

The terminal benefits for employees in Oman are provided in accordance with the Sultanate of Oman's labour law. The end of service benefits for employees in UAE are provided for in accordance with the employees' contracts of employment and applicable requirements of the UAE labour laws. For Egyptian employees the terminal benefits are provided in accordance with the Egyptian social security law.

Segment reporting

The bank's segmental reporting is based on the following operating segments: retail banking, corporate banking, investment banking, treasury and international banking and head office functions. Segment results are reported to the Chief Executive Officer of the Bank, (being the chief operating decision maker) and include items directly attributable to a segment as well as those that can be allocated on a reasonable basis.

Dividend on ordinary shares

Dividends on ordinary shares are recognised as a liability and deducted from equity when they are approved by the bank's shareholders. Interim dividends are deducted from equity when they are paid.

Dividends for the year that are approved after the balance sheet date are dealt with as an event after the balance sheet date.

Directors' remuneration

The board of directors' remuneration is accrued within the limits specified by the Capital Market Authority and the requirements of the Commercial Companies Law of the Sultanate of Oman.

Impairment of non-financial assets

The carrying amount of the Bank's non-financial assets, other than investment property and deferred tax assets are reviewed at each reporting date to determine whether there is any indication of impairment. An impairment loss is recognised only if the carrying amount of an asset exceeds its recoverable amount. An impairment loss is reversed, only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss has been recognised.

4 CASH AND BALANCES WITH CENTRAL BANKS

2011 USD'000	2012 USD'000		2012 RO'000	2011 RO'000
66,974	**80,974**	Cash	**31,175**	25,785
14,919	**9,234**	Treasury bills with Central Banks	**3,555**	5,744
233,766	**64,935**	Certificates of deposit with Central Banks	**25,000**	90,000
256,473	**403,916**	Other balances with Central Banks	**155,508**	98,742
572,132	**559,059**	**Cash and cash equivalents**	**215,238**	220,271
1,299	**1,299**	Capital deposit with Central Bank of Oman	**500**	500
573,431	**560,358**	**Cash and balances with Central Banks**	**215,738**	220,771

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

5 DUE FROM BANKS AND OTHER MONEY MARKET PLACEMENTS (NET)

2011 USD'000	2012 USD'000		2012 RO'000	2011 RO'000
59,657	**212,636**	Loans and advances to banks	**81,865**	22,968
330,257	**295,722**	Placement with banks	**113,853**	127,149
44,200	**73,073**	Demand balances	**28,133**	17,017
434,114	**581,431**	**Due from banks and other money market placements**	**223,851**	167,134
(16,940)	**(16,940)**	Less: allowance for credit losses	**(6,522)**	(6,522)
(177)	**(177)**	Less: reserved interest	**(68)**	(68)
416,997	**564,314**	**Net due from banks and other money market placements**	**217,261**	160,544

As at 31 December 2012 the bank has a limited inter-bank exposure of RO 6.6 million (2011: RO 6.6 million) against two large regional groups who had defaulted on their payment obligations. The bank has recorded a provision of 100% against the same.

6 LOANS AND ADVANCES TO CUSTOMERS (NET)

2011 USD'000	2012 USD'000		2012 RO'000	2011 RO'000
111,821	**102,935**	Overdrafts	**39,630**	43,051
2,026,681	**2,502,774**	Personal loans	**963,568**	780,272
2,213,052	**2,354,109**	Other loans	**906,332**	852,025
100,579	**148,795**	Loans against trust receipts	**57,286**	38,723
50,953	**50,847**	Bills discounted	**19,576**	19,617
4,503,086	**5,159,460**	**Gross loans and advances**	**1,986,392**	1,733,688
(128,460)	**(150,652)**	Allowance for credit losses	**(58,001)**	(49,457)
(34,943)	**(43,712)**	Reserved interest	**(16,829)**	(13,453)
4,339,683	**4,965,096**	**Net loans and advances**	**1,911,562**	1,670,778

6 LOANS AND ADVANCES TO CUSTOMERS (NET) (continued)

The movement in the allowance for credit losses and reserved interest accounts is set out below:

2011 USD'000	2012 USD'000		2012 RO'000	2011 RO'000
		Allowance for credit losses		
149,257	**128,460**	Balance at beginning of the year	**49,457**	57,464
49,174	**44,002**	Provided during the year	**16,941**	18,932
(18,382)	**(8,153)**	Released/recovered during the year	**(3,139)**	(7,077)
(39,561)	**(13,426)**	Written off during the year	**(5,169)**	(15,231)
(11,416)	**-**	Transfer during the year	**-**	(4,395)
(612)	**(231)**	Translation difference	**(89)**	(236)
128,460	**150,652**	**Balance at end of the year**	**58,001**	49,457
		Reserved interest		
29,982	**34,943**	Balance at beginning of the year	**13,453**	11,543
8,951	**14,197**	Reserved during the year	**5,466**	3,446
(1,164)	**(886)**	Released/recovered during the year	**(341)**	(448)
(400)	**(506)**	Released/recovered during the year to interest income	**(195)**	(154)
(2,413)	**(4,021)**	Written off during the year	**(1,548)**	(929)
(13)	**(15)**	Translation difference	**(6)**	(5)
34,943	**43,712**	**Balance at end of the year**	**16,829**	13,453

A further analysis of allowances for credit losses is set out below:

2011 USD'000	2012 USD'000		2012 RO'000	2011 RO'000
64,735	**74,751**	Specific impairment	**28,779**	24,923
63,725	**75,901**	Collective impairment	**29,222**	24,534
128,460	**150,652**		**58,001**	49,457

All loans and advances require payment of interest based on agreed tenors, some at fixed rates and others at rates that re-price prior to maturity. As of 31 December 2012, loans and advances on which interest is not being accrued or where interest has been reserved amounted to RO 79 million – USD 205.2 million (2011 – RO 64 million – USD 166.2 million).

During the year, the bank has written-off fully provided loans and advances amounting to RO 6.7 million – USD -17.4 million (2011: RO 16.2 million – USD 42.1 million) against impairment provisions where the bank believes the possibility of a recovery is low. The bank will continue to pursue the recovery of these loans through all possible means and any future recovery from these written-off loans will be recognised in the profit or loss for the year.

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.

6 LOANS AND ADVANCES TO CUSTOMERS (NET) (continued)

The table below analyses the concentration of gross loans and advances by various sectors.

2011 USD'000	2012 USD'000		2012 RO'000	2011 RO'000
2,026,681	**2,502,774**	Personal	**963,568**	780,272
322,813	**399,938**	Construction	**153,976**	124,283
477,039	**361,574**	Manufacturing	**139,206**	183,660
287,558	**304,958**	Wholesale and retail trade	**117,409**	110,710
254,520	**296,442**	Service	**114,130**	97,990
325,484	**294,491**	Transport and communication	**113,379**	125,312
257,901	**254,216**	Others	**97,873**	99,291
250,940	**245,325**	Financial institutions	**94,450**	96,612
82,735	**234,229**	Electricity, gas and water	**90,178**	31,853
90,340	**136,374**	Import trade	**52,504**	34,781
94,473	**94,013**	Mining and quarrying	**36,195**	36,372
31,574	**33,195**	Agriculture	**12,780**	12,156
18	**1,082**	Government	**417**	7
1,010	**849**	Export trade	**327**	389
4,503,086	**5,159,460**		**1,986,392**	1,733,688

The geographic distribution of loans and advances to customers, based on the location of the borrower is as follows:

2011 USD'000	2012 USD'000		2012 RO'000	2011 RO'000
4,286,271	**4,968,434**	Sultanate of Oman	**1,912,847**	1,650,214
151,091	**143,829**	United Arab Emirates	**55,374**	58,170
8,525	**6,463**	Egypt	**2,488**	3,282
57,199	**40,734**	Others	**15,683**	22,022
4,503,086	**5,159,460**		**1,986,392**	1,733,688

7 NON-TRADING FINANCIAL INVESTMENTS

	Carrying value 31/12/2012 RO'000	Cost 31/12/2012 RO'000	Carrying value 31/12/2011 RO'000	Cost 31/12/2011 RO'000
Available for sale investments				
Quoted investments - Oman				
Banking and investment sector	**741**	**758**	1,347	1,464
Industry sector	**1,162**	**973**	1,692	2,384
Service sector	**8,365**	**7,983**	6,884	8,004
Government development bonds	**86,170**	**86,170**	74,405	74,405
	96,438	**95,884**	84,328	86,257
Quoted investments – Foreign				
Government development bonds	**3,593**	**3,656**	3,649	3,830
Unquoted investments				
Banking and investment sector	**6,920**	**7,386**	6,776	7,386
Industry sector	**3,483**	**3,483**	-	-
Service sector	**288**	**288**	269	269
	10,691	**11,157**	7,045	7,655
Total non-trading investments	**110,722**	**110,697**	95,022	97,742
Total non-trading investments – USD'000	**287,590**	**287,525**	246,810	253,875

Included under unquoted available for sale investments are investments with a value of RO 3.91 million – USD 10.16 million (2011 – RO 0.40 million – USD 1.05 million), which are carried at cost, less any impairment losses, due to the unpredictable nature of future cash flows and the lack of other suitable methods for arriving at a reliable fair value. All other available for sale investments are carried at fair value.

During the year, the bank has recorded RO 1.54 million - USD 4.0 million (2011 – RO 2.29 million – USD 5.94 million) as impairment losses against its available for sale investments.

The impairment loss on available for sale investments is recognised in view of either a significant or prolonged decline in the fair value of the investment below cost.

7 NON-TRADING FINANCIAL INVESTMENTS (continued)

Details of significant investments

Details of investments exceeding 10% of the carrying value of the bank's investment available for sale portfolio are as follows:

31 December 2012	Bank's portfolio %	Carrying value RO'000	Cost RO'000	Carrying value USD'000	Cost USD'000
Government development bonds-Oman	**77.8**	**86,170**	**86,170**	**223,818**	**223,818**
31 December 2011					
Government development bonds-Oman	78.30	74,405	74,405	193,260	193,260

8 PREMISES AND EQUIPMENT

	Freehold land and buildings and leasehold improvements RO'000	Motor vehicles, furniture and equipment RO'000	Capital work in progress RO'000	Total RO'000
Reconciliation of carrying amount:				
Balance as at 1 January 2012, net of accumulated depreciation	13,009	6,508	988	20,505
Additions	133	940	2,843	3,916
Disposals	(141)	(23)	(19)	(183)
Transfers	1,010	443	(1,453)	-
Translation difference	(16)	2	-	(14)
Depreciation	(1,299)	(2,427)	-	(3,726)
Balance as at 31 December 2012, net of accumulated depreciation	**12,696**	**5,443**	**2,359**	**20,498**
At cost	21,844	24,565	2,359	48,768
At revaluation	3,766	-	-	3,766
Accumulated depreciation	(12,914)	(19,122)	-	(32,036)
Net carrying value at 31 December 2012	**12,696**	**5,443**	**2,359**	**20,498**
Net carrying value at 31 December 2012 – USD'000	**32,977**	**14,138**	**6,127**	**53,242**

8 PREMISES AND EQUIPMENT (continued)

	Freehold land and buildings and leasehold improvements RO'000	Motor vehicles, furniture and equipment RO'000	Capital work in progress RO'000	Total RO'000
At cost 1 January 2011	21,811	23,827	988	46,626
At revaluation	3,766	-	-	3,766
Accumulated depreciation	(12,568)	(17,319)	-	(29,887)
Net carrying value at 31 December 2011	**13,009**	**6,508**	**988**	**20,505**
Net carrying value at 31 December 2011 – USD'000	**33,790**	**16,904**	**2,566**	**53,260**

Freehold land stated at cost of RO 8.56 million – USD 22.22 million (2011 – RO 8.56 million – USD 22.22 million) is not depreciated. Land and buildings include three buildings on freehold land, which were re-valued at their open market value for existing use by an independent professional valuer as of 31 October 2010, at RO 3.77 million (USD 9.79 million) from the then existing value of RO 2.81 million (USD 7.30 million). On revaluation, the gross carrying amount of each building re-valued was restated so that the net carrying amount of the asset after revaluation equals its re-valued amount. Should the buildings be carried at cost less depreciation, the net carrying amount would have been RO 0.88 million – USD 2.29 million (2011 – RO 1.12 million – USD 2.91 million).

9 OTHER ASSETS

2011 USD'000	**2012 USD'000**		**2012 RO'000**	2011 RO'000
59,811	**58,988**	Interest receivable and others	**22,710**	23,027
28,681	**28,753**	Positive fair value of derivatives (note 33)	**11,070**	11,042
69,873	**72,332**	Customers' indebtedness for acceptances	**27,848**	26,901
158,365	**160,073**		**61,628**	60,970
8,982	**4,652**	Amount receivable from BCCI	**1,791**	3,458
(8,982)	**(4,652)**	Less: provision for amount due from BCCI	**(1,791)**	(3,458)
-	**-**		**-**	-

During the year RO 1.7 million was received from BCCI towards the final dividend. Full impairment provision has been recorded by the bank against the remaining amounts due from BCCI.

10 DUE TO BANKS AND OTHER MONEY MARKET DEPOSITS

2011 USD'000	**2012 USD'000**		**2012 RO'000**	2011 RO'000
549,223	**528,000**	Acceptances and borrowings	**203,280**	211,451
30,385	**18,616**	Other balances	**7,167**	11,698
579,608	**546,616**		**210,447**	223,149

11 CUSTOMERS' DEPOSITS

2011 USD'000	2012 USD'000		2012 RO'000	2011 RO'000
810,584	**1,002,504**	Current accounts	**385,964**	312,075
978,899	**1,254,400**	Savings accounts	**482,944**	376,876
2,258,631	**2,630,769**	Term deposits	**1,012,846**	869,573
107,273	**12,987**	Certificates of deposit	**5,000**	41,300
4,155,387	**4,900,660**		**1,886,754**	1,599,824

12 OTHER LIABILITIES

2011 USD'000	2012 USD'000		2012 RO'000	2011 RO'000
67,436	**74,281**	Interest payable & others	**28,598**	25,963
2,629	**3,026**	Staff entitlements	**1,165**	1,012
69,873	**72,332**	Liabilities under acceptances	**27,848**	26,901
28,717	**29,005**	Negative fair value of derivatives (note 33)	**11,167**	11,056
168,655	**178,644**		**68,778**	64,932
		Staff entitlements are as follows:		
2,291	**2,652**	End of service benefits	**1,021**	882
338	**374**	Other liabilities	**144**	130
2,629	**3,026**		**1,165**	1,012
		Movement in the end of service benefits liability are as follows:		
2,501	**2,291**	Liability as at 1 January	**882**	963
494	**704**	Expense recognised in the statement of comprehensive income	**271**	190
(704)	**(343)**	End of service benefits paid	**(132)**	(271)
2,291	**2,652**	**Liability as at 31 December**	**1,021**	882

13 TAXATION

2011 USD'000	2012 USD'000		2012 RO'000	2011 RO'000
		Current tax expense		
12,836	**15,462**	Current year	**5,953**	4,942
(1,158)	**168**	Deferred tax adjustment	**65**	(446)
11,678	**15,630**		**6,018**	4,496

13 TAXATION (continued)

The bank is liable to income tax at the following rates:

- Sultanate of Oman : 12% of consolidated taxable income in excess of RO 30,000
- United Arab Emirates : 20% of taxable income
- Egypt : 20% of taxable income

Set out below a reconciliation between income tax calculated on accounting profits with income tax expense for the year:

2011 USD'000	2012 USD'000		2012 RO'000	2011 RO'000
100,514	**121,246**	Accounting profit	**46,680**	38,698
12,062	**14,540**	Tax at applicable rate	**5,598**	4,644
1,364	**764**	Non-deductible expenses	**294**	525
(917)	**(857)**	Tax exempt revenues	**(330)**	(353)
(831)	**1,183**	Others	**456**	(320)
11,678	**15,630**		**6,018**	4,496

The bank's liabilities for taxation in the Sultanate of Oman has been assessed up to the year ended 31 December 2007.

The tax assessments of the Egypt operations in respect of the different taxes applicable are at different stages of completion with the respective tax authorities. The bank's liability in respect of its branch in Abu Dhabi has been agreed with the tax authorities up to 31 December 2011.

2011 USD'000	2012 USD'000		2012 RO'000	2011 RO'000
		Tax liability		
		Current year		
12,836	**15,462**	Income tax and other taxes	**5,953**	4,942
		Prior year		
774	**(691)**	Income tax and other taxes	**(266)**	298
13,610	**14,771**		**5,687**	5,240

Recognised deferred tax assets

2011 USD'000	2012 USD'000		2012 RO'000	2011 RO'000
		Deferred tax assets are attributable to the following:		
1,158	**990**	Deductible temporary differences Provisions	**381**	446
94	**72**	Available for sale investments -Overseas	**28**	36
1,252	**1,062**		**409**	482

Deferred tax is calculated at 12% (2011 – 12%).

De-recognised deferred tax assets

2011 USD'000	2012 USD'000		2012 RO'000	2011 RO'000
-	**168**	Deductible temporary differences Provisions	**65**	-

14 SUBORDINATED DEBT

2011 USD'000	2012 USD'000		2012 RO'000	2011 RO'000
79,481	**142,078**	At I January	**54,700**	30,600
62,597	**18,182**	Received during the year	**7,000**	24,100
142,078	**160,260**		**61,700**	54,700

(i) Placements received in 2012 are repayable in December 2018.

(ii) Placements received in prior years are repayable up to 2017.

15 SHARE CAPITAL

2011 USD'000	2012 USD'000		2012 RO'000	2011 RO'000
415,584	**519,481**	Authorised - ordinary shares of RO 0.100 each	**200,000**	160,000
280,779	**287,799**	Issued and fully paid - ordinary shares of RO 0.100 each	**110,803**	108,100

The increase in the authorised share capital has been made in view of planned expansion, including the establishment of the Islamic Banking Window.

As of 31 December 2012, the following shareholders held 10% or more of the bank's capital:

	Number of shares '000	% Holding
The Commercial Bank of Qatar	**386,699**	34.90%
Suhail Bahwan Group (Holdings) L.L.C	**163,370**	14.74%

The percentage shareholding is calculated based on the total shares of the bank outstanding at the reporting date.

16 SHARE PREMIUM RESERVE

The share premium of RO 34.5 million (USD 89.5 million) represents the premium collected on issue of 10 million shares by the bank through a private placement for RO 4.45 (USD 11.56) per share. This was approved by the Bank's shareholders at the Bank's Extraordinary General Meeting held on 25 June 2005 at which time the face value of the Bank's share was RO 1.

17 LEGAL RESERVE

The legal reserve, which is not available for distribution, is accumulated in accordance with the requirements of the Commercial Companies Law of Oman and the Union Law No. 10 of Abu Dhabi. The annual appropriations must not be less than 10% of the profit for the year until such time that the respective reserve account balance amounts to at least one third of the share capital in Oman and half of the branch capital in Abu Dhabi. At 31 December 2012, the legal reserve of Oman has reached one third of the issued capital.

18 GENERAL RESERVE

The general reserve was created on 9 May 2006 by way of a transfer from the subordinated debt reserve to a general reserve. The transfer was made on account of prepayment of certain subordinated debt during 2006 resulting in surplus in subordinated debt reserve. This reserve is available for distribution.

19 OTHER NON-DISTRIBUTABLE RESERVES

	Available for sale reserve RO '000	Revaluation reserve RO '000	Subordinated debt reserve RO '000	Total RO '000
At 1 January 2012	(328)	3,766	14,860	18,298
Net movement on available for sale investments	1,489	-	-	1,489
Tax effect of net losses on available for sale financial investments	(8)	-	-	(8)
Transfer to subordinated debt reserve	-	-	10,940	10,940
At 31 December 2012	**1,153**	**3,766**	**25,800**	**30,719**
At 31 December 2012 – In USD'000	**2,995**	**9,782**	**67,013**	**79,790**

(i) The revaluation reserve represents the surplus on revaluation of building and is not available for distribution until the related assets have been disposed off or used.

(ii) The subordinated debt reserve represents an annual transfer towards subordinated debt which is due to mature within the next five years period (note 14). The reserve is available for transfer back to retained earning upon maturity of the private placement.

20 DIVIDENDS PAID AND PROPOSED

The Board of Directors have proposed a cash dividend of RO 0.0175 per share totalling RO 19.4 million (USD 0.045 per share totalling USD 50.4 million) for the year ended 31 December 2012, which is subject to the approval of the shareholders at the Annual General Meeting to be held in March 2013.

At the Annual General Meeting held in March 2012, a cash dividend of RO 0.0175 per share totalling RO 18.9 million (USD 0.045 per share totalling USD 49.1 million) and stock dividend of RO 0.0025 per share totalling RO 2.7 million (USD 0.006 per share totalling USD 7.0 million) for the year ended 31 December 2011 was approved and subsequently paid.

21 CONTINGENT LIABILITIES AND COMMITMENTS

To meet the financial needs of customers, the bank enters into various commitments and contingent liabilities. Even though these obligations may not be recognized on the statement of financial position, they do contain credit risk and are therefore part of the overall risk of the bank.

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 expiration 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 requirements.

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.

Contingent liabilities

As of the reporting date, commitments on behalf of customers for which there were corresponding customer liabilities consisted of the following:

2011 USD'000	**2012 USD'000**		**2012 RO'000**	2011 RO'000
1,134,769	**1,186,288**	Guarantees	**456,721**	436,886
184,229	**155,590**	Documentary letters of credit	**59,902**	70,928
1,318,998	**1,341,878**		**516,623**	507,814

21 CONTINGENT LIABILITIES AND COMMITMENTS (continued)

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

2011 USD'000	2012 USD'000		2012 RO'000	2011 RO'000
548,179	488,639	Financial institutions	188,126	211,049
302,369	361,325	Construction	139,110	116,412
129,481	128,197	Electricity, gas and water	49,356	49,850
96,709	111,818	Wholesale and retail trade	43,050	37,233
92,192	88,145	Manufacturing	33,936	35,494
27,961	74,514	Service	28,688	10,765
65,351	70,725	Others	27,229	25,160
45,875	15,060	Transport and communication	5,798	17,662
9,810	1,912	Mining and Quarrying	736	3,777
421	956	Agriculture	368	162
356	506	Personal	195	137
294	81	Import trade	31	113
1,318,998	1,341,878		516,623	507,814

Guarantees include RO 0.1 million – USD 0.3 million (Dec 2011: RO 0.1 million – USD 0.3 million) relating to non-performing loans.

Commitments

2011 USD'000	2012 USD'000		2012 RO'000	2011 RO'000
197,977	388,639	Undrawn commitment	149,626	76,221
735	2,114	Capital expenditure	814	283
8,114	7,218	Operating lease commitments	2,779	3,124
		Future minimum lease payments:		
3,312	3,096	Not later than one year	1,192	1,275
4,558	4,122	Later than one year and not later than five years	1,587	1,755
244	-	Later than five years	-	94
8,114	7,218		2,779	3,124

Branches

The bank has deposited in the countries concerned, the following amounts of capital as support for its overseas branches. These amounts cannot be withdrawn without the approval of the Central Banks of the countries concerned.

2011 USD'000	2012 USD'000		2012 RO'000	2011 RO'000
14,294	14,294	Abu Dhabi branch	5,503	5,503
50,000	50,000	Egypt branches	19,250	19,250
64,294	64,294		24,753	24,753

Legal claims

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

Fiduciary assets

The fair value of securities as of 31 December 2012 held on trust for customers amounts to RO 59.07 million -USD 153.43 million (2011 – RO 50.40 million – USD 130.91 million).

22 INTEREST INCOME

2011 USD'000	2012 USD'000		2012 RO'000	2011 RO'000
237,631	**270,865**	Interest from customers	**104,283**	91,488
4,852	**7,319**	Interest from banks	**2,818**	1,868
242,483	**278,184**		**107,101**	93,356

Interest bearing assets, other than investments earned interest at an overall effective annual rate of 5.07% for the year ended 31 December 2012 (31 December 2011 – 5.31%).

23 INTEREST EXPENSE

2011 USD'000	2012 USD'000		2012 RO'000	2011 RO'000
87,618	**94,979**	Interest to customers	**36,567**	33,733
3,730	**8,714**	Interest to banks	**3,355**	1,436
91,348	**103,693**		**39,922**	35,169

For the year ended 31 December 2012, the average overall effective annual cost of bank's funds was 1.98% (31 December 2011 – 2.13%).

24 OTHER OPERATING INCOME

2011 USD'000	2012 USD'000		2012 RO'000	2011 RO'000
26,995	**25,083**	Fees and commission income	**9,657**	10,393
(47)	**(55)**	Fees and commission expense	**(21)**	(18)
26,948	**25,028**	**Net fees and commissions**	**9,636**	10,375
42,016	**37,426**	Service charges	**14,409**	16,176
2,130	**990**	Profit on sale of investments	**381**	820
8,005	**8,504**	Net gains from foreign exchange dealings	**3,274**	3,082
1,849	**1,379**	Miscellaneous income	**531**	712
3,990	**5,992**	Income from bonds and others	**2,307**	1,536
3,498	**2,410**	Dividend income	**928**	1,347
88,436	**81,729**		**31,466**	34,048

25 OTHER OPERATING EXPENSES

2011 USD'000	2012 USD'000		2012 RO'000	2011 RO'000
12,262	12,013	Establishment costs	4,625	4,721
24,707	30,338	Operating and administration costs	11,680	9,512
353	314	Directors' remuneration	121	136
37,322	42,665		16,426	14,369

26 RELATED PARTY TRANSACTIONS

Management service agreement with a shareholder

The Board of Directors of the National Bank of Oman SAOG had entered into a Management Services Agreement with its strategic partner, The Commercial Bank of Qatar in 2005 to provide NBO with management services. As the management and processes of the Bank have been substantially strengthened, the Commercial Bank of Qatar did not extend the term of the agreement on its expiry in March 2011.

Other related party transactions:

In the ordinary course of business, the bank conducts transactions with certain of its directors and/or shareholders and companies over which they have significant interest. The aggregate amounts of balances with such related parties are as follows:

	2012			2011		
	Principal shareholder RO'000	Others RO'000	Total RO'000	Principal shareholder RO'000	Others RO'000	Total RO'000
Loans and advances	-	53,677	53,677	-	33,398	33,398
Customer's deposits	-	9,631	9,631	-	9,353	9,353
Due from banks	34,682	-	34,682	14	-	14
Due to banks	9,683	13,475	23,158	25,083	12,423	37,506
Subordinated debt	-	5,500	5,500	-	2,500	2,500
Letter of credit, guarantees and acceptance	2,177	2,724	4,901	1,500	5,796	7,296
Standby revolving credit facility	77,000	-	77,000	77,000	-	77,000
Risk indemnities received	546	4,000	4,546	-	8,000	8,000

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

	2012			2011		
	Principal shareholder RO'000	Others RO'000	Total RO'000	Principal shareholder RO'000	Others RO'000	Total RO'000
Interest income	13	1,460	1,473	11	1,171	1,182
Commission income	5	19	24	-	21	21
Interest expense	353	355	708	261	421	682
Other expenses	205	1,148	1,353	120	872	992
Director's remuneration and sitting fees	-	200	200	-	200	200

26 RELATED PARTY TRANSACTIONS (continued)

	2012			2011		
	Principal shareholder USD'000	Others USD'000	Total USD'000	Principal shareholder USD'000	Others USD'000	Total USD'000
Loans and advances	-	139,421	139,421	-	86,748	86,748
Customer›s deposits	-	25,016	25,016	-	24,294	24,294
Due from banks	90,082	-	90,082	36	-	36
Due to banks	25,152	35,000	60,152	65,151	32,268	97,419
Subordinated debt	-	14,286	14,286	-	6,494	6,494
Letter of credit, guarantees and acceptance	5,655	7,075	12,730	3,896	15,055	18,951
Standby revolving credit facility	200,000	-	200,000	200,000	-	200,000
Risk indemnities received	1,418	10,390	11,808	-	20,779	20,779

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

	2012			2011		
	Principal shareholder USD'000	Others USD'000	Total USD'000	Principal shareholder USD'000	Others USD'000	Total USD'000
Interest income	33	3,793	3,826	29	3,042	3,071
Commission income	13	49	62	-	55	55
Interest expense	916	922	1,838	678	1,094	1,772
Other expenses	533	2,983	3,516	312	2,265	2,577
Directors remuneration and sitting fees	-	519	519	-	519	519

Details regarding senior management compensation are set out below:

2011 USD'000	2012 USD'000		2012 RO'000	2011 RO'000
		Salaries and other short term benefits		
4,972	5,147	- Fixed	1,981	1,914
1,005	1,652	- Discretionary	636	387
5,977	6,799		2,617	2,301

27 BASIC AND DILUTED EARNING PER SHARE

Earning per share is calculated by dividing the profit for the year by the weighted average number of shares outstanding during the year as follows:

	2012	2011
Profit for the year (RO'000s)	**40,662**	34,202
Weighted average number of shares outstanding during the year (in '000s)	**1,108,025**	1,108,025
Earnings per share (RO)	**0.037**	0.031
Profit for the year (USD'000s)	**105,616**	88,836
Weighted average number of shares outstanding during the year (in '000s)	**1,108,025**	1,108,025
Earnings per share (USD)	**0.10**	0.08

During the year 2012, the bank issued stock dividend of RO 0.0025 per share totalling RO 2.7 million (USD 0.006 per share totalling USD 7.0 million) to the existing shareholders. As issue was without any consideration, the number of ordinary shares outstanding before the event is adjusted for the proportionate change in the number of ordinary shares outstanding as if the event had occurred at the beginning of the earliest period presented.

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

28 CAPITAL ADEQUACY

The bank maintains an actively managed capital base to cover risks inherent in the business. The adequacy of the bank's capital is monitored using, among other measures, the rules and ratios established by the Basel Committee on Banking Supervision and adopted by the Central Bank of Oman in supervising the bank.

During the past year, the bank had complied in full with all its externally imposed capital requirements.

Capital management

The primary objectives of the bank's capital management are to ensure that the bank complies with externally imposed capital requirements and that the bank maintains strong credit ratings and healthy capital ratios in order to support its business and to maximise shareholders' value.

The bank manages its capital structure and makes adjustments to it in the light of changes in economic conditions and the risk characteristics of its activities. In order to maintain or adjust the capital structure, the bank may adjust the amount of dividend payment to shareholders, return capital to shareholders or issue capital securities. The Capital Management Policy was revised during the year to incorporate the regulatory changes.

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.

28 CAPITAL ADEQUACY (continued)

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

2011 USD'000	2012 USD'000		2012 RO'000	2011 RO'000
		Capital base		
670,288	**726,439**	Tier 1 - shareholders' funds	**279,679**	258,061
167,205	**170,527**	Tier 2 - subordinated debt and collective impairment provisions	**65,653**	64,374
837,493	**896,966**	**Total capital base**	**345,332**	322,435
		Risk weighted assets		
5,004,016	**5,768,641**	Credit risk	**2,220,927**	1,926,546
402,166	**432,860**	Operational risk	**166,651**	154,834
63,735	**26,081**	Market risk	**10,041**	24,538
5,469,917	**6,227,582**	**Total risk weighted assets**	**2,397,619**	2,105,918
15.3%	**14.4%**	**Risk asset ratio (Basel II norms)**	**14.4%**	15.3%

29 RISK MANAGEMENT

The primary objective of risk management is to safeguard the bank's resources from the various risks which the bank faces. The Risk Group comprises of Corporate Credit Risk, Retail Credit Risk, Market Risk, Operational Risk, Information Security and Business Continuity Risk, Legal Risk, Loan Review Mechanism and Remedial Management. All risk management functions report to Chief Risk Officer and are independent from Business Units. The bank has exposure to the following risks:-

CREDIT RISK

Credit risk is the risk that the bank will incur a loss because its customers, clients or counterparties failed to discharge their contractual obligations to the bank. The bank manages and controls credit risk by setting internal limits on the amount of risk it is willing to accept for individual counterparties and groups (single obligors) and industry sectors in line with the guidelines of Central Bank of Oman. The bank computes expected losses on credit exposure on the basis of risk classification of both corporate and retail loans in the delinquent category based on the guidelines of Central Bank of Oman.

Credit risk management

Credit Risk is managed within the regulatory requirements of Central Bank of Oman; risk framework provided in the Board approved Risk Charter and Credit Policies and Procedures. The policies and procedures are periodically reviewed to ensure alignment to the current best practices. Credit exposures are approved by delegated authorities based on delegation by the Board and Board Risk Committee. The delegation of authorities is based on the size of the single obligor exposure, the credit quality (internal, external rating) as well as level of credit risk mitigation (collateral, guarantees, etc.) for the proposed exposures. For retail exposures, there is delegation of authority for handling exceptions to approved program lending. Control, monitoring and management of credit exposures are done in coordination with respective Business Units as per established procedures.

Corporate credit

Corporate Credit Risk Division is responsible for independent assessment and control of the risks related to all Corporate, Business Banking and Financial Institutions exposures. The Division reviews and assesses credit risk for proposed exposures prior to facilities being committed to customers by the concerned business units. Renewals and reviews of facilities are subject to the same process. Each proposal is also assessed with respect to established concentration limits for various economic sectors, countries, risk grades, etc. and deviations, if any are highlighted. The bank follows risk based pricing and each credit proposal is also assessed based on internal benchmarks of required risk adjusted returns. The bank has implemented a customized Moody's Risk Analyst model for risk rating corporate borrowers. Corporate Credit Risk Division also provides advice and guidance to business units with a view to promoting best practices throughout the bank in the management of credit risk.

29 RISK MANAGEMENT (continued)

CREDIT RISK (continued)

Corporate credit (continued)

In addition to formal annual credit risk reviews of each corporate facility, more frequent reviews are also undertaken for watch list accounts, public companies and large exposures. Further, the bank has introduced quarterly review of financial institutions and country portfolio including stress tests and review of adverse rating migrations and outlooks in line with best practices and regulatory guidelines.

A comprehensive review of the Corporate Credit Portfolio is conducted on a quarterly basis and provided to the Senior Management and the Board Risk Committee. Salient areas covered in the review include:-

- Exposures downgraded/negatively migrated
- Weighted average credit grade profile
- Portfolio concentration/ performance
- Position of restructured exposures
- Position of past due exposures
- Exposures secured by equity
- Exposures to real estate and leasing sectors
- Syndicated exposures
- New relationships
- Exposures to senior members and non-resident borrowers
- Exposures to countries / financial institutions
- Clean lending and name lending exposures

Retail credit

Retail Credit Division manages the credit risk in the retail portfolio. Credit facilities are offered to retail customers primarily based on Product Programs approved by Risk Committee of the Board. The lending criteria for these programs are regularly reviewed and revised, if required, based on an on-going analysis of product performance and portfolio credit quality and perceived risk. Credit facilities outside the Product Programs are individually assessed by the Retail Credit Risk Division and approved as per the delegated authorities.

A review of the Retail Credit Portfolio is conducted on a monthly basis and provided to the Management Risk Committee, and every quarter the preceding month's report is presented to the Board Risk Committee. Salient areas covered in the review include:

Portfolio review

Management Summary of Delinquency and NPA trends (which includes product-wise delinquency analysis, vintage analysis, and delinquencies across various credit criteria, etc.)

Projects undertaken / fulfilled during the month

Recoveries

Several system enhancements and new processes have been introduced across critical activities to improve processing quality and efficiency, and to enhance the recovery methodologies of the retail portfolio. The bank has reworked its strategy of lending through adoption of stricter lending criteria and continuous monitoring of the portfolio and is in the process of implementing a Loan origination system, Credit Scoring Module and Collections solution to enhance its Retail Credit Risk framework.

Loan review mechanism

The bank has established an independent Loan Review Mechanism Division with a mandate for constantly evaluating the quality of the loan book; balance between risk and reward and to bring about qualitative improvements in credit administration. The division evaluates the effectiveness of loan administration, integrity of the credit grading process, assessment of general and specific loan loss provisions, portfolio quality, etc.

29 RISK MANAGEMENT (continued)

CREDIT RISK (continued)

Remedial management

The bank's Remedial Management Division relentlessly pursues each delinquent account, by using all available measures, to reduce exposure and maximize recoveries to progressively improve the status of the portfolio and whenever appropriate rehabilitates these relationships so that they can be returned to the business lines as fully performing accounts.

Risk mitigation policies

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

Maximum exposure to credit risk

Gross maximum exposure 2011 USD'000	**Gross maximum exposure 2012 USD'000**		**Gross maximum exposure 2012 RO '000**	Gross maximum exposure 2011 RO '000
506,457	**479,385**	Balances with Central Banks	**184,563**	194,986
416,997	**564,314**	Due from banks and other money market placements(net)	**217,261**	160,544
4,339,683	**4,965,096**	Loans and advances to customers (net)	**1,911,562**	1,670,778
246,810	**287,590**	Non-trading financial investments	**110,722**	95,022
158,365	**160,073**	Other assets	**61,628**	60,970
5,668,312	**6,456,458**	**Total on balance sheet exposure**	**2,485,736**	2,182,300
1,134,769	**1,186,288**	Guarantees	**456,721**	436,886
184,229	**155,590**	Documentary letters of credit	**59,902**	70,928
197,977	**388,639**	Undrawn commitment	**149,626**	76,221
15,000	**-**	Credit default swaps	**-**	5,775
1,531,975	**1,730,517**	**Total off balance sheet exposure**	**666,249**	589,810

The above table represents the worst case scenario of credit risk exposure to the bank at 31 December 2012 and 2011 without taking into account the collateral held or other credit enhancements. Management is confident that the bank has suitable policies to measure and control the credit risk. In addition credit risk is mitigated through collaterals in the form of mortgages and guarantees wherever required.

29 RISK MANAGEMENT (continued)

CREDIT RISK (continued)

An analysis of the credit quality of the bank's loan and advances is set out below:

	Performing loans (neither past due nor impaired) RO'000	Loans past due and not impaired RO'000	Non performing loans RO'000	Gross loans RO'000
Balance as at 1 January 2012	1,637,368	32,283	64,037	1,733,688
Additions during the year	515,527	280,503	17,791	813,821
Attrition during the year	(240,059)	(292,428)	(21,913)	(554,400)
Written-off during the year	-	-	(6,717)	(6,717)
Balance as at 31 December 2012	**1,912,836**	**20,358**	**53,198**	**1,986,392**
Balance as at 31 December 2012 – USD'000s	**4,968,405**	**52,878**	**138,177**	**5,159,460**
Balance as at 31 December 2011	1,637,368	32,283	64,037	1,733,688
Balance as at 31 December 2011 – USD'000s	4,252,904	83,852	166,330	4,503,086

An ageing analysis of the bank's loans which are past due but not impaired is set out below:

	Loans in arrears 1-30 days RO'000	Loans in arrears 31-60 days RO'000	Loans in arrears 61-89 days RO'000	Total RO'000
Loans and advances to customers (net) at				
31 December 2012	**2,438**	**11,470**	**6,450**	**20,358**
31 December 2012 – USD'000s	**6,332**	**29,792**	**16,754**	**52,878**
31 December 2011	12,017	12,921	7,345	32,283
31 December 2011 – USD'000s	31,213	33,561	19,078	83,852

Collateral and other credit enhancements

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

- Charges over business assets such as premises, inventory and accounts receivable
- Lien on fixed deposits
- Cash margins
- Mortgages over residential and commercial properties
- Pledge of marketable shares and securities
- The housing loans are secured by mortgage over the residential property.

The Management monitors the market value of collateral, requests additional collateral in accordance with the underlying agreement, and monitors the market value of collateral obtained during its review of the adequacy of the allowance for impairment losses.

29 RISK MANAGEMENT (continued)

CREDIT RISK (continued)

It is the bank's policy to dispose of repossessed properties in an orderly fashion. The proceeds are used to reduce or repay the outstanding claim. In general, the bank does not occupy repossessed properties for business use.

An analysis of the collateral held and other credit enhancement held against loan and advances granted is as follows:

	Performing loans (neither past due nor impaired) RO'000	Loans past due and not impaired RO'000	Non performing loans RO'000	Total RO'000
Collateral available	913,138	41,737	11,117	965,992
Guarantees available	28,024	-	-	28,024
Government soft loans*	5,616	-	5,182	10,798
Balance as at 31 December 2012	**946,778**	**41,737**	**16,299**	**1,004,814**
Balance as at 31 December 2012 – USD'000s	**2,459,163**	**108,408**	**42,335**	**2,609,906**
Balance as at 31 December 2011	881,597	8,714	16,160	906,471
Balance as at 31 December 2011 – USD'000s	2,289,862	22,634	41,974	2,354,470

* Government Soft Loans are guaranteed by the Government to the extent of the outstanding principal.

The amount of total secured loan and advances is less than the total value of collateral as stated above.

Impairment and provisioning policy

An assessment is made at each reporting date to determine whether there is objective evidence that a specific financial asset may be impaired. If such evidence exists, the estimated recoverable amount of that asset is determined and any impairment loss, based on the net present value of future anticipated cash flows, recognised in the statement of comprehensive income. In addition the bank creates collective provision.

A further analysis of the bank's non-performing loans in accordance with the classification requirements of Central Bank of Oman is as follows:

	Substandard RO'000	Doubtful RO'000	Loss RO'000	Total RO'000
Balance as at 1 January 2012	15,800	20,282	27,955	64,037
Additions during the year	3,145	1,652	12,994	17,791
Attrition during the year	(11,956)	(3,539)	(6,418)	(21,913)
Written-off during the year	-	-	(6,717)	(6,717)
Balance as at 31 December 2012	**6,989**	**18,395**	**27,814**	**53,198**
Balance as at 31 December 2012 – USD'000s	**18,153**	**47,779**	**72,245**	**138,177**
Balance as at 31 December 2011	15,800	20,282	27,955	64,037
Balance as at 31 December 2011 – USD'000s	41,039	52,681	72,610	166,330

29 RISK MANAGEMENT (continued)

CREDIT RISK (continued)

Movement of rescheduled loans:

	2012 RO'000	2011 RO'000
Balance as at 1 January	78,053	88,695
Additions during the year	3,611	21,392
Attrition during the year	(27,408)	(32,034)
Balance as at 31December	**54,256**	78,053
Balance as at 31December – USD'000s	**140,925**	202,735

LIQUIDITY RISK

Liquidity risk is the risk that the bank will be unable to meet its payment obligations when they fall due under normal and stressed circumstances. To limit this risk, the management continuously looks for opportunities to diversify its funding sources in addition to its core deposit base, manages assets with liquidity in mind, and monitors future cash flows and liquidity on a daily basis. This incorporates an assessment of expected cash flows and the availability of high grade collateral which could be used to secure additional funding if required.

The bank maintains liquidity by continually assessing, identifying and monitoring changes in funding needs required to meet strategic goals set in terms of the overall strategy. In addition the bank holds certain liquid assets as part of its liquidity risk management strategy.

The bank manages the liquidity risk based on the Central Bank of Oman guidelines and the Liquidity and Liquidity Contingency Policies, which are approved and periodically reviewed by the Board Risk Committee. Liquidity Risk position is monitored regularly through analysis of various reports, such as, Maturity of Assets and Liabilities, Liquidity Lines, Early Warning Indicators and Stock Ratios. Further, the bank also periodically conducts stress tests on liquidity based on market and bank specific events in line with Basel Committee recommendations. The liquidity position of the bank and stress test scenarios are regularly reviewed by the management and also discussed at the Board Risk Committee.

29 RISK MANAGEMENT (continued)

LIQUIDITY RISK (continued)

The maturity profile of the assets, liabilities and equity at 31 December 2012 is as follows:

	On demand within 3 months RO'000	3 to 12 months RO'000	Subtotal less than 12 months RO'000	1 to 5 years RO'000	Over 5 years RO'000	Subtotal over 12 months RO'000	Total RO'000
Cash and balances with Central Banks	128,296	34,973	163,269	32,456	20,013	52,469	215,738
Due from banks and other money market placements (net)	168,512	48,749	217,261	-	-	-	217,261
Loans and advances (net)	461,545	110,386	571,931	354,349	985,282	1,339,631	1,911,562
Non-trading financial investments	89,985	-	89,985	20,737	-	20,737	110,722
Premises and equipment	-	-	-	-	20,498	20,498	20,498
Deferred tax asset	409	-	409	-	-	-	409
Other assets	59,737	1,797	61,534	94	-	94	61,628
Total assets	908,484	195,905	1,104,389	407,636	1,025,793	1,433,429	2,537,818
Due to banks and other money market deposits	104,572	9,625	114,197	96,250	-	96,250	210,447
Customers' deposits	409,083	597,154	1,006,237	540,303	340,214	880,517	1,886,754
Other liabilities	58,091	7,194	65,285	3,493	-	3,493	68,778
Taxation	5,687	-	5,687	-	-	-	5,687
Subordinated debt	-	-	-	54,700	7,000	61,700	61,700
Shareholders' equity	-	-	-	-	304,452	304,452	304,452
Total liabilities and shareholders' equity	577,433	613,973	1,191,406	694,746	651,666	1,346,412	2,537,818

	On demand within 3 months USD'000	3 to 12 months USD'000	Subtotal less than 12 months USD'000	1 to 5 years USD'000	Over 5 years USD'000	Subtotal over 12 months USD'000	Total USD'000
Cash and balances with Central Banks	333,236	90,839	424,075	84,301	51,982	136,283	560,358
Due from banks and other money market placement (net)	437,693	126,621	564,314	-	-	-	564,314
Loans and advances (net)	1,198,818	286,717	1,485,535	920,387	2,559,174	3,479,561	4,965,096
Non-trading financial investments	233,728	-	233,728	53,862	-	53,862	287,590
Premises and equipment	-	-	-	-	53,242	53,242	53,242
Deferred tax asset	1,062	-	1,062	-	-	-	1,062
Other assets	155,161	4,668	159,829	244	-	244	160,073
Total assets	2,359,698	508,845	2,868,543	1,058,794	2,664,398	3,723,192	6,591,735
Due to banks and other money market deposits	271,616	25,000	296,616	250,000	-	250,000	546,616
Customers' deposits	1,062,554	1,551,049	2,613,603	1,403,384	883,673	2,287,057	4,900,660
Other liabilities	150,885	18,686	169,571	9,073	-	9,073	178,644
Taxation	14,771	-	14,771	-	-	-	14,771
Subordinated debt	-	-	-	142,078	18,182	160,260	160,260
Shareholders' equity	-	-	-	-	790,784	790,784	790,784
Total liabilities and shareholders' equity	1,499,826	1,594,735	3,094,561	1,804,535	1,692,639	3,497,174	6,591,735

29 RISK MANAGEMENT (continued)

LIQUIDITY RISK (continued)

The maturity profile of the assets, liabilities and equity at 31 December 2011 is as follows:

	On demand within 3 months RO'000	3 to 12 months RO'000	Subtotal less than 12 months RO'000	1 to 5 years RO'000	Over 5 years RO'000	Subtotal over 12 months RO'000	Total RO'000
Cash and balances with Central Banks	147,601	27,989	175,590	29,467	15,714	45,181	220,771
Due from banks and other money market placements (net)	145,746	3,248	148,994	11,550	-	11,550	160,544
Loans and advances (net)	346,923	182,198	529,121	339,762	801,895	1,141,657	1,670,778
Non-trading financial investments	78,256	-	78,256	16,766	-	16,766	95,022
Premises and equipment	-	-	-	-	20,505	20,505	20,505
Deferred tax asset	482	-	482	-	-	-	482
Other assets	58,955	1,811	60,766	204	-	204	60,970
Total assets	777,963	215,246	993,209	397,749	838,114	1,235,863	2,229,072
Due to banks and other money market deposits	91,094	132,055	223,149	-	-	-	223,149
Customers' deposits	371,258	454,444	825,702	509,060	265,062	774,122	1,599,824
Other liabilities	56,210	6,832	63,042	1,890	-	1,890	64,932
Taxation	5,240	-	5,240	-	-	-	5,240
Subordinated debt	-	-	-	30,600	24,100	54,700	54,700
Shareholders' equity	-	-	-	-	281,227	281,227	281,227
Total liabilities and shareholders' equity	523,802	593,331	1,117,133	541,550	570,389	1,111,939	2,229,072

	On demand within 3 months USD'000	3 to 12 months USD'000	Subtotal less than 12 months USD'000	1 to 5 years USD'000	Over 5 years USD'000	Subtotal over 12 months USD'000	Total USD'000
Cash and balances with Central Banks	383,378	72,699	456,077	76,538	40,816	117,354	573,431
Due from banks and other money market placement (net)	378,561	8,436	386,997	30,000	-	30,000	416,997
Loans and advances (net)	901,098	473,242	1,374,340	882,499	2,082,844	2,965,343	4,339,683
Non-trading financial investments	203,262	-	203,262	43,548	-	43,548	246,810
Premises and equipment	-	-	-	-	53,260	53,260	53,260
Deferred tax asset	1,252	-	1,252	-	-	-	1,252
Other assets	153,131	4,704	157,835	530	-	530	158,365
Total assets	2,020,682	559,081	2,579,763	1,033,115	2,176,920	3,210,035	5,789,798
Due to banks and other money market deposits	236,608	343,000	579,608	-	-	-	579,608
Customers' deposits	964,306	1,180,374	2,144,680	1,322,234	688,473	2,010,707	4,155,387
Other liabilities	146,000	17,746	163,746	4,909	-	4,909	168,655
Taxation	13,610	-	13,610	-	-	-	13,610
Subordinated debt	-	-	-	79,481	62,597	142,078	142,078
Shareholders' equity	-	-	-	-	730,460	730,460	730,460
Total liabilities and shareholders' equity	1,360,524	1,541,120	2,901,644	1,406,624	1,481,530	2,888,154	5,789,798

29 RISK MANAGEMENT (continued)

MARKET RISK

The bank is exposed to market risk, which is the risk that the fair value of the financial assets held by the bank will fluctuate because of changes in market prices. Market risk arises from changes in the fair value of open positions held in foreign exchange, interest rate, currency, equity, credit spreads, etc. Market Risk is managed based on the Central Bank of Oman guidelines and the Market Risk Policy, which is approved and periodically reviewed by the Board Risk Committee. Stress tests incorporating adverse movements in equity value, foreign exchange, etc. are also periodically conducted and reviewed by the Management and Board Risk Committee.

The bank offers hedging products to its customers to hedge their genuine exposures, related to interest rate risk, foreign exchange risk and commodity risk. The counterparty credit risk exposures for such transactions (interest rate swaps, commodities contracts, currency forwards and options, etc.) are assessed based on the positive marked-to-market values of the contracts and the potential future exposures. The bank has adopted risk weightings in line with best practices being followed by other banks to capture the credit risk related to these off-balance exposures.

Equity risk

The proprietary equity positions are held in the 'Available for Sale' category. The market risk is monitored though daily mark-to-market reports which are circulated to the management and required actions, if any, are promptly taken. The portfolio is also monitored and managed as per the Investment Policy approved by the Board Risk Committee.

Interest rate risk

The principal market risk to which non-trading portfolio is exposed is the risk of loss from fluctuation in the future cash flows or fair values of financial instruments because of changes in market interest rates.

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 re-pricing of assets and liabilities.

Methods and assumptions used in preparing the sensitivity analysis: The methods for interest rate sensitivity analysis are Maturity Gap Analysis (which measures the interest rate sensitivity of earnings) and Duration (which measures the interest rate sensitivity of capital). These are in line with the BIS in its paper on 'Principles for the Management and Supervision of Interest Rate Risk' issued in July 2004.

Interest rate risk is managed by monitoring the sensitivity of the bank's financial assets and liabilities to various standardized interest rate shocks. Standardised shocks include a 100 basis point and 200 basis point parallel shifts in yield curves. The impact of these shocks is analysed in the context of its impact on Earnings and Economic Value. The impact is compared against internal limits which have been formulated in line with the Central Bank of Oman and Basel Committees guidelines. The analysis is regularly reviewed by the Management and Board Risk Committee.

Earning impact of 200 basis points parallel shift in interest rate is provided below:

As at December 2012	200 bps increase	200 bps decrease
Earnings impact - RO'000s	9,087	(9,087)
Earnings impact - USD'000s	**23,602**	**(23,602)**

In addition, stress scenarios based on specific events or market disruptions are also analysed and presented at monthly ALCO meetings to estimate the impact on liquidity and earnings.

The bank has been consistently using the above methods/assumptions to conduct interest rate sensitivity analysis. The above sensitivity analysis is carried out at monthly rests and results thereof monitored against the in-house limits and the results are also actively deliberated at the ALCO meetings and presented to the Board Risk Committee.

29 RISK MANAGEMENT (continued)

MARKET RISK (continued)

There have not been any significant changes in Interest Rate Risk management process in the bank during the year.

The bank's interest sensitivity position based on contractual re-pricing arrangements at **31 December 2012** is as follows:

	Average effective interest rate	On demand within 3 months RO'000	3 to 12 months RO'000	1 to 5 years RO'000	Over 5 years RO'000	Non interest sensitive RO'000	Total RO'000
Cash and balances with Central Banks	0.08%	28,554	-	-	-	187,184	215,738
Due from banks and other money market placements (net)	1.53%	195,373	21,888	-	-	-	217,261
Loans and advances (net)	5.67%	822,246	296,461	361,907	393,077	37,871	1,911,562
Non-trading financial investments	3.00%	6,870	10,000	73,115	-	20,737	110,722
Premises and equipment	N/A	-	-	-	-	20,498	20,498
Deferred tax asset	N/A	-	-	-	-	409	409
Other assets	N/A	-	-	-	-	61,628	61,628
Total assets		1,053,043	328,349	435,022	393,077	328,327	2,537,818
Due to banks and other money market deposits	1.59%	210,447	-	-	-	-	210,447
Customers' deposits	1.89%	212,521	686,977	343,400	-	643,856	1,886,754
Other liabilities	N/A	-	-	-	-	68,778	68,778
Taxation	N/A	-	-	-	-	5,687	5,687
Subordinated debt	6.55%	-	-	54,700	7,000	-	61,700
Shareholders' equity	N/A	-	-	-	-	304,452	304,452
Total liabilities and shareholders' equity		422,968	686,977	398,100	7,000	1,022,773	2,537,818
Total interest rate sensitivity gap		630,075	(358,628)	36,922	386,077	(694,446)	-
Cumulative interest rate sensitivity gap		630,075	271,447	308,369	694,446	-	-

29 RISK MANAGEMENT (continued)

MARKET RISK (continued)

The bank's interest sensitivity position based on contractual re-pricing arrangements at **31 December 2012** is as follows:

	Average effective interest rate	On demand within 3 months USD'000	3 to 12 months USD'000	1 to 5 years USD'000	Over 5 years USD'000	Non interest sensitive USD'000	Total USD'000
Cash and balances with Central Banks	0.08%	74,166	-	-	-	486,192	560,358
Due from banks and other money market placements (net)	1.53%	507,462	56,852	-	-	-	564,314
Loans and advances (net)	5.67%	2,135,704	770,029	940,018	1,020,979	98,366	4,965,096
Non-trading financial investments	3.00%	17,844	25,974	189,909	-	53,863	287,590
Premises and equipment	N/A	-	-	-	-	53,242	53,242
Deferred tax asset	N/A	-	-	-	-	1,062	1,062
Other assets	N/A	-	-	-	-	160,073	160,073
Total assets		2,735,176	852,855	1,129,927	1,020,979	852,798	6,591,735
Due to banks and other money market deposits	1.59%	546,616	-	-	-	-	546,616
Customers' deposits	1.89%	552,003	1,784,356	891,948	-	1,672,353	4,900,660
Other liabilities	N/A	-	-	-	-	178,644	178,644
Taxation	N/A	-	-	-	-	14,771	14,771
Subordinated debt	6.55%	-	-	142,078	18,182	-	160,260
Shareholders' equity	N/A	-	-	-	-	790,784	790,784
Total liabilities and shareholders' equity		1,098,619	1,784,356	1,034,026	18,182	2,656,552	6,591,735
Total interest rate sensitivity gap		1,636,557	(931,501)	95,901	1,002,797	(1,803,754)	-
Cumulative interest rate sensitivity gap		1,636,557	705,056	800,957	1,803,754	-	-

29 RISK MANAGEMENT (continued)

MARKET RISK (continued)

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

	Average effective interest rate	On demand within 3 months RO'000	3 to 12 months RO'000	1 to 5 year RO'000	Over 5 year RO'000	Non interest sensitive RO'000	Total RO'000
Cash and balances with Central Banks	0.05%	95,744	-	-	-	125,027	220,771
Due from banks and other money market placements (net)	1.60%	160,184	360	-	-	-	160,544
Loans and advances (net)	5.92%	691,848	292,283	286,118	379,427	21,102	1,670,778
Non-trading financial investments	3.62%	-	-	78,257	-	16,765	95,022
Premises and equipment	N/A	-	-	-	-	20,505	20,505
Deferred tax asset	N/A	-	-	-	-	482	482
Other assets	N/A	-	-	-	-	60,970	60,970
Total assets		947,776	292,643	364,375	379,427	244,851	2,229,072
Due to banks and other money market deposits	0.75%	216,219	6,930	-	-	-	223,149
Customers' deposits	2.19%	216,000	494,645	364,273	-	524,906	1,599,824
Other liabilities	N/A	-	-	-	-	64,932	64,932
Taxation	N/A	-	-	-	-	5,240	5,240
Subordinated debt	7.26%	-	-	30,600	24,100	-	54,700
Shareholders' equity	N/A	-	-	-	-	281,227	281,227
Total liabilities and shareholders' equity		432,219	501,575	394,873	24,100	876,305	2,229,072
Total interest rate sensitivity gap		515,557	(208,932)	(30,498)	355,327	(631,454)	-
Cumulative interest rate sensitivity gap		515,557	306,625	276,127	631,454	-	-

29 RISK MANAGEMENT (continued)

MARKET RISK (continued)

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

	Average effective interest rate	On demand within 3 months USD'000	3 to 12 months USD'000	1 to 5 year USD'000	Over 5 year USD'000	Non interest sensitive USD'000	Total USD'000
Cash and balances with Central Banks	0.05%	248,686	-	-	-	324,745	573,431
Due from banks and other money market placements (net)	1.60%	416,062	935	-	-	-	416,997
Loans and advances (net)	5.92%	1,797,007	759,177	743,164	985,525	54,810	4,339,683
Non-trading financial investments	3.62%	-	-	203,264	-	43,546	246,810
Premises and equipment	N/A	-	-	-	-	53,260	53,260
Deferred tax asset	N/A	-	-	-	-	1,252	1,252
Other assets	N/A	-	-	-	-	158,365	158,365
Total assets		2,461,755	760,112	946,428	985,525	635,978	5,789,798
Due to banks and other money market deposits	0.75%	561,608	18,000	-	-	-	579,608
Customers' deposits	2.19%	561,039	1,284,792	946,164	-	1,363,392	4,155,387
Other liabilities	N/A	-	-	-	-	168,655	168,655
Taxation	N/A	-	-	-	-	13,610	13,610
Subordinated debt	7.26%	-	-	79,481	62,597	-	142,078
Shareholders' equity	N/A	-	-	-	-	730,460	730,460
Total liabilities and shareholders' equity		1,122,647	1,302,792	1,025,645	62,597	2,276,117	5,789,798
Total interest rate sensitivity gap		1,339,108	(542,680)	(79,217)	922,928	(1,640,139)	-
Cumulative interest rate sensitivity gap		1,339,108	796,428	717,211	1,640,139	-	-

Currency risk

Currency risk is the risk that the value of a financial instrument will fluctuate due to changes in foreign exchange rates. The bank has set limits on open positions by currency. Positions are monitored on a daily basis and hedging strategies used to ensure positions are maintained within established limits.

The foreign exchange positions in the books of the bank are largely held on account of customers and any variations in the exchange rates are absorbed by the customers.

Foreign exchange VAR is computed monthly for all non-pegged currencies at 99% confidence level and a holding period of 10 days. Additionally earnings impact of a 15% adverse movement in exchange rates for all open positions is factored in the monthly stress tests.

The bank had the following significant net exposures denominated in foreign currencies:

2011 USD'000	**2012 USD'000**		**2012 RO'000**	2011 RO'000
52,260	**6,971**	US Dollar	**2,684**	20,120
22,556	**2,574**	UAE Dirham	**991**	8,684
984	**13,392**	Others	**5,156**	379

29 RISK MANAGEMENT (continued)

OPERATIONAL RISK

Operational risk is the risk of loss arising from systems failure, human error, fraud or external events. When controls fail to perform, operational risks can cause damage to reputation, have legal or regulatory implications, or lead to financial loss. The bank cannot expect to eliminate all operational risks, but through a control framework and by monitoring and responding to potential risks, the bank is able to manage the risks. Controls include effective segregation of duties, access, authorization and reconciliation procedures, staff training and assessment processes, including the use of internal audit. Further, the Bank now has established an operational loss appetite statement to monitor losses under various operational loss categories and any breaches of set off thresholds will be reported to the Board Risk Committee. In addition to this, the bank has an operational loss reporting database.

STRATEGIC RISKS

The Bank monitors strategic risks through regular reporting at the Board Risk Committee. This also includes reviews of Human Resource related risks and the monitoring of strategic project risks.

30 CONCENTRATIONS

The bank seeks to manage its credit risk exposure through diversification of lending activities to avoid undue concentrations of risk with individuals or groups of customers in specific locations or businesses. It also obtains security when appropriate.

The distribution of assets, liabilities and contingent items by geographical regions as of **31 December 2012** is as follows:

	Sultanate of Oman RO'000	UAE RO'000	Egypt RO'000	Others RO'000	Total RO'000
Cash and balances with Central Banks	201,919	7,737	6,082	-	215,738
Due from banks and other money market placements (net)	-	10,359	2,560	204,342	217,261
Loans and advances (net)	1,851,790	44,612	-	15,160	1,911,562
Non-trading financial investments	106,107	-	3,593	1,022	110,722
Premises and equipment	19,809	286	403	-	20,498
Deferred tax asset	409	-	-	-	409
Other assets	53,644	1,340	810	5,834	61,628
Total assets	2,233,678	64,334	13,448	226,358	2,537,818
Due to banks and other money market deposits	5,840	36,706	4,620	163,281	210,447
Customers' deposits	1,790,936	43,692	18,852	33,274	1,886,754
Other liabilities	60,781	1,795	368	5,834	68,778
Taxation	5,152	98	437	-	5,687
Subordinated debt	61,700	-	-	-	61,700
Shareholders' equity	299,215	4,818	419	-	304,452
Liabilities and shareholders' equity	2,223,624	87,109	24,696	202,389	2,537,818
Contingent liabilities	313,260	36,427	574	166,362	516,623

30 CONCENTRATIONS (continued)

	Sultanate of Oman USD'000	UAE USD'000	Egypt USD'000	Others USD'000	Total USD'000
Cash and balances with Central Banks	**524,465**	**20,096**	**15,797**	**-**	**560,358**
Due from banks and other money market placements (net)	**-**	**26,906**	**6,649**	**530,759**	**564,314**
Loans and advances (net)	**4,809,844**	**115,875**	**-**	**39,377**	**4,965,096**
Non-trading financial investments	**275,603**	**-**	**9,332**	**2,655**	**287,590**
Premises and equipment	**51,452**	**743**	**1,047**	**-**	**53,242**
Deferred tax asset	**1,062**	**-**	**-**	**-**	**1,062**
Other assets	**139,335**	**3,481**	**2,104**	**15,153**	**160,073**
Total assets	**5,801,761**	**167,101**	**34,929**	**587,944**	**6,591,735**
Due to banks and other money market deposits	**15,169**	**95,340**	**12,000**	**424,107**	**546,616**
Customers' deposits	**4,651,782**	**113,486**	**48,966**	**86,426**	**4,900,660**
Other liabilities	**157,873**	**4,662**	**956**	**15,153**	**178,644**
Taxation	**13,381**	**255**	**1,135**	**-**	**14,771**
Subordinated debt	**160,260**	**-**	**-**	**-**	**160,260**
Shareholders' equity	**777,182**	**12,514**	**1,088**	**-**	**790,784**
Liabilities and shareholders' equity	**5,775,647**	**226,257**	**64,145**	**525,686**	**6,591,735**
Contingent liabilities	**813,662**	**94,616**	**1,491**	**432,109**	**1,341,878**

The distribution of assets, liabilities and off balance sheet items by geographical regions as of 31 December 2011 is as follows:

	Sultanate of Oman RO'000	UAE RO'000	Egypt RO'000	Others RO'000	Total RO'000
Cash and balances with Central Banks	206,084	5,580	9,107	-	220,771
Due from banks and other money market placements (net)	-	25,283	271	134,990	160,544
Loans and advances (net)	1,599,279	49,306	171	22,022	1,670,778
Non-trading financial investments	90,294	-	3,649	1,079	95,022
Premises and equipment	19,744	126	635	-	20,505
Deferred tax asset	482	-	-	-	482
Other assets	52,372	746	693	7,159	60,970
Total assets	1,968,255	81,041	14,526	165,250	2,229,072
Due to banks and other money market deposits	8,508	31,639	-	183,002	223,149
Customers' deposits	1,501,611	32,130	26,725	39,358	1,599,824
Other liabilities	56,001	1,131	641	7,159	64,932
Taxation	4,349	242	649	-	5,240
Subordinated debt	54,700	-	-	-	54,700
Shareholders' equity	261,046	4,383	15,798	-	281,227
Liabilities and shareholders' equity	1,886,215	69,525	43,813	229,519	2,229,072
Contingent liabilities	293,037	35,625	824	178,328	507,814

30 CONCENTRATIONS (continued)

The distribution of assets, liabilities and off balance sheet items by geographical regions as of 31 December 2011 is as follows:

	Sultanate of Oman USD'000	UAE USD'000	Egypt USD'000	Others USD'000	Total USD'000
Cash and balances with Central Banks	535,282	14,494	23,655	-	573,431
Due from banks and other money market placements (net)	-	65,670	704	350,623	416,997
Loans and advances (net)	4,153,971	128,068	444	57,200	4,339,683
Non-trading financial investments	234,529	-	9,478	2,803	246,810
Premises and equipment	51,284	327	1,649	-	53,260
Deferred tax asset	1,252	-	-	-	1,252
Other assets	136,032	1,938	1,800	18,595	158,365
Total assets	5,112,350	210,497	37,730	429,221	5,789,798
Due to banks and other money market deposits	22,099	82,179	-	475,330	579,608
Customers' deposits	3,900,287	83,455	69,416	102,229	4,155,387
Other liabilities	145,457	2,938	1,665	18,595	168,655
Taxation	11,295	629	1,686	-	13,610
Subordinated debt	142,078	-	-	-	142,078
Shareholders' equity	678,042	11,384	41,034	-	730,460
Liabilities and shareholders' equity	4,899,258	180,585	113,801	596,154	5,789,798
Contingent liabilities	761,136	92,532	2,140	463,190	1,318,998

31 SEGMENTAL INFORMATION

For management purposes, the bank is organised into four operating segments based on business units and are as follows:

- Retail banking offers various products and facilities to individual customers to meet everyday banking needs.
- Corporate banking delivers a variety of products and services to corporate customers that include lending, accepting deposits, trade finance and foreign exchange.
- Investment banking offers investment products such as asset management, corporate advisory and brokerage services to retail customers as well as high net worth individuals and institutional clients.
- Treasury provides a full range of treasury products and services including money market and foreign exchange to the clients in addition to managing liquidity.
- International banking offers services such as issuance of guarantee, risk participation, syndications, etc.

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

Segment information is as follows:

Year ended 31 December 2012	Retail banking RO'000	Corporate banking RO'000	Investment banking RO'000	Treasury and international banking RO'000	Head office RO'000	Total RO'000
Net interest income	37,462	25,216	(338)	962	3,877	67,179
Other income	18,615	5,229	2,096	3,612	1,914	31,466
Operating profit	35,166	27,663	1,001	4,270	(16,140)	51,960
Impairment provisions (net)	(2,475)	(2,930)	(1,471)	-	1,596	(5,280)
Profit	32,691	24,733	(470)	4,270	(20,562)	40,662
Total assets	936,151	993,947	20,959	106,146	480,615	2,537,818
Total liabilities and equity	692,836	1,152,235	34,193	5,834	652,720	2,537,818

Year ended 31 December 2012	Retail banking USD'000	Corporate banking USD'000	Investment banking USD'000	Treasury and international banking USD'000	Head office USD'000	Total USD'000
Net interest income	97,304	65,496	(878)	2,499	10,070	174,491
Other income	48,350	13,582	5,444	9,382	4,971	81,729
Operating profit	91,339	71,852	2,600	11,091	(41,922)	134,960
Impairment provisions (net)	(6,429)	(7,610)	(3,821)	-	4,146	(13,714)
Profit	84,912	64,242	(1,221)	11,091	(53,408)	105,616
Total assets	2,431,561	2,581,681	54,439	275,704	1,248,350	6,591,735
Total liabilities and equity	1,799,574	2,992,818	88,813	15,153	1,695,377	6,591,735

For management purposes the bank also reports the segment information of its operations by the following geographical locations:

(i) Oman,
(ii) United Arab Emirates (UAE),
(iii) Egypt

Transactions between the above segments are conducted at estimated market rates on an arm's length basis.

31 SEGMENTAL INFORMATION (continued)

Segment information by geography is as follows:

For the year ended 31 December 2012	Sultanate of Oman RO'000	UAE RO'000	Egypt RO'000	Total RO'000
Segment revenue				
Interest income - external	104,047	1,857	1,197	107,101
Interest income - internal	-	40	1,636	1,676
Other operating income - external	29,971	630	865	31,466
Other operating income- internal	191	-	-	191
Total	134,209	2,527	3,698	140,434
Segment costs				
Interest costs – external	38,402	546	974	39,922
Interest costs - internal	243	88	1,345	1,676
Other operating expenses - external	40,516	1,379	1,064	42,959
Other operating expenses – internal	-	62	129	191
Depreciation	3,515	127	84	3,726
Credit loss expense - customer loan	15,859	1,079	3	16,941
Impairment losses on available for sale investments	1,471	-	70	1,541
Recoveries	(11,282)	(1,244)	(676)	(13,202)
Taxation	5,677	54	287	6,018
Total	94,401	2,091	3,280	99,772
Segment profit for the year	39,808	436	418	40,662
Other information				
Segment assets	2,448,605	53,258	35,955	2,537,818
Segment capital expenses	3,612	289	15	3,916

31 SEGMENTAL INFORMATION (continued)

For the year ended 31 December 2012	Oman USD'000	UAE USD'000	Egypt USD'000	Total USD'000
Segment revenue				
Interest income - external	270,252	4,823	3,109	278,184
Interest income - internal	-	104	4,249	4,353
Other operating income - external	77,847	1,636	2,246	81,729
Other operating income - internal	496	-	-	496
Total	348,595	6,563	9,604	364,762
Segment costs				
Interest costs - external	99,745	1,418	2,530	103,693
Interest costs - internal	630	229	3,494	4,353
Other operating expenses - external	105,236	3,582	2,764	111,582
Other operating expenses – internal	-	161	335	496
Depreciation	9,130	330	218	9,678
Credit loss expense - customer loan	41,193	2,802	7	44,002
Impairment losses on available for sale investments	3,822	-	181	4,003
Recoveries	(29,304)	(3,231)	(1,756)	(34,291)
Taxation	14,745	140	745	15,630
Total	245,197	5,431	8,518	259,146
Segment profit for the year	103,398	1,132	1,086	105,616
Other information				
Segment assets	6,360,014	138,332	93,390	6,591,736
Segment capital expenses	9,382	751	39	10,172

Segment information is as follows:

Year ended 31 December 2011	Retail banking RO'000	Corporate banking RO'000	Investment banking RO'000	Treasury and international banking RO'000	Head office RO'000	Total RO'000
Net interest income	28,138	26,386	(536)	368	3,831	58,187
Other income	20,798	5,379	2,935	3,680	1,256	34,048
Operating profit	30,575	28,658	1,588	3,012	(15,054)	48,779
Impairment provisions (net)	(2,766)	(5,030)	(2,285)	-	-	(10,081)
Profit	27,809	23,628	(697)	3,012	(19,550)	34,202
Total assets	756,724	927,100	16,968	42,493	485,787	2,229,072
Total liabilities and equity	581,682	856,350	18,412	36,575	736,053	2,229,072

31 SEGMENTAL INFORMATION (continued)

Year ended 31 December 2011	Retail banking USD'000	Corporate banking USD'000	Investment banking USD'000	Treasury and international banking USD'000	Head office USD'000	Total USD'000
Net interest income	73,085	68,535	(1,392)	956	9,951	151,135
Other income	54,022	13,971	7,623	9,558	3,262	88,436
Operating profit	79,416	74,436	4,125	7,823	(39,102)	126,698
Impairment provisions (net)	(7,184)	(13,065)	(5,935)	-	-	(26,184)
Profit	72,232	61,371	(1,810)	7,823	(50,780)	88,836
Total assets	1,965,517	2,408,052	44,073	110,371	1,261,785	5,789,798
Total liabilities and equity	1,510,862	2,224,286	47,823	95,000	1,911,827	5,789,798

Segment information by geography is as follows:

For the year ended 31 December 2011	Oman RO'000	UAE RO'000	Egypt RO'000	Total RO'000
Segment revenue				
Interest income - external	89,207	3,040	1,109	93,356
Interest income - internal	-	12	2,121	2,133
Other operating income - external	32,763	601	684	34,048
Other operating income - internal	199	-	-	199
Total	122,169	3,653	3,914	129,736
Segment costs				
Interest costs - external	33,588	561	1,020	35,169
Interest costs - internal	422	142	1,569	2,133
Other operating expenses - external	37,010	1,369	870	39,249
Other operating expenses – internal	-	91	108	199
Depreciation	4,084	31	92	4,207
Credit loss expense - customer loan	17,243	1,542	147	18,932
Provision – others	-	-	712	712
Impairment losses on available for sale investments	2,288	-	-	2,288
Recoveries	(9,026)	(1,074)	(1,751)	(11,851)
Taxation	4,089	199	208	4,496
Total	89,698	2,861	2,975	95,534
Segment profit for the year	32,471	792	939	34,202
Other information				
Segment assets	2,134,614	59,617	34,841	2,229,072
Segment capital expenses	2,451	92	9	2,552

31 SEGMENTAL INFORMATION (continued)

For the year ended 31 December 2011	Oman USD'000	UAE USD'000	Egypt USD'000	Total USD'000
Segment revenue				
Interest income - external	231,706	7,896	2,881	242,483
Interest income - internal	-	31	5,509	5,540
Operating income - external	85,098	1,561	1,777	88,436
Operating income - internal	517	-	-	517
Total	317,321	9,488	10,167	336,976
Segment costs				
Interest costs - external	87,242	1,457	2,649	91,348
Interest costs - internal	1,096	369	4,075	5,540
Operating expenses - external	96,130	3,556	2,260	101,946
Operating expenses – internal	-	236	281	517
Depreciation	10,607	81	239	10,927
Credit loss expense - customer loan	44,787	4,005	382	49,174
Provision – others	-	-	1,849	1,849
Impairment losses on available for sale investments	5,943	-	-	5,943
Recoveries	(23,444)	(2,790)	(4,548)	(30,782)
Taxation	10,621	517	540	11,678
Total	232,982	7,431	7,727	248,140
Segment profit for the year	84,339	2,057	2,440	88,836
Other information				
Segment assets	5,544,453	154,849	90,496	5,789,798
Segment capital expenses	6,366	239	23	6,628

32 FAIR VALUE OF FINANCIAL INSTRUMENTS

It is the bank's intention to hold loans and advances granted to customers to maturity. As a result the fair value of performing loans is arrived at using the discounted cash flow analysis based on a discount rate equal to the prevailing market rates of interest for loans having similar terms and conditions. The bank considers that the fair value of financial instruments at 31 December 2012 and 2011 are not significantly different to their carrying value at each of those dates.

Fair value of financial instruments

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

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

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

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

32 FAIR VALUE OF FINANCIAL INSTRUMENTS (continued)

The following table shows an analysis of financial instruments recorded at fair value by level of the fair value hierarchy:

31 December 2012	Level 1 RO'000	Level 2 RO'000	Level 3 RO'000	Total RO'000
Financial assets				
Investments - available for sale:				
Government development bonds	89,763	-	-	89,763
Quoted equities	10,268	-	-	10,268
Other unquoted equities	-	10,691	-	10,691
Total	100,031	10,691	-	110,722
Derivative financial instruments:				
Purchase contracts	-	66,657	-	66,657
Sale contracts	-	66,657	-	66,657
Interest rate swaps	-	138,276	-	138,276
Currency options	-	45,483	-	45,483
Commodity hedging	-	51,161	-	51,161
Total	-	368,234	-	368,234
Total financial assets	100,031	378,925	-	478,956
Total financial assets – In USD'000s	259,821	984,221	-	1,244,042

31 December 2011	Level 1 RO'000	Level 2 RO'000	Level 3 RO'000	Total RO'000
Financial assets				
Investments - available for sale:				
Government development bonds	78,054	-	-	78,054
Quoted equities	9,923	-	-	9,923
Other unquoted equities	-	7,045	-	7,045
Total	87,977	7,045	-	95,022
Derivative financial instruments:				
Purchase contracts	-	79,169	-	79,169
Sale contracts	-	79,169	-	79,169
Interest rate swaps	-	152,076	-	152,076
Interest rate caps	-	142	-	142
Credit default swaps	-	5,775	-	5,775
Currency options	-	31,076	-	31,076
Commodity hedging	-	16,793	-	16,793
Total	-	364,200	-	364,200
Total financial assets	87,977	371,245	-	459,222
Total financial assets – In USD'000s	228,511	964,273	-	1,192,784

32 FAIR VALUE OF FINANCIAL INSTRUMENTS (continued)

During the reporting period ended 31 December 2012 and 31 December 2011, there were no transfers between Level 1 and Level 2 fair value measurements, and no transfers into and out of Level 3 fair value measurements.

33 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. The bank uses the following derivative financial instruments:

Derivative product types

Forwards are contractual agreements to either buy or sell a specified currency, commodity or financial instrument at a specific price and date in the future. Forwards are customised contracts transacted in the over-the-counter market.

Swaps are contractual agreements between two parties to exchange movements in interest or foreign currency rates and equity indices, and (in the case of credit default swaps) to make payments with respect to defined credit events based on specified notional amounts.

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. The bank transacts only in currency options for its customers.

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. Hedging specific financial instruments and forecasted transactions as well as strategic hedging against overall balance sheet exposures achieve this.

The bank uses forward foreign exchange contracts, options and currency swaps to hedge against specifically identified currency risks. In addition, the bank uses interest rate swaps to hedge against the cash flow risks arising from certain fixed interest rate loans and deposits.

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 positive and negative fair values of derivative financial instruments, which are equivalent to the market values, together with the notional amounts analysed by the term to maturity. The notional amount is 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.

				Notional amounts by term to maturity		
31 December 2012	**Positive fair value RO'000 (note 9)**	**Negative fair value RO'000 (note 12)**	**Notional amount RO'000**	**Within 3 months RO'000**	**3 - 12 months RO'000**	**1 - 5 years RO'000**
Interest rate swaps	9,753	(9,753)	138,276	4,762	6,901	126,613
Forward foreign exchange purchase contracts	64	(361)	66,657	48,716	17,941	-
Forward foreign exchange sales contracts	370	(170)	66,657	48,649	18,008	-
Currency options	325	(325)	45,483	33,253	12,230	-
Commodity hedging	558	(558)	51,161	30,980	20,181	-
Total	**11,070**	**(11,167)**	**368,234**	**166,360**	**75,261**	**126,613**
Total – USD'000	**28,753**	**(29,005)**	**956,452**	**432,104**	**195,483**	**328,865**

31 December 2011	Positive fair value RO'000 (note 9)	Negative fair value RO'000 (note 12)	Notional amount RO'000	Notional amounts by term to maturity		
				Within 3 months RO'000	3 - 12 months RO'000	1 - 5 years RO'000
Interest rate swaps	9,453	(9,453)	152,076	6,037	8,166	137,873
Credit default swaps	-	(26)	5,775	5,775	-	-
Forward foreign exchange purchase contracts	41	(341)	79,169	72,396	6,773	-
Forward foreign exchange sales contracts	348	(36)	79,169	72,401	6,768	-
Interest rate caps	-	-	142	80	62	-
Currency options	320	(320)	31,076	15,660	15,416	-
Commodity hedging	880	(880)	16,793	16,495	298	-
Total	11,042	(11,056)	364,200	188,844	37,483	137,873
Total – USD'000	28,681	(28,717)	945,974	490,504	97,358	358,112

34 COMPARATIVE AMOUNTS

Certain of the corresponding figures for 2011 have been reclassified in order to conform with the presentation for the current year. Such reclassifications were made within the same notes to the financial statements and do not affect previously reported profit or equity.

These reclassifications have been done as a result of adoption of new standards and interpretations and to improve the quality of information presented. The reclassifications do not affect the reported profit for the year 2011.

National Bank of Oman Branches

66 Branches in Oman

1 Branch in Egypt

1 Branch in UAE (Abu Dhabi)

7 Sadara Wealth Management Centers

Muscat Region (South)

Main Branch C.B.D. Area
Tel: 24 778 350, 24 778 352

GETCO Building CBD
Tel: 24 778 060, 24 778 055,
24 778 056, 24 778 059

Muscat
Tel : 24 737 837, 24 740 595

Hamriya
Tel: 24 835 221, 24 835 223,
24 833 792, 24 831 520

Bait Al Falaj
Tel: 24 700 166, 24 702 130

Corniche
Tel: 24 715 103, 24 714 245

Mina Al-Fahal
Tel: 24 677 020, 24 565 561

Wattaya
Tel : 24 563 830, 24 560 585

Qurum
Tel : 24 562 615, 24 560 050

Shatti Al Qurum
Tel : 24 607 161

Al Amerat
Tel: 24 875 766, 24 877 379

Muscat Region (North)

Muscat International Airport
Tel: 24 510 007, 24 510 543, 24 521 448

Bowsher
Tel: 24 587 291, 24 587 294 ,24587293

Corporate Branch Booth
Tel: 24 510 049 , 24 510 137,

Seeb Town
Tel: 24 423 511, 24 423 512, 24420441, 24 421 773

Al Khuwair
Tel: 24 486 481, 24 486 441,24486479

Azaiba R/A
Tel: 24 591 341, 24 597 855, 24590145

Azaiba North
Tel: 24 527 262, 24 527 272

Ma'abella
Tel: 24 453 314, 24 455 957

Mawaleh
Tel: 24 511 164, 24 511 165, 24511167

Ghoubrah R/A
Tel: 24 491 062, 24 497 229

Al Khuwair North
Ministry of Health Building
Tel: 24 602 763, 24 692 310 , 24 692 309

Quriyat
Tel: 24 846 100, 24 846 415

Al Khoudh
Tel: 24 537 950, 24 537 951

Musandam Region

Khasab
Tel: 26 730 467, 26 731 442

Bukha
Tel: 26 828 014

Dakhiliyah & Dhahira Region

Nizwa
Tel: 25 410 072, 25 410 043, 25 413 169

Nizwa Firq
Tel: 25 431 140, 25 432 149

Ibri
Tel: 25 691 161, 25 690 782

Al Araqi
Tel: 25 694 342, 25 694 141

Bahla
Tel: 25 419 673, 25 420 772

Sumail
Tel: 25 351 483, 25 350 355

Fanja
Tel: 25 360 444, 25 361 190

Al Hamra
Tel: 25 422 008, 25 423 121

Dhank
Tel: 25 676 603

Buraimi Region

Buraimi
Tel: 25 653 037, 25 655 226

Batinah Region

Saham
Tel: 26 855 146, 26 855 299, 26857979

Al Khaboura
Tel: 268 05 155, 26802970,
26802232, 26802380

Batinah Region (continued)

Bidaya
Tel: 26 709 240, 26 709 340

Shinas
Tel: 26 747 663, 26 748 394

Liwa
Tel: 26 762 073, 26 762 075, 26762073

Sohar Hambar
Tel: 26 859 104, 26 859 106

Sohar Industrial Branch
Tel: 26 751 925, 26 751 309

Suwaiq
Tel: 26 860 518, 26 862 764

Barka
Tel: 26 882 368, 26 882 007

Musn'a
Tel: 26 868 145, 268 68 136

Mullada
Tel: 26 871 118, 26 870 182

Rustaq
Tel: 26 878 332, 26 878 334

Rustaq New
Tel: 26 875 241, 26 875 254

Afi
Tel: 26 780 972

Dhofar Region

Salalah Main Branch
Tel: 23 291 604, 23 290 170, 23 290 710

Salalah 23rd July Street Branch
Tel: 23 298 019, 23 298 027

Hafa
Tel: 23 291 952, 23 291 940

Sultan Qaboos Hospital
Tel: 23 211 042, 23 211 092

Salalah Port
Tel: 23 219 024, 23 219 373

Mirbat
Tel: 23 268 346, 23 268 345

Sadah
Tel: 23 226 031, 23 225 283

Sharqiyah Region (South)

Sur
Tel: 25 540 246, 25 545 158

Bilad Bani Bu Ali
Tel: 25 5 54 015, 25 5 54 138

Ja'alan
Tel: 25 550 950, 25 550 110

Masira
Tel: 25 504 026, 25 504 516

Al Kamil
Tel: 25 557 524, 25 557 770

Sharqiyah Region (North)

Ibra
Tel: 25 570 015, 2 5570 144

Al Mudaibi
Tel: 25 578 014, 25 578 484

Sinaw
Tel: 25 524 212, 25 524 223

Duqum
Tel: 25 427 101,25 427 130, 25 427 172

Sadara Wealth Management Centers

CBD Center
Tel: 24 778 009, Fax: 24 778 500

Al Khuwair
Tel: 24 487 356, Fax: 24 487 355

Shatti Center
Tel: 24 607 679, Fax: 24 693 620

MAF Center
Tel: 24 567 223, Fax: 24 567 033

Sohar Center
Tel: 26 859 103, Fax: 26 859 110

Salalah Center
Tel: 23 298 092, Fax: 23 297 135

Sur Center
Tel: 25 545 414, Fax: 25 542 046

Overseas Branches

Egypt
Country Head Office
Tel: +(202) 229 00413

United Arab Emirates

Abu Dhabi
Tel: (+9712) 634 8111, 639 3028

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P.O. Box 751,
Ruwi, Muscat
Sultanate of Oman

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