Annual Report

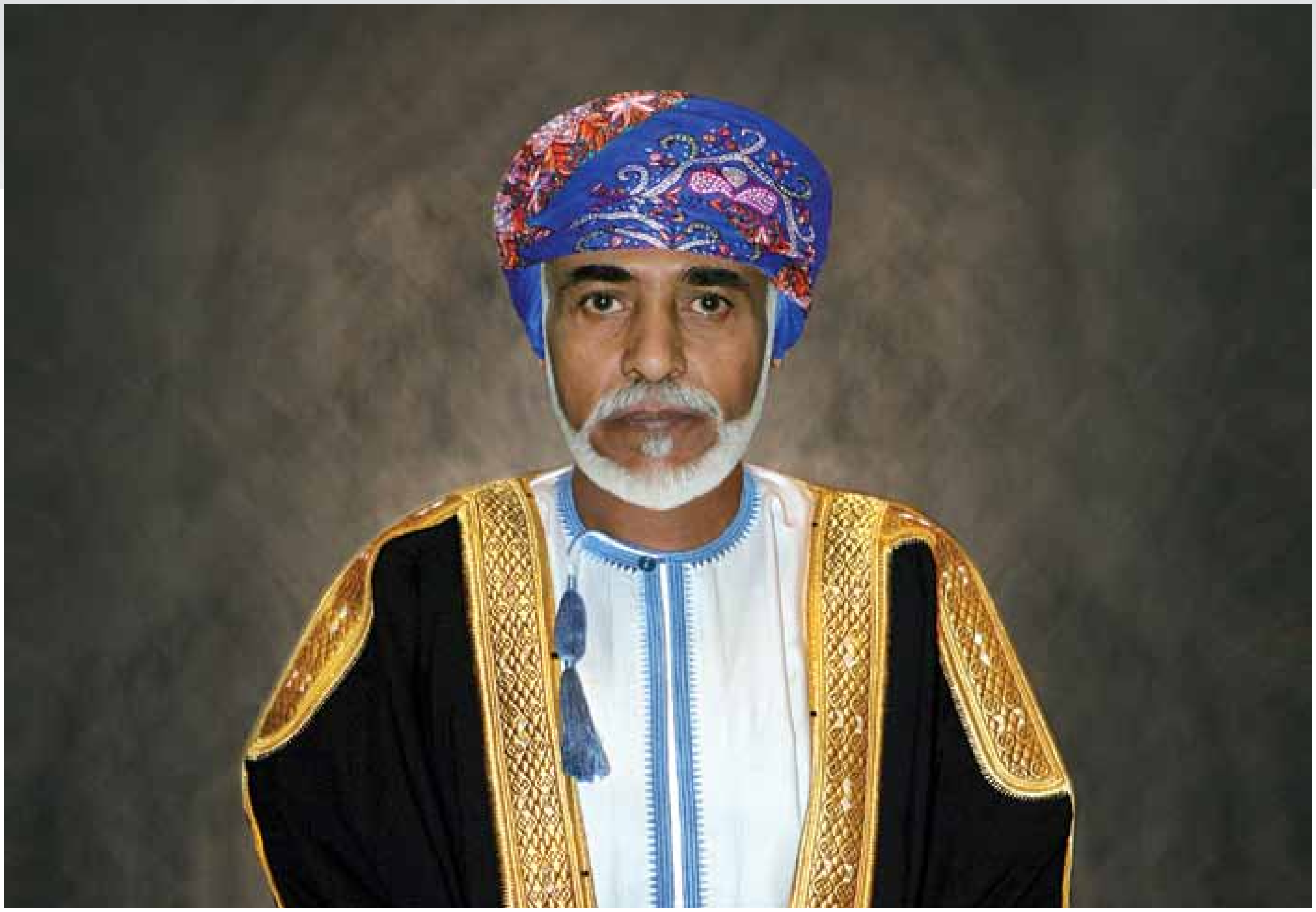
2011

البنك الوطني العماني
National Bank of Oman

For You. For Our Nation.

“We have always affirmed our continued attention to the development of human resources and we said that these resources take top priority in our plans and programmes as the human being is the cornerstone of every development structure and a pivotal component around which all types of development revolve as their ultimate goal is the happiness of the individual, providing him with a means of a decent living and guaranteeing his security and safety. As youth are the present and future of the nation we gave them the attention and care they deserve throughout the years of the blessed Renaissance as the government endeavoured to provide them with education, training, qualifications and employment opportunities.”

Excerpts from the Speech of **His Majesty Sultan Qaboos bin Said**
at The Opening of the 5th Term of The Council of Oman 3lst October 2011



His Majesty Sultan Qaboos Bin Said

Table of Contents

Chairman's Report	1
Board of Directors	5
Executive Management	9
Corporate Governance Report	12
Basel II Report	28
Management Discussion and Analysis Report	48
Financials	61
NBO Branches	116

To Our Esteemed Shareholders

It gives me great pleasure to share with you the results of the Bank for the year ended 31 December 2011. The core business lines of the Bank reported a good performance for the year despite the regional and global concerns.

Oman Economy

Oman experienced an estimated real GDP growth of 6% in 2011 and despite a 17% increase in government expenditure, the overall fiscal surplus is expected to reach 8.2% of GDP due, mainly, to a rapid growth in oil revenues. With a majority of Oman's oil exports being made to Asia, the Oman economy has been largely unaffected by the recent turmoil in global financial markets and the Eurozone sovereign debt crisis.

Expenditure in the Eighth Five Year Plan has increased by 26% due, primarily, to financial decisions taken by the Government in response to certain social requirements. Large public investment programs, which are likely to be implemented during 2012, are expected to help sustain growth over the medium term. In the long term, Oman's economic outlook will depend on successful economic diversification.

Financial Performance

The Bank's net profit after tax increased by 26% to RO 34.2 million for the twelve months ended 31 December 2011 compared with RO 27.2 million for 2010.

In 2011 net interest income grew to RO 58.2 million, an increase of 5% over the previous year with the cost of funds improving to 2.13% for the year ended 31 December 2011 compared with 2.64%. Net spreads were 3.18% in 2011.

Other income was a strong driver of revenue growth in 2011, with significant improvement in the ratio of non-interest income to total income, at 37%, up from 29% in 2010.

Operating expenses increased by 9% to RO 43 million for the year ended 31 December 2011 as the Bank continued to invest in its employees, systems and delivery channel network. The cost to income ratio improved from 51% to 47% on a year on year basis due to higher levels of income.

Net provisions for credit losses and investments for the year were higher than the previous year by RO 2.1 million predominantly due to an increase in impairment of the investments classified under the available for sale category. Recoveries and release from provisions on credit losses and loans written off increased by RO 3.6 million during the year, a 43% improvement

The Bank believes in giving back to the society from which it derives its revenues and in 2011, National Bank of Oman's community investment was RO 200,000.

over the previous year. The Bank continues to reduce non-performing loans, with the non-performing loan ratio standing at 2.9% at the end of December 2011 as compared to 3.5% in 2010.

During the twelve months ended 31 December 2011, customer lending increased by 23% to RO 1.7 billion. Customer deposits grew by 21% over the previous year to RO 1.6 billion.

The Board has recommended a cash dividend of RO 0.0175 per share as well as a stock dividend of RO 0.0025 per share, based on the dividend policy approved by the Board of Directors.

Capital

In the last quarter of 2011, the Bank raised subordinated debt of RO 24.1 million through a private placement to further strengthen its tier II capital. The Bank's regulatory capital now stands at RO 322 million. The Capital Adequacy Ratio was 15.3%, as at 31 December 2011, well above the Central Bank's minimum requirement of 12%.

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's commitment to effective Corporate Governance was recognized by the Capital Market Authority through the award of First Runner Up, under the banking category.

During the Annual General Meeting, the Board of Directors will propose, for Shareholders' approval, the appointment of new Statutory Auditors for 2012 in accordance with statutory requirements.

Corporate Social Responsibility (CSR)

CSR is the way the Bank integrates social, environmental and economic concerns into its values, culture, decision making, strategy and operations, in a transparent and responsible manner.

At the request of Regulators, Business Partners, Civil Society and Donors, the responsibility of managing the impact of our social, economic and environmental activities, in a way that continues to benefit our business, has been gradually integrated into the Bank's practices.

The Bank believes in giving back to the society from which it derives its revenues and in 2011, National Bank of Oman's community investment was RO 200,000. In addition to financial contributions, the Bank's employee involvement programs encourage staff to give their time, energy and expertise to benefit local communities.

Additionally, the Bank will publish a Sustainability Report for 2011 – the first for a local Bank in the Sultanate.

The Year Ahead

The Bank looks at 2012 with optimism as continued government spending is expected to maintain the growth momentum.

The Wholesale and Investment Banking franchise will continue to support domestic project financing and related activity, whilst the provision of Mortgages, the cards business and low cost deposit activities will remain the key focus for Retail Banking.

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

It is our plan to offer Islamic Banking in 2012 as part of our franchise following the recent approval by the Central Bank of Oman for introducing Islamic Banking in Oman.

Appreciation

The members of the Board of Directors join me in acknowledging and thanking our valued customers, correspondent banks and shareholders for their continued confidence 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

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 and Member of the Risk Committee of the Board.

He is Director of The Board of Investcorp Bank, NYC, USA and The International Advisory Board of The Brookings Institute, Washington DC, USA. A retired Air Vice Marshal by profession, Mr Mohammed Mahfoodh Al Ardhi joined the Royal Air Force (RAFO) of Oman 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 U.K 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 23 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 the GCC.

Sayyidah Rawan holds a M.Sc in Economics & Finance from Loughborough University U.K. She also holds a Post Graduate Diploma in Investment Analysisfrom Stirling University, U.K. 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.

Director of Oman Dental College (S.A.O.G.), Al Suwadi Power Co. S.A.O.C., Bahwan Veolia Water L.L.C. and Sharqiyah Desalination Co. S.A.O.C. Chief Financial Officer, Bahwan Engineering Company, which is part of the Suhail Bahwan Group (Holding) L.L.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. Chairman of the Risk Committee and Member of the Credit Committee of the Board.

Mr. Al Habsi is Director of MOD Pension Fund, having 20 years experience in the financial sector.

He holds directorship in various joint stock companies. He is Deputy Chairman of Gulf Custody Co Oman and Member of Board GrowthGate Corp, a regional Private Equity Co.

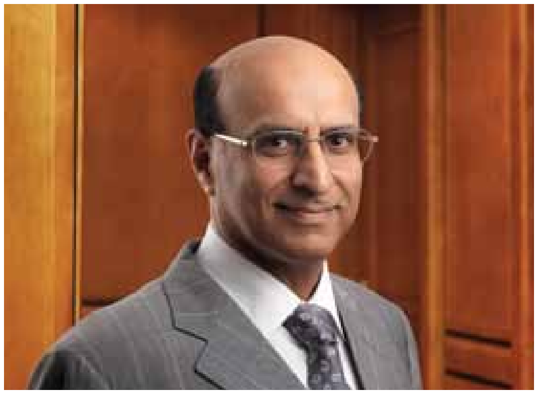
Mr. Saleh holds M.B.A. and M.Sc. in Finance both from University of Maryland of College Bark (U.S.A.), B.S.B.A. and B.A. from Boston University (U.S.A.).

Saif Said Salim Al Yazidi
Director

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

Member of the Board of Oman International Development and Investment Company and 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 MBA degree from McMaster University Canada.

Robert Sharpe
Director

Director since March 2011. Member of the Board Audit Committee and Board Risk Committee.

Mr. Sharpe is the Vice Chairman of Orient 1. He has over 30 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 U.K.

He holds a Diploma in Sales Marketing Management.

Faisal Abdullah Al Farsi
Director

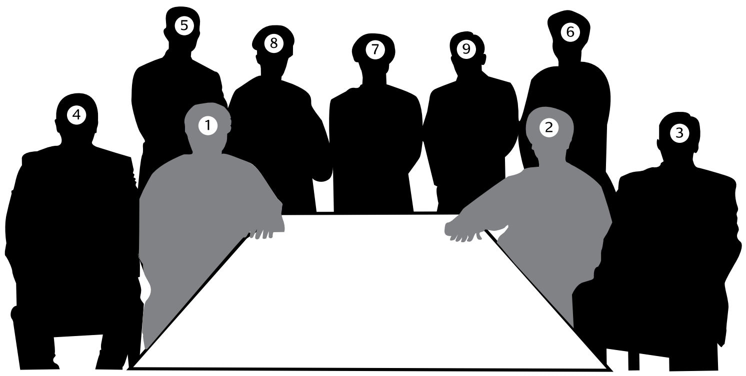
Director since September 2011. Member of the Board Audit Committee.

In 1995 he joined the Public Authority for Social Insurance where he occupied various positions which include Head of Pensions, Grants & Gratuities, Head of Work Injuries and Occupational Diseases.

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. He is the Manager of Insurance Benefits at the 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. **Stephen Clayton**
   Chief Risk Officer
6. **Nasser Salim Al Rashdi**
   Chief Internal Auditor
7. **Mansoor Darwish Al Raisi**
   Deputy General Manager - Compliance
8. **Nasser Mohammed Al Hajri**
   Chief Human Resources Officer
9. **V. Balasubramanian**
   Chief Financial Officer

In accordance with the directives of the Code of Corporate Governance promulgated by 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.

corporate governance report 2011

For You. For Our Nation.

P.O. Box 1750, Ruwi 112
Ernst & Young Building
Qurum
Muscat, Sultanate of Oman
Tel: +968 2455 9559 Fax: +968 2456 6043
muscat@om.ey.com
www.ey.com/me
C.R. No. 1/36809/5
P. R. No. MH/4

Report of Factual Findings on the corporate governance reporting of National Bank of Oman SAOG and its application of the corporate governance practices in accordance with the CMA code of corporate governance

TO THE SHAREHOLDERS OF NATIONAL BANK OF OMAN SAOG

We have performed the procedures prescribed in Capital Market Authority (CMA) circular no 16/2003, dated 29 December 2003 with respect to the accompanying corporate governance report of National Bank of Oman SAOG (the bank) and its application of corporate governance practices in accordance with the CMA Code of Corporate Governance issued under circular no. 11/2002 dated 3 June 2002 and the CMA Rules and Guidelines on disclosure, issued under CMA administrative decision 5, dated 27 June 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 extent of the bank's compliance with the code as issued by the CMA.

We report our findings below:

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

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

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

Our report is solely for the purpose set forth in the first paragraph of this report and for your information and is not to be used for any other purpose. This report relates only to the accompanying corporate governance report of National Bank of Oman SAOG to be included in its annual report for the year ended 31 December 2011 and does not extend to any financial statements of National Bank of Oman SAOG, taken as a whole.

Ernst & Young

23 January 2012
Muscat

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 2011 by winning the First Runner Up – Banking Category - '2nd Corporate Governance Excellence Award 2011', organised by Capital Market Authority (CMA).

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.

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.

Appointment of Directors

The Board is comprised of 11 members who have been elected by the shareholders in March 2011 for a period of three years. However consequent to a juristic person decision to replace his representative in the Board, The members of the Board approved this replacement decision. The current term of all the Directors expires in March 2014.

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 to 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.

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.

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.

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

*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 22nd MARCH 2011 (Yes/No/NA)
Mr. Omar Hussain Al Fardan – Chairman	EXCOB	Nil	6	Yes
Mr. Mohammed Mahfoodh Al Ardhi – Deputy Chairman	BRC, CCB	NIL	5	NA
Sayyidah Rawan Ahmed Al Said	EXCOB, BAC	3	6	Yes
Sheikh Abdullah Bin Ali Bin Jabor Al Thani	CCB	Nil	4	Yes
Mr. Anil Kumar Nahar	BAC, BRC	NIL	5	Yes
Mr. Andrew Charles Stevens	EXCOB, CCB	Nil	6	Yes
Mr. Saif Said Al Yazidi	BAC, CCB	2	5	Yes
Mr. Saleh Nasser Al Habsi	BRC, CCB	1	6	Yes
Mr. Suresh M Shivdasani	BRC, EXCOB	Nil	5	Yes
Mr. Robert Sharpe	BAC, BRC	Nil	5	NA
Mr. Faisal Abdullah Al Farsi	BAC	Nil	Nil	NA
Dr Younis Khalfan Al Akhzami	BAC, EXCOB	Nil	4	Yes
Mr. Imad Kamal Sultan	CCB, BRC	1	1	Yes
Mr. Hugh Edward Thompson	BAC, BRC	Nil	Nil	Yes

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

Number and Dates of Board Meetings

National Bank of Oman held 6 Board meetings during 2011. They were on 31st January, 22nd March, 20th April, 15th June, 15th September and 14th December 2011. The maximum interval between two meetings was 91 days. This is in compliance with Article 4 of the Code, which requires meetings to be held within a maximum time gap of four months.

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 2011 is RO 904,478

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 incentives 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 2011 of the Directors is RO 135,172.222 subject to the Annual General Meeting approval proposed to be held on 25th March 2012.

The details of the sitting fees paid or accrued for payment during 2011 are as follows:

Table 3

Name of the Directors	Total Fees RO	Remarks
Mr. Omar Hussain Al Fardan - Chairman	4,000.000	
Mr. Mohammed Mahfoodh Al Ardhi - Deputy Chairman	6,561.111	Appointed on 22nd March 2011
Sayyidah Rawan Ahmed Al Said	4,600.000	
Mr. Anil Kumar Nahar	4,100.000	
Mr. Imad Kamal Sultan	1,005.556	Resigned on 22nd March 2011
Sheikh Abdullah Bin Ali Bin Jabor Al Thani	7,600.000	
Mr. Andrew Charles Stevens	9,000.000	
Mr. Hugh Edward Thompson	400.000	Resigned on 22nd March 2011
Dr Younis Khalfan Al Akhzami	3,200.000	Resigned on 21st Sep 2011
Mr. Saleh Nasser Al Habsi	8,800.000	
Mr. Saif Said Al Yazidi	7,761.111	
Mr. Robert Sharpe	4,100.000	Appointed on 22nd March 2011
Mr. Suresh M Shivdasani	3,700.000	
Total	**64,827.778**	

The total hotel and travel expense related to the Board Members during 2011 is RO 34,386

Board Committees

As at December 2011, The Board of Directors has four standing committees, the Credit Committee, the Audit Committee, the Risk Committee and the Executive Committee.

Audit Committee of the Board

The Audit Committee comprises five independent members. The committee has met six times in 2011.
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 – Independent	5	
Mr. Anil Kumar Nahar	Member - Independent	6	
Mr. Saif Al Yazidi	Member - Independent	5	
Dr. Younis Al Akhzami	Member - Independent	2	Resigned in September 2011
Mr. Hugh Edward Thompson	Member - Non Independent	1	Resigned on 22nd March 2011
Mr. Robert Sharpe	Member - Independent	5	

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.

Credit Committee of the Board (CCB)

The Credit Committee comprises of 5 members and met 8 times during 2011. 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	6	Appointed on 22.03.2011
Mr. Andrew Charles Stevens	Member	8	
Mr. Saleh Nasser Al Habsi	Member	7	
Sheikh Abdullah Bin Ali Bin Jabor Al Thani	Member	5	
Mr. Saif Said Al Yazidi	Member	4	Appointed on 22.03.2011
Mr. Imad Kamal Sultan	Ex-Chairman	2	Resigned on 22.03.2011

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.

Risk Committee of the Board

The Risk Committee of the Board comprises of five members and met four times during the year2011. 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:

Risk Committee of the Board: (continued)

Table 6

Name	Position	Meetings Attended	Remarks
Mr. Saleh Nasser Al Habsi	Chairman	4	
Mr. Suresh M Shivdasani	Member	2	
Mr. Anil Nahar	Member	2	Appointed on 22.03.2011
Mr. Robert Sharpe	Member	3	Appointed on 22.03.2011
Mr. Mohammed Mahfoodh Al Ardhi	Member	1	Appointed on 22.03.2011
Mr. Hugh Edward Thompson	Member	1	Resigned on 22.03.2011
Mr. Imad Kamal Sultan	Member	1	Resigned on 22.03.2011
Mr. Saif Said Al Yazidi	Member	-	Resigned on 22.03.2011
Sheikh Abdullah Bin Ali Bin Jabor Al Thani	Member	1	Resigned on 22.03.2011

Executive Committee of the Board (EXCOB)

The Executive Committee of the Board comprises of five members and met five times during the year 2011. 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	5	
Sayyidah Rawan Ahmed Al Said	Member	3	
Mr. Andrew Charles Stevens	Member	5	
Dr. Younis Khalfan Al Akhzami	Member	2	Resigned in September 2011
Mr. Suresh Shivdasani	Member	2	

The main responsibilities of the EXCOB are stated below:

- To recommend for Board approval strategies and policies to be pursued by the Bank.
- To review and recommend to the Board all policies relating to the Bank's organization and operations including all necessary authorities required by Executive Management in the execution of their responsibilities.
- Appointment and movement of key executives in the Bank.
- To review and approve major changes in the Bank's organizational structure at the level of Divisional Heads and above.
- To oversee the performance and implementation of any property-related projects.

Board Member Profiles

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 Al Fardan 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 and Member of the Risk Committee of the Board.

He is Director of The Board of Investcorp Bank, NYC, USA and The International Advisory Board of The Brookings Institute, Washington DC, USA. A retired Air Vice Marshal by profession, Mr Mohammed Mahfoodh Al Ardhi joined the Royal Air Force (RAFO) of Oman 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 U.K 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 23 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 the GCC.

Sayyidah Rawan holds a M.Sc in Economics & Finance from Loughborough University U.K. She also holds a Post Graduate Diploma in Investment Analysis from Stirling University, U.K. 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.

Director of Oman Dental College (S.A.O.G), Al Suwadi Power Co. S.A.O.C., Bahwan Veolia Water L.L.C and Sharqiyah Desalination Co. S.A.O.C. Chief Financial Officer, Bahwan Engineering Company, which is part of the Suhail Bahwan Group (Holding) L.L.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. Chairman of the Risk Committee and Member of the Credit Committee of the Board.

Mr. Al Habsi is Director of MOD Pension Fund, having 20 years experience in the financial sector.

He holds directorship in various joint stock companies. He is Deputy Chairman of Gulf Custody Co Oman and Member of Board GrowthGate Corp, a regional Private Equity Co.

Mr. Saleh holds MBA and M.Sc. in Finance both from University of Maryland of College Bark (U.S.A.), B.S.B.A. and B.A. from Boston University (U.S.A.).

Mr. Saif Said Salim Al Yazidi, Director

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

Member of the Board of Oman International Development and Investment Company and 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 MBA degree from McMaster University Canada.

Mr. Robert Sharpe, Director

Director since March 2011. Member of the Board Audit Committee and Board Risk Committee.

Mr. Sharpe is the Vice Chairman of Orient 1. He has over 30 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 U.K.

He holds a Diploma in Sales Marketing Management.

Mr. Faisal Abdullah Al Farsi, Director

Director since September 2011. Member of the Board Audit Committee.

In 1995 he joined the Public Authority for Social Insurance where he occupied various positions which include Head of Pensions, Grants & Gratuities, Head of Work Injuries and Occupational Diseases.

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. He is the Manager of Insurance Benefits at the Public Authority for Social Insurance.

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. During the year 2011 the GM-COO , GM-Strategy & Developments ,GM-Retail Banking, DGM-Head of Finance, DGM-Head of Human Resources, DGM-Head of Financial Institutions, AGM-Head of Operations, AGM-Head of IT Projects and AGM-Internal Audit left the bank services and have adequately been replaced. The following table gives details of the top five management officers along with their positions:

Table (8)

Name	Position
Salaam Said Al Shaksy	Chief Executive Officer
Ahmed Jaffer Al Musalmi	Deputy Chief Executive Officer
Humayun Kabir	General Manager - Wholesale Banking
Stephen Clayton	Chief Risk Officer
Harshdeep Singh Munjal	General Manager - Retail and Private Banking

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 2011

NBO AND MSM BANK & INVESTMENT INDEX - FY 2011

Table (9)

Banks & Investment index			
Month	High	Low	Closing
Jan-11	8,926.700	8,164.900	8,369.550
Feb-11	8,408.030	6,804.870	6,811.420
Mar-11	7,416.380	6,898.240	6,921.310
Apr-11	7,576.770	6,921.310	7,194.830
May-11	7,231.110	6,402.480	6,518.730
Jun-11	6,683.570	6,405.150	6,442.550
Jul-11	6,557.060	6,367.770	6,368.580
Aug-11	6,461.610	5,827.670	6,443.100
Sep-11	6,536.100	6,305.600	6,317.200
Oct-11	6,328.970	6,197.770	6,222.160
Nov-11	6,228.660	6,019.030	6,021.750
Dec-11	6,410.810	6,026.880	6,385.670

NBO price			
Month	High	Low	Closing
Jan-11	0.355	0.312	0.335
Feb-11	0.340	0.289	0.304
Mar-11	0.325	0.300	0.319
Apr-11	0.330	0.306	0.312
May-11	0.323	0.304	0.322
Jun-11	0.330	0.310	0.320
Jul-11	0.333	0.315	0.322
Aug-11	0.324	0.290	0.316
Sep-11	0.322	0.300	0.312
Oct-11	0.315	0.300	0.315
Nov-11	0.310	0.301	0.306
Dec-11	0.322	0.308	0.320

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.

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.

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 (10)

Year	Cash dividend	Bonus shares
2007	17.5%	17.5%
2008	17.5%	Nil
2009	12 %	Nil
2010	15 %	Nil
2011(proposed subject to shareholders approval)	17.5%	2.5%

Corporate Social Responsibility (CSR)

During the year 2011, the Bank distributed donations to the charitable organizations and other non profitable organizations and participated in CSR initiatives totaling RO. 170,483.700 as approved by the Annual General Meeting held on 22nd March 2011.

Details of NBO main donations and CSR initiatives during the year 2011:

Table (11)

Amount (OMR)	Details
5,000.000	Oman Road Safety Association
16,000.000	Oman Association for The Disabled
5,000.000	AL Noor Association for the Blind
5,000.000	The National Cancer Awareness Association
1,000.000	Environment Society Of Oman
500.000	Employee Volunteer Group - Matching Program
4,500.000	AIESEC Oman - World Largest Student Run Organisation
400.000	Plant a Book Campaign - OHBDA
10,495.000	Sustainability Report 2011
170.000	Al Rahma Group
5,000.000	Oman Heart Association
5,000.000	Oman Hereditary Blood Disorder Association (OHBDA)
500.000	Muscat Autism Center
8,000.000	Association of Early Intervention for Children with Disabilities
41,000.000	Ministry of Social Development - Centers for Children with Special Needs
50,000.000	Ministry of Social Development - Low Income Social Security Homes
9,168.700	Women of Excellence - NBO Women Initiative Network
3,000.000	Outward Bound Oman
750.000	National Traffic Safety
170,483.700	Total

Distribution of Shareholding

Major shareholders (5% and above)

Table (12)

Shareholder name	No. of shares as on 31st December 2011	% of Capital
Commercial Bank of Qatar	377,267,410	34.90
Suhail Bahwan Group Holding LLC	159,385,410	14.74
HSBC A/C Ministry Of Defence Pension Fund	82,777,900	7.66
Civil Service Employees Pension Fund	81,175,270	7.51
Public Authority for Social Insurance	64,805,315	5.99

The shareholding pattern as on 31 December 2011 was:

Number of Shares	Number of Shareholders	Total Shares	% of Capital
7,000,000 and above	16	955,109,155	88
3,000,000 to 6,999,999	5	24,542,661	2
1,500,000 to 2,999,999	13	27,866,214	3
500,000 to 1,499,999	31	27,843,647	3
100,000 to 499,999	138	31,191,662	3
Below 100,000	6484	14,446,661	1
Total		**1,081,000,000**	**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.

Auditors:

During the Annual General Meeting your Board of Directors intends to propose for Shareholder's approval the appointment of new external Auditors for 2012 as per statutory requirements. (Existing Auditors Ernst and Young completed their four years term as prescribed by CMA.)

Changes to the composition of Board and changes in Senior Management during 2011 have been fully covered in the Corporate Governance report.

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.

Ernst & Young – Statutory Auditors

Ernst & Young are the statutory auditor's of the Company. Ernst & Young is one of Oman's oldest established accounting firms, having had a permanent office in the country since 1974. The practice comprises 200 professionals, and is working under the direction of six partners. The Oman office forms part of Ernst & Young's MENA practice, with 113 partners and over 5,079 other professionals in 18 offices in 13 countries throughout the region. The MENA practice is member firm of Ernst & Young Global, operating in more than 140 countries with approximately 152,000 personnel world-wide.

During the year 2011, RO. 67,275 was accrued / paid to the external auditors against the audit and related assurance services.

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 2011

For You. For Our Nation.

ERNST & YOUNG

P.O. Box 1750, Ruwi 112
Ernst & Young Building
Qurum
Muscat, Sultanate of Oman
Tel: +968 2455 9559 Fax: +968 2456 6043
muscat@om.ey.com
www.ey.com/me
C.R. No. 1/36809/5
P. R. No. MH/4

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

We have performed the procedures agreed with you and as prescribed in the Central Bank of Oman (CBO) circular no. BM 1027 dated 4 December 2007 with respect to the Basel II – Pillar III disclosures (the disclosures) of National Bank of Oman SAOG (the bank) as at and for the year ended 31 December 2011. The disclosures were prepared by the bank's management in accordance with the related requirements set out in CBO circular number BM 1009 dated 13 September 2006 and circular number BM 1027 dated 4 December 2007 (the circulars). Our engagement was undertaken in accordance with the International Standard on Related Services applicable to agreed-upon procedures engagements. The procedures, as set out in Circular number BM 1027, were performed solely to assist you in evaluating the bank's compliance with the related disclosure requirements set out in the CBO Circular number BM 1009.

We report our findings as follows:

We found that the bank's disclosures are free from any material misrepresentation.

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

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

Our report is solely for the purpose set forth in the first paragraph of this report and for your information and is not to be used for any other purpose. This report relates only to the accompanying disclosures to be included in the bank's annual report for the year ended 31 December 2011 and does not extend to any financial statements of the bank taken as a whole or to any other reports of the bank.

Ernst & Young

31 January 2012
Muscat

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

This is a stand alone entity.

CAPITAL STRUCTURE

The authorised share capital of the bank as at 31 December 2011 is 1,600,000,000 shares of RO 0.100 each.

The issued and paid up capital of the bank as at 31 December 2011 is 1,081,000,000 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 banks capital structure as at close of 31 December 2011, 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	108,100
2	Share premium	34,465
3	Legal reserves	38,642
4	General reserves	4,419
5	Sub-ordinated loan reserve	14,860
6	Stock dividend	2,703
7	Retained earnings	55,682
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	**258,871**
	Deductions	
14	Goodwill	-
15	Deferred tax asset	(482)
16	Intangible Assets, including cumulative unrealised losses recognised directly in equity	(328)
17	Reciprocal crossholding of bank capital, artificially designed to inflate the capital position of banks	
	Sub-total	(810)
18	**Tier I capital after the above deductions**	**258,061**
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 banks' net worth for aggregate of such investments	-

CAPITAL STRUCTURE (continued)

Sl. No.	Elements of Capital	Amount in RO 000's
21	50% of shortfall in the regulatory capital requirements in the un-consolidated entities	-
22	50% of investments in unconsolidated banking and financial subsidiary companies associates or affiliates, etc	-
	Sub-total	-
23	**Tier I capital after all deductions**	**258,061**
	Tier II Capital	
24	Undisclosed reserves	-
25	Revaluation reserves / Cumulative fair value gains or losses on available for sale instruments	
26	General loan loss provision/General loan loss reserve	24,534
27	Sub-ordinated debt	39,840
28	Hybrid debt capital instruments	-
29	**Total Tier II Capital**	**64,374**
	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 banks' 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 unconsolidated banking and financial subsidiary companies associates or affiliates, etc	-
	Total deductions from Tier II	-
	Tier II Capital (Net)	**64,374**
34	**Tier III Capital (eligible)**	-
35	**Total Regulatory Capital**	**322,435**

Note: Retained earnings are after deduction of RO 18.9 million towards proposed cash dividend and RO 2.7 million towards proposed stock 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 ensuring that too much "excess" capital is not held unnecessarily)
- Incentive 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 as 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.

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), 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. The ICAAP has been reviewed and approved by the Board. Following the guidelines issued by the Central Bank of Oman in December 2011, assessment under ICAAP will be carried out and a trial run as recommended shall be submitted to the CBO in the coming year.

Quantitative Disclosures:

Position as at 31.12.11 **(RO'000)**

Sl. No.	Details	Amount
1	**Tier I capital (after supervisory deductions)**	**258,061**
2	**Tier II capital (after supervisory deductions & upto eligible limits)**	**64,374**
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**	**1,926,546**
6	**Risk Weighted Assets (RWAs) – Operational Risk**	**154,834**
7	**Total Risk Weighted Assets (RWAs) – Banking Book + Operational Risk**	**2,081,380**
8	Minimum required capital to support RWAs of banking book and operational risk	249,766
	i) Minimum required Tier I capital for banking book and operational risk	185,392
	ii) Tier II capital required for banking book and operational risk	64,374
9	Tier I capital available for supporting Trading Book	72,669
10	Tier II capital available for supporting Trading book	-
11	**Risk Weighted Assets (RWAs) – Trading Book**	**24,538**
12	Total capital required to support Trading Book	2,945
13	Minimum Tier I capital required for supporting Trading Book	839
14	Used Eligible Tier III Capital	-
15	**Total Regulatory Capital**	**322,435**
16	**Total Risk Weighted Assets – Whole bank**	**2,105,918**
17	**BIS Capital Adequacy Ratio**	**15.31**
18	Unused but eligible Tier III Capital	-

CAPITAL ADEQUACY (continued)

Certain additional capital adequacy disclosures are as follows:

Position as at 31.12.11 **(RO'000)**

Sl. No.	Details	Gross balance (Book value)	Net balance (Book value)	Risk Weighted Assets
1	On balance sheet item	2,261,018	2,182,686	1,623,826
2	Off balance sheet item	354,618	354,618	280,975
3	Derivatives	21,745	21,745	21,745
4	Operational Risk	-	-	154,834
5	Market Risk	-	-	24,538
	Total	2,637,381	2,559,049	2,105,918
6	Tier I Capital	258,061	-	-
7	Tier 2 Capital	64,374	-	-
8	Tier 3 Capital	-	-	-
9	Total Regulatory Capital	322,435	-	-
9.1	Capital requirement for credit risk	231,186	-	-
9.2	Capital requirement for market risk	2,945	-	-
9.3	Capital requirement for operational risk	18,580	-	-
10	Total required Capital	252,711	-	-
11	Tier I Ratio	12.25	-	-
12	Total Capital ratio	15.31	-	-

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, SME 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 SME 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.

In 2011, based on the prevailing market conditions, the competitive landscape and the economic unrests, the Bank sustained its continuous monitoring of the portfolio and revised the lending criteria 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 is also in the process of implementing an automated Loan Origination System and a Credit Scoring Module 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.

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 Risk (continued)

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.

Credit Risk (continued)

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:

- 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. 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 2011:

(RO'000)

Sl. No.	Type of Credit Exposure	Average Gross Exposure		Total Gross Exposure as at	
		Current Year	Previous Year	31 December 11	31 December 10
1	Overdrafts	47,259	47,007	43,051	59,376
2	Personal loans	696,029	638,514	780,272	645,047
3	Loans against trust receipts	40,082	36,833	38,723	37,509
4	Other loans	802,981	737,471	852,025	682,076
5	Bills purchased / discounted	15,471	10,272	19,617	8,361
6	Any other	-	-	-	-
	Total	**1,601,822**	**1,470,097**	**1,733,688**	**1,432,369**

(ii) Geographic distribution of exposures, broken down in significant areas by major types of credit exposure as at 31 December 2011:

(RO'000)

Sl. No.	Type of Credit Exposure	Oman	Other GCC countries	OECD countries	India	Pakistan	Others	Total
1	Overdrafts	34,444	8,297	-	-	-	310	43,051
2	Personal loans	776,998	2,118	-	-	-	1,156	780,272
3	Loans against trust receipts	34,782	3,941	-	-	-	-	38,723
4	Other loans	784,467	60,190	5,552	-	-	1,816	852,025
5	Bills purchased / discounted	19,523	94	-	-	-	-	19,617
6	Any other	-	-	-	-	-	-	-
	Total	**1,650,214**	**74,640**	**5,552**	**-**	**-**	**3,282**	**1,733,688**

Credit Risk (continued)

(iii) Industry or counter party type distribution of exposures, broken down by major types of credit exposure as at 31 December 2011:

(RO'000)

Sl. No.	Economic Sector	Overdraft	Loans	Bills Purchased / Discounted	Others	Total	Off Balance Sheet Exposure
1	Import trade	-	-	-	34,781	34,781	113
2	Export trade	-	389	-	-	389	-
3	Wholesale and retail trade	9,342	97,300	259	3,809	110,710	37,233
4	Mining and quarrying	1,199	31,517	3,656	-	36,372	3,777
5	Construction	5,414	110,902	7,967	-	124,283	116,412
6	Manufacturing	2,496	180,776	255	133	183,660	35,494
7	Electricity, gas and water	-	31,853	-	-	31,853	49,850
8	Transport and Communication	218	125,094	-	-	125,312	17,662
9	Financial institutions	10,221	86,391	-	-	96,612	211,049
10	Services	3,700	93,507	783	-	97,990	10,765
11	Personal loans	-	780,272	-	-	780,272	137
12	Agriculture and allied activities	1,058	11,098	-	-	12,156	162
13	Government	-	7	-	-	7	20,673
14	Non-Resident lending	-	35,750	-	-	35,750	-
15	All Others	9,403	47,441	6,697	-	63,541	4,487
	Total	**43,051**	**1,632,297**	**19,617**	**38,723**	**1,733,688**	**507,814**

(iv) Residual contractual maturity as at 31 December 2011, 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	2,153	142,019	8,158	4,937	157,267	125,922
2	1-3 months	2,153	159,055	10,002	18,446	189,656	100,143
3	3-6 months	2,153	74,637	1,457	15,289	93,536	65,404
4	6-9 months	2,153	41,406	-	51	43,610	22,595
5	9-12 months	2,153	90,082	-	-	92,235	26,158
6	1-3 years	10,762	183,311	-	-	194,073	141,915
7	3-5 years	10,762	134,927	-	-	145,689	11,819
8	Over 5 years	10,762	806,860	-	-	817,622	13,858
	Total	**43,051**	**1,632,297**	**19,617**	**38,723**	**1,733,688**	**507,814**

Credit Risk (continued)

(v) Total loans broken down by major industry or counter party type as at 31 December 2011:

(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	34,781	-	348	-	-	-	1,380
2	Export Trade	389	389	-	389	-	-	-
3	Wholesale & Retail Trade	110,710	10,707	1,000	3,194	5,067	810	72
4	Mining & Quarrying	36,372	-	364	-	-	-	-
5	Construction	124,283	22,195	1,021	5,911	2,000	4,500	274
6	Manufacturing	183,660	6,616	1,770	2,348	2,489	149	5,598
7	Electricity, gas and water	31,853	-	319	-	-	-	-
8	Transport and Communication	125,312	1,523	1,238	372	218	301	-
9	Financial Institutions	96,612	-	966	-	-	-	-
10	Services	97,990	1,004	970	563	506	268	81
11	Personal Loans	780,272	14,997	15,311	5,871	2,294	6,807	8,694
12	Agriculture and Allied Activities	12,156	5,373	68	567	710	-	-
13	Government	7	-	-	-	-	-	-
14	Non-Resident Lending	35,750	-	358	2,200	-	-	-
15	All Others	63,541	1,233	801	3,508	169	6,097	61
	Total	**1,733,688**	**64,037**	**24,534**	**24,923**	**13,453**	**18,932**	**16,160**

(vi) Amount of impaired loans as at 31 December 2011, 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	1,650,214	49,734	23,636	15,983	10,959	17,243	8,655
2	Other GCC Countries	74,640	11,308	831	5,948	2,387	1,542	507
3	OECD Countries	5,552	-	56	-	-	-	-
4	India	-	-	-	-	-	-	-
5	Pakistan	-	-	-	-	-	-	-
6	Others	3,282	2,995	11	2,992	107	147	6,998
	Total	**1,733,688**	**64,037**	**24,534**	**24,923**	**13,453**	**18,932**	**16,160**

Credit Risk (continued)

(vii) Movements of gross loans

(RO'000)

Movement of Gross Loans during the year ended 31 December 2011

Sl. No.	Details	Performing Loans		Non performing Loans			
		Standard	Special Mention	Sub-Standard	Doubtful	Loss	Total
1	Opening balance	1,284,112	86,950	7,515	16,843	36,949	1,432,369
2	Migration / changes (+/-)	(58,212)	22,043	10,361	13,247	12,561	-
3	New loans	920,564	54	411	515	2,527	924,071
4	Recovery of loans	(556,293)	(29,567)	(2,487)	(10,050)	(8,195)	(606,592)
5	Loans written off	-	-	-	(273)	(15,887)	(16,160)
6	Closing balance	1,590,171	79,480	15,800	20,282	27,955	1,733,688
7	Provisions held	23,689	3,045	3,798	6,278	12,647	49,457
8	Reserve interest	-	-	626	1,435	11,392	13,453

Credit Risk – Disclosures for portfolios subject to the standardized approach

Qualitative Disclosures:

The bank is following Moody's rating for both sovereign and inter bank 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.

Quantitative Disclosures:

Exposure amount as at 31 December 2011, 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	321,253	-	-	-	1,442	-	322,695
2	Banks	-	118,684	-	60,453	3,815	6,590	189,542
	Unrated							
1	Corporate	-	56,808	-		647,730	-	704,538
2	Retail	-	-	-	-	659,572	-	659,572
3	Claims secured by residential property	-	-	58,540	-	46,283	-	104,823
4	Claims secured by commercial property	-	-	-	-	134,247	-	134,247
5	Past due loans			-	-	58,444	-	58,444
6	Other assets	25,785	4,133	-	-	56,925	313	87,156
7	Off-balance Sheet Items	6,237	32,819	-	82,300	255,008	-	376,364
	Total Banking Book	**353,275**	**212,444**	**58,540**	**142,753**	**1,863,466**	**6,903**	**2,637,381**

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. The collaterals considered are cash and provisions against impaired loans.

Quantitative Disclosures:

Eligible financial collateral

Sl. No.	Details	Amount
1	Corporate 100% Cash	38,692
2	Past due loans(provisions)	39,640
3	Total	78,332

The capital requirement on credit risk as at 31 December 2011 is RO (‘000) 231,186.

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.

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 10% to reflect the general market risk.

Capital required for trading book as at 31 December 2011:

- Foreign Exchange Risk - RO (‘000) 2,945

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 (Continued)

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 points(bps) 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 (bps) 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 2011	200 bps increase	200 bps decrease
Earnings impact - RO'000s	8,829	(8,829)
Earnings impact - USD'000s	22,932	(22,932)

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.

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 2011 was as follows:

	Average effective interest rate	On demand within 3 months	3 to 12 months	1 to 5 years	Over 5 years	Non interest sensitive	Total
		RO'000	RO'000	RO'000	RO'000	RO'000	RO'000
Cash and balances with Central Banks	0.05%	95,744	-	-	-	125,027	220,771
Due from banks and other money market placements	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 assets	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 funds	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**	**-**	**-**

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.

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 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.

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 Bank also 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 2011 was as follows:

	On demand within 3 months	3 to 12 months	Subtotal less than 12 months	1 to 5 years	Over 5 years	Subtotal over 12 months	Total
	RO'000	RO'000	RO'000	RO'000	RO'000	RO'000	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	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 assets	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 funds	-	-	-	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**

Information Security and Business Continuity Management

The growing technology and easy to access of the hacking tools has thrown new challenges to the banking industry which have been effectively met through enhancements to the information security framework of the Bank and through development and implementation of appropriate policies and procedures.

The initiatives undertaken to improve corporate governance include; a comprehensive third party security assessment review of the business applications, operating systems, databases and communication and security assets. The information security architecture of the Bank was enhanced through implementation of a minimum security baseline for all systems.

Business continuity readiness was successfully tested and proved with effective management of the crisis situations during the year. The Bank successfully tested the disaster recovery infrastructure for all critical systems with expected recovery time objectives of the supported business services.

The key initiatives on the business continuity readiness included detailed study on the technology gap analysis of the Bank's information technology infrastructure from recovery perspective, review of business impact analysis and upgrade of the branch communication infrastructure to higher bandwidth. A focused drive for business continuity awareness was undertaken covering all branches and other operating offices.

Bank established a comprehensive Risk management framework pertaining to cards for protecting itself against the fraud threats present worldwide including implementation of a near real time debit card fraud monitoring solution.

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 the 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) 18,580

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.

This report on Basel II disclosures set out from pages no 28 to 46 was authorized for issue by the Board of Directors on 23rd January 2012

Omar Hussain Al Fardan
Chairman

In recognition of the best practices and corporate governance measures applied by it, the National Bank of Oman has crowned its achievements in 2011 by winning the First Runner Up – Banking Category- ‘2nd Corporate Governance Excellence Award 2011’, organised by Capital Market Authority (CMA).

Management Discussion & analysis report 2011

For You. For Our Nation.

Economic Development

Oman experienced steady economic growth in 2011. Initial projections indicate an expected real GDP growth of 6% in 2011. Despite a 17% increase in Government expenditure, the overall fiscal surplus of the Sultanate is expected to reach 8.2% of the GDP for the year 2011 backed by rapid growth in oil revenues

Oman's economy has been largely unaffected by the recent turmoil in the global financial markets, as well as the Eurozone debt crisis mainly on account of majority of its oil dominated exports being made to Asian countries.

Industry expansion, particularly in the metals sector has also been a highlight of the year 2011. Oman has set a strong record in the export of minerals and quarried goods. Aluminium mining and production has been an especially important development during the year.

The Sultanate has also been successful in attracting foreign direct investment in recent years.

The Banking sector saw new initiatives with the Central Bank approving the introduction of Islamic Banking.

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
- 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 civil service 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.

Despite a 17% increase in Government expenditure, the overall fiscal surplus of the Sultanate is expected to reach 8.2% of the GDP for the year 2011 backed by rapid growth in oil revenues.

Oman Banking Sector – Year 2011

The Oman Banking sector reported a strong growth in the year 2011. Total assets increased to RO 18.4 billion as at December 2011 against RO 15.6 billion in December 2010, an increase of 18%. Cash on hand and deposits of commercial banks with CBO stood at RO 978 million at the end of December 2011 compared to RO 1.52 billion for the same period the previous year. Total credit grew by 17% to RO 12.5 billion as at December 2011 which accounted for 68% of the total assets. While credit to the Government sector declined by 31%, credit to public enterprises and private sector increased by 58 % and 13 % respectively. Commercial Bank's overall investments in securities increased by 49% during the year to December 2011 as compared the same period a year ago. The increase was mainly on account of Central Bank of Oman certificates of deposits which grew from RO 0.8 billion as at close of December 2010 to RO 1.4 billion as at close of December 2011.

On the liabilities side of the balance sheet, total deposits in Rial Omani as well as foreign currency witnessed a year on year growth of 19.6% to RO 12.6 billion in December 2011 from RO 10.5 billion in December 2010. Private sector deposits increased by 11% to close at RO 8 billion at December 2011 against RO 7.3 billion a year ago. Government deposits grew by 47% whereas deposits of public enterprises showed an increase of 13% during the twelve months ended 31st December 2011.

The report highlights the leading change by the CEO and the management team currently in place and the ensuing transformation of operations as the Bank seeks to build on its strength and regain market share.

The provisional figures of net profits of commercial banks stood at RO 262 million at the end of December 2011 compared to RO 257 million at the end of December 2010.

Overall, the banking sector in Oman is set for healthy growth in year 2012. Heavy government expenditure as indicated earlier is expected to foster credit expansion. New Bank's expected to enter the market 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.

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

National Bank of Oman (NBO) 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.

During the year, the committed line facility provided by CBQ has been enhanced to USD 200 million as against USD 70 million originally sanctioned. This has enabled the Bank to retain its strength in dollar liquidity.

NBO 2011

In Sept 2011, Fitch rating agency assigned a long term issuer default rating of BBB+ to the Bank. The report highlights the leading change by the Bank's Chief Executive Officer and the management team currently in place and the ensuing transformation of operations as the Bank seeks to build on its strength and regain market share through a clear business expansion and diversification strategy. The report comments positively on the earnings and profitability being in line with the peers, as well as the decline in the NPL and the lack of liquidity concerns.

Retail and Private Banking

Achievement

- **First Bank in Oman to launch 'Mobile Banking' services in May 2011**
- **Launched the Gold Savings Account in July 2011**
- **Launched the Customer Consultant Award in December 2011**

Financial Performance

The Bank's net profit after tax increased by 26% to RO 34.2 million for the twelve months ended 31 December 2011 compared with RO 27.2 million for 2010.

Net interest income grew by 5% to RO 58.2 million for 2011 over the previous year with the cost of funds improving to 2.13% for the year ended 31 December 2011 compared with 2.64%. Net spread stood at 3.18% as at December 2011. Other income was a strong driver of revenue growth in 2011, with significant improvement in the ratio of non-interest income to total income, at 37%, up from 29%.

Operating expenses increased by 9% to RO 43 million for the year ended 31 December 2011 as the Bank continued to invest in its employees, systems and delivery channel network. The cost to income ratio improved from 51% to 47% on a year on year basis due to higher levels of income.

Net provisions for credit losses and investments for the year were higher than the previous year by RO 2.1 million predominantly due to an increase in impairment of the investments classified under the available for sale category. Recoveries and release from provisions on credit losses and loans written off increased by RO 3.6 million during the year, a 43% improvement over the previous year. The Bank continues to reduce the non-performing loans, with the non-performing loan ratio at 2.9% at the end of December 2011 against 3.5% in 2010.

During the twelve months ended 31 December 2011, customer lending increased by 23% to RO 1.7 billion. Customer deposits grew by 21% over the previous year to RO 1.6 billion.

The performance of various segments is covered in detail in the financial statements under segmental information (note 30)

Key developments - Core segments

Retail and Private Banking

The Retail and Private Banking Division has had a year of resounding success that was unprecedented. On its path to success, it has set new records in business growth, volumes, innovative products and profitability. 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 also continued to invest substantially in customer facing initiatives, which included increasing the Bank's network in terms of both intensity and spread, to 69 branches by December 2011. Additionally the ATM and CCDM network grew to 178 machines during the same period with enhanced features to improve percentage uptime and customer experience. As a first in Oman, the Call Centre launched 24hrs availability to 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 proposition, 'Sadara,' is the only private banking product in Oman to obtain ISO certification and has also successfully launched the Gold Savings Account as well as the new Elite Savings Account, both generating volumes that substantially exceeded expectations. Other initiatives include Home Contents insurance as well as the launch of the Customer Consultant Award, where customers provide NBO with their suggestions and stand the chance of winning the monthly prize on offer.

The Al Kanz savings account scheme continues to set new records with continued growth in market share during 2011.

Four Credit Card promotions were successfully launched in the summer of 2011, while all Credit and Debit Cards were rebranded and the Infinite Credit Card was launched to a few selected customers.

In keeping with its progress on Omanisation, the Bank has continuously promoted and selected local talent to take on more senior positions within the division. All branch staff continue to be Omani nationals and ongoing training programmes are in place to develop their overall product knowledge and sales skills.

In 2012, the Bank will continue its focus on delivering superior customer service, while on the product front; Al Kanz will remain a key focus area, followed by the Mortgage Business, Credit and Debit Cards, Wealth Management and Bancassurance.

Wholesale Banking

Achievement

- Strengthened synergies between Divisions of Wholesale Banking through CST " Client Service Team" integrated approach to service the corporate client with 360 degree offering.
- Lead arranged US $ 205 million long term facility to Oman Aluminum Rolling Mill with a share of US $ 103 million for NBO.
- Underwritten US$ 127 million facility to Telecommunications & manufacturing sector besides arranging short term and revolving credit facilities of US $ 775 million through other banks for the transport sector.

Wholesale Banking

Our Wholesale Banking Group has been structured to meet the diverse banking, advisory, and risk management needs of our corporate clients. In 2011 the Division surpassed the expectations of the customers by offering a collaborative platform consisting of Corporate Banking and Investment Banking backed by a capable and responsive Treasury, Transaction Banking and Financial Institutions Group thus becoming a one stop shop for all their requirements.

Corporate Banking

In 2011, the division focused its attention on identifying and adding to its business, high quality assets and 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.

NBO played a prominent role in the landmark infrastructure power project at Sur. The bank has also closely associated itself with Duqm as the emerging industrial and port town by making available a large financing package for the development of Duqm frontier town which is billed as one of the top 100 projects in the Middle East. The bank is also actively pursuing opportunities in other large projects coming up in Duqm in the year 2012.

In addition to pursuing and converting business opportunities in large public and private sectors, the Bank continued to focus on the protection of its existing asset values especially in the real estate sector in which the bank continues to exercise utmost caution. Thanks to the realistic and cautious restructuring and reschedulement program which was put in place in 2009 for some of the large players in this sector, the Bank was successful in minimizing the impact of the continued slowdown in the real estate sector.

> NBO played a prominent role in the landmark infrastructure power project at Sur. The Bank has also closely associated itself with Duqm.

Key initiatives of the division identified as a part of the strategy of the Bank will see actual implementation in the year 2012.

The Transaction Banking unit which was established two years ago to enhance the services to corporate customers of the bank by providing dedicated operational service continues its efforts to provide value added and personalized service to corporate customers. The Corporate Internet Banking (CIB) services being provided by this unit is used by a majority of the corporate customers and is considered one of the best in the market. The bank will continue to invest in technology and people to provide even more value adds through its CIB. Trade Services, bulk remittances and Corporate Internet Banking services have proved to be a success with most of the corporate customers of the Bank actively using these for their banking requirements.

The Corporate Banking franchise will continue to support domestic project financing and related activity in the coming year.

Investment Banking

It was a challenging year for investment banking around the world with most developed and developing stock markets performing poorly. The Muscat Securities Market was no exception to this.

Despite the economic challenges, the Investment Banking Division performed creditably and booked significant dividend income during the year. The division continued to build market share by obtaining new mandates and is now the leading player in the Fund Custody and Administration business in the Sultanate.

Wholesale Banking

Achievement

- **Brokerage : NBO maintained a top ten position throughout 2011 in the Broker Rankings for the first time.**
- **Fund Custody and Administration : NBO consolidated its position as the undisputed top service provider for local mutual funds during 2011 with Assets under custody of around USD 500 million.**
- **Asset Management : Structured NBO's first ever GCC Mutual Fund.**

The division is a key player in Asset Management and is further strengthening its position in the coming year through expansion of its investment products base to local as well as regional investors. The Corporate Finance & Advisory unit forayed into private equity, corporate advisory and merger & acquisition areas. It has bagged mandates on the advisory side and has bid for a number of deals in this area. The Brokerage unit turned in a commendable performance, increasing its overall market share. Given its long and successful track record and the confidence that the Bank enjoys with its customers, the coming year promises to be a year of transformation for the Division.

The Bank intends to launch a mutual fund in the year 2012 through its Investment banking division.

Treasury

The treasury division, in 2011 has augmented its prominence in the domestic market as a key strategic partner to corporate clients. This has been achieved by offering a broad spectrum of treasury services including those which assist corporate clients to manage related risks in their business operations. The division has achieved major strides in the alternative products suite established in 2010 especially in its specialized product offerings in foreign exchange and commodities.

2012 brings optimism of sustained growth in the domestic market. This, supported by steady energy prices will provide the requisite impetus for our bank's growth which in turn will help the treasury division partner in evolving opportunities generated by the Bank.

International Banking – Financial Institutions Group (FIG)

The Bank's corporate clients have access to international trade and payment products, owing to the strong alliances that Financial Institutions Group division has established with a large network of international banks in GCC, Asia, Europe and America along with local banks and other financial institutions. The Bank's global banking partnerships facilitates corporate clients to avail of a broad spectrum of products and services related to their trade and financing requirements at the opportune time.

> The Bank's global banking partnerships facilitate corporate clients to avail a broad spectrum of products and services related to their trade and financing requirements at the opportune time.

In 2011 the Bank's correspondent banking base was enhanced. This has translated in continued seamless global relationship management and a broad range of products and services to meet the needs of the corporate clients, with the help of the Bank's global partners and a dedicated experienced team.

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-assessment of all risks as part of preparation of ICAAP (Internal Capital Adequacy Assessment Process). This was submitted to the Central Bank of Oman. Following the guidelines received from the Central Bank of Oman, assessment under ICAAP as a trial run will be carried out as recommended. In line with the 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; balancing risk and reward and to bring about further qualitative improvements in credit administration.

Corporate Credit Risk

The division was involved in developing a Corporate Credit Risk Strategy for adopting a structured approach to credit growth and 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 small and mid-sector corporate segment with adequate credit facilities for their business requirements.

The continued stress in the global markets, especially in Europe and USA resulted in an unprecedented downgrading of countries and banks by the rating agencies. The bank took immediate 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 weak credits.

Retail Credit Risk

Credit facilities are offered to retail customers primarily based on Product Programs approved by the Board Risk Committee. The lending criteria were continually revised through a thorough review of the Credit Policy. Credit facilities outside the Product Programs were individually assessed by the Consumer Credit Risk Division and approved as per the delegated authorities.

> The Bank has implemented an automated Loan Collection System in order to enhance its collections and recovery processes. It is also in the process of implementing an automated Loan Origination System.

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 the retail portfolio.

The Bank has implemented an automated Loan Collection System in order to enhance its collections and recovery processes. It is also in the process of implementing an automated Loan Origination System and a Credit Scoring Module to further enhance its Consumer Credit Risk framework.

Liquidity Risk Management

With the continuing turmoil and slow recovery in the international markets, especially in Europe, the Bank continued to face the challenge of managing its liquidity position in view of the restricted availability of long term funding at reasonable rates in both Omani Rials and USD. At the same time, there was a glut of short tenor Omani Rials in the banking system leading to close-to-nil yields on Central Bank of Oman CDs.

There was increased focus on the frequent projection of gaps for both Omani Rials and US Dollars, and based on this, the ALCO (Asset Liability Committee) was able 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 currency gaps and Stress Tests.

> The Bank is planning to implement a new integrated Treasury Front Office, Mid-Office and Back Office System.

Market Risk Management

During the year, the Market Risk division reviewed the investment policies in view of the depressed market conditions, and new limits on trigger levels and volatile securities were introduced in order to better manage the downside risks.

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

Interest Rate Risk in the Banking Book was analyzed at regular frequencies, and presented at 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 planning to implement a new integrated Treasury Front Office, Mid-Office and Back Office system to enhance the capturing the 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 from 3.5% in 2010 to 2.9% in 2011 and enabled the Bank to reclaim an aggregate of RO 11.8 million in recoveries & releases in 2011.

Information Security and Business Continuity Management

Advancing technology and easy to access hacking tools have thrown open new challenges to the banking industry which have been effectively met through enhancements to the information security framework of the bank and through development and implementation of appropriate policies and procedures.

The initiatives undertaken to improve corporate governance include a comprehensive security assessment review of the business application including Symphony the new branch front end system. The information security architecture of the bank was enhanced through implementation of a minimum security baseline for all systems.

The key initiatives on the business continuity readiness included a detailed study on the technology gap analysis of the bank's information technology infrastructure from recovery perspective, review of business impact analysis and upgrade of the branch disaster recovery communication infrastructure to GPRS technology. A focused drive for business continuity awareness was undertaken covering all branches and other operating offices.

Compliance

The Bank's approach to managing compliance is proactive and is premised on specific regulatory requirements in the markets it operates, such as those mandated by the Central Bank of Oman and the Capital Market Authority, as well as internationally accepted principles. The Bank fosters a culture of compliance which is seen not only as a requirement of law but also as a good business practice.

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 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.

Operations

2011 has been a successful and eventful year for the Operations Division for implementing a positive change in the operational services. The division played a key role in supporting the lines of business in their asset expansion endeavor.

The division was actively involved in the implementation of the Loan Origination System (LOS) and the Trade Innovation system. This will improve the turnaround time for retail asset products and trade financing activity.

Investment banking operations provided fund custody and administration support towards new mandates during the year.

Information Technology

Information Technology Division is a strategic and capable business partner helping to shape NBO strategy though a keen understanding of the business goals and contributing to this by leveraging technology to achieve clear business results. ITD is working in partnership with the Business units to shift the technology away from a model based on products, transactions, touch points, and internal departments toward one based on customers, processes, integrated experiences, and the Bank-wide value of information to allow us to exceed our customer's expectations by providing innovative, timely, reliable, cost effective, and secure information technology services.

> 2011 has been a successful and eventful year for the Operations Division for implementing a positive change in the operational service.

The following are some of the deliverables by the Division during 2011:

- Mobile Banking and Online Bill Payments
- Fraud Monitoring System
- Trade Innovation, Loan Origination and Collection System
- Reimbursement Cards
- WINDOWS 7 migration

Human Resources

The year 2011 has been a significant year with several key initiatives undertaken by the Human Resources division (HRD) which continues to remain closely aligned with corporate objectives and business functions.

In 2011, the Human Resource strategic transformation process was conceptualized. This included initiatives such as re-organization of the HR functional Structure, review of HR policies and compensation benefits, etc.

In order to strengthen communication between the staff and the management, the division introduced the HR Help Desk, a bi-monthly HR-Labour Union Forum as well as the HR Executive Committee. The Learning & development strategy was designed towards addressing staff training needs, overall career development of staff and succession plans, while the Organizational Effectiveness/Development section will oversee the

development of competencies, overhauling of Job descriptions, manpower planning and optimization to name a few.

Upgradation to the existing Human Resources Management System is under way and will further improve the overall service deliveries to staff.

Finance

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

During the year, the division played a significant role in the establishment of ICAAP (Internal Capital Adequacy Assessment Process) for the bank. It was also actively involved in cost management, balance sheet management and various bank wide strategic projects, which helped to reduce costs / enhance revenue opportunities. Significant progress was also made in the closure of pending tax assessments.

Key initiatives in 2011 include enhancing the insurance related process resulting in the reduction of turnaround time (TAT) towards better customer service.

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.

Corporate Social Responsibility (CSR) & Corporate Communications

The CSR & Corporate Communications Division plays a pivotal role in supporting the Bank's goals by providing the best service to suit its Stakeholders' needs. The division ensures that the responsibility of managing the impact of social, economic and environmental activities in a way that continues to benefit the bank's business has been gradually integrated into the Bank's practices. Through employee involvement programs, the division also encourages staff to give their time, energy and expertise to benefit local communities.

Internal Audit Function

The Internal audit division is a totally independent function reporting to the Board of Directors through the Board Audit Committee.

The division uses a 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 Bank's policies and plans within the regulatory framework.

It 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 internationally recognized internal audit governance portal that enabled the automation of the audit process from risk assessment through reporting; tie risks to key processes and organizations that feeds 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 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 Compliance division and the Internal Audit division and their recommendations.

Outlook

The Oman economy exudes a positive outlook for 2012, with increased Government expenditure in strategic infrastructure projects boosting economic growth. Large public investment programs by the Government which are under way, include a rail network as well as new air and sea ports. The budget for year 2012, which is based on an oil price of USD 75 per barrel includes a sizeable expenditure in the fields of education and social infrastructure. This will ensure that growth opportunities continue to be available to banks.

In the long term, the Oman economy hinges on economic diversification. The Eight Five Year Development Plan which serves as an economic blueprint for the 2011-15 period, places significant focus on developing several non-hydrocarbons sectors including industry, tourism and agriculture. With Muscat chosen as the Arab Tourism Capital for 2012 by the Arab Tourism Council, this sector is likely to show a further boost in revenues.

Financial decisions taken by the Government in response to certain social requirements has resulted in an increase in the expenditure of the Eighth Five Year Plan by 26%. These include improving living standards and creating new employment opportunities.

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.

In line with its aim of sustainable growth, the bank has during the year established and is in the process of implementation of its strategic plan with respect to financial performance, customer and products, process and service improvements as well as development of its employees.

The bank also plans to launch Islamic Banking as part of its franchise, in the year 2012.

Oman will remain the primary focus in the coming year, as the bank capitalizes on the UAE franchise as an additional service point for its Omani customers. The Egypt operations will continue on a care and maintain basis. 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 2012 with optimism, as continued Government expenditure expects to maintain growth momentum, creating adequate opportunities for the banking sector.

Salaam Al Shaksy
Chief Executive Officer

ERNST & YOUNG

P.O. Box 1750, Ruwi 112
Ernst & Young Building
Qurum
Muscat, Sultanate of Oman
Tel: +968 2455 9559 Fax: +968 2456 6043
muscat@om.ey.com
www.ey.com/me
C.R. No. 1/36809/5
P. R. No. MH/4

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

Report on the Financial Statements

We have audited the accompanying financial statements of National Bank of Oman SAOG ('the bank'), which comprise the statement of financial position as at 31 December 2011, 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.

Board of Director's Responsibility for the Financial Statements

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

Auditor's Responsibility

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's 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 audit opinion.

Opinion

In our opinion, the financial statements present fairly, in all material respects, the financial position of the bank as at 31 December 2011 and its financial performance and cash flows for the year then ended in accordance with International Financial Reporting Standards.

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.

Ernst & Young

23 January 2012
Muscat

Statement of Financial Position As at 31st December 2011

2010 USD'000	**2011 USD'000**		**Notes**	**2011 RO'000**	2010 RO'000
		ASSETS			
591,010	**573,431**	Cash and balances with Central Banks	3	**220,771**	227,539
218,584	**416,997**	Due from banks and other money market placements (net)	4	**160,544**	84,155
3,541,200	**4,339,683**	Loans and advances to customers (net)	5	**1,670,778**	1,363,362
163,982	**246,810**	Non-trading financial investments	6	**95,022**	63,133
58,060	**53,260**	Premises and equipment	7	**20,505**	22,353
18	**1,252**	Deferred tax asset	12	**482**	7
115,208	**158,365**	Other assets	8	**60,970**	44,355
4,688,062	**5,789,798**	**TOTAL ASSETS**		**2,229,072**	1,804,904
		LIABILITIES, SUBORDINATED DEBT AND EQUITY			
		LIABILITIES			
343,753	**579,608**	Due to banks and other money market deposits	9	**223,149**	132,345
3,441,273	**4,155,387**	Customers' deposits	10	**1,599,824**	1,324,890
122,297	**168,655**	Other liabilities	11	**64,932**	47,084
10,844	**13,610**	Taxation	12	**5,240**	4,175
3,918,167	**4,917,260**	**TOTAL LIABILITIES**		**1,893,145**	1,508,494
		SUBORDINATED DEBT			
79,481	**142,078**	Subordinated debt	13	**54,700**	30,600
		EQUITY			
280,779	**280,779**	Share capital	14	**108,100**	108,100
89,519	**89,519**	Share premium	15	**34,465**	34,465
91,927	**100,369**	Legal reserve	16	**38,642**	35,392
11,478	**11,478**	General reserve	17	**4,419**	4,419
38,306	**47,527**	Other non-distributable reserves	18	**18,298**	14,748
42,117	**49,138**	Proposed cash dividend	19	**18,918**	16,215
-	**7,021**	Proposed stock dividend	19	**2,703**	-
136,288	**144,629**	Retained earnings		**55,682**	52,471
690,414	**730,460**	**TOTAL EQUITY**		**281,227**	265,810
4,688,062	**5,789,798**	**TOTAL LIABILITIES, SUBORDINATED DEBT AND EQUITY**		**2,229,072**	1,804,904

The financial statements were authorised for issue on 23rd January 2012 in accordance with a resolution of the Board of Directors.

Chairman **Chief Executive Officer**

The attached notes 1 to 33 form part of these financial statements.

2010 USD'000	2011 USD'000		Notes	2011 RO'000	2010 RO'000
247,205	**242,483**	Interest income	21	**93,356**	95,174
(102,722)	**(91,348)**	Interest expense	22	**(35,169)**	(39,548)
144,483	**151,135**	Net interest income		**58,187**	55,626
58,416	**88,436**	Other operating income	23	**34,048**	22,490
202,899	**239,571**	**OPERATING INCOME**		**92,235**	78,116
		OPERATING EXPENSES			
(59,322)	**(64,624)**	Staff costs		**(24,880)**	(22,839)
(34,520)	**(37,322)**	Other operating expenses	24	**(14,369)**	(13,290)
(9,922)	**(10,927)**	Depreciation	7	**(4,207)**	(3,820)
(103,764)	**(112,873)**			**(43,456)**	(39,949)
99,135	**126,698**	**PROFIT FROM OPERATIONS BEFORE IMPAIRMENT LOSSES AND TAX**		**48,779**	38,167
(41,249)	**(49,174)**	Credit loss expense – customers' loan	5	**(18,932)**	(15,881)
11,026	**19,546**	Recoveries and releases from provision for credit losses	5	**7,525**	4,245
10,455	**11,236**	Recoveries from loans and advances written off		**4,326**	4,025
800	**-**	Recoveries/releases from provision for credit losses on banks		**-**	308
(1,631)	**(5,943)**	Impairment losses on available for sale investments	6	**(2,288)**	(628)
-	**(1,849)**	Provision – others		**(712)**	-
(20,599)	**(26,184)**	TOTAL IMPAIRMENT LOSSES (NET)		**(10,081)**	(7,931)
78,536	**100,514**	**PROFIT BEFORE TAX**		**38,698**	30,236
(7,961)	**(11,678)**	Taxation	12	**(4,496)**	(3,065)
70,575	**88,836**	**PROFIT FOR THE YEAR**		**34,202**	27,171
		OTHER COMPREHENSIVE INCOME			
306	**(6,750)**	Net movement on available for sale investments		**(2,599)**	118
2,481	**-**	Surplus on revaluation of building		**-**	955
338	**-**	Net movement on cash flow hedge		**-**	130
44	**75**	Tax effect of net results on available for sale financial investments		**29**	17
3,169	**(6,675)**	**OTHER COMPREHENSIVE (EXPENSE) INCOME FOR THE YEAR**		**(2,570)**	1,220
73,744	**82,161**	**TOTAL COMPREHENSIVE INCOME FOR THE YEAR**		**31,632**	28,391
		Earnings per share:			
0.06	**0.08**	Basic and diluted, profit for the year attributable to equity holders	26	**0.032**	0.025

The attached notes 1 to 33 form part of these financial statements.

(RO'000)	Share capital (note 14)	Share premium (note 15)	Legal reserve (note 16)	General reserve (note 17)	Other non-distributable reserves (note 18)	Proposed cash dividend (note 19)	Proposed stock dividend (note 19)	Retained earnings	Total
Balance at 1 January 2010	108,100	34,465	32,675	4,419	8,008	12,972	-	49,752	250,391
Total comprehensive income for the year	-	-	-	-	1,220	-	-	27,171	28,391
Transfer to subordinated debt reserve	-	-	-	-	5,520	-	-	(5,520)	-
Transfer to legal reserve	-	-	2,717	-	-	-	-	(2,717)	-
Proposed dividend	-	-	-	-	-	16,215	-	(16,215)	-
Dividend paid	-	-	-	-	-	(12,972)	-	-	(12,972)
Balance at 31 December 2010	108,100	34,465	35,392	4,419	14,748	16,215	-	52,471	265,810
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	**-**	**-**	**-**	**-**	**(2,570)**	**-**	**-**	**34,202**	**31,632**
Transfer to subordinated debt reserve	**-**	**-**	**-**	**-**	**6,120**	**-**	**-**	**(6,120)**	**-**
Transfer to legal reserve	**-**	**-**	**3,250**	**-**	**-**	**-**	**-**	**(3,250)**	**-**
Dividend paid	**-**	**-**	**-**	**-**	**-**	**(16,215)**	**-**	**-**	**(16,215)**
Proposed cash dividend	**-**	**-**	**-**	**-**	**-**	**18,918**	**-**	**(18,918)**	**-**
Proposed stock dividend	**-**	**-**	**-**	**-**	**-**	**-**	**2,703**	**(2,703)**	**-**
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 2011 – In USD'000	280,779	89,519	91,927	11,478	38,306	42,117	-	136,288	690,414
Balance at 31 December 2011 – In USD'000	**280,779**	**89,519**	**100,369**	**11,478**	**47,527**	**49,138**	**7,021**	**144,629**	**730,460**

The attached notes 1 to 33 form part of these financial statements.

2010 USD'000	2011 USD'000		Notes	2011 RO'000	2010 RO'000
		OPERATING ACTIVITIES			
78,536	**100,514**	Profit before taxation		**38,698**	30,236
		Adjustments for:			
9,922	**10,927**	Depreciation	7	**4,207**	3,820
2,304	**(15,836)**	Provision for credit losses (net)		**(6,097)**	887
1,631	**5,943**	Impairment losses on available for sale investments	6	**2,288**	628
(3,779)	**-**	Impairment losses and interest reserve on bank loans		**-**	(1,455)
-	**1,177**	Provision against collateral assets		**453**	-
-	**(694)**	Profit on sale of equipment (net)		**(267)**	-
(2,997)	**(2,130)**	Profit on sale of investments	23	**(820)**	(1,154)
(4,237)	**(7,488)**	Investment income		**(2,883)**	(1,631)
81,380	**92,413**	Operating profit before changes in operating assets and liabilities		**35,579**	31,331
80,675	**855**	Due from banks and other money market placements		**329**	31,060
(154,912)	**18,000**	Due to banks and other money market deposits		**6,930**	(59,641)
(8,447)	**(782,647)**	Loans and advances to customers		**(301,319)**	(3,252)
45,153	**-**	Financial assets at fair value through profit or loss		**-**	17,384
(48,361)	**(44,314)**	Other assets		**(17,061)**	(18,619)
166,551	**714,114**	Customers' deposits		**274,934**	64,122
32,166	**46,358**	Other liabilities		**17,848**	12,384
1,984	**-**	Deposit with Central Bank of Oman		**-**	764
196,189	**44,779**	**Cash from operations**		**17,240**	75,533
(10,151)	**(9,990)**	Taxes paid		**(3,846)**	(3,908)
186,038	**34,789**	**Net cash from operating activities**		**13,394**	71,625
		INVESTING ACTIVITIES			
(109,861)	**(115,877)**	Purchase of non-trading investments		**(44,613)**	(42,296)
25,639	**22,244**	Proceeds from sale of non-trading investments		**8,564**	9,871
(32,537)	**(6,629)**	Purchase of premises and equipment	7	**(2,552)**	(12,527)
107	**1,151**	Disposal of premises and equipment		**443**	41
3,156	**3,990**	Income from bond and other investments	23	**1,536**	1,215
1,081	**3,498**	Dividend income	23	**1,347**	416
(96)	**185**	Translation differences on premises and equipment and tax		**71**	(37)
(112,511)	**(91,438)**	Net cash used in investing activities		**(35,204)**	(43,317)
		FINANCING ACTIVITIES			
(33,694)	**(42,117)**	Payment of dividend		**(16,215)**	(12,972)
7,792	**62,597**	Net movement in subordinated debt	13	**24,100**	3,000
(25,902)	**20,480**	Net cash from (used in) financing activities		**7,885**	(9,972)
47,625	**(36,169)**	**(DECREASE) INCREASE IN CASH AND CASH EQUIVALENTS**		**(13,925)**	18,336
702,626	**750,251**	Cash and cash equivalents at the beginning of the year		**288,847**	270,511
750,251	**714,082**	**CASH AND CASH EQUIVALENTS AT THE END OF THE YEAR**		**274,922**	288,847
		REPRESENTING:			
589,711	**572,132**	Cash and balances with Central Banks	3	**220,271**	227,039
160,540	**141,950**	Deposits and balances with other banks and financial institutions (net)		**54,651**	61,808
750,251	**714,082**			**274,922**	288,847

The attached notes 1 to 33 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, corporate 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 1,339 employees as at 31 December 2011 (2010: 1,306).

2 ACCOUNTING POLICIES

2.1 Basis of preparation

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 fair value through profit and loss.

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.

2.2 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.

2.3 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.

2 ACCOUNTING POLICIES (continued)

2.3 Significant accounting judgments and estimates (continued)

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.), concentrations of risks and economic data (including levels of unemployment, real estate prices indices and the performance of different individual groups).

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.

Deferred tax assets

Deferred tax assets are recognised for all unused tax losses to the extent that it is probable that taxable profit will be available against which the losses can be utilised. Significant management judgment is required to determine the amount of deferred tax assets that can be recognised, based upon the likely timing and level of future taxable profits together with future tax planning strategies.

2.4 Change in accounting policies and disclosures

The accounting policies are consistent with those used in the previous financial year except as follows:

The bank has adopted the following new and amended IFRS and IFRIC interpretations as of 1 January 2011:

- IAS 24 Related Party Transactions (Amendment)
- IAS 32 Financial Instruments: Presentation – Classification of Rights Issues (Amendment)
- IFRIC 19 Extinguishing Financial Liabilities with Equity Instruments
- Improvements to IFRSs (May 2010)

The adoption of the standards or interpretations applicable to the bank is described below:

IAS 24 Related Party Transactions (Amendment)

The IASB issued an amendment to IAS 24 that clarifies the definitions of a related party. The new definitions emphasise a symmetrical view of related party relationships and clarifies the circumstances in which persons and key management personnel affect related party relationships of an entity. In addition, the amendment introduces an exemption from the general related party disclosure requirements for transactions with government and entities that are controlled, jointly controlled or significantly influenced by the same government as the reporting entity. The adoption of the amendment did not have any impact on the financial position or performance of the bank.

IAS 32 Financial Instruments: Presentation – Classification of Rights Issues (Amendment)

The IASB issued an amendment to IAS 32 that clarifies definition of a financial liability in order to classify rights issues (and certain options or warrants) as equity instruments in cases where such rights are given pro rata to all of the existing owners of the same class of an entity's non-derivative equity instruments, or to acquire a fixed number of the entity's own equity instruments for a fixed amount in any currency. The adoption of the amendment did not have any impact on the financial position or performance of the bank.

2 ACCOUNTING POLICIES (continued)

2.4 Change in accounting policies (continued)

IFRIC 19 Extinguishing Financial Liabilities with Equity Instruments

In November 2009, the IASB issued IFRIC 19 Extinguishing Financial Liabilities with Equity. The interpretation clarifies that equity instruments issued to a creditor to extinguish a financial liability qualify as consideration paid. The equity instruments issued are measured at their fair value. In case that this cannot be reliably measured, the instruments are measured at the fair value of the liability extinguished. Any gain or loss is recognised immediately in profit or loss. The adoption of this interpretation has had no effect on the financial statements of the bank.

Improvements to IFRSs

In May 2010, the IASB issued its third omnibus of amendments to its standards, primarily with a view to removing the inconsistencies and clarifying the wordings. There are separate transitional provisions for each standard. The amendments resulting from improvements to IFRSs did not have any significant impact on the accounting policies, financial positions or performance of the bank.

Standards issued but not yet effective:

Standards issued but not yet effective up to the date of issuance of the bank's financial statements are listed below. This listing of standards and interpretations issued are those that the bank reasonably expects to have an impact on disclosures, financial position or performance when applied at a future date. The bank intends to adopt these standards when they become effective.

IAS 1 Financial Statement Presentation – Presentation of Items of Other Comprehensive Income (OCI)

The amendments to IAS 1 change the grouping of items presented in OCI. Items that could be reclassified (or recycled) to profit or loss at a future point in time (for example, upon derecognition or settlement) would be presented separately from items that will never be reclassified. The amendment affects presentation only and has no impact on the bank's financial position.

IFRS 7 Financial Instruments: Disclosures — Enhanced Derecognition Disclosure Requirements

The amendment requires additional disclosure about financial assets that have been transferred but not derecognised to enable the user of the bank's financial statements to understand the relationship with those assets that have not been derecognised and their associated liabilities. In addition, the amendment requires disclosures about continuing involvement in derecognised assets to enable the user to evaluate the nature of, and risks associated with, the entity's continuing involvement in those derecognised assets. The amendment becomes effective for annual periods beginning on or after 1 July 2011. The amendment affects disclosure only and will have no impact on the bank's financial position or performance.

IFRS 9 Financial Instruments: Classification and Measurement

IFRS 9 as issued reflects the first phase of the IASBs work on the replacement of IAS 39 and applies to classification and measurement of financial assets and financial liabilities as defined in IAS 39. The standard is effective for annual periods beginning on or after 1 January 2015. In subsequent phases, the IASB will address hedge accounting and impairment of financial assets. The completion of this project is expected over the first half of 2012. The adoption of the first phase of IFRS 9 will have an effect on the classification and measurement of the bank's financial assets and liabilities. The bank will quantify the effect in conjunction with the other phases, when issued, to present a comprehensive picture.

IFRS 13 Fair Value Measurement

IFRS 13 establishes a single source of guidance under IFRS for all fair value measurements. IFRS 13 does not change when an entity is required to use fair value, but rather provides guidance on how to measure fair value under IFRS when fair value is required or permitted. The bank is currently assessing the impact that this standard will have on the financial position and performance. This standard becomes effective for annual periods beginning on or after 1 January 2013.

2 ACCOUNTING POLICIES (continued)

2.5 Summary of 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.

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.

2 ACCOUNTING POLICIES (continued)

Available for sale (continued)

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.

2 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

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.

2 ACCOUNTING POLICIES (continued)

Taxation (continued)

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.

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.

Cash flow hedges

For designated and qualifying cash flow hedges, the effective portion of the gain or loss on the hedging instrument is initially recognised directly in equity in the cash flow hedge reserve. The ineffective portion of the gain or loss on the hedging instrument is recognised immediately in profit or loss for the the year.

When the hedged cash flow affects the profit or loss, the gain or loss on the hedging instrument is ‘recycled’ in the corresponding income or expense line of the profit or loss for the year . When a hedging instrument expires, or is sold, terminated, exercised, or when a hedge no longer meets the criteria for hedge accounting, any cumulative gain or loss existing in equity at that time remains in equity and is recognised when the hedged forecast transaction is ultimately recognised in the profit or loss for the year. When a forecast transaction is no longer expected to occur, the cumulative gain or loss that was reported in equity is immediately transferred to 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.

2 ACCOUNTING POLICIES (continued)

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 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.

2 ACCOUNTING POLICIES (continued)

Impairment of financial assets (continued)

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 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.

2 ACCOUNTING POLICIES (continued)

Fee and commission income (continued)

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.

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 Omani employees are provided in accordance with the Sultanate of Oman's Social Insurance Law of 1991. For Egyptian employees the terminal benefits are provided in accordance with the Egyptian social security law. Provision for staff terminal benefits is the amount of future benefit that employees have earned in return for their service in the current and prior periods, discounted to its present value.

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.

2 ACCOUNTING POLICIES (continued)

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.

3 CASH AND BALANCES WITH CENTRAL BANKS

2010 USD'000	**2011 USD'000**		**2011 RO'000**	2010 RO'000
91,104	**66,974**	Cash	**25,785**	35,075
6,029	**14,919**	Treasury bills with Central Banks	**5,744**	2,321
116,883	**233,766**	Certificates of deposit with the Central Banks	**90,000**	45,000
375,695	**256,473**	Other balances with the Central Banks	**98,742**	144,643
589,711	**572,132**	**Cash and cash equivalents**	**220,271**	227,039
1,299	**1,299**	Capital deposit with the Central Bank of Oman	**500**	500
591,010	**573,431**	**Cash and balances with Central Banks**	**220,771**	227,539

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

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

2010 USD'000	**2011 USD'000**		**2011 RO'000**	2010 RO'000
58,343	**59,657**	Loans and advances to banks	**22,968**	22,462
150,260	**330,257**	Placement with banks	**127,149**	57,850
27,098	**44,200**	Demand balances	**17,017**	10,433
235,701	**434,114**	**Due from banks and other money market placements**	**167,134**	90,745
(16,940)	**(16,940)**	Less: allowance for credit losses (refer note below)	**(6,522)**	(6,522)
(177)	**(177)**	Less: reserved interest	**(68)**	(68)
218,584	**416,997**	**Net due from banks and other money market placements**	**160,544**	84,155

As at 31 December 2011 the bank has a limited inter-bank exposure of 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.

5 LOANS AND ADVANCES TO CUSTOMERS (NET)

2010 USD'000	**2011 USD'000**		**2011 RO'000**	2010 RO'000
154,223	**111,821**	Overdrafts	**43,051**	59,376
1,675,447	**2,026,681**	Personal loans	**780,272**	645,047
1,771,626	**2,213,052**	Other loans	**852,025**	682,076
97,426	**100,579**	Loans against trust receipts	**38,723**	37,509
21,717	**50,953**	Bills discounted	**19,617**	8,361
3,720,439	**4,503,086**	**Gross loans and advances**	**1,733,688**	1,432,369
(149,257)	**(128,460)**	Allowance for credit losses	**(49,457)**	(57,464)
(29,982)	**(34,943)**	Reserved interest	**(13,453)**	(11,543)
3,541,200	**4,339,683**	**Net loans and advances**	**1,670,778**	1,363,362

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

2010 USD'000	**2011 USD'000**		**2011 RO'000**	2010 RO'000
		Allowance for credit losses		
149,561	**149,257**	Balance at beginning of the year	**57,464**	57,581
41,249	**49,174**	Provided during the year	**18,932**	15,881
(10,374)	**(18,382)**	Released/recovered during the year	**(7,077)**	(3,994)
(29,855)	**(39,561)**	Written off during the year	**(15,231)**	(11,494)
-	**(11,416)**	Transfer during the year	**(4,395)**	-
(1,324)	**(612)**	Translation difference	**(236)**	(510)
149,257	**128,460**	**Balance at end of the year**	**49,457**	57,464
		Reserved interest		
27,374	**29,982**	Balance at beginning of the year	**11,543**	10,539
9,984	**8,951**	Reserved during the year	**3,446**	3,844
(652)	**(1,164)**	Released/recovered during the year	**(448)**	(251)
(1,810)	**(400)**	Released/recovered during the year to interest income	**(154)**	(697)
(4,896)	**(2,413)**	Written off during the year	**(929)**	(1,885)
(18)	**(13)**	Translation difference	**(5)**	(7)
29,982	**34,943**	**Balance at end of the year**	**13,453**	11,543

5 LOANS AND ADVANCES TO CUSTOMERS (NET) (Continued)

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

2010 USD'000	2011 USD'000		2011 RO'000	2010 RO'000
97,195	**64,735**	Specific impairment	**24,923**	37,420
52,062	**63,725**	Collective impairment	**24,534**	20,044
149,257	**128,460**	**Balance at end of the year**	**49,457**	57,464

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 2011, loans and advances on which interest is not being accrued or where interest has been reserved amounted to RO 64 million – USD 166.2 million (2010 – RO 61.3 million – USD 159.2 million).

During the year, the bank has written-off fully provided loans and advances amounting to RO 16.2 million – USD 42.1 million (2010: RO 13.4 million – USD 34.8 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.

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

Total 2010 USD'000	Total 2011 USD'000		Total 2011 RO'000	Total 2010 RO'000
1,675,447	**2,026,681**	Personal	**780,272**	645,047
457,681	**477,039**	Manufacturing	**183,660**	176,207
16,964	**325,484**	Transport and communication	**125,312**	6,531
356,644	**322,813**	Construction	**124,283**	137,308
194,870	**287,558**	Wholesale and retail trade	**110,710**	75,025
213,272	**257,901**	Others	**99,291**	82,110
190,447	**254,520**	Service	**97,990**	73,322
228,639	**250,940**	Financial institutions	**96,612**	88,026
52,930	**94,473**	Mining and quarrying	**36,372**	20,378
92,262	**90,340**	Import trade	**34,781**	35,521
209,023	**82,735**	Electricity, gas and water	**31,853**	80,474
30,917	**31,574**	Agriculture	**12,156**	11,903
1,242	**1,010**	Export trade	**389**	478
101	**18**	Government	**7**	39
3,720,439	**4,503,086**	**Total**	**1,733,688**	1,432,369

5 LOANS AND ADVANCES TO CUSTOMERS (NET) (Continued)

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

	Retail and personal loans RO'000	Business and Government RO'000	Real estate loans RO'000	2011 Total RO'000	2010 Total RO'000
Sultanate of Oman	**776,998**	**702,174**	**171,042**	**1,650,214**	1,335,829
United Arab Emirates	**2,118**	**49,392**	**6,660**	**58,170**	64,651
Egypt	**1,156**	**2,126**	**-**	**3,282**	11,011
Others	**-**	**12,725**	**9,297**	**22,022**	20,878
Total – 31 December 2011	**780,272**	**766,417**	**186,999**	**1,733,688**	1,432,369
Total – 31 December 2010	645,047	592,829	194,493	-	1,432,369

	Retail and personal loans USD'000	Business and Government USD'000	Real estate loans USD'000	2011 Total USD'000	2010 Total USD'000
Sultanate of Oman	**2,018,177**	**1,823,829**	**444,265**	**4,286,271**	3,469,686
United Arab Emirates	**5,501**	**128,291**	**17,299**	**151,091**	167,925
Egypt	**3,003**	**5,522**	**-**	**8,525**	28,600
Others	**-**	**33,051**	**24,148**	**57,199**	54,228
Total – 31 December 2011	**2,026,681**	**1,990,693**	**485,712**	**4,503,086**	3,720,439
Total – 31 December 2010	1,675,447	1,539,816	505,176	-	3,720,439

6 NON-TRADING FINANCIAL INVESTMENTS

	Carrying value 31/12/2011 RO'000	Cost 31/12/2011 RO'000	Carrying value 31/12/2010 RO'000	Cost 31/12/2010 RO'000
Available for sale investments				
Quoted investments - Oman				
Banking and investment sector	**1,347**	**1,464**	185	190
Industry sector	**1,692**	**2,384**	1,723	1,763
Service sector	**6,884**	**8,004**	7,998	8,706
Government development bonds	**74,405**	**74,405**	43,101	43,101
	84,328	**86,257**	53,007	53,760
Quoted investments – Foreign				
Banking and investment sector	**-**	**-**	1,422	1,363
Government development bonds	**3,649**	**3,830**	995	995
	3,649	**3,830**	2,417	2,358
Unquoted investments				
Banking and investment sector	**6,776**	**7,386**	7,643	6,636
Service sector	**269**	**269**	66	66
	7,045	**7,655**	7,709	6,702
Total available for sale investments	**95,022**	**97,742**	63,133	62,820
Total non-trading investments – USD'000	**246,810**	**253,875**	163,982	163,169

6 NON-TRADING FINANCIAL INVESTMENTS (Continued)

Included under unquoted available for sale investments are investments with a value of RO 0.40 million – USD 1.05 million (2010 – RO 0.20 million – USD 0.52 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 2.29 million - USD 5.94 million (2010 – RO 0.63 million – USD 1.63 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.

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 2011	**Bank's portfolio %**	**Carrying value RO'000**	**Cost RO'000**
Government development bonds-Oman	**78.30**	**74,405**	**74,405**

31 December 2010	Bank's portfolio %	Carrying value RO'000	Cost RO'000
Government development bonds-Oman	68.27	43,101	43,101
Investment stabilization fund	10.08	6,365	5,000

7 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 2011, net of accumulated				
depreciation	14,513	5,720	2,120	22,353
Additions	60	731	1,761	2,552
Disposals	(20)	(62)	(93)	(175)
Transfers	302	2,498	(2,800)	-
Translation difference	(16)	(2)	-	(18)
Depreciation	(1,830)	(2,377)	-	(4,207)
Balance as at 31 December 2011, net of accumulated depreciation	**13,009**	**6,508**	**988**	**20,505**
At cost	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**
Net carrying value at 31 December 2010	14,513	5,720	2,120	22,353
Net carrying value at 31 December 2010 – USD'000	37,696	14,857	5,507	58,060

7 PREMISES AND EQUIPMENT (Continued)

Freehold land stated at cost of RO 8.56 million - USD 22.22 million (2010 - 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 existing value of RO 2.81 million (USD 7.30 million). On revaluation, the gross carrying amount of each building revalued 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 1.12 million – USD 2.91 million (2010 - RO 1.39 million – USD 3.61million)

8 OTHER ASSETS

2010 USD'000	2011 USD'000		2011 RO'000	2010 RO'000
52,115	**59,811**	Interest receivable and others	**23,027**	20,064
12,145	**28,681**	Positive fair value of derivatives (note 32)	**11,042**	4,676
50,948	**69,873**	Customers' indebtedness for acceptances	**26,901**	19,615
115,208	**158,365**		**60,970**	44,355
8,982	**8,982**	Amount receivable from BCCI	**3,458**	3,458
(8,982)	**(8,982)**	Less: provision for amount due from BCCI	**(3,458)**	(3,458)
-	**-**		**-**	-

The Government of the Sultanate of Oman has agreed, unconditionally, to guarantee payments of all and any sums, which are due to the bank by Bank of Credit and Commerce International (BCCI) up to a maximum of RO 38.9 million (USD 101.0 million). BCCI is in liquidation.

On 7 July 2008, the bank has cancelled and returned the guarantee to the Government discharging it of all related liabilities. Full impairment provision has been recorded by the bank against the remaining amounts due from BCCI.

During the year, receivable amounting to RO 4.4 million was written off against provision held.

9 DUE TO BANKS AND OTHER MONEY MARKET DEPOSITS

2010 USD'000	2011 USD'000		2011 RO'000	2010 RO'000
325,000	**549,223**	Acceptances and borrowings	**211,451**	125,125
18,753	**30,385**	Other balances	**11,698**	7,220
343,753	**579,608**		**223,149**	132,345

10 CUSTOMERS' DEPOSITS

2010 USD'000	2011 USD'000		2011 RO'000	2010 RO'000
774,538	**810,584**	Current accounts	**312,075**	298,197
777,441	**978,899**	Savings accounts	**376,876**	299,315
1,726,904	**2,258,631**	Term deposits	**869,573**	664,858
162,390	**107,273**	Certificates of deposit	**41,300**	62,520
3,441,273	**4,155,387**		**1,599,824**	1,324,890

11 OTHER LIABILITIES

2010 USD'000	2011 USD'000		2011 RO'000	2010 RO'000
56,108	**67,436**	Interest payable and others	**25,963**	21,601
2,875	**2,629**	Staff entitlements	**1,012**	1,107
50,948	**69,873**	Liabilities under acceptances	**26,901**	19,615
12,366	**28,717**	Negative fair value of derivatives (note 32)	**11,056**	4,761
122,297	**168,655**		**64,932**	47,084
		Staff entitlements are as follows:		
2,501	**2,291**	End of service benefits	**882**	963
374	**338**	Other liabilities	**130**	144
2,875	**2,629**		**1,012**	1,107
		Movement in the end of service benefits liability are as follows:		
2,213	**2,501**	Liability as at 1 January	**963**	852
568	**494**	Expense recognised in the statement of comprehensive income	**190**	219
(280)	**(704)**	End of service benefits paid	**(271)**	(108)
2,501	**2,291**	**Liability as at 31 December**	**882**	963

12 TAXATION

2010 USD'000	2011 USD'000		2011 RO'000	2010 RO'000
		Current tax expense		
7,961	**12,836**	Current year	**4,942**	3,065
-	**(1,158)**	Deferred tax adjustment	**(446)**	-
7,961	**11,678**		**4,496**	3,065

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 is reconciliation between income tax calculated on accounting profits with income tax expense for the year:

12 TAXATION (Continued)

2010 USD'000	2011 USD'000		2011 RO'000	2010 RO'000
78,536	**100,514**	Accounting profit	**38,698**	30,236
9,423	**12,062**	Tax at applicable rate	**4,644**	3,628
470	**1,364**	Non-deductible expenses	**525**	181
(1,215)	**(917)**	Tax exempt revenues	**(353)**	(468)
(717)	**(831)**	Others	**(320)**	(276)
7,961	**11,678**		**4,496**	3,065

The bank's liabilities for taxation in the Sultanate of Oman has been assessed up to the year ended 31 December 2006. The assessment for tax year 2007 has been finalized but yet to be received.

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 2010.

2010 USD'000	2011 USD'000		2011 RO'000	2010 RO'000
		Tax liability		
		Current year		
7,961	**12,836**	Income tax and other taxes	**4,942**	3,065
		Prior year		
2,883	**774**	Income tax and other taxes	**298**	1,110
10,844	**13,610**		**5,240**	4,175

Recognised deferred tax assets:

2010 USD'000	2011 USD'000		2011 RO'000	2010 RO'000
		Deferred tax assets are attributable to the following:		
-	**1,158**	Timing differences Provisions	**446**	-
18	**94**	Available for sale investments - Overseas	**36**	7
18	**1,252**		**482**	7

Deferred tax is calculated at 12% (2010 – 12%).

13 SUBORDINATED DEBT

2010 USD'000	2011 USD'000		2011 RO'000	2010 RO'000
71,688	**79,481**	At I January	**30,600**	27,600
7,793	**62,597**	Received during the year	**24,100**	3,000
79,481	**142,078**		**54,700**	30,600

(i) Placements received in 2011 are repayable in October and November 2017.

(ii) Placements received in 2010 are repayable in January 2016.

14 SHARE CAPITAL

2010 USD'000	2011 USD'000		2011 RO'000	2010 RO'000
415,584	415,584	Authorised - ordinary shares of RO 0.100 each	**160,000**	160,000
280,779	280,779	Issued and fully paid - ordinary shares of RO 0.100 each	**108,100**	108,100

As of 31 December 2011, the following shareholders held 10% or more of the bank's capital:

	Number of shares '000	% Holding
The Commercial Bank of Qatar	**377,267**	**34.90%**
Suhail Bahwan Group (Holdings) L.L.C	**159,385**	**14.74%**

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

15 SHARE PREMIUM RESERVE

The share premium of RO 34.5 million (USD 89.6 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.

16 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 2011 the legal reserve of Oman has reached one third of the issued capital.

17 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.

18 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 2011	2,242	3,766	8,740	14,748
Net movement on available for sale investments	(2,599)	-	-	(2,599)
Tax effect of net losses on available for sale financial investments	29	-	-	29
Transfer to subordinated debt reserve	-	-	6,120	6,120
At 31 December 2011	**(328)**	**3,766**	**14,860**	**18,298**
At 31 December 2011 – In USD'000	**(852)**	**9,782**	**38,597**	**47,527**

(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 13). The reserve is available for transfer back to retained earning upon maturity of the private placement.

19 DIVIDENDS PAID AND PROPOSED

The Board of Directors have proposed 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, which is subject to the approval of the shareholders at the Annual General Meeting to be held in March 2012.

At the Annual General Meeting held in March 2011, a cash dividend of RO 0.015 per share totalling RO 16.2 million (USD 0.039 per share totalling USD 42.1 million) for the year ended 31 December 2010 was approved and subsequently paid.

20 CONTINGENT LIABILITIES AND COMMITMENTS

To meet the financial needs of customers, the bank enters into various irrevocable 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.

20 CONTINGENT LIABILITIES AND COMMITMENTS (Continued)

Contingent liabilities

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

2010 USD'000	2011 USD'000		2011 RO'000	2010 RO'000
1,015,678	**1,134,769**	Guarantees	**436,886**	391,036
212,745	**184,229**	Documentary letters of credit	**70,928**	81,907
1,228,423	**1,318,998**		**507,814**	472,943

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

2010 USD'000	2011 USD'000		2011 RO'000	2010 RO'000
544,434	**548,179**	Financial institutions	**211,049**	209,607
318,805	**302,369**	Construction	**116,412**	122,740
17,405	**129,481**	Electricity, gas and water	**49,850**	6,701
76,109	**96,709**	Wholesale and retail trade	**37,233**	29,302
103,966	**92,192**	Manufacturing	**35,494**	40,027
105,266	**65,351**	Others	**25,160**	40,527
7,639	**45,875**	Transport and communication	**17,662**	2,941
43,249	**27,961**	Service	**10,765**	16,651
9,932	**9,810**	Mining and Quarrying	**3,777**	3,824
1,078	**421**	Agriculture	**162**	415
475	**356**	Personal	**137**	183
65	**294**	Import trade	**113**	25
1,228,423	**1,318,998**		**507,814**	472,943

Guarantees include RO 0.1 million – USD 0.3 million (Dec 2010: RO 0.1 million – USD 0.3 million) relating to non-performing loans.

Commitments

2010 USD'000	2011 USD'000		2011 RO'000	2010 RO'000
268,616	**197,977**	Undrawn commitment	**76,221**	103,417
3,400	**735**	Capital expenditure	**283**	1,309
7,566	**8,114**	Operating lease commitments	**3,124**	2,913
		Future minimum lease payments:		
3,008	**3,312**	Not later than one year at the reporting date	**1,275**	1,158
4,301	**4,558**	Later than one year and not later than five years at the reporting date	**1,755**	1,656
257	**244**	Later than five years	**94**	99
7,566	**8,114**	Aggregate operating lease expenditure contracted for at the reporting date	**3,124**	2,913

20 CONTINGENT LIABILITIES AND COMMITMENTS (Continued)

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.

2010 USD'000	2011 USD'000		2011 RO'000	2010 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 2011 held on trust for customers amounts to RO 50.40 million – USD 130.91 million (2010 – RO 53.95 million – USD 140.13 million).

21 INTEREST INCOME

2010 USD'000	2011 USD'000		2011 RO'000	2010 RO'000
241,699	**237,631**	Interest from customers	**91,488**	93,054
5,506	**4,852**	Interest from banks	**1,868**	2,120
247,205	**242,483**		**93,356**	95,174

Interest bearing assets, other than investments earned interest at an overall effective annual rate of 5.31% for the year ended 31 December 2011 (31 December 2010 – 5.92%).

22 INTEREST EXPENSE

2010 USD'000	2011 USD'000		2011 RO'000	2010 RO'000
97,179	**87,618**	Interest to customers	**33,733**	37,414
5,543	**3,730**	Interest to banks	**1,436**	2,134
102,722	**91,348**		**35,169**	39,548

For the year ended 31 December 2011, the average overall effective annual cost of bank's funds was 2.13% (31 December 2010 – 2.64%).

23 OTHER OPERATING INCOME

2010 USD'000	2011 USD'000		2011 RO'000	2010 RO'000
24,774	**26,995**	Fees and commission income	**10,393**	9,538
(47)	**(47)**	Fees and commission expense	**(18)**	(18)
24,727	**26,948**	Net fees and commissions	**10,375**	9,520
19,592	**42,016**	Service charges	**16,176**	7,543
2,997	**2,130**	Profit on sale of investments	**820**	1,154
6,369	**8,005**	Net gains from foreign exchange dealings	**3,082**	2,452
494	**1,849**	Miscellaneous income	**712**	190
3,156	**3,990**	Income from bonds and others	**1,536**	1,215
1,081	**3,498**	Dividend income	**1,347**	416
58,416	**88,436**		**34,048**	22,490

24 OTHER OPERATING EXPENSES

2010 USD'000	2011 USD'000		2011 RO'000	2010 RO'000
11,397	**12,262**	Establishment costs	**4,721**	4,388
22,759	**24,707**	Operating and administration costs	**9,512**	8,762
364	**353**	Directors' remuneration	**136**	140
34,520	**37,322**		**14,369**	13,290

25 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 during the past 6 years, the Commercial Bank of Qatar advised NBO that they do not wish to 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:

	2011			2010		
	Principal shareholder RO'000	**Others RO'000**	**Total RO'000**	Principal shareholder RO'000	Others RO'000	Total RO'000
Loans and advances	**-**	**33,398**	**33,398**	-	28,695	28,695
Customer's deposits	**-**	**9,353**	**9,353**	-	13,899	13,899
Due from banks	**14**	**-**	**14**	11,615	-	11,615
Due to banks	**25,083**	**12,423**	**37,506**	86	-	86
Subordinated debt	**-**	**2,500**	**2,500**	-	1,500	1,500
Letter of credit, guarantees and acceptance	**1,500**	**5,796**	**7,296**	-	13,287	13,287
Standby revolving credit facility	**77,000**	**-**	**77,000**	26,950	11,550	38,500
Risk indemnities received	**-**	**8,000**	**8,000**	4,284	-	4,284

25 RELATED PARTY TRANSACTIONS (Continued)

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

	2011			2010		
	Principal shareholder RO'000	**Others RO'000**	**Total RO'000**	Principal shareholder RO'000	Others RO'000	Total RO'000
Interest income	**11**	**1,171**	**1,182**	46	1,094	1,140
Commission income	**-**	**21**	**21**	-	120	120
Interest expense	**261**	**421**	**682**	96	597	693
Other expenses	**120**	**872**	**992**	345	672	1,017
Director's remuneration and sitting fees	**-**	**200**	**200**	-	200	200

	2011			2010		
	Principal shareholder USD'000	**Others USD'000**	**Total USD'000**	Principal shareholder USD'000	Others USD'000	Total USD'000
Loans and advances	**-**	**86,748**	**86,748**	-	74,532	74,532
Customer's deposits	**-**	**24,294**	**24,294**	-	36,101	36,101
Due from banks	**36**	**-**	**36**	30,169	-	30,169
Due to banks	**65,151**	**32,268**	**97,419**	223	-	223
Subordinated debt	**-**	**6,494**	**6,494**	-	3,896	3,896
Letter of credit, guarantees and acceptance	**3,896**	**15,055**	**18,951**	-	34,512	34,512
Standby revolving credit facility	**200,000**	**-**	**200,000**	70,000	30,000	100,000
Risk indemnities received	**-**	**20,779**	**20,779**	11,127	-	11,127

	2011			2010		
	Principal shareholder USD'000	**Others USD'000**	**Total USD'000**	Principal shareholder USD'000	Others USD'000	Total USD'000
Interest income	**29**	**3,042**	**3,071**	119	2,842	2,961
Commission income	**-**	**55**	**55**	-	312	312
Interest expense	**678**	**1,094**	**1,772**	249	1,551	1,800
Other expenses	**312**	**2,265**	**2,577**	896	1,745	2,641
Directors remuneration and sitting fees	**-**	**519**	**519**	-	519	519

Details regarding senior management compensation are set out below:

2010 USD'000	**2011 USD'000**		**2011 RO'000**	2010 RO'000
		Salaries and other short term benefits		
6,338	**4,972**	Fixed	**1,914**	2,440
3,457	**1,005**	Discretionary	**387**	1,331
9,795	**5,977**		**2,301**	3,771

26 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:

2010 USD'000	**2011 USD'000**		**2011 RO'000**	2010 RO'000
70,575	**88,836**	Profit for the year	**34,202**	27,171
1,081,000	**1,081,000**	Weighted average number of shares outstanding during the year (in '000s)	**1,081,000**	1,081,000
USD 0.06	**USD 0.08**	Earnings per share	**RO 0.032**	RO 0.025

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.

27 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 as well as Internal capital adequacy assessment process (ICAAP) requirements.

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

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

2010 USD'000	**2011 USD'000**		**2011 RO'000**	2010 RO'000
		Capital base		
632,675	**670,288**	Tier 1 - shareholders' funds	**258,061**	243,580
111,462	**167,205**	Tier 2 - subordinated debt and collective impairment provisions	**64,374**	42,913
744,137	**837,493**	Total capital base	**322,435**	286,493
		Risk weighted assets		
4,263,234	**5,004,016**	Credit risk	**1,926,546**	1,641,345
380,403	**402,166**	Operational risk	**154,834**	146,455
150,026	**63,735**	Market risk	**24,538**	57,760
4,793,663	**5,469,917**	Total risk weighted assets	**2,105,918**	1,845,560
15.5%	**15.3%**	Risk asset ratio (Basel II norms)	**15.3%**	15.5%

28 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:-

28.1 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, SME 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.

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 new stress tests and quarterly reviews of adverse rating migrations and outlooks on financial institution group (FIG) exposures 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

28 RISK MANAGEMENT (Continued)

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.

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.

28 RISK MANAGEMENT (Continued)

Maximum exposure to credit risk

Gross maximum exposure 2010 USD'000	**Gross maximum exposure 2011 USD'000**		**Gross maximum exposure 2011 RO '000**	Gross maximum exposure 2010 RO '000
499,906	**506,457**	Balances with Central Banks	**194,986**	192,464
218,584	**416,997**	Due from banks and other money market placements	**160,544**	84,155
3,541,200	**4,339,683**	Loans and advances to customers (net)	**1,670,778**	1,363,362
163,982	**246,810**	Non-trading financial investments	**95,022**	63,133
115,208	**158,364**	Other assets	**60,970**	44,355
4,538,880	**5,668,311**	**Total on balance sheet exposure**	**2,182,300**	1,747,469
1,015,678	**1,134,769**	Letter of guarantee	**436,886**	391,036
212,745	**184,229**	Letter of credit	**70,928**	81,907
268,616	**197,977**	Undrawn commitment	**76,221**	103,417
20,000	**15,000**	Credit default swaps	**5,775**	7,700
12,145	**28,681**	Derivative financial instruments	**11,042**	4,676
1,529,184	**1,560,656**	**Total off balance sheet exposure**	**600,852**	588,736

The above table represents the worst case scenario of credit risk exposure to the bank at 31 December 2010 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.

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 2011	**1,341,082**	**29,980**	**61,307**	**1,432,369**
Additions during the year	**820,013**	**64,436**	**39,622**	**924,071**
Attrition during the year	**(523,727)**	**(62,133)**	**(20,732)**	**(606,592)**
Written-off during the year	**-**	**-**	**(16,160)**	**(16,160)**
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**
Balance as at 31 December 2010	1,341,082	29,980	61,307	1,432,369
Balance as at 31 December 2010 – USD'000s	3,483,330	77,870	159,239	3,720,439

28 RISK MANAGEMENT (Continued)

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 2011	**12,017**	**12,921**	**7,345**	**32,283**
31 December 2010	10,665	14,715	4,600	29,980

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.

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 paid RO'000	Non performing loans RO'000	Total RO'000
Collateral available	**851,902**	**8,714**	**10,717**	**871,333**
Guarantees available	**23,376**	**-**	**-**	**23,376**
Government soft loans*	**6,319**	**-**	**5,443**	**11,762**
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**
Balance as at 31 December 2010	832,020	2,567	38,149	872,736
Balance as at 31 December 2010 – USD'000s	2,161,091	6,668	99,088	2,266,847

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

28 RISK MANAGEMENT (Continued)

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 2011	**7,515**	**16,843**	**36,949**	**61,307**
Additions during the year	**10,772**	**13,762**	**15,088**	**39,622**
Attrition during the year	**(2,487)**	**(10,050)**	**(8,195)**	**(20,732)**
Written-off during the year	**-**	**(273)**	**(15,887)**	**(16,160)**
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**
Balance as at 31 December 2010	7,515	16,843	36,949	61,307
Balance as at 31 December 2010 – USD'000s	19,519	43,748	95,972	159,239

Movement of rescheduled loans:

	2011 RO'000	2010 RO'000
Balance as at 1 January	**88,695**	71,402
Additions during the year	**21,392**	27,575
Attrition during the year	**(32,034)**	(10,282)
Balance as at 31December	**78,053**	88,695
Balance as at 31December – USD'000s	**202,735**	230,377

28.2 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 thorough 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.

28 RISK MANAGEMENT (Continued)

The maturity profile of the assets, liabilities and equity at 31 December 2011 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	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

28 RISK MANAGEMENT (Continued)

The maturity profile of the assets, liabilities and equity at 31 December 2010 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	161,535	20,447	181,982	28,990	16,567	45,557	227,539
Due from banks and other money market placements	69,028	3,577	72,605	11,550	-	11,550	84,155
Loans and advances (net)	235,857	122,652	358,509	243,971	760,882	1,004,853	1,363,362
Non-trading financial investments	44,096	-	44,096	19,037	-	19,037	63,133
Premises and equipment	-	-	-	-	22,353	22,353	22,353
Deferred tax asset	-	-	-	7	-	7	7
Other assets	41,956	1,984	43,940	415	-	415	44,355
Total assets	552,472	148,660	701,132	303,970	799,802	1,103,772	1,804,904
Due to banks and other money market deposits	7,220	-	7,220	125,125	-	125,125	132,345
Customers' deposits	318,045	309,005	627,050	456,996	240,844	697,840	1,324,890
Other liabilities	38,727	3,690	42,417	4,667	-	4,667	47,084
Taxation	4,175	-	4,175	-	-	-	4,175
Subordinated debt	-	-	-	27,600	3,000	30,600	30,600
Shareholders' equity	-	-	-	-	265,810	265,810	265,810
Total liabilities and shareholders' equity	368,167	312,695	680,862	614,388	509,654	1,124,042	1,804,904

	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	419,571	53,109	472,680	75,299	43,031	118,330	591,010
Due from banks and other money market placement	179,293	9,291	188,584	30,000	-	30,000	218,584
Loans and advances (net)	612,615	318,577	931,192	633,691	1,976,317	2,610,008	3,541,200
Non-trading financial investments	114,535	-	114,535	49,447	-	49,447	163,982
Premises and equipment	-	-	-	-	58,060	58,060	58,060
Deferred tax asset	-	-	-	18	-	18	18
Other assets	108,977	5,153	114,130	1,078	-	1,078	115,208
Total assets	1,434,991	386,130	1,821,121	789,533	2,077,408	2,866,941	4,688,062
Due to banks and other money market deposits	18,753	-	18,753	325,000	-	325,000	343,753
Customers' deposits	826,091	802,610	1,628,701	1,187,003	625,569	1,812,572	3,441,273
Other liabilities	100,591	9,584	110,175	12,122	-	12,122	122,297
Taxation	10,844	-	10,844	-	-	-	10,844
Subordinated debt	-	-	-	71,689	7,792	79,481	79,481
Shareholders' equity	-	-	-	-	690,414	690,414	690,414
Total liabilities and shareholders' equity	956,279	812,194	1,768,473	1,595,814	1,323,775	2,919,589	4,688,062

28 RISK MANAGEMENT (Continued)

28.3 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 sheet exposures.

Equity risk

The proprietary equity positions are held in the 'Available for Sale' category. The market risk is monitored through 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 2011	200 bps increase	200 bps decrease
Earnings impact - RO'000s	8,829	(8,829)
Earnings impact - USD'000s	22,932	(22,932)

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 analyses are 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.

28 RISK MANAGEMENT (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 2011 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	0.05%	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	-	-

28 RISK MANAGEMENT (Continued)

The bank's interest sensitivity position based on contractual re-pricing arrangements at 31 December 2011 was 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	0.05%	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	-	-

28 RISK MANAGEMENT (Continued)

The bank's interest sensitivity position based on contractual re-pricing arrangements at 31 December 2010 was 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%	45,000	2,322	-	-	180,217	227,539
Due from banks and other money market placements (net)	1.45%	83,658	497	-	-	-	84,155
Loans and advances (net)	6.63%	575,794	182,259	216,123	376,690	12,496	1,363,362
Non-trading financial investments	3.89%	-	-	44,096	-	19,037	63,133
Premises and equipment	N/A	-	-	-	-	22,353	22,353
Deferred tax asset	N/A	-	-	-	-	7	7
Other assets	N/A	-	-	-	-	44,355	44,355
Total assets		704,452	185,078	260,219	376,690	278,465	1,804,904
Due to banks and other money market deposits	1.05%	132,345	-	-	-	-	132,345
Customers' deposits	2.78%	182,775	288,657	351,508	8,000	493,950	1,324,890
Other liabilities	N/A	-	-	-	-	47,084	47,084
Taxation	N/A	-	-	-	-	4,175	4,175
Subordinated debt	7.51%	-	-	27,600	3,000	-	30,600
Shareholders' equity	N/A	-	-	-	-	265,810	265,810
Total liabilities and shareholders' equity		315,120	288,657	379,108	11,000	811,019	1,804,904
Total interest rate sensitivity gap		389,332	(103,579)	(118,889)	365,690	(532,554)	-
Cumulative interest rate sensitivity gap		389,332	285,753	166,864	532,554	-	

28 RISK MANAGEMENT (Continued)

The bank's interest sensitivity position based on contractual re-pricing arrangements at 31 December 2010 was 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%	116,883	6,031	-	-	468,096	591,010
Due from banks and other money market placements (net)	1.45%	217,293	1,291	-	-	-	218,584
Loans and advances (net)	6.63%	1,495,569	473,400	561,358	978,416	32,457	3,541,200
Non-trading financial investments	3.89%	-	-	114,535	-	49,447	163,982
Premises and equipment	N/A	-	-	-	-	58,060	58,060
Deferred tax asset	N/A	-	-	-	-	18	18
Other assets	N/A	-	-	-	-	115,208	115,208
Total assets		1,829,745	480,722	675,893	978,416	723,286	4,688,062
Due to banks and other money market deposits	1.05%	343,753	-	-	-	-	343,753
Customers' deposits	2.78%	474,740	749,758	913,008	20,779	1,282,988	3,441,273
Other liabilities	N/A	-	-	-	-	122,297	122,297
Taxation	N/A	-	-	-	-	10,844	10,844
Subordinated debt	7.51%	-	-	71,689	7,792	-	79,481
Shareholders' equity	N/A	-	-	-	-	690,414	690,414
Total liabilities and shareholders' equity		818,493	749,758	984,697	28,571	2,106,543	4,688,062
Total interest rate sensitivity gap		1,011,252	(269,036)	(308,804)	949,845	(1,383,257)	
Cumulative interest rate sensitivity gap		1,011,252	742,216	433,412	1,383,257	-	

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:

2010 USD'000	**2011 USD'000**		**2011 RO'000**	2010 RO'000
150,229	**52,260**	US Dollar	**20,120**	57,838
38,870	**22,556**	UAE Dirham	**8,684**	14,965
5,301	**984**	Others	**379**	2,041

28 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, authorisation and reconciliation procedures, staff training and assessment processes, including the use of internal audit.

29 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 2011 was 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

29 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	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

The distribution of assets, liabilities and off balance sheet items by geographical regions as of 31 December 2010 was 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	208,257	3,663	15,619	-	227,539
Due from banks and other money market placements (net)	612	4,181	8,900	70,462	84,155
Loans and advances (net)	1,283,669	58,814	-	20,879	1,363,362
Non-trading financial investments	59,786	-	995	2,352	63,133
Premises and equipment	21,535	65	753	-	22,353
Deferred tax asset	7	-	-	-	7
Other assets	38,884	1,204	2,150	2,117	44,355
Total assets	1,612,750	67,927	28,417	95,810	1,804,904
Due to banks and other money market deposits	1,175	17	-	131,153	132,345
Customers' deposits	1,240,890	28,130	29,569	26,301	1,324,890
Other liabilities	43,134	1,419	414	2,117	47,084
Taxation	3,150	134	891	-	4,175
Subordinated debt	30,600	-	-	-	30,600
Shareholders' equity	247,180	3,589	15,041	-	265,810
Liabilities and shareholders' equity	1,566,129	33,289	45,915	159,571	1,804,904
Contingent liabilities	259,813	55,592	721	156,817	472,943

29 CONCENTRATIONS (continued)

The distribution of assets, liabilities and off balance sheet items by geographical regions as of 31 December 2010 was 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	540,927	9,514	40,569	-	591,010
Due from banks and other money market placements (net)	1,590	10,860	23,117	183,017	218,584
Loans and advances (net)	3,334,205	152,764	-	54,231	3,541,200
Non-trading financial investments	155,289	-	2,584	6,109	163,982
Premises and equipment	55,935	169	1,956	-	58,060
Deferred tax asset	18	-	-	-	18
Other assets	100,998	3,127	5,584	5,499	115,208
Total assets	4,188,962	176,434	73,810	248,856	4,688,062
Due to banks and other money market deposits	3,052	44	-	340,657	343,753
Customers' deposits	3,223,091	73,065	76,803	68,314	3,441,273
Other liabilities	112,037	3,686	1,075	5,499	122,297
Taxation	8,182	348	2,314	-	10,844
Subordinated debt	79,481	-	-	-	79,481
Shareholders' equity	642,024	9,322	39,068	-	690,414
Liabilities and shareholders' equity	4,067,867	86,465	119,260	414,470	4,688,062
Contingent liabilities	674,838	144,395	1,873	407,317	1,228,423

30 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 and market risk.
- 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.

30 SEGMENTAL INFORMATION (Continued)

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

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

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.

30 SEGMENTAL INFORMATION (Continued)

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

30 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
Other operating income - external	85,098	1,561	1,777	88,436
Other 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
Other operating expenses - external	96,130	3,556	2,260	101,946
Other 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

30 SEGMENTAL INFORMATION (Continued)

Segment information is as follows:

Year ended 31 December 2010	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	24,037	27,622	1	358	3,608	55,626
Other income	11,733	4,444	2,536	2,702	1,075	22,490
Operating profit	18,670	28,867	1,764	2,368	(13,502)	38,167
Impairment provisions (net)	(5,347)	(2,264)	(628)	308	-	(7,931)
Profit	13,323	26,603	1,136	2,676	(16,567)	27,171
Total assets	619,745	741,868	19,037	19,369	404,885	1,804,904
Total liabilities and equity	519,151	661,619	35,841	-	588,293	1,804,904

Year ended 31 December 2010	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	62,434	71,745	3	930	9,371	144,483
Other income	30,475	11,543	6,587	7,018	2,793	58,416
Operating profit	48,494	74,979	4,582	6,151	(35,071)	99,135
Impairment provisions (net)	(13,887)	(5,881)	(1,631)	800	-	(20,599)
Profit	34,605	69,099	2,951	6,951	(43,031)	70,575
Total assets	1,609,727	1,926,930	49,447	50,309	1,051,649	4,688,062
Total liabilities and equity	1,348,444	1,718,491	93,094	-	1,528,033	4,688,062

30 SEGMENTAL INFORMATION (Continued)

Segment information by geography is as follows:

For the year ended 31 December 2010	Oman RO'000	UAE RO'000	Egypt RO'000	Total RO'000
Segment revenue				
Interest income - external	90,797	3,280	1,097	95,174
Interest income - internal	38	1	2,156	2,195
Other operating income - external	21,747	585	158	22,490
Other operating income - internal	173	-	-	173
Total	112,755	3,866	3,411	120,032
Segment costs				
Interest costs - external	37,595	923	1,030	39,548
Interest costs - internal	589	7	1,599	2,195
Other operating expenses - external	33,695	1,260	1,174	36,129
Other operating expenses – internal	-	97	76	173
Depreciation	3,694	29	97	3,820
Credit loss expense - customer loan	14,339	1,533	9	15,881
Impairment losses on available for sale investments	628	-	-	628
Recoveries	(6,756)	(437)	(1,385)	(8,578)
Taxation	2,882	91	92	3,065
Total	86,666	3,503	2,692	92,861
Segment profit for the year	26,089	363	719	27,171
Other information				
Segment assets	1,720,472	47,486	36,946	1,804,904
Segment capital expenses	13,440	26	16	13,482

30 SEGMENTAL INFORMATION (Continued)

For the year ended 31 December 2010	Oman USD'000	UAE USD'000	Egypt USD'000	Total USD'000
Segment revenue				
Interest income - external	235,837	8,519	2,849	247,205
Interest income - internal	98	3	5,600	5,701
Operating income - external	56,487	1,519	410	58,416
Operating income - internal	449	-	-	449
Total	292,871	10,041	8,859	311,771
Segment costs				
Interest costs - external	97,650	2,397	2,675	102,722
Interest costs - internal	1,530	18	4,153	5,701
Operating expenses - external	87,520	3,273	3,049	93,842
Operating expenses – internal	-	252	197	449
Depreciation	9,595	75	252	9,922
Credit loss expense - customer loan	37,244	3,982	23	41,249
Impairment losses on available for sale investments	1,631	-	-	1,631
Recoveries	(17,549)	(1,135)	(3,597)	(22,281)
Taxation	7,486	236	239	7,961
Total	225,107	9,098	6,991	241,196
Segment profit for the year	67,764	943	1,868	70,575
Other information				
Segment assets	4,468,758	123,340	95,964	4,688,062
Segment capital expenses	34,909	68	42	35,019

31 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 2011 and 2010 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.

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

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

31 FAIR VALUE OF FINANCIAL INSTRUMENTS (Continued)

31 December 2010	Level 1 RO'000	Level 2 RO'000	Level 3 RO'000	Total RO'000
Financial assets				
Investments - available for sale:				
Government development bonds	44,096	-	-	44,096
Quoted equities	11,328	-	-	11,328
Other unquoted equities	-	7,709	-	7,709
Total	55,424	7,709	-	63,133
Derivative financial instruments:				
Purchase contracts	-	41,890	-	41,890
Sale contracts	-	41,890	-	41,890
Interest rate swaps	-	160,720	-	160,720
Interest rate caps	-	383	-	383
Credit default swaps	-	7,700	-	7,700
Currency options	-	27,080	-	27,080
Commodity hedging	-	2,232	-	2,232
Total	-	281,895	-	281,895
Total financial assets	55,424	289,604	-	345,028
Total financial assets – In USD'000s	143,959	752,218	-	896,177

During the reporting period ended 31 December 2011 and 31 December 2010, 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.

32 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.

32 DERIVATIVES (continued)

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 2011	Positive fair value RO'000 (note8)	Negative fair value RO'000 (note 11)	Notional amount RO'000	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

32 DERIVATIVES (continued)

31 December 2010	Positive fair value RO'000 (note8)	Negative fair value RO'000 (note 11)	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	4,212	(4,212)	160,720	1,500	7,144	152,076
Credit default swaps	-	(45)	7,700	-	1,925	5,775
Forward foreign exchange purchase contracts	40	(55)	41,890	41,268	622	-
Forward foreign exchange sales contracts	55	(80)	41,890	41,269	621	-
Interest rate caps	-	-	383	80	181	122
Currency options	187	(187)	27,080	19,037	8,043	-
Commodity hedging	182	(182)	2,232	2,232	-	-
Total	4,676	(4,761)	281,895	105,386	18,536	157,973
Total – USD'000	12,145	(12,366)	732,195	273,730	48,145	410,320

33 COMPARATIVE AMOUNTS

Certain of the corresponding figures for 2010 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 2010.

69 Branches in Oman

3 Branches in Egypt

1 Branch in UAE (Abu Dhabi)

6 Sadara Wealth Management Centers

Branch Network

For You. For Our Nation.

Muscat Region (South)

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

MBD
Tel: 24 778 556, 24 778 550, 24 778 553

Corporate Branch (HO)
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

Ma'abella Suq
Tel: 24 4 52 304, 24 452 387, 24511167

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

Buraimi Region

Buraimi
Tel: 25 653 037, 25 655 226

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

Batinah Region (North)

Safeer Sohar
Tel: 26 841 967, 26 844 372

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

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

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

Batinah Region (North)

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

Duqm
Tel: 25427101,25427130, 25427172

Sadara Wealth Management Centers

CBD Center
Tel: 24778009, Fax: 24778500

Al Khuwair
Tel: 24487356, Fax: 24487355

Shatti Center
Tel: 24607679, Fax: 24693620

MAF Center
Tel: 24567223, Fax: 24567033

Sohar Center
Tel: 26859103, Fax: 26859110

Salalah Center
Tel: 23298092, Fax: 23297135

Overseas Branches

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

Heliopolis
133-135, Abdel Aziz Fahmy Street,
Heliopolis Masr El Gedida, Cairo
Tel: (+202) 22900154/157/158

Mohandessin
34, El Batal Ahmed Abdul Aziz Street
Mohandessin Giza
(+202) 37617041 / 37617042

Alexandria
(+203) 3936929 - 3936927

United Arab Emirates

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

National Bank of Oman
P.O. Box 751
Ruwi 112
Muscat
Sultanate of Oman

www.nbo.co.om