بنك ظفار
BankDhofar

ANNUAL REPORT 2013

Top 20 - 2013
OER Awards

1st Prize Corporate Governance Excellence Award
Capital Market Authority

The Best Retail Bank in Oman
Global Finance Market Review

The Best Retail Bank in Oman
the Global Banking & Finance review Awards

Best Islamic Window for 2013
in Oman - the Global Financial Market Awards (GFM)

Omanisation Award
Ministry of Manpower

2nd Prize Best banks in Oman
- Business Today magazine

FAST FORWARD

Straight-through-processing (STP)
of Euro payments and financial transactions - Commerzbank, Germany.

Platinum award
Middle East region for Bank's Business Process Management system (BPM) an initiative by Newgen worldwide

Silver award
in the Banking and Financial sector at the 7th Oman Web Awards

His Majesty Sultan Qaboos Bin Said

TABLE OF CONTENTS

The Board of Directors' report for the financial year ended 31st December 2013

Dear Shareholders,

On behalf of the Board of Directors of BankDhofar S.A.O.G., I am pleased to present you the Bank's Financial Statements and the Auditors' Report for the financial year ended 31st December 2013.

BankDhofar wins Capital Market Authority Corporate Governance Excellence Award 2013

1st Prize Corporate Governance Excellence Award
Capital Market Authority

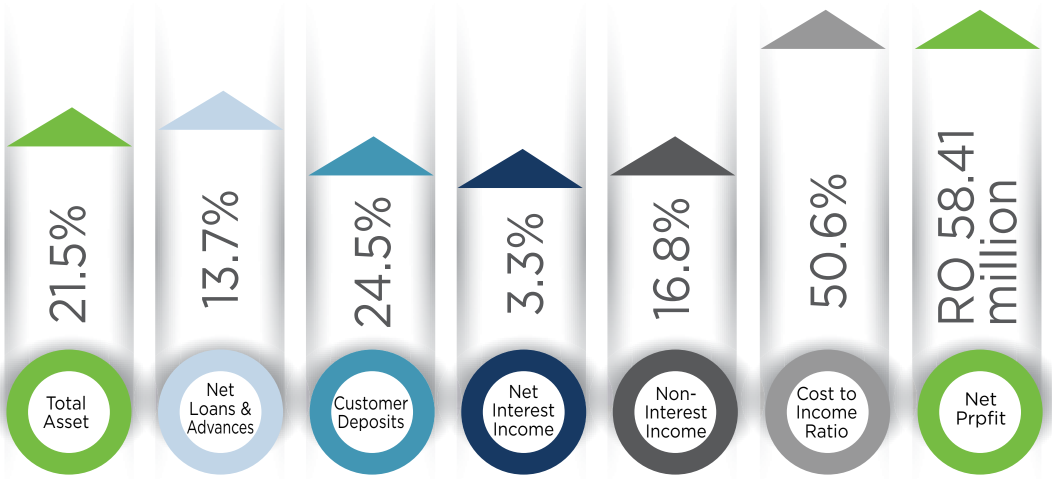
Financial Performance in 2013

The Bank continued to grow in all key areas in the year 2013; the net Loans and Advances extended to customers achieved a growth of 13.7% from RO 1.67 billion at the end of 2012 to reach RO 1.90 billion at the end of December 2013. Further, the customer deposits mobilized by the bank achieved a growth of 24.5% from RO 1.63 billion at the end of 2012 to reach RO 2.03 billion at the end of 2013.

The key profitability indicators have also achieved positive growths, as net interest income grew from RO 64.37 million in 2012 to reach RO 66.51 million during the year 2013 signifying a growth of 3.3%. Non-interest income such as fees and commissions, foreign exchange profit, investment and other income have shown a significant growth of 16.8% to reach RO 23.04 million in 2013 compared to RO 19.72 million achieved in the previous year.

The Cost to Income ratio during the year 2013 was at a level of 50.6% as compared to 44.1% in 2012. The provisions for loan impairment, net of recovery (excluding legal case recovery), during the year 2013 are RO 4.23 million, as against the RO 4.15 million during the previous year 2012.

The net profit for the year 2013 achieved by the Bank is RO 58.41 million as against RO 37.74 million, including the effect of Legal case write back of RO 26.1 million (before taxes), in 2013.



Corporate Governance

The Bank has fully complied with all directives of the Code of Corporate Governance issued by the Capital Market Authority. The Bank has also assessed and reviewed the internal control procedures of the Bank during the year 2013.

In compliance with Article (101) of the Commercial Companies Law No. 4/1974 and its amendments, the Board of Directors would like to disclose that the total amount received in 2013 as sitting fees was RO 86,000 and the proposed remuneration for the same year is RO 114,000.

Proposed Dividends

The Board of Directors recommends cash dividend of 14% amounting to RO 16.94 million and a Bonus share issue of 11%, aggregating to 133.1 million shares of RO 0.100 each, of the Share capital of the Bank.

The percentage of dividends distributed to the Shareholders in the last five years is as follows:

Year	2008	2009	2010	2011	2012
Cash Dividends	15.5%	15%	12.5%	7%	15%
Bonus Shares	4.5%	10%	12.5%	20.2%	10%

Maisarah- Islamic Banking Services

Maisarah Islamic Banking Services started its operations in March 2013 and has successfully completed the first period of its operation with two branches located in Muscat and Dhofar region. To cater to the needs of the customers, Maisarah has successfully launched many attractive products in Financing and Deposits during its initial stage of operations.

Maisarah has achieved Total assets of nearly OMR 50 million, including net financing of OMR 27.9 million, Sukuk investment of OMR 10 million and Deposits and equity of unrestricted investment accountholders of OMR 3.7 million by the end of year 2013. During the period Maisarah has incurred a net loss (before taxes) of OMR 2.20 million. Sitting fees of RO 14,100 was paid and remuneration of RO 18,000 was accrued for Sharia Supervisory Board Members for the year 2013.

Awards and Accolades during 2013

Our Bank won the following awards during the year 2013:

The Best Retail Bank in Oman
Global Finance Market Review

The Best Retail Bank in Oman
the Global Banking & Finance review Awards

2nd Prize - Best banks in Oman
Business Today magazine

The Best Islamic Banking Window for 2013 in Oman
the Global Financial Market Awards

Omanisation Award
Ministry of Manpower

1st Prize Corporate Governance Excellence Award
Capital Market Authority

Oman Economic Review 'Top 20
Best Performing companies' listed in Muscat Securities Market (MSM)

Platinum award
Middle East region for Bank's Business Process Management system (BPM) an initiative by NewGen Worldwide

Silver award
in the Banking and Financial sector for best internet banking portal, at the 7th Oman Web Awards

Straight-through-processing (STP)
of Euro payments and financial transactions - Commerzbank, Germany.

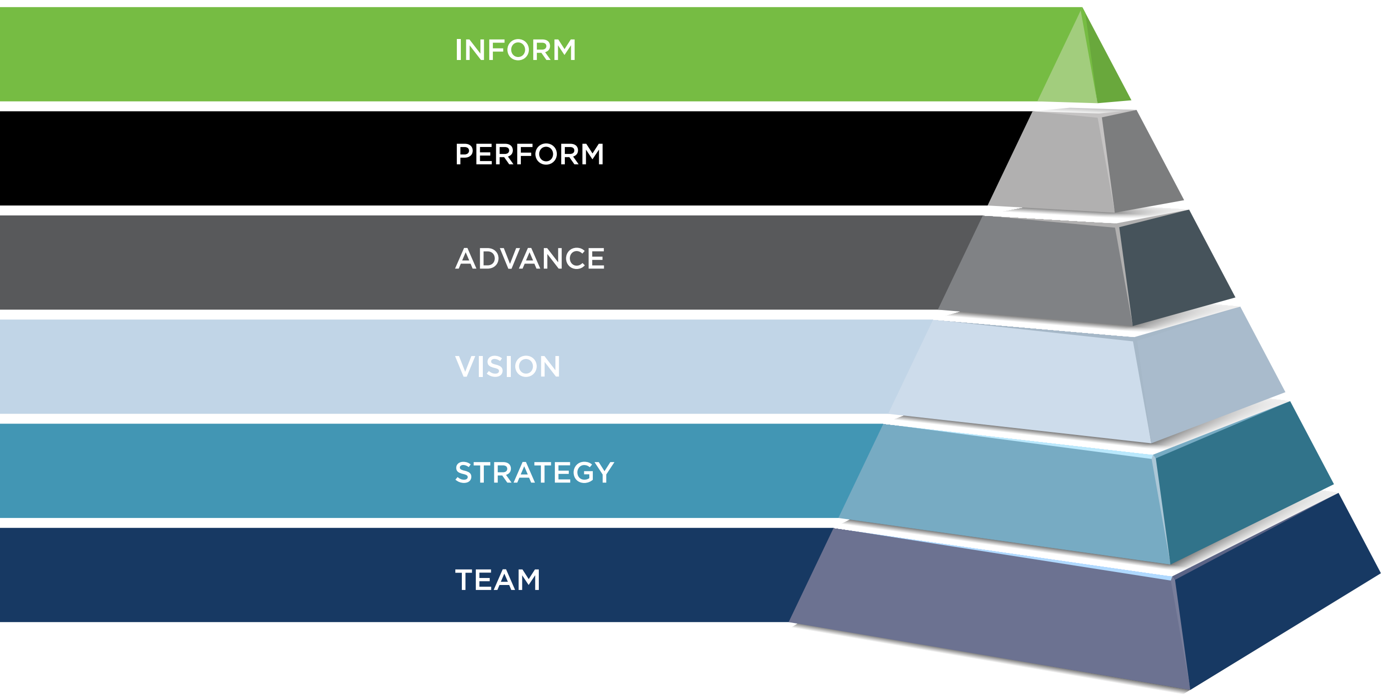
Acknowledgment

On behalf of the Board, I would like to thank our valuable customers for their patronage and confidence they have reposed in the Board of Directors and the Executive Management. Also I thank the shareholders for their continuous support and moreover I thank Chairman and Sharia Supervisory Board of Maisarah Islamic Banking Services for their great efforts made and contributions, diligent Staff and Management for their performance in the year 2013.

The Board of Directors also wishes to thank the Central Bank of Oman for its valuable guidance to the local banking sector.

Finally, on behalf of the Board of Directors, employees and the management I would like to express our most sincere gratitude to **His Majesty Sultan Qaboos Bin Said** for his wise leadership and generous support to the private sector.

Eng. Abdul Hafidh Salim Rajab Al-Aujaili
Chairman



Members of the Board of Directors

1

Name of Director:
Eng. Abdul Hafidh
Salim Rajab Al-Aujaili

Basis of Membership:
Chairman Non-executive
Non-Independent
Shareholder Director

No. of other Directorships held: –

4

Name of Director:
Mr. Ahmed Said
Mohammed Al Mahrezi

Basis of Membership:
Member Non-executive
Independent
Non-shareholder Director

No. of other Directorships held: 1

5

Name of Director:
Mr. Saleh Nasser Juma
Al Araimi

Basis of Membership:
Member Non-executive
Independent
Shareholder Director

No. of other Directorships held: 3

7

Name of Director:
Mr. Tariq Abdul Hafidh
Salim Al-Aujaili

Basis of Membership:
Member Non-executive
Non-Independent
Non-shareholder Director

No. of other Directorships held: 3

2

Name of Director:
Sheikh Hamoud Mustahail Ahmed Al Mashani

Basis of Membership:
Vice-Chairman Non-executive Independent Non-shareholder Director

No. of other Directorships held: 3

3

Name of Director:
Sheikh Qais Mustahail Ahmed Al Mashani

Basis of Membership:
Member Non-executive Non-Independent Shareholder Director

No. of other Directorships held: 3

6

Name of Director:
Mr. Mohammed Yousuf Alawi Al Ibrahim

Basis of Membership:
Member Non-executive Independent Non-shareholder Director

No. of other Directorships held: 2

8

Name of Director:
Eng. Abdul Sattar Mohammed Abdullah Al Murshidi

Basis of Membership:
Member Non-executive Independent Shareholder Director

No. of other Directorships held: -

9

Name of Director:
Mr. Majid Said Sulaiman Al Bahri

Basis of Membership:
Member Non-executive Independent Shareholder Director

No. of other Directorships held: -

Executive Team

Abdul Hakeem Al-Aujaili
Acting CEO

Shankar Sharma
DGM-Chief Financial Officer

Nasser Said Al Bahantah
DGM-Human Resources

Bashir Al Subhi
AGM-International Banking

Mohammed Iqbal Al Balushi
AGM-Central Operations & Support Services

Mohammed Al Riyami
AGM-Internal Audit

Ranganathan Palanthandalam Madapusi
Head of Risk Management

Kamal Al Murazza
DGM-Wholesale Banking

Faisal Al Wahaibi
DGM-Retail Banking

Ahmed Al Ibrahim
DGM-Government Relations

Shaleen Chugh
AGM-Large Corporate & Syndications Wholesale Banking

Hani Macki
AGM-Mid Corporate & Business Banking

Tariq Taha
AGM-Chief Information & Transformation Officer

Depti Rai
Head of Compliance

Corporate governance report for the year ended 31st December 2013

KPMG
4th Floor, HSBC Bank Building
MBD
P.O. Box 641
P.C. 112
Sultanate of Oman

Tel 968 24709181
Fax 968 24700839

Report to the Shareholders of Bank Dhofar SAOG ("the Bank") of Factual Findings in connection with the Corporate Governance Report of the Bank and application of the Corporate Governance practices in accordance with Capital Market Authority Code of Corporate Governance

We have performed the procedures prescribed in the Capital Market Authority ("CMA") Circular No. 16/2003 dated 29 December 2003 with respect to the Corporate Governance Report of the Bank ("the Report") and its application of the Corporate Governance practices in accordance with the CMA Code of Corporate Governance ("the Code") issued under Circular No. 11/2002 dated 3 June 2002, and the CMA Rules and Guidelines on disclosure, issued under CMA Administrative Decision 5/2007, dated 27 June 2007, as amended. The Report is set out on pages 18 to 31

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

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

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

This report is solely for the purpose set forth in the second paragraph above, and for inclusion, with the Report, in the Bank's annual report, and is not to be used for any other purpose. This report relates only to the Report included in the Bank's annual report for the year ended 31 December 2013 and does not extend to the financial statements or any other reports of Bank Dhofar SAOG, taken as a whole.

29 January 2014

Khalid Masud Ansari

Report on Corporate Governance

Part One

1 - Corporate Governance Philosophy:

Corporate governance is an essential element in attaining, enhancing and retaining confidence of the bank's stakeholders. Corporate governance lays down the relationship and responsibilities between shareholders, board of directors and senior management of the bank through the structure of setting objectives, formulating strategies, controlling and monitoring performance while ensuring compliance with regulations in letter and spirit and promoting a culture of transparency through disclosures and commitment to highest ethical standards.

The Board of Directors of Bank Dhofar SAOG (the Bank) bear the principal responsibility of fashioning the Corporate Governance code as appropriate to the Bank within the broad framework enunciated by the Central Bank of Oman (CBO) and the Capital Market Authority (CMA). It is also charged with the responsibility of subjecting the code to periodic review to keep it refurbished and contemporary.

Decision-making within the Bank has been broadly divided into two levels. The Board of Directors (the Board) at the apex level, as trustees of the shareholders, bear the responsibility of strategic supervision of the Bank, apart from fulfilling statutory obligations. Some of the major responsibilities of the Board are discharged through five sub-committees, viz. the Board Credit Committee, Board Audit Committee, Board Risk Management Committee, Board HR Committee and Board Investment Committee. These sub-committees which operate under the Board approved charters have been meeting regularly and have contributed significantly to the effective functioning of the code of corporate governance. The charters of these committees meet with all the requirements as laid down in the Code of Corporate Governance enunciated by the CBO and the CMA. In addition, the Board carries the responsibility of approving the strategic plans and internal policies to institute adequate controls for achievement of the set objectives and compliance with rules and regulations. The executive management of the Bank comprises the Senior Managers headed by the Chief Executive Officer.

Through this two-tiered interlinked governance process, a wholesome balance has been created between the need for focus and executive freedom, and the need for supervision, control and checks and balances of all activities and transactions.

The formal Code of Corporate Governance prescribes the highest ethical standards in the conduct of the Bank's business. The Senior Members of the Bank are fully cognizant of their responsibilities in setting personal examples so that the code is internalized within the Bank and becomes part of its culture.

2. Board of Directors

The Responsibilities of the Board of Directors

The Board has the full authority to perform all acts required for managing the Bank and protecting and growing the shareholders' interests pursuant to its objectives besides securing the interests of other stakeholders. Such authority is not limited or restricted except as provided by the law, the Articles of Association or resolutions of the General Meetings. However, such authority is not extended to the operational matters and day-to-day affairs of the bank which remains a responsibility of the Senior Management.

The responsibilities and functions of the Board include the following:

- Charting the overall strategic direction of the Bank and reviewing and approving the annual business and strategic plans.
- Monitoring the Bank's performance and evaluating whether the business is properly managed in accordance with the Bank's set plans.
- Approving the interim and annual financial statements and providing accurate information at the right time to the shareholders, in accordance with the instructions of the Capital Market Authority.
- Forming various Board sub-committees, approving their charters and reviewing the functions of these committees.
- Reviewing all audit reports submitted by internal and external auditors and statutory agencies.
- Ensuring that the Bank conducts its operations in an ethical and transparent manner.
- Assessing and approving the proper delegation of authorities to executive management.
- Evaluating the functions and the performance of the Chief Executive Officer and other key employees.

Further, the Board exercises objective independent judgment on corporate affairs after having access to accurate, relevant and timely information.

Size and Terms of the Board

The Board consists of nine (9) non-executive directors who are elected by the shareholders at the Annual General Meeting. The term of office of the Board of Directors is three years and each Director can be re-elected for a similar period. The term of the current Board expires in March 2016.

Composition and Selection of the Board

Members of the Board of Directors are elected from among the Bank's shareholders or non-shareholders provided that a shareholder candidate owns not less than 50,000 shares of the Bank. All members of the Board of Directors shall be non-executive Directors.

A minimum of one-third of the Board members shall be independent Directors, meeting the amended definition of independent director by Capital Market Authority vide its Circular No.E/14/2012 dated 24 October 2012 which states that a director shall be deemed non-independent in the following cases:

1. If he holds ten percent or more of the company shares or the shares of parent company or subsidiary or fellow company
2. If he is representing a juristic person who holds ten percent or more of the company shares or the shares of parent company or subsidiary or fellow company.
3. If he is a senior executive, during the past two years, of the company or parent company or subsidiary or fellow company.
4. If he is a first degree relative of any of the directors of the company or parent company or subsidiary or fellow company.
5. If he is a first degree relative of any of the senior executives of the company or parent company or subsidiary or fellow company.
6. If he is a director of the parent company or subsidiary or fellow company of the company to which he stands as candidate for its board.
7. If he is an employee, during the past two years, of any of associated parties of the company or parent company or subsidiary or fellow company including chartered accountants and major suppliers or if holds controlling share in any of such parties during the past two years.

Please note that CMA has temporarily suspended the application of above definition by their circular E/9/2013 dated 20/11/2013. However, our Bank is complying with more stringent provisions of E/14/2012 dated 24 October 2012.

The nomination of Board members is within rules and condition of the election of directors as issued by CMA. The election process is through direct secret ballot whereby each sharerholder shall have a number of vote's equivalent to the number of shares he/she holds. Every shareholder shall have the right to vote for one candidate or more provided the total number of votes in the voting form is equivalent to the number of shares he/she holds.

At present all the directors of the Board are non-executive, three are dependent and six are Independent within the scope of the definitions laid down by the Capital Market Authority.

Board Committees

The Board has the following five permanent Board Committees, whose objectives, powers and procedures are governed by the terms of reference of the respective Committees as enshrined in their Charters, approved by the Board:

- **Board Credit Committee**
- **Board Audit Committee**
- **Board Risk Management Committee**
- **Board HR Committee**
- **Board Investment Committee**

Additional committees may be established from time to time based on business needs. Each committee has access to the information and resources it requires, including direct access to staff and consultants. The Board has selected the committee members based on their professional backgrounds, skills and other qualities they bring to the committees.

Sharia Supervisory Board

Sharia Supervisory Board was formulated in the year 2012 for guiding the Islamic Banking operations of the Bank.

Part Two

1. Members of the Board of Directors

The Board of Directors of Bank Dhofar (SAOG) consisted of the following before 19 March 2013:

S. No	Name of Director	Basis of membership			No. of other directorships held
1	Eng. Abdul Hafidh Salim Rajab Al-Aujaili	Chairman Non-executive	Non-Independent	Shareholder Director	-
2	Sheikh Hamoud Mustahail Ahmed Al Mashani	Vice-Chairman Non-executive	Independent	Non-shareholder Director	3
3	Sheikh Qais Mustahail Ahmed Al Mashani	Member Non-executive	Non-Independent	Shareholder Director	3
4	Mr. Ahmed Said Mohammed Al Mahrezi	Member Non-executive	Independent	Non-shareholder Director	1
5	Mr. Saleh Nasser Juma Al Araimi	Member Non-executive	Independent	Shareholder Director	3
6	Mr. Mohammed Yousuf Alawi Al Ibrahim	Member Non-executive	Independent	Non-shareholder Director	2
7	Mr. Ali Ahmed Salim Al Mashani (replaced by Eng. Abdul Sattar Mohammed Abdullah Al Marshdi in the AGM meeting held on 19 March 2013)	Member Non-executive	Independent	Non-shareholder Director	-
8	Mrs. Najah Musallim Al Kiyumi (replaced by Mr. Majid Said Sulaiman Al Bahry in the AGM meeting held on 19 March 2013)	Member Non-executive	Independent	Shareholder Director	-
9	Mr. Tariq Abdul Hafidh Salim Al-Aujaili	Member Non-executive	Non-Independent	Non-shareholder Director	3

The Board of Directors of Bank Dhofar (SAOG) consists of the following after 19 March 2013 *:

S. No	Name of Director	Basis of membership			No. of other directorships held
1	Eng. Abdul Hafidh Salim Rajab Al-Aujaili	Chairman Non-executive	Non-Independent	Shareholder Director	-
2	Sheikh Hamoud Mustahail Ahmed Al Mashani	Vice-Chairman Non-executive	Independent	Non-shareholder Director	3
3	Sheikh Qais Mustahail Ahmed Al Mashani	Member Non-executive	Non-Independent	Shareholder Director	3
4	Mr. Ahmed Said Mohammed Al Mahrezi	Member Non-executive	Independent	Non-shareholder Director	1
5	Mr. Saleh Nasser Juma Al Araimi	Member Non-executive	Independent	Shareholder Director	3
6	Mr. Mohammed Yousuf Alawi Al Ibrahim	Member Non-executive	Independent	Non-shareholder Director	2
7	Mr. Tariq Abdul Hafidh Salim Rajab Al-Aujaili	Member Non-executive	Non-Independent	Non-shareholder Director	3
8	Eng. Abdul Sattar Mohammed Abdullah Al Marshdi	Member Non-executive	Independent	Shareholder Director	-
9	Mr. Majid Said Sulaiman Al Bahry	Member Non-executive	Independent	Shareholder Director	-

* Board of Directors was elected in the Annual General Meeting held on 19 March 2013. Ministry Of Defense Pension Fund has replaced its representative in the Bank's Board of Director by nominating Mr. Majid Bin Said Bin Suleiman Al Bahri instead of Brig. Saif Bin Ali Bin Shaikhan Al Amri. Brig. Saif Bin Ali Bin Shaikhan Al Amri has not attended any Board meetings. Required disclosures and regulatory approvals were taken in this regard.

The Board of Directors held 15 meetings during 2013 as follows:

29 Jan 13	24 Apr 13	26 Sep 13
3 Mar 13	18 Jun 13	29 Oct 13
17 Mar 13	15 Jul 13	3 Dec 13
19 Mar 13	28 Jul 13	17 Dec 13
16 Apr 13	25 Sep 13	30 Dec 13

Details of meetings and remuneration of the Board of Directors of Bank Dhofar (SAOG) are as follows:

S. No	Name of Director	Capacity of Membership	No. of Meetings Attended	Directors' Benefits (Amount in RO)	
				Fees Paid	Remuneration Proposed
1	Eng. Abdul Hafidh Salim Rajab Al-Aujaili	In Personal Capacity	15	10,000	14,605
2	Sheikh Hamoud Mustahail Ahmed Al Mashani	In Personal Capacity	7	4,500	13,105
3	Sheikh Qais Mustahail Ahmed Al Mashani	Representative of Dhofar International Development & Investment Holding Company (SAOG)	10	9,600	11,605
4	Mr. Ahmed Said Mohammed Al Mahrezi	In Personal Capacity	11	10,000	12,784
5	Mr. Saleh Nasser Juma Al Araimi	Representative of Public Authority for Social Insurance	14	10,000	12,784
6	Mr. Mohammed Yousuf Alawi Al Ibrahim	In Personal Capacity	12	10,000	11,925
7	Mr. Ali Ahmed Al Mashani	In Personal Capacity	-	-	-
8	Mrs. Najah Musallim Al Kiyumi	Representative of Ministry of Defense Pension Fund	4	4,200	-
9	Mr. Tariq Abdul Hafidh Salim Al-Aujaili	In Personal Capacity	9	10,000	13,105
10	Eng. Abdul Sattar Mohd Abdullah Al Murshidi	Representative of Malatan Trading and Contracting LLC	9	10,000	12,783
11	Mr. Majid Said Sulaiman Al Bahry	Representative of Ministry of Defence Pension Fund	8	7,400	11,604
TOTAL				**85,700**	**114,300**

2. Sharia Supervisory Board (SSB)

The SSB consists of five members. The objectives of SSB include:

- To Provide the Sharia rulings in all activities of the Islamic Banking Window (IBW)
- To supervise the compliance of the IBW with Islamic Sharia rules
- To enhance the IBW contribution in spreading the awareness and contribute in development of the Islamic banking

Name of Member	Designation	No. of Meetings Attended (2012 & 2013)	Honorarium (Amount in RO)	
			Fees Paid	Remuneration Proposed
Sheikh Dr. Salim bin Ali bin Ahmed Al Dhahab	Chairman	12	4,800	6,000
Sheikh Dr. Mohammed bin Ali bin Mahmoud Al Lawati	Member	12	3,600	4,000
Sheikh Ahmed bin Awadh bin Abdul-Rahman Al-Hassaan	Member	12	3,600	4,000
Sheikh Dr. Abdullah bin Mubarak Al Abri	Member	6	1,800	4,000
Sheikh Hamoud Abdullah Hamed Al Rashdi	Resigned Member	1	300	-
Sheikh Dr. Mohammad Ameen Ali Qattan	Member (Non-Voting)	4	Refer Note	Refer Note
		Total	**14,100**	**18,000**

Note:
On 29 January 2013, Sheikh. Hamoud Abdullah Hamed Al Rashdi resigned due to health reasons and was replaced by Sheikh Dr. Abdullah bin Mubarak Al Abri. This was duly disclosed on the Muscat Securities Market and subsequently approved by the AGM held on 19 March 2013.

Sheikh Dr. Mohammad Ameen Ali Qattan was appointed as a non-voting member of SSB on 19 March 2013. He is appointed under contract with Amanie Advisory Services (AAS) for which an amount of RO 23,100 was paid during the year 2013 to AAS.

The Sharia Supervisory Board has held 12 meetings which includes 1 meeting held in 2012 before commencement of Maisarah operations.

3. Board Credit Committee

The Board Credit Committee consists of members with proper experience, skills and initiative. The objectives of the Executive Committee is to discharge responsibilities on behalf of the Board in deciding on specific policy matters demanding in-depth study and analysis, deliberation and interactive consideration and decisions on micro matters of business beyond the powers delegated to the management, but considered less important to receive the full Board's attention and time.

The Board members of the Board Credit Committee before 19 March 2013 were:

Name of Director	Designation	No. of Meetings Attended (before 19 March 2013)
1. Eng. Abdul Hafidh Salim Rajab Al-Aujaili	Chairman of the Board Credit Committee	4
2. Sheikh. Qais Mustahail Ahmed Al Mashani	Member	2
3. Mr. Ahmed Said Mohammed Al Mahrezi	Member	3
4. Mr. Ali Ahmed Salim Al Mashani	Member	-
5. Mr. Tariq Abdul Hafidh Salim Rajab Al-Aujaili	Member	3

The Board members of the Board Credit Committee after 19 March 2013 are:

Name of Director	Designation	No. of Meetings Attended (after 19 March 2013)
1. Eng. Abdul Hafidh Salim Rajab Al-Aujaili	Chairman of the Board Credit Committee	12
2. Sheikh. Hamoud Mustahail Ahmed Al Mashani	Member	3
3. Eng. Abdul Sattar Mohd Abdullah Al Marshidi	Member	7
4. Mr. Mohammed Yousuf Alawi Al Ibrahim	Member	9

The Board Credit Committee held 16 meetings during 2013.

4. Board Audit Committee

The Audit Committee was formed by the Board of Directors with the following main objectives and responsibilities:

- To focus the attention of the Board and top management of the Bank on the importance of strong financial reporting and risk management.
- To monitor the adequacy of internal controls in the Bank and to take appropriate steps to improve them where required.
- To monitor the Bank's compliance with legal and regulatory provisions, its articles of association, charter, by-laws and rules established by the Board of Directors.
- To identify the risk areas of the Bank's operations to be covered in the scope of the internal and external audits during the year.
- To monitor the effectiveness of the internal audit function and approve the audit plan as well as the availability of adequate resources (personnel and tools) and information access.
- To recommend the appointment / change of the external auditors and determine and review their terms of engagement.
- To meet the External Auditors and hear their views before forwarding the annual financial statements to the Board for approval.
- To report and bring to the attention of the Board any matters of concern with regard to the fore-going and any material accounting or auditing concerns identified as a result of the external or internal audits, or examination by supervisory authorities.

The Members of the Board Audit Committee before 19 March 2013 were:

Name of Director	Designation	No. of Meetings Attended (before 19 March 2013)
1. Sheikh. Hamoud Mustahail Ahmed Al Mashani	Chairman of the Audit Committee	1
2. Mr. Saleh Nasser Juma Al Araimi	Member	2
3. Mr. Mohammed Yousuf Alawi Al Ibrahim	Member	1
4. Mrs. Najah Musallim Al Kiyumi	Member	2

The Members of the Board Audit Committee after 19 March 2013 are:

Name of Director	Designation	No. of Meetings Attended (after 19 March 2013)
1. Mr. Saleh Nasser Juma Al Araimi	Chairman of the Audit Committee	6
2. Mr. Ahmed Said Mohammed Al Mahrezi	Member	3
3. Sheikh. Qais Mustahail Al Mashani	Member	4
4. Mr. Majid Said Sulaiman Al Bahry	Member	4

The Board Audit Committee held 8 meetings in 2013.

5. Board Risk Management Committee:

The Risk Management Committee of the Board was formed by the Board of Directors to focus on issues relating to Risk Management policies and procedures on a Bank-wide basis by arriving at a judicious policy decision collectively.

Roles and Responsibilities:

- To understand the risks undertaken by the Bank and ensure that they are appropriately managed.
- To develop risk policies, limits and procedures after assessment of the Bank's risk bearing capacity.
- To identify, monitor and measure the overall risk profile of the Bank.
- To verify models used for pricing complex products and transfer pricing.
- To review the risk models as development takes place in the markets and also identify new risks.
- To ensure that the risk policies developed clearly spell out the quantitative prudential limits on various segments of Bank's operations.
- To build stress scenarios to measure the impact of unusual market conditions and monitor variance between the actual volatility in portfolio values and those predicted by the risk measures.
- To monitor compliance with various risk parameters by business lines.
- To hold the line management accountable for the risks under their control.
- To oversee and ensure the implementation of CBO's guidelines on risk management systems in Banks.

The members of the Board Risk Management Committee before 19 March 2013 were:

Name of Director	Designation	No. of Meetings Attended (Before 19 March 2013)
1. Mr. Mohammed Yousuf Alawi Al Ibrahim	Chairman of the Board RM Committee	1
2. Mr. Saleh Nasser Juma Al Araimi	Member	1
3. Mrs. Najah Musallim Al Kiyumi	Member	1

The members of the Board Risk Management Committee after 19 March 2013 are:

Name of Director	Designation	No. of Meetings Attended (After 19 March 2013)
1. Mr. Ahmed Said Mohammed Al Mahrezi	Chairman of the Board RM Committee	4
2. Mr. Tariq Abdul Hafidh Salim Al Aujaili	Member	5
3. Mr. Saleh Nasser Juma Al Araimi	Member	4
4.Mr. Majid Said Sulaiman Al Bahry	Member	4

The Board Risk Management Committee held 6 meetings in 2013.

6. Board Human Resources Committee:

The Human Resources Committee of the Board of Directors was formed in March 2005 by the Board to ensure that the overall human resources developments at Bank level are as per the strategic direction of the Bank.

At a strategic level, the Committee is responsible for reviewing and monitoring the following:

- Ensure manpower plans take into account, the strategic and specific resources requirements at the Bank to achieve strategic plans
- Review the Omanisation plans and ensure certain defined positions are ear-marked for prospective Omanis within a prescribed period of time
- Review exit interviews and note any dismissals or resignations for middle management and top management
- Review the recruitment policy adopted by the Human Resources Department
- Review the qualifications and experience of specific candidates for the positions at the top management levels
- Review and monitor compensation and reward policy and procedures
- Review and monitor training and development policy and process

The members of the Board Human Resources Committee before 19 March 2013 were:

Name of Director	Designation	No. of Meetings Attended (Before 19 March 2013)
1. Mr. Tariq Abdul Hafidh Sailm Al Aujaili	Chairman of the Board HR Committee	3
2. Sheikh. Qais Mustahail Ahmed Al Mashani	Member	3
3. Mr. Ali Ahmed Salim Al Mashani	Member	-

The members of the Board Human Resources Committee after 19 March 2013 are:

Name of Director	Designation	No. of Meetings Attended (After 19 March 2013)
1. Mr. Tariq Abdul Hafidh Salim Al Aujaili	Chairman of the Board HR Committee	3
2. Sheikh Qais Mustahail Ahmed Al Mashani	Member	3
3. Eng. Abdul Sattar Mohammed Abdullah Al Marshidi	Member	3

The Board Human Resources Committee held 6 meetings in 2013.

7. Board Investment Committee

The Board Investment Committee is a newly formed Board committee on 19 March 2013.The Committee oversees management practices on investment matters. The Committee, on behalf of the Board, monitors investment activities, as well as compliance with policies and regulatory requirements. The Committee ensures that the management undertakes appropriate measures to recognize adverse trends, to identify problems in investment portfolio. The Committee also approves investments (in accordance with the authorities granted by the Board and as specified in the Authority Matrix) and wherever relevant, investment matters in business activities.

The members of the Board Investment Committee during 2013 are:

Name of Director	Designation	No. of Meetings Attended
1. Eng. Abdul Sattar Mohammed Abdullah Al Marshidi	Chairman of the Board Investment Committee	7
2. Mr. Tariq Abdul Hafidh Salim Al Aujaili	Member	3
3. Mr. Mohammed Yousuf Alawi Al Ibrahim	Member	7

The Board Investment Committee held 7 meetings in 2013.

8. Directors' Remuneration and Executives Pay

As all members of the Board are non-executive directors, no fixed salary or performance-linked incentives are applicable. The non-executive directors are paid an annual remuneration and sitting fees for attending the Board / Committee meetings. Directors' proposed remuneration and sitting fees paid during 2013 are as follows:

	Proposed Remuneration RO	Sitting Fees Paid RO	Total RO
Chairman of the Board	14,605	10,000	24,605
Board Members	99,695	75,700	175,395
Total	**114,300**	**85,700**	**200,000**

The Bank's top six executives, namely the CEO (since resigned), Acting CEO, GM –Wholesale Banking (since resigned), DGM – Retail Banking, DGM - Finance, DGManager - Treasury & International have received the following in 2013:

	Salaries, Performance Bonus & Others
Top Six Executives	**RO 1,591,000**

Incentives other than the fixed payments are linked to the performance. Performance is measured against the preset objective for contribution towards achievement of Bank's overall goals. The period of services contract for expatriate executives is two years while the notice period for the executives is three months.

9. Compliance with Regulatory and Control Requirements

The Bank adhered to and complied with all relevant regulatory requirements in the last three years except one instance in 2012 when the bank was penalized for RO 66 by two of its regulators. The Bank has taken all corrective and necessary measures to avoid similar instance in future.

Also the Bank complied with all provisions of the Code of Corporate Governance issued by the Capital Market Authority.

10. Communication with Shareholders and Investors

All financial and non financial information are disseminated in a timely manner and a cost efficient access is provided to the users. The management provides regular updates to the market on the Bank's performance and new developments. The management discussion and Analysis Report form part of the annual report besides detailed disclosures in accordance with regulatory requirements and international standards.

The Bank publishes its quarterly interim financial statements and also hosts these and other relevant information at its website (www.bankdhofar.com) and Muscat Securities Market (MSM) website (www.msm.gov.om). The quarterly results are also published in two local newspapers in Arabic and English. These results remain available for the shareholders from the Bank. Bank's all official news releases are displayed on the Bank's website.

11. Market Price Data

a. Share Price Movements

The high/low share price information of the Bank during the financial year ended 31 December 2013 compared with Muscat Securities Market Financial Sector Index is as follows:

2013	BankDhofar Share Price (RO)			MSM Financial Sector Index
Month	High	Low	Closing	Closing
January	0.374	0.357	0.371	6763.81
February	0.400	0.372	0.380	7050.81
March	0.416	0.359	0.383	7271.51
April	0.400	0.371	0.374	7499.45
May	0.380	0.351	0.354	7718.99
June	0.378	0.340	0.362	7728.43
July	0.382	0.367	0.370	8820.42
August	0.390	0.363	0.365	8198.92
September	0.370	0.360	0.366	8113.85
October	0.366	0.358	0.360	8166.84
November	0.368	0.354	0.354	8127.79
December	0.370	0.356	0.364	8153.11

b. Major Shareholders

The following are the major shareholders who own more than 5% of the outstanding shares as at 31 December 2013:

Sr. No.	Shareholder	Percentage of Ownership
1	Dhofar International Development & Investment Holding Company (SAOG)	27.82%
2	Eng. Abdul Hafidh Salim Rajab Al Ajuaili & his companies	20.84%
3	Civil Service Pension Fund	10.04%
4	Ministry of Defence Pension Fund	8.58%
5	Public Authority of Social Insurance	8.26%
6	H.E. Yousuf bin Alawi bin Abdullah & his Companies	6.85%
7	Qais Omani Establishment LLC	6.27%
8	Others	11.34%
	Total	**100%**

12. Profile of the Statutory Auditors

The shareholders of the Bank appointed KPMG as the Bank's external auditors for the year 2013. KPMG is a leading accounting firm in Oman and is a part of KPMG Lower Gulf that was established in 1974. KPMG in Oman employs more than 130 people, amongst whom are 4 Partners, 5 Directors and 20 Managers, including Omani nationals and is a member of the KPMG network of independent firms affiliated with KPMG International Co-operative. KPMG is a global network of independent firms providing Audit, Tax and Advisory services and has more than 155,000 people working together in 155 countries worldwide. KPMG in Oman is accredited by the Capital Market Authority (CMA) to audit joint stock companies (SAOG's).

13. Acknowledgment

The Board of Directors acknowledges confirmation of:

- Its responsibility for the preparation of the financial statements in accordance with the applicable standards and rules.
- Review of the efficiency and adequacy of internal control systems of the bank and that it complies with rules and regulations and internal policies.
- There are no material matters that affect the continuation of the bank and its ability to continue its operations during the next financial year.

14. Other Matters

- During 2013, the Bank has fully complied with all directives of the Code of Corporate Governance issued by the CMA.
- The Bank has been declared as the winner for the Corporate Excellence Governance Award 2013 by the Capital Market Authority. The award distribution ceremony was held on 17 December 2013 at 6.00 pm at Grand Hyatt.
- The Statutory Auditors of the Bank are KPMG. The Professional fees paid or payable to auditors for 2013 is RO 49,105. This amount represents RO 38,850 paid for audit services and RO 10,255 paid for non-audit services. In addition, the professional fees paid or payable for Islamic Banking Window is RO 16,500. This amount represents RO 10,000 for audit services and RO 6,500 for Sharia audit.
- The last Annual General Meeting was held on 19 March 2013. The meeting was conducted as per statutory requirements.

Management discussion and analysis report for the year ended 31st December 2013

Strategy and Planning

With a rich history of 23 years of operating in Oman, BankDhofar continued on a steady stride to becoming the ‘best bank for you’. 2013 was a year of reinforcing the Bank's identity as a progressive bank that focuses on providing the customer with the best banking experience suitable to their needs.

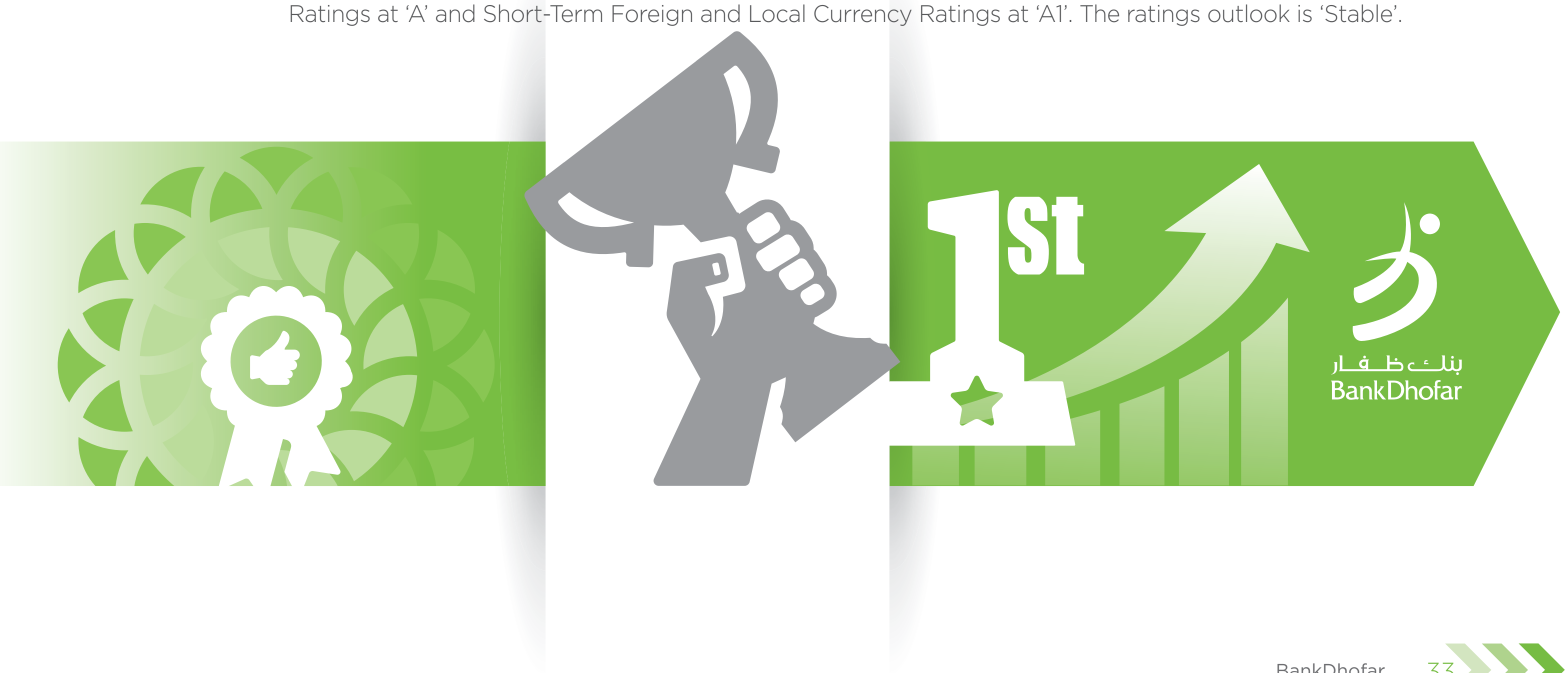
The Bank has been able to establish a solid platform for delivering services to the customer, quickly and conveniently. This was accomplished by enhancing the Bank’s delivery model through several means, whether it is branches, e-channels, or product variety, the customer and their experience is always at the center of it all.

Now as the Bank enters the third year of its 5 Year Plan, the customer stands to fully realize the benefits of the many initiatives implemented in 2013. Moving forward, the Bank’s internal operations and Human Resources will be an area of major focus. By focusing on people and processes together to complete the experience, BankDhofar will distinguish itself as the leading provider of conventional and Islamic financial services.

Economic Scenario and Outlook

The positive domestic economic performance continued in 2013 due to the prudent macro-economic policies adopted by the government among other things. As per the budget unveiled earlier this year, the domestic GDP is forecasted to increase by 5.0% in 2014. In line with the diversification plan, major thrust is given to growth and development of non-oil segments such as tourism, agriculture , fisheries etc. Total revenue during the year is forecasted to increase by 4.9 per cent to RO11.7 billion and total expenditure to increase by five per cent to RO13.5 billion. Oil prices have been considered at $85 per barrel and at an average daily production of 945,000 barrel of oil per day for the 2014 budget projections. The increased government expenditure, of which approximately 24% is directed towards development projects is likely to results in newer projects being undertaken, increase the employment opportunities for nationals, pave way for the development of Small Medium Enterprises (SME) sector etc.

Standard & Poor's (S&P) Ratings Services recently affirmed its A/A-1 long- and short-term foreign and local currency sovereign credit rating and also assigned a stable outlook. Another international credit rating agency, Capital Intelligence (CI) has also affirmed Oman's Long-Term Foreign Currency and Local Currency Sovereign Ratings at 'A' and Short-Term Foreign and Local Currency Ratings at 'A1'. The ratings outlook is 'Stable'.



Wholesale Banking Group

BankDhofar Corporate Banking endeavors to be the most preferred, professional and reliable corporate bank delivering superior service to its target customers through a team of motivated and skilled personnel in a cost-effective manner through building and strengthening corporate relationships with an acceptable risk and reward policy.

Wholesale Banking Group (WBG) consists of the following departments:
(i). Large Corporate Banking and Project Finance & Syndications Department (ii) Mid Sector Corporates Department (iii) Business Banking Department (iv) Payments & Cash Management Services (v) Corporate Advisory & Investment Banking (vi) Remedial Management Department (vii) Trade Products (Sales)

The rationale behind this set up is to focus on different segments of businesses and provide a full range of Commercial and Corporate banking services under a single umbrella, through dedicated relationship managers. The business strategy for WBG is guided by all-round business growth with quality portfolio by adhering to various statutory and regulatory guidelines. Different departments within Wholesale Banking Group complement each other in extending timely and efficient service to customers, and facilitate better internal controls and process efficiencies. WBG has undertaken many initiatives in consolidation of operations and also integration of different activities with customer centric approach.

In this regard, the Bank has identified a new business opportunity in Small & Medium Enterprises (SMEs) and brought this under the fold of Wholesale Banking Group so as to bestow special attention to this area. CBO guidelines on SME funding and also Government initiatives for the development of the small & medium enterprises in the Sultanate provide an opportunity for the Bank to associate with the development of this sector. In order to strengthen the Government's initiative and to enhance its participation in the growth & development of the SME sector, the Bank has chalked out a long term business strategy for this important segment.

Large Corporate Banking & Project Finance & Syndications Department

Large Corporate Banking continues to play a vital role in WBG by concentrating on top end customers with large exposures. The customer base also spans various industries which include Trading, Manufacturing, Services and Contracting. Similarly, the credit requirements of these high-end customers are varied and dynamic which is in tune with changing business opportunities. Thus, constant interaction with customers is needed to understand their business cycle & working capital requirements.

Our emphasis continues to be on the development of tailormade financial solutions that are suited to the particular needs of the customers. Regular coordination cooperation meetings among various departments of the Bank are being held to ensure prompt delivery/sale of different Bank's products (viz. retail banking, treasury and personal banking products) to our customers, irrespective of the banking segment they belong to. The department also strengthened the Relationship Team by providing dedicated Credit Analysts for back office support functions, which has improved the control mechanism and turnaround time for customers. The Bank also introduced a new Credit approval automation process for quick credit assessment by introducing a software package which resulted in quicker turnaround times, and a better information capture & retrieval process.

Project Finance & Syndications Department

The Bank has a dedicated team of professionals in this area to arrange, syndicate and participate in various infrastructure and other projects initiated by the Government /semi Government companies and private sector. It has worked out a strategy to increase the mix of working capital, project finance & syndication exposure for such customers, so as to optimize the return on the portfolio under this segment.

Over the years, the Bank has participated in many of the major infrastructural projects including the projects of Oman India Fertilizer Company LLC, Sohar Aluminium, Oman LNG, Oman Gas, Salalah Port, Oman Refinery expansion and the six power and water projects. The Bank has a good relationship with local, regional and international banks for the purpose of ensuring full participation.

Mid Sector Corporate

The Bank created a dedicated division, namely the mid segment Corporate Banking Department, which caters to the needs of growing corporates. The Bank is adopting a sectoral approach, in marketing new offerings/products for various businesses from each sector. An exhaustive list of potential clients in each segment is prepared and a bundled suite of retail and treasury products is offered, to attract new customers.

Over a longer term, this particular segment is expected to witness growth in tandem with the growth of the country's economy. The focused approach for this particular segment will enable the Bank to reap the benefits arising out of the growth in the individual businesses, who eventually transform into large corporate customers.

Business Banking Department

Realizing the importance of the Small & Medium enterprises (SME) to the development of a vibrant economy, BankDhofar has taken strategic initiatives to further the development of SME's in the country. This is in tune with the recently issued CBO guidelines and other Governmental initiatives. The Bank has created a separate department headed by a Senior Management official and worked out a Business strategy for this segment so as to focus on this thrust area. The Small & Medium Enterprises' business requirements are wide and varied in nature, and credit exposure to this segment is associated with peculiar risk characteristics. The customers in this segment need to be handled by skilled and experienced resources to understand the specific business requirements to provide timely & adequate credit delivery. In this direction, the Bank is initiating steps to further strengthen the resources and processes aimed at providing efficient banking services to this emerging business segment, the Bank endeavours to achieve quality growth in portfolio, by participating in the development of SME businesses in the country.

Payments & Cash Management Services

Cash Management is a set of services/products that a corporate uses to manage all aspects of the financial cash flows i.e. collection of revenue, disbursements of expenses/ payables, tracking as well as the investment of surplus funds. This helps corporates to stay afloat financially. The Bank proposes to offer technologically advanced tailormade products & services to customers that can add convenience value in their day to day banking needs. The department was created to offer the above value added services to corporate customers, is headed by an experienced resource and expects to increase its share in this line of business.

Corporate Advisory & Investment Banking Services

Wholesale Banking offers specialized services of strategic advisory across a range of industry sectors including Oil & Gas, Telecom, and Financial Institutes, by providing tailor made solutions and products such as M&A, Divestitures, Capital Planning, Capital Structures, Private Placement, Startups, Joint Ventures, Business Re-engineering, Feasibility Studies, Financial Structuring, Raising Equity and Raising Debt, so as to maximize bottom-line opportunities for the Bank's clients. The Bank proposes to further strengthen the Corporate Advisory Team to provide seamless services to our corporate customers to serve as a one stop shop. The business under this segment is driven by a well experienced Senior Manager.

Remedial Management Department:

This department has been created within the WBG group to identify Early Warning signals and incipient sickness problems in accounts. This department helps the front office business units in initiating appropriate advisory & restructuring measures for the identified incipient sick account, in a timely manner in order to maintain a healthy portfolio.

Trade Products (Sales) Department:

A separate Trade Products Sales Department markets and develops products in the Trade Finance area. A dedicated officer from the department assesses the needs of corporate clients specific to trade finance and suggests suitable structured products to improve usage of non-fund based (NFB) facilities from the Bank.

Retail Banking Division

The Retail Banking Division (RBD) of BankDhofar continued its focus on providing value-added products and services to the customers. The Bank continued its growth and expansion strategy in 2013, strengthening its distribution channels with the addition of more branches, ATMs and CDMs, besides launching Mobile Banking.

The year 2013 saw the addition of 3 new branches in Salalah Grand Mall, Adam and Al Duqum. The year ended with 65 branches, 2 kiosks, 140 ATMs and 48 CDMs.

Retail Products, Business & Segments

During 2013, the Retail Products, Business & Segments team has worked on enhancing existing products as well as designing, developing and implementing new products and offerings.

Retail Assets Products

In 2013, to drive growth in the overall asset portfolio, several best-in-class personal loan and housing loan product offers and campaigns were launched. In 2013 BankDhofar launched two new lending products (Car loan and Education loan), providing an exclusive banking experience for customers by making these loans the most competitive products in market. The housing loan campaign continued for the second year, providing best customer service in Oman, facilitating customers to own a new home within 5 days at most competitive and affordable pricing. The Bank also launched a special package to target large corporate employees. With focused effort in a number of key areas, BankDhofar saw a healthy growth in the personal lending and housing loan segment.

Retail Liabilities Products

In February 2013, the new savings scheme was launched. The Bank offered a weekly prize of OMR 5,000 and 10,000, a monthly prize of OMR 100,000 and annual prize of OMR 1 Million. Due to the enhanced scheme the Savings product showed considerable growth in the Bank's Liabilities Portfolio.

Credit Card Business

In 2013 BankDhofar launched the Pre-embossed Credit Cards to provide customers with prestigious credit cards that are internationally recognized. The Cards business unit is an important wing within the retail business space, with special focus on identifying areas of enhancement, improving card performance and profitability. The Cards business unit is also looking at developing new policies and products to promote cards, having competitive campaigns to give card customers the best value for their money, and ensuring that the Bank develops and maintains its competitive edge at all points in time.

A renewed focus on cards resulted in developing a long term strategy for the Bank's credit cards portfolio, with clear business objectives and expectations in terms of contributions from the portfolio.

Bancassurance Products

Bancassurance offers domestic helper and family protection, in addition to motor insurance. These services are provided by the Bank through an insurance agency. The insurance covers all kinds of policies and offers the best no claim bonus discount in the market.

Retail Segments

During 2013, the Retail Segments team worked simultaneously with Retail Liabilities and

Assets units to launch savings and loans products that catered to the needs of the different customer segments, ensuring maximum customer satisfaction as well as aiding in the growth of the Bank's Asset and Liabilities portfolios. Retail Segments enhanced the Bank's product services and benefits for each of its customer segments. In February 2013, BankDhofar launched the Salary Acquisition scheme where daily prizes were offered to double the customer's salary.

The Bank strongly believes in the need for bringing about a positive change in the lives of different segments of society and focuses on all types of products that fall within the development of the key segments and their importance and overall benefit, both to individuals and to society. The prime objective of the segment division is to include the benefits reaching the largest number of individuals; the youth and job-seekers and the lucrative VIP segment.

Customer Relationship Management (CRM)

There is a large opportunity to improve customer experience and boost sales if the Bank has additional information about its customers. The CRM project will also help the Bank determine which customers are eligible for other products. Moreover, obtaining additional information about customers enables the Bank to measure or focus on:

- Customer acquisition
- Customer satisfaction
- Customer retention
- Improving the effectiveness of communications to customers, improving response rates and returns on marketing investment
- Prepare for launch of other products & services

Electronic Banking

The world over, banks are reorienting their business strategies towards new opportunities offered by e-banking. E-banking has enabled banks to scale borders, change strategic behaviour and thus bring about new possibilities.

Today, most customers use multiple channels to research products, open, use and manage their accounts, resolve issues and receive notifications. The key for the Bank is to determine the optimal channel mix for each customer that will maximize revenue (or reduce costs) without significantly reducing customer satisfaction or engagement.

The Bank believes that, through e-banking, customers today can interact with their bank more effectively. The eBanking team is, therefore, focusing on migrating customers from traditional banking to BankDhofar Online Banking, Mobile Banking and Self-Service machines.

Self Service Machines are distributed across the country with a host of convenient services such as Nawras prepaid top-up and bill payment. In addition, American Express card holders can pay their past dues through the Bank's CDMs.

The highlight of the e-banking Department this year was the launch of Mobile Banking which was introduced on 10th September 2013. This was a totally customer-centric initiative with carefully selected features such as fund transfer within the Bank, prayer timings, locator, utility payments and more. Through Mobile Banking, the Bank has migrated customers from the traditional way to a much better experience through state-of-the-art technology. The application was downloaded by several users with very positive reviews and feedback.

To complete the loop, the Bank's Call Centre has introduced even more services to enhance customer experience. The Inter-active Voice Recoding (IVR) system has been enhanced with features such as announcement of expected waiting time/queue size, call back facility and a new system for outbound dialing. In total, 12 new services have been added this year to the Call Centre service list.

As part of the distribution plan for 2013, the electronic channels witnessed a remarkable development which improved service levels. New services were added in the Call Center such as:

1. The following features were introduced on our IVR system
   - **a.** Announcement of expected waiting time
   - **b.** Announcement of queue size
   - **c.** Call back facility
   - **d.** Show customer waiting time to the agents
   - **e.** Announcement of balance
2. A new system was introduced for Outbound Dialing
3. LOS System: The Call Center is now equipped to respond to customers asking about the status of their loans
4. 3D Token : Resetting and unlocking
5. STP – Set up Password for Online Banking
6. Assisted the CRM with Data clean up using the outbound dialing
7. Pre-imposed card activation by emails
8. Enable, disable, unsubscribe, unlock, and detag customers on Mobile Banking

The Call Center helped in generating increased amount of business through inbound and outbound campaigns. To ensure customer satisfaction, a strict quality control procedure has been implemented. Furthermore, the Call Center staff were put through periodic training programs on products and customer handling skills. Over the last 12 months, the Call Center continued witnessing an increase in the number of calls being handled by staff.

The ATM network has increased to 140 ATMs and 48 CDMs. including 14 additional ATMs and 5 CDMs were added during 2013. New services were added such as foreign currency withdrawals for BankDhofar and non BankDhofar customers with multiple rates for multiple customer segments at selected ATMs, due payments for American Express cards through BankDhofar CDMs and bill payments and top up for Nawras subscribers through BankDhofar CDMs.

More services were added to internet banking such as local fund transfers with competitive rates. The instant registration process and the creation of pre-printed User ID and passwords helped to increase the number of customers using internet banking channel in both Retail and Corporate segments. More services were added to Internet Banking such as Nawras top up and bill payment, in addition to AMEX payments where customers maintaining a BankDhofar account and holding an AMEX card can pay their dues. In addition, eBanking has witnessed a significant turning point with the launch of Mobile Banking which is totally customer-centric with features such as utility payment, credit card payment, mobile top up, prayer timing, locator, etc. and offers an excellent customer experience.

Retail Projects and Customer Experience

In 2013, the Retail Project and Customer Experience team worked as a catalyst for the Retail banking division and helped achieve customer focus, stakeholder value and business process management delivery. Major deliveries included conceptualization and deployment of the following projects and assignments which has been ‘first to market’ as well.

- Evening banking model
- Loan Origination System (LOS)
- MGM operating model to sell and serve effectively
- Instant issuance deployment
- Teller Cash Recyclers (TCR)
- KIOSK banking (Mini branch model)
- Home abolishment model journey being initiated, to enable customers to transact easily across the branch network

Key business processes were studied, gaps identified and re-engineered cross-functionally to optimize and remove steps that did not add value.

Treasury & International Banking

Treasury BankDhofar prides itself on being one of the proficient Dealing Rooms in Oman, providing corporate and individual clients with a wide selection of foreign exchange (FX) & Interest Rate products ranging from the traditional to the customized. Our expert team provides solutions that meet the demands of liquidity, cash flow management, interest rate fluctuations and FX volatility.

Treasury provides client-centric solutions and according to their needs, Treasury offers FX products ranging from Spot, Forward and Swaps that helps valued clients hedge their FX exposure.

In addition, Treasury Division provides its valued customers with up-to-date information about products and markets on daily basis by emails, and has conducted various workshops for its esteemed clientele, with the aim of outlining the different hedging techniques and services offered in the Treasury Dept.

The Department's working hours have been changed as well to cater more to clients' needs. The Dealing Room is available from 07:45 local time to 19:00 hrs local time from Monday to Thursday, from 07:45 to 15:00 hrs local time on Sunday and from 09:00 to 15:00 hrs on Friday. They also offer an order taking, monitoring, advisory, and execution service outside normal hours; ensuring clients' needs are met. Treasury is also happy to provide information on market developments, ideas on managing exposures, even organizing seminars on specific topics.

In the wake of global economic crises across major financial markets since 2008, the Treasury division is consistently performing proficiently. Especially during 2013, when the deposits grew significantly the cost of funds was kept low. During 2013, the Division actively participated in different types of treasury tools in order to enhance further the Bank's yield on its liquid cash.

BankDhofar is one of the leading market makers in USD/OMR spot and swaps. The Bank offers attractive interest rates on foreign currency deposits in all major currencies to corporate, retail and high net worth individuals. BankDhofar Treasury offers highly competitive exchange rates against all currencies, especially to the emerging markets, GCC and G7 currencies.

Investments

During 2013, the Bank's investment portfolio yielded a total realized investment income of OMR 5.72 million. The portfolio follows a disciplined investment approach rather than timing the market. This, along with its active management style and emphasis on minimizing market risk by staying diversified in terms of sectors and individual holdings, enabled it to achieve high returns at lower than market risk. The Bank has adequate internal portfolio risk monitoring controls in place. Going forward, the Bank plans to grow its portfolio and further diversify its investments both in terms of asset classes and geography, so as to optimize returns on funds invested.

International Banking

The International Banking division establishes and maintains all international Correspondent Banking relationships of BankDhofar. The division ensures that BankDhofar's corporate and retail clients have access to the world through the Bank's wide network of leading correspondent banks. Capitalizing on the excellent relationship with leading regional and global banks, the division actively assists BankDhofar's corporate customers with their global trade finance requirements. Adequate credit lines from financial institutions around the globe have helped BankDhofar increase its ability to support the increasing business needs of customers.

BankDhofar continues to be cautious in its appetite towards cross border risks and has been able to identify very select business that has a sensible credit approach in terms of risk and tenor. The Bank's focus is to assure placement of sufficient money market, forex and trade lines for its correspondent banks. The Bank also ensures that correspondent banks have adequate lines for their forex and trade requirements.

BankDhofar is an active player in bilateral/syndicated/club loans and maintains a good overseas credit portfolio. The Bank retains good contacts with countries in the Middle East, Europe, Asia, South East Asia and Africa. The International Banking division has been visiting counterparties in countries in which such exposures are taken to strengthen the business relationship with correspondent banks.

The International Banking division will continue to identify the Treasury relationships and Trade Finance self-liquidating transactions within the GCC and regional markets to build a sustainable long-term relationship that would benefit both BankDhofar and its customers.

Government Banking

The Government Banking Department is an important unit of the Bank, with a focus on forging and maintaining strong business relationships with all government and quasi government organizations. This department facilitates all government banking requirements such as deposits, loans, trade, remittances and retail products, to build a relationship that is mutually beneficial.

With dedicated Relationship Managers, the department coordinates with all the branches and other units of the Bank to ensure customer satisfaction is achieved.

Information & Transformation Division

As part of the Bank re-engineering and optimizing its processes and organization structure, the Information & Transformation Division has realigned to serve the future growth of the Bank with optimal utilization of resources.

During 2013, the division took fundamental steps in laying down best practice governance through the alignment to the ITIL 'Information Technology Infrastructure Library' governance model, introducing a proper Change and Demand management that worked actively with other bank departments to prioritize the IT projects and make the best use of the available resources to serve the Bank's strategic objectives. The division also invested in its human capital through extensive training to all staff on the ITIL governance model.

Along with the maturity of the ITIL governance, the Information & Transformation Division pioneered the role of establishing an Enterprise Project Management Office (EPMO), guided by the best practice project management methodologies. This office works actively with the rest of departments to manage cross functional projects and ensure proper controls are in place to deliver projects on time within scope and budget to deliver maximum value for our shareholders.

The Transformation Department also pioneered the role of process re-engineering, with the Bank moving actively toward engaging the younger generation through alternative channels like e-banking and mobile banking. A cross functional team was formed to improve processes across the Bank with the aim to simplify transactions and make the banking experience for valued customers the Best in Gulf. 300+ processes are being evaluated, analyzed and adapted in a continuous improvement model that will leverage the Bank's extensive years of experience in the market along with new technologies deployed in the past couple of years.

The Transformation Department successfully led several projects that made a direct impact on customer experience in the branches. Today with instant issuance, customers can open an account and receive their ATM card during the same transaction, allowing the customer to start banking from day one with no delays. We also introduced automation to further our loan application processes, cutting down the turnaround time to competitive timings, compared to our peers in the industry.

A Mobile Banking solution was introduced during the year which is highly convenient, user friendly and provides a suite of comprehensive and value added services. Now, our customers can perform fund transfers, utility bill payments, mobile top-up and inquire with a host of other banking services at their fingertips. Additional services like loan payments, money transfers, online savings account opening requests, demand draft requests etc will soon be available on the mobile platform to transform the way our customers bank with us.

To position our Islamic banking window 'Maisarah' as one of the leaders in the market, the Information Technology division (IT) implemented the Islamic Core Banking platform providing Islamic Banking solutions and investment tools to address business needs. Recently the Bank implemented the Fixed Deposit Islamic product to meet customer needs and 'Diminishing Musharakah' product was implemented to meet the corporate customer's need. Maisarah customers can use their Islamic ATM card on any ATM worldwide through OmanNET and VISA gateways. Islamic ATM cards are also accepted on Point of Sale devices.

The Bank has further expanded its ATM/CDM network. It continues to meet the highest possible technological standards and provide an impressive average of 99% + uptime on terminals. BankDhofar continues to spend on uptime initiatives and has completed four such initiatives this year. The Bank's terminals are now able to service customers without paper journals, as a centralized storing and retrieval system for electronic journals has been implemented. ATM cash holding capacity has further been enhanced to ensure availability of sufficient cash during long holidays. Emphasis is given on custodian training so that terminals are kept in optimal working condition. The Bank has evaluated and selected unified monitoring tools for monitoring and handling incidents across ATMs and CDMs. This year we certified our ATMs with Master Card for acquiring transactions.

In the merchant acquiring business, the Bank introduced a new Point of Sale (POS) device last year. Our POS devices facilitate greater speed, efficiency and cost effectiveness as well as adhering to the highest international security standards and are Oman Switch certified. In 2013, the Bank has introduced dial-up POS devices to extend its coverage in Oman where mobile data coverage is not available. BankDhofar's POS devices were enabled to accept AMEX and Diner cards this year.

To enhance customer experience at branches and provide speedy services, the Digital Signage and Queue management system was implemented at select branches. Customers can also view the latest promotions and products on the LCD screens at these branches. This service will be extended to more branches in the coming year.

The Business Process Management (BPM) platform was further enhanced for retail and corporate processes and additional functionalities like RAROC (Risk Adjusted Return on Capital) was developed for effective Risk Management. The platform is continually leveraged to automate new processes supporting major re-engineering initiatives and driving efficiencies.

The Bank has invested in implementing Microsoft identity management software which is a self-service password reset solution to enable staff across the Bank to securely reset their passwords without helpdesk support. This helps the Bank to reduce the costs associated with resetting passwords, lowering user downtime and frees up valuable helpdesk resources.

Information Technology Division has implemented virtualization at its Disaster Recovery (DR) site to maximize uptime of the systems, consolidate the number of servers, the cost of power, cooling and administration; thus resulting in cost saving. Virtual machines are added to increase 50% spare capacity available on Virtual Infrastructure to cater to future requirements.

The Bank has completed the setup of a Disaster Recovery site for Islamic Banking to ensure business continuity for Islamic banking operations. Various channels/systems (CDM, AML & Datamart) were newly added to the DR approved list this year and business owners of each of these systems were able to test these systems successfully during the DR drill.

The Bank has implemented wireless network in identified locations to provide mobility and facilitate staff in accessing resources without being wired. Apart from the above, the Bank has invested in upgrading both hardware and software infrastructure such as databases, desktops and several applications including core banking. This brought enriched features for improved performance, security, manageability, productivity and greater stability.

Human Resources

The Human Resource Division of BankDhofar believes in synergizing human potential through alignment of corporate and personal goals, moving corporate culture from process to performance outcomes, developing a talent pool for success, managing people & perceptions; and always ensuring that each day is made better. This, in turn, serves as a major catalyst for creating a lasting performance culture and concentrating more on best practices to enhance the levels of Employee Engagement.

In line with the Bank's vision, retention and motivation of the workforce remains an imperative task for the HR function. The Department has taken several critical steps in this direction to ensure that we continue to remain efficient and productive in our operations, given the challenging business environment.

Year 2013 saw major Talent Management initiatives which included the Women's Development Program, launch of E-learning, Graduate Development Program, Corporate Masterclass Program and the Management Excellence Program, to name just a few. With the launch of these programs we have embarked on a journey of developing a culture which routinely identifies high potential people and accelerating their exposure to a wide range of developmental experiences. The experiences and positives from these initiatives will serve as a springboard for expanding the same

across other training and development initiatives of the bank.

On the Omanisation front, we lived up to regulatory requirements by hiring a mix of fresh as well as experienced Omani nationals, which reflects our commitment and dedication to His Majesty's vision of developing young Omanis. One of the key challenges for the year

2014 will be to retain the Omani national workforce through structured development initiatives aimed at harnessing their potential and providing a platform for faster growth.

In a year of business challenges, we adopted a highly need-based and focused approach to address priority value-added training requirements. During the year 2013 we conducted and organized 263 training programs with 2750 participants. Aiming to cover a wider range of programs and participants, the e-learning initiative was launched in 2013.

Progressing further on the Balanced Scorecard implemented last year, we reached out to a wider audience this year by managing the performance management and appraisal process through

Balanced Scorecard. This serves as a strong measure in building a 'Strong People and Performance' culture in the bank. To be in line with the market standards and to benchmark best practices, we participated in HAY salary survey during the year.

The state-of-the-art learning and development center 'BankDhofar Academy' which was opened last year with a strong commitment to being a continuous learning organization, with its strategic and development oriented training programs, helps the Bank in fostering learning excellence, competence and unbridled talent to enable BankDhofar to be a leader in business and people practices.

Employee engagement is vital for any organization's success. BankDhofar is committed to creating fulfilling work experiences that enable employees to contribute fully to the Bank's short, medium and long term goals. In our journey towards achieving the Bank's vision, the employee engagement program was launched to understand employees better and to know what makes them engaged. The employee engagement survey was an overwhelming success with a participation rate of 83%. A follow up, 'Let's Talk, Employees' voice interactive program was also launched this year, to enable open communication within the Bank. These initiatives will enable the Bank to focus on key areas to create an environment in which employees will do their best work, promote a positive work-life balance, and foster a sense of energy, ownership and personal commitment to their work.
The HR Department's aim is to inspire and tap into our employees' innovation, and recognize and reward significant achievements. This is directed towards the ultimate objective of making BankDhofar the best place to work.

Central Operations Division (COD)

The scope of COD has widened with centralization of branch functions and transfer of functional areas from Head Office Departments to COD, during the year. The volume of transactions processed at COD has continued to grow steadily and by effective utilization of technological solutions to automate routine processes, productivity of the team is being increased. COD also works towards maintaining high operational standards, efficiency and reduce operational errors.

COD has been continuously working on streamlining the work flows at the branches aimed at improving and simplifying the processes at the branches, thus eliminating operational errors and enabling the branches to focus on customer service and business development.

As per the Bank's Strategic Plan, Branches Operations Department (BOD) was established during the year. The initiatives taken by the Division in maintaining and monitoring ATMs/CDMs, have resulted in improvement to 99% ATMs/CDMs uptime throughout the year. The Division has also contributed significantly in planning and conducting Disaster Recovery Drills and testing of Business Continuity Plans at Branches by assisting Risk Management Division.

Retail Banking Division was supported by allowing Branches to take faster credit decisions on Retail Loans as the Division promptly provided BCSB reports directly to Branches through a centralized channel. Further, a specialized Retail Remedial Team was set up to assist Branches by maintaining direct and close follow up with Retail Customers for recovery of past dues in Retail Loan products. Due to such concentrated follow up, any abnormal growth in Non-Performing Assets / Loan Loss Provisioning for Retail Loan Portfolio was mitigated.

Branches Operation Department

As per the Bank's Strategic Plan, the Branches Operations Department (BOD) was established in 2013. The initiatives taken by this Division in maintaining and monitoring ATMs/CDMs have resulted in improvement to 99% ATM/CDM uptime throughout the year. The Division has also contributed significantly by assisting Risk Management Division in planning and conducting Disaster Recovery Drills and testing of Business Continuity Plans at branches.

The Retail Banking Division was strengthened by allowing branches to take faster credit decisions on Retail Loans, as the Division promptly provided BCSB reports directly to Branches through a centralized channel. Further, a specialized Retail Remedial Team was set up to assist Branches by maintaining direct and close follow up with Retail Customers for recovery of past dues in Retail Loan products. Due to such concentrated follow up, any abnormal growth in Non-Performing Assets / Loan Loss Provisioning for Retail Loan Portfolio was avoided.

The following tasks were successfully completed in 2013.

Key achievements of 2013:

- Improved ATM uptime for all branches, achieving above 99%.
- Reduced retail defaulted account provisions to the lowest.
- Completed centralization of BCSB Report request in all regions with nil complaints.
- Successfully coordinated with Finance department to reduce the number of outstanding items related to balancing of account in branches by 70%.
- Successfully monitored cash holding limits of branches, followed up with cash excess report to guide branches on maintaining cash balance limits.
- Coordinated with Credit Operations Department (COD) in review & rationalization of existing Branch reports, based on necessity and updating of logic for the reports generated.
- Process review, simplification and automation of
  - Roll out of Teller Cash Recycle first phase
  - CBO correspondence on public prosecution letters
  - ROP letters for CCTV camera recording on ATM & CDM
  - Assist COD in monitoring of excess cash holdings at branches
- Successful support and coordination with Internal Audit Department to facilitate special investigations.
- Successful guiding and coordination with Retail Banking Division on expanding branches network within the stipulated time frame.
- Coordination with Risk Management in Business Continuity Planning (BCP) and with branches on disaster recovery drill.
- Successful support and coordination with Investment Department during IPO.

Card Services Department

The Bank's Card Services recorded healthy growth this year. In 2013, the Card Service Center

(CSC) launched the Bank's Point of Sale (POS) acquiring services to become the second acquirer in the Omani market: a significant milestone for BankDhofar. The Bank's POS services are offered to a sizeable network retail merchants and some Government entities, providing end-to-end solutions to corporate clients.

Another noteworthy achievement of the Card Services Centre was the launch of the Bank's first Islamic Debit Card, in association with Visa. This product enhances the Bank's Islamic Banking capabilities, offering Islamic Banking customers the gamut of Visa services to access their accounts worldwide.

The Card Services Centre also upgraded the Bank's existing Al Riadah Visa Infinite Cards and Al Riadah Master Cards from magnetic strip cards to CHIP based cards, resulting in better security features for the Bank's Priority Banking customers (Al Riadah). This feature will protect cardholders from potential fraudulent usage / skimming of their cards.

During the course of the year, various card offerings, promotions and merchant tie-ups were arranged by the Card Services Center for the Bank's cardholders. These value-added promotions enhance the benefits accrued to cardholders, while also improving the visibility of the Bank.

The Card Services Center also launched new credit card SMS services during the year. This service provides customers appropriate information and reminders about their usage/balance periodically, without them having to monitor their accounts closely. Customers have welcomed this initiative as convenient and easy.

Risk Management

Risk Management Structure

The primary responsibility of understanding the risks assumed by the Bank and ensuring that these risks are appropriately managed is vested with the Board of Directors of the Bank. The Board has set risk policies, limits and procedures by assessing the risk bearing capacity of the Bank.

The overall risk management has been delegated to an independent Risk Management Committee (RMC) of the Board of Directors of the Bank, which monitors and controls the overall risk profile (ncluding the Islamic Window 'Maisarah'). The RMC reports to the full Board on matters of significance and keeps the Board continuously updated with the Risk Management processes in the Bank. In this task, RMC relies on an independent Risk Management Division.

The Bank has a well-established Risk Management Division (RMD) with a team of competent and experienced professionals. The primary responsibility of the RMD is to ensure on a continuous basis that an effective risk management framework exists and the various divisions of the Bank (including Maisarah) function within this framework. RMD also functions as an interface between the Management and the Board in defining appropriate risk tolerance levels for various business lines and operating divisions, ensuring that policies and procedures are tailored to the defined tolerance levels.

The Bank's risk management strategy statement is expressed as follows:

- Compliance with regulatory capital requirements
- Ensuring balanced performance across business units
- Placing emphasis on the diversity, quality and stability of earnings
- Making disciplined and selective strategic investments
- Maintaining capital adequacy
- Providing qualitative and quantitative benchmarks to gauge broad alignment between initiatives and risk appetite
- Stable funding and strategic liquidity management allowing for business planning within the liquidity risk tolerance and regulatory requirements

The Bank defines risk strategy and risk appetite on the basis of the strategic plan to ensure alignment of risk, capital and performance targets. The risk strategy of the Bank includes the Risk and Capital Plan and risk appetite, which allow the Bank to:

- Review the capital adequacy requirement goals with respect to risk, considering the Bank's strategic focus and business plans;
- Assess risk-bearing capacity with regard to internal and external requirements; and
- Apply stress testing to assess the impact on the capital demand, capital base and liquidity position.

Management of Various Risks

A brief account on the various identifiable risks and their risk management process is given below:

• Credit Risk

Credit risk is defined as the possibility that a borrower or counterparty will fail to meet its obligation in accordance with agreed terms in relation to lending, trading, hedging, settlement and other financial transactions. This risk is primarily managed by proper assessment of inherent risks in credit proposals and ensuring a balanced portfolio of customers meeting the risk appetite of the Bank. The Bank also ensures dealing with customers of good credit standing, a thorough and professional credit assessment process, obtaining collaterals to mitigate risks and continuous monitoring of the accounts. The Bank has taken the following measures to mitigate credit risk:

- Credit Risk Policy addresses credit risk emanating from lending to corporate, individuals and broad criteria for retail loans in a structured manner and is reviewed/updated on a regular basis. The policy has been defined for both Conventional Banking and Maisarah (Islamic window) separately. The policies of the Bank encompasses organizational responsibilities, prudential limits, credit risk rating standards, risk pricing standards, loan review mechanism, delinquent account management and portfolio management.
- Counterparty Credit Risk Policy addresses credit risk from banks as counterparties. The maximum exposure that can be taken on counterparty is specified by an internally developed model in conventional banking and through judgmental approach in Maisarah.
- The Bank has a credit risk rating system and a risk grade is assigned objectively to a borrower based on the single point score provided by the rating model. The grade is assigned to the Standard category of borrowers on a scale of 7.
- Various credit risk models are used to assess the obligor risk as well as the facility risk in conventional banking. Thus, while assessing the credit risk of the borrower, both probability of default and loss given default is estimated. In case of Maisarah, obligor rating is undertaken.
- Risk Adjusted Return on Capital (RAROC) is computed to assess the risk based pricing of each facility, which facilitates in informed decision making.
- The Bank conducts stress tests to assess the impact of credit risk on capital adequacy and profitability under stress situations.
- All the corporate credit proposals from both conventional banking and Maisarah are reviewed by the RMD to assess the risk factors and suggest mitigants. The observations of RMD form an important input in credit decision.

The Bank employs experienced and competent staff in the areas of Corporate Banking and Maisarah and provides them with regular training to upgrade and hone their credit skills. Detailed credit policies and procedures, strict adherence to the segregation of duties principle, elaborate and well defined authority levels, periodical audit and examination by the internal auditors ensure that the culture of risk permeates through the business divisions supported by a rigorous environment of checks and balances.

• Liquidity Risk

Liquidity Risk is the potential inability of the Bank to meet its maturing obligations to counterparty.

Liquidity planning and management are necessary to ensure that the Bank has the ability to fund its liquidity requirement effectively and to meet current and future potential obligations such as loan commitments, contingent liquidity commitments and unexpected deposit outflows.

The Bank has constituted Asset-Liability Management Committee (ALCO), which is responsible for setting the broad framework for managing the liquidity risk effectively for both the conventional banking and Maisarah. The responsibility of managing the liquidity risk of the Bank, within this framework, lies with the Treasury Department of the entities viz., conventional banking and Maisarah, which discharges this function with the assistance of other business divisions of the Bank. The Bank has a Board approved policy for both the entities on liquidity management which encompasses assessment of liquidity gaps through cash flow and static approach, reserve against deposits, lending ratio, mitigation of liquidity risk and contingency measures. The Bank has set up a Middle office within RMD to ensure that the Treasury Department of both the entities operates within these guidelines.

The Middle office regularly monitors the liquidity position of the Bank and helps in managing the liquidity gaps, well in time. It also conducts liquidity risk stress test periodically and the Treasury Department ensures that sufficient liquid assets are available with the Bank to meet any business exigency.

- **Market Risk**

Market risk is the risk of loss arising from unexpected changes in financial prices arising out of changes in interest rate, exchange rate, bond, equity and commodity prices. The Bank has major exposure in currency, equity and interest rate risk.

Treasury Risk Policy and Investment Management Policy of the Bank address all the aspects of the market risks. The Treasury Risk Policy addresses foreign exchange risk and interest rate risk whereas the Investment Management Policy addresses the equity risk.

The major foreign currency in which the Bank deals on a regular basis is United States Dollar (USD). The established parity between US Dollar and Omani Rial (OMR) substantially reduces this risk. However, in order to control currency exposure risk, limits for intraday and overnight positions have been set up in addition to currency-wise stop loss limits. Limit on net open position has been placed to restrict the Treasury department to take undue currency exposure as per prudential norms set by Central Bank of Oman (CBO). All these limits are monitored by the Middle office of the Bank.

The Bank manages the interest rate risk by matching the re-pricing of assets and liabilities and operating within the set gap limits. Middle office in RMD regularly monitors the impact of adverse movement in interest rate on profitability and economic value of equity in conventional banking.

Maisarah is also vulnerable to profit rate risk. Profit rate risk is the risk that Maisarah may incur a financial loss as a result of mismatch in the profit rate on the Maisarah assets and Investment Account Holders. The profit distribution to Investment Account Holders is based on profit sharing agreements. Therefore, Maisarah is not subject to any significant profit rate risk. However, the profit sharing agreements will result in displaced commercial risk when Maisarah's results do not allow to distribute profits in line with the market rates. In order to mitigate displaced commercial risk, Maisarah has set up prudential reserve accounts such as Profit Equalisation Reserve (PER) and Investment Risk Reserve (IRR).

Middle office monitors equity portfolio through daily reporting and assess the risk inherent in the quoted domestic equity portfolio through Value at Risk (VaR) approach. Various limits like stop loss limit, transaction deal limit and realized loss limit are in place to manage the equity risk. All the investment proposals categorized under Available for Sale (AFS) or Held Till Maturity (HTM) are reviewed by RMD to provide independent view on the risks associated with them.

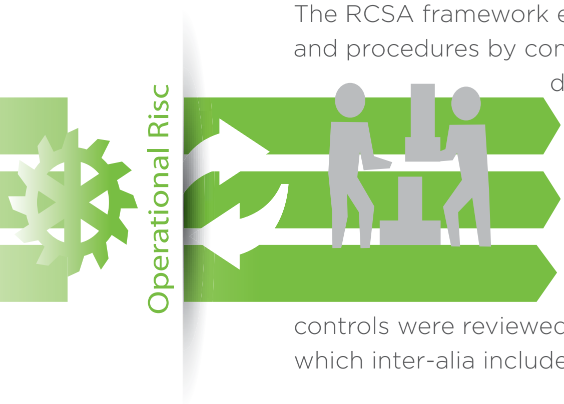
Middle office conducts stress tests periodically to assess the impact of adverse movement of market variables on profitability and capital adequacy and places the same to the RMC.

• Operational Risk

Operational risk is the risk of loss resulting from inadequate or failed internal systems, processes, and people or from external events. The Bank has detailed policies and procedures that are regularly updated to ensure that a sound internal control environment exists in the Bank. Management Risk Committee (MRC), comprising Senior Management of the Bank, precedes RMC in reviewing, evaluating and monitoring of operational risk management. Business Units are responsible for management of operational risks within their respective scope of duties. In the financial year 2013, the Bank's operational risks were well controlled and losses from operational risks were kept at low level. Trained and competent staff oversees the various operational functions of the Bank.

Taking the New Capital Accord Implementation as an opportunity, the Bank has developed a comprehensive operational risk management framework comprising of the Operational Risk Management (ORM) policy, Risk Control and Self-Assessment (RCSA), Key Risk Indicator (KRI), Loss Data Management (LDM) Framework. The ORM policy of the Bank provides the ORM framework which includes ORM components, management process, measurement process and governance, roles and responsibilities. Continuing the task of improvement in existing systems and processes, the management system and tools for operational risks were further strengthened during the year.

The RCSA framework enables the Bank to identify the operational weaknesses in the systems and procedures by conducting self-assessment workshops. A team of experts in various departments assesses the operational weaknesses in the system and its likely impact on the Bank. RMD in association with business units has been able to complete the RCSA exercise for all the departments and branches excluding Maisarah. The RCSA exercise of Maisarah shall be undertaken on stabilisation of the processes. During RCSA exercise, processes in various departments were reviewed from operational risk point of view and wherever high risk events were identified, the extant controls were reviewed. With the completion of RCSA exercise, risk register has been created, which inter-alia includes inherent risk events, control effectiveness and residual risks.



The KRI framework enables us to identify and monitor the key risks. KRIs of all the departments have been identified and are being monitored on a monthly basis. Loss Data Management framework lays down the procedure to identify, record and report the internal and external loss events. The data on operational loss is collated on a regular basis and is presented to MRC and RMC. In order to avoid unexpected shocks to the financial position of the Bank, a reporting system on 'Potential Losses' has also been introduced. Potential Losses can be defined as operational events that has not actually crystallized into actual loss but has a potential of adversely impacting the Bank's bottom-line.

Operational Risk Management Unit (ORMU) in RMD is responsible for implementation, development and coordination of all the operational risk activities of the Bank, while working towards achievement of stated goals and objectives.

The Risk Management Division (RMD) conducts regular training programmes for staff at various levels to inculcate 'risk awareness' and to spread the general 'risk management culture' in the Bank. Professional training in diversified forms is also imparted to improve the employees' risk management skills.

• Business Continuity Management (BCM)

The Bank has adopted Business Continuity/Disaster Recovery Plan with a view to continue business operations and critical customers services at all times both at Conventional and Islamic Banking services. The plan addresses employee health and safety, potential disruptions from the unanticipated loss of services or infrastructure, resumption of business operations in the face of an emergency or disaster. Business Impact Analysis, Business Continuity/Disaster Recovery testing, Awareness Programs etc. are conducted in tune with the regulatory guidelines for meeting any unforeseen circumstances. The key initiatives on the business continuity readiness included the following:

- Business Continuity Planning (BCP) Task Force, a Management level committee has been set up and entrusted with the responsibility of overall supervision for the implementation and maintaining a sound BCP for the Bank. The committee ensures that plans formulated are implemented and tested.
- Bank maintains an alternate/BCP site equipped with redundancy and contingency features to ensure business continuity for resuming critical business activities in emergent scenarios. During the year 2013, Bank has strengthened BCP Site seating capacity and infrastructure considering various worst case scenarios. Additional workspace has been created for critical business units to resume business services in the event of a disaster.
- During the year 2013, along with the IT Disaster Recovery Drill, bankwide BCP testing exercise was also conducted to test check the resilience of technical as well as business recovery. Testing was conducted in coordination with business units to test check transaction systems using business test cases and also to test the preparedness, recovery of applications, recovery timings, assembly of key resources, functioning of equipments, coordination of business units / branches etc. The testing results along with the gaps and action taken are apprised to the risk committees at the Management and Board level.
- For the cause of human safety and security, fire drill exercises are also conducted in Head Office building. Through fire drills, safety and security procedures are reinforced and the preparedness and recovery capabilities of the Coordinators/Floor leaders/Fire wardens are tested.
- As part of creating awareness, specific as well as comprehensive awareness programmes are also conducted to imbibe the importance of BCP amongst staff.
- The contact number of key persons is provided to all the staff so that they can contact the relevant person in case of emergency. The detail of key persons are provided as follows:

Position
BCP Head – Acting Chief Executive Officer
Head, Risk Management
BCP Manager

• Country Risk

Country risk arises from changes in the value of foreign exposure due to country specific conditions, which may result from economic, social, political or natural events and may relate to factors such as exchange controls, currency devaluations, nationalization or expropriation of assets among others.

Country risk policy addresses the country risk that may arise due to cross border exposure in a structured manner. The Bank has in place a country risk assessment methodology which grades each country based on their risk profile. Suitable limits are assigned to undertake the business based on the internal risk rating grade of the countries.

Middle office in association with Treasury department monitors the country risk and takes suitable steps in event of any downgrade or change in the economic activity of any country.

• Implementation of Basel II and Basel III

The Bank is computing the capital adequacy as per Basel II norms as directed by Central Bank of Oman (CBO). As per the CBO directives, the Bank has adopted Standardized Approach for both Credit and Market Risk and Basic Indicator Approach for Operational Risk. With effect from 01.01.2014, Bank will also adopt Basel III capital standards as directed by CBO. The Bank has also adopted the liquidity standards of Basel III ie implementation of Liquidity Coverage Ratio and Net Stable Funding Ratio with effect from March 2013.

The Bank has laid down a road map to move towards adoption of advanced approaches of Basel II and to improve the risk management systems. The road map defines various activities/projects to be undertaken along with the timeline and is monitored by Risk Management Committee of Board of Directors. Most of the models and systems are developed by the risk management team internally through the expertise available in the Bank.

The Bank is confident that with the established Risk Management Processes and their continued enhancement, it will move towards adopting advanced approaches of Basel II for computation of capital requirements, while keeping the quality, consistency and transparency of capital base as per Basel III norms.

• Fraud Risk Management

The Bank considers Fraud as an integral part of the risk and control assessments and it has put in place various internal controls to prevent it.

Following the Central Bank of Oman (CBO) directives, the Anti-Fraud Department was established in the Bank in the year 2011 in order to manage the risk of fraud by developing and execution of proactive anti-fraud strategies and fraud risk management in the Bank. The activities of the Department include but not limited to continuous staff training and customer awareness campaigns on various types of frauds. All new employees attend fraud awareness as part of induction program.

The Bank's Board of Directors, the Senior Management and Staff are all committed to further promote a culture based on good social values, ethics and honesty in the Bank.

The Bank continues to take managing the Risk of Fraud seriously and accordingly all incidents of frauds are fully investigated, disciplinary action taken against perpetrators and / or irresponsible employees in addition to reporting all cases to Royal Oman Police and CBO immediately, once the incidents become known to the Bank.

Anti-Fraud Policy Framework and Whistleblower policies are in place. Further, a comprehensive Staff Code of Conduct is displayed in all offices / branches and copy of the same is provided to all staff members at the time of joining the Bank. Staff are encouraged to be vigilant at all times and to report any suspicious activities through the appropriate channels as outlined in the policies.

Compliance & Corporate Governance Division

Compliance is defined as adherence to laws, rules, regulations, organizational standards and codes of conduct applicable to the banking activities. It is an integral part of the Bank's business activities and concerns everyone at BankDhofar.

Corporate governance is the system by which companies are directed and controlled. The boards of directors are responsible for the governance of their companies. The shareholder's role in governance is to appoint the directors and the auditors to satisfy themselves that an appropriate governance structure is in place. The responsibilities of the board include setting the company's strategic aims, providing the leadership to put them into effect, supervising the management of the business and reporting to shareholders on their stewardship. The board's actions are subject to laws, regulations and the shareholders in general meeting.

Compliance Division co-ordinates with various stakeholders to ensure Compliance with local and international standards on Corporate Governance. BankDhofar has a well-defined Corporate Governance framework with clearly defined roles and responsibilities. A well-established Compliance Policy and Standards Manual clearly specify roles, responsibilities of the Compliance Division and duties of other departments and units towards Compliance. Compliance Division performs its roles independently and the Board oversees management of compliance risk in the Bank.

Compliance function is responsible for identifying, assessing, advising, monitoring and reporting on various compliance risks and specifically deals with matters such as prevention of Money Laundering and Terrorist financing. The function is organized through a risk-based approach and an annual compliance plan which is approved by the Board.

BankDhofar has received first position in the Corporate Governance Excellence Awards 2013 by the Capital Market Authority (Oman Center for Corporate Governance). Compliance function has been strengthened over the years to complement the growth of the Bank's business.

Recovery Dept

In keeping with the department mission statement of recovering maximum NPAs in order to maximize the augmentation of Bank's working funds, the department ensures the proactive monitoring of all NPAs to maximize the recoveries by adopting the following methods;

- Effective monitoring of all legal cases with our external law firms by having regular meetings with them to review the progress made on each cases.
- Coordinating with Royal Oman Police / Regulatory Bodies in order to expedite the process
- Gathering / Maintaining market information to identify assets / investments of our defaulters.
- Rescheduling of NPAs
- Negotiating with Customers for settlement of classified loans on mutually acceptable terms
- Maintaining effective MIS system.

Trade Finance

Trade Finance Department is a full-fledged specialized department of the Bank handling specific trade requirements of the Bank's Corporate, Retail and FI customers. The Department liaisons closely with the Bank's Wholesale Banking, Retail Banking and Treasury & International Departments in providing various fund based credit facilities like Export Bills, Discounting and Import Financing and non-fund based credit facilities like Letters of Credit, Guarantees, Avalization, Export and Import Bill Collection and Risk participation for local and overseas transactions to the Bank's Corporate, Retail and FI customers.

During the Year 2013, the Bank continued to perform strongly in its non-fund business in an extremely competitive market. The Bank could achieve increase in Trade Finance volume by providing best in class customer service and leveraging the correspondent relationships in order to maximize the return on transactions. The department has been successful in retaining and developing its core team members over the last few years which has positively contributed to its ability to meet the challenges in a turbulent international market. The Bank's Trade Finance Team is continuously trained internally and updated with the latest developments in the local and international markets.

Policies & Procedures Department

The Policies & Procedures department (PPD) continued to maintain an integrated model for linking strategies with everyday business processes & decision making at every level. The maintenance of the above stated integrated model brought together, standardized and systematized all risk, control, compliance and governance processes. Further, it helped in improving efficiency of the operational framework.

PPD mainly undertakes the following activities:

- Acts as a nodal department and work closely with Management, Business, Operations, and others to maintain and improvise internal governance & control framework of the Bank.
- Ensures that documents are designed to support business strategy & operations and promote sound working practices.
- Ensures that documents are accurate, clear-cut, presented consistently and uniformly, and are easily identifiable and accessible.
- Ensures that documents are periodically reviewed for accuracy and applicability to address changing business dynamics.

In 2013, apart from the core activities of developing and reviewing policies & procedures, the department has made significant contributions in successful implementation of various projects, such as roll-out of Maisarah (BankDhofar Islamic window) and review of Authorities matrix & Committee charters of the Bank.

Credit Administration Department

The Credit Administration Department is involved in post-credit operations and is the custodian for all security documentation of the Bank pertaining to Large Corporate, Mid Sector, Business Banking/SME, Syndication & Project Finance, Maisarah Islamic Banking and Retail Loans.

The Credit Administration Department is responsible for supporting the Wholesale Banking Group, Maisarah Islamic Banking, Retail Banking, Trade Finance and Treasury related to the daily operational functions.

In April / May 2012, the disbursement of the centralization of Housing Loans was entrusted to the Credit Administration Department with the launch of the 'Daruna' Housing Loan Scheme. Subsequent to the implementation of new Business Process Management (Loan Origination System), the disbursement of Personal Loans and all credit processes of Maisarah products i.e. Ijarah, Murabaha & Diminishing Musharaka are centralized at Credit Administration Department.

A significant development is the creation of a Wholesale Banking Monitoring Unit within the Credit Administration Department, which handles monitoring of contract financing & covenants, expired limits, excess over limits, receipt of financial statements and the like.

A separate team for 'Credit Administration - Retail Banking' has been established at the Department which will be responsible for post-credit operations of all Retail Banking facilities including Car Loans and Educational Loans. The Department is responsible for creation & execution of Mortgages, Commercial Charges, and Pledging of public quoted shares.

In addition, the Department is responsible for coordinating with the Bank Credit Statistics Bureau (BCSB) related functions and part of Central Bank Compliance reporting. Several monitoring and reporting functions of the department were automated during the year, with a view to streamlining operations and maximizing efficiency.

Credit Control Department

The Credit Control Department (CCD) is responsible for the implementation of the Loan Review Mechanism (LRM). LRM is a comprehensive and independent credit review process, distinct from Risk Management and Internal Audit functions. The scope of LRM covers evaluation of various credit processes, loan documentation, loan supervision, risk grading and loan loss provisioning for large and critical Corporate accounts with various units in Wholesale Banking Div.

A review mechanism of this nature facilitates timely corrective measures for any deficiencies observed in specific reviews. It also aids the Bank in taking proactive steps to improve upon any weaknesses or irregularities observed in various credit management processes. During the year 2013, the Credit Control Department has conducted loan reviews with respect to Corporate accounts covering over 90% of the aggregate Corporate credit facilities sanctioned in a year.

As regards Retail Loan reviews, all Personal and Housing loans approved at Head Office level during the year, were independently reviewed by Credit Control Department to ensure adherence to the Bank's lending policies and delegated authorities. In addition, post-disbursement reviews of all Retail loans were also conducted on a daily basis through MIS and any irregularities noticed were taken up for corrective action.

During the year, the Credit Control Department also conducted various portfolio reviews to monitor adherence by business divisions to various internal and regulatory sectoral ceilings on loan and advances as per Credit Risk Policy. The Department has also independently reviewed the quarterly IFRS provisioning exercise. Further, proposals for classification and de-classification of Non-Performing Assets were also reviewed on an ongoing basis.

In line with the Bank's vision, the Credit Control Department will continue to play its independent role in reviewing and strengthening various credit control measures in credit management processes.

Marketing and Corporate Communications (M&CC)

During 2013, the department has initiated the rebranding projects which aimed at reintroducing the look and feel of the Bank's logo, press advertisements, and branch layouts which are designed to ensure customer convenient. There have been different projects, initiatives and campaigns handled by M&CC throughout 2013. These campaigns and initiatives varied from products & services launches, sponsoring social and community based, handling internal events and campaigns targeting employees of BankDhofar.

Key campaigns, events and initiatives

- **Launch of Savings Scheme**
- **Launch of Education Loan**
- **Launch of Youth & Student Banking**
- **Launch of Mobile Banking**
- **Launch of Staff Savings Scheme**

M&CC role has been very essential promoting BankDhofar products, services and different offerings. Though the focus in 2013 was through conventional media channels, in last quarter of the year M&CC has shifted the focus to more engaging and interacting mediums like social media networks. The bank has strengthened its social presence by having a dedicated team managing its accounts in Facebook, Twitter, LinkedIn and Instagram. This enabled the bank to get first hand feedback from its existing and potential customers on its products, services, news and updates.

Corporate Social Responsibility

BankDhofar's Corporate Social Responsibility (CSR) strategy and policy were redrafted after identifying our impact areas as a financial institution in Oman with a three pronged approach in mind, in order to cover the basics of CSR principles gaining most mileage on the programs implemented from a sustainability perspective. We therefore focused on Social, Environmental and Workplace as the initial step toward a more wholesome and integrated approach to addressing the concerns off all stakeholders.

Our impact on the environment as a business and general awareness is one such pillar that BankDhofar is addressing both internally as well as externally through partnerships with the likes of the Environment Society of Oman, as well as assessing our Greenhouse Gas emissions and carbon footprint and plans to implement an Environmental Management System in the near future to manage this. Community and social awareness campaigns as well as a strong focus on engaging our staff is being promoted through various campaigns that have been launched. Below is a list of a few such activities:

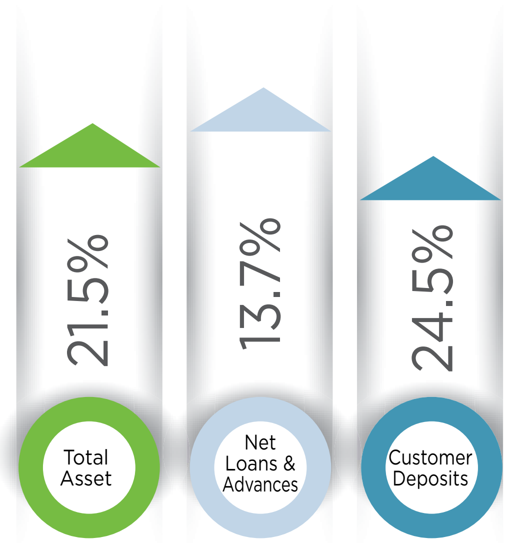
- **Partnership with a local school for the blind in support of e-learning programs**
- **Bank wide collection drive of food items for underprivileged family to mark World Food Day**
- **Supporting SQU's communications department in new media channels research**
- **Partnership in the health sector on prevalent issues and international conferences**
- **Support of the first charity set up for the Elderly**
- **Partnership with the association of early intervention for children with disabilities**
- **Partnership with Tawasul supporting their Annual Civil Society's Leaders Dialogue focus on what's next in CSR**

Keeping in line with the guidelines provided by the Central Market Authority and Central Bank of Oman, BankDhofar is gaining momentum to position itself as such by addressing a number of needs that have spanned across a focus on people and youth with special needs to supporting projects within colleges and universities focusing on youth and Small & Medium Enterprise's in Oman via partnerships with global NGO's such as INJAZ Oman/Junior Achievement. This milestone of separating CSR initiatives from philanthropic activities is paving the way to a new chapter in

CSR in the banking & financial industry in Oman as a reflection of the innovative and progressive changes taking place.

BankDhofar furthermore is gearing itself through thorough research, risk assessment and stakeholder engagement as a baseline to become an institution engaged in best practice and has been laying the framework and keeping abreast of internationally accepted standards of Sustainability such as the Global Reporting Index GRI, ISO 26000 and the United Nations Global Compact UNGC. Our vision is to be holistic in our approach to CSR and build a model based on stakeholder engagement, sustainability, responsible lending and social, environmental and workplace responsibility and awareness.

Financial Performance of the Bank



The Bank continued to grow in all key areas in the year 2013, the net Loans and Advances extended to customers achieved a growth of 13.7% from RO 1.67 billion at the end of 2012 to reach RO 1.90 billion at the end of December 2013. Further, the customer deposits mobilized by the bank achieved a growth of 24.5% from RO 1.63 billion at the end of 2012 to reach RO 2.03 billion at the end of 2013.

An analysis of our loans and advances portfolio as at December 31, 2013 along with the comparative figures for the prior period is as follows:

OMR MILLION

Particulars	2013	2012
Overdrafts	111.9	130.6
Loans	1,724.6	1,499.9
Loans against trust receipts	77.8	88.0
Bills discounted	13.1	3.5
Advance against credit cards	7.9	7.9
Others	18.9	18.1
Islamic Banking Window Financing	**28.3**	-
Gross loans and advances to customers	**1,982.5**	**1,748.0**
Less: Allowance for impairment	(80.6)	(75.5)
Net Loans and Advances	**1,901.9**	**1,672.5**

The ratio of total non-performing advances (NPA) to gross loans improved to 2.95% at the end of 2013 from 3.18% at the end of 2012.

There was a growth of 24.5% in customer deposits from OMR 1.63 billion at the end of 2012 to OMR 2.03 billion at the end of 2013.

The composition of customer deposits at the end of 2013 along with the corresponding figures for the prior period is as follows:

OMR MILLION

Particulars	2013	2012
Current accounts	652.3	322.2
Saving accounts	322.5	269.8
Margin accounts	5.3	4.2
Islamic Banking Window Deposits	3.7	-
Total customer deposits	**2,031.7**	**1,634.6**

Shareholders' Equity

The shareholders' equity at the end of 2013 increased to OMR 303.6 million from OMR 261.5 million at the end of 2012. At the end of 2013 an amount of OMR 5.84 million was transferred to legal reserve being 10% of net profit.

The analysis of shareholders' funds at the end of 2013 along with the corresponding figures for the prior period is as follows:

OMR MILLION

Particulars	2013	2012
Share capital	121.01	110.01
Share premium	40.02	40.02
Special Reserve *	18.49	-
Legal reserve	31.49	25.65
Subordinated loan reserve	26.25	11.25
Proposed distribution - cash	16.94	16.50
Proposed distribution – bonus shares	13.31	11.00
Investment revaluation reserve	1.75	1.56
Retained earnings	34.35	45.51
Total Shareholders' Equity	**303.61**	**261.50**

*Created by the Bank due to the recognition of legal case recovery in the statement of income of OMR 26.1million

As a result of the increase in shareholders' equity the net assets per share reached OMR 0.251 baizes at the end of 2013 compared with OMR 0.238 baizes at the end of 2012.

Income Statement

(OMR "000)

Particulars	2013	2012
Net Interest Income	66,341	64,369
Net Income From Islamic Financing and Investment Activities	173	-
Fees and Commissions	8,905	6,546
Other Income	14,139	13,178
Operating Income	89,558	**84,093**
Total Operating Costs	(45,316)	(37,047)
Operating Profit	44,242	**47,046**
Net Profit	58,407	**37,745**

The key profitability indicators have also achieved positive growths, as net interest income grew from RO 64.37 million in 2012 to reach RO 66.34 million during the year 2013 signifying a growth of 3.1%. Non-interest income such as fees and commissions, foreign exchange profit, investment and other income have shown a significant growth of 16.8% to reach RO 23.04 million in 2013 compared to RO 19.72 million achieved in the previous year.

The Cost to Income ratio during the year 2013 was at a level of 50.6% as compared to 44.1% in 2012. The provisions for loan impairment and imapirment of available-for-sale investments, net of recovery (excluding legal case recovery), during the year 2013 are RO 4.23 million, as against the RO 4.15 million during the previous year 2012.

The net profit for the year 2013 achieved by the Bank is RO 58.41 million as against RO 37.74 million, including the effect of Legal case write back of RO 26.1 million (before taxes), in 2013.

The proposed profit appropriation for 2013 comparing with the previous year 2012 is provided in the following table:

(OMR "000)

Particulars	2013	2012
Proposed dividends – cash	16,942	16,502
Proposed dividends - bonus shares	13,311	11,001
To Special reserve*	18,488	-
To legal reserve	5,840	3,775
To/(From) subordinated loan reserve	15,000	(23,367)
To/(From) retained earnings	(11,174)	29,834

*Created by the Bank due to the recognition of legal case recovery in the statement of income of OMR 26.1million

The percentage of dividends distributed to the Shareholders for the last five years is as follows:

Year	2008	2009	2010	2011	2012
Cash Dividends	15.5%	15%	12.5%	7%	15%
Bonus Shares	4.5%	10%	12.5%	20.2%	10%

Net Profits and Shareholders Equity for the last five years including the current year is as follows:

(OMR "000)

Year	2009	2010	2011	2012	2013
Net Profit for the year	25,393	33,280	13,976*	37,745	58,407**
Total Shareholders' Equity	204,007	226,500	229,237	261,504	303,607

* 2011 includes legal case loss charge off of OMR 26.1 million

** 2013 includes recovery from the case of OMR26.1 million

Future Prospects

The Bank won innumerable awards from several regional and international institutions for excelling in various categories in Banking in the year 2013, including the Best Islamic Window. The Bank has prudently grown, from strength to strength with strong fundamentals, in terms of both sustainable credit growth and deposits mobilization in the year 2013. Maisarah Islamic banking also progressed well in 2013 being the first year of operation, with lots of potential opportunities in the pipeline already for the year 2014. The Bank moving into the third year of its' challenging 5-year plan, will continue to emerge strongly within the local financial market. The Bank has carefully planned the launch of a series of attractive products, services and other initiatives besides streamlining its processes in 2014 to improve the turnaround time for customers and to fully engage and develop its people to maximize efficiencies and reward its Shareholders. The bank is also continuing to invest heavily in advanced technology to provide "Best in Class" banking experience to its customers like for instance the "Cardless ATM withdrawal" which was recently launched with immense response from all quarters.

The Bank is strategically well placed to achieve robust growth in 2014 and in the coming years to support the strong economic development of the Sultanate of Oman and is always grateful for the great Wisdom and Leadership provided by His Majesty Sultan Qaboos Bin Said Al Said.

Financial highlights of last five years

Financial highlights of last five years

(In RO'000) For the year	2013	2012	2011	2010	2009
Net interest income	66,341	64,369	60,318	57,251	49,227
Net income from islamic financing and investment activities	173	-	-	-	-
Non interest income	23,044	19,724	18,273	14,064	15,802
Operating costs	45,316	37,047	33,444	29,195	23,658
Operating profit (before Impairment losses)	44,242	47,046	45,147	42,120	41,371
Profit from operations	66,137	42,900	15,859	37,918	29,021
Net profit for the year	58,407	37,745	13,976	33,280	25,393
At year-end					
Total assets	2,605,379	2,143,830	1,960,591	1,664,296	1,509,265
Net loan portfolio	1,901,910	1,672,508	1,495,661	1,261,736	1,194,243
Customer deposits	2,031,746	1,634,628	1,519,318	1,249,605	1,101,267
Shareholders' equity	303,607	261,504	229,237	226,500	204,007
Share capital	121,013	110,012	91,524	81,355	73,959
Full service branches	65	62	59	56	54
ATMs	140	126	120	93	88
Staff	1,350	1,266	1,202	1,062	937

Financial ratios of last five years

Financial ratios of last five years

	As at 31 December 2013	As at 31 December 2012	As at 31 December 2011	As at 31 December 2010	As at 31 December 2009
I. PROFITABILITY					
Return on weighted average equity	20.67%	15.38%	6.13%	15.46%	12.94%
Return on weighted average capital	50.56%	37.46%	16.17%	40.90%	35.09%
Return on average assets	2.46%	1.84%	0.77%	2.11%	1.81%
Non-interest income to operating income	25.73%	23.45%	23.25%	19.72%	24.30%
Operating expenses to operating income	50.60%	44.05%	42.55%	40.94%	36.38%
II. LIQUIDITY					
Net loans to total deposits	88.95%	97.05%	94.76%	94.49%	99.41%
Total customer deposits to total deposits	95.03%	94.85%	96.26%	93.58%	91.67%
III. ASSET QUALITY RATIOS					
Loan loss provisions to total loans	4.07%	4.32%	4.93%	5.38%	5.06%
Non-performing loans to total loans	2.95%	3.18%	3.79%	4.75%	4.81%
Loan loss provisions to total Non-performing loans	137.91%	135.58%	129.33%	113.23%	105.20%
IV. CAPITAL ADEQUACY					
BIS Risk Asset Ratio	14.09%	14.96%	14.79%	14.02%	14.81%
BIS Risk Asset Ratio on Tier one Capital	11.07%	10.92%	11.16%	12.43%	12.53%
Shareholder's Equity/ Total Assets	11.65%	12.20%	11.69%	13.61%	13.72%

Branch/ ATM/ CDM Network

BRANCH	TEL. NO.	FAX NO.	P.O. BOX	ATM	CDM
Ghala	Dir/ 24216000 - 24216001 - 24216002	24216006	468, P.C 115 MSQ	●	●
Adam	Dir/25215000 - 25215001	25215050	222, PC 618, Adam	●	●
Adam	Dir/25215000 - 25215001	25215050	222, PC 618, Adam	●	●
Al Duqum	Dir/25215801 -25215800	25215888	1507,PC 112 Ruwi	●	
Al Ees Sur	Dir/ 25545867-25544350 - 25541912	25543710	323, PC 411Al Ees Sur	●	●
Al Ghashab(Rustaq)	Dir/ 26875759 - 26878737	26878797	216, PC 329 Burj Redh	●	
Al Khuwair Ministry	Dir/ 24694710-24694725-24694715	24694730	1591, PC 130 Aziba	●	
Al Khuwar 2	Dir/ 24484880 - 24480008 - 24485554	24483366	2717, PC 112 Ruwi	●	
Al Muntrib	25583853- 25584049	25583510	154, PC 421 Mintrib	●	
Amarat	Dir/ 24877838-24876580 - 24876120	24875829	346 PC 119 Amerat	●	
Araqi	25695071 - 25694126	25695047	90, PC 515 Iraqi	●	
B.Al-Mauz	Dir/ 25443365- 25443466 - 25443460	25443462	97, PC 616 B. Al-Mawz	●	
Bahla	Dir/25420003- 25420021 - 25420292 -	25420387	661, PC 612 Bahla	●	
Barka	Dir/ 26884423 - 26884428	26884451	751, PC 320 Barka	●	
Bausher Polyclinic	24502606 - 24596994	24595323	568, PC 115 MSQ	●	
Bid Bid	Dir/ 25369254 - 25369044 - 25369033	25369055	307, PC 613 Bid Bid	●	
Buraimi	25651696 - 25651989	25651115	278, PC 512 Buraimi	●	●
Buraimi Industrial Area	25669821 – 25669822 – 25669823 - 25669824	25669825	867, PC 512	●	●
Dhofar University Booth	Dir/23237789-23237785-23237782	23237745	2334, PC 211 Salalah	●	●
Falaj Al Qabail	26750156-26750928-26751378	26750891	209,PC 322 Falaj Al Qabail	●	
G.Muttrah	Dir/ 24793297- 24707959 - 24706636	24706103	85, PC 114 Jibroo	●	
Hafeet	Dir/ 26817646 - 26817991 - 26817992	26817993	596 PC 319 Saham	●	
Ibra	Dir/ 25571632 - 25571631-25571658	25570646	514, PC 413 Ibra	●	●
Ibra	Dir/ 25571632 - 25571631-25571658	25570646	514, PC 413 Ibra	●	●
Ibri	Dir/ 25692283-25689341 - 25689685	25690341	28, PC 511 Ibri	●	
Izki	Dir/ 25340393 - 25340089-25341016	25340204	412, PC 614 Izki	●	
J. B. B. Ali	Dir/ 25553414 - 25553440	25553446	10 PC416 Jalan	●	●
J. B. B. Hassan	Dir/ 25551020 - 25551025	25551181	222, PC 415 JBBH	●	●
kamil Al Wafi	Dir/ 25557134 - 25557501	25557962	294, PC 412 Al-Kamil	●	
Khaboura	26801028-26801686	26805130	423, PC 326 Khaboura	●	●
Khoudh	Dir/ 24536132 -24545026	24545268	761, PC 132 Khoudh	●	●
Mabellah	Dir/ 24451520-24451540-24451539	24451542	1507, PC 112 Ruwi	●	●
MBD	Dir/ 24750516 - 24790466	24798621	1507, PC 112 Ruwi	●	●
MGM	Dir/ 24216666	24216600	1507 PC 112 Ruwi	●	●
Mirbat	Dir/23268007 - 23268038	23268080	199, PC 220 Salalah	●	●
Mudhaibi	Dir/25578110 - 25578113	25578114	454,PC 420 Mudhaibi	●	●
Muladdah	Dir/ 26868544 - 26868553	26868549	106 PC 341 Muladdah	●	●
Muscat	Dir/ 24 737865 - 24736614 - 24736606 -24 737066	24739166	1613, PC 114 Muttrah	●	●
Muscat Intl. Airport	Dir/ 24510537-24510101- 24 510102	24510468	56, Pc Seeb PC 111	●	
Muttrah	Dir/ 24712970 -24714452 -24 714279	24713556	1441, PC 112 Ruwi	●	●
New Bausher	24614768 - 24614786	24614764	895, PC 115 MSQ	●	●
New Salalah	Dir/23297534-23296158-23297492	23294263	2334, PC 211Salalah	●	●
Nizwa	Dir/ 25411028- 25410234 - 25411370	25411234	83, PC 611 Nizwa	●	●

BRANCH	TEL. NO.	FAX NO.	P.O. BOX	ATM	CDM
Quriyat	Dir/ 24845195-24845193-24845192	24845173	145, PC 120 Quriyat	●	●
Qurum	Dir/ 24568351 - 24567671 - 24567673	24567679	994, PC 116 Mina Al Fahal	●	●
Raysut	Dir/23219219-23219262-23219216	23219197	2334, PC 211 Salalah,	●	●
Rustaq	Dir/ 26876039 - 26875117	26875591	25, PC 318 Rustaq	●	
Ruwi	24831090- 24835854	24831892	1442, PC 112 Ruwi	●	●
Saada	Dir/ 23227177 - 23 225463 - 23225409	23225179	2334, PC 211 Salalah	●	●
Saham	Dir/ 26854400 - 26856699	26855277	92, PC 319 Saham	●	●
Salalah	Dir/ 23290644 - 23292299 - 23294863 - 23291631	23295291	2334, PC 211 Salalah	●	●
Salalah commercial District	Dir/23380700-23380719-23380721	23202761	2334, PC 211Salalah	●	●
Salalah Grand Mall	Dir/ 233818200 - 23381201	23381222	2334, PC 211 Salalah	●	
Salalah-Al Gharbiah	Dir/ 23298046-23297526-23297536	23295084	2334, PC 211 Salalah	●	●
Samad A'Shan	Dir/ 25526736 - 25526529	25526574	123, PC 423 Samad	●	
Seeb Town	Dir/ 24425851 - 24425852 - 24424434 - 24423373	24425627	347, PC 121 Al-Seeb	●	●
Shinas	Dir/ 26748302-26748306-26748308	26748304	434,PC 324 Shinas	●	●
Sinaw	Dir/ 25524663 - 25524367	25524823	296, PC 418 Sinaw	●	●
Sohar Al Ghail	Dir/26943400 – 26943401-26943402	26943444	21, PC 311 Sohar	●	●
Sumail	Dir/ 25351283 -25350543- 25351188	25350094	199, PC 620 Samail	●	
Sur	Dir/ 25546677- 25541255 - 25540256	25540615	75, PC 411 Sur	●	●
Suwaiq	Dir/ 26862001- 26862010	26862102	585, PC 315 Suwaiq	●	●
Taqa	Dir/23258108 - 23258113	23258366	43 , PC 218 Salalah	●	●
Wadi Kabir	24814127 - 24814126	24814128	1507, PC 112 Ruwi	●	●
Wattayah	Dir/24563211 - 24566731	24 566 732	1507, PC 112 Ruwi	●	●
Yanqul	Dir/25672009-25672018-25672031	25672041	440,PC500 Yanqul	●	●

Offsite ATM/ CDM Network

Location name	Region
SHELL SUMAIL LIZGH	DHAKLIYA
ASAFALAH IBRA	SHARQIYA
SULTAN CENTER AAMERAT	MUSCAT
QURUM CITY CENTER	MUSCAT
AL HAIL MAHA	MUSCAT
OMAN OIL HAMBAR	BATINAH
AL KHOUTHER	BATINAH
ARMED FORCES HOSPITAL	MUSCAT
AZAIBA	MUSCAT
OMAN OIL QURUM HEIGHT	MUSCAT
FALAJ AL QABAIL	BATINAH
OMAN OIL AL HAIL	MUSCAT
MAWALEH SHELL	MUSCAT
OMAN EXHIBITION - SEEB	MUSCAT
AL BAHJA CENTER	MUSCAT
SALALAH (AL-QOAF)	DHOFAR
SAROOJ FILLING STATION	MUSCAT
OMAN OIL AL-KHUWAIR	MUSCAT
AL KHUWAIR PIC-N-SAVE	MUSCAT
SALALAH SHELL	DHOFAR
SALALAH HAFFA	DHOFAR
SALALAH NEW	DHOFAR
SALALAH AWAQADIN	DHOFAR
SALALAH - DAHAREEZ	DHOFAR
AL-SALAAM	DHOFAR
SOHAR UNIVERSITY	BATINAH
TYEBAT HYPERMARKET	BATINAH
OMAN OIL MAWALEH	MUSCAT
SALALAH - SQH	DHOFAR
AL-KHOUD	MUSCAT
CITY CENTRE (SEEB)	MUSCAT
QURAIYAT SHELL	MUSCAT
BURAIMI	BURAIMI
SHELL IBRI	DHAHIRA
OMAN OIL SUR	SHARQIYA
ISHTEQRAR HYPERMARKET	DHOFAR
SAADA	DHOFAR
MQ MAHA STATION	MUSCAT
MARS GHUBRA	MUSCAT
OMAN OIL AL KHOUDH	MUSCAT
MUSCAT INTER AIRPORT	MUSCAT
MAHA NEXT WAVE	MUSCAT
EXHIBITION OUTDOOR	MUSCAT

Location name	Region
JBBA	SHARQIYA
MOD GATE 5	MUSCAT
NIZWA UNIVERSITY	DHAKLIYA
SHINAS TECHNICAL COLLEGE	BATINAH
SALALAH TECHNICAL COLLEGE	DHOFAR
AL NASER CLUB SALALAH	DHOFAR
MINTRIB	SHARQIYA
OMAN OIL AL WASIL	SHARQIYA
SHELL JEFNAIN	DHAKLIYA
JAWHARAT SHATTI	MUSCAT
HUJAIRMAT	DHAHIRA
SALALAH AIRPORT	DHOFAR
SULTAN CENTER AZAIBA	MUSCAT
ABU NAIF	DHOFAR
AIJA SUR	SHARQIYA
ENMAR HYPERMARKET	BATINAH
TAYEBAT SAMAD A'SHAN	SHARQIYA
MAWALEH VEG. MARKET	MUSCAT
OMAN OIL SHINAS	BATINAH
FALAJ ALMASHAIKH	SHARQIYA
IBRA TECHNICAL COLLEGE	SHARQIYA
LULU SALALAH	DHOFAR
MUSCAT GRAND MALL	MUSCAT
LULU NIZWA	DHAKLIYA
SUR AL MURTAFAA	SHARQIYA
MIA ARRIVALS	MUSCAT
MAHA WADI MAAWIL	BATINAH
WAHI ALMURR BAHLA	DHAKLIYA
OMAN OIL AUQAD	DHOFAR
SOHAR	BATINAH
CDM	
GRAND MALL	MUSCAT
SUR ALAIJA	SHARQIYA
MOD GATE 5	MUSCAT
MUSCAT INTERNATIONAL AIRPORT	MUSCAT

Disclosure requirements under pillar-III of basel II.

31st December 2013

KPMG
4th Floor, HSBC Bank Building
MBD
P.O. Box 641
P.C. 112
Sultanate of Oman

Tel 968 24709181
Fax 968 24700839

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

We have performed the procedures agreed with you and as prescribed in the Central Bank of Oman ("CBO") Circular No. BM 1027 dated 4 December 2007 ("the Procedures") with respect to the Basel II – Pillar III and Basel III disclosures ("the Disclosures") of Bank Dhofar SAOG (the "Bank") set on pages 70 to 107 as at and for the year ended 31 December 2013. The Disclosures were prepared by the Management in accordance with CBO Circular No. BM 1009 dated 13 September 2006, Circular No. BM 1027 dated 4 December 2007 and Circular No. BM 1114 dated 17 November 2013. Our engagement was undertaken in accordance with the International Standard on Related Services applicable to agreed-upon procedures engagements. The Procedures were performed solely to assist you in evaluating the Bank's compliance with the disclosure requirements set out in CBO Circular No. BM 1009 dated 13 September 2006, as amended and Circular No. BM 1114 dated 17 November 2013.

We report our findings as follows:

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

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

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

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

29 January 2014

KPMG

DISCLOSURE REQUIREMENTS UNDER PILLAR – III OF BASEL II.

1. Introduction:

The following detailed qualitative and quantitative public disclosures are provided in accordance with Central Bank of Oman (CBO) rules and regulations on capital adequacy standards issued through circular BM 1009 on Guidelines on Basel II, Islamic Banking Regulatory Framework and BM 1114 on Regulatory Capital and Composition of Capital Disclosure Requirement under Basel III. The purpose of these requirements is to complement the capital adequacy requirements and the Pillar II – Supervisory review process. These disclosures are intended for market participants to assess key information about the Bank's exposure to various risks and to provide a consistent and understandable disclosure framework for easy comparison among banks operating in the market.

The major highlights of the Central Bank of Oman (CBO) regulations on capital adequacy are:

As per Basel II:

a. To maintain capital adequacy ratio (CAR) at a minimum of 12%;

b. To adopt the standardized approach for credit risk for implementing Basel II, using national discretion for:

   o Adopting the credit rating agencies as external credit assessment institutions (ECAI) for claims on sovereigns and Banks;

   o Adopting simple/comprehensive approach for Credit Risk Mitigants (CRM)

   o Treating all corporate exposures as unrated and assign 100% risk weight.

c. To adopt standardized approach for market risk and basic indicator approach for operational risk.

d. Capital Adequacy returns must be submitted to CBO on a quarterly basis; and

e. The Bank's external auditors must review capital adequacy returns.

As per Basel III

a. The predominant form of capital shall be Tier 1 capital of which Common Equity Tier (CET1) will be the predominant component.

b. To maintain capital adequacy ratio (CAR) at a minimum of 12% plus the capital conservation buffer, which shall be operative from 01.01.2014.

   o Within the overall requirement of 12% CAR, Tier 1 ratio has been prescribed at a minimum of 9%,

   o Within the minimum Tier 1 ratio of 9%, minimum CET 1 ratio has been prescribed at 7%,

   o With a minimum CET 1 ratio of 7%, additional Tier 1 capital can be admitted only up to a maximum of 2% of Risk Weighted Assets (RWA).

   o Further, within the minimum overall capital ratio of 12%, Tier 2 capital can be admitted up to a maximum of 3% of RWA of the Bank.

c. Capital conservation buffer requirements have been prescribed in addition to minimum CET 1, to be built up by individual Banks during normal times and draw down the same during periods of stress. This has been prescribed at 2.5% of total RWA and has to be brought in proportion of 0.625% beginning January 1, 2014 and taking full effect by January 1, 2017. Thus the capital adequacy requirement shall be 14.5% by 2017, assuming a 0% counter cyclical capital buffer.

As per Islamic Banking Regulatory Framework:

Islamic Windows of domestic conventional banks shall maintain a minimum allocated capital of OMR 10 million.

2. Scope of Application:

The Bank has no subsidiaries or significant investments. However, Bank has an Islamic window "Maisarah". Accordingly, the information in the document pertains to the consolidated entity i.e., for both conventional banking & Maisarah. The disclosure pertaining to Maisarah is provided separately at the end of this document.

3. Basel II Disclosures:

3.1. Capital Structure:

The capital base for complying with capital standards is quite distinct from accounting capital. The regulatory capital is broadly classified into three categories – Tier I, Tier II and Tier III. BankDhofar's capital structure consists of Tier I capital and Tier II capital.

Tier I capital includes paid up capital, share premium, legal and general reserves and other disclosed free reserves, including subordinated loan reserves, non-cumulative perpetual preferred stocks and retained earnings (available on a long term basis) less regulatory adjustments like cumulative losses of financial instruments classified as available for sale, goodwill & other intangibles.

Tier II (Supplementary capital) consists of undisclosed reserves, revaluation reserves/cumulative fair value gains on available for sale instruments, general loan loss provision/ general loan loss reserve in capital, hybrid debt capital instruments and subordinated term debt subject to certain conditions. Tier II capital of the Bank also includes 45% of Investment revaluation reserve and general provisions to the extent of 1.25% of total risk weighted assets.

The use of Tier III (short term subordinated debt) is limited only for part of the requirements of the explicit capital charge for market risks. The Bank does not have any Tier III capital and there are no innovative or complex capital instruments in the capital structure.

The details of capital structure are provided as under:

CAPITAL STRUCTURE :	RO'000 Amount
Paid up capital	121,013
Legal reserve	31,492
Share premium	40,018
Special reserve	18,488
Subordinated loan reserve	26,250
Retained earnings	34,339
Proposed bonus shares	13,311
Common Equity Tier (CET) I capital	284,911
Less Goodwill	(2,780)
Cumulative unrealized losses recognized directly in equity	(28)
Common Equity Tier I Capital – Regulatory Adjustments	(2,808)
Total CET I capital	282,103
Additional Tier I Capital	-
Total Tier I Capital	282,103
Investment revaluation reserve (45% only)	802
General provision (Max of 1.25% of total risk weighted assets)	27,250
Subordinated loans	48,750
Total Tier II capital	76,802
Total eligible capital (Tier I + Tier II Capital)	358,905

3.2 Capital Adequacy:

The Bank has adopted Standardized Approach (SA) for computation of capital charge for credit risk and market risk, and Basic Indicator Approach (BIA) for operational risk. Under Standardized approach for credit risk, the Bank has adopted simple approach for recognizing collaterals in the Banking Book and for risk weighting the claims on Sovereigns and Banks, credit ratings of external credit assessment institutions is used. Assessment of capital adequacy is carried out in conjunction with the capital adequacy reporting to the CBO.

The Bank's capital adequacy ratio is 14.09% as against the CBO requirement of 12%. The Bank's policy is to manage and maintain its capital with the objective of maintaining strong capital ratio and high rating. The Bank maintains capital levels that are sufficient to absorb all material risks the Bank is exposed to and provides market return to the shareholders. The Bank also ensures that the capital levels comply with regulatory requirements and satisfy the external rating agencies and other stakeholders including depositors and senior creditors. The whole objective of the capital management process in the Bank is to ensure that the Bank remains adequately capitalized at all times.

The Bank has in place Internal Capital Adequacy Assessment Process (ICAAP) for assessing Bank's capital adequacy in relation to the risk profiles as well as a strategy for maintaining the capital level. The objective of ICAAP document is to explain the Risk policies adopted, Target risk structure and Capital planning, the process of assessing the capital adequacy for credit, market and operational risk, Specific assessment procedures for risks not covered under Pillar I, process of Internal Control Mechanism and stress testing methodologies adopted by the Bank.

Bank has also formed working group on capital planning which regularly meets and assess the capital adequacy to support projected asset growth. The capital adequacy ratio is periodically assessed and reported to the Risk Management Committee (RMC) of the Board of Directors. The composition of capital in terms of Tier I, II and III are also analyzed to ensure capital stability and to reduce volatility in the capital structure.

i) Position of various Risk weighted Assets is presented as under:

Sl. No	Details	Gross Balances (Book Value) RO'000	Net Balances (Book Value)* RO'000	Risk Weighted Assets RO'000
1	On balance sheet items	2,756,062	2,639,409	2,042,547
2	Off balance sheet items	329,325	301,307	276,639
3	Derivatives	18,685	18,685	4,943
4	Total Credit Risk	3,104,072	2,959,401	2,324,129
5	Market Risk			56,798
6	Operational Risk			166,581
7	Total Risk Weighted Assets			2,547,508

* Net of provisions and, reserve interest

ii) Detail of Capital Adequacy:

Sl. No	Details	RO'000
1	Total CET 1/Tier 1 Capital	282,103
2	Tier 2 Capital	76,802
3	Tier 3 Capital	-
4	Total eligible capital	358,905
5	Capital Requirement for Credit Risk	278,895
6	Capital Requirement for Market Risk	6,816
7	Capital Requirement for Operational Risk	19,990
8	Total Required Capital	305,701
9	Tier 1 Capital Ratio	11.07%
10	Total Capital Adequacy Ratio	14.09%

3.3 Risk Exposure and Assessment:

The risks to which banks are exposed to and the techniques that banks use to identify, measure, monitor and control those risks are important factors that market participants consider in their assessment of an institution. In this section, several key banking risks are considered: credit risk, market risk, interest rate risk in the banking book and operational risk. For each separate risk area (e.g. credit, market, operational, banking book interest rate risk) the Bank describes its risk management objectives and policies, including scope and nature of risk reporting and/or measurement systems and risk mitigation strategies.

3.3.1 Credit Risk:

Credit risk is defined as the possibility that a borrower or counterparty will fail to meet its obligations in accordance with agreed terms. Credit risk, therefore, arises from the Bank's dealings with or lending to a corporate, individual, another bank, financial institution or a country. The objective of credit risk management is to minimize the probable losses and maintaining credit risk exposure within acceptable parameters.

The Bank has well established credit risk policy duly approved by the Board which establishes prudent standards, practices in managing credit risk and setting up prudent bench marks, limits for management of credit risks. Continuous review of the credit risk policy is done to adapt to the business environment and regulatory requirements at all times.

The Board of Directors delegate credit approval powers for Wholesale Banking and Retail Banking functional areas, which are clearly defined in Authorities Matrix contained in the Manual on Delegation of Authority. All concerned executives are responsible to ensure that they exercise their delegated powers in terms of the approved Authorities Matrix and seek appropriate special approvals wherever required.

Board Credit Committee is the topmost credit approving authority of the Bank which is mainly responsible for approving all credit proposals beyond the authority level of the management. The senior management executives are also empowered with certain loan approving limits beyond which the credit proposals shall be considered by the Management Credit Committee (MCC) which is empowered to consider all credit related issues up to certain limits.

Credit risk is managed by the Risk Management Division (RMD) through a system of independent risk assessment of all the Corporate, Mid sector and Small and Medium Enterprise credit proposals before they are considered by the appropriate approving authorities. The borrowers in the Standard Category are assigned a risk rating on a scale of 7 grades based on quantitative as well as qualitative parameters. All accounts reflecting weakness in financials or operations as defined by CBO are assigned the grade 8 (Special Mention category) for closer monitoring. RMD approves the risk grade of the borrower and also identifies the risk factors in the credit proposal and suggests suitable mitigation. This facilitates the approving authorities in making informed credit decision. In addition RMD reviews grading of obligors, and conducts regular analysis of the credit portfolio. Every corporate account is reviewed annually and in case of accounts graded as 6, 7 and 8 (Special Mentioned category accounts); reviews are conducted at higher frequency.

The Bank has also established Credit Control department which looks after Loan Review Mechanism (LRM). LRM helps in ensuring credit compliance with the post-sanction processes/ procedures laid down by the Bank from time to time. It involves taking up independent account-specific reviews of individual credit exposures as per the Board approved LRM Policy. Credit Control department also monitors various credit concentration limits. Counterparty/group exposures are limited to 15% of the Bank's capital base as stipulated by CBO and where a higher limit is required for projects of national importance prior approval of CBO is obtained. The credit control department also undertakes monitoring of the retail loans.

Retail lending is strictly in accordance with the CBO guidelines. The Bank introduced a scoring mechanism as a selection tool for the personal loans in conventional banking. Bank has also implemented Loan Origination System (LOS) which has automated the workflow of retail loan credit proposals in conventional banking. In Maisarah, retail financing is mainly in auto and housing finance category.

In addition to these, the Bank also undertakes business with other banks. The maximum exposures to these banks are defined through internally developed model and the total exposure to such counterparty banks is linked to the net worth of the Bank. The Bank has also implemented country risk limits approved by the Board to ensure portfolio diversification in terms of sovereign and geographical exposure. Specific country risk limits have been set up based on the internal risk rating grades assigned to various countries and these limits are reviewed on half yearly basis.

In the absence of acceptable external credit rating agency in the Sultanate of Oman, the Bank has obtained approval of the CBO to treat all corporate exposures as unrated and accordingly assign risk weight of 100% for computing capital requirements under Basel II. The same convention has also been applied to Maisarah financing.

Past dues and impaired exposures are defined in accordance with the relevant CBO regulations. Specific and general provisions are computed periodically in accordance with the CBO regulations as well as other applicable accounting standards. General loan loss provisions equivalent to 1% of the loans categorized as Standard and Special Mention for meeting the latent loan losses are provided for. However, a general loss provision of 2% of the Standard and Special Mention personal loans is created considering the heightened risk inherent in personal loans. Furthermore, all housing finance, other than that occupied by customer, is subject to a 2% general loss provision.

All lending decisions are made after giving due consideration to credit risk policy requirements.

Credit Risk exposure of the Consolidated entity (i.e. both Conventional banking & Maisarah)

i) Analysis of gross credit exposures, plus average gross exposure over the period broken down by major types of credit exposure:

Sl. No.	Type of Credit Exposure	Average Gross exposure RO'000	Average Gross exposure RO'000	Total Gross exposures RO'000	Total Gross exposures RO'000
	Conventional	2013	2012	2013	2012
1	Overdrafts	122,483	130,559	111,959	120,272
2	Loans	1,628,317	1,499,949	1,724,640	1,472,942
3	Loans against trust receipts	80,132	88,009	77,792	76,477
4	Others	18,879	18,058	18,907	14,796
5	Bills purchased /discounted	9,647	3,532	13,099	3,493
6	Advance against credit cards	7,811	7,881	7,864	7,597
		1,867,269	1,747,988	1,954,261	1,695,577
	Islamic				
7	Murabaha Receivables	167	-	237	-
8	Ijarah Assets	8,603	-	17,606	-
9	Musharaka Financing	5,368	-	10,425	-
	Total Islamic	14,138	-	28,268	-
	TOTAL	1,881,407	1,747,988	1,982,529	1,695,577

ii) Geographic distribution of exposures, broken down in significant areas by major types of credit exposure:

Sl. No	Type of Credit Exposure	Oman RO'000	Other GCC Countries RO'000	*OECD Countries RO'000	India RO'000	Pakistan RO'000	Other RO'000	Total RO'000
		1	2	3	4	5	6	7
1	Overdrafts	105,525	-	-	-	-	-	105,525
2	Personal Loans	886,389	-	-	-	-	-	886,389
3	Loans against trust Receipts	77,557	235	-	-	-	-	77,792
4	Other Loans	852,384	-	-	-	-	-	852,384
5	Bills Purchased / negotiated	13,099	-	-	-	-	-	13,099
6	Any other	19,072	-	-	-	-	-	19,072
	Total	1,954,026	235	-	-	-	-	1,954,261
	Islamic							
7	Murabaha Receivables	237	-	-	-	-	-	237
8	Ijarah Assets	17,606	-	-	-	-	-	17,606
9	Musharaka Financing	10,425	-	-	-	-	-	10,425
	Total Islamic	28,268	-	-	-	-	-	28,268
7	Total	1,982,294	235	-	-	-	-	1,982,529

Overdrafts and others included in Personal loans and others

*excluding countries included in column 2

iii) Industry or counterparty type distribution of exposures broken down by major types of credit exposures:

Sl. No.	Economic Sector	Overdraft RO'000	Loans & Financing RO'000	Bills purchased RO'000	Others RO'000	Total RO'000	Off balance sheet exposures RO'000
1	Import Trade	11,385	56,672	63	25,213	93,333	26,540
2	Export Trade	4	10	-	277	291	95
3	Wholesale & Retail trade	6,682	25,879	-	7,681	40,242	13,571
4	Mining & Quarrying	4,892	30,632	726	1,517	37,767	1,281
5	Construction	40,676	160,828	1,337	34,048	236,889	287,929
6	Manufacturing	10,048	138,373	1,499	24,100	174,020	42,739
7	Electricity, gas & water	86	40,556	118	182	40,942	513
8	Transport & Comm.	74	92,189	-	-	92,263	309
9	Fin. Institutions	2,238	107,303	9,342	283	119,166	18,659
10	Services	20,767	82,296	-	2,084	105,147	59,670
11	Personal	6,434	856,093	-	7,699	870,226	310
12	Agriculture & Allied	1,677	5,721	14	86	7,498	814
13	Government	-	126,931	-	-	126,931	5,430
14	Non Resident lending	-	4,911	-	235	5,146	54
15	All others	6,996	24,514	-	1,158	32,668	4,038
16	Total (1 to 15)	111,959	1,752,908	13,099	104,563	1,982,529	461,952

iv) Residual contractual maturity breakdown of the whole portfolio, broken down by major types of credit exposure:

Sl. No.	Time Band	Overdrafts RO'000	Loans & Financing RO'000	Bills purchased/ Discounted RO'000	Others RO'000	Total RO'000	Off-balance sheet exp. RO'000
1	Up to 1 month	5,598	11,688	13,099	3,307	33,692	169,506
2	1-3 months	5,598	137,929	-	1,330	144,857	35,164
3	3-6 months	5,598	41,627	-	4,011	51,236	47,607
4	6-9 months	5,598	13,947	-	8,275	27,820	11,163
5	9 – 12 months	5,598	1,267	-	4,338	11,203	21,712
6	1-3 years	27,990	168,590	-	19,676	216,256	95,115
7	3 – 5 years	27,990	85,125	-	18,784	131,899	68,051
8	Over 5 years	27,989	1,292,735	-	44,842	1,365,566	13,634
9	TOTAL	111,959	1,752,908	13,099	104,563	1,982,529	461,952

v) Analysis of loan & financing book by major industry or counterparty type:

Sl. No.	Economic Sector	Gross loans & Financing RO'000	Of which NPLs / NPAs RO'000	General provision held RO'000	Specific prov. Held RO'000	Reserve Interest / Profit RO'000	Specific Prov. Made during the year RO'000	Adv. Written off during year RO'000
1	Import Trade	93,333	6,795	866	1,468	4,998	34	-
2	Export Trade	291	14	3	3	10	-	-
3	Wholesale & Retail	40,242	17,036	232	5,002	12,119	32	-
4	Mining & Quarrying	37,767	5	378	4	1	290	-
5	Construction	236,889	4,122	2,328	1,776	1,962	35	1
6	Manufacturing	174,020	738	1,733	244	260	75	-
7	Electricity, gas & water	40,942	1	410	1	-	-	-
8	Transport& Communications	92,263	3	923	1	2	-	-
9	Financial Institutions	119,166	-	1,192	-	-	-	-
10	Services	105,147	550	1,046	211	334	54	1,054
11	Personal	870,226	23,744	15,791	10,641	9,506	3,926	66
12	Agriculture & Allied	7,498	9	75	7	1	1	-
13	Government	126,931	-	1,269	-	-	-	-
14	Non-Resident lending	5,146	4,911	3	4,429	486	-	-
15	All Others	32,668	531	634	139	131	108	-
16	TOTAL (1 to 15)	1,982,529	58,459	26,883	23,926	29,810	4,555	1,121

vi) Geographical distribution of amount of impaired loans:

Sl. No.	Countries	Gross loans / financing RO'000	Of which NPLs / NPAs RO'000	General provisions held RO'000	Specific provisions Held RO'000	Reserve Interest / Profit RO'000	Specific Provisions Made during the year RO'000	Advances Written off during year RO'000
1	Oman	1,977,383	53,528	26,880	19,497	29,324	4,555	1,121
2	Other GCC countries	5,146	4,931	3	4,429	486	-	-
3	OECD countries	-	-	-	-	-	-	-
4	India	-	-	-	-	-	-	-
5	Pakistan	-	-	-	-	-	-	-
6	Others	-	-	-	-	-	-	-
7	TOTAL	1,982,529	58,459	26,883	23,926	29,810	4,555	1,121

vii) Movement of Gross Loans/Financing:

Movement of Gross Loans/Financing during the year							
Sl No	Details	Performing Loans		Non-performing Loans			Total
		Standard RO'000	S.M. RO'000	Substandard RO'000	Doubtful RO'000	Loss RO'000	RO'000
1	Opening Balance	1,641,388	50,928	2,011	3,585	50,076	1,747,988
2	Migration/changes (+/-)	12,390	(15,489)	989	(72)	2,182	-
3	New Loans	641,958	79,032	77	186	4,637	725,890
4	Recovery Loans	(446,932)	(39,205)	(363)	(173)	(1,675)	(488,348)
5	Loans written off	-	-	(5)	-	(2,996)	(3,001)
6	Closing Balance	1,848,804	75,266	2,709	3,526	52,224	1,982,529
7	Provisions held*	26,883		638	1,494	21,794	50,809
8	Reserve Interest			158	383	29,269	29,810

*Indicate the general provisions held under performing loans and specific provisions under non-performing loans

3.3.2 Credit Risk: Disclosures for portfolios subject to the Standardized Approach:

i) The Bank has obtained CBO approval vide its letter dated December 11, 2006 to use the ratings of Moody's, Standard & Poor (S&P) or Fitch for risk weighting claims on sovereigns and banks. However, as mentioned earlier, the Bank has obtained CBO approval to treat all corporate exposures as unrated and assign 100% risk weight on all of them. Similar convention has been applied for Maisarah as well.

ii) The Bank is adopting the simplified approach for collateral recognition under the standardized approach, where 0% risk weight is assigned for the exposures covered by cash collateral. The total exposure covered by cash collateral, which attracts 0% risk weight is RO 90.94 million All other credit exposures of Corporate and Retail are assigned 100% risk weight (except mortgage loans, where valuation of the mortgaged house property is not older than 3 years, are assigned 35% risk weight).

iii) The Bank also conducts stress tests using simulation technique on portfolio basis at regular intervals to assess the impact of credit risk on its profitability and capital adequacy for conventional banking. The same is placed before the Risk Management Committee of Board of Directors. The stress test for Maisarah shall be conducted from next year onwards.

3.3.3 Credit Risk Mitigation (CRM): Disclosures for Standardized approaches:

The Bank has adopted the simple approach for credit risk mitigation and no offsetting of the collaterals is done to calculate the capital requirement. However, the main CRM techniques followed by the Bank are based on collaterals which the Bank endeavors to obtain for its exposures, as far as commercially practicable. The collaterals mainly consist of real estate properties, shares listed on the Muscat Securities Market (MSM), government bonds, unlisted shares and Bank fixed deposits. However, the Bank's predominant form of eligible collateral as defined by CBO in its guidelines and for capital adequacy computation purposes is in the form of cash, acceptable Bank guarantees and shares listed on the MSM main index.

The Bank has credit risk rating framework comprising of Risk Rating system which is a single point indicator of diverse risk factors of a Borrower and assists in taking credit decisions in a consistent manner. The risk rating framework is having 8 performing loan grades (including special mention) and 3 non-performing loan grades. The rating grade indicates the default probability of the borrower's obligation. The Bank has also implemented the facility rating system for conventional banking based on Basel II foundation approach which considers the collateral support, seniority and other structural aspects of the facilities provided.

The Bank shall also develop required systems for estimation of Probability of Default (PD), Loss Given Default (LGD) and Exposure at Default (EAD) in order to adopt the advanced approaches under Basel II gradually. A road map to put in place risk management systems to prepare the Bank to adopt advanced approaches of Basel II has been laid down and a suitable risk based information system is also being developed. Bank has already started conducting training programme on risk management practices for the staff and such trainings shall be intensified further to ensure percolation of risk culture across the Bank.

Bank has also implemented model on Risk Adjusted Return on Capital (RAROC) for conventional banking which provides the risk based pricing, which refers to a process of identifying risks, understanding them and subsequently pricing them appropriately. It is an important aspect of prudent credit risk management and is essential for maintaining financial discipline while giving loans. It helps in not only identifying, but also understanding the risk and pricing it appropriately. Implementing such a system shall provide a competitive edge to the Bank in improving the quality of the portfolio and will also cover the cost of doing business in the form of pricing.

The Bank expects to refine the existing risk management systems and practices on an ongoing basis and with that experience, approach the CBO with a framework to move to Internal Rating Based approach (IRB), for its approval at an appropriate time.

3.3.4 Market Risk:

Market Risk is the risk to the Bank's earnings and capital due to changes in the interest rates, profit rates or prices of securities, foreign exchange and equities, as well as the volatilities of those changes. The Bank for International Settlements (BIS) defines market risk as "the risk that the value of 'on' or 'off' balance sheet positions will be adversely affected by movements in equity and interest rate markets, currency exchange rates and commodity prices". Market Risk has been categorized into interest rate risk, profit rate risk, foreign exchange risk, commodity price risk and equity price risk.

Bank has a comprehensive Treasury Risk Policy for both conventional and Islamic banking and Investment Management Policy for conventional banking which encompasses assessment, monitoring and management of all the above market risks. Bank has defined various internal limits to monitor market risk and is computing the capital requirement as per standardized approach of Basel II.

Details of various market risks faced by the Bank are set out below:

i) Interest Rate Risk (IRR) for conventional banking: Interest rate risk is the risk where changes in market interest rates might adversely affect a Bank's financial condition. The immediate impact (up to one year) of changes in interest rates is on the Net Interest Income (NII) and a long term impact (more than one year) of changing interest rates is on the Bank's net worth.

The responsibility of interest rate risk management rests with the Bank's Asset and Liability Management Committee (ALCO). Bank periodically computes the IRR on the Banking book that arises due to re-pricing mismatches in interest rate sensitive assets and liabilities. The impact of IRR on the earnings of the Bank is computed and placed to ALCO on monthly basis. An internal limit has been set up to monitor the impact of Interest rate risk on NII. Similarly, Bank has developed a model to assess the impact of IRR on the Bank's net worth based on duration gap analysis method and an internal limit has also been fixed for the same.

Details relating to re-pricing mismatches and the interest rate risk thereon are placed to the ALCO and also to the Risk Management Committee of the Board on periodic basis. In addition, scenario analysis assuming a 200 basis point parallel shift in interest rates and its impact on the interest income and net profit of the Bank are assessed on a quarterly basis and placed to Risk Management Committee with proposals for corrective action if necessary.

Impact on earnings and economic value of equity due to adverse movement of 100 bps and 200 bps in interest rate in conventional banking is provided as under:

(RO in 000's)

Position as at 31.12.2013 Impact on	+ or – 1%	+ or – 2%
Earnings	9.77	19.54
Economic Value of Equity	21,308.60	42,617.20
Impact on earning as a % of NII	14.99%	29.98%
Impact as a % of Bank's Net worth	5.92%	11.84%

iii) Profit Rate Risk (PRR):

Profit rate risk is the risk that Maisarah will incur a financial loss as a result of mismatch in the Profit rates on assets & Investment Account Holder (IAH). The profit distribution to IAH is based on Profit Sharing Agreements. Therefore, Maisarah is not subject to any significant PRR. However, the profit sharing agreements will result in displaced commercial risk when a Maisarah result does not allow it to distribute profits in line with the market rates.

Maisarah has a Profit Distribution Policy in place which details the process and management of Profit Distribution, including setting up of Profit Equalization & Investment Risk Reserve. The responsibility of profit rate risk management rests with the Bank's Asset and Liability Management Committee (ALCO). Maisarah periodically computes the PRR on the Banking book.

iv) Foreign Exchange Risk:

Foreign Exchange Risk maybe defined as the risk that a Bank may suffer losses as a result of adverse exchange rate movements during a period in which it has an open position, either spot or forward, or a combination of the two, in an individual foreign currency.

The responsibility of management of foreign exchange risk rests with the Treasury department. The Bank has set up internal limit of 40% of Tier I capital to monitor foreign exchange open positions. Most of the foreign exchange transactions are conducted for corporate customers and mostly are on back to back basis. Bank has also defined various limits for foreign currency borrowing and lending.

The Bank also conducts stress tests to assess the impact of foreign exchange risk on its profitability and capital adequacy and the same is placed to Risk Management Committee of Board of Directors on regular basis.

v) Commodity Risk: Commodity Risk occurs due to volatility in the prices of the commodities. Presently the Bank has no exposure to the commodity market.

vi) Equity Position Risk: Equity Position risk occurs due to change in the market value of the Bank's portfolio as a result of diminution in the market value of the equity securities. The responsibility of management of equity position risk rests with the Investment Management Department of the Bank. The Bank does not hold trading position in equities in conventional banking and does not hold any position in equities in Maisarah. The Bank's portfolio is marked to market on regular basis and the difference in the book value and market value are adjusted against revaluation reserve. The Bank also conducts regular stress test on equity position risk and assesses its impact on profitability and capital adequacy.

Bank has introduced the Value at Risk (VaR) method in conventional banking for the domestic quoted equity portfolio. Out of total quoted portfolio of OMR 12.02Mn (i.e. both Equity and Bond portfolio) as on 31.12.2013, VaR has been computed on total quoted equity portfolio of OMR 11.96 Mn, which works out to OMR 249K at 95% confidence level and 2.09% of the domestic quoted equity portfolio.

vii) The Capital Charges: The capital charge for the entire market risk exposure is computed as per the standardized approach using the duration method and in accordance with the guidelines issued by CBO in its circular BM 1009. The Bank adopts duration method in measuring interest rate risk in respect of debt securities held in trading book. The Bank does not hold any trading position in equities and in commodities necessitating capital charge to cover the market risk. Foreign exchange risk capital charge is computed on the three month average of the sum of net short positions or net long positions, whichever is higher of the foreign currency positions held by the Bank.

The capital charge for various components of market risk is presented below:

Type of risk	RO'000 Amount
Interest Rate Risk	-
Equity Position Risk	-
Commodities Position risk	-
Foreign Exchange position risk	4,544
TOTAL	4,544

For assessing the Market risk, the Bank shall, with the approval of CBO, graduate to more advanced measurement techniques from the present Standardized method.

3.3.5 Liquidity Risk

Liquidity risk is the potential inability to meet the liabilities as they become due. It arises when the banks are unable to generate cash to cope with a decline in deposits or increase in assets.

The Bank's Liquidity Risk Management is governed by the Treasury Risk Policy document approved by the Board of Directors as well as the provisions of relevant CBO guidelines on liquidity risk management. The Treasury risk policy also incorporates contingency funding plans and measures, so as to be in a position to meet all maturing liabilities as well as to fund asset growth and business operations. The contingency funding plan includes effective monitoring of the cash flows on a day to day basis, holding of tradable high quality liquid assets, which may be readily disposed off in sizeable amount etc.

The Bank monitors its liquidity risk through cash flow approach and stock approach in conventional banking and through cash flow approach in Maisarah. Under cash flow approach the Bank generates Maturity of Assets and Liabilities (MAL) report which captures all the maturing assets and liabilities into various pre-set time buckets ranging from one month to above five years. The mismatches in various time buckets indicate liquidity gap and the Bank strictly adheres to the CBO set limit of 15% of cumulative liabilities (outflows) on mismatches (liquidity gaps) in time buckets up to one year. In addition, the Bank has also set up internal limit on mismatches in time buckets beyond one year. Under stock approach, the Bank monitors the liquidity risk through liquidity ratios, which portrays the liquidity stored in the balance sheet.

Treasury department of the Bank controls and monitors the liquidity risk and ensures that the Bank is not exposed to undue liquidity risk and at the same time makes optimum use of its funds. Middle office in Risk Management Division also monitors the liquidity position of the Bank and provides the liquidity gap positions to Treasury Department to manage it.

Middle office also undertakes regular stress test for conventional banking using simulation technique that provides the requirement of liquidity over a given horizon at a certain confidence level.

The Bank has reconciled the statement of Maturity of Assets and Liabilities with the discussions under IFRS (Refer item no. 35 of the Notes to financial statements).

3.3.6 Operational Risk:

Basel Committee on Banking Supervision has defined operational risk as "the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events." This definition includes legal risk, but excludes strategic and reputational risk. Legal risk includes, but is not limited to, exposure to fines, penalties, punitive damages resulting from supervisory actions, as well as private settlements.

Bank has a well-defined Operational Risk Management (ORM) policy which inter-alia includes Operational Risk Events, Operational Risk losses and ORM process. Business and Functional units are primarily responsible for taking and managing Operational Risk on a day-to-day basis. Risk Management Division provides guidance and assistance in the identification of risk and in the ongoing operational risk management process. Bank has set up Operational Risk Management Committee to identify, manage, measure, monitor, mitigate and report operational risks.

Basel II has provided three different approaches viz., Basic Indicator approach (BIA), The standardized approach (TSA) and Advanced measurement approach to compute the capital charge of Operational Risk. The Bank has adopted the BIA for computing the capital charge for Operational Risk as per CBO guidelines. The approach requires the Bank to provide 15% of the average gross income for the last three years as capital charge for operational risk.

While the Bank has adopted BIA approach for capital adequacy calculation purposes, initiatives has also been taken to move towards adopting The Standardized Approach by mapping the business activities into eight business lines and assessing the operational risk in each of them.

The system of collecting and collating data on operational risk events has been improved further to build a strong loss data base and to move over to the advanced measurement system for operational risk as required by the CBO guidelines. The loss data are being captured using Operational Risk Management System and complete history of the loss data is maintained.

Bank also undertakes Risk Control and Self-Assessment exercise by which the inherent risk in various processes of each business unit is identified and control against these risks are assessed for their design and effectiveness. The residual risk (i.e. inherent risk after controls) provides the potential loss amount and based on residual risk, the controls are improved further.

Bank is also identifying and monitoring the Key Risk Indicators (KRIs) for each business unit. Each KRI has defined threshold limit and an escalation criteria is also attached to it. A breach in threshold of the KRI escalates the risk to the higher authority. All the Operational Risk Management tools are configured in Operational Risk Management System.

4. Basel III Disclosures:

Capital Adequacy Norms

The Bank has calculated its Common Equity Tier 1 (CET1), Tier 1 and Total Capital Ratios in the following manner:

i. CET1 Capital Ratio = Common Equity Tier 1 Capital/ Total RWA

ii. Tier 1 Capital Ratio= Tier 1 Capital/ Total RWA

iii. Total Capital Ratio = Total Capital/ Total RWA

Tier 1 Capital is the sum of CET1 Capital and Additional Tier 1 Capital (AT1) and Total Capital is the sum of Tier 1 Capital and Tier 2 Capital.

The denominator, viz., Total risk-weighted assets (RWA) is calculated as the sum of credit risk weighted assets, market risk-weighted assets, and operational risk-weighted assets, as provided for in BM-1009 and Islamic Banking Regulatory Framework. In the case of Islamic banks, CBO has provided an adjustment of alpha of 30% in the RWA in the manner stipulated under Article 2.3.1 of title 5 of IBRF relating to Capital adequacy. However, as per communication received from CBO, for the time being no adjustment is applicable in the computation of RWA.

Based on the presently prescribed level of capital adequacy, banks operating in the Sultanate will be required to maintain at all times, the following minimum capital adequacy ratios:

CET 1 Capital Ratio: 7% of risk weighted assets

Tier 1 Capital Ratio: 9% of risk weighted assets (Going concern capital)

Total Capital Ratio: 12% of risk weighted assets (Gone concern capital)

Within the minimum Tier I ratio of 9%, Additional CET1 items will be admitted up to a maximum of 2% of Risk Weighted Assets of the Bank. Further, within the minimum overall capital of 12%, Tier 2 capital will be admitted up to a maximum of 3% of Risk Weighted Assets of the Bank.

With effect from 01-01-2014, Capital Conservation Buffer (CCB) shall be implemented in a phased manner. The CCB shall be 2.5% of the total RWA and every year the buffer will be enhanced by 0.625%, thereby reaching a level of 2.5% in 2017. Further, CBO may also implement Countercyclical Capital Buffer, which is intended to protect the banking sector as a whole from systemic risk that is often developed during an economic upswing, when there is a tendency towards excessive aggregate credit growth. The Countercyclical Capital Buffer lies between 0% and 2.5% of the total RWA; however presently the countercyclical capital buffer is not operationalized. Thus by the end of 2017, assuming a zero countercyclical capital buffer, banks shall operate above CET1, Tier 1 and Total Capital levels of 9.5%, 11.5% and 14.5% respectively.

Thus based on the Basel III requirement, the capital structure of the Bank (as a consolidated entity) is presented as per Annexure I. A reference is invited to paragraph 91 of the Basel III rules, which states that banks should disclose "a full reconciliation of all regulatory capital elements back to the balance sheet in the audited financial statements". The reconciliation process laid down is aimed at addressing the issues of disconnect between the numbers disclosed for the calculation of regulatory capital and the numbers used in the published financial statements. However, there is no difference between the regulatory consolidation and the accounting consolidation. The components used in the definition of capital disclosure template are provided as per Annexure IIa and the same are mapped to the composition of capital disclosure template as per Annexure IIb.

Basel II, Pillar 3 guidance states that banks should provide qualitative disclosure that sets out "Summary information on the terms and conditions of the main features of all capital instruments, especially in the case of innovative, complex or hybrid capital instruments." Banks are required to disclose a description of the main features of regulatory capital instruments along with the full terms and conditions of the regulatory capital instruments issued by them. Bank has two types of capital instruments viz., Common Shares and Subordinated Debt. The summary disclosure for these regulatory capital instrument issued by the Bank is provided at Annexure III.

Liquidity Standards:

Bank has adopted Basel III liquidity standards and is reporting the liquidity coverage ratio and net stable funding ratio to CBO with effect from March 2013.

Liquidity Coverage Ratio (LCR): This ratio aims to ensure that a bank maintains an adequate level of unencumbered, high-quality liquid assets that can be converted into cash to meet its liquidity needs for a 30 calendar day time horizon under a significantly severe liquidity stress scenario. The ratio is calculated as follows –

LCR = Stock of High Quality Liquid Assets / Cash Outflow for next 30 days

As per guidelines, the value of the ratio should be minimum 100% (i.e. the stock of high-quality liquid assets should at least equal total net cash outflows) on monthly basis and Bank is maintaining the same.

Net Stable Funding Ratio (NSFR): The net stable funding ratio is designed to ensure that banks rely more on long term funding and they maintain a sound funding structure over a horizon of one year to withstand Bank specific stress events. The ratio aims to reduce over-reliance on short term funding to create long term assets, especially during times of volatile liquidity conditions. The ratio is calculated as follows

Net Stable Funding Ratio = Available Stable Funding (ASF) / Required Stable

Funding (RSF) *100

As per guidelines, this ratio needs to be greater than 100% and Bank maintained the same.

5. Disclosures of Maisarah:

Introduction:

Maisarah Islamic Banking Services (Maisarah) is an Islamic Window of BankDhofar S.A.O.G (the Bank), established after obtaining license from the Central Bank of Oman (CBO). The principal activities of the Maisarah include taking saving, investment accounts, providing Shari'a Compliant forms of financing as well as managing investor's money on the basis of Mudarabah or Wakala, providing commercial banking services and other investment activities.

The Public disclosures under this section have been prepared in accordance with the CBO requirements outlined in the Islamic Banking Regulatory Framework (IBRF), Title 5: Capital Adequacy, Pillar III – Market Discipline.

5.1 Capital Structure:

The capital base for complying with capital standards is quite distinct from accounting capital. The regulatory capital is broadly classified into two categories – Tier I and Tier II. Maisarah's capital structure mainly consists of Tier I capital. Tier I capital includes paid up capital, share premium, legal and general reserves and other disclosed free reserves, including subordinated loan reserves, non-cumulative perpetual preferred stocks and retained earnings (available on a long term basis).

Tier II (Supplementary capital) consists of undisclosed reserves, revaluation reserves/cumulative fair value gains on available for sale instruments, general loan loss provision/ general loan loss reserve in capital and subordinated term debt subject to certain conditions.

Capital Adequacy determination for Islamic Finance Entities (IFE) differs from Conventional financial institutions (CFI) in that:

a) Its financing arrangements are either asset-based or profit and loss sharing (Musharakah) or Profit and loss bearing (Mudarabah)

b) Much of the funding is raised through unrestricted investment accounts that are, in principle, a form of equity.

Investment Account Holders (IAH) that impose no restrictions on investment of funds by the Bank are deemed Unrestricted Investment Account Holders (UIAH). Restricted Investment Account Holders (RIAH) imposes certain restrictions with regards to how and for what purpose the funds should be invested. Maisarah accepted deposits as Unrestricted Investments.

As such, the underlying assets involved under the Shari'a Compliant financing contracts may be exposed to Market (price) Risk, as well as to Credit Risk in respect of the amount due from the counterparty. Risk weighted assets (RWA) financed by Profit Sharing Investment Accounts (PSIA), in principle, are excluded in the calculation of the denominator of the capital ratio, insofar as the commercial risk of these assets do not affect the capital of the shareholders. In practice, however, a proportion of these, or even the full amount, may be subject to a capital requirement, depending upon the extent of risk-sharing between shareholders and UIAH. However, as per communication received from CBO, RWA shall be computed in the same way as in conventional banking.

The details of capital structure are provided as under:

COMMON EQUITY TIER I CAPITAL	RO'000 Amount
Paid up capital	12,500
Legal reserve	-
Retained earnings/ (Accumulated losses)	(2,202)
Cumulative unrealized losses recognized directly in equity	-
COMMON EQUITY TIER I CAPITAL	10,298
ADDITIONAL TIER I CAPITAL	-
TOTAL TIER I CAPITAL	10,298
TIER II CAPITAL	
Investment revaluation Reserve (45% only)	-
General Provision (Max of 1.25% of total risk weighted assets)	285
PER & IRR	0
TOTAL TIER II CAPITAL	285
TOTAL ELIGIBLE CAPITAL (TIER I + TIER II)	10,583

Unrestricted IAH Funds	RO'000 Amount
PER (Shareholders Component)	0.018
PER (IAH Component)	0.027
IRR	0.014

5.2 Capital Adequacy

The Bank has adopted Standardized Approach (SA) for computation of capital charge for credit risk and market risk, and Basic Indicator Approach (BIA) for operational risk. Under Standardized approach for credit risk, the Bank has adopted simple approach for recognizing collaterals in the Banking Book and for risk weighting the claims on Sovereigns and Banks, credit ratings from external credit assessment institutions is used. Assessment of capital adequacy is carried out in conjunction with the capital adequacy reporting to the CBO.

Maisarah capital adequacy ratio is 33.72% as against the CBO requirement of 12%. The Bank's policy is to manage and maintain its window capital with the objective of maintaining strong capital ratio and high rating. Maisarah maintains capital levels that are sufficient to absorb all material risks to which it is exposed to and provides market return to the shareholders. Maisarah also ensures that the capital levels comply with regulatory requirements. The whole objective of the capital management process in Maisarah is to ensure that Maisarah remains adequately capitalized at all times.

i) Position of various Risk weighted Assets (RWA) is presented as under:

Sl. No	Details	Gross Balances (Book Value) RO'000	Net Balances (Book Value)* RO'000	Risk Weighted Assets RO'000
1	On balance sheet items	50,304	50,304	29,481
2	Off balance sheet items	2,990	2,990	598
3	Derivatives	-	-	-
4	Total Credit Risk (RWA)	53,294	53,294	30,079
5	Market Risk (RWA)	-	-	-
6	Operational Risk (RWA)			1,305
7	Total Risk Weighted Assets			31,384

* Net of specific provisions and reserve interest

ii) Detail of Capital Adequacy:

Sl. No	Details	RO'000
1	Tier 1 Capital	10,298
2	Tier 2 Capital	285
3	Total Regulatory Capital	10,583
4	Capital Requirement for Credit Risk	3,766
5	Capital Requirement for Market Risk	-
6	Capital Requirement for Operational Risk	157
7	Total Required Capital	3,923
8	Tier 1 Capital Ratio	32.81%
9	Total Capital Adequacy Ratio	33.72%

iii) Capital Requirement by Types of Islamic Financing Contracts:

Sl. No	Details	Gross Balances (Book Value) RO'000	Net Balances (Book Value)* RO'000	Risk Weighted Assets RO'000
1	Murabaha Receivables	237	232	237
2	Ijarah Assets	17,606	17,425	6,162
3	Diminishing Musharaka Financing	10,425	10,325	10,234

* Net of provisions and reserve profit

5.3 Risk Exposure and Assessment:

The risks to which banks are exposed to and the techniques that banks use to identify, measure, monitor and control those risks are important factors that market participants consider in their assessment of an institution. In this section, several key banking risks are considered: credit risk, market risk and operational risk. For each separate risk area (e.g. credit, market, operational) Maisarah describes its risk management objectives and policies, including scope and nature of risk reporting and/or measurement systems and risk mitigation strategies.

5.3.1 Credit Risk:-

Credit risk is defined as the possibility that a customer or counterparty will fail to meet its obligations in accordance with agreed terms. Credit risk, therefore, arises from Maisarah's dealings with or financing to a corporate, individual, another bank or financial institution. The objective of credit risk management is to minimize the probable losses and maintaining credit risk exposure within acceptable parameters.

Maisarah has well established credit risk policy duly approved by the Board which establishes prudent standards, practices in managing credit risk and setting up prudent bench marks, limits for management of credit risks. The Board of Directors delegate credit approval powers for functional areas, which are clearly defined in Authorities Matrix contained in the Manual on Delegation of Authority. All concerned executives are responsible to ensure that they exercise their delegated powers in terms of the approved Authorities Matrix and seek appropriate special approvals wherever required.

Board Credit Committee is the topmost credit approving authority of the Bank which is mainly responsible for approving all credit proposals beyond the authority level of the management. The senior management executives are also empowered with certain finance approving limits beyond which the credit proposals shall be considered by the Management Credit Committee (MCC) which is empowered to consider all credit related issues up to certain limits.

Credit risk is managed by the Risk Management Division (RMD) through a system of independent risk assessment of all the credit proposals before they are considered by the appropriate approving authorities. The customer in the Standard Category are assigned a risk rating on a scale of 7 grades based on quantitative as well as qualitative parameters. All accounts reflecting weakness in financials or operations as defined by CBO are assigned the grade 8 (Special Mention category) for closer monitoring. RMD approves the risk grade of the customer and also identifies the risk factors in the credit proposal and suggests suitable mitigation. This facilitates the approving authorities in making informed credit decision. In addition RMD reviews grading of obligors, and conducts regular analysis of the credit portfolio. Every corporate account is reviewed annually and in case of accounts graded as 6, 7 and 8 (Special Mentioned category accounts), reviews have been prescribed at higher frequency. However, the customers who do not publish audited financials are treated as unrated.

Retail financing is strictly in accordance with the CBO guidelines.

In addition to these, Maisarah also undertakes business with other banks. The maximum exposures to these banks are defined using a judgmental approach and restrictions are put in place on the total exposure to such counterparty banks. Maisarah has also implemented country risk limits approved by the Board to ensure portfolio diversification in terms of sovereign and geographical exposure. Specific country risk limits have been set up based on the external risk rating grades assigned to various countries and these limits are reviewed on half yearly basis.

In the absence of acceptable external credit rating agency in the Sultanate of Oman, the Bank has obtained approval of the CBO to treat all corporate exposures as unrated and accordingly assign risk weight of 100% for computing capital requirements under Basel II. The same convention is used for Maisarah as well.

Past dues and impaired exposures are defined in accordance with the relevant CBO regulations. Specific and general provisions are computed periodically in accordance with the CBO regulations as well as other applicable accounting standards. General loan loss provisions equivalent to 1% of the financing categorized as Standard and Special Mention for meeting the latent financing losses are provided for. However, a general loss provision of 2% of the Standard and Special Mention personal financing is created considering the heightened risk inherent in retail finance.

All financing decisions are made after giving due consideration to credit risk policy requirements.

i) Analysis of gross credit exposures, plus average gross exposure over the period broken down by major types of credit exposure:

Sl. No.	Type of Credit Exposure	Average Gross exposure 2013 RO'000	Total Gross exposures 2013 RO'000	Percentage of total financing
1	Murabaha Receivables	167	237	0.84%
2	Ijarah Assets	8,603	17,606	62.28%
3	Diminishing Musharakah Financing	5,368	10,425	36.88%
4	TOTAL	14,138	28,268	

ii) Geographic distribution of exposures, broken down in significant areas by major types of credit exposure:

Sl. No	Type of Credit Exposure	Oman RO'000 1	Other GCC Countries RO'000 2	*OECD Countries RO'000 3	Other RO'000 4	Total RO'000 5
1	Murabaha Receivables	237	-	-	-	237
2	Ijarah Assets	17,606	-	-	-	17,606
3	Diminishing Musharakah Financing	10,425	-	-	-	10,425
4	Any other	-	-	-	-	-
5	Total	28,268	-	-	-	28,268

*excluding countries included in column 2

iii) Industry or counterparty type distribution of exposures broken down by major types of credit exposures:

Economic Sector	Murabaha receivables RO'000	Diminishing Musharaka Financing RO'000	Ijarah Muntahia Bittamleek RO'000	Off balance sheet exposures RO'000
31 December 2013				
Import trade	-	-	-	2,990
Mining and quarrying	-	1,494	-	-
Construction	-	6,958	-	-
Manufacturing	-	1,670	-	-
Services	-	303	-	-
Retail	237	-	17,606	-
Total	237	10,425	17,606	2,990

iv) Residual contractual maturity breakdown of the whole portfolio, broken down by major types of credit exposure:

	Murabaha receivables RO'000	Diminishing Musharaka Financing RO'000	Ijarah Muntahia Bittamleek RO'000	Off Balance sheet exposures RO'000
31 December 2013				
Up to 1 month	5	196	126	-
1 - 3 months	10	392	251	-
3 - 6 months	14	588	377	2,990
6 - 9 months	14	531	377	-
9 - 12 months	14	512	377	-
1 - 3 years	109	5,470	3,014	-
3 – 5 years	71	1,953	2,966	-
Over 5 years	-	783	10,118	-
Total	237	10,425	17,606	2,990

v) Analysis of asset book by major industry or counterparty type:

	Performing Murabaha receivables RO'000	Performing Diminishing Musharaka Financing RO'000	Performing Ijarah Muntahia Bittamleek RO'000	General provisions made during the year RO'000
31 December 2013	-	-	-	-
Mining and quarrying	-	1,494	-	(14)
Construction	-	6,958	-	(67)
Manufacturing	-	1,670	-	(16)
Services	-	303	-	(3)
Retail	237	-	17,606	(185)
Total	237	10,425	17,606	(285)

vi) Financing by type of counterparty:

Segment	RO'000	%
Retail	17,843	63.12%
Corporate	10,425	36.88%

5.3.2 Credit Risk: Disclosures for portfolios subject to the Standardized Approach:

i) The Bank has obtained CBO approval vide its letter dated December 11, 2006 to use the ratings of Moody's, Standard & Poor (S&P) or Fitch for risk weighting claims on sovereigns and banks. However, as mentioned earlier, the Bank has obtained CBO approval to treat all corporate exposures as unrated and assign 100% risk weight on all of them. The same convention has been adopted for Maisarah as well.

ii) The Bank is adopting the simplified approach for collateral recognition under the standardized approach, where 0% risk weight is assigned for the exposures covered by cash collateral. The total exposure covered by cash collateral, which attracts 0% risk weight is NIL. All other credit exposures of Corporate and Retail (except house finance, where valuation of the property is not older than 3 years, are assigned 35% risk weight) are assigned 100% risk weight.

5.3.3 Credit Risk Mitigation: Disclosures for Standardized approaches:

The Bank has adopted the simple approach for credit risk mitigation and no offsetting of the collaterals is done to calculate the capital requirement. However, the main CRM techniques followed by the Bank are based on collaterals which the Bank endeavors to obtain for its exposures, as far as commercially practicable. The collaterals mainly consist of real estate properties.

The Bank has credit risk rating framework comprising of Risk Rating system which is a single point indicator of diverse risk factors of a Customer and assists in taking credit decisions in a consistent manner. The risk rating framework is having 8 performing assets grades (including special mention) and 3 nonperforming assets grades. The rating grade indicates the default probability of the customer's obligation. The same rating framework has been adopted by Maisarah as well.

5.3.4 Market Risk:

Market Risk is the risk to the Bank's earnings and capital due to changes in the profit rates or prices of securities, foreign exchange and equities, as well as the volatilities of those changes. The Bank for International Settlements (BIS) defines market risk as "the risk that the value of 'on' or 'off' balance sheet positions will be adversely affected by movements in equity and interest rate markets, currency exchange rates and commodity prices". Market Risk has been categorized into profit rate risk, foreign exchange risk, commodity price risk and equity price risk.

Maisarah has a comprehensive Treasury Risk Policy which encompasses assessment, monitoring and management of all the above market risks. Bank has defined various internal limits to monitor market risk and is computing the capital requirement as per standardized approach of Basel II.

Details of various market risks faced by the Bank are set out below:

i) Profit Rate Risk (PRR): Profit rate risk is the risk that Maisarah will incur a financial loss as a result of mismatch in the Profit rates on assets & IAH. The profit distribution to IAH is based on Profit Sharing Agreements. Therefore, Maisarah is not subject to any significant PRR. However, the profit sharing agreements will result in displaced commercial risk when Maisarah results do not allow it to distribute profits in line with the market rates.

   Maisarah has a detailed Profit Distribution Policy in place which details the process and management of Profit Distribution, including setting up of Profit Equalization & Investment Risk Reserve. The responsibility of profit rate risk management rests with the Bank's Asset and Liability Management Committee (ALCO). Maisarah periodically computes the PRR on the Banking book.

ii) Foreign Exchange Risk:

   The responsibility of management of foreign exchange risk rests with the Treasury department. Presently, Maisarah does not have a major foreign exchange exposure. There is only one placement in US dollar which has been financed through borrowing of the same tenor.

iii) Commodity Risk: Presently Maisarah has no exposure to the commodity market.

iv) Equity Position Risk: Presently Maisarah has no exposure to the Equity market.

v) The Capital Charges: The capital charge for the entire market risk exposure is computed as per the standardized approach using the duration method and in accordance with the guidelines issued by CBO in IBRF. Maisarah does not hold any trading position in equities and in commodities necessitating capital charge to cover the market risk. There is no net open position in the foreign exchange exposure, thus the capital charge for various components of market risk in Maisarah is NIL.

5.3.5 Liquidity Risk

Maisarah's Liquidity Risk Management is governed by the Treasury Risk Policy document approved by the Board of Directors as well as the provisions of relevant CBO guidelines on liquidity risk management.

Maisarah monitors its liquidity risk through cash flow approach. Under cash flow approach Maisarah generates Maturity of Assets and Liabilities (MAL) report which captures all the maturing assets and liabilities into various pre-set time buckets ranging from one month to above five years. The mismatches in various time buckets indicate liquidity gap and Maisarah strictly adheres to the CBO set limit of 15% of cumulative liabilities (outflows) on mismatches (liquidity gaps) in time buckets up to one year. In addition, Maisarah has also set up internal limit on mismatches in time buckets beyond one year.

Treasury department of Maisarah controls and monitors the liquidity risk and ensures that the Bank is not exposed to undue liquidity risk and at the same time makes optimum use of its funds. Middle office in Risk Management Division also monitors the liquidity position of Maisarah.

5.3.6 Operational Risk:

Maisarah has a well-defined Operational Risk Management (ORM) policy which inter-alia includes Operational Risk Events, Operational Risk losses and ORM process. Business and Functional units are primarily responsible for taking and managing Operational Risk on a day-to-day basis. Risk Management Division provides guidance and assistance in the identification of risk and in the ongoing operational risk management process. Bank has set up Operational Risk Management Committee to identify, manage, measure, monitor, mitigate and report operational risks.

Basel II has provided three different approaches viz., Basic Indicator approach (BIA), The standardized approach (TSA) and Advanced measurement approach to compute the capital charge of Operational Risk. The Bank has adopted the BIA for computing the capital charge for Operational Risk as per CBO guidelines. The approach requires Maisarah to provide 15% of the average gross income for the last three years as capital charge for operational risk. Since, it is first year of Maisarah's operation accordingly one year gross income is taken into consideration for calculating charge which amounts to OMR 157K.

5.4 Investment Account Holders (IAH)

Maisarah manages and deploys the equity of IAH according to rules and regulations laid down in IBRF. Maisarah holds and maintains two separate pools of funds, one for its own funds and another for Equity of its IAH. Both of these pools are managed in accordance with Shari'a requirements and standard of prudence is applied in the context of managing the overall portfolio to enable Maisarah to exercise its fiduciary responsibilities. Maisarah is authorized by the IAH to invest the funds in the manner Maisarah deems fit without laying down any restrictions as to where, how and for what purpose the funds should be invested.

The composition, characteristics, diversification and concentration of portfolios are monitored within appropriate risk limits and indicators detailed in Maisarah's credit risk liquidity risk and other risks policies. The strategic objectives of the investments of the fund are:

1) Investments in Shari'a compliant opportunities

2) Targeted returns

3) Compliance with Credit Policy & overall investment plan

4) Diversified Portfolio

Funds are invested in Shari'a Compliant commercial or Retail financing as short, medium or long term investments excluding strategic investments. Under all the aforesaid arrangement, Maisarah can commingle the IAH funds with its own (Self-Financed). Some of the assets right from inception is designated exclusively as self-financed. These self-financed assets are deducted from total assets to arrive at "Jointly Financed Assets (JFA)". To separate the JFA into Self-Financed and IAH, Maisarah applies formula to identify the proportional share of each fund's in the JFA.

Maisarah's share of profit as a Mudarib for managing equity of IAH and their share of income is based on the terms and conditions of the related Mudarib agreements. These funds are invested in Islamic modes of financing and investments including Murabaha, Mudarabah, Musharakah and Ijarah. There are no separate designations for Portfolio Managers, Investment Advisors and trustee. IAH accounts are managed at Head Office level by relevant departments.

Investors' share of income is calculated based on the income generated from joint investment accounts after deducting the expenses related to investment pool "Mudarib Expenses". Mudarib expenses include all expenses incurred by Maisarah, including specific provisions, but excluding staff cost and depreciation. Maisarah's Mudarib Profit is deducted from Investors' share of income before distributing such income.

The basis applied by Maisarah in arriving at the IAH share of income is [Total Investments income less Investment Pools Expenses] divided by [average funds generating income (shareholders & equity of IAH) times average funds of IAH]. Total administrative expenses for profit distribution purposes are borne by Maisarah.

Investment account holders by category:

Category	Amount RO'000
Saving Account	1,118
Term deposit	18

Profit Equalization Reserve (PER)

Maisarah appropriates a certain amount in excess of the profit to be distributed to equity of IAH before taking in to consideration the Mudarib share of income. This is used to maintain a certain level of return on investment for equity of IAH.

Investment Risk Reserve (IRR)

Maisarah deducts IRR as per approved policy from the profit distributable to equity of IAH, after allocating the Mudarib share in order to cater against future losses for equity of IAH.

Displaced Commercial Risk (DCR)

Maisarah is exposed to DCR in the event of having equity of IAH profit rates that are lower than market rates. Maisarah has mitigated the risk through setting up of reserves that will be used in case of a drop in IAH profit rates.

5.4.1 Shari'a Compliance

The most distinct feature of any Islamic bank is its compliance with the principles of Shari'a in all its activities, operations, transactions and investments. To ensure compliance with the rules and principles of Shari'a, Maisarah has a fully independent setup of Shari'a Governance system.

The Shari'a Compliance and Audit Department have been setup with the purpose of examination and assessment of the extent to which the Institution is observing Shari'a Principles, Fatwas, guidelines and instructions issued by the Shari'a Supervisory Board of Maisarah. It also ensures a proper segregation exists between Maisarah and the parent bank with regards to services, products, funds and investments.

The Unit comes under the direct supervision of Shari'a Supervisory Board.

Non Shari'a Compliant Income

Maisarah is committed to contributing to charity any income generated from non-Islamic sources. Accordingly, any earning prohibited by Shari'a is credited to charity funds to be used for social welfare purposes.

During the year, Maisarah charged no penalty for default and / or late payments from the customers.

Zakat

In accordance with the Policy of Maisarah, the responsibility to pay Zakat is on the shareholders & IAH.

5.4.2 Break-up of PER and IRR

The following table summarized the breakdown of analysis of PER and IRR of IAH:

S. No.	Details	%
1	PER to PSIA Ratio	0.004%
2	IRR to PSIA Ratio	0.001%

5.4.3 Movement in PER & IRR

The following table summarized the movement in PER & IRR during the year

	RO'000 PER	RO'000 IRR
Balance at January 1	-	-
Amount apportioned from income allocated equity of IAH	0.045	0.014
Amount utilized during the year	-	-
Balance at December 31	0.045	0.014

The PER & IRR will revert to IAH as per the terms and conditions of the Mudaraba Contract.

As IAH funds are co-mingled with Maisarah's funds for investments, no priority is granted to, neither the Mudarib nor the Rab ul maal, for the purpose of Investments and distribution of profits.

Annexure I

Basel III Capital Disclosure Template

S. No.	Particulars	Amount Subject to Pre-Basel III treatment RO'000
	Common Equity Tier 1 Capital: Instruments and reserves	
1	Directly issued qualifying common share capital (and equivalent for non-joint stock companies) plus related stock surplus	161,031
2	Retained Earnings	47,650
3	Accumulated other comprehensive income (and other reserves)	76,230
4	Directly issued capital subject to phase out from CET1 (only applicable to non-joint stock companies)	
	Public Sector capital injections grandfathered until 1 January 2018	
5	Common share capital issued by subsidiaries and held by third parties (amount allowed in group CET 1)	
6	Common Equity Tier 1 Capital before regulatory adjustments	284,911
	Common Equity Tier 1 Capital: Regulatory Adjustments	
7	Prudential valuation adjustments	
8	Goodwill (net of related tax liability)	2,780
9	Other intangibles other than mortgage-servicing rights (net of related tax liability)	28
10	Deferred tax assets that rely on future profitability excluding those arising from temporary differences (net of related tax liability)	-
11	Cash Flow hedge reserve	-
12	Shortfall of provisions to expected loss	-
13	Securitization gain on sale (as set out in para 14.9 of CP-1)	-
14	Gains and losses due to changes in own credit risk on fair valued liabilities	-
15	Defined benefit pension fund net assets	-
16	Investments in own shares (if not already netted off paid-in capital on reported balance sheet)	-
17	Reciprocal cross holdings in common equity	-

18	Investments in the capital of banking, financial, insurance and takaful entities that are outside the scope of regulatory consolidation, net of eligible short positions, where the bank does not own more than 10% of the issued share capital (amount above 10% threshold)	-
19	Significant investments in the common stock of banking, financial, insurance and takaful entities that are outside the scope of regulatory consolidation, net of eligible short positions (amount above 10% threshold)	-
20	Mortgage servicing rights (amount above 10% threshold)	-
21	Deferred tax assets arising from temporary differences (amount above 10% threshold, net of related tax liability)	-
22	Amount exceeding the 15% threshold)	-
23	of which: significant investments in the common stock of financials	-
24	of which: mortgage servicing rights	-
25	of which: deferred tax assets arising from temporary differences	-
26	National specific regulatory adjustments	-
	Regulatory adjustments applied to common equity Tier 1 in respect of amount subject to pre-basel III treatment	-
27	Regulatory adjustments applied to common equity Tier 1 due to insufficient Additional Tier 1 and Tier 2 to cover deductions	
28	Total regulatory adjustments to common equity Tier 1	2,808
29	Common Equity Tier 1 capital (CET 1)	282,103
	Additional Tier 1 Capital: Instruments	
30	Directly issued qualifying Additional Tier 1 instruments plus related stock surplus	-
31	of which: classified as equity under applicable accounting standards	-
32	of which: classified as liabilities under applicable accounting standards	-
33	Directly issued capital instruments subject to phase out from Additional Tier 1	-
34	Additional Tier 1 instruments (and CET 1 instruments not included in row 5) issued by subsidiaries and held by third parties (amount allowed in group AT 1)	-
35	of which: instruments issued by subsidiaries subject to phase out	-
36	Additional Tier 1 capital before regulatory adjustments	-
	Additional Tier 1 Capital: Regulatory Adjustments	

37	Investments in own Additional Tier 1 instruments	-
38	Reciprocal cross holdings in Additional Tier 1 instruments	-
39	Investments in the capital of banking, financial, insurance and takaful entities that are outside the scope of regulatory consolidation, net of eligible short positions, where the bank does not own more than 10% of the issued common share capital of the entity (amount above 10% threshold)	-
40	Significant investments in the capital of banking, financial, insurance and takaful entities that are outside the scope of regulatory consolidation (net of eligible short positions)	-
41	National specific regulatory adjustments	-
	Regulatory adjustments applied to Additional Tier 1 in respect of amount subject to pre-basel III treatment	-
42	Regulatory adjustments applied to Additional Tier 1 due to insufficient Tier 2 to cover deductions	-
43	Total regulatory adjustments to Additional Tier 1	-
44	Additional Tier 1 capital (CET 1)	-
45	Tier 1 capital (T1 = CET 1 + AT 1)	282,103
	Tier 2 capital: Instruments and provisions	
46	Directly issued qualifying Tier 2 instruments plus related stock surplus	48,750
47	Directly issued capital instruments subject to phase out from Tier 2	
48	Tier 2 instruments (and CET 1 and AT 1 instruments not included in rows 5 or 34) issued by subsidiaries and held by third parties (amount allowed in group Tier 2)	
49	of which: instruments issued by subsidiaries subject to phase out	
50	Provisions and cumulative fair value gains on available for sale instruments	28,052
51	Tier 2 capital before regulatory adjustments	76,802
	Tier 2 capital: Regulatory Adjustments	
52	Investments in own Tier 2 instruments	-
53	Reciprocal cross holdings in Tier 2 instruments	-
54	Investments in the capital of banking, financial, insurance and takaful entities that are outside the scope of regulatory consolidation, net of eligible short positions, where the bank does not own more than 10% of the issued common share capital of the entity (amount above 10% threshold)	-

55	Significant investments in the capital of banking, financial, insurance and takaful entities that are outside the scope of regulatory consolidation (net of eligible short positions)	-
56	National specific regulatory adjustments	-
	Regulatory adjustments applied to Tier 2 in respect of amount subject to pre-basel III treatment	-
57	Total Regulatory Adjustments to Tier 2 capital	-
58	Tier 2 Capital (T 2)	76,802
59	Total Capital (TC = T 1 + T 2)	358,905
	Risk Weighted Assets in respect of amounts subject to pre-Basel III treatment	
	of which: (insert name of adjustment)	
	of which: (insert name of adjustment)	
60	Total Risk Weighted Assets (60a + 60b + 60c)	2,547,508
60a	of which: Credit Risk Weighted Assets	2,324,129
60b	of which: Market Risk Weighted Assets	56,798
60c	of which: Operational Risk Weighted Assets	166,581
	Capital Ratios	
61	Common Equity Tier 1 (as a percentage of risk weighted assets)	11.07%
62	Tier 1 (as a percentage of risk weighted assets)	11.07%
63	Total capital (as a percentage of risk weighted assets)	14.09%
64	Institution specific buffer requirement (minimum CET 1 requirement plus capital conservation buffer plus countercyclical buffer requirements plus G-SIB/ D-SIB buffer requirements expressed as a percentage of risk weighted assets)	7.00%
65	of which: capital conservation buffer requirement	0.00%
66	of which: bank specific countercyclical buffer requirement	0.00%
67	of which: D-SIB/ G-SIB buffer requirements	0.00%
68	Common Equity Tier 1 available to meet buffers (as a percentage of risk weighted assets)	2.07%

	National Minima (if different from Basel III)	
69	National common equity Tier 1 minimum ratio (if different from Basel III minimum)	NA
70	National Tier 1 minimum ratio (if different from Basel III minimum)	NA
71	National total capital minimum ratio (if different from Basel III minimum)	NA
	Amounts below the thresholds for deduction (before risk weighting)	
72	Non-significant investments in the capital of other financials	-
73	Significant investments in the common stock of financials	-
74	Mortgage servicing rights (net of related tax liability)	-
75	Deferred tax assets arising from temporary differences (net of related tax liability)	-
	Applicable caps on the inclusion of provisions in Tier 2	
76	Provisions eligible for inclusion in Tier 2 in respect of exposures subject to standardized approach (prior to application of cap)	27,250
77	Cap on inclusion of provisions in Tier 2 under standardized approach	29,052
78	Provisions eligible for inclusion in Tier 2 in respect of exposures subject to internal ratings based approach (prior to application of cap)	-
79	Cap for inclusion of provisions in Tier 2 under internal ratings based approach	-
	Capital instruments subject to phase-out arrangements (only applicable between 1 Jan 2018 and 1 Jan 2022)	
80	Current cap on CET 1 instruments subject to phase out arrangements	NA
81	Amount excluded from CET 1 due to cap (excess over cap after redemptions and maturities)	NA
82	Current cap on AT 1 instruments subject to phase out arrangements	NA
83	Amount excluded from AT 1 due to cap (excess over cap after redemptions and maturities)	NA
84	Current cap on T 2 instruments subject to phase out arrangements	NA
85	Amount excluded from T 2 due to cap (excess over cap after redemptions and maturities)	NA

Annexure IIa

The components used in the definition of capital disclosure template are provided below:

Reconciliation of reported balance sheet and the regulatory scope of consolidation			
Particulars	Balance sheet as in published financial statement As at period ended 31st Dec 2013	Under regulatory scope of consolidation As at period ended 31st Dec 2012	Reference
Assets			
Cash & Balances with CBO	345,758		
Balances with bank and money at call and short notice	85,098		
Investments:	178,001		
Of which Held to Maturity	153,366		
Out of investments in Held to Maturity:			
Investments in Subsidiaries			
Investments in Associates & Joint Ventures			
Of which Available for Sale	24,635		
Out of investments in Available for Sale:			
Investments in Subsidiaries			
Investments in Associates & Joint Ventures			
Of which Held for Trading			
Loans & Advances	1,938,182		
Of which,			
Loans & Advances to domestic banks			
Loans & Advances to Non Resident Banks	36,272		
Loans & Advances to domestic customers			
Loans & Advances to Non Resident Customers for domestic operations			
Loans & Advances to Non Resident Customers for operations abroad			
Loans & Advances to SMEs			
Financing from Islamic Banking Window			
Fixed Assets	10,903		
Other Asset	47,437		
Of which,			
Goodwill & Intangible Assets	2,780		a
Out of which			
Goodwill			
Other Intangibles (excluding MSRs)			
Deferred Tax Assets			

Goodwill on Consolidation			
Debit balance in Profit & Loss Account			
Total Assets	2,605,379		
Capital & Liabilities			
Paid up capital	121,013		
of which:			
Amount eligible for CET 1	121,013		h
Amount eligible for AT1	-		i
Reserves & Surplus	182,594		J
Share Premium	40,018		k
Special Reserve	18,488		p
Legal Reserve	31,492		L
Subordinated loan reserve	26,250		M
Investment Revaluation Reserve (Gains are included at 45% in Tier II and losses in full are deducted from Tier I)	1,754	(28)	N
Retained Earnings ((The proposed dividend payment amount is excluded from retained earnings)	64,592	47,650	O
Total Capital	303,607		
Deposits			
Of which,			
Deposit from Banks	106,334		
Customer Deposits	2,028,069		
Deposit of Islamic Banking Window	3,677		
Other deposits (pl specify)			
Borrowings			
Of which,			
From CBO			
From Banks			
From other Institutions & Agencies			
Borrowings in the form of bonds, debentures & Sukuks			
Others (Plz specify) (Subordinated Loans)	75,000	48,750	
Other liabilities & provisions	88,692		
Of which,			
DTLs related to goodwill			
DTLs related to intangible assets	333		
Total Liabilities	2,605,379		

Annexure IIb

The components mentioned in above table are mapped to the composition of capital disclosure template, which is provided below:

Table 2c: Common Equity Tier 1 capital: instruments and reserves			
S.No.		Component of regulatory capital reported by bank	Source based on reference numbers/letters of the balance sheet under the regulatory scope of consolidation from step 2
1	Directly issued qualifying common share (and equivalent for non-joint stock companies) capital plus related stock surplus	121,013	H
2	Retained earnings	163,898	k,l,m,o,p
3	Accumulated other comprehensive income (and other reserves)		
4	Directly issued capital subject to phase out from CET1 (only applicable to non-joint stock companies)		
5	Common share capital issued by subsidiaries and held by third parties (amount allowed in group CET1)		
6	Common Equity Tier 1 capital before regulatory adjustments	284,911	
7	Prudential valuation adjustments	28	n
8	Goodwill (net of related tax liability)	2,780	a

Annexure III

Main features template for capital instruments

Bank has two types of capital instruments viz., Common Shares and Subordinated Debt. The minimum level of summary disclosure for these regulatory capital instrument issued by the Bank is presented as under:

Common Shares

Disclosure for Main Features of regulatory capital instruments – Common Shares		
1	Issuer	Bank Dhofar
2	Unique identifier (e.g. CUSIP, ISIN or Bloomberg identifier for private placements	OM0000002549
3	Governing law(s) of the instrument	law of Sultanate of Oman
	Regulatory Treatment	
4	Transitional Basel III rules	Common Equity Tier I
5	Post-transitional Basel III rules	Common Equity Tier I
6	Eligible at solo/ group/ group & solo	Solo
7	Instrument type (types to be specified by each jurisdiction)	Ordinary shares
8	Amount to be recognized in regulatory capital (currency in Mn, as of most recent reporting date)	121
9	Par Value of Instrument	121
10	Accounting Classification	Shareholder›s equity
11	Original date of issuance	Common shares have been issued many times. The comparative position of the last 2 years has been provided in point 18 of notes to accounts.
12	Perpetual or dated	Perpetual
13	Original Maturity date	No maturity
14	Issuer call subject to prior supervisory approval	No
15	Optional call date, contingent call dates and redemption amount	Not applicable
16	Subsequent call dates, if applicable	Not applicable
	Coupons / Dividends	
17	Fixed or floating dividend coupon	No coupon
18	Coupon rate & any related index	Not applicable

19	Existence of a dividend stopper	Yes
20	Fully discretionary, partially discretionary or mandatory	Fully discretionary
21	Existence of step up or other incentive to redeem	No
22	Non-cumulative or cumulative	Non-cumulative
23	Convertible or non-convertible	Non-convertible
24	If convertible, conversion trigger(s)	Not applicable
25	If convertible, fully or partially	Not applicable
26	If convertible, conversion rate	Not applicable
27	If convertible, mandatory or optional conversion	Not applicable
28	If convertible, specify instrument type convertible into	Not applicable
29	If convertible, specify issuer of instrument it converts into	Not applicable
30	Write down features	Yes
31	If Write down, write down triggers	Non viability
32	If Write down, full or partial	Full
33	If Write down, permanent or temporary	Permanent
34	If temporary write down, description of write up mechanism	Not applicable
35	Position in subordination hierarchy in liquidation (specify instrument type immediately senior to instrument)	Fully subordinated (Subordinated debt are senior to ordinary shares)
36	Non-compliant transitioned features	No
37	If yes, specify non complaint features	Not applicable

Subordinated Loan 1

	Disclosure for Main Features of regulatory capital instruments – Subordinated debt	
1	Issuer	BankDhofar
2	Unique identifier (e.g. CUSIP, ISIN or Bloomberg identifier for private placements	Not applicable
3	Governing law(s) of the instrument	law of Sultanate of Oman
	Regulatory Treatment	
4	Transitional Basel III rules	Tier II
5	Post-transitional Basel III rules	Tier II
6	Eligible at solo/ group/ group & solo	Solo
7	Instrument type (types to be specified by each jurisdiction)	Subordinated Loan
8	Amount to be recognized in regulatory capital (currency in Mn, as of most recent reporting date)	RO 50 Mn
9	Par Value of Instrument	RO 50 Mn
10	Accounting Classification	Subordinated Loan
11	Original date of issuance	15/11/2011
12	Perpetual or dated	Dated
13	Original Maturity date	15/12/2016
14	Issuer call subject to prior supervisory approval	Yes
15	Optional call date, contingent call dates and redemption amount	Not applicable
16	Subsequent call dates, if applicable	Not applicable
	Coupons / Dividends	
17	Fixed or floating dividend coupon	Fixed
18	Coupon rate & any related index	5.5% p.a.
19	Existence of a dividend stopper	Not applicable
20	Fully discretionary, partially discretionary or mandatory	Mandatory
21	Existence of step up or other incentive to redeem	No
22	Non-cumulative or cumulative	Non-cumulative
23	Convertible or non-convertible	Non-convertible
24	If convertible, conversion trigger(s)	Not applicable

25	If convertible, fully or partially	Not applicable
26	If convertible, conversion rate	Not applicable
27	If convertible, mandatory or optional conversion	Not applicable
28	If convertible, specify instrument type convertible into	Not applicable
29	If convertible, specify issuer of instrument it converts into	Not applicable
30	Write down features	Yes
31	If Write down, write down triggers	No
32	If Write down, full or partial	Not applicable
33	If Write down, permanent or temporary	Not applicable
34	If temporary write down, description of write up mechanism	Not applicable
35	Position in subordination hierarchy in liquidation (specify instrument type immediately senior to instrument)	All the depositors
36	Non-compliant transitioned features	No
37	If yes, specify non complaint features	Not applicable

Subordinated Loan 2

Disclosure for Main Features of regulatory capital instruments – Subordinated debt		
1	Issuer	BankDhofar
2	Unique identifier (e.g. CUSIP, ISIN or Bloomberg identifier for private placements	Not applicable
3	Governing law(s) of the instrument	law of Sultanate of Oman
	Regulatory Treatment	
4	Transitional Basel III rules	Tier II
5	Post-transitional Basel III rules	Tier II
6	Eligible at solo/ group/ group & solo	Solo
7	Instrument type (types to be specified by each jurisdiction)	Subordinated Loan
8	Amount to be recognized in regulatory capital (currency in Mn, as of most recent reporting date)	RO 25 Mn
9	Par Value of Instrument	RO 25 Mn
10	Accounting Classification	Subordinated Loan
11	Original date of issuance	17/12/2012
12	Perpetual or dated	Dated
13	Original Maturity date	17/01/2018
14	Issuer call subject to prior supervisory approval	Yes
15	Optional call date, contingent call dates and redemption amount	Not applicable
16	Subsequent call dates, if applicable	Not applicable
	Coupons / Dividends	
17	Fixed or floating dividend coupon	Fixed
18	Coupon rate & any related index	5.125% p.a.
19	Existence of a dividend stopper	Not applicable
20	Fully discretionary, partially discretionary or mandatory	Mandatory
21	Existence of step up or other incentive to redeem	No
22	Non-cumulative or cumulative	Non-cumulative
23	Convertible or non-convertible	Non-convertible
24	If convertible, conversion trigger(s)	Not applicable
25	If convertible, fully or partially	Not applicable
26	If convertible, conversion rate	Not applicable
27	If convertible, mandatory or optional conversion	Not applicable
28	If convertible, specify instrument type convertible into	Not applicable
29	If convertible, specify issuer of instrument it converts into	Not applicable
30	Write down features	Yes
31	If Write down, write down triggers	No
32	If Write down, full or partial	Not applicable
33	If Write down, permanent or temporary	Not applicable
34	If temporary write down, description of write up mechanism	Not applicable
35	Position in subordination hierarchy in liquidation (specify instrument type immediately senior to instrument)	All the depositors
36	Non-compliant transitioned features	No
37	If yes, specify non complaint features	Not applicable

Financial statements for the year ended

31st December 2013

KPMG

KPMG
4th Floor, HSBC Bank Building
MBD
P.O. Box 641
P.C. 112
Sultanate of Oman

Tel 968 24709181
Fax 968 24700839

INDEPENDENT AUDITORS' REPORT TO THE SHAREHOLDERS OF BANK DHOFAR SAOG

Report on the financial statements

We have audited the financial statements of Bank Dhofar SAOG ("the Bank"), set out on pages 110 to 162 which comprise the statement of financial position as at 31 December 2013, the statements of comprehensive income, changes in equity and cash flows for the year then ended, and notes, comprising a summary of significant accounting policies and other explanatory information.

Management's responsibility for the financial statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with International Financial Reporting Standards, the disclosure requirements of the Capital Market Authority and the Commercial Companies Law of 1974, as amended, 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.

Auditors' responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those standards require that we comply with relevant ethical requirements and plan and perform the audit to obtain reasonable assurance about 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 our judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the 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 2013, and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

Report on other legal and regulatory requirements

In our opinion the financial statements of the Bank as at and for the year ended 31 December 2013, in all material respects, comply with:

- the relevant disclosure requirements of the Capital Market Authority; and
- the Commercial Companies Law of 1974, as amended.

Emphasis of matter

Without qualifying our opinion, we draw attention to note 6 on page 125 which sets out the basis on which recovery from a legal case in the amount of RO 26.1 million is recognised as income during the year 2013. This was charged as loss from a legal case during the year 2011.

29 January 2014

Khalid Masud Ansari

C.R. No. 1/30936/6

Statement of financial position
as at 31 December 2013

2013 USD'000	2012 USD'000		Notes	2013 RO'000	2012 RO'000
		Assets			
898,073	541,545	Cash and balances with Central Bank of Oman	*5*	**345,758**	208,495
315,247	253,013	Loans and advances to banks	*7*	**121,370**	97,410
4,940,026	4,344,177	Loans and advances to customers	*8*	**1,901,910**	1,672,508
63,987	30,099	Available-for-sale investments	*9*	**24,635**	11,588
398,353	260,743	Held-to-maturity investments	*10*	**153,366**	100,386
7,221	8,252	Intangible asset	*11*	**2,780**	3,177
28,319	24,499	Property and equipment	*12*	**10,903**	9,432
115,992	106,062	Other assets	*13*	**44,657**	40,834
6,767,218	5,568,390	**Total assets**		**2,605,379**	2,143,830
		Liabilities			
276,192	230,325	Due to banks	*14*	**106,334**	88,675
5,277,262	4,245,787	Deposits from customers	*15*	**2,031,746**	1,634,628
230,369	218,242	Other liabilities	*16*	**88,692**	84,023
194,805	194,805	Subordinated loans	*17*	**75,000**	75,000
5,978,628	4,889,159	**Total liabilities**		**2,301,772**	1,882,326
		Shareholder's equity			
314,320	285,745	Share capital	*18*	**121,013**	110,012
103,943	103,943	Share premium	*19*	**40,018**	40,018
48,021	-	Special reserve	*20 (d)*	**18,488**	-
81,797	66,628	Legal reserve	*20 (a)*	**31,492**	25,652
68,182	29,221	Subordinated loan reserve	*20 (b)*	**26,250**	11,250
4,556	4,042	Investment revaluation reserve	*20 (c)*	**1,754**	1556
167,771	189,652	Retained earnings	*21*	**64,592**	73,016
788,590	679,231	**Total shareholders' equity**		**303,607**	261,504
6,767,218	5,568,390	**Total liabilities and shareholders' equity**		**2,605,379**	2,143,830
1,199,875	984,177	**Contingent liabilities and commitments**	*32*	**461,952**	378,908
0.652	0.618	**Net assets per share (Rial Omani)**	*22*	**0.251**	0.238

The financial statements on pages 110 to 162 were approved by the Board of Directors on 29 January 2014 and were signed on their behalf by:

Eng. Abdul Hafidh Salim Rajab Al-Aujaili
Chairman

Abdul Hakeem Al-Aujaili
Acting Chief Executive Officer

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

Report of the Auditors - page 109

Statement of comprehensive income
for the year ended 31 December 2013

2013 USD'000	2012 USD'000		Notes	2013 RO'000	2012 RO'000
259,836	243,379	Interest income		100,037	93,701
(87,522)	(76,187)	Interest expense		(33,696)	(29,332)
172,314	167,192	**Net interest income**	23	66,341	64,369
488	-	Income from Islamic financing and investment activities		188	-
(39)	-	Unrestricted investment account holders' share of profit		(15)	-
449	-	**Net income from Islamic financing and investment activities**		173	-
25,527	18,958	Fees and commission income		9,828	7,299
(2,397)	(1,956)	Fees and commission expense		(923)	(753)
23,130	17,002	**Net fees and commission income**		8,905	6,546
36,725	34,229	Other income	24	14,139	13,178
232,618	218,423	**Operating income**		89,558	84,093
(108,512)	(88,345)	Staff and administrative costs	25	(41,777)	(34,013)
(9,192)	(7,881)	Depreciation	12	(3,539)	(3,034)
(117,704)	(96,226)	**Operating expenses**		(45,316)	(37,047)
114,914	122,197	**Profit from operations**		44,242	47,046
(19,190)	(18,294)	Provision for loan impairment	26	(7,388)	(7,043)
8,195	8,283	Recoveries from allowance for loan impairment	26	3,155	3,189
(3)	(13)	Bad debts written-off		(1)	(5)
-	(745)	Impairment of available-for-sale investments	9	-	(287)
67,868	-	Recovery from a legal case	6	26,129	-
171,784	111,428	**Profit from operations after provision**		66,137	42,900
(20,078)	(13,390)	Income tax expense	27	(7,730)	(5,155)
151,706	98,038	**Profit for the year**		58,407	37,745
151,706	98,038	**Profit for the year**		58,407	37,745
		Other comprehensive income:			
		Items that are or may be reclassified to statement of income:			
6,356	3,725	Net changes in fair value of available-for-sale investments	9	2,447	1,434
(5,842)	(2,057)	Reclassification adjustment on sale of available-for-sale investments	9	(2,249)	(792)
152,220	99,706	**Total comprehensive income for the year**		58,605	38,387
0.125	0.088	**Earnings per share basic and diluted (Rials Omani)**	28	0.048	0.031

The accompanying notes form an integral part of these financial statements.
Report of the Auditors - page 109

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

	Notes	Share capital RO'000	Share premium RO'000	Special reserve RO'000	Legal reserve RO'000	Subordinated loans reserve RO'000	Investment revaluation reserve RO'000	Retained earnings RO'000	Total RO'000
1-Jan-2013		**110,012**	**40,018**	**-**	**25,652**	**11,250**	**1,556**	**73,016**	**261,504**
Total comprehensive income for the year									
Profit for the year		-	-	-	-	-	-	58,407	58,407
Other comprehensive income for the year									
Net change in fair value of available-for-sale investments		-	-	-	-	-	2,447	-	2,447
Transfer to statement of income on sale of available-for -sale of investments		-	-	-	-	-	(2,249)	-	(2,249)
Impairment of available-for-sale investments		-	-	-	-	-	-	-	-
Total comprehensive income for the year		**-**	**-**	**-**	**-**	**-**	**198**	**58,407**	**58,605**
Transfer to legal reserve	*20*	-	-	-	5,840	-	-	(5,840)	-
Transactions with owners recorded directly in equity									
Dividend paid for 2012	*38*	-	-	-	-	-	-	(16,502)	(16,502)
Bonus shares issued for 2012	*38*	11,001	-	-	-	-	-	(11,001)	-
Transfer to subordinated loan reserve	*20*	-	-			15,000	-	(15,000)	-
Transfer to special reserve	*20*	-	-	18,488	-	-	-	(18,488)	-
31-Dec-2013		**121,013**	**40,018**	**18,488**	**31,492**	**26,250**	**1,754**	**64,592**	**303,607**
		USD'000	**USD'000**	**USD'000**	**USD'000**	**USD'000**	**USD'000**	**USD'000**	**USD'000**
1-Jan-2013		**285,745**	**103,943**	**-**	**66,628**	**29,221**	**4,042**	**189,652**	**679,231**
Total comprehensive income for the year									
Profit for the year		-	-	-	-	-	-	151,706	151,706
Other comprehensive income for the year									
Net change in fair value of available-for-sale investments		-	-	-	-	-	6,356	-	6,356
Transfer to statement of income on sale of available-for -sale of investments		-	-	-	-	-	(5,842)	-	(5,842)
Impairment of available-for-sale investments		-	-	-	-	-	-	-	-
Total comprehensive income for the year		**-**	**-**	**-**	**-**	**-**	**514**	**151,706**	**152,220**
Transfer to legal reserve	*20*	-	-	-	15,169	-	-	(15,169)	-
Transactions with owners recorded directly in equity									
Dividend paid for 2012	*38*	-	-	-	-	-	-	(42,861)	(42,861)
Bonus shares issued for 2012	*38*	28,575	-	-	-	-	-	(28,575)	-
Transfer to subordinated loan reserve	*20*	-	-	-	-	38,961	-	(38,961)	-
Transfer to special reserve	*20*	-	-	48,021	-	-	-	(48,021)	-
						-			
31-Dec-2013		**314,320**	**103,943**	**48,021**	**81,797**	**68,182**	**4,556**	**167,771**	**788,590**

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

Report of the Auditors - page 109

Statement of changes in equity
for the year ended 31 December 2012

	Notes	Share capital RO'000	Share premium RO'000	Legal reserve RO'000	Sub ordinated loans reserve RO'000	Investment revaluation reserve RO'000	Retained earnings RO'000	Total RO'000
1-Jan-2012		**91,524**	**58,506**	**21,877**	**34,617**	**627**	**22,086**	**229,237**
Total comprehensive income for the year								
Profit for the year		-	-	-	-	-	37,745	37,745
Other comprehensive income for the year								
Net change in fair value of available-for-sale investments		-	-	-	-	1,434	-	1,434
Transfer to statement of income on sale of available-for -sale of investments		-	-	-	-	(792)	-	(792)
Impairment of available-for-sale investments		-	-	-	-	287	-	287
Total comprehensive income for the year		**-**	**-**	**-**	**-**	**929**	**37,745**	**38,674**
Transfer to legal reserve	*20*	-	-	3,775	-	-	(3,775)	-
Transactions with owners recorded directly in equity								
Dividend paid for 2011	*38*	-	-	-	-	-	(6,407)	(6,407)
Bonus shares issued for 2011	*38*	18,488	(18,488)	-	-	-	-	-
Transfer to subordinated loan reserve	*20*	-	-		15,133	-	(15,133)	-
Transfer to retained earnings	*20*	-	-	-	(38,500)	-	38,500	-
31-Dec-2012		**110,012**	**40,018**	**25,652**	**11,250**	**1,556**	**73,016**	**261,504**

	Notes	USD'000	USD'000	USD'000	USD'000	USD'000	USD'000	USD'000
1-Jan-2012		**237,724**	**151,964**	**56,823**	**89,915**	**1,628**	**57,366**	**595,420**
Total comprehensive income for the year								
Profit for the year		-	-	-	-	-	98,039	98,039
Other comprehensive income for the year								
Net change in fair value of available-for-sale investments		-	-	-	-	3,725	-	3,725
Transfer to statement of income on sale of available-for -sale of investments		-	-	-	-	(2,057)	-	(2,057)
Impairment of available-for-sale investments		-	-	-	-	745	-	745
Total comprehensive income for the year		**-**	**-**	**-**	**-**	**2,414**	**98,039**	**100,453**
Transfer to legal reserve	*20*	-	-	9,805	-	-	(9,805)	-
Transactions with owners recorded directly in equity								
Dividend paid for 2011		-	-	-	-	-	(16,642)	(16,642)
Bonus shares issued for 2011		48,021	(48,021)	-	-	-	-	-
Transfer to subordinated loan reserve	*20*	-	-	-	39,306	-	(39,306)	-
Transfer to retained earnings	*20*	-	-	-	(100,000)	-	100,000	-
31-Dec-2012		**285,745**	**103,943**	**66,628**	**29,221**	**4,042**	**189,652**	**679,231**

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

Report of the Auditors - page 109

Statement of cash flows
for the year ended 31 December 2013

2013 USD'000	2012 USD'000		2013 RO'000	2012 RO'000
		Cash flows from operating activities		
311,234	288,584	Interest, commission and other receipts	**119,825**	111,105
(85,821)	(75,044)	Interest payments	**(33,041)**	(28,892)
(43,013)	(70,319)	Cash payments to suppliers and employees	**(16,560)**	(27,073)
182,400	143,221		**70,224**	55,140
		Decrease in operating assets		
(606,846)	(469,366)	Loans and advances to customers	**(233,636)**	(180,706)
(20,795)	(124,935)	Loans and advances to banks	**(8,006)**	(48,100)
(88,795)	15,247	Receipts from treasury bills and certificates of deposits (net)	**(34,186)**	5,870
(716,436)	(579,054)		**(275,828)**	(222,936)
		Increase in operating liabilities		
1,031,475	299,506	Deposits from customers	**397,118**	115,310
46,613	75,543	Due to banks	**17,946**	29,084
1,078,088	375,049		**415,064**	144,394
544,052	(60,784)	**Net cash from operating activities**	**209,460**	(23,402)
(12,930)	(4,795)	Income tax paid	**(4,978)**	(1,846)
531,122	(65,579)	**Net cash from (used in) operating activities**	**204,482**	(25,248)
		Cash flows from investing activities		
5,122	4,405	Investment income	**1,972**	1,696
(64,033)	(11,033)	Purchase of investments	**(24,653)**	(4,248)
29,914	12,218	Proceeds from sale of investments	**11,517**	4,704
1,036	1,036	Dividend received	**399**	399
(13,231)	(10,503)	Purchase of property and equipment	**(5,094)**	(4,044)
462	719	Proceeds from sale of property and equipment	**178**	277
(40,730)	(3,158)	**Net cash used in investing activities**	**(15,681)**	(1,216)
		Cash flow from financing activities		
-	64,935	Subordinated loan	**-**	25,000
-	(100,000)	Subordinated loan repaid	**-**	(38,500)
(42,862)	(16,642)	Dividend paid	**(16,502)**	(6,407)
(42,862)	(51,707)	**Net cash used in financing activities**	**(16,502)**	(19,907)
447,530	(120,444)	**Net change in cash and cash equivalents**	**172,299**	(46,371)
657,029	777,473	Cash and cash equivalents at the beginning of the year	**252,956**	299,327
1,104,559	657,029	**Cash and cash equivalents at the end of the year**	**425,255**	252,956
898,073	541,545	**Cash and balances with Central Bank of Oman** (Note 5)	**345,758**	208,495
(1,298)	(1,298)	Capital deposit with Central Bank of Oman	**(500)**	(500)
160,519	119,078	Loans and advances to banks due within 90 days	**61,800**	45,845
48,815	-	Treasury bills within 90 days	**18,794**	
(1,550)	(2,296)	Due to banks within 90 days	**(597)**	(884)
1,104,559	657,029	**Cash and cash equivalents for the purpose of the cash flow statement**	**425,255**	252,956

The accompanying notes form an integral part of these financial statements.
Report of the Auditors - page 109

Notes to the Financial Statements
for the year ended 31 December 2013

1. Legal status and principal activities

Bank Dhofar SAOG ("the Bank") is incorporated in the Sultanate of Oman as a public joint stock company and is principally engaged in corporate, retail and investment banking activities. During the year 2013, the Bank also started its Islamic Banking Window with an allocated capital of RO 12.5 million from the core paid up capital of the shareholders. The Bank has a primary listing on the Muscat Securities Market ("MSM") and its principal place of business is the Head Office, Capital Business District ("CBD"), Muscat, Sultanate of Oman.

2. Basis of preparation

a) Statement of compliance

These financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") as issued by International Accounting Standards Board (IASB), disclosure requirements of the Capital Market Authority and the Commercial Companies Law of 1974, as amended.

b) Basis of measurement

The financial statements have been prepared on the historical cost basis except for derivative financial instruments, financial instruments at fair value through profit and loss and available-for-sale financial assets which are measured at fair value.

c) Functional and presentation currency

Items included in the Bank's financial statements are measured using Rials Omani which is the currency of the primary economic environment in which the Bank operates, rounded off to the nearest thousand.

d) Use of estimates and judgements

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

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised and in any future periods affected.

Information about significant areas of uncertainty and critical judgements in applying accounting policies that have the most significant effect on the amounts recognised in the financial statements are described in note 4.

e) Accounting policies

During the year, the Bank has adopted the following standards effective for the annual period beginning on or after 1 January 2013. The new standards had no significant impact on the financial statements of the Bank, other than additional disclosures which are required under the below standards:

- IAS 1 (amendment) - Presentation of items of other comprehensive income
- IFRS 7 (Amendment) - Offsetting financial assets and financial liabilities
- IFRS 13 - Fair value measurement

The accounting policies set below have been consistently applied in dealing with items that are considered material in relation to the Bank's financial statements to all the periods presented.

Notes to the Financial Statements
for the year ended 31 December 2013

3. Principal accounting policies

3.1. Foreign currency translations

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised in the statement of income. Translation differences on non-monetary items, such as equities held at fair value through profit or loss, are reported as part of the fair value gain or loss. Translation differences on non-monetary items, other than those held at cost, such as equities classified as available-for-sale financial assets, are included in the investment revaluation reserve in equity.

3.2. Financial instruments

3.2.1. Recognition

The Bank recognises loans and advances, deposits, debt securities and subordinated liabilities on the date at which they originated. Regular way purchases and sales of financial assets are recognised on the trade date at which the Bank commits to purchase and sell the asset. All other financial assets and liabilities (including assets and liabilities at fair value through profit or loss) are initially recognised on the trade date at which the Bank becomes a party to the contractual provisions of the instrument.

A financial asset or financial liability is measured initially at fair value, plus for an item not at fair value through profit or loss, transaction costs that are directly attributable to its acquisition or issue.

3.2.2. Classification

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

3.2.2.1. Financial assets at fair value through profit or loss

This category has two sub-categories: financial assets held for trading, and those designated at fair value through profit or loss at inception. A financial asset is held in this category if acquired principally for the purpose of short-term profit taking or if so designated by management. Derivatives are also categorised as held for trading unless they are designated as hedges instruments.

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

- Doing so significantly reduces measurements inconsistencies that would arise if the related derivatives were treated as held for trading and the underlying financial instruments were carried at amortised costs;

- Certain investments, that are managed and evaluated on a fair value basis in accordance with documented risk management or investments strategy and reported to key management personnel on that basis are designated at fair value through profit or loss; and

- Financial instruments, containing one or more embedded derivatives significantly modify the cash flows, are designated at fair value through profit or loss.

Gains and losses arising from changes in the fair value of derivatives that are managed in conjunction with designated financial assets or financial liabilities are included in the statement of income.

3.2.2.2. Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They can be originated or acquired by the bank with no intention of trading the receivable and comprise loans and advances to banks and customers other than bonds purchased at original issuance.

Notes to the Financial Statements
for the year ended 31 December 2013

3. Principal accounting policies (continued)

3.2. Financial instruments (continued)

3.2.2.3. Available-for-sale investments

Available-for-sale investments are those intended to be held for an indefinite period of time, which may be sold in response to needs for liquidity or changes in interest rates, exchange rates or equity prices.

3.2.2.4. Held-to-maturity investments

Investments with fixed or determinable payments and fixed maturity dates that the Bank has the positive intention and ability to hold to maturity are classified as held-to-maturity investments. Held-to-maturity investments are recorded at amortised costs using the effective interest method less any impairment, with revenue recognised on an effective yield basis.

3.2.3. Derecognition

The Bank recognises financial assets at fair value through profit or loss and available-for-sale assets on the trade date, the date it commits to purchase or sell the asset. From this date any gains and losses arising from changes in fair value of the assets are recognised. Loans and receivables, deposits and subordinated liabilities are recognised on the date they are originated.

Financial assets are derecognised when the rights to receive cash flows from the financial assets have expired or where the Bank has transferred substantially all risks and rewards of ownership. A financial liability is derecognised when it is extinguished.

3.2.4. Measurement

Financial assets are measured initially at fair value plus transaction costs for all financial assets not carried at fair value through profit or loss.

Subsequent to initial recognition all financial assets at fair value through profit or loss and all available-for-sale assets are measured at fair value, except equity instrument that does not have a quoted market price in an active market and whose fair value cannot be reliably measured is stated at cost, including transaction costs, less impairment losses.

All non-trading financial liabilities and loans and receivables are measured at amortised cost less impairment losses. Amortised cost is calculated on the effective interest rate method. Premiums and discounts, including initial transaction costs, are included in the carrying amount of the related instrument and amortised based on the effective interest rate of the instrument.

3.2.5. Fair value measurement principles

The fair values of quoted investments in active markets are based on current bid prices. If the market for a financial asset is not active (and for unlisted securities), the Bank establishes fair value by using valuation techniques. These include the use of recent arm's length transactions, discounted cash flow analysis and other valuation techniques commonly used by market participants.
Where discounted cash flow techniques are used, estimated future cash flows are based on management's best estimates and the discount rate is a market related rate at the reporting date for an instrument with similar terms and conditions.

The fair value of derivatives that are not exchange-traded is estimated at the amount that the Bank would receive or pay to terminate the contract at the reporting date taking into account current market conditions and the current credit worthiness of the counter-parties.

3.2.6. Gains and losses on subsequent measurement

Gains and losses arising from changes in the fair value of the financial assets at fair value through profit or loss category are included in the statement of income in the period in which they arise. Gains and losses arising from changes in the fair value of available-for-sale financial assets are recognised in other comprehensive income, until the financial asset is derecognised or impaired at which time the cumulative gain or loss previously recognised in other comprehensive income is recognised in the statement of income.

Notes to the Financial Statements
for the year ended 31 December 2013

3. Principal accounting policies (continued)

3.3. Cash and cash equivalents

For the purpose of the cash flow statement, cash and cash equivalents comprise balances with less than three months' maturity from the date of acquisition, including: cash on hand, non-restricted cash deposited with the Central Bank of Oman, amounts due to / from other banks and eligible treasury bills and certificate of deposits.

3.4. Treasury bills and certificate of deposits

Treasury bills and certificates of deposit issued for a term longer than three months are classified as available-for-sale or held-to-maturity at the date of acquisition.

3.5. Offsetting

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

Income and expenses are presented on a net basis only permitted under IFRS's or for gains and losses arising from a group of similar transaction such as in the Banks trading activity.

3.6. Impairment of financial assets

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

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

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

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

Notes to the Financial Statements
for the year ended 31 December 2013

3. Principal accounting policies (continued)

3.6. Impairment of financial assets (continued)

The calculation of the present value of the estimated future cash flows of a collateralised financial asset reflects the cash flows that may result from foreclosure less costs for obtaining and selling the collateral, whether or not foreclosure is probable.

For the purposes of a collective evaluation of impairment, financial assets are grouped on the basis of similar credit risk characteristics (i.e. on the basis of the Bank's grading process that considers asset type, industry, geographical location, collateral type, past-due status and other relevant factors). Those characteristics are relevant to the estimation of future cash flows for groups of such assets by being indicative of the debtors' ability to pay all amounts due according to the contractual terms of the assets being evaluated.

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

Estimates of changes in future cash flows for groups of assets should reflect and be directionally consistent with changes in related observable data from period to period (for example, changes in unemployment rates, property prices, payment status, or other factors indicative of changes in the probability of losses in the group and their magnitude). The methodology and assumptions used for estimating future cash flows are reviewed regularly by the Bank to reduce any differences between loss estimates and actual loss experience.

When a loan is known to be uncollectible, all the necessary legal procedures have been completed, and the final loss has been determined, the loan is written off against the related provision for loan impairment. Such loans are written off after all the necessary procedures have been completed and the amount of the loss has been determined. Subsequent recoveries of amounts previously written off are included in the statement of income.

If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised (such as an improvement in the debtor's credit rating), the previously recognised impairment loss is reversed by adjusting the allowance account. The amount of the reversal is recognised in the statement of income.

The Bank assesses at each reporting date whether there is objective evidence that a financial asset or a group of financial assets, other than investments at fair value through profit and loss, is impaired. In the case of equity investments classified as available-for-sale, a significant or prolonged decline in the fair value of the security below its cost is considered in determining whether the assets are impaired. If any such evidence exists for available-for-sale financial assets, the cumulative loss – measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that financial asset previously recognised in profit or loss – is removed from other comprehensive income and recognised in the statement of income. Impairment losses recognised in the statement of income on equity instruments are not reversed through the statement of income. If, in a subsequent period, the fair value of a debt instrument classified as available for sale increases and the increase can be objectively related to an event occurring after the impairment loss was recognised in profit or loss, the impairment loss is reversed through the statement of income.

Notes to the Financial Statements
for the year ended 31 December 2013

3. Principal accounting policies (continued)

3.7. Property and equipment

Items of property and equipment are stated at cost less accumulated depreciation and impairment loss. Depreciation is calculated so as to write off the cost of property and equipment, other than freehold land and capital work-in-progress, by equal instalments over their estimated economic useful lives from the date the asset is brought into use, as follows:

	Years
Buildings	7 - 25
Furniture and fixtures	3 - 7
Motor vehicles	3 - 5
Computer equipment	4
Core banking system	10

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at each reporting date. An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount. The recoverable amount is the higher of the asset's fair value less costs to sell and value in use.

Gains and losses on disposal of property and equipment are determined by reference to their carrying amount and are taken into account in determining operating profit. Repairs and renewals are charged to the statement of income when the expense is incurred. Subsequent expenditure is capitalised only when it increases the future economic benefits embodied in the item of property and equipment. All other expenditure is recognised in the statement of income as an expense when incurred.

3.8. Intangible assets

Goodwill represents the excess of the cost of an acquisition over the fair value of the net identifiable assets acquired at the date of acquisition. Goodwill is tested annually for impairment and carried at cost less accumulated impairment losses.

3.9. Provisions

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

3.10. Dividends

Dividends are recognised as a liability in the year in which they are declared.

3.11.Interest income and expense

Interest income and expense are recognised in the statement of income using the effective interest method.

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

Once a financial asset or a group of similar financial assets has been written down as a result of an impairment loss, interest income is recognised using the rate of interest used to discount the future cash flows for the purpose of measuring the impairment loss.

Notes to the Financial Statements
for the year ended 31 December 2013

3. Principal accounting policies (continued)

3.12. Fees and commission income

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

3.13. Taxation

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

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

Deferred income tax is provided in full, on temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes (the tax base). The amount of deferred tax provided is based on the expected manner of realisation or settlement of the carrying amount of assets and liabilities, using tax rates enacted or substantively enacted at the reporting date. The principal temporary differences arise from depreciation of property and equipment and provisions.

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.

3.14. Employee benefits

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

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

3.15. Derivative financial instruments

Derivatives are stated at fair value. Fair values are obtained from quoted market prices in active markets, including recent market transactions, and valuation techniques, including discounted cash flow models and options pricing models, as appropriate. All derivatives are carried as assets when fair value is positive and as liabilities when fair value is negative.

The best evidence of the fair value of a derivative at initial recognition is the transaction price (i.e., the fair value of the consideration given or received) unless the fair value of that instrument is evidenced by comparison with other observable current market transactions in the same instrument (i.e. without modification or repackaging) or based on a valuation technique whose variables include only data from observable markets. When such evidence exists, the Bank recognises profits on the day of the transaction.

The method of recognising the resulting fair value gain or loss depends on whether the derivative is designated as a hedging instrument, and if so, the nature of the item being hedged. Although the Bank enters into derivative instruments for hedging purposes, certain derivative instruments do not qualify for hedge accounting. Changes in the fair value of any derivative instrument that does not qualify for hedge accounting are recognised immediately in the statement of income.

Notes to the Financial Statements
for the year ended 31 December 2013

3. Principal accounting policies (continued)

3.15. Derivative financial instruments (continued)

3.15.1 Embedded derivatives

Derivatives embedded in other financial instruments or other host contracts are treated as separate derivatives when their risks and characteristics are not closely related to those of the host contracts and the host contracts are not measured at fair value with changes in fair value recognised in profit or loss.

3.15.2 Hedge accounting

The Bank designates certain hedging instruments, which include derivatives, embedded derivatives and non-derivatives in respect of foreign currency risk, as either fair value hedges, cash flow hedges, or hedges of net investments in foreign operations. Hedges of foreign exchange risk on firm commitments are accounted for as cash flow hedges.

At the inception of the hedge relationship, the entity documents the relationship between the hedging instrument and the hedged item, along with its risk management objectives and its strategy for undertaking various hedge transactions. Furthermore, at the inception of the hedge and on an ongoing basis, the bank documents whether the hedging instrument that is used in a hedging relationship is highly effective in offsetting changes in fair values or cash flows of the hedged item.

3.15.3 Fair value hedges

Changes in the fair value of derivatives that are designated and qualify as fair value hedges are recorded in profit or loss immediately, together with any changes in the fair value of the hedged item that are attributable to the hedged risk. The change in the fair value of the hedging instrument and the change in the hedged item attributable to the hedged risk are recognised in the line of the statement of income relating to the hedged item.

Hedge accounting is discontinued when the Bank revokes the hedging relationship, the hedging instrument expires or is sold, terminated, or exercised, or no longer qualifies for hedge accounting. The adjustment to the carrying amount of the hedged item arising from the hedged risk is amortised to profit or loss from that date.

3.15.4 Cash flow hedges

The effective portion of changes in the fair value of derivatives that are designated and qualify as cash flow hedges are deferred in equity. The gain or loss relating to the ineffective portion is recognised immediately in profit or loss, and is included in the “other gains and losses” line of the statement of income.

Amounts deferred in equity are recycled in profit or loss in the periods when the hedged item is recognised in profit or loss, in the same line of the statement of income as the recognised hedged item. However, when the forecast transaction that is hedged results in the recognition of a non-financial asset or a non-financial liability, the gains and losses previously deferred in equity are transferred from equity and included in the initial measurement of the cost of the asset or liability.

Hedge accounting is discontinued when the Bank revokes the hedging relationship, the hedging instrument expires or is sold, terminated, or exercised, or no longer qualifies for hedge accounting. Any cumulative gain or loss deferred in equity at that time remains in equity and is recognised when the forecast transaction is ultimately recognised in profit or loss. When a forecast transaction is no longer expected to occur, the cumulative gain or loss that was deferred in equity is recognised immediately in profit or loss.

3.16. Sale and repurchase agreements

Securities sold subject to repurchase agreements (repos) are reclassified in the financial statements as pledged assets when the transferee has the right by contract or custom to sell or repledge the collateral; the counterparty liability is included in amounts due to other banks, deposits from banks, other deposits or deposits due to customers, as appropriate. Securities purchased under agreements to resell (reverse repos) are recorded as loans and advances to other banks or customers, as appropriate. The difference between sale and repurchase price is treated as interest and accrued over the life of the agreements using the effective interest method. Securities lent to counterparties are also retained in the financial statements.

Securities borrowed are not recognised in the financial statements, unless these are sold to third parties, in which case the purchase and sale are recorded with the gain or loss included in trading income.

Notes to the Financial Statements
for the year ended 31 December 2013

3. Principal accounting policies (continued)

3.17. Borrowings

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

3.18. Segment reporting

A segment is a distinguishable component of the Bank that is engaged either in providing products or services (business segment), or in providing products or services within a particular economic environment (geographical segment), which is subject to risks and rewards that are different from those of other segments. The Bank currently operates only in the Sultanate of Oman. The Bank's primary format for reporting segmental information is business segments, based upon management and internal reporting structure. The Bank's main business segments are corporate and retail banking.

3.19. Fiduciary assets

Assets held in trust or in a fiduciary capacity are not treated as assets of the Bank in the statement of financial position.

3.20. Trade and settlement date accounting

All "regular way" purchases and sales of financial assets are recognised on the trade date, i.e. that date the Bank commits to purchase the assets. Regular way purchase or sales are purchases or sales of financial assets that require delivery of assets within the time frame generally established by regulation or convention in the market place.

3.21. Directors' remuneration

Directors' remuneration is calculated in accordance with the Commercial Companies Law of 1974.

3.22. Standards not yet effective

Management anticipates that the adoption of these Standards and Interpretations in future periods will have no material impact on the financial statements of the Bank in the period of initial application except:

- IFRS 9 Financial Instruments: Classification and Measurement (effective from 1 January 2015) deals with classification and measurement of financial assets. The requirements of this standard represent a significant change from the existing requirements in IAS 39 in respect of financial assets.

- Offsetting Financial Assets and Financial Liabilities (Amendments to IAS 32) – (effective on or after 1 January 2014)

- Defined Benefit Plans: Employee Contributions (Amendments to IAS 19) – (effective on or after 30 June 2015)

The management are in the process of determining the impacts, if any, on the Bank's financial position and financial performance.

4. Critical accounting judgment and key sources of estimation uncertainty

(a) Classification of investments

Management decides on acquisition of an investment whether it should be classified as held for trading, carried at fair value through profit or loss, available-for-sale or held-to-maturity investments.

Available-for-sale investments

Management follows the guidance set out in International Accounting Standard (IAS) 39 Financial Instruments: Recognition and Measurement on classifying non-derivative financial assets as available-for-sale. This classification requires management's judgement based on its intentions to hold such investments.

Notes to the Financial Statements
for the year ended 31 December 2013

4. Critical accounting judgment and key sources of estimation uncertainty (continued)

Held-to-maturity investments

Management follows the guidance of IAS 39 on classifying non-derivative financial assets with fixed or determinable payments and fixed maturity as held-to-maturity. This classification requires significant judgements. In making this judgement, the Management evaluates its intention and ability to hold such investments to maturity. If the Management fails to keep these investments to maturity other than for the specific circumstances-for example, selling an insignificant amount close to maturity – it will be required to classify the entire class as available-for-sale. The investments would, therefore, be measured at fair value.

(b) Fair value estimation

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

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

(c) Impairment

Impairment losses on loans and advances

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

Impairment of goodwill

Determining whether goodwill is impaired requires an estimation of the value in use of the cash-generating units to which goodwill has been allocated. The value in use calculation requires the Bank to estimate the future cash flows expected to arise from the cash-generating unit and a suitable discount rate in order to calculate present value.

Impairment of available-for-sale investment

Management determines that available-for-sale investments are impaired when there has been a significant or prolonged decline in the fair value below its cost. This determination of what is significant or prolonged requires judgement. In making this judgement, management evaluates among other factors, the normal volatility in share price. In addition, impairment may be appropriate when there is evidence of deterioration in the financial health of the investee, industry and sector performance, changes in technology and operational and financing cash flows.

(d) Useful life of property and equipment

Depreciation is charged so as to write off the cost of assets over their estimated useful lives. The calculation of useful lives is based on management's assessment of various factors such as the operating cycles, the maintenance programs, and normal wear and tear using its best estimates.

Notes to the Financial Statements

for the year ended 31 December 2013

5. Cash and balances with Central Bank of Oman

	2013 RO'000	2012 RO'000
Cash in hand	**24,294**	20,468
Balances with the Central Bank of Oman	**131,464**	118,027
Certificate of deposits with maturity of 90 days or less	**190,000**	70,000
	345,758	208,495

At 31 December 2013, cash and balances with Central bank of Oman included balances with the Central Bank of Oman amounting to RO 500,000 (2012: RO 500,000) as minimum reserve requirements. These funds are not available for the Bank's daily business.

Outstanding certificate of deposits as of 31 December 2013 were issued by the Central Bank of Oman.

6 Recovery from a legal case

The Enforcement Court vide its order ref 1959/2006/10484 dated 25 June 2011 had ordered the Bank to transfer an amount of RO 26.1 million to its account (which has been paid) in connection with the legal case filed by Oman International Bank ("OIB") (currently HSBC Oman) against Ali Redha Al-Lawati and his companies (Ali Redha Trading and Muttrah Holding) and the Bank wherein Ali Redha Al-Lawati and his companies had claimed to own 1.925 million shares of the Bank and OIB (currently HSBC Oman) had claimed that these shares were pledged in its favour. This was categorically disputed by the Bank from the beginning and clarified clearly that this pledge was invalid and baseless due to lack of clear supporting documentation.

The case was primarily filed against Majan International Bank ("MIB") in 2001, which was acquired by the Bank in 2003 and the disputed shares were MIB shares.

On 24 July 2011, the Primary Court with the bench of three judges issued a judgment overruling the above judgment of the Enforcement Court that imposed an attachment of RO 26.1 million and considered the attachment as null and void. This judgment was appealed by OIB (currently HSBC Oman), Ali Redha and his group companies on 3 August 2011. The Appeal Court on 12 March 2012 rejected the appeal and upheld the Primary Court judgment.

On 25 March 2013, the Bank received a cheque of RO 26.1 million from the Primary Court in Muscat and the case against the Bank has been closed.

7. Loans and advances to banks

Syndicated loans to other banks	**36,639**	32,465
Less: impairment allowance	**(367)**	-
Net syndicated loans to other banks	**36,272**	32,465
Placements with other banks	**77,591**	53,107
Current clearing accounts	**7,507**	11,838
	121,370	97,410

At 31 December 2013, there are no placements with any banks representing 20% or more of the Bank's placements (2012: three placements with one local bank).

Notes to the Financial Statements
for the year ended 31 December 2013

8. Loans and advances to customers

	2013 RO'000	2012 RO'000
Overdrafts	**111,959**	130,559
Loans	**1,724,640**	1,499,949
Loans against trust receipts	**77,792**	88,009
Bills discounted	**13,099**	3,532
Advance against credit cards	**7,864**	7,881
Others	**18,907**	18,058
Islamic Banking Window financing	**28,268**	-
Gross loans and advances	**1,982,529**	1,747,988
Less: Impairment allowance	**(80,619)**	(75,480)
Net loans and advances	**1,901,910**	1,672,508

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

	2013 RO'000	2012 RO'000
(a) **Allowance for loan impairment**		
1 January	**48,064**	47,548
Allowance during the year	**7,021**	7,043
Released to the statement of income during the year	**(3,155)**	(3,189)
Written off during the year	**(1,121)**	(3,338)
31 December	**50,809**	48,064
(b) **Reserved interest**		
1 January	**27,416**	30,006
Reserved during the year	**5,437**	6,403
Released to the statement of income during the year	**(1,103)**	(875)
Written off during the year	**(1,940)**	(8,118)
31 December	**29,810**	27,416
Total impairment allowance	**80,619**	75,480

As a matter of policy, the Bank considers waiver / write-off or settlement only in such cases where the Bank is satisfied that the recovery of the full outstanding liabilities from the borrower is not possible in the normal course of business or out of the securities realisation or through enforcement of the guarantee (wherever available) and that legal action will not yield higher recoveries after considering the time and costs involved.

Proposals for waivers /write off are not formula driven and are decided on case by case basis after weighing all pros and cons. The rationale is invariably documented. In all cases, the Bank aims to recover the maximum value through enforcement of collaterals/guarantees etc.

In 2012, the Bank has written off RO 10.59 million as technical write off.

Notes to the Financial Statements
for the year ended 31 December 2013

8. Loans and advances to customers (continued)

Interest is reserved by the Bank against loans and advances which are impaired, to comply with the rules, regulations and guidelines issued by the Central Bank of Oman.

Under the Central Bank of Oman's guidelines for provision against classified loans and advances, at 31 December 2013, out of the total provisions of RO 80,619,390 (2012: RO 75,479,554) a collective provision was made on a general portfolio basis amounting to RO 26,883,000 (2012: RO 24,447,000). General provision includes RO 285,000 against loans and advances of Islamic window.

At 31 December 2013, impaired loans and advances on which interest has been reserved amount to RO 57,421,242 (2012: RO 54,550,882) and loans and advances on which interest is not being accrued amount to RO 1,257,648 (2012: RO 1,389,352).

Loan and advances are summarised as follows:

	2013		2012	
	Loans and advances to customers	Loans and advances to banks	Loans and advances to customers	Loans and advances to banks
	RO'000	RO'000	RO'000	RO'000
Neither past due nor impaired	**1,905,902**	**121,737**	1,680,052	97,410
Past due but not impaired	**18,168**	**-**	12,264	-
Impaired	**58,459**	**-**	55,672	-
Gross loans and advances	**1,982,529**	**121,737**	1,747,988	97,410
Less: Impairment allowance	**(80,619)**	**(367)**	(75,480)	-
Total	**1,901,910**	**121,370**	1,672,508	97,410

Loans and advances neither past due nor impaired

The credit quality of the portfolio of loans and advances that were neither past due nor impaired can be assessed by reference to the internal rating system adopted by the Bank.

Loans and advances past due but not impaired

	2013 RO'000	2012 RO'000
Past due up to 30 days	**12,296**	6,838
Past due 30 – 60 days	**4,324**	4,139
Past due 60 – 89 days	**1,548**	1,287
Total	**18,168**	12,264

Notes to the Financial Statements
for the year ended 31 December 2013

8. Loans and advances to customers (continued)

Impaired

	2013 RO'000	2012 RO'000
Substandard	**2,709**	2,011
Doubtful	**3,526**	3,585
Loss	**52,224**	50,076
Total	**58,459**	55,672

Fair value of collaterals

Upon initial recognition of loans and advances, the fair value of collateral is based on valuation techniques commonly used for the corresponding assets. In subsequent periods, the fair value is updated by reference to market price or indexes of similar assets.

Loans and advances renegotiated

Restructuring activities include extended payment arrangements, approved external management plans, modification and deferral of payments. Restructuring policies and practices are based on indicators or criteria which, in the judgment of management, indicate that payment will most likely continue. These policies are kept under continuous review. Restructuring is most commonly applied to term loans, in particular customer finance loans. Renegotiated loans that are classified as standard amounted to RO 3,247,551 at 31 December 2013 (2012: RO 5,210,000).

9. Available-for-sale investments

a) **Equity investments**

	Cost RO'000	Fair value 2013 RO'000	2012 RO'000
Quoted on the Muscat Securities Market			
Banking and investments	**1,147**	**1,324**	1,635
Services	**4,053**	**4,389**	4,278
Industrial	**5,982**	**6,303**	2,749
	11,182	**12,016**	8,662
Unquoted			
Omani companies	**1,699**	**2,619**	2,926
	1,699	**2,619**	2,926
	12,881	**14,635**	11,588

b) **Sukuk**

	Cost RO'000	Fair value 2013 RO'000	2012 RO'000
Unquoted			
Omani company	**10,000**	**10,000**	**-**
	10,000	**10,000**	-
	22,881	**24,635**	11,588

At 31 December 2013, the market value of the Sukuk approximates to the carrying value.

Notes to the Financial Statements
for the year ended 31 December 2013

10. Held-to-maturity investments

	2013 RO'000	2012 RO'000
Treasury bills	**74,661**	23,094
Government Development Bonds	**78,705**	77,292
	153,366	100,386

Outstanding treasury bills were issued by central banks outside Sultanate of Oman for a term of 3 to 6 months and carry interest rates ranging from 0.38% to 2.91% per annum (2012: 0.33% to 0.39%) per annum.

Outstanding Government Development Bonds carry interest ranging from 3.25% to 5.50% (2012: 3.25% to 5.50%) per annum and mature from 2014 to 2022.

11. Intangible asset

The movement in goodwill account is as follows:

	2013 RO'000	2012 RO'000
1 January	**3,177**	3,574
Impaired during the year	**(397)**	(397)
31 December	**2,780**	3,177

Intangible asset represents goodwill which resulted from the acquisition of branches of the Commercial Bank of Oman in the year 2001 and merger with Majan International Bank in the year 2003. Goodwill is tested for impairment each year.

12. Property and equipment

	Freehold land RO'000	Buildings RO'000	Furniture And fixtures RO'000	Motor vehicles RO'000	Computer equipment RO'000	Capital work-in-progress RO'000	Total RO'000
Cost							
1 January 2013	140	1,573	10,423	1,591	14,917	164	28,808
Additions	-	-	1,921	203	2,883	87	5,094
Disposals	-	-	(93)	(128)	(117)	-	(338)
31 December 2013	**140**	**1,573**	**12,251**	**1,666**	**17,683**	**251**	**33,564**
Depreciation							
1 January 2013	-	938	7,248	1,150	10,040	-	19,376
Charge for the year	-	59	1,253	323	1,904	-	3,539
Disposals	-	-	(86)	(127)	(41)	-	(254)
31 December 2013	**-**	**997**	**8,415**	**1,346**	**11,903**	**-**	**22,661**
Carrying value							
31 December 2013	**140**	**576**	**3,836**	**320**	**5,780**	**251**	**10,903**
31 December 2012	140	635	3,175	441	4,877	164	9,432

Notes to the Financial Statements
for the year ended 31 December 2013

13. Other assets

	2013 RO'000	2012 RO'000
Acceptances	**37,213**	33,447
Interest receivable	**4,328**	3,352
Prepaid expenses	**2,158**	2,101
Dividends receivable	**-**	8
Positive fair value of derivatives (note 33)	**247**	-
Other receivables	**711**	1,926
	44,657	40,834

14. Due to banks

Inter bank borrowings	**105,737**	87,791
Payable on demand	**597**	884
	106,334	88,675

At 31 December 2013, two borrowings with one bank represented 20% or more of the Bank's borrowings (2012: three banks). The Bank has not had any defaults of principal, interest or other breaches during the year on its borrowed funds.

At 31 December 2013, Inter bank borrowings includes Islamic Window's inter bank borrowings with other bank of RO 7,700,000.

15. Deposits from customers

Current accounts	**652,337**	322,219
Savings accounts	**322,472**	269,817
Time deposits	**1,047,953**	1,038,405
Margin accounts	**5,307**	4,187
Islamic Banking Window deposits	**3,677**	-
	2,031,746	1,634,628

Current accounts and time deposits include deposits from the Government of the Sultanate of Oman and its entities amounting to RO 802,103,000 as at 31 December 2013 (2012: RO 562,397,000).

At 31 December 2013, deposits from customers include Islamic window's current deposits, saving deposits and time deposits of RO 3,677,000.

Notes to the Financial Statements
for the year ended 31 December 2013

16. Other liabilities

	2013 RO'000	2012 RO'000
Acceptances	**37,213**	33,447
Interest payable	**4,203**	3,533
Creditors and accruals	**37,848**	40,497
Income tax provision	**7,969**	5,251
Deferred tax liability (note 27)	**588**	554
Negative fair value of derivatives (note 33)	**-**	40
Employee terminal benefits	**871**	701
	88,692	84,023

Employee terminal benefits

The Bank's net liability and the movement in the employee terminal benefits during the year are as follows:

1 January	**701**	683
Expense recognised in the statement of income	**245**	176
Paid to employees	**(75)**	(158)
	871	701

17. Subordinated loans

Subordinated loan - RO	**75,000**	75,000
	75,000	75,000

In December 2012, the Bank availed RO 25 million unsecured subordinated loan from the major shareholders for a tenor of 5 years and one month. This facility carries a fixed rate of interest payable half yearly with principle being repaid on maturity.

In November 2011, the Bank availed RO 50 million unsecured subordinated loan from the major shareholders for a tenor of 5 years and one month. This facility carries a fixed rate of interest payable half yearly, with principal being repaid on maturity.

Notes to the Financial Statements
for the year ended 31 December 2013

18. Share capital

The authorised share capital consists of 2,200,000,000 ordinary shares of RO 0.100 each (2012: 2,200,000,000 ordinary shares of RO 0.100 each).

At 31 December 2013, the issued and paid up share capital comprise 1,210,128,121 ordinary shares of RO 0.100 each (2012: 1,100,116,474 ordinary shares of RO 0.100 each).

Shareholders

The following shareholders of the Bank own 10% or more of the Bank's share capital:

		2013		2012
	No. of shares	%	No. of shares	%
Dhofar International Development and Investment Company SAOG	**336,600,000**	**27.8%**	305,767,544	27.8%
Eng. Abdul Hafidh Salim Rajab Al Aujaili and his related Companies	**252,174,876**	**20.8%**	229,249,889	20.8%
Civil Service Employees' Pension Fund	**121,542,165**	**10.1%**	111,124,474	10.1%
Total	**710,317,041**	**58.7%**	646,141,907	58.7%
Others	**499,811,080**	**41.3%**	453,974,567	41.3%
	1,210,128,121	**100.0%**	1,100,116,474	100.0%

The Shareholders, in the Annual General Meeting held on 28 March 2012, approved an allocation of RO 10,000,000 in respect of Islamic Banking window from the core paid up capital of the shareholders.

On 30 July 2013, the Board of Directors proposed the increase of Islamic Banking Window's allocated capital from RO 10,000,000 to RO 12,500,000 from the core paid up capital of the shareholders. A resolution to approve the increase in share capital will be presented to the shareholders at the annual general meeting.

19. Share premium

In the year 2008, the Bank issued 176,921,306 shares by way of rights issue at a premium of RO 0.300 resulting in an increase in share premium by RO 53,076,392.

On 28 March 2012, the Shareholders of the Bank in the annual general meeting approved the issuance of 20.20% bonus shares amounting to RO 18,487,814 (184,878,143 shares of par value RO 0.100 each) from the share premium account.

20. Reserves

(a) **Legal reserve**

	2013 RO'000	2012 RO'000
1 January	**25,652**	21,877
Appropriation for the year	**5,840**	3,775
31 December	**31,492**	25,652

Notes to the Financial Statements
for the year ended 31 December 2013

20. Reserves (continued)

(a) Legal reserve (continued)

In accordance with Article 106 of the Commercial Companies Law of 1974, annual appropriations of 10% of profit are made to the legal reserve until the accumulated balance of the reserve is equal to one-third of the Bank's paid up share capital. This reserve is not available for distribution.

(b) Subordinated loans reserves

	2013 RO'000	2012 RO'000
1 January	**11,250**	34,617
Appropriation for the year:		
Subordinated loan reserve - US Dollar	**-**	5,133
Subordinated loan reserve – RO	**15,000**	10,000
Transfer to retained earnings on maturity - US Dollar	**-**	(38,500)
31 December	**26,250**	11,250

Subordinated loan reserve

Consistent with the Bank for International Settlement ("BIS") Guidelines on capital adequacy, the Bank transfers an amount equivalent to 20% of the value of the subordinated loan each year to the subordinated loan reserve until the maturity of the loan. The amount of the reserve will be transferred to retained earnings through the statement of changes in equity upon settlement of the subordinated loan.

(c) Investment revaluation reserve

The movements in the investments revaluation reserve is analysed below:

	2013	2012
1 January	**1,556**	627
Increase in fair value	**2,447**	1,434
Impairment of available-for-sale investments taken to statement of income	**-**	287
Net transfer to statement of income on sale of available-for-sale investments	**(2,249)**	(792)
31 December	**1,754**	1,556

(d) Special reserve

During the year 2013, the Bank recognised in the statement of income, recovery from a legal case of RO 26.1 million, out of which, the Bank allocated RO 18.49 million (equivalent amount that was used from share premium account for issuance of bonus shares, which was approved by the Shareholders in the annual general meeting held on 28 March 2012) to a special reserve to strengthen capital and requires prior approval of CBO for any distribution from this 'special reserve account' (refer note 6).

21. Retained earnings

Retained earnings represent the undistributed profits generated by the Bank since incorporation.

Notes to the Financial Statements
for the year ended 31 December 2013

22. Net assets per share

Net assets per share are calculated by dividing the net assets at the year end by the number of shares outstanding at 31 December as follows:

	2013 RO'000	2012 RO'000
Net assets (RO)	**303,607,000**	261,504,000
Number of shares outstanding at 31 December (Nos.)	**1,210,128,121**	1,100,116,474
Net assets per share (RO)	**0.251**	0.238

23. Net interest income

Loans and advances to customers	**97,781**	93,106
Debt investments	**629**	193
Money market placements	**1,615**	392
Others	**12**	10
Total interest income	**100,037**	93,701
Deposits from customers	**(32,472)**	(27,711)
Money market deposits	**(1,224)**	(1,621)
Total interest expense	**(33,696)**	(29,332)
Net interest income	**66,341**	64,369

Included in interest income from debt investments is an amount of RO 437,000 (2012: RO 97,573) being interest income from held-to-maturity investments.

Included in interest expenses from customers is interest on subordinated loan against related parties of RO 4,031,050 (2012: RO 2,810,188).

24. Other income

Foreign exchange	**1,257**	1,162
Investment income (see below)	**5,724**	2,954
Miscellaneous income	**7,158**	9,062
	14,139	13,178
Investment income		
Dividend income- available-for-sale investments	**399**	391
Gain on disposal of available-for-sale investments	**2,542**	867
Income on Sukuk	**88**	-
Financial instruments at fair value through profit or loss	**723**	-
Interest income on Government Development Bonds/Other bonds	**1,972**	1,696
	5,724	2,954

Notes to the Financial Statements
for the year ended 31 December 2013

25. Staff and administrative costs

(a) Staff costs

	2013 RO'000	2012 RO'000
Salaries and allowances	**22,690**	19,705
Other personnel costs	**2,493**	1,974
Scheme costs	**1,047**	963
Non-Omani employees terminal benefit	**245**	176
	26,475	22,818

At 31 December 2013, the Bank had 1,350 employees (2012: 1,266 employees).

(b) Administrative costs

	2013 RO'000	2012 RO'000
Occupancy costs	**3,340**	2,884
Operating and administration cost	**10,474**	7,221
Impairment of goodwill	**397**	397
Others	**1,091**	693
	15,302	11,195
	41,777	34,013

26. Impairment of financial assets

	2013 RO'000	2012 RO'000
Impairment of available-for-sale investments	**-**	287
Provision for loan impairment (note 7 and 8)	**7,388**	7,043
Loans written-off	**1**	5
	7,389	7,335
Recoveries from provision for loan impairment (note 8)	**(3,155)**	(3,189)
Net impairment charge of financial assets	**4,234**	4,146

Notes to the Financial Statements
for the year ended 31 December 2013

27. Income tax

(a) Income tax expense:

	2013 RO'000	2012 RO'000
Current tax		
Current year	**7,696**	5,045
Deferred tax		
Current year	**16**	38
Prior years	**18**	72
Tax expense for the year	**7,730**	5,155

(b) Reconciliation:

The Bank is liable to income tax for the year 2013 in accordance with the income tax laws of the Sultanate of Oman at the rate of 12% on taxable profits in excess of RO 30,000. The following is a reconciliation of income taxes calculated at the applicable tax rate with the income tax expense:

	2013 RO'000	2012 RO'000
Accounting profit for the year	**66,137**	42,900
Tax liability at the rates mentioned above	**7,933**	5,144
Tax exempt revenue	**(363)**	(151)
Non-deductible expenses	**142**	90
Deferred tax prior years	**18**	72
Tax expense	**7,730**	5,155

Notes to the Financial Statements
for the year ended 31 December 2013

27. Income tax (continued)

(c) Temporary differences which give rise to deferred tax liability are as follows:

Particulars	2012 RO'000	Recognised in statement of income RO'000	2013 RO'000
Property, plant and equipment	(206)	**(73)**	**(279)**
Intangible asset	(372)	**39**	**(333)**
Provisions	24	**-**	**24**
Net deferred tax liability	(554)	**(34)**	**(588)**

(d) Status of previous year returns:

The tax returns of the Bank for the years 2009 to 2012 have not yet been agreed with the Secretariat General for Taxation at the Ministry of Finance.

Management are of the opinion that additional taxes, if any, related to the open tax years would not be significant to the Bank's financial position as at 31 December 2013.

28. Earnings per share (basic and diluted)

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

	2013 RO'000	2012 RO'000
Profit for the year (RO)	**58,407,000**	37,745,000
Weighted average number of shares outstanding during the year	**1,210,128,121**	1,210,128,121
Earnings per share basic and diluted (RO)	**0.048**	0.031

Earnings per share (basic and diluted) have been derived by dividing the profit for the year attributable to the shareholders by the weighted average number of shares outstanding. As there are no dilutive potential shares, the diluted earnings per share is identical to the basic earnings per share.

During the year 2013, the Bank issued 110.01 million bonus shares of RO 0.100 each to the existing shareholders, since the bonus issue was without consideration; the issue is treated as if it had occurred prior to the beginning of year 2012.

Notes to the Financial Statements

for the year ended 31 December 2013

29. Related parties transactions

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

	2013 RO'000	2012 RO'000
Loans and advances		
Directors and shareholders holding less than 10% interest in the Bank	**14,680**	11,690
Directors and shareholders holding 10% or more interest in the Bank	**45,921**	25,391
	60,601	37,081
Subordinated loans		
Directors and shareholders holding less than 10% interest in the Bank	**35,000**	35,000
Directors and shareholders holding 10% or more interest in the Bank	**40,000**	40,000
	75,000	75,000
Deposits and other accounts		
Directors and shareholders holding less than 10% interest in the Bank	**79,131**	127,357
Directors and shareholders holding 10% or more interest in the Bank	**314,609**	229,495
	393,740	356,852
Contingent liabilities and commitments		
Directors and shareholders holding less than 10% interest in the Bank	**1,807**	2,380
Directors and shareholders holding 10% or more interest in the Bank	**159**	14,750
	1,966	17,130
Remuneration paid to Directors		
Chairman		
– remuneration proposed	**15**	15
– sitting fees paid	**10**	10
Other Directors		
– remuneration proposed	**99**	102
– sitting fees paid	**76**	73
	200	200
Other transactions		
Rental payment to a related party	**464**	374
Remuneration and fees paid to Sharia' Board of Islamic Banking Window	**32**	-
Other transactions	**65**	60

Notes to the Financial Statements
for the year ended 31 December 2013

29. Related parties transactions (continued)

	2013 RO'000	2012 RO'000
Key management compensation		
Salaries and other benefits	**1,570**	923
End of service benefits	**21**	36
	1,591	959

30. Fiduciary assets

At 31 December 2013 and 2012, there were no funds under management with the Bank.

31. Single borrower and senior members

(a) **Single borrower**

	2013 RO'000	2012 RO'000
Total direct exposure	**173,327**	68,524
Number of Members	**3**	2

(b) **Senior members**

	2013 RO'000	2012 RO'000
Total exposure:		
Direct	**62,471**	39,297
Indirect	**1,966**	17,130
	64,437	56,427
Number of Members	**27**	23

Notes to the Financial Statements
for the year ended 31 December 2013

32. Contingent liabilities and commitments

(a) Credit related contingent items

Letters of credit, guarantees and other commitments for which there are corresponding customer liabilities:

	2013 RO'000	2012 RO'000
Letters of credit	**70,425**	70,239
Guarantees and performance bonds	**70,767**	136,197
Advance payment guarantees	**161,615**	79,633
Payment guarantees	**145,245**	78,048
Others	**13,900**	14,791
	461,952	378,908

At 31 December 2013, letters of credit, guarantees and other commitments amounting to RO 18,318,000 (2012: RO 13,408,000) are counter guaranteed by other banks.

(b) Legal cases

One of the Bank's customers filed a lawsuit against the Bank claiming compensation of RO 1,037,550 for commercial and moral damages. A judgment was issued directing the Bank to pay RO 400,000 to the Plaintiff. This judgment was upheld by the Appeal Court and the Bank challenged the same in the Supreme Court. On 23 May 2012, the Supreme Court revoked the Appeal Court confirmation of the primary judgment. Further, the Supreme Court directed the Appeal Court to review the primary judgment. The final decision is awaited.

The Bank, had earlier received in its favour a final judgment directing the Plaintiff to pay to the Bank an amount of RO 381,203 together with interest at the rate of 10.5% per annum up to the date of final payment.

(c) Capital and investment commitments

	2013 RO'000	2012 RO'000
Contractual commitments for property and equipment	**2,106**	2,015

33. Derivative financial instruments

The Bank uses the following derivative instruments for both hedging and non-hedging purposes:

Currency forwards represent commitments to purchase foreign and domestic currency, including undelivered spot transactions. Currency swaps are commitments to exchange one set of cash flows for another. Swaps result in an economic exchange of currencies. No exchange of principal takes place, except for certain currency swaps. The Bank's credit risk represents the potential cost to replace the swap contracts if counterparties fail to perform their obligation. This risk is monitored on an ongoing basis with reference to the current fair value, a proportion of the notional amount of the contracts and the liquidity of the market. To control the level of credit risk taken, the Bank assesses counterparties using the same techniques as for its lending activities.

Notes to the Financial Statements
for the year ended 31 December 2013

33. Derivative financial instruments (continued)

The notional amounts of certain types of financial instruments provide a basis for comparison with instruments recognised on the statement of financial position but do not necessarily indicate the amounts of future cash flows involved or the current fair value of the instruments and, therefore, do not indicate theBank's exposure to credit or price risks. The derivative instruments become favourable (assets) or unfavourable (liabilities) as a result of fluctuations in market interest rates or foreign exchange rates relative to their terms. The aggregate contractual or notional amount of derivative financial instruments on hand, the extent to which instruments are favourable or unfavourable, and thus the aggregate fair values of derivative financial assets and liabilities shown within other assets and other liabilities, can fluctuate significantly from time to time. The fair values of derivative instruments held are set out below:

At 31 December 2013		**Fair value increase / decrease**	
	Contract / notional amount RO'000	**Assets RO'000**	**Liabilities RO'000**
Foreign exchange derivatives			
Currency forward - purchase contracts	**186,851**	**576**	**-**
Currency forward - sales contracts	**186,714**	**-**	**329**

At 31 December 2012		**Fair value increase / decrease**	
	Contract / notional amount RO'000	**Assets RO'000**	**Liabilities RO'000**
Foreign exchange derivatives			
Currency forward - purchase contracts	46,430	67	-
Currency forward - sales contracts	46,473	-	107

The following table indicates the year in which the cash flows associated with derivatives that are expected to impact statement of income.

		Assets		**Liabilities**
	2013	**2012**	**2013**	**2012**
	RO'000	**RO'000**	**RO'000**	**RO'000**
Expected cash flow less than 6 months	**247**	-	**-**	40

Notes to the Financial Statements
for the year ended 31 December 2013

34. Fair value information

Based on the valuation methodology outlined below, the fair values of all financial instruments at 31 December 2013 are considered by the Management not to be materially different to their book values.

Estimation of fair values

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

Loans and advances

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

Investments

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

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

Current account balances due to and due from banks

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

Bank and customer deposits

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

Notes to the Financial Statements
for the year ended 31 December 2013

34. Fair value information (continued)

Other financial instruments

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

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

Fair value versus carrying amounts

The fair value of the financial assets and liabilities approximates their carrying value as stated in the statement of financial position.

Fair value measurements recognised in the statement of financial position

The following table provides an analysis of financial instruments that are measured subsequent to initial recognition at fair value, grouped into levels 1 to 3 based on the degree to which the fair value is observable:

- Level 1 fair value measurements are those derived from quoted prices (unadjusted) in active markets for identical assets or liabilities;
- Level 2 fair value measurements are those derived from inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices); and
- Level 3 fair value measurements are those derived from valuation techniques that include inputs for the asset or liability that are not based on observable market data (unobservable inputs).

At 31 December 2013	**Level 1**	**Level 2**	**Level 3**	**Cost**	**Total**
	RO'000	**RO'000**	**RO'000**	**RO'000**	**RO'000**
Available-for-sale investments					
Equity instruments	**12,016**	-	**2,619**	**-**	**14,635**
Sukuk	**-**	**-**	**-**	**10,000**	**10,000**
At 31 December 2012					
Available-for-sale investments					
Equity instruments	8,662	-	2,926	-	11,588

Valuation techniques include net present value and discounted cash flow models, comparison with similar instruments for which market observable prices exist and other valuation models. Assumptions and inputs used in valuation techniques include risk-free and benchmark interest rates, credit spreads and other premia used in estimating discount rates, bond and equity prices, foreign currency exchange rates, equity and equity index process and expected price volatilities and correlations.

Observable prices or model inputs are usually available in the market for listed debt and equity securities, exchange-traded derivatives and simple over-the-counter derivatives such as interest rate swaps. Availability of observable market prices and model inputs reduces the need for management judgment and estimation and also reduces the uncertainty associated with determining fair values. Availability of observable market prices and inputs varies depending on the products and markets and is prone to changes based on specific events and general conditions in the financial markets.

Notes to the Financial Statements
for the year ended 31 December 2013

35. Financial risk management

The important types of financial risks to which the Bank is exposed are credit risk, liquidity risk and market risk. The risk management division of the Bank is an independent and dedicated unit reporting directly to the Risk Management Committee ("RMC") of the Board. The division's primary responsibility is to assess, monitor and recommend strategies for control of credit, market and operational risk. The absence of any direct or indirect reporting lines and permanent membership in all the Bank's committees are among the factors which reflect the independence of the Risk Management Divisions working and the key role it plays within the Bank.

The risk management framework is pivoted on a host of committees involving the executive management and the Board of Directors ("the Board") for approval and reporting purposes. The Board has the overall authority for approval of strategies and policies, which it exercises through it's various sub-committees. The Risk Management Committee of the Board is responsible for reviewing and recommending to the full Board for approval all risk policies and procedures. RMC also reviews the risk profile of the Bank as presented to it by the RMD and appraises the full Board in its periodic meetings.

Credit risk

The most important risk to which the Bank is exposed, is credit risk. To manage the level of credit risk, the Bank deals with counter-parties of good credit.

Executive Committee of the Board is the final credit approving authority of the Bank which is mainly responsible for approving all credit proposals beyond the authority level of the management and also for reviewing and approving credit policies. This committee is also the final authority for approving investments beyond the authority of the management. The Management Credit Committee ("MCC") is the management decision making body which is empowered to consider all credit related issues upto certain limits.

Credit risk is managed by the RMD through a system of independent risk assessment in credit proposals beyond a threshold limit of RO 100,000 before they are considered by the appropriate approving authorities. The Bank has in place a risk grading system for analyzing the risk associated with credit. This facilitates the approving authorities in making their credit decision. In addition, RMD assists/ reviews grading of obligors, conducts regular macro analysis of the credit portfolio, and monitors credit concentration limits. Maximum counterparty/group exposures are limited to 15% of the Bank's capital base as stipulated by CBO and where a higher limit is required for projects of national importance prior CBO approval is obtained. Individual country limits using external leading rating agencies have also been set up to ensure portfolio diversification in terms of sovereign risk ratings and geographical exposure. These limits are approved by the Board. Retail lending is strictly in accordance with the CBO guidelines. The analysis of credit is given below:

Notes to the Financial Statements
for the year ended 31 December 2013

35. Financial risk management (continued)

Credit risk (continued)

(a) Geographical concentrations

	Assets			Liabilities		
	Gross loans and advances to banks	Gross loans and advances	Investment securities	Deposits from customers	Due to banks	Contingent liabilities
	RO'000	RO'000	RO'000	RO'000	RO'000	RO'000
31 December 2013						
Sultanate of Oman	**35,399**	**1,977,383**	**103,340**	**2,028,843**	**92,827**	**379,346**
Other GCC countries	**11,164**	**5,146**	**65,300**	**2,624**	**2,085**	**42,224**
Europe and North America	**21,357**	**-**	**9,361**	**57**	**7,709**	**22,183**
Africa and Asia	**53,817**	**-**	**-**	**222**	**3,713**	**18,199**
	121,737	**1,982,529**	**178,001**	**2,031,746**	**106,334**	**461,952**
31 December 2012						
Sultanate of Oman	38,175	1,741,403	88,880	1,631,711	10,175	292,818
Other GCC countries	5,898	5,687	23,094	2,699	66,809	29,033
Europe and North America	33,877	898	-	-	82	38,994
Africa and Asia	19,460	-	-	218	11,609	18,063
	97,410	1,747,988	111,974	1,634,628	88,675	378,908

(b) Customer concentrations

	Assets			Liabilities		
	Gross loans and advances to banks	Gross loans and advances	Investment securities	Deposits from customers	Due to banks	Contingent liabilities
	RO'000	RO'000	RO'000	RO'000	RO'000	RO'000
31 December 2013						
Personal	-	**870,226**	-	**447,248**	**-**	**310**
Corporate	**121,737**	**985,372**	**99,296**	**782,395**	**106,334**	**456,212**
Government	-	**126,931**	**78,705**	**802,103**	**-**	**5,430**
	121,737	**1,982,529**	**178,001**	**2,031,746**	**106,334**	**461,952**
31 December 2012						
Personal	-	789,742	-	374,414	-	13,909
Corporate	97,410	843,978	34,682	697,817	88,675	360,048
Government	-	114,268	77,292	562,397	-	4,951
	97,410	1,747,988	111,974	1,634,628	88,675	378,908

Notes to the Financial Statements
for the year ended 31 December 2013

35. Financial risk management (continued)

Credit risk (continued)

(c) Economic sector concentrations

	Assets	Liabilities	
	Gross loans and advances	Deposits from customers	Contingent liabilities
	RO'000	RO'000	RO'000
31 December 2013			
Personal	**870,226**	**447,248**	**310**
International trade	**93,624**	**17,537**	**26,635**
Construction	**236,889**	**65,243**	**287,929**
Manufacturing	**174,020**	**22,034**	**42,739**
Wholesale and retail trade	**40,242**	**6,155**	**13,571**
Communication and utilities	**133,205**	**22,381**	**822**
Financial services	**119,166**	**30,572**	**18,659**
Government	**126,931**	**802,103**	**5,430**
Other services	**105,147**	**126,510**	**59,670**
Others	**83,079**	**491,963**	**6,187**
	1,982,529	**2,031,746**	**461,952**

	Assets	Liabilities	
	Gross loans and advances	Deposits from customers	Contingent liabilities
	RO'000	RO'000	RO'000
31 December 2012			
Personal	789,742	374,414	13,909
International trade	99,387	17,185	24,463
Construction	217,077	60,838	196,370
Manufacturing	154,985	23,035	44,213
Wholesale and retail trade	40,091	6,247	12,205
Communication and utilities	57,828	16,004	12,669
Financial services	88,864	31,329	322
Government	114,268	562,397	4,951
Other services	95,661	129,237	54,723
Others	90,085	413,942	15,083
	1,747,988	**1,634,628**	**378,908**

Notes to the Financial Statements
for the year ended 31 December 2013

35. Financial risk management (continued)

Credit risk (continued)

(d) Gross credit exposure

	Total gross exposure		Monthly average gross exposure	
	2013	2012	2013	2012
	RO'000	RO'000	RO'000	RO'000
Overdrafts	**111,959**	130,559	**122,483**	120,272
Loans	**1,724,640**	1,499,949	**1,628,317**	1,472,942
Loans against trust receipts	**77,792**	88,009	**80,132**	76,477
Bills discounted	**13,099**	3,532	**9,647**	3,493
Advance against credit cards	**7,864**	7,881	**7,811**	7,597
Advance against receivable	**18,907**	18,058	**18,879**	14,796
Islamic Banking Window financing	**28,268**	-	**14,139**	-
Total	**1,982,529**	**1,747,988**	**1,881,408**	**1,695,577**

(e) Geographical distribution of exposures:

	Sultanate of Oman	Other countries	Total
	RO'000	RO'000	RO'000
31 December 2013			
Overdrafts	**111,959**	**-**	**111,959**
Loans	**1,719,729**	**4,911**	**1,724,640**
Loans against trust receipts	**77,557**	**235**	**77,792**
Bills discounted	**13,099**	**-**	**13,099**
Advance against credit cards	**7,864**	**-**	**7,864**
Others	**18,907**	**-**	**18,907**
Islamic Banking Window financing	**28,268**	**-**	**28,268**
	1,977,383	**5,146**	**1,982,529**
31 December 2012			
Overdrafts	130,559	-	130,559
Loans	1,493,653	6,296	1,499,949
Loans against trust receipts	87,720	289	88,009
Bills discounted	3,532	-	3,532
Advance against credit cards	7,881	-	7,881
Others	18,058	-	18,058
	1,741,403	**6,585**	**1,747,988**

Notes to the Financial Statements
for the year ended 31 December 2013

35. Financial risk management (continued)

Credit risk (continued)

(f) Industry type distribution of exposures by major types of credit exposures:

	Overdrafts	Loans	Bills discounted	Others	Total	Off balance sheet exposures
	RO'000	RO'000	RO'000	RO'000	RO'000	RO'000
31 December 2013						
Import trade	**11,385**	**56,672**	**63**	**25,213**	**93,333**	**26,540**
Export trade	**4**	**10**	**-**	**277**	**291**	**95**
Wholesale/retail trade	**6,682**	**25,879**	**-**	**7,681**	**40,242**	**13,571**
Mining and quarrying	**4,892**	**30,632**	**726**	**1,517**	**37,767**	**1,281**
Construction	**40,676**	**160,828**	**1,337**	**34,048**	**236,889**	**287,929**
Manufacturing	**10,048**	**138,373**	**1,499**	**24,100**	**174,020**	**42,739**
Electricity, gas and water	**86**	**40,556**	**118**	**182**	**40,942**	**513**
Transport and communication	**74**	**92,189**	**-**	**-**	**92,263**	**309**
Financial institutions	**2,238**	**107,303**	**9,342**	**283**	**119,166**	**18,659**
Services	**20,767**	**82,296**	**-**	**2,084**	**105,147**	**59,670**
Personal loans	**6,434**	**856,093**	**-**	**7,699**	**870,226**	**310**
Agriculture and allied activities	**1,677**	**5,721**	**14**	**86**	**7,498**	**814**
Government	**-**	**126,931**	**-**	**-**	**126,931**	**5,430**
Non-resident lending	**-**	**4,911**	**-**	**235**	**5,146**	**54**
Others	**6,996**	**24,514**	**-**	**1,158**	**32,668**	**4,038**
	111,959	**1,752,908**	**13,099**	**104,563**	**1,982,529**	**461,952**
31 December 2012						
Import trade	11,247	62,484	-	25,400	99,131	24,372
Export trade	5	13	-	238	256	91
Wholesale/retail trade	6,612	25,085	-	8,394	40,091	12,205
Mining and quarrying	4,093	17,109	218	2,116	23,536	2,450
Construction	49,542	136,432	1,006	30,097	217,077	196,370
Manufacturing	9,405	107,419	2,142	36,019	154,985	44,213
Electricity, gas and water	52	34,234	156	58	34,500	8,585
Transport and communication	204	23,124	-	-	23,328	4,084
Financial institutions	2,972	85,868	-	24	88,864	322
Services	30,415	62,234	-	3,012	95,661	54,723
Personal loans	8,695	773,313	-	7,734	789,742	13,909
Agriculture and allied activities	2,164	5,093	10	84	7,351	915
Government	-	114,265	-	3	114,268	4,951
Non resident lending	-	6,296	-	289	6,585	30
Others	5,153	46,980	-	480	52,613	11,688
	130,559	**1,499,949**	**3,532**	**113,948**	**1,747,988**	**378,908**

Notes to the Financial Statements
for the year ended 31 December 2013

35. Financial risk management (continued)

Credit risk (continued)

(g) Residual contractual maturities of the portfolio by major types of credit exposures:

	Overdrafts RO'000	Loans RO'000	Bills discounted RO'000	Others RO'000	Total RO'000	Off balance sheet exposures RO'000
31 December 2013						
Upto 1 month	**5,598**	**11,688**	**13,099**	**3,307**	**33,692**	**169,506**
1 - 3 months	**5,598**	**137,929**	**-**	**1,330**	**144,857**	**35,164**
3 - 6 months	**5,598**	**41,627**	**-**	**4,011**	**51,236**	**47,607**
6 - 9 months	**5,598**	**13,947**	**-**	**8,275**	**27,820**	**11,163**
9 - 12 months	**5,598**	**1,267**	**-**	**4,338**	**11,203**	**21,712**
1 - 3 years	**27,990**	**168,590**	**-**	**19,676**	**216,256**	**95,115**
3 – 5 years	**27,990**	**85,125**	**-**	**18,784**	**131,899**	**68,051**
Over 5 years	**27,989**	**1,292,735**	**-**	**44,842**	**1,365,566**	**13,634**
	111,959	**1,752,908**	**13,099**	**104,563**	**1,982,529**	**461,952**
31 December 2012						
Upto 1 month	6,528	3,806	17	683	11,034	96,187
1 - 3 months	6,528	106,753	-	4,044	117,325	35,311
3 - 6 months	6,528	46,836	-	6,743	60,107	37,800
6 - 9 months	6,528	1,061	-	22,941	30,530	20,796
9 - 12 months	6,527	201	-	5,304	12,032	15,137
1 - 3 years	32,640	104,629	537	19,886	157,692	101,628
3 – 5 years	32,640	87,172	218	9,830	129,860	54,400
Over 5 years	32,640	1,149,491	2,760	44,517	1,229,408	17,649
	130,559	**1,499,949**	**3,532**	**113,948**	**1,747,988**	**378,908**

Notes to the Financial Statements
for the year ended 31 December 2013

35. Financial risk management (continued)

Credit risk (continued)

(h) Distribution of impaired loans, past due and not past due loans by type of industry:

	Performing loans RO'000	Non performing loans RO'000	General provisions held RO'000	Specific provisions held RO'000	Interest reserve RO'000	Specific provision during the year RO'000	Advances written off during the year RO'000
31 December 2013							
Import trade	**86,538**	**6,795**	**866**	**1,468**	**4,998**	**34**	**-**
Export trade	**277**	**14**	**3**	**3**	**10**	**-**	**-**
Wholesale/retail trade	**23,206**	**17,036**	**232**	**5,002**	**12,119**	**32**	**-**
Mining and quarrying	**37,762**	**5**	**378**	**4**	**1**	**290**	**-**
Construction	**232,767**	**4,122**	**2,328**	**1,776**	**1,962**	**35**	**1**
Manufacturing	**173,282**	**738**	**1,733**	**244**	**260**	**75**	**-**
Electricity, gas and water	**40,941**	**1**	**410**	**1**	**-**	**-**	**-**
Transport and communication	**92,260**	**3**	**923**	**1**	**2**	**-**	**-**
Financial institutions	**119,166**	**-**	**1,192**	**-**	**-**	**-**	**-**
Services	**104,597**	**550**	**1,046**	**211**	**334**	**54**	**1,054**
Personal loans	**846,482**	**23,744**	**15,791**	**10,641**	**9,506**	**3,926**	**66**
Agriculture and allied activities	**7,489**	**9**	**75**	**7**	**1**	**1**	**-**
Government	**126,931**	**-**	**1,269**	**-**	**-**	**-**	**-**
Non resident lending	**235**	**4,911**	**3**	**4,429**	**486**	**-**	**-**
Others	**32,137**	**531**	**634**	**139**	**131**	**108**	**-**
	1,924,070	**58,459**	**26,883**	**23,926**	**29,810**	**4,555**	**1,121**
31 December 2012							
Import trade	93,107	6,024	931	1,492	4,203	98	2,910
Export trade	206	50	2	11	17	-	16
Wholesale/retail trade	24,906	15,185	249	4,981	10,276	23	-
Mining and quarrying	23,532	4	235	3	-	2	
Construction	212,084	4,993	2,121	1,985	2,269	554	198
Manufacturing	154,199	786	1,542	241	211	70	-
Electricity, gas and water	34,473	27	345	6	5	-	-
Transport and communication	23,325	3	233	1	2	-	-
Financial institutions	88,809	55	888	5	45	-	-
Services	92,696	2,965	927	1,257	1,708	13	71
Personal loans	769,399	20,343	15,218	9,392	8,210	3,257	143
Agriculture and allied activities	7,343	8	73	7	1	1	-
Government	114,268	-	1,143	-	-	-	-
Non resident lending	1,777	4,808	18	4,140	382	290	-
Others	52,192	421	522	96	87	65	-
	1,692,316	**55,672**	**24,447**	**23,617**	**27,416**	**4,373**	**3,338**

Notes to the Financial Statements
for the year ended 31 December 2013

35. Financial risk management (continued)

Credit risk (continued)

(i) Distribution of impaired loans and gross loans by geographical distribution:

	Gross loans	Non-performing loans	General provisions held	Specific provisions held	Interest reserve	Specific provision made during the year	Advances written off during the year
	RO'000	RO'000	RO'000	RO'000	RO'000	RO'000	RO'000
31 December 2013							
Sultanate of Oman	**1,977,383**	**53,528**	**26,880**	**19,497**	**29,324**	**4,555**	**1,121**
Other countries	**5,146**	**4,931**	**3**	**4,429**	**486**	**-**	-
	1,982,529	**58,459**	**26,883**	**23,926**	**29,810**	**4,555**	**1,121**
31 December 2012							
Sultanate of Oman	1,741,403	50,864	24,429	19,477	27,034	4,083	3,338
Other countries	6,585	4,808	18	4,140	382	290	-
	1,747,988	55,672	24,447	23,617	27,416	4,373	3,338

(j) Maximum exposure to credit risk without consideration of collateral held:

	2013 RO' 000	2012 RO' 000
Treasury bills	**74,661**	23,094
Loans and advances to banks	**121,370**	97,410
Loans and advances to customers	**1,901,910**	1,672,508
Government development bonds	**78,705**	77,292
	2,176,646	1,870,304
Off-balance sheet items		
Financial guarantees	**377,627**	293,878
	2,554,273	2,164,182

At 31 December 2013, impairment losses would have increased by RO 1,628,368 (2012: RO 2,712,067) had collateral not been obtained by the Bank for the impaired loans and advances.

Notes to the Financial Statements
for the year ended 31 December 2013

35. Financial risk management (continued)

Liquidity risk

Liquidity risk is the potential inability to meet the Bank's liabilities that are settled by delivering cash or another financial asset as they become due. It arises when the Bank is unable to generate cash to cope with a decline in deposits or increase in assets.

Bank's Liquidity Risk Management is governed by the Treasury Risk Policy document approved by the Board of Directors as well as the provisions of relevant CBO guidelines on liquidity risk management. The Treasury risk policy also incorporates contingency plans and measures so as the Bank is always in a position to meet all maturing liabilities as well as to fund asset growth and business operations. The contingency funding plan includes effective monitoring of the cash flows on a day to day basis, holding of tradable high quality liquid assets, which may be readily disposed off in sizeable amount etc. The Bank also has in place adequate lines of credit from both local and international Banks to meet any unforeseen liquidity requirements.

The Bank monitors its liquidity risk through cash flow approach and stock approach. Under cash flow approach Bank generates Maturity of Assets and Liabilities (MAL) report which captures all the maturing assets and liabilities into various pre-set time buckets ranging from one month to five years. The mismatches in various time buckets indicate liquidity gap and Bank strictly adheres to the CBO set limit of 15% of cumulative liabilities (outflows) on mismatches (liquidity gaps) in time buckets upto one year. In addition, the Bank has also set up internal limit on mismatches in time buckets beyond one year. Under stock approach, Bank monitors the liquidity risk through liquidity ratios, which portrays the liquidity available at the reporting date.

Treasury department of the Bank controls and monitors the liquidity risk and ensures that the Bank is not exposed to undue liquidity risk and at the same time make optimum use of its funds. Middle office in Risk Management Division also monitors the liquidity position of the Bank and provide the liquidity gap to Treasury Department to meet liquidity gaps.

Notes to the Financial Statements
for the year ended 31 December 2013

35. Financial risk management (continued)

Liquidity risk (continued)

Maturity profile of assets and liabilities

	Due on demand and up to 30 days	More than 1month to 6 months	More than 6 months to 12 months	More than 1 year to 5 years	Over 5 years	Total
	RO'000	RO'000	RO'000	RO'000	RO'000	RO'000
31 December 2013						
Cash and balances with Central Bank of Oman	345,258	-	-	-	500	345,758
Loans and advances to banks	44,778	54,001	13,101	9,490	-	121,370
Loans and advances to customers	177,818	270,857	75,957	468,683	908,595	1,901,910
Available-for-sale investments	-	-	14,635	10,000	-	24,635
Held-to-maturity investments	20,511	54,150	20,662	45,496	12,547	153,366
Intangible asset	-	-	-	-	2,780	2,780
Property and equipment	-	-	-	-	10,903	10,903
Other assets	32,905	7,152	1,468	15	3,117	44,657
Total assets	621,270	386,160	125,823	533,684	938,442	2,605,379
Due to banks	66,046	40,288	-	-	-	106,334
Deposits from customers	193,575	424,962	403,383	450,323	559,503	2,031,746
Other liabilities	51,008	16,695	3,017	16,305	1,667	88,692
Subordinated loans	-	-	-	75,000	-	75,000
Shareholders' equity	-	58,407	-	-	245,200	303,607
Total liabilities and shareholders' equity	310,629	540,352	406,400	541,628	806,370	2,605,379

Notes to the Financial Statements
for the year ended 31 December 2013

35. Financial risk management (continued)

Liquidity risk (continued)

Maturity profile of assets and liabilities (continued)

	Due on demand and up to 30 days	More than 1month to 6 months	More than 6 months to 12 months	More than 1 year to 5 years	Over 5 years	Total
	RO'000	RO'000	RO'000	RO'000	RO'000	RO'000
31 December 2012						
Cash and balances with Central Bank of Oman	207,995	-	-	-	500	208,495
Loans and advances to banks	62,727	6,583	28,100	-	-	97,410
Loans and advances to customers	149,656	259,996	72,904	410,931	779,021	1,672,508
Available-for-saleInvestments	-	-	11,588	-	-	11,588
Held-to-maturity Investments	-	23,094	-	66,853	10,439	100,386
Intangible asset	-	-	-	-	3,177	3,177
Property and equipment	-	-	-	-	9,432	9,432
Other assets	7,417	30,823	2,554	40	-	40,834
Total assets	427,795	320,496	115,146	477,824	802,569	2,143,830
Due to banks	45,095	20,480	15,400	7,700	-	88,675
Deposits from customers	158,745	386,236	371,028	570,410	148,209	1,634,628
Other liabilities	20,012	38,312	4,440	18,901	2,358	84,023
Subordinated loans	-	-	-	50,000	25,000	75,000
Shareholders' equity	-	37,745	-	-	223,759	261,504
Total liabilities and shareholders' equity	223,852	482,773	390,868	647,011	399,326	2,143,830

Notes to the Financial Statements
for the year ended 31 December 2013

35. Financial risk management (continued)

Market risk

Market risk includes currency risk, interest rate risk and equity price risk.

(a) Currency risk

The Bank is exposed to currency risk through its transactions in foreign currencies. The major foreign currency to which the Bank is exposed is the US Dollar which is effectively pegged to Rial Omani. The Bank finances a significant portion of its financial assets in the same currencies as the relevant measurement currencies to mitigate its foreign currency risk.

The Bank's transactional exposures give rise to foreign currency gains and losses that are recognised in the statement of income. The Bank ensures that its net exposure is kept to an acceptable level by buying and selling foreign currencies at spot rates when considered appropriate. Foreign exchange risk is computed on the average of the sum of net short positions or net long positions, whichever is higher of the foreign currency positions held by the bank. The foreign currency exposures are given below:

Foreign currency exposures

	2013 RO'000	2012 RO'000
Net assets denominated in US Dollars	**56,229**	16,553
Net assets denominated in other foreign currencies	**2,090**	1,194
	58,319	17,747

(b) Interest rate risk

The Bank's operations are subject to the risk of interest rate fluctuations to the extent that interest-earning assets and interest-bearing liabilities are reset at different times. Risk management activities are aimed at optimising net interest income, given market interest rate levels, consistent with the Bank's business strategies. The Bank manages mismatches by following policy guidelines and reduces risk by matching the repricing of assets and liabilities. Details relating to re-pricing mismatches and the interest rate risk thereon are placed to the ALCO in its regular meetings and also to the Risk Management Committee of the Board. Impact on earnings due to interest rate risk in the banking book is as follows:

Impact on earnings due to interest rate risk in the banking book

	+ or – 1%		+ or – 2%	
	2013 RO'000	2012 RO'000	2013 RO'000	2012 RO'000
Omani Rials	**8,258**	5,944	**16,516**	11,888
US Dollars	**2,064**	1,203	**4,128**	2,406
Others currencies	**201**	159	**402**	317

Notes to the Financial Statements

for the year ended 31 December 2013

35. Financial risk management (continued)

Market risk (continued)

(b) Interest rate risk (continued)

Interest rate sensitivity gap

Sensitivity to interest rates arises from mismatches in the period to repricing of assets and that of the corresponding liability. The Bank manages these mismatches by following policy guidelines and reduces risk by matching the repricing of assets and liabilities.

	Effective average interest rate	Due on demand and within 30 days	Due within 1 to 6 months	Due within 7 to 12 months	Due within 1 to 5 years	Due after 5 years	Non-interest bearing	Total
	%	RO'000	RO'000	RO'000	RO'000	RO'000	RO'000	RO'000
31 December 2013								
Cash and balances with Central Bank of Oman	0.13%	190,000	-	-	-	500	155,258	345,758
Loans and advances to banks	1.2%	44,778	58,804	17,788	-	-	-	121,370
Loans and advances to customers	5.5%	321,524	809,613	46,432	385,401	338,940	-	1,901,910
Available-for-sale investments		-	-	-	-	-	24,635	24,635
Held-to-maturity investments	1.7%	20,511	54,150	20,662	45,496	12,547	-	153,366
Intangible asset		-	-	-	-	-	2,780	2,780
Property and equipment		-	-	-	-	-	10,903	10,903
Other assets		-	-	-	-	-	44,657	44,657
Total assets		576,813	922,567	84,882	430,897	351,987	238,233	2,605,379
Due to banks	0.9%	65,449	40,288	-	-	-	597	106,334
Deposits from customers	1.7%	529,275	238,469	345,684	396,848	5,018	516,452	2,031,746
Other liabilities		-	-	-	-	-	88,692	88,692
Subordinated loan	5.4%	-	-	-	75,000	-		75,000
Shareholders' equity		-	58,407	-	-	-	245,200	303,607
Total liabilities and shareholders' equity		594,724	337,164	345,684	471,848	5,018	850,941	2,605,379
On-balance sheet gap		(17,911)	585,403	(260,802)	(40,951)	346,969	(612,708)	
Cumulative interest sensitivity gap		(17,911)	567,492	306,690	265,739	612,708		

Notes to the Financial Statements
for the year ended 31 December 2013

35. Financial risk management (continued)

Market risk (continued)

(b) Interest rate risk (continued)

Interest rate sensitivity gap (continued)

	Effective average interest rate	Due on demand and within 30 days	Due within 1 to 6 months	Due within 7 to 12 months	Due within 1 to 5 years	Due after 5 years	Non-interest bearing	Total
	%	RO'000	RO'000	RO'000	RO'000	RO'000	RO'000	RO'000
31 December 2012								
Cash and balances with Central Bank of Oman	0.9%	70,000	-	-	-	500	137,995	208,495
Loans and advances to banks	0.9%	64,460	32,950	-	-	-	-	97,410
Loans and advances to customers	5.8%	149,656	259,996	72,904	410,931	779,021	-	1,672,508
Available-for-sale investments	-	-	-	-	-	-	11,588	11,588
Held-to-maturity investments	1.5%	-	23,094	-	66,853	10,439	-	100,386
Intangible asset		-	-	-	-	-	3,177	3,177
Property and equipment		-	-	-	-	-	9,432	9,432
Other assets		-	-	-	-	-	40,834	40,834
Total assets		284,116	316,040	72,904	477,784	789,960	203,026	2,143,830
Due to banks	1.3%	44,820	43,580	-	-	-	275	88,675
Deposits from customers	1.7%	259,941	246,478	279,603	435,501	200	412,905	1,634,628
Other liabilities		-	-	-	-	-	84,023	84,023
Subordinated loan	5.5%	-	-	-	50,000	25,000	-	75,000
Shareholders' equity		-	37,745	-	-	-	223,759	261,504
Total liabilities and shareholders' equity		304,761	327,803	279,603	485,501	25,200	720,962	2,143,830
On-balance sheet gap		(20,645)	(11,763)	(206,699)	(7,717)	764,760	(517,936)	
Cumulative interest sensitivity gap		(20,645)	(32,408)	(239,107)	(246,824)	517,936	-	

Notes to the Financial Statements
for the year ended 31 December 2013

35. Financial risk management (continued)

Market risk (continued)

(c) Equity risk

Bank is exposed to the volatility in the prices of the securities held under equity portfolio. Equity investments held are for strategic/long term rather than for trading purposes and hence, Bank does not hold trading positions in equity investments. However, Bank's portfolio is marked to market on regular basis and the difference in the book value and market value are adjusted against investment revaluation reserve in shareholder's equity and for impaired investments to statement of income.

Further, Bank also conducts stress testing and sensitivity analysis to take an informed decision on equity risk exposure.

If equity price for listed shares had been 5% lower:

If there is adverse impact of 5% on equity portfolio, the value of the portfolio may decrease by RO 598,015 (2012: decrease by RO 418,413).

If equity price for unlisted shares had been 5% lower:

The financial statements include holdings in unlisted shares which are measured at fair value. Fair value is estimated using either Net Asset Value (NAV) provided by the fund managers or book value per share of the investee company. If the estimation were 5% higher / lower while all other variables were held constant, the carrying amount of the shares would decrease / increase by RO 133,710 (2012: decrease / increase by RO 146,280).

Operational risk

The Bank has adopted the Basic Indicator Approach under Basel II for the purpose of measuring capital charge for Operational Risk. The approach requires the Bank to provide 15% of the average three years gross annual income as capital charge for operational risk.

36. Capital management

The Bank manages its capital to ensure that it will be able to continue as a going concern while maximising the return to shareholders within acceptable risk return framework. The Bank's overall strategy remains unchanged from prior year.

The capital base of the Bank consists of debt, which includes borrowings disclosed in note 17, and equity attributable to shareholders of the Bank comprising issued share capital, share premium, reserves and retained earnings as disclosed in notes 18 to 21.

Notes to the Financial Statements
for the year ended 31 December 2013

36. Capital management (continued)

Capital adequacy

The ratio of equity to risk weighted assets, as formulated by the Basel II and Basel III, for the year ended 31 December 2013 is 14.09 % (2012: 14.96%).

Capital structure	2013 RO'000	2012 RO'000
Common Equity Tier (CET) I/ TIER I CAPITAL		
Paid up capital	**121,013**	110,012
Legal reserve	**31,492**	25,652
Share premium	**40,018**	40,018
Special reserve	**18,488**	-
Subordinated loan reserve	**26,250**	11,250
Retained earnings	**34,339**	45,513
Proposed bonus shares	**13,311**	11,001
CET I/Tier I Capital	**284,911**	243,446
Additional Tier I regulatory adjustments:		
Goodwill	**(2,780)**	(3,177)
Negative investment revaluation reserve	**(28)**	(124)
Total CET I/ Tier I capital	**282,103**	240,145
TIER II CAPITAL		
Investment revaluation reserve	**802**	756
General provision	**27,250**	24,447
Subordinated loan	**48,750**	63,750
Total Tier II capital	**76,802**	88,953
Total eligible capital	**358,905**	329,098
Risk weighted assets		
Banking book	**2,324,129**	2,005,481
Trading book	**56,798**	37,853
Operational risk	**166,581**	156,465
Total	**2,547,508**	2,199,799
CET I/ Tier I capital	**282,103**	240,145
Tier II capital	**76,802**	88,953
Tier III capital	**-**	-
Total regulatory capital	**358,905**	329,098
CET I/ Tier I capital ratio	**11.07%**	10.92%
Total capital ratio	**14.09%**	14.96%

Notes to the Financial Statements
for the year ended 31 December 2013

37. Segmental information

The Bank is organised into three main business segments:

1) Retail banking – incorporating, private customer current accounts, savings, deposits, investment savings products, custody, credit and debit cards, consumer loans and mortgages;

2) Corporate banking – incorporating direct debit facilities, current accounts, deposits, overdrafts, loan and other credit facilities, foreign currency and derivative products; and

3) Treasury and investments

Other operations comprise investment management and institutional finance neither of which constitutes a separately reportable segment.

Transactions between the business segments are on normal commercial terms and conditions. Funds are ordinarily allocated between segments, resulting in funding cost transfers disclosed in operating income. Interest charged for these funds is based on the Bank's cost of capital. There are no other material items of income or expense between the business segments.

Segment assets and liabilities comprise operating assets and liabilities, being the majority of the statement of financial position, but exclude items such as taxation and borrowings.

Internal charges and transfer pricing adjustments have been reflected in the performance of each business. Revenue sharing agreements are used to allocate external customer revenues to a business segment on a reasonable basis.

At 31 December 2013	Retail banking	Corporate banking	Treasury and investments	Total
	RO'000	RO'000	RO'000	RO'000
Segment operating revenues	57,808	40,161	2,256	100,225
Other revenues	9,428	5,512	8,104	23,044
Segment operating revenues	67,236	45,673	10,360	123,269
Interest expenses	(12,315)	(15,361)	(6,035)	(33,711)
Net operating income	54,921	30,312	4,325	89,558
Segment cost				
Operating expenses including depreciation	(24,479)	(15,527)	(5,310)	(45,316)
Impairment for loans and investment net recoveries from allowance for loans impairment	(1,823)	(2,044)	(367)	(4,234)
Legal case written back	10,355	13,264	2,510	26,129
Profit from operations after provision	38,974	26,005	1,158	66,137
Tax expenses	(4,556)	(3,039)	(135)	(7,730)
Net profit for the year	34,418	22,966	1,023	58,407
Segment assets	947,588	1,246,011	492,766	2,686,365
Less: Impairment allowance	(36,039)	(44,580)	(367)	(80,986)
Total segment assets	911,549	1,201,431	492,399	2,605,379
Segment liabilities	488,143	1,632,295	181,334	2,301,772

Notes to the Financial Statements
for the year ended 31 December 2013

37. Segmental information (continued)

Included in the above segment information the results of Islamic Banking Window as below:

At 31 December 2013	Retail banking RO'000	Corporate banking RO'000	Treasury and investments RO'000	Total RO'000
Segment operating revenues	98	56	34	188
Other revenues	18	74	88	180
Segment operating revenues	116	130	122	368
Unrestricted investment account holders' share of profit	(4)	-	(11)	(15)
Net operating income	112	130	111	353
Segment cost				
Operating expenses including depreciation	(804)	(461)	(1,005)	(2,270)
Impairment allowance	(185)	(100)	-	(285)
Net loss for the year	(877)	(431)	(894)	(2,202)
Segment assets	18,302	10,711	21,292	50,306
Less: Impairment allowance	(185)	(100)	-	(285)
Total segment assets	18,117	10,611	21,292	50,020
Segment liabilities	5,058	1,095	7,782	13,935

Notes to the Financial Statements
for the year ended 31 December 2013

37. Segmental information (continued)

At 31 December 2012	Retail banking RO'000	Corporate banking RO'000	Treasury and investments RO'000	Total RO'000
Segment operating revenues	56,889	36,216	596	93,701
Other revenues	11,020	3,817	4,887	19,724
Segment operating revenues	67,909	40,033	5,483	113,425
Interest expenses	(10,721)	(13,327)	(5,284)	(29,332)
Net operating income	57,188	26,706	199	84,093
Segment cost				
Operating expenses including depreciation	(20,375)	(12,966)	(3,706)	(37,047)
Impairment for loans and investment net recoveries from allowance for loans impairment	(4,967)	1,108	(287)	(4,146)
Profit from operations after provision	31,846	14,848	(3,794)	42,900
Tax expenses	(2,330)	(2,825)	-	(5,155)
Net profit (loss) for the year	29,516	12,023	(3,794)	37,745
Segment assets	860,402	1,079,524	279,384	2,219,310
Less: Impairment allowance	(32,820)	(42,660)	-	(75,480)
Total Segment assets	827,582	1,036,864	279,384	2,143,830
Segment liabilities	411,334	1,307,317	163,675	1,882,326

38. Proposed dividend

The Board of Directors in their meeting held on 29 January 2014 proposed a cash dividend of 14% (2012: 15%) for the year ended 31 December 2013 amounting to RO 16.94 million (2012: RO 16.50 million) and a bonus share issue of 11% (2012: 10%) amounting to 133,114,093 shares (2012: 110,011,647 shares) of RO 0.100 each. A resolution to approve these dividends and the increase in share capital will be presented to the shareholders at the annual general meeting.

During the year, unclaimed dividend amounting to RO 29,171 (2012: RO 1,290) was transferred to the Investor's Trust Fund account as per the guidelines issued by the Capital Market Authority of Oman.

39. Comparative figures

Certain amounts of the prior year financial statement have been reclassified to conform with the current year's presentation except Note 36.

Maisarah Islamic Banking Services

ميسرة
MAISARAH
للخدمات المصرفية الإسلامية
Islamic Banking Services

Annual Report 2013

TABLE OF CONTENTS

Annual Report of Shari'a Supervisory Board

31st December 2013

To: General Assembly and Board of Directors of Maisarah Islamic Banking Services - Bank Dhofar

Assalam Alaikum Wa Rahrmat Allah Wa Barakatuh

All perfect praise be to Allah; and may Allah send blessing and peace upon the noblest of Messengers, our Prophet Muhammad, sallallah. u. 'alayhi wasallam, his family and Companions

In compliance with the Shari'a Supervisory Board charter, we submit the following report for the year ended on 31/12/2013:

We have reviewed the principles and the contracts relating to the transactions and applications introduced by Maisarah Islamic Banking Services (MIBS) during the period ended on 31/12/2013. We have also conducted our review to form an opinion as to whether the MIBS has complied with Shari'a principles and also with the specific Fatawa, rulings and guidelines issued by us.

Maisarah's management is responsible for ensuring that the Maisarah conducts its business in accordance with Shari'a principles. It is our responsibility to form an independent opinion, based on our review of the operations of Maisarah, and report to you.

We conducted our review which included examining, on a test basis, of each type of transaction, the relevant documentation and procedure adopted by Maisarah.
We planned and performed our review so as to obtain all the information and explanations which we consider necessary in order to provide us with sufficient evidence to give reasonable assurance that the Maisarah has not violated Shari'a principles; In our opinion:

a) The contracts, transactions and dealings entered into by the Maisarah during the year ended 2013 that we have reviewed are in compliance with Shari'a principles;
b) The allocation of profits and charging of losses relating to investment accounts conform to the basis that had been approved by us in accordance with Shari'a principles;

We have identified the following areas where we believe there is room for further improvement by the management of Maisarah in order to follow truly the letter and spirit of the Shari'a and to enhance the public's confidence in Islamic banking in general and the Maisarah in particular:

a) MIBS needs to continue focus on the training through tailor made programs and practical workshops.
b) Public awareness programs and seminars should be conducted to create awareness of Islamic banking
c) As MIBS operations are expected to increase in 2014, therefore, management should further focus on ensuring highest standard of Shari'a compliance and cooperation with the Shari'a Compliance and Audit Department.

We beg Allah the almighty to grant us all the success and straight-forwardness.
Wassalam Alikum Wa Rahmat Allah Wa Barakatuh

Signatures:-

Sheikh Dr. Salim Bin Ali Bin Ahmed Al Dhahab – Chairman

Sheikh Dr. Mohammed Bin Ali Bin Mahmoud Al Lawati - Member

Sheikh Ahmed Bin Awadh Bin Abdul-Rahman Al – Hassaan - Member

Sheikh Dr. Abdullah Bin Mubarak Al Abri – Member

Sheikh Dr. Mohammad Ameen Ali Qattan - Member

Shari'a Supervisory Board Members

1

Name of Chairman:
Sheikh Dr. Salim bin Ali bin Ahmed Al Dhahab

Basis of Membership:
Chairman of Shari'a Supervisory Board

No. of other Directorships held: None

2

Name of Member:
Sheikh Ahmed bin Awadh bin Abdul-Rahman Al-Hassaan

Basis of Membership:
Member

No. of other Directorships held: None

3

Name of Member:
Sheikh Dr. Mohammed bin Ali bin Mohmoud Al Lawati

Basis of Membership:
Member

No. of other Directorships held: None

4

Name of Member:
Sheikh Dr. Abdullah bin Mubarak Al Abri

Basis of Membership:
Member

No. of other Directorships held: None

5

Name of Member:
Sheikh Dr. Mohammad Ameen Ali Qattan

Basis of Membership:
Member

No. of other Directorships held: None

Management Team

Sohail Niazi
Chief Islamic Banking Officer

Faisal Ali Abdullah Al Tamimi
Head of Corporate

Ismail Jama Ismail Bait Isihaq
Financial Controller

Yousuf Mohammed Suleiman Al Balushi
Head of Treasury

Jamsheed Hamza
Head of Retail

Syed Muzaffar Alam
Head of Operations

Muhammed Abdullah Dewaya
Head of Sharia Compliance & Audit

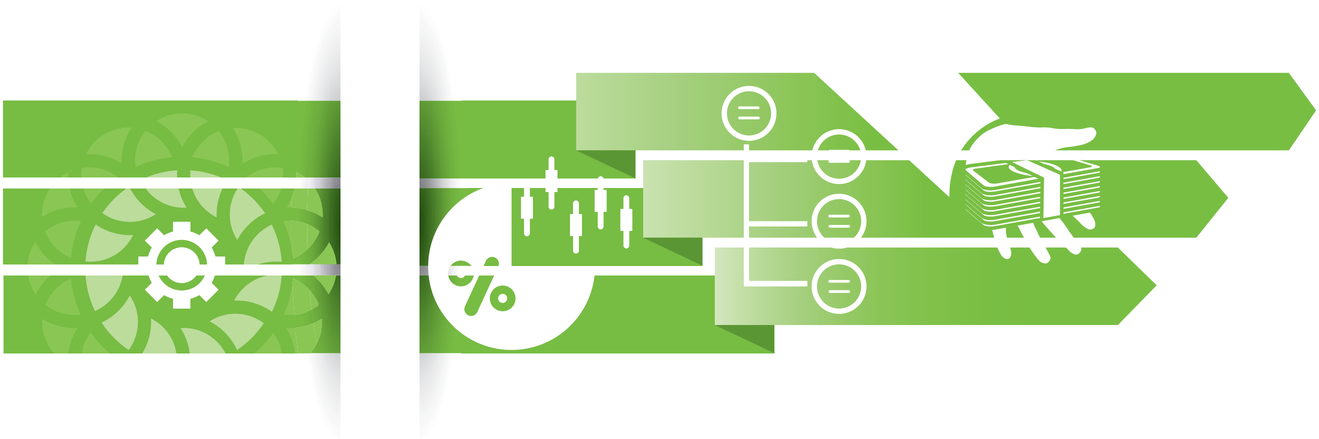
Management discussion and analysis report for the year ended 31st December 2013

Pursuant to the Royal Decree on Islamic Banking and with compliance of Islamic Banking Regulatory Framework which is issued by the Central Bank of Oman (CBO), BankDhofar SAOG introduced Islamic Banking for its customers and people of Oman in 2013. With the active role and full support of management, Board and shareholders, Maisarah Islamic Banking Services (MIBS) was launched as a window of BankDhofar in accordance with the guidance provided in Islamic Banking Regulatory Framework (IBRF) issued by CBO in March 2013. MIBS started its official operations from the month of March 2013 with two 2 branches; first one in Azaiba - Muscat region and the other in Salalah - Dhofar region.

Under the concept of 'Bank within a Bank', a completely segregated unit was set up with Corporate, Retail, Treasury, Products, Operations and Shari'a departments to operate the Islamic Banking Window. A strong team with knowledge and experience was brought on board, which helped to drive the business and achieve the targets set for the year. MIBS started its operation with an initial core capital of OMR 10 Million. However, based on business and regulatory requirements, the Board of Directors approved an increase in capital to reach RO 12.5 Million on 27th August 2013.

Retail Finance and Islamic Branch Network

Maisarah Retail business started operation in March 2013 with two branches. The Retail business was launched with two asset products – Home Finance and Auto Finance and three liability products – Current Account, Saving Account and Fixed Deposits. Reaching the target for twelve months was challenged due to the late commencement of operations. However, with a strong team and customer friendly branches, the team achieved the target earlier than planned. With the successful establishment of two branches in Azaiba and Salalah, Retail Department is rolling out the third branch in Sohar and plans to open additional branches in 2014 based on market conditions. With the established and newly planned branches, the retail business is expected to continue to grow while meeting all financing and liability targets.



Wholesale Banking Services

Maisarah Wholesale Banking business started operation in August 2013 with an aim to be the leader in Islamic financing solutions provider for Corporate, Mid Sector and Small & Medium Enterprises (SME) customers. Maisarah established an experienced team and has launched innovative wholesale banking products and services.

The Corporate environment in Oman is dramatically evolving and witnessing significant growth. Maisarah's Wholesale Banking objective is to provide Shari'a compliant financing solutions with a strong focus on customer needs driven by specialized industry insights, technological innovation and the highest commitment to service quality.

Although Maisarah Wholesale department was recently established, it has employed professionals with extensive Islamic Banking expertise and able to introduce products that meet the requirements of its customers. It offers a comprehensive suite of products and services geared to meet the demand and challenges of the corporate sector.
Its areas of expertise and focus include:

- **Understanding customer's businesses to fulfill their business needs.**
- **In-depth knowledge of varied industry sectors in Oman.**
- **Innovative solutions covering corporate finance, real-estate, investment banking, project finance, trade and commodity finance, capital and debt market products, treasury products and international banking services.**

Also, Maisarah's business relationships go beyond merely offering products.
At Maisarah Wholesale Banking, the vision is to partner with the customers to help identify areas for growth and efficiency while suggesting practical, cost-effective ways to take advantage of the opportunities that arise.

Treasury Management and Services

Maisarah Treasury has a distinct role to ensure that MIBS funds and currency positions are managed prudently by adhering to internal and regulatory limits throughout its business operations with overall objective of achieving planned growth.

During the year Maisarah Treasury actively managed cash-flows related to Omani Riyal emanating out of branches and Islamic Trade Finance operations. Initially in the year 2013 Maisarah's Treasury established Nostro relationships with correspondent banks in six major financial centers of the world. This will give the ability to branches to support the clients for outward and inward remittances, and assist Trade Finance business operations. The Treasury has also obtained sizeable funding limits and has signed bilateral Wakala agreements with the majority of local Islamic Banks and Windows. Maisarah's Treasury continues to explore opportunities to further extend this to cover overseas Islamic Banks in GCC and other financial centers in 2014.

Towards the end of 2013, treasury initiated a Maisarah specific liability product with two variations: Wakala (Ameen) Term Deposit and Wakala (Ameen) Investment Accounts. These products will be rolled out soon to help Maisarah grow the business by fulfilling customers' needs.

Recently, Maisarah Treasury has taken a leading role by investing in the first Corporate Sukuk issued in Oman in October, 2013. With an array of planned offerings of Liability, Forex products for domestic corporate and interbank clients, expansion of Nostro agents and additional bilateral Wakala agreements with local and overseas Islamic Banks, Maisarah Treasury will play an important role in accomplishing the planned growth of MIBS in the year 2014.

Product Development

One of the major initiatives of MIBS was the establishment of product development capacity within Maisarah to fulfill business and customers' requirements. With innovative and professional approach and working with leading sharia compliant product development consultants, the Product Development team rolled out various products and services during the year. The team continues to work on many innovative wholesale, retail and treasury products to ensure that Maisarah is leading Islamic banking solutions and services provider in Oman.

Shari'a Supervisory Board

Shari'a Supervisory Board (SSB) with an aim of creating a Sharia Compliant window that upholds the highest Sharia standards held twelve meetings during the year. Under the Chairmanship of Sheikh Dr. Salim Bin Ali Bin Ahmed Al Dhahab, and membership of Sheikh Dr. Mohammed bin Ali bin Mahmoud Al Lawati, Sheikh Ahmed bin Awadh bin Abdul-Rahman Al-Hassaan, Sheikh Dr. Abdullah bin Mubarak Al Abri, Sheikh Dr. Mohammad Ameen Ali Qattan, the SSB reviewed and approved all products and services that were launched by MIBS. The SSB fulfilled its responsibility of playing an important role of Sharia governance in line with CBO Islamic Banking Regulatory Framework (IBRF) and industry best practice with the help of Sharia Compliance and Audit Department.

Sharia Compliance and Audit Department

In order to ensure that all the business operations conducted by Maisarah are in-line with the Sharia principles a full-fledged Sharia Compliance and Audit department is working under the supervision of Sharia Supervisory Board (SSB). The department is headed by a qualified and experienced Sharia scholar assisted by a team of Sharia compliance and Audit officers. During Maisarah's initial establishment period which ended by December 2013, twelve meetings of SSB, including one meeting held in 2012, were conducted to review and approve new products, policies, procedures, manuals, documents and other business issues.

To implement Sharia controls and ensure highest standards of Sharia compliance, Sharia department has made it mandatory that before the execution, the complete transaction structures must be presented to Sharia department for its review and approval. This practice helps in identifying the potential risk of Sharia non-compliance in the transaction before its execution.

As 2013 was the first year of MIBS, Sharia audit department performed immediate Sharia Audit of the transactions covering all business segments and provided recommendations to highest standards of sharia practices.

As per CBO guidelines , Maisarah has entered into an engagement with an External Sharia Auditor who conducted a third party independent external Sharia audit. This has further increase the credibility of the internal Sharia audit and public confidence in Maisarah.
With the objective to increase proficiency of the staff in Islamic banking, Sharia department has conducted numerous training sessions covering different products and Islamic banking details.

In 2014, Maisarah business operations is expected to increase with launch of new innovative products and services, the Sharia department will continue to be highly involved in ensuring that products and services offered to valued customers must meet highest standards of Sharia compliance.

Maisarah Operations & Support Team (MOST)

Undertakes back-end processes of Maisarah Islamic Banking Services functions. Some of the functions processed by MOST include Payroll, Inward Clearing, Bulk Transfer Cheques, Inward Remittances, Collection of Foreign Currency Cheques, Payments through RTGS/ACH and Review of monthly Balancing Certificates. As a part of Bank's strategy, MOST plays a major role in expanding its scope of work by centralising more activities pertaining to Operations, thus relieving the business units from backend functions and thereby achieving process-optimisation and cost-reduction. MOST also continuously works on streamlining and re-engineering the process thus minimizing operational process and errors. Working closely to ensure operations of the division are smooth and seamless, MOST is the link between MIBS and the support services in parent bank working under Service Level Agreements (SLAs) with the departments of BankDhofar namely Central Operations, Card Centre, Credit Administration, Logistics, Premises & Procurement (LPP), Human Resources (HR), Recoveries, Credit Control, & ITD.

In addition to the above teams, MIBS support teams consisting of Finance, Credit Administration and Risk contribute to ensure that business functions in seamless and efficient manner. To build the foundation, during the year key areas of focus for the MIBS team were as follows:

- **Ensure that the business units are well established and functional.**
- **Ensure that correct accounting treatment is followed as per AAOIFI and IBRF guidelines for all the products launched by MIBS.**
- **Achieve the budgeted numbers for the year.**
- **Ensure a strong team is recruited and deployed.**
- **Ensure the team members are trained and provided with up to date knowledge on Islamic banking.**
- **Ensure accurate and timely reporting to Management and Regulatory authorities.**
- **Establish the most preferred Islamic Banking service provider in Oman.**

Working in line with the above mission, Maisarah was recognized and awarded as the Best Islamic Window in Oman for the year 2013 by Global Financial Markets. The recognition was also received from customers, who expressed their satisfaction for the services provided by Maisarah.

MIBS, foresee the challenge of 2014 as a year of more competition among the Islamic Banking entities. The 2013 saw establishment of two Islamic banks and six windows. Most of the competitors were focused on developing the infrastructure. However, in 2014 the competition will heat up as all Islamic Banking entities will work hard to gain the market share. Keeping this in view and to exceed shareholders' expectation, in 2014, MIBS will be focusing on two major areas – Operational Excellence and Financial Performance to achieve its growth plans. The strategy and plan will be revolving around these two key objectives.

Financial Performance

Maisarah Islamic Banking started its operations with effect from 3 March 2013 and has successfully achieved total asset of OMR 50 Million, including net financing of OMR 27.9 Million and Sukuk investment of OMR 10 Million at end of year 2013.

Further, the customer deposit has reached to OMR 3.6 Million at the end of year 2013.
An analysis of our Financing portfolio as at December 31, 2013 is as follows:

Particulars	OMR in Million
Murabaha receivables	0.2
Diminishing Musharaka financing	10.4
Ijarah Muntahia Bittamleek	17.6
Gross Financing to customers	28.2
Less: Allowance for impairment	(0.3)
Net Financing	**27.9**

No non – performing financing were reported till the year end December 2013.

The composition of customer deposits at the end of 2013 is as follows:

Particulars	OMR in Million
Current accounts	2.5
Saving accounts	1.1
Term deposits	0.02
Total customer deposits	**3.62**

Assigned capital

Maisarah Islamic Banking Services has been assigned a capital of OMR 12.5 Million.

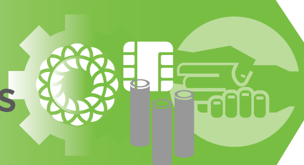
Income Statement

Particulars	OMR in Million
Net profit income	0.26
Fees, commissions & other income	0.09
Operating Income	0.35
Total operating costs	(2.27)
Net Operating Loss	**(1.92)**
Net loss	**(2.20)**

During the period Maisarah has earned a total profit income of OMR 0.275 Million from Murabaha, Ijarah Muntahia Bittamleek, Diminishing Musharaka, Wakala placement and financial asset at fair value through equity. However, the profit expense of OMR 0.015 Million was incurred on Savings account, Term deposit account and Wakala Inter Bank deposits.

The net loss of OMR 2.20 Million for the period was nearly in line with the plan. It includes mainly pre- operating cost of OMR 0.496 Million attributed to staring of business in addition to general and administrative cost of OMR 1.77 Million during the commencement period. Further, an amount of OMR 0.285 Million was provided during the period as a general provision which has also been included in the net loss.

Future Prospects



Maisarah Islamic Banking Services has carefully planned many new products, initiatives, services, technologies and processes in 2014 to delight its customers, fully engage and develop its people and reward its shareholders

It is very well placed to show robust growth in the future and contribute to economic development of the Sultanate of Oman by fulfilling the financial needs of its customers.

Financial statements for the year ended 31st December 2013

KPMG
4th Floor, HSBC Bank Building
MBD
P.O. Box 641
P.C. 112
Sultanate of Oman

Tel 968 24709181
Fax 968 24700839

INDEPENDENT AUDITORS' REPORT TO THE SHAREHOLDERS OF MAISARAH ISLAMIC BANKING SERVICES – WINDOW OF BANK DHOFAR SAOG

Report on the financial statements

We have audited the financial statements of Maisarah Islamic Banking Services– Window of Bank Dhofar SAOG ("the Bank"), set out on pages 176 to 198 which comprise the statement of financial position as at 31 December 2013, and the income statement, statement of changes in owners' equity and statement of cash flows for the period from 3 March 2013 to 31 December 2013, and notes, comprising a summary of significant accounting policies and other explanatory information.

Management's responsibility

Management is responsible for the preparation and fair presentation of these financial statements in accordance with the Financial Accounting Standards ("FAS") issued by the Accounting and Auditing Organization for Financial Institutions ("AAOIFI") and the Shari'a rules and principles determined by the Shari'a Supervisory Board of the Bank 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.

Auditors' responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with Auditing Standards for Islamic Financial Institutions issued by AAOIFI. Those standards require that we comply with relevant ethical requirements and plan and perform the audit to obtain reasonable assurance about 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 our 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, we consider internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

Opinion

In our opinion, the financial statements present fairly, in all material respects, the financial position of the Bank as at 31 December 2013 and its financial performance and its cash flows for the period then ended in accordance with the FAS issued by AAOIFI and the Shari'a rules and principles as determined by the Shari'a Supervisory Board of the Bank.

29 January 2014

Khalid Masud Ansari

C.R. No. 1/20036/6

Statement of Financial Position

As on 31 December 2013

2013 USD		Note	2013 RO
	Assets		
7,867,036	Cash and balances with Central Bank of Oman	5	3,028,809
20,000,000	Due from banks and financial institutions	6	7,700,000
602,140	Murabaha receivables – net	7	231,824
26,817,626	Diminishing Musharaka financing	8	10,324,786
25,974,026	Financial assets at fair value through equity	9	10,000,000
45,262,314	Ijarah Muntahia Bittamleek – net	10	17,425,991
746,449	Property and equipment – net	11	287,383
2,053,063	Intangible asset – net	12	790,429
597,652	Other assets	13	230,096
129,920,306	**Total assets**		**50,019,318**
	Liabilities, equity of unrestricted investment account holders and owners' equity		
	Liabilities		
78,441,558	Due to Head office and other banks	14	30,200,000
8,537,761	Qard Hasan from Head office	15	3,287,038
6,602,979	Current accounts		2,542,147
6,642,522	Other liabilities	16	2,557,371
100,224,820	**Total liabilities**		**38,586,556**
2,948,429	**Equity of unrestricted investment account holders**	17	**1,135,145**
	Owners' equity		
32,467,532	Capital	18	12,500,000
(5,720,475)	Accumulated losses		(2,202,383)
26,747,057	**Total owners' equity**		10,297,617
129,920,306	**Total liabilities, equity of unrestricted investment account holders and owners' equity**		**50,019,318**
7,766,000	**Contingent liabilities**	29	**2,989,910**

The financial statements were approved by the Board of Directors on 29 January 2014 and signed on its behalf by:

Chairman

Chief Islamic Banking Officer

The notes on pages 180 to 198 form an integral part of these financial statements.
The independent auditor's report is set forth on page 175

Income Statement

For the period from 3 March 2013 to 31 December 2013

USD		Note	RO
	Income		
14,735	Murabaha	20	5,673
238,738	Ijarah Muntahia Bittamleek	21	91,914
145,197	Diminishing Musharaka	22	55,901
89,457	Wakala placement	23	34,441
227,273	Profit on financial assets at fair value through equity	24	87,500
715,400			275,429
	Less:		
(11,922)	Return on unrestricted investment account holders		(4,590)
(27,634)	Return on interbank Wakala deposit		(10,639)
(39,556)			(15,229)
675,844	**Maisarah's share in income from investment as a Mudarib and Rabul Maal**		260,200
241,135	Revenue from banking services		92,837
691	Foreign exchange gain – net		266
917,670	**Total revenue**		353,303
(1,287,057)	Pre-operating expenses	25	(495,517)
(2,748,395)	Staff costs	26	(1,058,132)
(1,553,036)	General and administrative expenses	27	(597,919)
(740,932)	Impairment allowance	7,8&10	(285,259)
(308,725)	Depreciation and amortization	11&12	(118,859)
(6,638,145)	**Total expenses**		(2,555,686)
(5,720,475)	**Net loss for the period**		(2,202,383)

The notes on pages 180 to 198 form an integral part of these financial statements.
The independent auditor's report is set forth on page 175

Statement of changes in owners' equity

for the period from 3 March 2013 to 31 December 2013

	Capital	Accumulated losses	Total
	RO	RO	RO
Capital	12,500,000	-	12,500,000
Net loss for the period	-	(2,202,383)	(2,202,383)
Balance as at 31 December 2013	**12,500,000**	**(2,202,383)**	**10,297,617**

	Capital	Accumulated losses	Total
	USD	USD	USD
Capital	32,467,532	-	32,467,532
Net loss for the period	-	(5,720,475)	(5,720,475)
Balance as at 31 December 2013	**32,467,532**	**(5,720,475)**	**26,747,057**

The notes on pages 180 to 198 form an integral part of these financial statements.
The independent auditor's report is set forth on page 175

Statement of cash flows

For the period from 3 March 2013 to 31 December 2013

2013 USD		2013 RO
	Cash flows from operating activities	
(5,720,475)	Net loss for the period	(2,202,383)
	Adjustments for:	
308,725	Depreciation and amortization	118,859
868,774	Depreciation on Ijarah assets	334,478
740,932	Impairment allowance	285,259
36	Investment risk reserve	14
117	Profit equalization reserve	45
(3,801,891)	**Cash flows used in operating activities before changes in operating assets and liabilities**	(1,463,728)
	Operating assets and liabilities:	
(616,348)	Murabaha receivables	(237,294)
(46,751,060)	Ijarah Muntahia Bittamleek assets	(17,999,158)
154,106	Proceeds from sale in Ijarah Muntahia Bittamleek assets	59,331
(27,078,486)	Diminishing Musharaka financing	(10,425,217)
(398,805)	Other asset	(153,540)
6,642,522	Other liabilities	2,557,371
5,230,678	Qard Hasan from Head Office	2,013,811
(66,619,284)	**Net cash used in operating activities**	(25,648,424)
	Cash flows from investing activities	
(25,974,026)	Purchase of financial asset at fair value through equity	(10,000,000)
(25,974,026)	**Net cash used in investing activities**	(10,000,000)
	Cash flows from financing activities	
6,602,979	Current account	2,542,147
2,948,277	Unrestricted investment account holders	1,135,086
32,467,532	Capital	12,500,000
42,018,788	**Net cash from financing activities**	16,177,233
(50,574,522)	**Cash and cash equivalents at the end of the period**	(19,471,191)
	Cash and cash equivalents at the end of the period comprise:	
7,867,036	Cash and balances with CBO	3,028,809
20,000,000	Due from banks and financial institutions	7,700,000
(78,441,558)	Due to Head office and other banks	(30,200,000)
(50,574,522)		(19,471,191)

The notes on pages 180 to 198 form an integral part of these financial statements.
The independent auditor's report is set forth on page 175

Notes to the financial statements
For the period from 3 March 2013 to 31 December 2013

1 LEGAL STATUS AND PRINCIPAL ACTIVITIES

Maisarah Islamic Banking Services ("Maisarah") was established in Sultanate of Oman as window of Bank Dhofar SAOG. Maisarah's operations commenced on 3 March 2013 and it currently operates through 2 branches in the Sultanate under the license issued by the Central Bank of Oman on 27 February 2013.

The principle activities of Maisarah is taking demand, saving and deposit accounts, providing Murabaha finance, Ijarah financing and other Shari'a compliant forms of financing as well as managing investor's money on the basis of Mudaraba or agency for a fee, providing commercial banking services and other investment activities.

Maisarah's activities are regulated by the Central Bank of Oman ("CBO") and supervised by Shari'a Supervisory Board ("SSB") comprising of five members.

2 BASIS OF PREPARATION

2.1 Statement of compliance

The financial statements of Maisarah Islamic Banking Services are prepared in accordance with the Financial Accounting Standards ("FAS") issued by the Accounting and Auditing Organization for Islamic Financial Institutions ("AAOIFI"), the Shari'a rules and principles as determined by the SSB of Maisarah and the applicable laws and regulations issued by the CBO.

Maisarah complies with the requirements of AAOIFI, for matters for which no AAOIFI standards exist, Maisarah uses the relevant International Financial Reporting Standards ("IFRS") or International Accounting Standards ("IAS") as issued by International Accounting Standards Board ("IASB").

Statement of changes in restricted investment amount, statement of sources of funds in zakah and charity and statement of sources and uses of funds in Qard Fund have not been presented as these are not applicable / relevant to Maisarah's operations.

2.2 Basis of measurement

The financial statements are prepared on a historical cost basis, except for certain investments carried at fair value.

2.3 Functional and presentation currency

Items included in Maisarah's financial statements are measured using Rials Omani ("RO") which is the currency of the primary economic environment in which Maisarah operates, rounded off to the nearest Rial Omani.

2.4 Use of estimates and judgements

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

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the period in which the estimate is revised and in any future periods affected.

Information about significant areas of uncertainty and critical judgements in applying accounting policies that have the most significant effect on the amounts recognized in the financial statements are described in note 4.

Notes to the financial statements
For the period from 3 March 2013 to 31 December 2013

3 SIGNIFICANT ACCOUNTING POLICIES

The accounting policies set below have been consistently applied in dealing with items that are considered material in relation to Maisarah's financial statements to the period presented.

3.1 Foreign currency translations

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at period-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised in income statement.

3.2 Investments

Equity and debt type instruments at fair value through equity
This includes all equity and debt type instruments that are not fair valued through income statement. Subsequent to acquisition, investments designated at fair value through equity are re-measured at fair value with unrealised gains or losses recognised proportionately in owners' equity and equity of unrestricted investment account holders until the investment is derecognised or determined to be impaired at which time the cumulative gain or loss previously recorded in owners' equity or equity of investment accountholders is recognised in income statement.

3.3 Derecognition of financial assets and liabilities

A financial asset (or, where applicable a part of a financial asset or part of a group of similar assets) is derecognized when:
(i) the right to receive cash flows from the asset has expired;
(ii) Maisarah has transferred its rights to receive cash flows from the asset and either (a) has transferred substantially all the risks and rewards of the asset, or (b) has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset.

A financial liability is derecognized when the obligation specified in the contract is discharged, cancelled or expired.

3.4 Fair value measurement principles

The fair values of quoted investments in active markets are based on current bid prices. If the market for a financial asset is not active (and for unlisted securities), Maisarah establishes fair value by using valuation techniques. These include the use of recent arm's length transactions, discounted cash flow analysis and other valuation techniques commonly used by market participants.

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

3.5 Cash and cash equivalents

For the purpose of the cash flow statement, cash and cash equivalents comprise balances with less than three months' maturity from the date of acquisition, including: cash on hand, non-restricted cash deposited with the Central Bank of Oman, amounts due to / from other banks.

3.6 Offsetting

Financial assets and liabilities are offset and the net amount is reported in the statement of financial position when there is a legally enforceable right to set off the recognised amounts and there is an intention to settle on a net basis, or realise the asset and settle the liability simultaneously in accordance with Shari'a principles and guidelines.

Income and expenses are presented on a net basis only for permitted transactions.

3.7 Murabaha receivables

Murabaha receivables are stated net of deferred profits and provisions for impairment.

3.8 Musharaka investments

Musharaka investments are stated at the fair value less provision for impairment.

3.9 Ijarah Muntahia Bittamleek assets

Ijarah Muntahia Bittamleek assets are initially recorded at cost. Ijarah Muntahia Bittamleek is a lease whereby the legal title of the leased asset passes to the lessee at the end of the Ijarah (lease term), provided that all Ijarah instalments are settled.

Depreciation is calculated using the straight-line method on all Ijarah Muntahia Bittamleek assets, at rates calculated to write off the cost of each asset over its useful life or period of the lease whichever is lower.

3.10 Property and equipment

Items of property and equipment are stated at cost less accumulated depreciation and impairment loss. Depreciation is calculated so as to write off the cost of property and equipment, other than freehold land and capital work-in-progress, by equal installments over their estimated economic useful lives from the date the asset is brought into use, as follows:

	Years
Furniture, fixtures and equipment	3 - 7
Motor vehicles	3 - 5
Computer equipment	4

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at each reporting date. An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount. The recoverable amount is the higher of the asset's fair value less costs to sell and value in use.

Gains and losses on disposal of property and equipment are determined by reference to their carrying amount and are taken into account in determining operating profit. Repairs and renewals are charged to income statement when the expense is incurred. Subsequent expenditure is capitalized only when it increases the future economic benefits embodied in the item of property and equipment. All other expenditure is recognized in income statement as an expense when incurred.

3.11 Intangibles

Intangible assets are classified according to their useful life for a specified or unspecified period of time. Intangible assets with definite useful life are amortized during that life, and amortization is recorded in income statement. Intangible assets with indefinite useful life, are reviewed at each reporting date and impairment, if any is recorded in income statement.

Intangible assets arising from Maisarah's operations are not capitalized and are charged to the income statement as incurred.

Any indications of impairment of intangible assets are reviewed at the reporting date; in addition, the useful lives of these assets are reviewed annually. If expected useful lives vary from the estimated ones the change in estimate is adjusted prospectively.

Notes to the financial statements
For the period from 3 March 2013 to 31 December 2013

3.12 Equity of unrestricted investment accountholders

All unrestricted investment accounts are carried at cost plus profit and related reserves less amounts settled. Unrestricted investment account holders' share of income is calculated based on the income generated from investment accounts after deducting Mudarib's share. Operating expenses are charged to shareholders' funds and not included in the calculation.
The basis applied by Maisarah in arriving at the unrestricted investment account holders' share of income is total income from jointly financed Islamic assets less shareholders' income. Pre-agreed profit share generated from unrestricted investment account holders is deducted as Mudarib' s share after deducting profit equalisation reserve and the remaining amount is distributed to the unrestricted investment account holders after deducting investment risk reserve.

3.13 Profit equalisation reserve

Maisarah appropriates certain amount in excess of the profit to be distributed to unrestricted investment accounts before taking into consideration the Mudarib share of income. This will be used to maintain a certain level of return on investment for unrestricted investment account holders.

3.14 Investment risk reserve

Investment risk reserves are amounts appropriated out of the income of unrestricted investment account holders, after allocating the Mudarib' s share, to cater against future losses for unrestricted investment account holders.

3.15 Provisions

A provision is recognised in the statement of financial position when Maisarah has a legal or constructive obligation as a result of a past event, and it is probable that an outflow of economic benefits will be required to settle the obligation and the amount has been reliably estimated.

3.16 Earnings prohibited by Shari'a

All the funds mobilized and income earned by Maisarah is from Islamic sources. Maisarah is committed to avoid recognizing any income generated from non-Islamic sources. Accordingly, all non-Islamic income is credited to a charity account where Maisarah uses these funds for social welfare activities. It includes but not limited to cases/ transactions classified by Shari'a as non-compliant income and approved by the SSB to be forfeited, interest paid by other banks on Nostro accounts, late payment fee received from the customer in financing and investment transaction.

3.17 Zakah

The responsibility of payment of zakah is on individual shareholders and investment account holders.

3.18 Joint and self-financed

Investments, financing and receivables that are jointly owned by Maisarah and the unrestricted investment accounts holders are classified under the caption "jointly financed" in the financial statements. Investments, financing and receivables that are financed solely by Maisarah are classified under "self-financed".

3.19 Funds for Maisarah

Maisarah functions with funds specifically available for Islamic Banking activities and there is no commingling of funds with conventional banking financial business.

3.20 Revenue recognition

3.20.1 Murabaha receivables

Where the income is quantifiable and contractually determined at the commencement of the contract, income is recognized on a time-apportioned basis over the period of the contract based on the principal amounts outstanding. Where the income from a contract is not quantifiable, it is recognized when realized. Income related to non-performing accounts is excluded from income statement.

3.20.2 Musharaka investments

Income is recognised when the right to receive payment is established or on distribution by the Musharik, whereas the losses are charged to income on their declaration by the Musharik. Income related to non-performing accounts is excluded from income statement.

3.20.3 Ijarah Muntahia Bittamleek

Income from Ijarah Muntahia Bittamleek assets is recognised on a time-apportioned basis over the lease term, net of depreciation. Income related to non-performing Ijarah Muntahia Bittamleek assets is excluded from income statement.

3.20.4 Dividends

Dividends are recognised when the right to receive payment is established.

3.20.5 Fee and Commission income

Fee and commission income is recognised when earned.

3.20.6 Maisarah's share as a Mudarib

Maisarah's share as a Mudarib for managing unrestricted investment accounts is accrued based on the terms and conditions of the related Mudaraba agreements.

3.20.7 Income allocation

Income from jointly financed activities is allocated proportionately between unrestricted investment accounts in accordance to their pre-agreed assigned weightages and shareholders on the basis of the average balances outstanding during the year.

3.21 Taxation

Maisarah is Islamic Banking Window of Bank Dhofar SAOG, hence it is not taxable on a stand-alone basis as per the prevailing tax laws. Accordingly, no current tax and deferred tax has been accounted for in these financial statements.

Bank Dhofar SAOG is taxable on combined results i.e. including Maisarah's financial results, accounted for as per IFRS.

3.22 Employee benefits

End of service benefits are accrued in accordance with the terms of employment of Maisarah's employees at the reporting date, having regard to the requirements of the Oman Labour Law. Employee entitlements to annual leave and leave passage are recognized when they accrue to employees and an accrual is made for the estimated liability arising as a result of services rendered by employees up to the reporting date.
Contributions to a defined contribution retirement plan and occupational hazard insurance for Omani employees in accordance with the Omani Social Insurances Law of 1991 and its subsequent amendments are recognized as an expense in income statement as incurred.

Notes to the financial statements

For the period from 3 March 2013 to 31 December 2013

3.23 Shari'a supervisory board

All business activities, products, transactions, agreements, contracts and other relevant documents are subject to the supervision of the Shari'a Supervisory Board of Maisarah, which meets quarterly and consists of five prominent Shari'a scholars appointed by the Shareholders for a period of three years, namely:

Sr. No.	Name	Title
1	Sheikh Dr. Salim Bin Ali Bin Ahmed Al Dhahab	Chairman
2	Sheikh Dr. Mohammed bin Ali bin Mahmoud Al Lawati	Member
3	Sheikh Ahmed bin Awadh bin Abdul-Rahman Al-Hassaan	Member
4	Sheikh Dr. Abdullah bin Mubarak Al Abri	Member
5	Sheikh Dr. Mohammad Ameen Ali Qattan	Member

3.24 Trade date accounting

All "regular way" purchases and sales of financial assets are recognized on the trade date, i.e. that date Maisarah commits to purchase or sell the assets. Regular way purchases or sales are purchases or sales of financial assets that require delivery of assets within the time frame generally established by regulations or convention in the market place.

3.25 Segment reporting

A segment is a distinguishable component of Maisarah that is engaged either in providing products or services (business segment), or in providing products or services within a particular economic environment (geographical segment), which is subject to risks and rewards that are different from those of other segments.

Maisarah currently operates only in the Sultanate of Oman. Maisarah's primary format for reporting segmental information is business segments, based upon management and internal reporting structure. Maisarah's main business segments are retail banking, corporate banking, treasury and investments.

3.26 Fiduciary assets

Assets held in trust or in a fiduciary capacity are not treated as assets of Maisarah in the statement of financial position.

4 Critical accounting judgment and key sources of estimation uncertainty

(a) Impairment

Management reviews its financing portfolio to assess impairment at each reporting date. In determining whether an impairment loss should be recorded in the income statement, management makes judgements as to whether there is any observable data indicating that there is a measurable decrease in the estimated future cash flows from a portfolio of finances before the decrease can be identified with an individual receivable in that portfolio. This evidence may include observable data indicating that there has been an adverse change in the payment status of customers in a group that correlates with defaults on assets in the group. Management uses estimates based on historical loss experience for assets with credit risk characteristics and objective evidence of impairment similar to those in the portfolio when scheduling its future cash flows. The methodology and assumptions used for estimating both the amount and timing of future cash flows are reviewed regularly to reduce any differences between loss estimates and actual loss experience.

(b) Useful life of property and equipment and Ijarah Muntahia Bittamleek

Depreciation is charged so as to write off the cost of assets over their estimated useful lives. The calculation of useful lives is based on management's assessment of various factors such as the operating cycles, the maintenance programs, and normal wear and tear using its best estimates.

Notes to the financial statements
For the period from 3 March 2013 to 31 December 2013

5 Cash and balances with Central Bank of Oman

	2013 RO
Cash in hand	269,584
Balances with Central Bank of Oman	2,759,225
	3,028,809

6 Due from banks and financial institutions

	Self-Financed RO	Jointly Financed RO	Total RO
Wakala placement	2,066,193	5,633,807	7,700,000

The Wakala placement represents investment of RO 7.7 Million (USD 20 Million).

7 Murabaha receivables -net

	Self- Financed RO	Jointly Financed RO	Total RO
Gross Murabaha receivables	73,394	200,120	273,514
Less: Unearned income	(9,719)	(26,501)	(36,220)
	63,675	173,619	237,294
Less: impairment allowance	(1,468)	(4,002)	(5,470)
	62,207	169,617	231,824

Murabaha receivables past due but not impaired with the period less than 30 days amount to RO 14,144

8 Diminishing Musharaka Financing

	Self -Financed RO	Jointly Financed RO	Total RO
Diminishing Musharaka	2,797,468	7,627,749	10,425,217
Less: impairment allowance	(26,949)	(73,482)	(100,431)
	2,770,519	7,554,267	10,324,786

Fair value of collaterals

Upon initial recognition of Diminishing Musharaka, the fair value of collateral is based on valuation techniques commonly used for the corresponding assets. In subsequent periods, the fair value is updated by reference to market price or indexes of similar assets.

9 Financial asset at fair value through equity

	Self-Financed RO	Jointly Financed RO	2013 Total RO
Local un-listed sukuk	2,683,370	7,316,630	10,000,000

Maisarah has invested RO 10 million in Ijarah Sukuk issued by Modern Sukuk SAOC. At 31 December 2013, the market value of the Sukuk approximates to the carrying value.

Notes to the financial statements
For the period from 3 March 2013 to 31 December 2013

10 Ijarah Muntahia Bittamleek – net

	Self-Financed RO	Jointly Financed RO	Total RO
Cost			
Additions	4,829,834	13,169,324	17,999,158
Disposals	(16,100)	(43,900)	(60,000)
At 31 December 2013	4,813,734	13,125,424	17,939,158
Accumulated depreciation			
Charge for the period	89,753	244,725	334,478
Disposals	(180)	(489)	(669)
At 31 December 2013	89,573	244,236	333,809
Net book value at 31 December	4,724,161	12,881,188	17,605,349
Less: impairment allowance	(48,128)	(131,230)	(179,358)
Net Ijarah Muntahia Bittamleek	4,676,033	12,749,958	17,425,991

Ijarah Muntahia Bittamleek past due but not impaired is as follows:

Past due up to 30 days	673,526
Past due 30 – 60 days	25,195
Total	698,721

11 Property and equipment - net

	Furniture , fixtures & equipment RO	Motor vehicles RO	Computer equipment RO	Capital work in progress RO	Total RO
Cost					
Additions	191,935	18,100	117,787	15,311	343,133
At 31 December 2013	191,935	18,100	117,787	15,311	343,133
Accumulated depreciation					
Provided during the year	(28,927)	(4,199)	(22,624)	-	(55,750)
At 31 December 2013	(28,927)	(4,199)	(22,624)	-	(55,750)
Net book value at 31 December 2013	163,008	13,901	95,163	15,311	287,383

12 Intangible asset - net

	2013 RO
Computer software	853,538
Amortization	(63,109)
Net book value at 31 December 2013	790,429

13 Other assets

	2013 RO
Profit receivable	**133,702**
Prepaid expenses	**73,108**
Other	**23,286**
	230,096

14 Due to Head office and other banks

Due to Head office	**22,500,000**
Due to other banks	**7,700,000**
	30,200,000

Due to Head office and other banks comprises of Wakala deposits.

15 Qard Hasan from Head Office

Qard Hasan from Head Office	**3,287,038**

This amount represents profit-free Qard Hasan facility from Head Office.

16 Other liabilities

Payables	**2,361,438**
Profit payable	**9,093**
Accrued expenses	**186,840**
	2,557,371

17 Equity of unrestricted investment accountholders

Savings account	**1,117,586**
Term deposit	**17,500**
Profit equalization reserve	**45**
Investment risk reserve	**14**
	1,135,145

There is no restricted investment at reporting date.
Basis of distribution of the profit between owners' equity and unrestricted investment accountholders
The investment profits are distributed between owners' equity and unrestricted investment account holders for the period ended 31 December 2013 as follows:

	Percentage
Unrestricted investment account holders' share	60%
Mudarib' s share	40%

The investment risk reserve is deducted from investment account holders share after allocating the Mudarib' s share of profit as per the approved policy in order to cater against future losses of equity of unrestricted investment account holders. Investment risk reserve will revert to the investment account holders as per terms and conditions of Mudaraba contract.

Notes to the financial statements

For the period from 3 March 2013 to 31 December 2013

17 Equity of unrestricted investment accountholders (continued)

The profit equalization reserve is the amount Maisarah appropriates in excess of the profit to be distributed to equity of unrestricted account holders before allocating the Mudarib share of income to maintain a certain level of return. Profit equalization reserve will revert to owner's equity and unrestricted investment accountholders as per terms and condition of Mudaraba contract.

Unrestricted investment account holders funds are commingled with Maisarah's funds for investment, no priority is granted to any party for the purpose of investments and distribution of profits. The administration expenses are only charged on the Maisarah expenses.

18 Capital

The Head office has assigned a capital of RO 12.5 million to Maisarah from the core paid up capital of the shareholders.

19 Fiduciary assets

At 31 December 2013, there were no funds under management with Maisarah.

20 Murabaha income

			2013
	Self-Financed RO	Jointly Financed RO	Total RO
Murabaha income	1,522	4,151	5,673

21 Ijarah Muntahia Bittamleek income

	Self-Financed RO	Jointly Financed RO	Total RO
Income from Ijarah Muntahia Bittamleek	114,417	311,975	426,392
Less: Depreciation	(89,753)	(244,725)	(334,478)
	24,664	67,250	91,914

22 Diminishing Musharaka income

	Self-Financed RO	Jointly Financed RO	Total RO
Diminishing Musharaka income	15,000	40,901	55,901

23 Income on Wakala placement

	Self-Financed RO	Jointly Financed RO	Total RO
Income on Wakala placement	9,242	25,199	34,441

24 Profit on financial assets at fair value through equity

	Self-Financed RO	Jointly Financed RO	Total RO
Local un-listed sukuk	23,479	64,021	87,500

Notes to the financial statements
For the period from 3 March 2013 to 31 December 2013

25 Pre-operating expenses

	2013 RO
Staff cost	238,814
General administration cost	188,127
Others	68,576
	495,517

26 Staff costs

Salaries and allowances	981,984
Other personnel cost	73,535
Non-Omani employee terminal benefit	2,613
	1,058,132

27 General and administrative expenses

Occupancy cost	190,464
Operating and administration cost	407,455
	597,919

28 Related parties transactions

In the ordinary course of business, Maisarah conducts transactions with certain of its Directors, shareholders and companies over which they are able to exert significant influence. The aggregate amounts of balances with such related parties are as follows:
During the current year, there have been no financing, deposits and other facilities been provided by Maisarah to the Directors, Shari'a Supervisory Board and shareholders holding 10% or more.

Remuneration paid to Shari'a Supervisory Board	
Chairman	
- remuneration proposed	6,000
- sitting fees paid	4,800
Other members	
- remuneration proposed	12,000
- sitting fees paid	9,300
Other transactions	
Rental payment to a related party	69,120
Key management compensation	
Salaries and other benefits	139,944
End of service benefits	2,087

29 Contingent liabilities and commitments

(a) Credit related contingent items

Letters of credit and other commitments for which there are corresponding customer liabilities:

Letters of credit	2,989,910

(b) Capital and investment commitments

Contractual commitments for property and equipment	279,367

Notes to the financial statements
For the period from 3 March 2013 to 31 December 2013

30 Fair value information

Fair value is an amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction. Consequently, differences can arise between the carrying value and fair value estimates. As at the reporting date the fair values of Maisarah's financial instruments are not significantly different from their carrying values.

The following table provides an analysis of financial instruments that are measured subsequent to initial recognition at fair value, grouped into levels 1 to 3 based on the degree to which the fair value is observable:

- Level 1 fair value measurements are those derived from quoted prices (unadjusted) in active markets for identical assets or liabilities;
- Level 2 fair value measurements are those derived from inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices); and
- Level 3 fair value measurements are those derived from valuation techniques that include inputs for the asset or liability that are not based on observable market data (unobservable inputs).

At reporting date, Maisarah has investments in Sukuk, which are stated at cost.

31 Financial risk management

The important types of financial risks to which Maisarah is exposed are credit risk, liquidity risk and market risk. The risk management division of Maisarah is an independent and dedicated unit reporting directly to the Risk Management Committee ("RMC") of the Board. The division's primary responsibility is to assess, monitor and recommend strategies for control of credit, market and operational risk. The absence of any direct or indirect reporting lines and permanent membership in all Maisarah's committees are among the factors which reflect the independence of the Risk Management Division's working and the key role it plays within Maisarah.

The risk management framework is pivoted on a host of committees involving the executive management and the Board of Directors ("the Board") for approval and reporting purposes. The Board has the overall authority for approval of strategies and policies, which it exercises through its various sub-committees. RMC of the Board is responsible for reviewing and recommending to the full Board, approval risk policies and procedures. RMC also reviews the risk profile of Maisarah as presented to it by the Risk Management Division and appraises the full Board in its periodic meetings.

Credit risk

The most important risk to which Maisarah is exposed is credit risk. To manage the level of credit risk, Maisarah deals with counter-parties of good credit. Board Credit Committee is the final credit approving authority of Maisarah which is mainly responsible for approving all credit proposals beyond the authority level of the management. RMC is the management decision making body which is empowered to consider all credit related issues upto certain limits. Credit risk is managed by the Risk Management Division ("RMD") through a system of independent risk assessment in credit proposals before they are considered by the appropriate approving authorities. Maisarah has in place a risk grading system for analysing the risk associated with credit. This facilitates the approving authorities in making their credit decision. Maximum counterparty/group exposures are limited to 15% of the Bank's capital base as stipulated by CBO and where a higher limit is required for projects of national importance prior CBO approval is obtained. Individual country limits using Moody's, S&P and Fitch ratings have also been set up to ensure portfolio diversification in terms of sovereign risk ratings and geographical exposure. These limits are approved by the Board. Retail financing is strictly in accordance with the CBO guidelines. The analysis of credit portfolio is provided below. It is pertinent to mention that the credit portfolio consists of all standard accounts and there is no impairment in the portfolio.

Notes to the financial statements
For the period from 3 March 2013 to 31 December 2013

31 Financial risk management (continued)

(a) Geographical concentrations

All the financial asset and financial liabilities balance are based in Sultanate of Oman.

(b) Customer concentrations

Customer concentrations on asset (Gross)

	Due from banks and financial institutions	Murabaha receivables	Diminishing Musharaka financing	Ijarah Muntahia Bittamleek
	RO	RO	RO	RO
31 December 2013				
Retail	-	237,294	-	17,605,349
Corporate	7,700,000	-	10,425,217	-
	7,700,000	237,294	10,425,217	17,605,349

(c) Economic sector concentrations

	Murabaha receivables	Diminishing Musharaka Financing	Ijarah Muntahia Bittamleek
	RO	RO	RO
31 December 2013			
Personal	237,294	-	17,605,349
Construction	-	6,957,659	-
Manufacturing	-	1,670,200	-
Other services	-	303,683	-
Others	-	1,493,675	-
	237,294	10,425,217	17,605,349

(d) Gross credit exposure

	Total gross exposure 2013	Monthly average gross exposure 2013
	RO	RO
Murabaha receivables	237,294	167,425
Diminishing Musharaka Financing	10,425,217	5,368,439
Ijarah Muntahia Bittamleek	17,605,349	8,603,110

Notes to the financial statements
For the period from 3 March 2013 to 31 December 2013

31 Financial risk management (continued)

(e) Industry type distribution of exposures by major types of credit exposures:

	Murabaha receivables	Diminishing Musharaka Financing	Ijarah Muntahia Bittamleek	Off balance sheet exposures
	RO	RO	RO	RO
31 December 2013				
Import trade	-	-	-	2,989,910
Mining and quarrying	-	1,493,675	-	-
Construction	-	6,957,659	-	-
Manufacturing	-	1,670,200	-	-
Services	-	303,683	-	-
Retail	237,294	-	17,605,349	-
	237,294	10,425,217	17,605,349	2,989,910

(f) Residual contractual maturities of the portfolio by major types of credit exposures:

	Murabaha receivables	Diminishing Musharaka Financing	Ijarah Muntahia Bittamleek	Off Balance sheet exposures
	RO	RO	RO	RO
31 December 2013				
Upto 1 month	4,768	195,851	125,592	-
1 - 3 months	9,536	391,702	251,184	-
3 - 6 months	14,304	587,553	376,776	2,989,910
6 - 9 months	14,304	531,276	376,776	-
9 - 12 months	14,304	512,128	376,776	-
1 - 3 years	109,088	5,470,115	3,014,208	-
3 – 5 years	70,990	1,953,190	2,965,652	-
Over 5 years	-	783,402	10,118,385	-
	237,294	10,425,217	17,605,349	2,989,910

(g) Distribution of past due and not past due financing by type of industry:

	Performing Murabaha receivables	Performing Diminishing Musharaka Financing	Performing Ijarah Muntahia Bittamleek	General provisions made during the year
	RO	RO	RO	RO
31 December 2013				
Mining and quarrying	-	1,493,675	-	(14,389)
Construction	-	6,957,659	-	(67,026)
Manufacturing	-	1,670,200	-	(16,090)
Services	-	303,683	-	(2,926)
Retail	237,294	-	17,605,349	(184,828)
	237,294	10,425,217	17,605,349	(285,259)

Notes to the financial statements

For the period from 3 March 2013 to 31 December 2013

31 Financial risk management (continued)

(h) Maximum exposure to credit risk without consideration of collateral held:

There is no credit exposure provided without collateral.

Liquidity risk

Liquidity risk is the potential inability to meet Maisarah's liabilities as they become due, because of the difficulty in liquidating assets (market liquidity risk) or in obtaining adequate funding (funding liquidity risk). It arises when Maisarah is unable to generate cash to cope with a decline in deposits or increase in assets.

Maisarah's liquidity risk management is governed by the treasury risk policy document approved by the Board of Directors as well as the provisions of relevant CBO guidelines on liquidity risk management. Maisarah monitors its liquidity risk through cash flow approach. Under cash flow approach Maisarah generates Maturity of Assets and Liabilities (MAL) report which captures all the maturing assets and liabilities into various pre-set time buckets ranging from one month to five years. The mismatches in various time buckets indicate liquidity gap and Maisarah strictly adheres to the CBO set limit of 15% of cumulative liabilities (outflows) on mismatches (liquidity gaps) in time buckets upto one year. In addition, Maisarah has also set up internal limit on mismatches in time buckets beyond one year.

Treasury department of Maisarah controls and monitors the liquidity risk and ensures that the window is not exposed to undue liquidity risk and at the same time makes optimum use of its funds. Middle office in Risk Management Division also monitors the liquidity position of Maisarah.

Maturity profile of assets and liabilities

	Due on demand and up to 30 days	More than 1month to 6 months	More than 6 months to 12 months	More than 1 year to 5 years	Over 5 years	Total
	RO	RO	RO	RO	RO	RO
31 December 2013						
Cash and balances with Central Bank of Oman ("CBO")	3,028,809	-	-	-	-	**3,028,809**
Due from banks and financial institutions	7,700,000	-	-	-	-	**7,700,000**
Murabaha receivables - net	4,658	23,290	27,949	175,927	-	**231,824**
Diminishing Musharaka financing	193,964	969,821	1,033,352	7,351,793	775,856	**10,324,786**
Financial assets at fair value through equity	-	-	-	10,000,000	-	**10,000,000**
Ijarah Muntahia Bittamleek- net	124,313	621,563	745,875	5,918,939	10,015,301	**17,425,991**
Property and equipment – net	-	-	-	-	287,383	**287,383**
Intangible asset	-	-	-	-	790,429	**790,429**
Other asset	133,702	-	-	-	96,394	**230,096**
Total assets	**11,185,446**	**1,614,674**	**1,807,176**	**23,446,659**	**11,965,363**	**50,019,318**
Due to Head office and other banks	30,200,000	-	-	-	-	**30,200,000**
Qard Hasan from Head Office	-	-	-	3,287,038	-	**3,287,038**
Current accounts	508,429	889,751	508,429	-	635,538	**2,542,147**
Other liabilities	2,557,371	-	-	-	-	**2,557,371**
Equity of unrestricted investment account holders	55,879	126,259	114,759	558,793	279,455	**1,135,145**
Owner's equity	-	-	-	-	10,297,617	**10,297,617**
Total liabilities and account holders & owners' equity	**33,321,679**	**1,016,010**	**623,188**	**3,845,831**	**11,212,610**	**50,019,318**

Notes to the financial statements
For the period from 3 March 2013 to 31 December 2013

31 Financial risk management (continued)

Market risk

Market risk includes currency risk, profit rate risk and equity price risk.

(a) Currency risk

Maisarah is exposed to currency risk through its transactions in foreign currencies. The major foreign currency to which Maisarah is exposed is the US Dollar which is effectively pegged to Rial Omani. Presently Maisarah does not have major foreign exchange exposure. There is only one placement in US dollar which has been financed through Wakala deposit of the same tenure.

(b) Profit rate risk

Profit rate risk (PRR) is the risk that Maisarah will incur a financial loss as a result of mismatch in the profit rates on assets & investment accountholders. The profit distribution to investment accountholders is based on profit sharing agreements. However, the profit sharing agreements will result in displaced commercial risk when Maisarah results do not allow it to distribute profits in line with the market rates.

Maisarah has a detailed profit distribution policy in place which details the process and management of profit distribution, including setting up of profit equalization & investment risk reserve. The responsibility of profit rate risk management rests with the Maisarah's Asset and Liability Management Committee (ALCO).

Profit rate sensitivity gap

Sensitivity to profit rates arises from mismatches in the period to repricing of assets and that of the corresponding liability. Maisarah manages these mismatches by following policy guidelines and reduces risk by matching the repricing of assets and liabilities.

Notes to the financial statements
For the period from 3 March 2013 to 31 December 2013

31 Financial risk management (continued)

Market risk (continued)

Profit rate sensitivity gap (continued)

	Effective average profit rates	Due on demand and within 30 days	Due within 1 to 6 months	Due within 7 to 12 months	Due within 1 to 5 years	Due after 5 years	Non-profit bearing	Total
	%	RO	RO	RO	RO	RO	RO	RO
31December 2013								
Cash and balances with Central Bank of Oman	-	-	-	-	-	-	3,028,809	**3,028,809**
Due from banks and financial institutions	**0.91%**	7,700,000	-	-	-	-	-	**7,700,000**
Murabaha receivables	**5.13%**	4,658	23,290	27,949	175,927	-	-	**231,824**
Diminishing Musharaka Financing	**5.28%**	193,964	969,821	1,033,352	7,351,793	775,856	-	**10,324,786**
Financial assets at fair value through equity	**5%**	-	-	-	10,000,000	-	-	**10,000,000**
Ijara Muntahia Bit-tamleek - net	**4.32%**	124,313	621,563	745,875	5,918,939	10,015,301	-	**17,425,991**
Property and equip-ment - net	-	-	-	-	-	-	287,383	**287,383**
Intangible asset	-	-	-	-	-	-	790,429	**790,429**
Other asset	-	-	-	-	-	-	230,096	**230,096**
Total assets		**8,022,935**	**1,614,674**	**1,807,176**	**23,446,659**	**10,791,157**	**4,336,717**	**50,019,318**
Due to Head office and other banks	**0.47%**	30,200,000	-	-	-	-	-	**30,200,000**
Qard Hasan from Head office	-	-	-	-	-	-	3,287,038	**3,287,038**
Current accounts	-	-	-	-	-	-	2,542,147	**2,542,147**
Other liabilities	-	-	-	-	-	-	2,557,371	**2,557,371**
Equity of unrestrict-ed investment account holders	**0.52%**	55,879	126,259	114,759	558,793	279,455	-	**1,135,145**
Owner's equity	-	-	-	-	-	-	10,297,617	**10,297,617**
Equity of account holders & Total liabilities and shareholders' equity		**30,255,879**	**126,259**	**114,759**	**558,793**	**279,455**	**18,684,173**	**50,019,318**
On-balance sheet gap		**(22,232,944)**	**1,488,415**	**1,692,417**	**22,887,866**	**10,511,702**	**(14,347,456)**	**-**
Cumulative profit sensitivity gap		**(22,232,944)**	**(20,744,529)**	**(19,052,112)**	**3,835,754**	**14,347,456**	**-**	**-**

Notes to the financial statements
For the period from 3 March 2013 to 31 December 2013

31 Financial risk management (continued)

Market risk (continued)

(c) Equity risk

Presently Maisarah is not exposed to any equity price risk.

Operational risk

Maisarah has adopted the Basic Indicator Approach under Basel II for the purpose of measuring capital charge for Operational Risk. The approach requires Maisarah to provide 15% of the average three years gross annual income as capital charge for operational risk.

32 Segmental information

Maisarah is organised into three main business segments:

1) Retail banking – incorporating private customer current accounts, savings account, term deposits, murabaha and ijarah muntahia bittamleek;

2) Corporate banking – incorporating current accounts, savings account, term deposits and diminishing musharaka financing; and

3) Treasury & investments

Transactions between the business segments are on normal commercial terms and conditions. Funds are ordinarily allocated between segments, resulting in funding cost transfers disclosed in operating income. Profit charged for these funds is based on Maisarah's cost of capital. There are no other material items of income or expense between the business segments.

Segment assets and liabilities comprise operating assets and liabilities, being the majority of the statement of financial position.

Notes to the financial statements

For the period from 3 March 2013 to 31 December 2013

32 Segmental information (continued)

At 31 December 2013	Retail banking	Corporate banking	Treasury and investments	Total
	RO	RO	RO	RO
Segment operating revenues	97,587	55,901	121,941	275,429
Other revenues	17,637	75,378	88	93,103
Total segment operating revenues	115,224	131,279	122,029	368,532
Profit expenses	(4,577)	(13)	(10,639)	(15,229)
Net operating income	110,647	131,266	111,390	353,303
Segment cost				
Operating expenses including depreciation	(804,438)	(460,802)	(1,005,187)	(2,270,427)
Impairment allowance	(184,828)	(100,431)	-	(285,259)
Net loss for the year	(878,619)	(429,967)	(893,797)	(2,202,383)
Segment assets	18,301,600	10,711,503	21,291,474	50,304,577
Less: Impairment allowance	(184,828)	(100,431)	-	(285,259)
Total segment assets	18,116,772	10,611,072	21,291,474	50,019,318
Segment liabilities	5,196,305	1,835,184	31,555,067	38,586,556

33 Comparative

No comparative information has been presented as Maisarah has commenced its operation from 3 March 2013.

P.O. Box 1507, Ruwi 112, Sultanate of Oman

T +968 24 790 466

F +968 24 702 865

bankdhofar.com